

SME FINANCING AND ITS IMPACT ON FINANCIAL PERFORMANCE: A CASE STUDY ON DHAKA BANK LTD

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1. INTRODUCTION

Bangladesh is recognized as one of the most densely populated, least developed and agro-based countries in the world. In different international ranking published in the newspaper, Bangladesh occupies a very well position in corruption. But once, Bangladesh was famous for her glorious past too like in producing silk clothes. Thus, there are many opportunities to transform the problematic areas of Bangladesh into prospects. The name of one of the ways of transformation can be SME.

1.1 BACKGROUND

According to Ahmed (2006), SME development, one of the instruments of employment and income generation, human development and poverty alleviation, export promotion, stimulation of private ownership, competition and entrepreneurship and hence the driving forces behind the growth of a vibrant industrial market economy, has generated considerable interest among the policymakers, academics, business circle and the international donor agencies in recent times. The concept of SME is not new in Bangladesh but there is a lack of consciousness among people especially among most financial institutions in regards of cooperation.

Small and medium enterprises (SMEs) have long been considered as the principal driving force of the economy of Bangladesh. The biggest impediment to SMEs is the lack of sufficient capital needed to operate business. Most businesses often have to start with their own savings or by borrowing from friends and relatives, with bank financing coming later. Banks remain extremely reluctant to lend to small scale entrepreneurs who do not have any startup equity, despite sound business models. A World Bank (WB) paper titled "Bank financing for SMEs around the world", which used data from 91 banks from 45 countries, reports banks are less exposed and charge higher interest rates and fees to SMEs relative to large firms. A number of studies using firm-level survey data have shown that SMEs not

only perceive access to finance and the cost of credit to be greater obstacles than large firms do, but these factors also constrain SME performance more than in large firms. However, the WB found through its survey of banks that most banks (80 percent or more), independent of where they operate and of ownership type, perceive the SME segment to be large with good prospects (The Daily Star, April 17, 2009).

Dhaka Bank Limited is one of the well-reputed private commercial banks in Bangladesh that started SME financing from the year 2003. The current study attempts to explore the current situation of SME financing through performance analysis and if there is any impact of SME financing on the financial performance of Dhaka Bank Limited.

1.2 STATEMENT OF PROBLEM

In the industrial sector, the Small and Medium Enterprise (SME) is widely believed to be the potential engine of economic growth of Bangladesh. According to the National Private Sector Survey of Enterprises in Bangladesh (2003), the SME sector accounts for around 40 percent of gross manufacturing output, 80 percent of industrial employment, and 25 percent of the total labor force in this economy. The survey estimated that micro, small, and medium enterprises contributed around 20-25 percent of GDP. The sector was found to encompass about 79,754 establishments, of which 93.6 percent were small and 6.4 percent medium (ADB, 2004). Despite the significant contribution of SME sector to the economy, this sector has been seriously suffering from the limited access to financial services. The enterprises in this sector are not small enough to get credit facilities from MFIs and at the same time not large enough to get loans from formal financial institutions. (Bangladesh Bank, 2006).

Investment is very much essential for the growth of any industry and increased facilities in obtaining credits can enhance that growth. Finance is needed at the starting phase of a business as well as at the enduring phases. The entrepreneurs require mainly three types of finances, namely- (i) equity capital - to finance assets at the start of a business; (ii) debts - to refinance assets; and (iii) working capital - to maintain the day-to-day activities. However, the access to financing is recognized as the leading obstacle to SSI growth in Bangladesh, alike most other developing and under-developed countries (Rubayat, 2009). According to one statistics published by Bangladesh Bank, out of total SME loan outstanding, the stake of private commercial banks are decreased from 18.11% in December 2008 to 16.33% in December 2009 (Bangladesh Bank Monthly Update, February, 2010).

Again, according to a statistics published in The Daily Star on December, 03, 2010, the amounts of disbursed loan in the SME sector were more than Tk.10,000 crore, more than Tk. 12,000 crore and about to Tk. 14,000 crore in January-March, April-June and July-September quarters respectively that indicates, though the amount of loan disbursement is increasing, yet, the rate is very sluggish.

Bangladesh Bank annual report for fiscal 2006-07 revealed that, higher growth of the Small and Medium Enterprises (SMEs) can help cut poverty to a satisfactory level by eliminating various prejudices against labour intensive and creating jobs for the skilled manpower in the SME sector. The report said, the key reasons behind the SMEs are not entering into manufacturing are financial constrains, dismal state of utilities, technology and policy discriminations. On the others hand, banks and others financial institutions generally prefer large enterprise clients because of lower transition costs, and greater availability of collateral (The New Nation, January 02, 2008). Though Bangladesh Bank has taken different schemes and is refinancing private commercial banks at lower rate from its IDA and ADB fund to lend SME, not all banks are yet interested in SME lending because of several excuses like lack of collaterals, higher management cost in monitoring SME loan etc.

In a seminar on “Present and Future of SME Banking” held in Dhaka, FBCCI administrator Syed Manzur Elahi said that, private commercial banks would have to largely shift toward providing small and medium-sized loans given the risks associated with corporate banking. He also said that, corporate banking is profitable, but risks remain. If a corporate loan gets defaulted, it may involve Tk 1.0 billion that a private bank can hardly afford. On the other hand, a small or medium enterprise takes loans of manageable size. So, private banks will ultimately have to attach increased importance to SME banking (The Financial Express, January 17, 2008).

Thus, this study has tried to explore the current situation of SME financing through performance analysis in Dhaka Bank Limited (DBL), and if there is any impact of SME financing on the financial performance of Dhaka Bank Limited.

1.3 PURPOSE OF THE STUDY

The broad purpose of this report is to explore the current scenario of SME financing through performance analysis in Dhaka Bank Limited and if there is any impact of SME financing on the financial performance of Dhaka Bank Limited (DBL). Moreover, some specific purposes of this exploratory research are -

1. To identify the present situation of SME financing in Bangladesh
2. To know the growth, trend and contribution of SME financing in total loan outstanding, total costs of fund, total interest income, total non-performing loan and total number of borrowers for five year from year 2005 to year 2009
3. To find out if there is any significant difference between the mean of ROA of before and after the introduction of SME in DBL's lending portfolio
4. To sketch the problems and issues related to SME lending by DBL and finally,
5. To suggest steps to improve further in SME lending by DBL

1.4 METHODOLOGY

1.4.1 Sources of Data

Both primary and secondary sources were used for collecting information.

1.4.2 Methods of Data Collection

Different methods were followed for collecting information under primary and secondary sources. These are:

1.4.2.1 Primary Sources

For primary sources of information, direct observation, face to face in depth interview, and telephone interview were conducted.

1.4.2.2 Secondary Sources

For secondary information, SME related journals and articles of Government/ Non-government organizations and previous works on the related issues of SME were utilized.

1.4.3 Instruments for Collecting Information

For in-depth interview, information were collected through unstructured questionnaire and for published data, different search engines like Google scholar, yahoo etc., searching in the library etc. were done.

1.4.4 Selection of Interviewee

For the purpose of this report, relevant personnel from the management team were selected on the basis of the work experience in Dhaka Bank Ltd. for the interview. Also, those who are and were directly involved in credit division and in SME lending in Dhaka Bank Limited SME units and in Dhaka Bank Local Office, such as credit officers of DBL Local Office, SME unit and credit operation division, Head of SME unit etc. were taken under consideration for interview.

1.4.5 Sample Selection

To see if there is any impact of SME financing on financial performance of DBL, data have been divided into two major groups. One is, Return on Assets (ROA) of the years before the introduction of SME financing in DBL's total lending portfolio and ROA of the years after the introduction of SME financing. A sample of 5 years are selected to observe the impact analysis of SME financing on the total financial performance of DBL. The ROAs of year 1998 to year 2002 have been selected for pre SME financing study and ROAs of year 2005 to year 2009 have been selected for post SME financing study. Here the samples are called independent samples because observation has been done on ROA of Dhaka Bank Limited at two different points of time.

1.4.6. Data Analysis

Collected data are analyzed by using MS. Excel 2007 and to find out if there is any impact of SME financing in the financial performance of Dhaka Bank Limited, independent samples t-test has been done through SPSS 12, to show whether there is any impact of SME financing on ROA.

1.5 HYPOTHESES

In order to know whether any significant impact of SME financing is there in the financial performance of Dhaka Bank Limited, ROA is used to measure DBL's financial performance and following null and alternative hypotheses are initiated:

H₀: There is no impact of SME financing on ROA of Dhaka Bank Limited.

H₁: There is a significant impact of SME financing on ROA of Dhaka Bank Limited.

1.6 SCOPE

This study has been done on the SME lending performance of Dhaka Bank Limited. Only the supplier side is considered for analysis in this study.

1.7 LIMITATIONS

Two limitations were there in carrying out this study.

- One of the obstacles was availability of limited information. The concept of SME is, though not new, but the implementation of it is yet to be structured in Dhaka Bank. Though Dhaka Bank started SME lending from 2003, negligible exposure were found in SME in initial years. If at least ten years' data would be available, post-SME financing analysis would be done more meaningfully

and trend of SME lending in DBL would be much understandable. Again, Dhaka Bank Limited itself started its operation from June 1995. If at least 10 years' data would be available, pre-SME financing study would be done more meaningfully and hypothesis testing would be much more accurate and understandable.

- Getting appointment of top level management such as the board of directors was not possible because of their inflexible schedule.

2. LITERATURE REVIEW

2.1 SME Banking

In the SME sector of Bangladesh, studies done by foreign and national experts undertook some of the notable ones are; Uddin (2008), Chowdhury (2007), Miah (2006), Ahmed (2004). Uddin (2008) has stated that the economic efficiency and overall performance of the SMEs especially in the developing countries are considerably dependent upon macroeconomic policy environment and specific promotion policies pursued for their benefit.

Ahmed (2004), based on estimates of BSCIC, suggests that currently there are more than 600,000 small and cottage enterprise in Bangladesh. However more than 3 million micro enterprises are also in operation. In SME taskforce report (2006), it has been argued that manufacturing industries or enterprises are synonymous with small and cottage industries. SEDF (2003) reports that, more than 90% of all industrial units are SMEs. According to Chowdhury (2007), in context of Bangladesh, SME is characterized by low capitalization and limited assets, geographical diversity and high mortality, poor credit knowledge, very limited access to formal source of credit, cash intensity in transactions, very limited record keeping habit, poor financial disclosure on account of tax issues, high risk perception has led to high borrowing costs.

