

Investigation of Banker's Lending Criteria to SMEs and Assessment Thereof

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Abstract

Small and Medium Enterprises (SMEs) have large share in Pakistan's economy and they have major contribution in employment and GDP. The financing problem of SMEs is one of the major constraints for their success because banks normally try to avoid the risk of loaning in SMEs due to their small scale of operations. This study investigates banker's loaning criteria for SMEs. Banks in Multan are promoting SMEs by providing them loan. Government has developed and established policies for promoting SMEs in the consequence of which the sector may grow to flourish the economy. Bank loaning criteria is improving by the passage of time due to government support to SMEs. This study crosschecks the lending criteria highlighted by the bank with those argued by SMEs. This assessment is based on a standard questionnaire formulated on the basis of early studies. The factors identified in the questionnaire are Firm age, Firm size, firm size, Distance, Collateral security, Financial documentation, Collateral requirements, No. of sources, Loan relationship, and Deposit relationship. The most important factors considered by banks are collateral, firm size and firm age. The SMEs fulfilling all the factors considered important by banks are facilitated by banks. T-test is used to analyze the responses of SMEs and

Banks. Empirical findings show that all the factors are significant and affirmed by SMEs data. Businesses should focus on these factors to get more finances from the banks.

Key Terms: Lending Criteria, SMEs, Banks, Pakistan

JEL Classification Code: G20

Introduction

Loaning to small and medium businesses is getting more challenging for banks, as SMEs need finance not only for the growth of business but also for taking an initiative. Lots of formal procedures and processes involving the preparation and evaluation of feasibility reports are there. But in spite of all challenges, loan is being provided to SMEs not only for the sake of providing growth opportunities for such enterprises. Loans are being provided by banks of Multan to all SMEs but major of the banks in Multan restrict themselves to provide loan only to those SMEs who have had taken initiative and are in growing phase or those who required loan for networking purposes or acquiring businesses. Banks are more in responsibility phase while circulating finance as they are running the finance of depositors to make it profitable for both, the bank and the depositors. Major of the banks in Multan are obliging SMEs as this sector is in huge expansion to be more beneficial for banks. Unemployment in our country is bringing more people towards entrepreneurial activities so that they can initiate their own businesses and enhancement in entrepreneurship make SMEs more attractive.

Some years back, loaning policies were changed to provide loan to SMEs on more flexible basis to flourish the businesses and also for banks to generate profit. But as the year passes by it is observed that loan to SMEs are being provided but the loaning policies are getting tightened due to the abrupt raise of inflation and the continuous fluctuation in economy. The gradual instability in the factors of economy changes the attractive SME sub-sectors to most difficult SME sub-sector for credit approvals. The fluctuation in the sub-sectors of SMEs from more attractive to less attractive makes SME a risky sector, so the loaning policies of banks to provide loan to SME is getting tightened. Even the pressure of competition from banks and non-banks could not affect bank credit standards for approval of loan to SMEs.

Banks increase loaning to SMEs by providing them opportunities of growth. SME is a growing sector, banks promote SMEs in a way they are promoting medium enterprises but avoiding small enterprises. The enterprises who have had taken initiative but are in growing phase and are considered as small enterprises (by their asset values) are not obliged much by banks. Banks are providing loans to medium enterprises more conveniently than small enterprises. It is also observed, there is high financial gap for small enterprises as compared to medium enterprises. If small enterprises required Rs.5 million as a loan than only Rs.10lac or Rs.20lac is provided by banks. Small enterprises have fewer opportunities for growth than the medium enterprises. But as now, by the passage of time, the competition in established segment raises to force banks to focus on the lower segment. Now, both small enterprises and the medium enterprises is focused equal by banks to be obliged. As SMEs in Pakistan are more than the corporate industries, so SMEs have more chances of growth and are in huge expansion. Now, all banks are obliging SMEs by providing them loan for not only their success but also for the profit of banks.

It is highly observed that loaning policies for small enterprises are more tightened than the medium enterprises. It is also observed that small enterprises demand for loan less than the medium enterprises. Out of SMEs, 10% of the small enterprises demand loan from banks whereas 25% of medium enterprises demand loan from banks. Out of the loan demanded from SMEs, 75% of the applications from small enterprises are rejected by banks whereas 65% of the applications from medium enterprises are obliged by banks in a way to provide loan according to their demands.

In spite of all the precautions taken by banks in providing loan to SMEs, the graph of the percentage of bad debts generated by SMEs increase. SME is a risky sector in which the bad debts

percentage increases with the passage of time. There is flexibility in policies of banks while providing loan to SMEs. Sometimes, the SME loaning policies are tightened by banks to provide loan to SMEs who can fulfill all the requirements define by banks. And sometimes, loaning policies of banks are flexible to oblige SMEs by providing them loan on beneficial basis to seek more profit. For risky sub sectors, more mark up is charged by banks to occupy more profit. The most risky SME sub sector is jewelry sector due to the intense impact of inflation rate and the instable situation for the threat of being theft. Jewelry sector is the most difficult sector for the approval of credit by banks. But if the bank provide loan to jewelry sub sector then loan is provided on high mark up rate. So that the banks can averse risk by providing loan on high mark up to recover the lending amount on early basis. Due to instability in economic condition, the sectors that were more attractive are converted to least attractive sectors. As cotton weaving and textile was the most attractive sub sector of SME. But previous year due to natural disasters, the agriculture land passed through disasters and the cotton growth decreased to pull the cotton weaving and textile a less attractive sector. Due to change in economic stability, cotton weaving and textile and the jewelry sub sector is most difficult for credit approval. But loan have been provided to all sub sectors by banks in Multan. The risky sub sectors are provided by loan on high collateral requirements and on high mark up rate to cut the risk.

There are some constraints faced by SMEs while accessing to finance. As SMEs are treated like large corporate enterprises by major of the banks in Pakistan. However SMEs are far different from corporate enterprises. Financial records are not maintained by SMEs and when SMEs required for loan from banks, it is considered by banks that loan is asked on planned schedule. Whereas SMEs are more sensitive to loan, they are far different from corporate enterprises and demand loan with more sensitivity. They want loan to be provided on short time so that they can fulfill their requirements which appears on short duration. They are more sensitive for loan delivery time as compared to large enterprises. And also SMEs required low value loan transaction to be passed. So, this is required by banks to provide loan to SMEs on early duration so that they can avail the loan amount for required purposes. But banks loaning policies to SMEs are very complex and by following the policies, transactions required time to be passed and also get very costly. So loaning to SMEs get costly as well as time consuming.

The major barrier for SMEs for the access of finance from banks is the financial documentation. Financial documents are not maintained by major of the SMEs. Banks project the future cash flows of SMEs on fixed percentage. The projected percentage of future cash flows is determined by banks. And every bank is free to project the future cash flows of SMEs on the percentage fixed by them. But in spite of all the efforts made by banks in projecting the cash flows of SMEs, banks could not measure the performances of SMEs. So, financial document is important for SMEs in order to have access on finance from banks.

Banks complaint about the weak financial infrastructure of SMEs, as SMEs has weak credit information and collateral infrastructure. But in spite of the bank complaints, loans are being required by SMEs and on their requirements loan are provided by banks. Because SME is a major sector of Pakistan economy, its percentage reaches to 93% of Pakistan enterprises. So, if some SMEs are not on loaning criteria by banks then loans are not provided by banks to such SMEs. Loans are provided to such SMEs who are in strong position to fulfill the requirements of banks. As SMEs are large in number, so if half of the SMEs fulfill the requirements of bank in obtaining the finance then it seems that major of the SMEs demands are being filled by banks and banks have major loan portfolio with SMEs. But it doesn't mean that bank is providing loan to all SMEs. Loan is provided to only those SMEs that fulfill the requirements of banks and are provided with finance from banks in accordance with the bank's loaning criteria.

Banks consider firm size and firm age while providing loan to SMEs. Firm size is the most important for banks while determining the amount of loan required by SMEs along with the providence of loan by banks. The loaning criteria by major of the banks in Multan are, the loaning amount that is provided to SMEs is decided by banks after determining the size of the firm. The size of the firm is

determined through firm assets value along with the number of employees working in the firm. The firm having more asset value and more number of employees have easy access to finance and are obliged by banks easily while providing loan. And the firms having less assets value along with less number of employees are considered as small firms and are provided with loan but the loaning amount is restricted to be not more than Rs.10 million. And for medium enterprises the loaning amount provided by banks is Rs.75 million. Similarly firm age is also considered by banks and is important factor while providing loan to SMEs. Usually banks prefer SMEs who are in growing phase while providing them loan Banks are providing loan to SMEs but by considering and evaluating all the factors. All the banks in Multan are providing loan to SMEs to promote the sector. Loan is provided by banks to SMEs for the welfare of both banks and the SMEs. SME is an important sector in providing profit to banks as this sector is in continuous phase of expansion.