The recent study of SEDF (2006) reinforces the earlier findings that SMEs have limited access to bank financing. It shows that about two third of the SMEs did not approach for banks for loans. Most of them approached Banks for Working Capital Loans. Not all of them were granted loans. It takes about two months on an average to get loan sanctioned. The findings of SEDF (2006) reinforces that finance is a major constraint (SME Taskforce Report 2006). Research has shown that access to external finance is the most significant factor contributing to the growth of small firms (Brown et al., 2003). Unlike large firms that have ready

access both to debt and equity markets, the small firms have nowhere else to go but the banks

In the commercial banking industry there is a growing recognition that SMEs not only represent a viable market segment but that their needs are different and frequently underserved (Kai, 2009). The study reported here identifies the factors that SMEs (specifically, home building contractors) consider in selecting a banking partner.

2.2 Loan Outstanding

Molyneux and Thorton(1992), applying the model used by Bourke(1989) undertook the study to banks in a eighteen European countries. They used standardized accounting data published by the International bank credit Analysis Ltd (IBCL) to account for differences in accounting policies. The results show strong positive relationship between concentration of total loan outstanding that is bank's asset and the interest income.Ali Abdula (1994) on the other hand, using two accounting measures of banks performance (return on assets and return on equity) in Bahrain commercial banks found out that, bank size measured by total loan outstanding and individual products' loan to total loan ratio directly related to the bank's profitability.

2.3 Interest Income

Elizabeth (2004) and Diamond (1989) have revealed that, interest income is one of the major tools to measure the financial performance of commercial banks. They have also mentioned that, the higher the interest income, the lower is the cost of fund and the lower is the cost of fund, the more cost effective is the bank.Again, Stein(2002) and Tarawneh(2006) have mentioned that, besides net income, interest income is important for private commercial banks in performance analysis because, interest income reveals the profit generating ability of commercial banks as loan is the main income generating asset for banks.

2.4 Cost of Fund

The bank's relative cost of funds should positively influence profitability (Evan off and Fortiers, 1998; and Agu(1992)). Also, the greater the cost of funds, the lower the profit rate (Agu, 1992). Hays,Lurgio and Gilbert(2009) examined small and medium sized banks from the early 1970's until deregulation occurred in the early 1980's. They found that, profitable banks had lower interest and non interest expense than less profitable banks. In addition, the more profitable banks had lower cost of funds, greater use of transactions deposits, more marketable securities and higher capital levels. High performance banks during this period

made higher quality loans, held proportionately more capital, invested more in securities (especially long-term) and relied on lower cost funding sources compared with the average small bank.

2.5 Nonperforming Loan

Bank performance may determine the risk taking behavior of managers. Banks with high profitability are less pressured to revenue creation and thus less constrained to engage in risky credit offerings. However, inefficient banks are tempted to grant and to engage in more uncertain credits to defend their profitability and meet the prudential rules imposed by the monetary authorities (Boudriga, Boulila Taktak, Jellouli; 2009). Godlewski (2004) using the return on assets (ROA) as a proxy for performance, shows that banks profitability negatively impacts the level of nonperforming loans ratio. Ford and Oslon (1978) asserted that the elements beyond the control of management contribute modestly in the banks rate of return. They reported that the financial determinants of high performance banks are: interest on deposit that is cost of deposit, individual product loan to total loans, income from loan, loan loss provision to earning asset etc.

2.6 Number of Borrowers

A study by Sinkey (2002) reveals that, banks should utilize their relationship in order to get good bunch of borrowers because no matter what the amount is, the highest number of borrowers ensures bank's service quality and future good financial performance. Again Tarawneh (2006) in his study on financial performance of commercial banks has mentioned that number of borrower is one of the important factors to measure financial performance of commercial banks. Diamond (1989) and Diamond (1991) have examined the role of reputation acquired in banking relationships. In Diamond's model, the adverse selection and moral hazard problems in the pool of potential borrowers result in initially high equilibrium interest rates. Over time, some borrowers default and others repay their loans. As the banking relationship develops, the payment histories accumulate to form reputations, which reduce the lender's adverse selection and moral hazard problems. This process results in lower interest rates to firms acquiring reputations as non defaulting borrowers. Thus, number of borrower is vital for present and future financial performance of commercial banks.

2.7 ROA (Return on Assets)

Hays, Lurgio and Gilbert (2009) have mentioned in their study that, Banks' performance can be measured by return on assets (ROA). In their study, the

situation was to measure community bank's performance after the "Subprime Crisis". The determinants of performance of Greek banks during the period of EU financial integration (1990-2002) has been examined by Kosmidou (2008). He used an unbalanced pooled time series dataset of 23 banks. For bank performance measurement, he used the ratio of return on assets (ROA). Banking sector in Saudi Arabia has been examined by Ahmed and Khababa (1999). Among the three measures used in evaluating banks' performance, one the measures was ROA.

Wum et al.,(2007) investigated the impact of factors such as: financial development measured by financial interrelation ratio(FIR), the level of monetization measured by M2/ GDP and the level of capitalization, size, age of the bank, business orientation measured by the ratio of non-interest income, and per capita GDP on the Chinese commercial banks. The results indicated that the higher the levels of financial development, the better ROA performance for banks. The results also indicated a positive impact of per capita GDP on bank performance. However, a negative impact of size and business orientation on the ROA was found. In their study,Wum et al.(2007) used ROA to measure the financial performance of commercial banks.Unal et al., (2007) conducted a comparative performance analysis between the Turkish state-owned and private commercial banks during the period 1997-2006. They used net profit-loss, return on assets (ROA) and return on equity as proxies to measure profitability.

3. SME IN BANGLADESH: PRESENT SCENARIO

3.1 Defining Small and Medium Enterprises (SME) in Bangladesh

The Small and Medium Enterprises worldwide are recognized as engines of economic growth. The commonly perceived merits often emphasized for their promotion especially in the developing countries like Bangladesh include their relatively high labor intensity, dependence on indigenous skills and technology, contributions to entrepreneurship development and innovativeness and growth of industrial linkages.

Definition

According to the latest circular of Bangladesh Bank (Date - 26/05/2008), the definition of Small & Medium Enterprise sector is given below:

Small Enterprises - Small enterprises refer to those enterprises which are not any Public Limited Companies and which fulfill the following criteria-

Service Concern- Having an investment of Tk. 50,000 to Tk. 50, 00,000 excluding land & building and / or employing up to 25 workers.

Business Concern - Having an investment of Tk. 50,000 to Tk. 50, 00,000 excluding land & building and / or employing up to 25 workers.

Manufacturing Concern - Having an investment of Tk. 50,000 to Tk. 1,50,00,000 excluding land & building and / or employing up to 50 workers.

Medium Enterprises - Medium enterprises refer to those enterprises which are not any Public Limited Companies and which fulfill the following criteria-

Service Concern- Having an investment of Tk. 50,00,000 to Tk. 10,00,00,000 excluding land & building and / or employing up to 50 workers.

Business Concern - Having an investment of Tk. 50,00,000 to Tk. 10,00,00,000 excluding land & building and / or employing up to 50 workers.

Manufacturing Concern - Having an investment of Tk. 1,50,00,000 to Tk.20,00,00,000 excluding land & building and / or employing up to 150 workers.

SMEs in Bangladesh are also defined for purposes of industrial policies by Ministry of Industries (MOI). Historically, this definition has been in terms of fixed investment brackets, and a dual mode definition is in place, separate for manufacturing establishments, and service establishments.

According to the Industrial policy 2005, small and medium enterprises shall be categorized using the following definitions:

a. Manufacturing enterprise

Small enterprise - an enterprise should be treated as small if, in current market prices, the replacement cost of plant, machinery and other parts / components, fixtures, support utility, and associated technical services by way of capitalized costs (of turnkey consultancy services, for example), etc, excluding land and building, were to be up to tk. 15 million;

Medium enterprise - an enterprise would be treated as medium if, in current market prices, the replacement cost of plant, machinery and other parts / components, fixtures, support utility, and associated technical services by way of capitalized costs (such as turnkey consultancy services), etc, excluding land and building, were to be up to tk. 100 million;

b. Non-manufacturing enterprise

Small enterprise - an enterprise should be treated as small if it has less than 25 workers, in full time equivalents;

Medium enterprise - an enterprise would be treated as medium if it has between 25 and 100 employees

The Industrial Policy 1999 provides the following size classification scheme of the industries:

Large Industry: Employs more than 100 workers and/or has capital assets in excess of Tk. 30 Crore.

Medium Industry: Employs between 50 and 99 workers and/or has fixed capital assets in excess of Tk. 10 Crore but less than Tk. 30 Crore.

Small Industry: Employs less than 50 workers and/or have capital assets less than Tk.10 Crore.

Cottage Industry: Engaged in manufacturing activities with mostly family members.

3.2 Constraints in the Growth of SMEs

Alam (2006) observed that availability of finance is a major constraint to formation and growth of SMEs in Bangladesh. Banks are unwilling to expand their SME credit portfolio because they do not consider SME lending an attractive and profitable undertaking. This is so because SMEs are regarded as high risk borrowers because of their low capitalization insufficient assets and their inability to comply with collateral requirements of the banks. Administrative costs are also higher because close monitoring and supervision the SME operation becomes necessary. A study (2004) by Micro Industries Development Assistance and Services (MIDAS) revealed that sources of finance are mostly friends and family member in case of SME. MIDAS tried to identify the sources of funds of SMEs. These are:

Table 1: Sources of Fund for SMEs in Bangladesh

Sources of funds	Percentage of finance
<i>Informal sector</i>	41%
<i>Family members</i>	20%(interest free) 4% (with interest)
<i>NGO</i>	17%
<i>Bank</i>	18%

Source: MIDAS (2004)

According to Hallberg (2002), a stable macro-economy, an open trade and investment regime, and a competitive financial sector are argued to be most essential ingredients for a vibrant private sector. But with a law and order situation below the optimum level, corruption well above the level of acceptance and unstable political situation, the domestic environment of Bangladesh do not come to any help, rather hinders the prosperity of SME in this country.

In a paper by Montoo(2006), titled *The Role of Private Sector in Bangladesh*, 25 issues were identified as impediments to growth of the SME sector. The issues are-lack of long-term capital availability through banking channels; lack of long-term capital in the capital market and bond market, dumping of products, largely by smuggling, inefficient support infrastructure, widespread tariff anomalies; high customs' duties; complicated and cumbersome customs procedures, aggravated by extensive arbitrary powers exercised by customs officers; low productivity and a highly politicized labour sector; inconsistency among different government policy statements; an inefficient and corrupt judicial system; widespread corruption; political instability, leading to frequent strikes; high interest rates in the banking sector; a lack of credible statistics; lack of transparency and accountability in government decision making; lack of an appropriate education system to support an industrial economy; too many holidays;a slow process of deregulation and privatization; lack of an industry-friendly social and political environment; lack of good governance; lack of regulatory bodies; an uneven playing field between the private sector and the public sector; lack of local technology; lack of research and development; Government control on public utilities.