The overall aim of the study is to focus on loaning criteria of banks in Multan while providing loans to SMEs. The factors that are highly considered by bank while loaning to SMEs is discuss in this study to elaborate the loaning criteria of banks while loaning to SMEs. As the loaning decisions of banks based on the factors like firm size, firm age, financial documentation, collateral, distance, loan relationship, deposit relationship and no. of sources, so, by considering these factors bank decide either the loan be provided to a specific enterprise or not. This study elaborates not only the factors considered important by banks while providing loan to SMEs but also elaborate about the fulfillment of banks requirements by SMEs. The importance of the factors is explained in more detail in this study to elaborate about the lending criteria of banks to SMEs. The overall requirements of banks are highly considered by SMEs while having access on finance from banks. The data is collected from both banks and SMEs to know about the loaning decision of banks. Data is collected on the basis of questionnaire technique. Data is analyzed and result is obtained through t-test.

1. History of SMEs

The history of SMEs starts from 1949 when Nation Bank of Pakistan was established. It was the first government recognized bank in Pakistan and it takes initiative for the progress of SMEs. After that in October, 1998 SMEDA (SMEs development authority) was established and take the challenge of developing SMEs. In January 1, 2002 since its inception, SMEs bank (SMEB) provide loan to SMEs with the mission of providing financial assistance to SMEs so that they may contribute for economic development. Then Asian Development Bank takes an initiative of SME development program in 2004 and promotes SMEs by providing them loan. In March 2004 SMEDA discuss with Islamic Chamber of Commerce to arrange an event for SMEs in Pakistan. In 2005, International Finance Corporation of the World Bank provide loan of about \$7 million to Investment Bank Limited for the purpose to finance bank leasing equipment to SMEs and other sectors of Pakistan's economy. In 2008 Pakistan and Italy signed a contract and according to that contract Italy will provide soft loan to SMEs on zero interest for the purpose of development of SMEs in Pakistan. In June 1, 2011 union of SMEs demanded from government to develop ministry of SMEs in Pakistan. In June 3, 2011 member of world bank and State Bank of Pakistan launch series of Publications to help Pakistan banking system to promote loaning of finance to SMEs. In June11, 2011 State Bank of Pakistan signed an agreement between five leading banks in Pakistan and SMEDA, that banks will provide finance to SMEs and will promote the sector for the growth of economy. State Bank of Pakistan has opposed splitting SMEs into small enterprises and the medium enterprises. The splitting of the sector into two is highly discouraged by State Bank of Pakistan. In June 12, 2011 United Nations development program - small development program join SMEs development authority for the support and success of SMEs.

2. Literature Review

The financing policy to SMEs was tightened. But now the bank loaning policies are changing to fulfill the financial needs of SMEs.

Technology problem is always being a large problem for SMEs from being a long period. But now these problems have been overcome to a great extent. A decade ago, technology barriers have been considered by SMEs but now these problems are tried to be resolved. The major problem for any business while taking an initiative is financial access. Along with it many issues arrive, out of these all issues, many technology barriers also arrive but with the access to finance these all barriers have been resolved to major. (Nu, N, Yin.1999) is of the view that electricity problem is one of the major problem for all companies along with the problem of shortage of raw material, capital and foreign currency as financial problems. Technology barriers is also one of the major barrier in success of all companies either they are large, small or medium

Business owners are scared of financing barriers, they assumed that if they could not have financial access then they would not be able to take initiative or run the business. That becomes so scary for entrepreneurs that they are discouraging bank loans. And if the loans are not required by SMEs then it will be discouraging for banks as well as the bank profit will decline. To overcome the situation state bank change the policies of SMEs in order to have easy access to finance. And Government is taking step to overcome all the barriers in financing access to promote not only SMEs but also for the growth of economy and benefits of banks. (Kotey, 1999) is of the view that financing barriers let to business failure and that is the reason many owners or managers avoid taking long term debt.

Banks are highly considered about firm age and firm size. The businesses that have taken initiative and in early stage are avoided by banks while providing loan. And similarly the banks are highly reluctant to provide loan to those small or medium enterprises who are requiring loan on business plan and have not take initiative, in fact they are requiring loan to take initiative of their business from the borrowing amount. As such businesses are not obliged by banks then it gets difficult for the business owners to take initiative without the finance or the financial access. (Kudo, Toshihiro.2002) Banks are risk averse and avoid loaning to new ventures so bank financing is not in much access for new and small businesses. So it is difficult for new ventures to approach banks for financing as their financial needs are not obliged much by banks.

Banks are obliging SMEs by providing them loan. Banks are establishing and improving SME loaning policies so that the SMEs may have easy access on finance. SMEs occupy the major part of businesses and are in continuous expansion phase, so they are promoted by banks in developing SME policies. (Kang and senior fellow) the SMEs loaning is increasing gradually. Banks increase loaning to households and tried to eliminate SMEs risk along with the risk of loaning to large firms since 1997. The SMEs success helps to reduce unemployment rate to major extent. Banks have gradually improved their loaning system for SMEs. SMEs have major contributions for the welfare of economy, so, banks promote SMEs for their success.

Banks are reluctant to provide loan to those business owners that want loan on business plans but have not taken initiative, banks are highly concerned about firm age and firm size. Banks prefer loaning to those businesses that have been initiated or in the growing phase. This attitude of banks usually discouraged the business owners who have best business plan but they didn't take initiative as they have shortage of finance and are too much scared of the bank attitude and policies that they give up, but could not apply for finance from banks. (Kon and storey, 2003) analyze from cases of potential borrowers that there are some borrowers who have perfect business proposal and they can be obliged by banks if they demand for finance as they have potential and can fulfill the bank requirements but they do not apply for loan because they are scared of being rejected. Kon and storey is of the view that the borrowers have potential to access the finance and they have perfect business proposal to apply for loan from banks. They can easily fulfill the loaning criteria of banks but they do not apply for loan as

they are scared of loan rejection. That is the reason they didn't apply for loan and deprived themselves from external finance.

Major of the banks have separate SME sector for providing loan to SMEs. Some financial institutions are also working in Pakistan to provide loan. The major of the contribution in providing loan to SMEs is by banks. Banks are the main source of providing loan to SMEs. Banks have developed SME policies for improving SME loaning system to promote SMEs. (Cosh and Hughes, 2003) are of the view that banks are the main source of finance for SMEs. Banks are the main provider of finance to SMEs.

Banks have different attitude in providing loan. The loaning procedures vary from large banks to small banks. Large banks provide loan to SMEs on the basis of high requirements in the form of collateral and financial documentation. Large banks are highly concerned about their loaning policies and are highly risk averse. So, large banks provide loan to SMEs on strict basis. Whereas the small banks are less concerned about their loaning policies and provide loan to SMEs on the basis of relationship. (Cole, Goldberg and White, 2004) elaborate in their study that the banks have different criteria while providing loan to businesses, banks like large banks provide more loan to medium enterprises than the small enterprises on the base of financial documents and quantitative criteria whereas small banks are more concerned about relationships and provide loan on qualitative criteria.

Collateral is the most important part of loaning, without collateral loan would not be provided to SMEs by banks. Loaning relationship is also considered a very important factor by many of the banks in Multan. This is due to the fact that SMEs who can not provide financial documentation and assets for collateral can be provided by finance on the basis of relationship either in the form of loan relationship, deposit relationship or references. (Bruder, Neuberger and Doppner, 2006) concluded in their study that loan is not provided to those owners of businesses (SMEs) who are in ethnic minorities due to the fact that ethnic entrepreneurs do not have much fixed assets to be used as collateral for collateralized loaning. Such entrepreneurs do not have much information about external financing and relationship loaning, hence they increase financial gap. But if there can exist a better communication system between ethnic minorities and financial institution then financial gap can be reduced.

Banks improving their loaning policies so that they may oblige SMEs by providing them required loan amount. Banks have improved their loaning policies to great extent to promote the SME sector. Some improvements have been made and some are still in process to take the loaning system of bank to be at best. State bank is relaxing the SME loaning system to promote SME sector by considering both banks and SMEs. (Torre, Peria and Schmukler, 2008) are of the view that banks are improving their policies by providing new business models, technologies, and risk management systems to serve SMEs. Loans are provided by banks to SMEs and SMEs market is getting competitive but still need improvements.

It is also observed that if the customers are not satisfied then they will not be back. To satisfy the customers banks have to oblige in some ways. Otherwise the customers will not continue any relationship with banks and if they are discouraged then it means profitability of bank is discouraged. (Lindstrand and Lindbergh, 2010) are of the view that SMEs if find their loaning relationship good with banks then they promote relationship with banks.

Competition of banks also promotes providing finance to SMEs. Due to pressure of competition from banks and financial institution bring some flexibility in loaning system of banks. Government plays an important role in promoting SMEs by relaxing the loaning system to great extent. Loans are provided in major by focusing on structure of economy (either the natural disasters, inflation is effecting economy) and on size of SMEs because this factor is most important for providing loan. (Rocha, Farazi, Khouri and Pearce, 2011) explore in their study that SMEs are provided with loan if the financial infrastructure is improved. Competition of banks improved the system of loaning. Government of Middle East and North America is playing an important role for promoting SMEs. The authors are of the view that potential of financial access by SMEs is determined by structure of economy and size of SME sector.

Due to high risk involved in SMEs raise the cost of financing and markup charge on loan. (Kundid and Ercegovac, 2011) is of the view that SMEs are more risky in Republic of Croatia “optimal interest rate was set” which increased the refinancing cost and reduced credit supply.

Financial documentation is an important factor considered by banks while providing loans to SMEs. But it is clearly mentioned in prudential regulation by SBP that if SMEs couldn't maintain financial documentation as this sector is not developed much to keep all the financial records then banks may project future cash flows of SMEs to provide them loan. It is also necessary for banks to project future cash flows as by projecting future cash flows, banks can determine the risk involved in providing loan to SMEs and to overcome the risk involved in loaning by increasing the collateral. SBP has relaxed the loaning policies of SMEs to major extent, so that, this sector may grow to be developed. In spite of all the facts financial documentation is considered important by banks while providing loans to SMEs. To determine about credit history of SMEs, banks need financial documentation or can determine it through CBI report. (Regulation R-1) it is mentioned in regulation risk-1 that banks are free to predict about the future cash flows and can identify about the key drivers and key risk to SMEs, it is observed that large number of SMEs couldn't maintain financial records and SMEs shouldn't be declined access to credit merely for this reason.

Collateral is the most important factor considered by banks while providing loans to SMEs. State bank has relaxed the loaning system by allowing the banks to provide loan to SMEs without collateral to the limit of 3 million but beyond this limit, collateral may be properly required by banks for their satisfaction and security. Banks highly obliged those SMEs who have fixed assets of high value to be used as collateral while having financial access from banks. (Regulation R-3 and R-4), it is mentioned in regulation risk-3 that finance to the limit of 3 million is provided to SMEs without collateral. And it is mentioned in regulation risk-4 that if SMEs required finance above 3 million then the finance amount may be properly secured by banks for their satisfaction.

Banks are free to decide bank margin on loaning amount by considering the risk involved in loaning to SMEs. If the SME sub sector is risky then loan will be provided by banks on high bank margin, so that the principal amount may be recovered on early basis. But if the SME sub sector is not risky then loan will be provided to SMEs on less bank margin and the loaning policies are less tightened for non-risky sub sector. (Regulation R-5) it is mentioned in regulation risk-5 that banks are free to determine the margin requirements on facilities provided by them to their clients taking into account the risk profile of the borrower in order to secure their interest.

It is also required that banks may be aware of the utilization of loans provided to SMEs, so that they may analyze that the amount provided by banks are in safe hands. Banks have dual responsibilities while providing loans, as, bank act as a borrower (while taking finance) and lender (while providing finance). So, it is highly required by banks to be completely aware of the utilization of loans. If loan is not in safe hands then bank has to suffer for repayment of loan. So, banks prefer loaning to safe SMEs sub-sector to recover the principal amount timely. And for risky SMEs sub-sector bank raise the demand of collateral and also raises mark-up to averse the risk involved in loaning. (Regulation R-9) it is mentioned in regulation risk-9 that the bank should ensure that the loans have been properly utilized by the SMEs and the banks should develop an appropriate system for the utilization of loans.

3. Research Design

3.1. Variables

All the hypotheses are selected on the basis of Cole, Goldberg and White (2004).

3.1.1. Firm Age

Firm age is considered as important factor for the approval of loan. Older firms are most likely to be provided with loan. So there exist a positive relation between firm age and banks loaning decisions.

3.1.2. Firm Size

Firm size is considered on the basis of annual sales and number of employees. Larger firms have more potential to repay and hence are most likely to be provided with loan. Thus there exist a positive relation between firm size and banks loaning decisions.

3.1.3. Financial Documentation

Financial documentation is considered an important factor by banks while providing loans. The firm that maintains financial records can assure about repayments easily. So, it is positively correlated with bank decisions of making loans to firms.

3.1.4. Collateral

Collateral is considered by banks while loaning to firms as if the firms are not able to repay then banks can liquidate the collateral to recover the principal loaning amount. So, there exist a positive relation between collateral and banks loaning decisions.

3.1.5. Distance

This determines the distance between firm and bank. Higher the distance lower will be the loan availability by banks. So distance is considered important by banks while providing loan.

3.1.6. Number of Sources

Number of sources is the number of different sources from where the firm applied or taken the loan. It has a negative impact on bank loaning decisions.

3.1.7. Deposit Relationship

If there was a prior deposit relationship between firms and banks then banks are more aware of the financial condition of firms to provide loan. There exist a positive relation between deposit and banks loaning decisions.

3.1.8. Creditworthiness

If the firm and bank have prior loan relationship then it will be ambiguous that either the relationship may have a positive or negative effect on bank loaning decisions. If the firm has repaid the loan on timely basis with good terms then this relationship has positive effect on bank loaning decisions otherwise it may have a negative effect. So, loan relationship has dual impact on bank loaning decisions.

3.2. Hypotheses

H₁: Firm age is positively correlated with bank decisions of making loans to SMEs.

Firm age is considered to be a very important factor by major of the banks in Multan. Many banks in Multan provide loan to those enterprises that have age of three years or more. This is due to the fact that many banks are of the view that if the SMEs are recently established or have not taken initiative then the owner will have less potential to repay the loan and it will become risky for banks to provide loan to such enterprises. By considering the importance of this factor, banks highly oblige those SMEs having age three years or more. And banks are highly reluctant to provide loan to those enterprises that have recently taken initiative and have an age of 6 months or less. So, firm age is positively correlated with bank decisions of making loans to SMEs. Longer the firm age, higher will be the loaning to firm by banks.

H₂: Firm size is positively correlated with bank decisions of making loans to SMEs.

Firm size is considered on the basis of number of employees and assets of the firms. Higher the firm size, higher will be the cash flows of firms and it will get easy for firms to have financial access from banks. Banks usually oblige SMEs who have high firm size.

H₃: Financial documentation is positively correlated with bank decisions of making loans to SMEs.

Financial documentation is necessary to be maintained by firms in order to have financial access from banks. Banks consider financial documentation as an important factor, but if financial documentation is not maintained by firms then bank itself project the future cash flows of SMEs. And to some extent financial documentation is consider by banks.

H₄: Collateralized loan is positively correlated with bank decisions of making loans to SMEs.

Collateral is the most important factor in bank loaning decisions. Banks highly obliged those SMEs who have fixed assets (immoveable property) to be used as collateral in order to have on finance from banks. Banks also obliged those SMEs who have moveable assets as collateral but to least extent. Collateral being most important factor is highly considered by banks. And if the SMEs don't have assets to be used as collateral, then such are not obliged by banks and banks are highly reluctant to provide loan to such enterprises.

H₅: Distance is considered by banks while providing loan to SMEs.

Distance is an important factor in loaning decisions of banks. Higher the distance lower will be the banks loaning.

H₆: Number of sources is negatively correlated with bank decisions of making loans to SMEs.

If SME has taken loan from more than one banks and if couldn't repay the loaning amount in any of the bank then loan will not be provided to such SME. If SME has taken loan from more than one source then it would be determined through CBI report.