Again, according to Ahmed and Chowdhury (2009), at present SME sector is facing a lot of problems in Bangladesh. The author mentioned some of the following constraints that are creating obstacles on the way of SME growth:

a) Resource Scarcity

In Bangladesh scarcity of raw materials deters the ability of SME to be export oriented and limits its ability to reach to more advanced stages of international business. Also, a high rate of duty is placed in the import of basic raw materials for SMEs (The Daily Star, June 4, 2010).

b) High Employee Turnover

Due to limited growth of SME, most of the skilled employees leave SMEs. Levy (2003) observed that SMEs are knowledge creators but poor at knowledge retention.

c) Absence of Modern Technology

One of the main barriers for the development of SME in Bangladesh is inadequate technologies. Many SMEs have failed to adopt modern technology.

d) Poor Physical Infrastructure

Inadequate supply of necessary utilities like electricity, water, roads and highways hinder the growth of SME sector. Moreover unfavorable geographical conditions increase the transportation cost.

e) Financial Constraints

Availability of finance hinders the growth of SMEs in Bangladesh. Bangladeshi bank considers SMEs as high risk borrowers because of their inability to comply with the bank's collateral requirements. Only about 15-20% of the owners of SMEs own any immovable property. Bankers issue loan on the basis of ownership of immovable property as collateral risk. As a result it automatically excludes rest 80% SME's from the list of privileged clients of the banks. Whatever collateral SME's can manage gets used up in talking the term loan leaving them with no means to seek working capital loans from banks. Because of low access to institutional financing SME's rely on inefficient financing services from informal sources.

f) Lack of Uniform Definition

In Bangladesh, the definition of SME has changed overtime in different industrial policy announced by the government in different year. Absence of uniform definition makes the formulation and implementation of SME policy difficult.

g) Lack of Information

Miah (2006) has observed that SMEs have very limited use of information technology (IT). Accounting package is used by 1-2% of the SMEs. The use of computers is revealed by say 15% of the SMEs, while the use of the internet for business purposes applies to say 8-10% of SMEs.

h) Lack of Entrepreneurship Skills

Conservative attitude towards risk, lack of vision, ability to make plan and implementing those hinder the growth of SME in Bangladesh.

i) Participation of Women Entrepreneurs

Equality of opportunity is a major problem for SME. Female entrepreneurs are treated discriminately. They are not well represented in business organization. Government does not provide adequate institutional assistance for women entrepreneurs.

j) Access to Market and Lack of Awareness Regarding the Importance of Marketing Tool

For SME, owing a retail space is very expensive in the major cities in Bangladesh. As a result many customers are not interested to buy products and services from SMEs because they cannot judge the quality until they physically examine the product. In most of the cases, SMEs in Bangladesh are not able to use the Integrated Marketing Communication (IMC) tools. But these tools play the role of

important stimulus to motivate the customers and retain them. The country does not have enough marketing capability and resources to invest in marketing.

k) Bureaucracy

Wang (1995) observed that the inadequate government supports are top ranking constraints for SMEs. Unnecessary layers of Bureaucracy and red-taps reduce the competitiveness of SME and raising the cost of transactions and operations.

l) Absence of Transparent Legal System

The absence of an effective and transparent legal system discourages SMEs in exploring into risky ventures of business. There are a number of unnecessary formal requirements to start and run business that create high compliance costs and become barriers to SME development, growth and market entry.

m) Lack of Commitment to Innovation and Customer Satisfaction

Ernesto (2005) stated that to keep in pace with international competition, firms of all size are challenged to improve and innovate their products processes constantly. But in Bangladesh, SMEs are still not relating the importance of satisfying and retaining customers by offering novel and desired benefits.

n) Lack of Quality Assurance

Govt. has failed to frame a national quality policy, provide adequate support systems and establish a national quality certification authority. As a consequence SME of Bangladesh has failed to ensure the quality of their products and services both in local and international market.

o) Lack of Research and Development Facilities

It is observed that investment in R&D is still negligible in SME sector.

p) Fierce Competition with the Cheaper Foreign Goods

Fierce competition with the cheaper goods of China, Taiwan, Korea, India, and Thailand also poses threat to SME in Bangladesh.

3.3 Contribution of SME in the Economy of Bangladesh

In 2003, the International Consultancy Group (ICG) of the UK, in collaboration with the Micro Industries Development Assistance and Services (MIDAS), conducted the National Private Sector Survey of Enterprises in Bangladesh. The survey results drew the conclusion that there were approximately 6 million Small and Medium Enterprises (SMEs), which included enterprises with up to 100

workers employing a total of 31 million people, equivalent to 40 % of the population of the country of age 15 years and above. The survey also found that the industrial structure of SMEs consisted of primarily wholesale and retail trade and repairs (40 per cent), production and sale of agricultural goods (22 percent), services (15 percent), and manufacturing only (14 per cent). Thus the survey brought out the fact that the large untapped potential for expansion in manufacture and production could be exploited (or contributing more significantly to the national economy (Ahmed& Chowdhury, 2009).

Table 2: Contribution of SME to GDP of Bangladesh

Numbers of workers	Total Contribution to GDP (Taka)	Percentage of Total contribution
0-1	193 996 555 714	26
2-5	379 663 897 358	51
6-10	73 120 983 681	10
11-20	45 183 240 157	6
21-50	33 960 498 076	5
51-100	15 138 922 373	2
Total	741 064 097 360	100

Source: ICG/MIDAS Survey, 2003

Note: US \$ 1 = BDT 69.00

The above table 2 shows the contribution of SME in the GDP of Bangladesh, according to a survey of MIDAS(2003). Another imperative findings of the survey under discussion was that, SMEs contributed BDT 741 (\$ 12.5) billion i.e. nearly 25 per cent of the GDP (BDT 2,996 billion) in 2003. It is reflected from this survey that enterprises employing 2-5 workers contribute 51 percent share of the total SME contribution to the economy, followed by 26 percent by those having only one worker and 10 per cent by those having 6-10 workers. For LDCs like Bangladesh, SMEs are a highly cost-effective route for industrial development.

It is observed from table 2 that micro enterprises run by up to 10 workers contribute the most which is 87% of the total contribution from SMEs to GDP of Bangladesh. It is also observed that micro enterprises run by more than 21 workers contribute about 7% of total contribution from SME to GDP of Bangladesh.

The following table 3 provides the information regarding sector wise contribution of SMEs to GDP. It is reflected from the table that manufacturing sector contributes the highest contribution in GDP i.e., 38%. It is also observed from the table that agriculture and wholesale and retail sector contribute more than 22 percent each in the GDP of Bangladesh.

Table 3: Sector wise contribution of SME in GDP of Bangladesh (Tk.)

Sector	Total Contribution to GDP (Tk.)	% of Total Contribution
<i>Agriculture</i>	177 729 637 637	24
<i>Fishing</i>	32 872 674 464	4
<i>Manufacturing</i>	282 344 700 575	38
<i>Construction</i>	7 196 460 200	1
<i>Wholesale and Retail trade and Repairs</i>	171 335 861 390	23
<i>Hotels and Restaurants</i>	28 599 263 975	3
<i>Transport, Storage and Communication</i>	8 950 171 356	1
<i>Real state, Renting and Business activities</i>	13 771 436 794	2
<i>Education</i>	151 808 506	1
<i>Health and Social Work</i>	2 743 049 893	1
<i>Other Service activities</i>	15 632 094 785	2
Total	741 327 159 609	100

Source: ICG/MIDAS Survey, 2004

Note: US \$ 1 = BDT 69.00

According to the above table 3, it is clear that, other than agriculture, manufacturing and wholesale and retail trading business, other sectors have minimal contribution. Thus, there are lots of opportunities to develop other sectors in SMEs.

Table 4: Growth Pattern of SME

Year	Growth Percentage of Small Enterprises
<i>2001-2002</i>	7.69
<i>2002-2003</i>	7.21
<i>2003-2004</i>	7.45
<i>2004-2005</i>	7.93
<i>2005-2006</i>	9.21
<i>2006-2007</i>	10.28

Source: Bangladesh Economic Review 2006-2007

The above table 4 shows the growth pattern of SME. It is observed that during 2001-2002 to 2004-2005 in every financial year the growth rate of SME is about

7%. In 2005-2006 the growth rate was 9.21%. The highest growth was in 2006-2007 i.e., 10.28%

Table 5: Growth Pattern of Manufacturing Sector

Year	Growth Percentage of Manufacturing Sector
1972-2005	6.4
2001-02	5.48
2002-03	6.75
2003-04	7.10
2004-05	8.19
2005-06	10.77
2006-07	11.19
2015	Expected Growth 15

Source: Bangladesh Economic Review 2006-2007

The above table 5 shows the growth pattern of manufacturing sector. It is observed that the average growth during 1972 to 2005 was 6.4%. During 2001-2002 to 2006-2007 the highest growth was in year 2006-07 i.e., 11.19%. It is also observed that during 2002-2003 to 2005-2006 in every financial year the growth of manufacturing sector was more than 6%.

4. BACKGROUND OF DHAKA BANK LIMITED (DBL)

The economy of Bangladesh has been experiencing a rapid growth since the '90s. Industrial and agricultural development, international trade, inflow of expatriate Bangladeshi workers' remittance, local and foreign investments in construction, communication, power, food processing and service enterprises ushered in an era of economic activities. Urbanization and lifestyle changes concurrent with the economic development created a demand for banking products and services to support the new initiatives as well as to channelize consumer investments in a profitable manner. A group of highly acclaimed businessmen of the country grouped together to responded to this need and established Dhaka Bank Limited in the year 1995.

Dhaka Bank Limited is a scheduled bank that was incorporated under the Companies Act 1994. It started its operation on July 1995 with a target to play the vital role on the socioeconomic development of the country. Within this short time the bank has been successful in positioning itself as progressive and dynamic financial institution in the country. This is now widely acclaimed by the business community, from small entrepreneur to big merchant and conglomerates,

including top rated corporate and foreign investors, for modern and innovative ideas and financial solution. Aiming at offering commercial banking service to the customers' door around the country, The Bank has 50 branches across the country and a wide network of correspondents all over the world through its foreign correspondents. The Bank has plans to open more branches in the current fiscal year to expand the network.

5. PERFORMANCE ANALYSIS OF SME AND ITS IMPACT ON FINANCIAL PERFORMANCE OF DHAKA BANK LIMITED (DBL)

5.1 Performance Analysis of SME in terms of Loan Outstanding, Interest Income, Cost of Fund, Nonperforming Loan and Number of Borrowers

SME has already been integrated in the lending portfolio of Dhaka Bank Limited since the year 2003. The management of Dhaka Bank believes that, though DBL has pursued conservative policy in business expansion till now, it is quite aggressive in SME banking since the year of SME's inception in the product portfolio. Thus, to prove DBL management's belief, it is necessary to identify the contribution SME lending has put in the total financial performance of DBL. For performance analysis of SME, five crucial parameters are selected. These are -

- ❖ Loan Outstanding
- ❖ Interest Income
- ❖ Cost of Fund
- ❖ Non Performing Loan
- ❖ Number of Borrowers

A five year time period starting from year 2005 to 2009 has been selected to recognize the contribution of SME in total financial performance of DBL.