H₇: Deposit relationship is positively correlated with bank decisions of making loans to SMEs.

Deposit relationship is considered an important factor by banks. Due to prior deposit relationship, banks have financial records of SMEs.

H₈: Creditworthiness has direct impact on bank decisions of making loans to SMEs.

Creditworthiness is also important factor

3.3. Sampling Technique

Systematic sampling is used for the selection of sample of banks. Names of banks operating in Multan are arranged in descending order of their number of branches. The interval is calculated through formula i.e.

Interval = population size/ sample size

Interval = 22/11

Interval = 2

So every second bank is included in the sample of banks and for SMEs, two SMEs who have taken loan from each sample bank are surveyed to collect data. In this way the sample size of SMEs is 22.

3.4. Data Collection

The main source of data for the study is collected through 11 banks operating in Multan and 22 SMEs. The systematic sampling technique is used for the selection of samples. The sample of banks is selected through number of branches of banks. Banks name and their branches are arranged and written in descending order. Then the sampling interval is calculated through formula. And after specific interval the bank is selected to generate sample of 11 banks. Out of 22 banks operating in Multan, sample of 11 banks is selected on the basis of systematic sampling. Sample of SMEs is selected on the basis of banks. Banks provide loan to SMEs, so from every bank sample of 2 SMEs is selected by considering the total sample of 22 SMEs from 11 banks. The data is collected through questionnaire techniques while conducting surveys from banks and the associated SMEs. Data from two sources is collected so that the comparative study from banks and SMEs may lead towards positive ends. The same hypotheses will be asked in two different questionnaires to compare and analyze the results from

both banks and SMEs. The major factors that are considered while making questionnaires of both banks and SMEs are firm age, firm size, financial documentation, collateral, distance, loaning relationship, deposit relationship and number of sources. The question relating these factors are included in questionnaires to collect data from two sources i.e. banks and SMEs to analyze the importance of hypotheses.

3.5. Research Methodology

The survey is conducted through questionnaire technique. Every SME and bank is personally visited to collect detailed data according to the requirement of study. The questionnaires used for conducting surveys from banks and SMEs contain closed ended questions in major. The questions are basically related to collateral requirements of banks while loaning, importance of firm size and firm age, bank preferences for firm size and firm age, financial documentation to be maintained by SMEs, distance of SMEs from banks from whom the loan is required, number of sources and the effect of number of sources on banks decision of making loan, deposit and loan relationship. Major of the factors considered important by banks while providing loan to SMEs has given importance while conducting surveys through questionnaire. The quantitative approach is used for this study. T-test is used to obtain the results, analyze about the relationship between dependent and independent variable and to comparatively analyze the study. T-test is used for comparative analysis and value of significance is used to know about the correlation between dependent and independent variables. T-distribution is used to analyze hypotheses when the sample size is less than 30.

4. Empirical Findings

4.1. Results for Data Collected Through Banks

The hypotheses regarding loan approval decisions from data collected through banks and their analysis are.

Table-1: T-test applied on data collected through banks in Multan

Factors	t-stat	df	Sig.
Firm age	8.480	10	.000
Firm size (preference)	9.037	10	.000
Considered firm size	10.488	10	.000
Distance	4.100	10	.002
Collateral security	5.882	10	.000
Financial documentation	5.285	10	.000
Collateral requirements	8.964	10	.000
No. of sources	10.510	10	.000
Loan relationship	8.964	10	.000
Creditworthiness	8.964	10	.000

4.1.1. Firm Age

H₁: Firm age is negatively correlated with bank decisions of making loans to SMEs.

The null hypotheses is “firm age is positively correlated with bank decisions of making loans to SMEs” whereas the alternative hypotheses is “firm age is negatively correlated with bank decisions of making loans to SMEs”. Longer the firm age, higher will be the chance of providing loan to SMEs by banks. It is observed that banks are highly concerned about firm age while providing loan to SMEs through both theoretical and practical framework. The questions related firm age is added in questionnaire of banks to evaluate about the importance of firm age for banks while providing loan. It was observed that major of the banks are reluctant to provide loan to those enterprises who have not taken initiative and also to those enterprises that have an age of less than a year. T-test applied on data

collected from banks to analyze the results. The value of significance shows the relationship between dependent and independent variable. The value of significance comes out to be 0.000 from t-test applied on data collected from both banks, thus showing a strong relationship between firm age and loaning decisions of banks. T-value comes out to be 8.48 from bank collected data. The rejection region, to reject null hypotheses is less than and equal to 2.228 for banks. The t-value is greater than 2.228. So the null hypotheses is accepted that “firm age is positively correlated with bank decisions of making loans to SMEs”

4.1.2. Firm Size

H₂: Firm size is negatively correlated with bank decisions of making loans to SMEs.

The null hypotheses is “firm size is positively correlated with bank decisions of making loans to SMEs” and the alternative hypotheses is “firm size is negatively correlated with bank decisions of making loans to SMEs”. Firm size is very important factor considered by bank while providing loan to SMEs. Higher the firm size, higher will be the chance of providing loan to SMEs by banks. The size of the firm is considered on the basis of number of employees and firm annual sales. Banks are highly considered about firm size while providing loans to SMEs. The value of significance from banks is 0.000 thus showing a strong relationship between firm size and banks loaning decisions. T-value for preferring and considering of firm size is 9.037 and 10.488 from data collected about firm size through banks. The rejection region, to reject null hypotheses is less than and equal to 2.228 for banks. The resulted t-value is greater than 2.228. So the null hypotheses is accepted that “firm size is positively correlated with bank decisions of making loans to SMEs”

4.1.3. Financial Documentation

H₃: Financial documentation is negatively correlated with bank decisions of making loans to SMEs.

The null hypotheses is “financial documentation is positively correlated with bank decisions of making loans to SMEs” and alternative hypotheses is “financial documentation is negatively correlated with bank decisions of making loans to SMEs”. Financial documentation is considered important by banks while providing loan but it is also observed that loan is being provided to SMEs even if they are not maintaining the financial documentation. The reason is to improve the SME sector and to make it more progressive. It has also been mentioned in prudential regulation of state bank that if SMEs could not maintain financial documentation then bank can project about the future cash flows of firm. But the SMEs should not be discouraged and finance may be provided to SMEs.

The p-value from banks is 0.000 thus showing a strong relationship between financial documentation and banks loaning decisions. T-value for financial documentation is 5.285 from data collected through banks about financial documentation. The rejection region, to reject null hypotheses is less than and equal to 2.228 for banks. The resulted t-value for financial documentation is greater than 2.228. So the null hypotheses is accepted that “financial documentation is positively correlated with bank decisions of making loans to SMEs”

4.1.4. Collateralized Loan

H₄: Collateralized loan is negatively correlated with bank decisions of making loans to SMEs.

The null hypotheses is “collateralized loan is positively correlated with bank decisions of making loans to SMEs” and alternative hypotheses is “collateralized loan is negatively correlated with bank decisions of making loans to SMEs”. Collateral security is the most important factor considered by banks while providing loans to SMEs.

The value of significance from banks is 0.000 thus showing a strong relationship between collateral and banks loaning decisions. T-value for collateral security and collateral requirement are 8.964 and 5.882 from data collected through banks. The rejection region, to reject null hypotheses is less than and equal to 2.228 for banks. So, the t-values for collateral security and collateral requirement

are more than 2.228. Hence, the null hypotheses is accepted that “collateralized loan is positively correlated with bank decisions of making loans to SMEs”

4.1.5. Distance

H₅: Distance is not considered by banks while providing loan to SMEs.

The null hypothesis is “Distance is considered by banks while providing loan to SMEs.” and alternative hypothesis is “Distance is not considered by banks while providing loan to SMEs”. Distance is considered by some of the banks and other banks are of the view that they do not impose any restriction of distance for the finance access to SMEs. The value of significance from banks is 0.002, thus showing a strong relationship between distance and banks loaning decisions. T-value for distance is 4.1 from data collected through banks about distance. The rejection region, to reject null hypotheses is less than and equal to 2.228 for banks. The t-value for distance is more than 2.228. So the null hypotheses is accepted that “Distance is considered by banks while providing loan to SMEs”

4.1.6. Number of Sources

H₆: Number of sources is positively correlated with bank decisions of making loans to SMEs.

The null hypotheses is “Number of sources is negatively correlated with bank decisions of making loans to SMEs” and alternative hypotheses is “Number of sources is positively correlated with bank decisions of making loans to SMEs”. If the SMEs taking loan from more than one sources (i.e. from more than one bank and is confirmed through credit information bureau) then how it is considered by banks. The value of significance from bank data is 0.000, thus showing a strong relationship between no. of sources and bank loaning decisions. The t-test value is 10.510 and the rejection region is greater than and equal to 2.228. Thus the t-value is in rejection region and the null hypothesis is rejected. The accepted hypotheses is “Number of sources is positively correlated with bank decisions of making loans to SMEs”.

4.1.7. Deposit Relationship

H₇: Deposit relationship is negatively correlated with bank decisions of making loans to SMEs.

The null hypothesis is “Deposit relationship is positively correlated with bank decisions of making loans to SMEs” and an alternative hypothesis is “Deposit relationship is negatively correlated with bank decisions of making loans to SMEs”. The value of significance from banks is 0.000, thus showing a strong relationship between two. The value of t-test from banks data is 8.964 and the rejection region is less than and equal to 2.228. Thus the null hypothesis is accepted. “Deposit relationship is positively correlated with bank decisions of making loans to SMEs”

4.1.8. Creditworthiness

H₈: Loan relationship has positive impact on bank decisions of making loans to SMEs.

The null hypotheses is “Loan relationship has dual impact (sometimes positive and sometimes negative) on bank decisions of making loans to SMEs” and there are two alternative hypotheses, first alternative hypotheses is “Loan relationship has negative impact on bank decisions of making loans to SMEs” and the second alternative hypotheses is “Loan relationship has positive impact on bank decisions of making loans to SMEs” if the loan relationship remained good between banks and SMEs then the loan relationship has positive impact but if any of the banks or SMEs experience a bad experience then it will have negative impact. So, it seems to have dual impact. From banks data the value of significance is 0.000 thus showing a strong relationship between loan relationship and bank loaning decisions. T-value from bank data is 8.964. The rejection region for banks is ≤ -2.228 and ≥ 2.228 . And the acceptance region is between -2.228 and $+2.228$. So the null hypothesis is rejected. Now we may check for first alternative hypotheses and the rejection region start from ≤ 2.228 . Hence the t-value lies in the acceptance region. So, the first alternative hypothesis is accepted. According to second alternative hypotheses the rejection region is ≥ 2.228 . The t-value is in the rejection region and

so, the second alternative hypothesis is rejected, and hence, the accepted hypothesis is “Loan relationship has positive impact on bank decisions of making loans to SMEs”.

4.2. Results for Data Collected Through SMEs

The hypotheses regarding loan approval decisions from data collected through SMEs and their analysis are.

Table-2: T-test applied on data collected through SMEs in Multan

Factors	t-stat	df	Sig.
Firm Size	7.044	21	.000
Firm Age	34.641	21	.000
Collateral Requirements	9.003	21	.000
Financial Documentation	16.231	21	.000
Firm Size	18.976	21	.000
Collateral Security	12.990	21	.000
Distance	14.042	21	.000
Deposit Relationship	13.420	21	.000
Loan Relationship	12.990	21	.000
Impact of Deposit Relationship	17.390	21	.000
Impact of Creditworthiness	13.420	21	.000

4.2.1. Firm Age

H₁: Firm age is negatively correlated with bank decisions of making loans to SMEs

Firm age is most important factor considered, as the firm increases in age they will have more financial access from banks. Question related firm age is asked in different queries in questionnaire of SMEs to determine about the firm age who obtain finance from sample bank to analyze about the bank preference for firm age while providing finance. T-test applied on data collected from SMEs to analyze and compare the results. The value of significance shows the relationship between dependent and independent variable. The value of significance comes out to be 0.000 from t-test applied on data collected from both SMEs, thus showing a strong relationship between firm age and bank loaning decisions. T-value comes out to be 34.641 from SMEs collected data. The rejection region, to reject null hypotheses is less than and equal to 2.080 for SMEs. So, the t-value for firm age is > 2.080 . Hence, the assertion “firm age is positively correlated with bank decisions of making loans to SMEs” is accepted.

4.2.2. Firm Size

H₂: Firm size is negatively correlated with bank decisions of making loans to SMEs

Firm size is considered on the basis of annual sales of firms and number of employees. The queries relating firm size is asked in questionnaire of SMEs to analyze and compare the results of SMEs collected data from banks collected data. So, it is observed higher the firm size, higher will be the chance of availability of loans to SMEs by banks. Because, banks are of the view that if firm size is high then the firms will have more potential to repay the loans. Banks are highly considered about firm size while providing loans to SMEs. The value of significance from SMEs is 0.000 thus showing a strong relationship between firm size and banks loaning decisions. T-value for firm size is 7.044 from data collected about firm size through SMEs. The rejection region, to reject null hypotheses is less than and equal to 2.080 for banks. So, the t-value for firm size is more than 2.080. Hence, the null hypotheses is accepted that “firm size is positively correlated with bank decisions of making loans to SMEs”

4.2.3. Financial Documentation

H₃: Financial documentation is negatively correlated with bank decisions of making loans to SMEs.

Financial documentation is an important factor. Major of the banks oblige SMEs while focusing on proper financial documentation. But it is also observed that most of the SMEs have no potential to maintain financial documentation. This is the major constraint for SMEs in accessing finance. That's why State bank has relaxed the loaning policies to major extent by allowing banks to project future cash flows of SMEs. State bank restrict that no SMEs may be decline from loan on this single issue. But, in spite of all facts financial documentation is considered an important factor by banks while providing loan.

The value of significance from SMEs collected data is 0.000 thus showing a strong relationship between financial documentation and banks loaning decisions. T-value for financial documentation is 16.231 from data collected through SMEs about financial documentation. The rejection region, to reject null hypotheses is less than and equal to 2.080 for banks. So, the t-value for financial documentation is more than 2.080. Hence, the null hypotheses is accepted that "financial documentation is positively correlated with bank decisions of making loans to SMEs"

4.2.4. Collateralized Loan

H₄: Collateralized loan is negatively correlated with bank decisions of making loans to SMEs.

Collateral security is the most important factor considered by banks while providing loans to SMEs. The SMEs who have more immoveable assets to be used as collateral may have more access on finance through banks.

The value of significance from SMEs is 0.000 thus showing a strong relationship between collateral and banks loaning decisions. T-value for collateral security and collateral requirement are 12.990 and 9.003 from data collected through SMEs. The rejection region, to reject null hypotheses is less than and equal to 2.080 for SMEs. So, the t-values for collateral security and collateral requirement are more than 2.080. Hence, the null hypotheses is accepted that "collateralized loan is positively correlated with bank decisions of making loans to SMEs"

4.2.5. Distance

H₅: Distance is not considered by banks while providing loan to SMEs.

Distance is considered by most of the banks while providing loans to SMEs. The banks that do not prefer distance while providing loans to SMEs provide loan on the basis of references at most. The value of significance from SMEs is 0.000, thus showing a strong relationship between distance and banks loaning decisions. T-value for distance is 14.042 from data collected through SMEs about distance. The rejection region, to reject null hypotheses is less than and equal to 2.080 from SMEs. The t-value for distance is more than 2.080. So the null hypotheses is accepted that "Distance is considered by banks while providing loan to SMEs"

4.2.6. Number of Sources

H₆: Number of sources is positively correlated with bank decisions of making loans to SMEs.

If SMEs are taking loan from more than one source then it is to be analyzed that either the bank will provide loan to such SME or not. The data is analyzed on the basis of questionnaire of SMEs that every SME has taken loan from more than one bank. So, banks are obliging SMEs even if they have taken loan from more than one source. So, this shows a positive relation between two. Thus, the accepted hypotheses is "Number of sources is positively correlated with bank decisions of making loans to SMEs".

4.2.7. Deposit Relationship

H₇: Deposit relationship is negatively correlated with bank decisions of making loans to SMEs.

If the SME has prior deposit relationship with the bank from which the loan is required then it may have a positive impact on bank loaning decisions as the banks may have easy access on financial information of SMEs through deposit relationship. The value of significance about deposit relationship

and impact of deposit relationship from SMEs collected data is 0.000, thus showing a strong relationship between two. The value of t-test about deposit relationship and impact of deposit relationship from SMEs collected data are 13.420 and 17.390. The rejection region is less than and equal to 2.080. Thus the null hypothesis is accepted. "Deposit relationship is positively correlated with bank decisions of making loans to SMEs"

4.2.8. Creditworthiness

H₈: Loan relationship has positive impact on bank decisions of making loans to SMEs.