5.1.1 Loan Outstanding

Loans are the main assets of commercial banks. In case of Dhaka Bank also, there is no question of dissimilarity. The higher the amount of loan outstanding, the higher is the possibility of interest income and at the same time, the higher is possibility of loan default. Yet, the higher amount of loan outstanding reflects the relationship building ability of a bank. It also reflects the business expansion of a bank.

From a five year study on the loan outstanding performance of Dhaka bank Limited, an increase in the amount of loan outstanding is observed. The year-end amounts of SME loan outstanding and total loan outstanding from year 2005 to

year 2009 are mentioned in the following table. According to the table, though the amount of SME loan outstanding have been increased, the amount of total loan outstanding were not increased in the same rate as of SME. It means, over the five years, DBL has started focusing on SME and may be some other areas of lending did not get more attention. As a result, overall loan outstanding were increased at a slow rate.

Dhaka Bank started SME lending from the year 2003. Yet, year 2005 can be observed as a depressing year for SME loan outstanding compared to the total amount of loan outstanding. Following table 6 shows the year-end amount of SME loan outstanding and total loan outstanding from year 2005 to 2009.

Table 6: SME Loan Outstanding, Total Loan Outstanding the Contribution of SME Loan Outstanding in Total Loan Outstanding

Types	Years				
	2005	2006	2007	2008	2009
Total Loan Outstanding	23,372	34,049	39,972	49,698	52,910
SME Loan Outstanding	45	252.54	752.96	1,766.75	2,366.8
SME Loan Outstanding as % of Total Loan Outstanding	0.19%	0.74%	1.88%	3.55%	4.47%

Figure in Million Tk.

Source: Secondary

From the above table, it is revealed that only tk. 45 million SME loans were outstanding in the year ended at 2005 that was only 0.19% of total outstanding loan amounting tk. 23,372 million. In the year end at 2006, the SME loan outstanding amount was suddenly soared to tk. 252.54 million that is noticeable. In year 2006, the growth in SME loan outstanding was 461.20% that is astonishing. But the growth in total loan outstanding amount was steady as it was just 45.68% more than from the previous year compared to the growth of SME loan outstanding. In 2006, the SME loan outstanding was 0.74% of total outstanding loan, having a 289.47% $\left\{ \frac{0.74\% - 0.19\%}{0.19\%} \times 100\% = 289.47\% \right\}$ enhancing contribution in % of total loan outstanding.

Again, in the year 2007, the growth of both SME and total loan outstanding were lower than those of the year 2006. Though SME loan outstanding was increased by 198.15% (amounting tk. 500.42 million) to Tk. 752.96 million in year 2007, total loan outstanding was increased by only 17.40% (amounting Tk. 5923 million) to Tk. 39,972 million from Tk. 34,049 million in year 2006. Again, the growth of SME

loan outstanding in year 2007 was 57.035% $[(461.20\% - 198.15\%) / 461.20\% * 100 = 57.035\%]$ lower than the growth of SME loan outstanding in year 2006. The growth of total loan outstanding was 61.91% $[(45.68\% - 17.40\%) / 45.68\% * 100 = 61.91\%]$ lower than the growth of total loan outstanding in year 2006.

The contribution of SME loan outstanding in total loan outstanding has also been increased in a decreasing manner. The contribution of SME loan outstanding was 1.88% in total loan outstanding which was higher than that of the previous year. But the percentage (%) increase in the contribution was 154.05% $[(1.88\% - 0.74\%) / 0.74\% * 100 = 154.05\%]$ that was lower by 135.42% $(289.47\% - 154.05\% = 135.42\%)$ than the contribution change of year 2006.

In the year 2008, the growth in SME loan outstanding was further lower. Compared to the year 2007; year 2008 can be documented with a suppressing growth of 134.64% (amounting tk. 1013.79 million) reaching to tk. 1766.75 million in SME loan outstanding but a 24.33% growth (amounting tk. 9726 million) reaching to Tk.49,698 million in total loan outstanding. In the year 2008, SME loan outstanding growth was 32.05% $[(198.15\% - 134.64\%) / 198.15\% * 100 = 32.05\%]$ lower than the growth of that in year 2007 and total loan outstanding attained a 39.83% $[(24.33\% - 17.40\%) / 17.40\% * 100 = 39.83\%]$ higher growth than that of the year 2007 that was a positive sign. The involvement of SME loan outstanding was 3.55% in total loan outstanding in the year 2008 that was 88.83% $[(3.55\% - 1.88\%) / 1.88\% * 100 = 88.83\%]$ higher than the previous year's contribution.

In order to find out the share of SME loan outstanding in total loan outstanding in the year 2009, it is found from table 6 that SME loan outstanding grew by only 33.96% (amounting tk. 600.05 million) getting to Tk. 2366.8 million that was 4.47% of the total loan outstanding which grew by only 6.46% (amounting tk. 3212 million) getting to tk. 52,910 million. The growth of SME loan outstanding in year 2009 was 74.78% $[(134.64\% - 33.96\%) / 134.64\% * 100 = 74.78\%]$ lower than the growth of SME loan outstanding in year 2008. Again, in year 2009 the growth of total loan outstanding was 73.44% $[(24.33\% - 6.46\%) / 24.33\% * 100 = 73.44\%]$ lower than the growth of total loan outstanding in year 2008.

5.1.2 Interest Income

As loan is the most vital asset for a commercial bank or lending is the primary service of commercial banks, the prime source of income of a commercial bank is interest income from loan outstanding. This is of no exception for Dhaka Bank also. The interest income from SME loan outstanding over the years and interest

income on the total loan outstanding from the year 2005 to 2009. A five year period starting from year 2005 to 2009 has been selected for analysis.

According to the table 7, DBL earned 6.75 million tk. interest incomes from SME lending in the year 2005 that was 0.23% of the total interest income amounting Tk. 2897 million. Again, in the year 2006, the interest income from SME lending jumped to tk. 40.41 million contributing a share of 0.93% in total interest income amounting tk. 4342 million.

Table 7: Interest Income from SME Loan, Interest Income from Total Loan and Contribution of SME Interest Income in Total Interest Income

Types	Years				
	2005	2006	2007	2008	2009
Interest Income from Total Loan	2,897	4,342	5,636	7,171	7,466
Interest Income from SME Loan	6.75	40.41	120.47	300.35	390.52
SME Income as % of Total Interest Income	0.23%	0.93%	2.14%	4.19%	5.23%

Source: Secondary

A jumped growth trend in interest income from SME can be proved for the year 2006. Similar to the SME loan outstanding growth mood in the year 2006; interest income from SME achieved a 498.66% $\left[\frac{40.41-6.75}{6.75} \times 100 = 498.66\%\right]$ growth on its previous year's income. But the rate of growth in total interest income was diminutive compared to the growth rate in SME interest income. In year 2006, growth rate of interest income from total loan outstanding over the year was 49.88% only. In year 2006, the contribution of interest income from SME in total interest income rose by 304.35% $\left[\frac{0.93-0.23}{0.23} \times 100 = 304.35\%\right]$ that was a positive sign of contribution.

In the year 2007, interest income from SME attained a lower growth than that of the year 2006. Though the amount of interest income from SME increased, yet, a 198.15% growth (amounting tk. 80.06 million) was supporting to the year 2007 amount (reaching to the amount 120.47 million tk.) that was 60.26% $\left[\frac{198.15-498.66}{498.66} \times 100 = 60.26\%\right]$ lower than that of the previous year. In year 2007, interest income from SME was 2.14% of total interest income amounting tk. 5636 million, that was 130.11% higher $\left[\frac{2.14-0.93}{0.93} \times 100 = 130.11\%\right]$ than the contribution SME interest income made on total income in 2006. But, the growth of SME interest income contribution to total interest income in year 2007

was lower by 57.25% $\left[\frac{(304.35-130.11)}{304.35} \times 100 = 57.25\%\right]$ than the growth in contribution of SME interest income to total interest income of the year 2006.

In year 2008, the interest income from SME loan outstanding over the year increased by 149.31 % (amounting tk. 179.88 million) to tk. 300.35 million that grabbed 4.19% share in total interest income of DBL. But the enhancement of total interest income on loan outstanding in 2008 was only 27.24% (amounting tk. 1535 million) reaching to tk. 7171 million. The contribution of SME interest income to total interest income rose by 95.79% only $\left[\frac{(4.19-2.14)}{2.14} \times 100 = 95.79\%\right]$ that was 34.32 % ($130.11-95.79=34.32$) lesser than the contribution growth of the year 2007. Again, in year 2009, a 30.02% increase in interest income reaching to tk. 390.52 million generated by SME loan can be observed in the above table. This SME interest income held 5.23% of total interest income generated by total loan outstanding over the year 2009. Though SME interest income increased by 30.02%, total interest income grew by only a minimal rate of 4.11% reaching to tk. 7466 million. The contribution of SME interest income to total interest income was higher by 24.82% $\left[\frac{(5.23-4.19)}{4.19} \times 100 = 24.82\%\right]$ in year 2009, that was again lower by 70.97% ($95.79-24.82=70.97$) than the contribution growth of the year 2008.

5.1.3 Cost of Fund

Cost is one of the main concerns for business organizations that work to make profit. If cost is higher compared to revenue, profit will be lower and vice versa. It is true for Dhaka Bank also which is a profit making service organization. To measure the financial performance of a commercial bank, cost of fund is one of the pivotal issues because commercial banks' prime source of fund is deposits collected from general public and different business organizations. The rate of interest that commercial banks provide to the depositors creates main expense for the banks. Some overhead costs are added with the interest rate paid to the depositors and thus banks calculate their cost of fund for a particular year. Banks therefore apply the cost of fund rate on their loan outstanding over the year to obtain the taka amount of cost of fund for their different lending product. Thus the formula for calculating cost of fund is:

Average Cost of Fund = Average rate of Interest paid to the Depositors + Rate of Overhead Cost

Cost of Fund (Volume) = Avg. Rate of Cost of Fund x Total Loan Outstanding at the year-end

The above formula is provided by the Dhaka Bank Limited where they have not included the cost of equity capital. Dhaka Bank does not include equity capital in calculating their cost of fund. The reasons given by the management of DBL are, firstly, it is DBL's policy to calculate cost of fund to recognize profits from different lending product as the portion of equity capital is very negligible compared to the other source components of total fund available. Secondly, it is the policy of Bangladesh Bank for the foreign private banks (FPB) to deposit the entire amount of equity capital in Bangladesh Bank where the FPBs are unable to utilize the equity capital. Though, there is no written policy for the private commercial banks (PCB) to put their entire equity capital, yet, PCBs have to put certain amount of their depository capital as CRR (cash reserve ratio) and SLR (Statutory Liquidity Reserve) in Bangladesh Bank that is equal or higher than the total amount of equity capital. Thirdly, the amount of equity capital is very lower or negligible compared to deposit that is the major source of fund.