If the prior loan relationship remained good between banks and SMEs then the loan relationship has positive impact otherwise it may have negative impact. So, it seems to have dual impact. From SMEs data the value of significance about loan relationship and impact of loan relationship is 0.000 thus showing a strong relationship between loan relationship and bank loaning decisions. T-value from SMEs data about loan relationship and impact of loan relationship are 12.990 and 13.420. The rejection region for SMEs is ≤ -2.080 and ≥ 2.080 . And the acceptance region is between -2.080 and $+2.080$. So the null hypothesis is rejected. Now we may check for first alternative hypotheses and the rejection region start from ≤ 2.080 . Hence the t-value lies in the acceptance region. So, the first alternative hypothesis is accepted. According to second alternative hypotheses the rejection region is ≥ 2.080 . The t-value is in the rejection region and so, the second alternative hypotheses is rejected, hence, "Loan relationship has positive impact on bank decisions of making loans to SMEs".

5. Conclusion

In this study the banks loaning criteria is explored. Surveys with banks and SMEs are conducted to know about the loaning policies of banks and gradual improvement in banks loaning decision to fulfill SMEs financial needs. Banks are promoting SMEs and it is profitable for banks to provide loans to SMEs. Banks focus on firm size, firm age, owner age, firm profitability, proper financial documentation, distance, number of sources, loan and deposit relationship along with the length of relationship while loaning to SMEs. From the survey of banks and SMEs I found that out of all variables, the most important is the collateral requirements, firm size and firm age for banks while loaning to SMEs. These are the variables which are considered at most by banks while providing loan to SMEs.

Collateralized loaning is the most important of all factors. Banks require immovable assets as the most standard form of collateral security. Banks do not take moveable assets as collateral for loan due to the reason that the value of moveable assets reduces as the time passes by. So it is discouraged by banks to use moveable property as collateral. The restrictions imposed on type of assets being set as collateral usually create complications for SMEs to have an access to bank finance. After that, SBP, to relax the system of loaning to SMEs in order to encourage SMEs growth relax the collateral policies by allowing the banks to provide loan to SMEs with the limit of 3 million without collateral. But this is not highly encouraged by banks as banks are risk averse. For banks collateral is the most important factor that is considered at most for the provision of loans to SMEs.

Firm size and firm age are also very important factors considered by banks in order to provide loans to SMEs. Banks do not provide loan to those enterprises that have not taken business initiative and require loan for starting the business. Firm age is very important for banks while providing loan. The enterprises who have not taken initiative and their owners are requiring the finance to take a start for the business. If the loan is required on the basis of business plan and feasibility reports then loan is not provided to such SMEs. Similarly the firm size is also very important. Firm size is considered on the basis of annual sales and number of employees. Loan is provided to those SMEs on easy basis who are in growing stage or in established stage. Newly started businesses are not encouraged by banks most of the time.

Deposit relationship also has some positive effects on banks loaning decisions of making loans to SMEs. Due to deposit relationship, the SMEs financial documents get available to banks. And it gets easy for both banks and SMEs for financial access. As, banks while being aware of firm financial condition provide loan through easy policies and SMEs get easy financial access while loaning from banks. Loan relationship may also have positive impact but in some situations SMEs who have had prior loan relationship with banks could not maintain good relationship for long and may have negative impact on banks loaning decisions. But it is observed through t-values of data collected through both banks and SMEs that loan relationship has positive impact on bank loaning decisions. But if these three variables i.e. deposit relationship, loan relationship and financial documentation are not available even then the loan will be provided to SMEs. These three variables, if exist, has positive impact on bank loaning decisions but if not available, even then the loan will be provided to SMEs. As financial cash flows of SMEs can be projected by banks on percentage fixed according to bank's loaning policies. Same is the situation with number of sources. Number of sources is considered important for banks while providing loan to SMEs. As according to banks, the financial gap of SMEs is overcome if the loan is taken from number of sources. The financial needs of SMEs will be filled through more than one bank and banks get benefit in a way that less finance is invested from each bank. So, financial needs of SMEs is obliged if loan is required through multiple banks. And the risk for banks can be overcome. Number of sources is consider by bank in a good way but it doesn't mean that if the SME is not taking loan from number of sources then loan will not be provided by banks. Loan will be provided but the financial needs of SMEs wouldn't be filled. So, financial gap may exist between demanded loaning amounts by SMEs and supplied loaning amount by banks. Same is the situation of distance; distance has not much effect on loaning to SMEs by banks. Most of the banks in Multan considered distance an important factor while providing loan. But there are also some banks that provide loans to those enterprises that are at more distance, but in a situation like that, loan is provided on the basis of references.

This study deals with the loaning decisions of banks while making loans to SMEs. For further investigation the comparative study of loaning decisions of large and small banks to SMEs are to be considered. At most of the times the large banks loaning decision is different from small banks loaning decisions. Small banks are more likely to oblige SMEs than large banks.

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Appendix

Table-1: Distribution of SME Finance among Banks

Banks	% Share in SME Finance Portfolio
Big-five banks	43.40
Habib Bank Limited	15.55
National Bank of Pakistan	7.86
Allied Bank Limited	7.46
Muslim Commercial Bank Limited	6.72
United Bank Limited	5.81
Private banks (excluding big 5)	44.36
Public sector banks (excluding NBP)	4.82
Foreign banks	0.42
Islamic banks (excluding Al-Baraka Bank)	4.82
Specialized banks	2.19

Table-2: List of Banks and SMEs Surveyed

Names of Banks	Names of SMEs
ABL	Humpty Dumpty
Al- Islami Bank	City CNG and Services
Askari Bank	Amir fine export private ltd
Bank Al-Habib	Zakia fashion point
HBL	Fazal farms private ltd.
KASB	Ahmed Fine textile Mill
Khushhali Bank	Fazal Rehman fabrics Mill
MCB	SR Bakers
Silk Bank	Khan property dealers
Soneri Bank	Zakariya Store
Standard Chartered Bank	Nirala sweets
	Sami Bakers
	Multan Fabrics
	Mughees textiles
	The Builders
	Mid west
	Golden cotton
	Mehmood group of business
	Hashmi Drug Agency
	Rafi cotton
	Al-saeed enterprises
	Rafique shoe factory

Questionnaire from Banks on “Lending Criteria to SMEs by Banks in Multan”

Name of the bank _____

Branch Code _____

E-mail _____

* Small businesses: business who had taken initiative, those enterprises who have small businesses and asked for small loans.

* Medium businesses: the medium business is a progressing business in which the owner is experienced and asked for more loan required and there is succession in business.

1.1 What is the fixed percentage on which your bank project future cash flows of small enterprises?

- 1%-3%
- 4%-6%
- 7%-12%

- d) 13%-18%
 - e) 19%-25%
 - f) 26% or above
- 1.2 What is the fixed percentage on which your bank project future cash flows of medium enterprises?
- a) 1%-5%
 - b) 6%-10%
 - c) 11%-15%
 - d) 16%-20%
 - e) 21%-30%
 - f) 31% or above
- 2.1 What firm age to be considered while loaning to SMEs
- a) newly existed business
 - b) business with an age of 6 month
 - c) business with an age of 3 years
 - d) business with an age of 5 years or above
- 2.2. Is firm size preferred while loaning to SMEs?
- 2.3. What firm size is to be considered while loaning to SMEs
- a) firm recently taken initiative and in phase of small business
 - b) a growing firm
 - c) firm expanded to have branches
 - d) other
3. What is distance limit by your bank while loaning to SMEs?
- a) 1km-49km
 - b) 50km-99km
 - c) 100km-199km
 - d) 200km-499km
 - e) 500km or above
- 4.1 over the past year, how has your bank's credit standards as applied to the approval of loans to small enterprises changed
- a) Tightened considerably
 - b) Tightened somewhat
 - c) Remained basically unchanged
 - d) Eased somewhat
 - e) Eased considerably
- 4.2 over the past year how have your bank's credit standards as applied to the approval of loans to medium enterprises changed
- a) Tightened considerably
 - b) Tightened somewhat
 - c) Remained basically unchanged
 - d) Eased somewhat
 - e) Eased considerably
- 5.1 over the past year have the perception of risk affected your bank credit standard as applied to the approval of loans to small enterprises
- a) Credit standard tightened considerably
 - b) Credit standard tightened somewhat
 - c) Credit standard remained basically unchanged
 - d) Credit standard eased somewhat
 - e) Credit standard eased considerably
- 5.2 over the past year have the perception of risk affected your bank credit standard as applied to the approval of loans to medium enterprises

- a) Credit standard tightened considerably
 - b) Credit standard tightened somewhat
 - c) Credit standard remained basically unchanged
 - d) Credit standard eased somewhat
 - e) Credit standard eased considerably
6. Over the past year has the pressure of competition from bank and non-banks affected your bank credit standard as applied to the approval of loans to SMEs
- a) Credit standard tightened considerably
 - b) Credit standard tightened somewhat
 - c) Credit standard remained basically unchanged
 - d) Credit standard eased somewhat
 - e) Credit standard eased considerably
7. How have your bank margin on average loans to SME's changed
- a) Wider considerably
 - b) Wider somewhat
 - c) Remained basically unchanged
 - d) Narrowed somewhat
 - e) Narrowed considerably
- 8.1 What is the mark up charged for small enterprises
- a) 1%-4%
 - b) 5%-7%
 - c) 8%-11%
 - d) 12%-15%
 - e) 16% or above

Note: if (e) is selected then percentage should be mentioned.

- 8.2 What is the mark up charged for medium enterprises
- a) 1%-4%
 - b) 5%-7%
 - c) 8%-11%
 - d) 12%-15%
 - e) 16% or above

Note: if (e) is selected then percentage should be mentioned.

- 8.3 What is the bank margin on average loans to SME'S?
- a) 1%-4%
 - b) 5%-7%
 - c) 8%-11%
 - d) 12%-15%
 - e) 16% or above

Note: if (e) is selected then percentage should be mentioned.

- 9.1 How have your bank margin on riskier loans to small enterprises changed
- a) Wider considerably
 - b) Wider somewhat
 - c) Remained basically unchanged
 - d) Narrowed somewhat
 - e) Narrowed considerably
- 9.2 How have your bank margin on riskier loans to medium enterprises changed
- a) Wider considerably
 - b) Wider somewhat
 - c) Remained basically unchanged
 - d) Narrowed somewhat

e) Narrowed considerably

10.1 What is the bank margin on riskier loans to small enterprises?

- a) 1%-5%
- b) 6%-10%
- c) 11%-15%
- d) 16%-24%
- e) 25% or above

10.2 What is the bank margin on riskier loans to medium enterprises?

- a) 1%-5%
- b) 6%-10%
- c) 11%-15%
- d) 16%-24%
- e) 25% or above

11.1 Loaning to small enterprises is considered to be

- a) Risky
- b) Most risky
- c) Less risky
- d) Risk not considered

11.2 Loaning to medium enterprises is considered to be

- a) Risky
- b) Most risky
- c) Less risky
- d) Risk not considered

12.1 How are different risk factors considered by bank while loaning to small enterprises

Note: **MI** (most important), **I** (important), **Can't say**, **UI** (un important) **MUI** (most unimportant)

Risk factor	MI	I	Can't say	UI	MUI
a) unavailability of collateral security					
b) less documentation					
c) less valuable assets					
d) no references					
e) amount of loan					
f) any other					

12.2 How are different risk factors considered by bank while loaning to medium enterprises

Note: **MI** (most important), **I** (important), **Can't say**, **UI** (un important) **MUI** (most unimportant)

Risk factor	MI	I	Can't say	UI	MUI
a) unavailability of collateral security					
b) less documentation					
c) less valuable assets					
d) no references					
e) amount of loan					
f) any other					

13. What are loaning criteria to small enterprises?

14. What are loaning criteria to medium enterprises?

15.1 What are the collateral requirements on loan to small enterprises by your bank?

- a) Less than 110%
- b) 111%-120%
- c) 121%-130%
- d) 131% -140%
- e) 141%-160%

- f) 161% or above
- 15.2 What are the collateral requirements on loan to medium enterprises by your bank?
- Less than 110%
 - 111%-120%
 - 121%-130%
 - 131% -140%
 - 141%-160%
 - 161% or above
- 15.3 What are the collateral requirements on loan to SMEs by your bank?
- Less than 110%
 - 111%-120%
 - 121%-130%
 - 131% -140%
 - 141%-160%
 - 161% or above
16. What sort of data do you collate on SME on regular basis? Can you provide us with a selection of sample reports?
17. How risky is loaning to SME?
18. Do you provide loan to SMEs sub-sector if the loaning amount is minute but the sector is riskier?
- No providence as the sector is riskier
 - Provide loan as the loan amount is minute
 - No providence of loan either the loan amount is minute
 - Sometimes provide
 - Provide loan as the economy is flourishing
19. Do you provide loan to SMEs sub-sector if the loaning amount is high and the sector is riskier?
- No providence as the sector is riskier
 - No providence as the sector is riskier and the loaning amount is high
 - Provide loan
 - Sometimes provide
 - Provide loan as the economy is flourishing
20. Over the last year what is the most risky situation while loaning to SME?
21. What special lending criteria apply to higher risk sector?
22. What is the bank's policy on unsecured loans to SME?
23. Are all advances secured? What sort of security is taken?
24. What is the preferred age of borrowers?
- 15yrs-17yrs
 - 18yrs-25yrs
 - 26yrs-50yrs
 - 51yrs-69yrs
 - 70yrs or above
25. Does the bank make any distinction in its lending policies to exposures in?
- Rural v/s urban sectors
 - Size of entity
 - Ethnicity of borrower
26. Out of the following which SME sub-sectors are considered by the bank to be higher risk?
- Cotton weaving and textile
 - Metal products
 - Grain milling
 - Art silk
 - Jewelry

- f) Wood and furniture
- g) Other

Note: if 'other' then mentions the sector

27. What is the Percentage of applications received from non-start-up SMEs?
- a) 1%-15%
 - b) 16%-30%
 - c) 31%-50%
 - d) 51%-70%
 - e) 71% or above
28. What is the Percentage of applications accepted from non-start-up SMEs?
- a) 1%-15%
 - b) 16%-30%
 - c) 31%-50%
 - d) 51%-70%
 - e) 71% or above
29. What is the Percentage of applications received from start-up SMEs?
- a) 1%-15%
 - b) 16%-30%
 - c) 31%-50%
 - d) 51%-70%
 - e) 71% or above
30. What is the Percentage of applications accepted from start-up SMEs?
- a) 1%-15%
 - b) 16%-30%
 - c) 31%-50%
 - d) 51%-70%
 - e) 71% or above
31. How do banks deal with SME's that are start-ups, and few fixed assets to use as security?
32. What is the percentage of SMEs that your bank financed defaulted on their financing?
- a) 1%-15%
 - b) 16%-30%
 - c) 31%-50%
 - d) 51%-70%
 - e) 71% or above
- 33.1 What is the percentage of bad debts resulting from small enterprises?
- a) 1%-15%
 - b) 16%-30%
 - c) 31%-50%
 - d) 51%-70%
 - e) 71% or above
- 33.2 What is the percentage of bad debts resulting from medium enterprises?
- a) 1%-15%
 - b) 16%-30%
 - c) 31%-50%
 - d) 51%-70%
 - e) 71% or above
- 33.3 What is the percentage of bad debts resulting from SMEs?
- a) 1%-15%
 - b) 16%-30%
 - c) 31%-50%

- d) 51%-70%
- e) 71% or above

34. What is the average length of relationship with SMEs?

35. Which sub sector within the SME sector are particularly attractive?

- a) Cotton weaving and textile
- b) Metal products
- c) Grain milling
- d) Art silk
- e) Jewelry
- f) Wood and furniture
- g) Other

Note: if 'other' then mention the sector and please specify the reasons.

36. Which sub sector is most difficult for credit approvals?

- a) Cotton weaving and textile
- b) Metal products
- c) Grain milling
- d) Art silk
- e) Jewelry
- f) Wood and furniture
- g) Other

Note: if 'other' then mention the sector and please specify the reasons.