All the commercial banks that finance SMEs get some sort of refinancing from Bangladesh Bank. The rule is, a commercial bank can claim to get refinancing facilities from Bangladesh Bank based on the amount that are taken by customers as SME loan from that commercial bank. According to Bangladesh Bank SME refinancing scheme, the commercial banks get the claimed amount of SME loan outstanding at a bank rate of 5%. As per the rule, Dhaka Bank also gets refinancing facilities from Bangladesh bank but only few amounts of the claimed are collected from Bangladesh Bank at a rate of 5%.

Table 8: Refinanced Amount in SME Loan Outstanding

	<i>Figure in Million Tk.</i>				
	Year				
	2005	2006	2007	2008	2009
SME Loan Outstanding	45.00	252.54	752.96	1,766.75	2,366.80
Refinanced Loan Outstanding	0	0	27	155.87	235.73
Refinanced Loan outstanding % of total outstanding	0.00%	0.00%	3.59%	8.82%	9.96%

Source: Secondary

The above table 8 shows the amount of year-end SME loan outstanding, year-end refinanced amount of loan outstanding and refinanced amount of loan as % of total SME loan outstanding.

According to table 8, it is apparent that, in year 2005 and 2006, there was no refinancing amount outstanding on total SME loan outstanding. Thus, Dhaka banks

had to bear normal cost of fund on their SME loan outstanding. In year 2007, 2008 and 2009, Dhaka bank has some amount of refinancing amount outstanding that was amounting tk. 27 million, tk. 155.87 million and tk. 235.73 million respectively. The refinancing amounts outstanding in those years were 3.59%, 8.82% and 9.96% of SME loan outstanding at the year-end of 2007, 2008 and 2009 respectively. Thus, for the portion of refinanced amounts, cost of funds were comparatively lower than bank's overall cost of fund.

Following table 9 shows the amount of cost of fund in SME loan and the amount of cost of fund in total loan from year 2005 to 2009. According to the table, in year 2005, the volume of cost of fund in SME loan outstanding was found to be tk. 4.58 million that was 0.19% of cost of fund in total loan outstanding amounting to tk. 2376.93 million. A swelling growth was existing in the year 2006 in cost of fund of year-end SME loan outstanding.

Table 9: Cost of fund for SME Loan, Cost of Fund for Total Loan and Contribution of SME Cost of Fund in Total Cost of Fund

	Years				
	2005	2006	2007	2008	2009
Cost of Fund(Vol.) for Total Loan	2,376.93	3,806.68	4,516.84	5,730.18	5,788.35
Cost of Fund(Vol.) for SME Loan	4.58	28.23	84.01	196.85	250.25
Cost of Fund(SME) as % of Total Cost of Fund	0.19%	0.74%	1.86%	3.44%	4.32%

Figure in Million Tk.

Source: Secondary

As per the above table 9, it is revealed that, in the year 2006, the cost of fund for SME loan outstanding was bumped in to tk. 28.23 million having a growth of 516.93% over and above the amount of cost of fund of SME in year 2005. Compared to that, the cost of fund for total loan outstanding attained only a 60.15% growth (amounting tk. 1429.75 million) and reached to taka 3806.68 million. In the year 2006, though cost of fund of SME had higher growth, still, in total cost of fund, it was able to grip only 0.74% share that was 289.47%. [$\{(0.74\% - 0.19\%) / 0.19\% \} * 100\% = 289.47\%$] higher than that of the share on total cost of fund in year 2005.

In the year 2007, the growth rate of SME cost of fund was 197.56% (amounting tk. 55.78 million) than that of the cost of fund volume for SME in previous year

2006. The SME cost of fund amounting to Tk. 84.01 million thus achieved a share of 1.86% in the total cost of fund amounting tk. 4516.84 million in year 2007. The cost of fund for SME grew a lower of 61.78 % $\left[\frac{516.93\% - 197.56\%}{516.93\%} * 100\% = 61.78\%\right]$ in year 2007 compared to the growth of the year 2006. Also, the growth in contribution that SME cost of fund made in total cost of fund in 2007 was lower by 138.12% $\left[\frac{1.86\% - 0.74\%}{0.74\%} * 100\% = 151.35\%; (289.47\% - 151.35\% = 138.12\%)\right]$ compared to the contribution growth made in year 2006. On the other hand, total cost of fund grew by only 18.66 % (amounting tk. 710.16 million) and reached to tk. 4516.84 million. In year 2007, total cost of fund grew lesser by 68.98% $\left[\frac{60.15\% - 18.66\%}{60.15\%} * 100\% = 68.98\%\right]$ from the growth of that in the year 2006. It has been divulged in year 2008 that, the cost of fund for SME attained a growth of 134.31% (amounting tk. 112.84 million) over the year 2007 amount and reached to tk. 196.85 million. The total cost of fund in year 2008 enjoyed a bit higher growth of 26.86% that was 43.94% $\left[\frac{26.86\% - 18.66\%}{18.66\%} * 100\% = 43.94\%\right]$ higher than the growth of that in year 2007. In comparing cost of fund contribution of SME in total cost of fund, it is found that, in year 2008, SME cost of fund grasped a 3.44% share in total cost of fund that was 84.95% $\left[\frac{3.44\% - 1.86\%}{1.86\%} * 100\% = 84.95\%\right]$ higher than the contribution of year 2007. Yet, the SME cost of fund contribution growth made in year 2008 was lower by 66.40% $(151.35\% - 84.95\%)$ than the contribution growth made in the year 2007.

Lastly, in year 2009, the growth in SME cost of fund was 27.13 % (by tk. 53.4 million) reaching to tk. 250.25 million that was 79.80% $\left[\frac{134.31\% - 27.13\%}{134.31\%} * 100\% = 79.80\%\right]$ lower than the growth in SME cost of fund in year 2008. The growth in total cost of fund in year 2009 was only 1.02% (by tk. 58.17 million) reaching to tk. 5788.35 million, that was lower by 96.20% $\left[\frac{26.86\% - 1.02\%}{26.86\%} * 100\% = 96.20\%\right]$ compared to the growth achieved in the year 2008. The SME cost of fund grabbed a 4.32% share in total cost of fund in year 2009 that was 25.58% $\left[\frac{4.32\% - 3.44\%}{3.44\%} * 100\% = 25.58\%\right]$ higher than the contribution made in year 2008. But contribution growth made by SME cost of fund to total cost of fund in 2009 was lower by 59.37% $(84.95\% - 25.58\% = 59.37\%)$ than that of the growth made in year 2008.

According to the above table and elucidation, it is clear that the cost of fund for SME grew a somewhat steady manner though the increase in the growth in SME cost of fund was higher in initial years. It can be easily commented that, the contribution of SME cost of fund was increasing in the total cost of fund in year 2005 to 2009.

5.1.4 Non-Performing Loan

A non-performing loan is a loan that is in default or close to being in default that is, a loan that is not earning income and: (1) full payment of principal and/or interest is no longer anticipated, (2) principal or interest is 90 days or more delinquent, or (3) the maturity date has passed and payment in full has not been made. (*source:www.wikipedia.com*)

According to Bangladesh Bank vide BRPD circular No.07 dated 03.11.04, regulation no. 13, the non-performing loan is divided into four categories. These are:

- a) SMA or Specially mentioned Account
- b) SS or Substandard Loan
- c) DF or Doubtful Loan
- d) BL or Bad and Loss

Generally, interests on loan outstanding are calculated on daily basis but are charged to the clients' loan account on quarterly basis. But bank when calculating total interest income, applies per annum interest rate on the year end or 31st December loan outstanding.

SMA or Specially mentioned Account

When interest on loan or principal amount of loan is not paid by the borrower by 90 days from the due date, that loan account is called specially mentioned account or SMA.

SS or Substandard Loan

When interest on loan or principal amount of loan is not paid by the borrower by 180 days from the due date, that loan account is called substandard account or SS.

DF or Doubtful Loan

When interest on loan or principal amount of loan is not paid by the borrower by 270 days from the due date, that loan account is called doubtful loan account.

BL or Bad and Loss

When interest on loan or principal amount of loan is not paid by the borrower by 1 year or more from the due date, that loan account is called bad and loss account.

Banks generally maintain certain amount of provision in fear of having non-performing loan. But bank has to write-off that bad and loss loan by debiting provisioned amount for that particular loan.

The following table 10 states the total amount of non-performing loan and amount of non-performing loan in SME from year 2005 to year 2009. According to the following table, the total amount of non-performing loan was tk. 351 million and surprisingly, there was no non-performing loan in SME in the year 2005. In the second year of study that is, in year 2006, though the amount of non-performing loan grew by 57.83% (amounting tk. 203 million) compared to the year 2005 and reached to tk. 554 million, the non-performing loan in SME was absent. Thus, both in year 2005 and year 2006, the contribution of SME in total non-performing loan was nothing or “zero” which is a noticeable point.

Table 10: Non-Performing Loan in SME, Total Non-Performing Loan and Contribution of SME Non Performing Loan in Total Non Performing Loan

Types	Years				
	2005	2006	2007	2008	2009
Total Non Performing Loan (NPL)	351	554	1,258	1,908	2,946
Non Performing Loan (NPL) in SME	0.00	0.00	5.00	17.10	100.00
NPL(SME) as % of Total NPL	0.00%	0.00%	0.40%	0.90%	3.39%

Source: Secondary

In the year 2007, the total amount of non-performing loan grew by 127.08% or by tk. 704 million and reached to tk. 1258 million. The growth in total non-performing loan in year 2007 was 119.75% $[\{(127.08\% - 57.83\%) / 57.83\% \} * 100\% = 119.75\%]$ higher than that of the year 2006. As there was no non-performing loan in SME, the growth in SME non-performing loan was absent from the schedule. But from year 2007, SME non-performing loan started to contribute in the total non-performing loan and in 2007 the contribution was 0.40%.

A growth of 242% was experienced in SME non-performing loan in the year 2008. In year 2008, SME non-performing loan increased by amounting tk. 12.1 million and reached to tk. 17.10 million. On the other hand, a lower percentage increase was there in total non-performing loan in year 2008 compared to the year 2007. In 2008, a 51.67% increase (amounting 650 million tk.) in total non-performing loan was found that was 59.34% $[\{(127.08\% - 51.67\%) / 127.08\% \} * 100\% = 59.34\%]$ lower than the growth of year 2007. The contribution of SME non-performing loan in total

non-performing loan was 0.90% that was 125% $\left[\frac{(0.90\% - 0.40\%)}{0.40\%} * 100\% = 125\%\right]$ higher than the contribution % in the year 2007.

In the year 2009, a 484.80 % (amounting 82.9 million) increase in non-performing loan was revealed in SME that was tk. 100 million. This growth of increase was 100% $\left[\frac{(484.80\% - 242.00\%)}{242.00\%} * 100\% = 100\%\right]$ higher than the growth of increase in SME non-performing loan in the year 2008. Again, the growth in total non-performing loan was 54.40% (amounting 1038 million tk.) in year 2009 and the amount of total non-performing loan reached to tk.2946 million. The growth in total non-performing loan was 5.28% $\left[\frac{(54.40\% - 51.67\%)}{51.67\%} * 100\% = 5.28\%\right]$ higher than the growth of that in year 2008. In the year 2009, the contribution of SME non-performing loan to total non-performing loan was 3.39% that was 276.67% $\left[\frac{(3.39\% - 0.90\%)}{0.90\%} * 100\% = 276.67\%\right]$ higher than the contribution made in year 2008. Again, the 276.67% growth in the contribution made by SME non-performing loan in total non-performing loan was higher by 151.67% $(276.67\% - 125\% = 151.67\%)$ than that of the contribution made by SME in year 2008.

From the above table 10, it has already been exposed that the growth of SME non-performing loan and total non-performing loan were not smooth. Rather, in case of SME, the first two years of study faced a vacuum growth as there were no nonperforming loan in year 2005 and year 2006. After that, in year 2007, a small amount of loan in SME was non-performing that was a good sign but as the year passed by, from 2008, non-performing loan started to shadow SME in an increasing manner that was quite upsetting for Dhaka Bank. The disrupting rate of increase in total non-performing loan and the year-by-year higher contribution of SME non-performing loan to total non-performing loan are really alarming for Dhaka Bank.

5.1.5 Number of Borrowers

It is ultimate the customer or client or borrower who is the “Golden Goose” for commercial banks because from borrower comes income. As commercial banks are profit organization, profit is the ultimate goal. This profit or net income is one of the crucial ways to prove that the firm is performing well. But the business of the bank is other way around. Following table 11 shows the number of borrowers in SME loan and the number of borrowers in total loan from the year 2005 to 2009. According to the following table, there were 116 numbers of SME borrowers and 9358 number of total loan borrowers in Dhaka Bank Limited in the year 2005.

Table 11: Number of Borrowers in SME Loan, Number of Borrowers in Total Loan and Contribution of SME Borrowers in Total Number of Borrowers

Types	Year				
	2005	2006	2007	2008	2009
Total Number of Borrower	9,358	12,649	15,420	22,751	27,572
Number of Borrower in SME Loan	116	443	1,282	1,475	1,600
No. of SME Borrower in Total No. of Borrower	1.24%	3.50%	8.31%	6.48%	5.80%

Source: Secondary

In the year 2005, the contribution that SME made in terms of number of borrowers was 1.24% in total number of borrowers. Again, in year 2006, the number of SME borrowers grew by 282% and reached to 443 numbers. But the growth in total number of borrowers was much depressing because it grew only by 35% and reached to 12,649 numbers. In year 2006, the contribution made by SME to total number of borrowers was 3.50% that was 182.26% $\left[\frac{(3.5\% - 1.24\%)}{1.24\%} \times 100 = 182.26\%\right]$ higher than the previous year's contribution.

In the year 2007, total number of borrowers grew by only 22% reaching to 15,420 numbers. The growth in total number of borrowers was 37.14% $\left[\frac{(35\% - 22\%)}{35\%} \times 100 = 37.14\%\right]$ lower than the growth of that in the year 2006. Again, the number of SME borrowers grew by 189% reaching to 1,282 numbers that was 32.98% $\left[\frac{(282\% - 189\%)}{282\%} \times 100 = 32.98\%\right]$ lower than the growth of that in the previous year. The contribution of SME borrowers in total number of borrowers was 8.31% that was 137.43% $\left[\frac{(8.31\% - 3.50\%)}{3.50\%} \times 100 = 137.43\%\right]$ higher than that of the contribution made in year 2006. Thus, the contribution growth in year 2007 was 44.83% $[182.26\% - 137.43\% = 44.83\%]$ lower than the contribution growth of SME borrower in total number of borrowers in year 2006.

In the year 2008, a huge fall in the growth of number of borrowers in SME was present. As per the above table, SME number of borrowers grew by only 15% in 2008 and reached to 1,475 numbers. The growth in 2008 was 92.06% $\left[\frac{(189\% - 15\%)}{189\%} \times 100 = 92.06\%\right]$ lower than the previous year's growth in number of SME borrowers. Again, the growth of total number of borrowers was a bit higher than the previous year's growth. In 2008, total number of borrower grew by 48% (by 7,331 numbers) to 22,751 numbers of borrowers. The growth in total number of borrower was 118% $\left[\frac{(48\% - 22\%)}{22\%} \times 100 = 118\%\right]$ higher than that of the previous year's growth. The contribution made by SME number of borrowers in total

number of borrowers in 2008 was 6.48% that was lower by 22.02% [$\{(8.31\% - 6.48\%) / 8.315\} * 100 = 22.02\%$] that the previous year's contribution.

In the year 2009, the number of SME borrowers grew further low than the growth achieved in year 2008. The number of SME borrowers grew by only 8% and reached to 1600 numbers in 2009 that was 46.67% [$\{(15\% - 8\%) / 15\} * 100 = 46.67\%$] lower than the growth of that of year 2008. Again the total number of borrowers also grew by only 21 % (4,821 numbers) to 27,572 numbers in 2009 that was 56.25% [$\{(48\% - 21\%) / 48\} * 100 = 56.25\%$] lower than the growth of that in the year 2008. The contribution made by SME number of borrowers in total number of borrowers was 5.80% that was lower by 10.49% [$\{(6.48\% - 5.80\%) / 6.48\} * 100 = 10.49\%$] than that of the contribution made by SME borrowers in 2008.

According to the above table and clarification, the total number of borrowers are increasing at a fluctuating rate from year 2005 to year 2009. An increasing trend is revealed in the SME number of borrowers from year 2005 to year 2009. But the growth of increase was slower in those years.

Besides the above five parameters to analyze the performance of SME financing, based on the different articles' reference, ROA has been used to measure the financial performance of the bank as a whole. As the hypothesis is related to the study of ROA of pre SME financing period from year 1998 to year 2002 and post SME financing period from year 2005 to year 2009, both periods' ROA analyses have been done in the following to understand the situation of ROAs, their growths and their trends in pre SME financing and post SME financing period.

5.2 Return on Assets (ROA) Analysis

ROA or return on assets is the ratio of net income and average total assets. Tarawneh (2006), and Townsend et.al (2001) have shown that ROA can be used as the measure of financial performance of a private commercial bank. In other study of Elizabeth (2004), ROA is used as a measure of financial performance of private commercial banks. Thus in this study also, ROA is used as the prime measure of financial performance of Dhaka Bank Limited. Following table 12 and table 13 shows the ROA values for year 1998 to 2002 and year 2005 to year 2009 respectively.

Table 12: ROA from Year 1998 to Year 2002

	Year				
	(Figure in %)				
	1998	1999	2000	2001	2002
ROA	0.69	0.99	1.49	1.52	1.23

Source: Secondary

According to table 12, ROA of Dhaka Bank was increasing from year 1998 to year 2001 but in year 2002, ROA was decreased a bit. Correlating to table 12, figure 1 shows the growth of ROA of Dhaka Bank from year 1999 to year 2002.

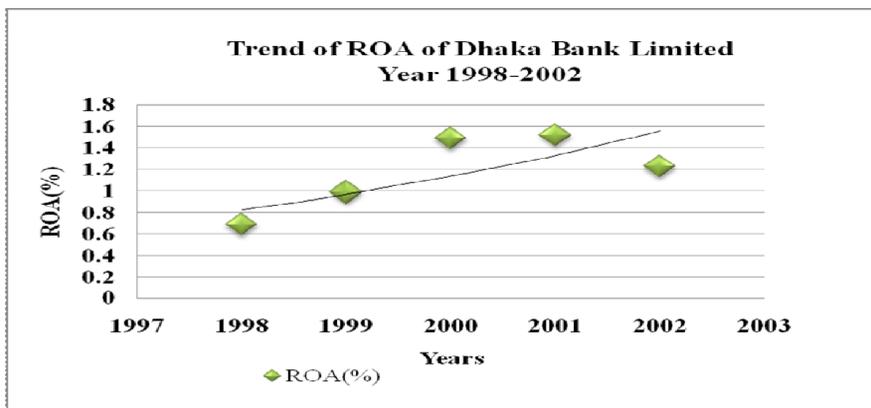


Figure 1: Trend of ROA of DBL (Year 1998 - Year 2002)

The above figure 1 shows the trend of ROA from the year 1998 to year 2002. According to the above trend graph, an increasing or upward movement is revealed in ROA from year 1998 to year 2002. Though the trend line has touched only one point of ROA in year 1999, other points are not that much far away than the trend line. Though, the ROA of year 2002 grew in a decelerating mood compared to the growth of ROA in other years from 1998 to 2002, the trend line is showing an accelerative progress in those years.

Table 13: ROA from Year 2005 to Year 2009

	Year (Figure in %)				
	2005	2006	2007	2008	2009
ROA	1.4	1.22	1.23	1.18	1.29

Source: Secondary

The above table 13 shows the ROAs from the year 2005 to year 2009. According to the above table, the ROA figures were both increased and decreased over the year 2005 to year 2009. For e.g., in the year 2005, the ROA was 1.4% but the ROA decreased in year 2006 and reached to 1.22%. Again, in 2007, ROA was 1.23% but in 2008, ROA decreased to 1.18% and so on.

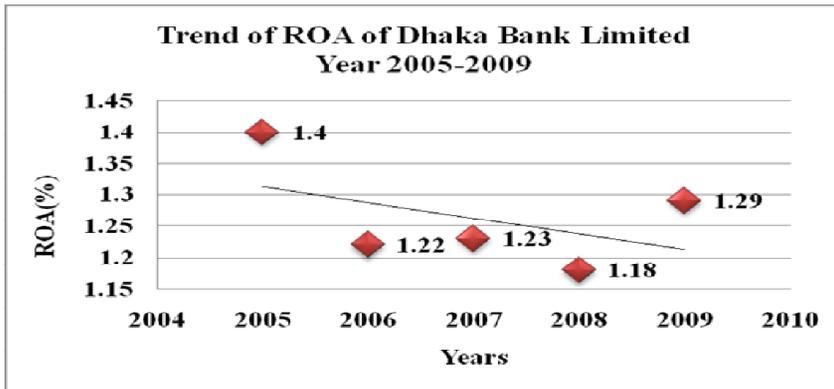


Figure 2: Trend of ROA of DBL (Year 2005 - Year 2009) Source: Secondary

The above figure shows the trend of ROA from the year 2005 to year 2009. If all the points on the above figure 2 would be added, a curvy movement could be found. But the trend line did not touch any single point and reveals a decreasing trend in the value of ROAs from a 2005 -2009 period. Among all the outliers, the nearest point of the trend line is the ROA value of the year 2007.