37. What information does the bank request?

38. Are there any initiatives your bank has put in place to improve the efficiency of lending to SMEs?

39.1 What are the barriers in financing to small enterprises?

- a) Less documentation
- b) Non-availability of financial information
- c) Less access to collateral
- d) No references
- e) Less valuable assets
- f) Other

Note: if 'other' then mentions the sector

39.2 What are the barriers in financing to medium enterprises?

- a) Less documentation
- b) Non-availability of financial information
- c) Less access to collateral
- d) No references
- e) Less valuable assets
- f) Other

Note: if 'other' then mentions the sector

40.1 What percentage of your loan portfolio is with small enterprises?

- a) 1%-15%
- b) 16%-30%
- c) 31%-50%
- d) 51%-70%
- e) 71% or above

40.2 What percentage of your loan portfolio is with medium enterprises?

- a) 1%-15%
- b) 16%-30%
- c) 31%-50%
- d) 51%-70%

- e) 71% or above
- 41.1 What is the average amount of finance per medium enterprise?
- Below 10m
 - Above 10m and below 50m
 - Above 50m
 - Below 75m
- 41.2 What is the average amount of finance per small enterprise?
- Below 1 lac
 - Above 1 lac and below 10 lac
 - Above 10 lac and below 20 lac
 - Above 20 lac
 - Below 75m
42. What percentage of SMEs lending is backed by collateral?
- 1%-15%
 - 16%-30%
 - 31%-50%
 - 51%-70%
 - 71% or above
43. If SMEs have financial records and documents are properly maintained then what would be the loaning criteria to SMEs by banks?
44. If SME is taking loan from more than one bank or financial institution then
- loan will be provided to SME
 - loan will not be provided to SME
 - SME will become too risky to provide loan
 - SME will be risky but loan would be provided
 - It would be more convenient for bank to provide loan to SME
45. What are the loaning criteria to small amend medium enterprises by banks?
- Loan is provided to small and medium enterprises by easy way
 - Loan is provided only if all the requirements of banks are filled by small and medium enterprises
- 46.1 What is the maximum loan amount provided by banks to small enterprises?
- >10lac
 - > 10 million
 - > or = 75 million
- 46.2 What is the maximum loan amount provided by banks to medium enterprises?
- > 10lac
 - >10 million
 - >or = 75 million
47. What would be the loaning criteria to SME who have had deposit relationship with bank?
48. What would be the loaning criteria to SME who have had loan relationship with bank?

Questionnaire from SMEs on “Lending Criteria to SMEs by Banks in Multan”

1. COMPANY PROFILE

- 1.1 Company name _____
 Address _____
 Telephone# _____
 E-mail _____
- 1.2 Person contacted _____ Person interviewed _____
- 1.3 Legal status _____

1.4 Number of employees

- a) <10
- b) 10-99
- c) 100-199
- d) 200-250
- e) 251-499
- f) >500

1.5 Type of activity

- a) Manufacturing
- b) Service
- c) Commerce & trade
- d) Others

1.6 Main products & Activities _____

1.7 Asset value _____

1.8 Annual turnover _____

2. What is the age of your firm?

- a) Newly existed business
- b) Business with an age of 6 months
- c) Business with an age of 3 years
- d) Business with an age of 5 years or above

3. What is the age of owner?

- a) 15 yrs-17 yrs
- b) 18 yrs-25 yrs
- c) 26 yrs-50 yrs
- d) 51 yrs - 69 yrs
- e) 70 yrs or above

4. Have you ever raised finance from?

- | | | |
|----------|-----------|-----------|
| a) Banks | b) Family | c) Others |
| Yes | Yes | Yes |
| No | No | No |

(if yes, please specify) _____

5. What were your problems while loaning from banks?

- a) Insufficient collateral
- b) Poor documentation
- c) Project proposal not accepted
- d) Previous credit record
- e) No personal contact in lending institutions
- f) Own contribution too small
- g) Other _____

6. Please list some SME policies of which you are aware?

7. In your opinion, which of the following banks support SMEs in Multan?

- a) HBL
- b) MCB
- c) Allied bank
- d) Bank Al Habib
- e) Askari bank
- f) Soneri bank
- g) Khushhali bank
- h) Silk bank
- i) Standard chartered bank

- j) KASB
 - k) RBS Bank Ltd
 - l) Other _____
8. In your opinion, what are the barriers to the credit approval of the SMEs in Multan
- a) Difficulty in accessing to credit
 - b) Low coordination between banks supporting SMEs
 - c) Too high cost of money
 - d) No documentation by SMEs
 - e) Less availability of valuable assets to be used as collateral by SMEs
 - f) Negative image of the entrepreneurs
 - g) Procedural difficulties in accessing to credit from banks
 - h) No personal contact and references
 - i) High loaning amount
 - j) Other (what exactly?) _____
9. In your opinion, what measures should be taken by banks to support the creation and development of SMEs in Multan?
- a) Simplify the system of borrowing
 - b) Facilitate access to financing
 - c) Banks should develop more policies for SMEs development
 - d) Decrease the amount of mark up(or interest)
 - e) Determine policies for SMEs more concretely and exactly
 - f) Give priority to women-entrepreneurs and create program of support of business-women
 - g) Other _____
- 10.1 Have you ever asked for credit support from any of the following banks?
- a) HBL
 - b) MCB
 - c) Allied bank
 - d) Bank Al Habib
 - e) Askari bank
 - f) Soneri bank
 - g) Khushhali bank
 - h) Silk bank
 - i) Standard chartered bank
 - j) KASB
 - k) RBS Bank Ltd
 - l) Other _____
- 10.2 if yes, at what stage you asked for SMEs support?
- a) Before creating a company
 - b) During the process of company set up
 - c) When company started to grow
 - d) When company started to have problems
11. What was the mark up charged by banks?
- a) 1-4%
 - b) 5-7%
 - c) 8-11%
 - d) 12-15%
 - e) 16% or above
12. Would you say that the amount of debt compared to the assets of your company has?
- a) Increased
 - b) Remained unchanged

- c) Decreased
- d) Not applicable, no debt

13. We will now consider the terms and conditions of the bank financing available to your firm, For each of the following items, could you please indicate whether they were increased, remained unchanged or were decreased the past one year?

- Was increased by the bank.....1
- Remained unchanged.....2
- Was decreased by the bank.....3

Terms and conditions:

- a) Level of interest rates
 - b) Level of the cost of financing other than interest rates (CHARGES, FEES, and COMMISSIONS)
 - c) Available size of loan or credit line
 - d) Available maturity of the loan
 - e) Collateral requirements
 - f) Other, e.g. loan covenants, required guarantees, information requirements, procedures, time required for loan approval.
14. What is the size of the last loan, of any kind, that your firm has obtained in the last one year?
- a) We did not take a loan
 - b) Smaller than 25 000 rupees
 - c) 25 000-100 000 rupees
 - d) 100 000 – 1 000 000 rupees
 - e) Rs.1 million – Rs10 million
 - f) Over Rs.10 million
 - g) Smaller than Rs.75 million
15. What was the mark up charged on last loan?
- a) 1-4%
 - b) 5-7%
 - c) 8-11%
 - d) 12-15%
 - e) 16% or above
16. Who provided you this last loan?
- a) Bank
 - b) Private individual – family or friend
 - c) Other sources (e.g. microfinance institutions, government-related sources)
17. What did you use this last loan for?
- a) Working capital
 - b) Land/ buildings or Equipment/vehicles
 - c) Research and development or intellectual property
 - d) Promotion
 - e) Staff training
 - f) Buying another business
 - g) Other
18. If you need external financing to realize your growth ambitions, what type of external financing would you prefer most?
- a) Bank loan
 - b) Loan from other sources (e.g. trade credit, related company, shareholder, public sources)
 - c) Equity investment
 - d) Other
19. And what amount of financing would you aim to obtain?

- a) Less than 25 000 rupees
 - b) 25 000 – 100 000 rupees
 - c) 100 000 – 1 000 000 rupees
 - d) Rs.1 million – Rs10 million
 - e) Over Rs.10 million
 - f) Smaller than Rs.75 million
20. What do you see as the most important limiting factor to get this financing?
- a) There are no obstacles
 - b) Insufficient collateral or guarantee
 - c) Interest rates or price too high
 - d) Financing not available at all
 - e) Other
21. What information does the bank request while providing loan to SMEs?
22. At what distance the bank is from where you borrowed
- a) 1km- 49km
 - b) 50km- 99km
 - c) 100km- 199km
 - d) 200km- 499km
 - e) 500 km or above
23. Do you have had any deposit relationship with the bank from where you borrowed?
Yes No
24. If yes, then in your concern the deposit relationship have any positive impact on loan approval from banks?
25. Do you have had any loan relationship with the bank from where you borrowed?
Yes No
26. If yes, then in your concern the loan relationship have any positive impact on loan approval from banks?