5.3 Hypothesis Testing

For testing the hypothesis mentioned in chapter 1, analysis of “Independent Sample t-test” has been done with ROA of Year 1998 to Year 2002 and ROA of Year 2005 to Year 2009 respectively with SPSS 12 .The result are shown below through table 14 and table 15.:

Table 14: Group Statistics

	Introduction of SME financing	N	Mean	Std. Deviation	Std. Error Mean
ROA	ROA without SME financing	5	1.1840	.35011	.15658
	ROA with SME financing	5	1.2640	.08562	.03829

Table 15: Independent Samples Test

	t-test for Equality of Means					95% Confidence Interval of the Difference	
	t	df	Sig. (2-tailed)	Mean Difference	Std. Error Difference	Lower	Upper
Equal variances assumed	-.496	8	.633	.0800	.16119	-.45170	.29170
Equal variances not assumed	-.496	4.477	.643	-.0800	.16119	-.50935	.34935

According to the above tables of SPSS outputs, the “sig value” that is also called “p-value” is 0.633.

According to the above table 15, the α value is 0.05 and sig value or p value is 0.633 which is greater than α value. That is the null hypothesis is accepted. Therefore, based on the above analysis, it can be proved that, there is no significant impact of SME financing on the financial performance of Dhaka Bank Limited.

6. FINDINGS

An analysis has been done on the SME financing situation of Dhaka Bank from year 2005 to year 2009 in terms of loan outstanding, interest income, cost of fund, non performing loan and number of borrowers and the impact of SME financing in the financial performance of Dhaka Bank. To analyze the impact of SME financing, an “Independent Sample t-test” has been done to know if there is any difference of the financial performance of Dhaka Bank represented by ROA before the introduction of SME financing in the lending portfolio and after the introduction of SME financing in the lending portfolio. From the analysis, following observations are found:

- i. Both the total loan outstanding and SME loan outstanding grew positively from the year 2005 to year 2009 but in both cases, the growth rates were decreasing. SME loan outstanding grew at a rate higher than that of total loan outstanding. The contributions of SME in terms of loan outstanding increased throughout the 2005-2009 year period but, the contribution was negligible such as 0.19% in the year 2005.
- ii. Similar to loan outstanding, both the interest income from SME loan outstanding and total loan outstanding grew positively throughout the study period but at a decreasing rate. In this case also, interest income from SME loan outstanding grew at a higher rate than that of total loan outstanding. The contribution of SME interest income to total interest income grew positively in the study period but, the percentages were very low such as 0.23% in year 2005.
- iii. In the first two years of the study period, no refinanced amount was outstanding but after that from year 2007, refinanced amount was there and the cost of fund for SME loan outstanding and total loan outstanding grew positively but at a decreasing rate that was a good sign. The

contributions of cost of fund for SME loan to total cost of fund were increasing but the contribution were negligible such as 1.86% in year 2007.

- iv. In the first two years of study period, though there was no nonperforming loan(NPL) in SME , still the total NPL grew positively at a fluctuating rate that is, in some years, total NPL increased while in other years total NPL decreased that is a alarming sign. Again, from year 2007, SME started to contribute insignificantly in NPL and the growth rate of NPL of SME was increasing positively that was again alarming and the growth rate of SME NPL was higher than that of total NPL.
- v. The number of SME borrowers though started to increase at a good rate for example-the growth rate was 282% in year 2006.But year by year of the study period, the growth rate decreased. The growth rates of total number of borrowers were not steady i,e, in some year the growth rate increased while in other years the growth rate decreased. The involvement of SME in terms of number of borrowers revealed a surprising trend. Till the year 2007, the contribution of SME increased in total number of borrowers though not significantly for example-in year 2005, the contribution of SME to total number of borrowers was 1.24%.From year 2008, the contribution started to decrease. That is, SME borrowers were not increased as expected.
- vi. Though the interest income from SME increased positively because of increasing SME loan outstanding, due to the presence of high growth rate of NPL in SME sector and lower growth rates of number of borrowers, the interest income increased at a decreasing rate.
- vii. As the higher or positively growing SME loan outstanding triggered to higher or positively growing the cost of fund for SME, due to the presence of refinancing facility of Bangladesh bank, the cost of fund grew at a decreasing rate. As the cost of fund increased positively, the interest income though increased, but did not increase at expected rate.
- viii. Again, because of refinancing facility, the growth in cost of fund for SME was positive yet decreasing. The DBL management commented that, they did not get the full amount of SME loan outstanding claimed to Bangladesh Bank. As a result, the cost of fund did not decrease at a rate that should be

happened. Therefore, the interest income from SME grew at a positive yet decreasing rate.

- ix. Besides higher SME loan outstanding, another reason for positive yet decreasing growth rate of interest income can be the higher interest rates in initial years and lower interest rates in later years of the study period charged by DBL on SME loan products.
- x. After the global financial turmoil, when the corporations especially the foreign currency earning sectors were under high pressure, the Government of Bangladesh started to focus more on SME by which the Govt. tried to boost up the economy. Again, Bangladesh Bank provided a clear definition for SME for the banks, emphasized on decreasing the lending rate for SMEs and started to refinance SME program to inspire banks. Other donor agencies for example-USAID started to refinance SME by providing bad and loss loan to different banks that have arrangements with them. The resulting situation is, DBL started to increase its SME loan outstanding and the interest income automatically started to increase. But due to different problems in SME financing (that are described in details in the next chapter) such as collateral problems, information insufficiency etc., the loan disbursement did not increase as expected. Relating to this, the total numbers of borrower increased at a fluctuating rate and the interest income increased at a decreasing rate.
- xi. From year 1993 to 2001, ROA increased but in year 2002, ROA decreased. Again, from year 2005 to 2009, ROA followed wavy pattern that means, in some years, ROA increased while in other years ROA decreased. It means, from year 2005 to 2009, as it has already been shown that, the total loan outstanding, interest income, cost of fund, total NPL increased, NI might not be increased proportionately to total loan outstanding. As a result, in the formula of $ROA = NI / \text{Average Total Assets}$, the denominator increased at a much higher rate than the numerator in some years. That is why, in some years, ROAs increased and in other years ROAs decreased.
- xii. From the impact analysis, it is found that, the sig. value or p value is greater than the α value. That indicates, there is no significant difference between ROAs of before and after the introduction of SME financing in the lending portfolio. Thus, it is proved that, there is no significant impact of SME financing on the total financial performance of Dhaka Bank Limited.

7. PROBLEMS ENCOUNTERED BY DHAKA BANK LIMITED IN SME FINANCING

The problems encountered by Dhaka Bank Limited in financing the Small and Medium Enterprises (SME) are as follows:

a) Problems in SME Definition

There is no universally accepted definition of small and medium industries. The Industrial Policy 1999 and the definition provided by Bangladesh Bank do not explain the rationale for the choice of the particular size classification scheme adopted by it. The classification schemes also suffer from some ambiguities. It is not clear from the definition which category an enterprise will belong to if the size of its capital assets and workforce fall into two different categories. For example, if an enterprise employ 75 workers and has Tk. 1 Crore worth of fixed assets should it be ranked as a small or a medium enterprise?

The definition also ignores capital intensity or automation. Some industries may be highly automated with heavy expenditure in fixed capital (say in excess of Tk. 100 Crore), but employ fewer than 100 workers, whereas some other enterprise, such as readymade garments, may employ more than 500 workers with an investment in fixed capital of less than Tk. 15 Crore. If we go by employment criterion, then the garment industry would be regarded as a large enterprise and the textile industry as a medium enterprise. But if we use the fixed capital criteria we shall reach the opposite conclusion. If we want to use both criteria simultaneously it will not be possible to classify them at all.

Another problem with the Industrial Policy 1999 definition is that fixed capital includes land. Unit price of land varies depending on location. Thus the value of fixed assets of two industrial factories, one located in, say, Dhaka metropolitan area and the other in a rural area will vary enormously because the land value in Dhaka could easily be 100 times more than that in a rural area outside of Dhaka city. Hence, two identical factories with identical buildings, machinery and workforce could be classified differently simply because of land value. Since the value of land does not play any direct role in production, it may be excluded from the calculation of fixed assets. In that case the value of fixed assets will be invariant to the firm's geographic location.

b) Insufficient Collaterals Provided by SMEs

SMEs are regarded as high-risk borrowers because of their low capitalization, insufficient assets and their inability to comply with collateral requirements of the bank. Generally, the small enterprise entrepreneurs are middle class or lower

middle-class people who starts their business by borrowing from private money lenders named as “Mohajon”, borrowing from friends, borrowing from cooperative societies or from banks. In case of bank borrowing, collateral is needed. In most of the cases, the entrepreneurs are obliged to put their stocks in trade as collateral and any other fixed assets (for e.g.-land, building etc.) as they do not have own land or other fixed assets. Stocks are regularly bought and sold and counted as secondary temporary collateral by the Bank. Thus, DBL faces collateral problems regarding SME financing.

c) Insufficient Information Provided by SMEs Entrepreneurs

In some cases, the SME entrepreneurs are not properly educated to maintain sufficient accounting records of their organization. Some of the SMEs are managed by entrepreneurs themselves with 2 to 5 employees who are in some cases, poor relatives or are family members of the entrepreneur. These entrepreneurs count only the sales of goods and cost of goods sold on daily basis but not in the proper way. Sometimes, these SMEs do not have TIN numbers and other necessary information. Thus, it becomes difficult by DBL branch officials to collect formal documents and financial statements from the client that support sanction and disbursement of SME loan. Also, for the lack of sufficient information, it becomes difficult for DBL to predict loan repayment ability by SMEs. Thus, the non-availability of client's detailed information is another type of obstacle faced by DBL.

d) Information Asymmetry

Sometimes, the SME clients provide misinformation to get bank loan. But when bank officials go for visit of both business and collateral provided; they find information regarding businesses and or collaterals that do not match with the information provided. This misinformation is vulnerable for DBL because if nonpayment of loan installment occurs, bank will have weak support for loan recovery that might cause the loan to be uncollectible. But in case of corporation, banks have cross matching with CIB report and other business reputation and corporations provide sufficient collateral to get loan. In case of nonpayment, bank will have strong support regarding corporate loan.

e) Lack of SME Clients' Experience in Business

To predict future sales, business experience is necessary. Also, to verify the projected sales, market reputation is necessary for which business experience is vital. As little capital is required to start a small business such as commodity business, stitching business etc. , anyone can start business at any time in Bangladesh now. Though the concept of SME is not new, it is still in an emerging

stage in our country. As a result, many people are becoming inspired and are starting their businesses in an adhoc basis. For this, many new enterprises are rising and financing these SMEs is vulnerable for DBL in that, these entrepreneurs do not have enough business experience and many of them are totally novice in business. So, the sales and working capital projection verification for financing and loan repayment becomes somewhat susceptible for DBL. This is another reason for DBL that create impediment in SME financing.

f) Higher Competition among Similar Businesses

The business that requires minimal capital with little knowledge can be copied easily by others. This is true for SMEs also. It happens regularly that, a business financed by one bank is copied by other in the same place. As a result ,the sales of the first business is decreased as other entrepreneurs are providing same product with less price. So, the bank that financed the first business is at risk of repayment of loan. This is one of the problems encountered by DBL in SME financing.

g) Ignorance and Inability to Express the Need of Loan

In some cases, the SME clients have lack of knowledge and awareness about the SME loans. According to an article of Bangladesh Women Chamber of Commerce and Industry (BWCCI) (2008), a statistics has been revealed for women entrepreneurs that is, in terms of educational level of women entrepreneurs, 10.9% have post graduation degree, 16.8% are graduates, 26.7% have higher secondary education, 34.7% have secondary school level education and 6.9% have minimum primary education. Only 4% of women entrepreneurs interviewed have no formal education but some of them mentioned that they could read and write. As many of the SME entrepreneurs have lack of business experience, they cannot predict the working capital need for their businesses. For this, when the entrepreneurs need loan, they make a hurry to borrow capital from local money lenders or from relatives and friends to avoid their embarrassment with the bank loan. So, when, the sales representatives of the bank go for marketing bank's product, many SME businesses cannot express their needs and purpose for capital. That is another problem faced by DBL.

h) Higher Processing Cost

It is not feasible to monitor and maintain SME with the large corporate clients. Close monitoring and supervision the SME operation is necessary for all times rather than the corporate loan because, SME businesses are not as structured as large or corporate businesses. Thus the overall processing or serving cost is comparatively higher than the large scale loans, because to get the same profit

(in terms of total amount) from corporate loan, the SME Financing Unit of DBL has to process quite a large number of SME loans as these are small scale loans in terms of loan amount. Also, in case of recovery, bank officials have to monitor more SME clients compared to the similar amount of loan recovery from a corporate client. So, more time, workforce and money are required to process SME loans rather than processing corporate loan.

i) Lengthy Loan Disbursement Process

Again, the loan delivery channels are highly centralized. It means, the branches gather the necessary particulars from the client and send it to the SME Financing Unit in the Head Office. The SME Financing Unit in the Head Office does the final approval and CPC (Central Processing Centre) provides final limit sanction of all SME loans. This increases not only the processing cost but also the serving time of any SME loan.

j) Shortage of Manpower and Lack of Proper Training

For a large amount of loan, DBL has to serve higher number of SME clients compared to the number of corporate clients. Also, many of the SME entrepreneurs in Bangladesh have lack of proper education. To make the entrepreneurs understand about the requirement, terms and conditions of getting SME loan, DBL officials need more time and efficiency that requires specific training. Also, more specific officials are needed for processing and monitoring SME which is not there in DBL. Currently, DBL has only 6 SME centers and one kiosk is different semi-urban and urban areas of Bangladesh. Thus, DBL suffers from manpower shortage and lack of training for SME lending that create obstacle in SME lending.

k) Dispersion of SME Clusters

DBL has financed in “Lungi” stitching in Belkuchi of Sirajgonj. There is a community on Belkuchi of Sirajgonj for stitching cotton sarees, lungi etc. If the number of businesses is adequate to reach at breakeven point of opening and fulfilling branch cost, it is feasible to open branch or sales center. In Bangladesh the SME clusters are dispersed in different districts. SME sector has been declared as thrust sector, it is still expanding and for this, it is costly to open a sales center or kiosk where there is not sufficient number of SME businesses in one kilometer of the SME branch to finance in order to reach at break-even point. This is another reason that deters DBL in financing SME as sufficient number of SME centers cannot be opened.

8. RECOMMENDATIONS

As a premier role player in the economy by direct involvement in money supply and raising the capital for business, the Banks are in a significant position for expanding and development of the SMEs in Bangladesh. Dhaka Bank Limited is pretty aware of this responsibility and has already stepped in to the field by extending finance this sector. Though currently, the SME unit of DBL is facing various problems in financing SMEs, the Bank is enthusiastic about the expansion of lending in SME sector and to improve it gradually in a short period.

Some of these problems like collection of necessary paper documents from the SME clients and poor legal framework that is the definition problem cannot be overcome that easily. Since the SME clients are mostly small-scale entrepreneurs, they do not maintain audited or organized financial statements like that of the corporate clients. Therefore, this problem with the documents will always be there till the development of the education level in mass population. Again, the SME Financing Unit of the Bank has nothing to do with the poor legal framework of SME financing. This is the sole responsibility of the policy makers to develop a proper legal framework for financing SMEs.

Considering the findings of this report and present market scenario the following steps can be recommended to catalyze the expansion of SME finance in Dhaka Bank Limited with a more developed and structured network:

a) Introduction of More Branches

The requirements and aspects of SME loan are quite different from that of corporate loan. The large branches are concentrated on generating high volume of profit from a single unit of business in order to match their business target. So, SME financing is not worthwhile from their perspective. But considering the risk involvement and net profit aspects in terms of input and output ratio from a single unit the SME loan is really feasible and attractive for the small, semi-urban and rural branches. So the Bank should expand more SME finance through these branches in order to make them profitable for the Bank.

b) Decentralization of Loan Sanction and Utilization of Multiple Channels

One of the problems faced by DBL is, the lengthy time and high cost in processing SME loan. In order to reduce the high cost and time of processing, DBL should take the following steps:

- ✓ DBL should develop various delivery channels and thus decentralizing the delivery channels, so that branches can process and deliver SME loans by themselves.

- ✓ DBL should utilize multiple channels to collect necessary information of the client before the processing of loan.

c) Introduction of Small SME Centers, KIOSKS

Dhaka Bank Limited should open many small booths, KIOSKS or SME Centers around the country for promotional purpose and for processing the SME loans. It can reach to the customers in the rural and semi-urban areas through these booths. In the big city like Dhaka and Chittagong where the branches are focused to the corporate clients, DBL can service the SME loans by setting up the small SME centers that can cover the most of specific community in a particular area. Places like Islampur, Bangshal, Aminbazar have huge unexploited demand for SME loan that can be met easily by establishing booths in these areas because in Islampur and Bangshal there are different types of retail business such as trading of electric parts, readymade garments etc. DBL should set up alternative channels of distribution like booths are essential for market penetration and as a competitive advantage over other institutions. It should be mentioned that though booths cannot work as branch but booths can be operated with minimum investment and operational cost. As the loan size is small it does not require assigning higher ranked officials for marketing and operating the Loan. The officers to senior officer level officials are good enough for this purpose so the administrative cost will also be low for this product.

d) Recruitment of Aggressive Sales Force

A pool of aggressive sales force focused on SME client hunting, SME loan processing should be increased. Specific marketing strategies should be developed to compete with other banks or financial institutions that provide SME financing facilities. Private Banks like BRAC Bank, Prime Bank Limited, Eastern Bank Limited and foreign Bank Standard Chartered Bank have already established their sales force in this regard. The sales force can be contractual in nature that will lessen the administrative cost because a regular official incurs fixed salary with other benefits costs. DBL has already this type of sales force for marketing and expanding the personal loan, Home Loan and Car Loan products.

e) Proper Monitoring

DBL should assign specific officers in the branches for monitoring and maintaining the SME finance and can arrange incentives for best performers. The concept for “Relationship Officer” for the SME loan should be built up who will not only look after the portfolio but also the lending mix closely with the SME business community to understand their need and make them aware of the benefit of SME loan in the Bank.

f) Arrangement of Training for Employees

DBL should recruit more officials who are interested in building their career in SME lending and adequate training should be arranged for the personnel who work with SME lending. Proper training should be provided to the branch employees so that they can understand the need of the customer and make the appropriate service available to them. The SME sales force should be properly trained and educated about the product and the market.

g) Arrangement of Training for the SME Entrepreneurs

Moreover DBL can arrange training on SME loan problems and solution for the SME clients to make the clients knowledgeable and to create awareness about SME loans. This special arrangement can create unique competitive advantage for DBL and more SME clients can be attracted and with the thorough interaction with them, the current problems that are encountered by DBL mentioned in chapter 10 can be solved with a mutual understanding that will on the other hand enhance the reputation of DBL.

h) Organization of Promotional Activities

DBL should take steps to promote SME loan to SME business persons. According to an article on The Daily Star dated 28.06.2010, many SME business persons are not informed about SME loan provided by banks in the Northern part of Bangladesh. Thus, DBL might arrange advertisements in radio and televisions and should print posters and banners mentioning the advantages of SME loan taken from DBL and provide those in the rural areas. These promotional activities might help a lot to DBL to get more SME clients.

i) Inauguration of Research and Development Wing

Dhaka Bank Limited should inaugurate research and development wing that will perform extensive research on SME to identify the problems in SME financing and to develop the SME financing more as the time is coming for SMEs to reign in Bangladesh.

9.0 Conclusion

The SMEs are worldwide recognized as engines of economic growth. The commonly perceived merits often emphasized for their promotion especially in the developing countries like Bangladesh include their relatively high labor intensity, dependence on indigenous skills and technology, contributions to entrepreneurship development and innovativeness and growth of industrial linkages. The case for fostering SME growth in Bangladesh is certain as these

industries offer bright prospects for creating large-scale employment and income earning opportunities at relatively low cost for the unemployed especially in the rural areas strengthening the efforts towards achieving high and sustainable economic growth which are critically important prerequisites for setting off poverty and socio-economic deprivation. Moreover, the Government is more serious about the SME sectors' development as govt. has allocated nearly 75% of the total industrial development budget and is likely to facilitate the SMEs with substantial duty cuts on the import of basic raw materials. From the above analyses and statistical presentation, it is already clear that, till now, SME financing has no significant impact on the total financial performance of Dhaka Bank Limited. The problems for SME financing and probable solutions are also given in the study. Thus, it is the time to wait and see the steps that DBL will take. The bottom line is not only the profit, but also to build better relationship with SME clients that is the generator of golden eggs. It is expected that, the golden eggs will eliminate the poverty from Bangladesh by developing the economy through the circulation of its value and its radiance in the life of the people.

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