

## Performance Evaluation of SMEs Loan of BRAC Bank Ltd: An Analysis

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### Abstract

*This paper attempts to draw the role of SME loan in Bangladesh. Particularly the small and medium enterprises (SMEs) deserve special attention. Generally Small and medium enterprises play a very important role in economic growth and industrial development of a country. For Bangladesh, SME have assumed special significance for poverty diminution programs and potential contribution to the overall industrial and economic growth. The present study is confined to an attachment of SME loan. This paper looks at the performance of small and medium enterprises that have received loans from BRAC Bank Limited with a center of attention on employment generation. The study is based on both primary and secondary data. This research will be of potential value in accelerating the development of SME loan in Bangladesh.*

**Keywords:** SME, BRAC Bank, SE, SME loan, BBL.

### Introduction

The SME play very important roles in the national economy of Bangladesh by making up over 90 percent of industrial enterprises, providing employment to industrial workers and contributing to the one-third of industrial value-added to GDP (Hossain,1998). However, policies and initiatives to develop SME and to increase their competitiveness are a priority for these countries (Ahmed, 2001). The definition of SME is not unique; it varies across countries and in some countries the definition differs further between sectors such as number of people employed and size of capital, sales, and assets and so on.

According to the Bangladesh Industrial Policy 2010, small and medium enterprises (SME) can be defined in the following ways: Small enterprise (SE) may be manufacturing or service oriented. In manufacturing, small enterprise would be those with assets worth Tk. 5 to 100 million and/or 25 to 99 workers, whereas in service industry and in business, small enterprises will be those which employ 10 to 25 and have assets worth Tk. 500,000 to 10 million. Medium enterprise may be also manufacturing or service oriented. In manufacturing, medium enterprise would be those with assets worth Tk. 100 to 300 million (minus land and factory building, and including replacement value) and/or 100 to 250 workers, whereas in service industry and in business, medium enterprises will be those which employ 50 to 100 workers and have assets worth Tk. 10 to 150 million. SME loan is the financial support to small and medium sized enterprises and represents major function of the general business finance market. SME loan is the major source of capital for SME. This study is conducted on BRAC Bank Limited, Rajshahi Branch, Bangladesh. In Bangladesh, many Commercial Banks and NGOs along with some Government

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Banks are providing SME loan to the SME. Therefore, SME loan is the capital disbursement to SME at a certain interest rate. Capital is supplied through the business finance market in the form of bank loans and overdrafts; leasing and hire-purchase arrangements.

BRAC Bank Limited launched credit for the SME in 2002 in recognition of their exceptional requirement (Rabbani and Sulaiman, 2012). SME Loan is of dominant importance as the greatest share of the total revenue of the bank is generated from it. The success of a bank, therefore, depends on how efficiently and judiciously it makes use of its available resources. In formulating SME loan judgment and making quality in SME Loan, the lending officer must be equipped with all information needed to evaluate a borrower's character, management competence, capacity, ability to provide collaterals and external conditions which may affect his ability in meeting financial obligations. This study has found that SME have a momentous role in employment generation, poverty decrease and overall economic improvement, particularly for a developing economy like Bangladesh.

## **Importance of the Study**

Small & Medium Enterprise (SME) plays a pivotal role in the economic growth and development of Bangladesh. Actually, SME works as [the platform](#) for job creation, [income](#) generation, and development of forward and backward industrial linkages and fulfillment of local social needs. SMEs occupy a unique position in the economy of Bangladesh. Mainly private sector development depends on them. In view of present economic development effort in Bangladesh the SME sector plays an important role. SME contributions to value addition in manufacturing is in the range of 20 to 25 percent of GDP and there are approximately six million SMEs, which include enterprises with up to 100 workers employing a total of 31 million people – equivalent to 40 per cent of the population of our country aged 15 years and above. To put it simply, SMEs are the heart of the industrial sector of the country, employs the bulk of the working population and are owned by Bangladeshi entrepreneurs. They provide a huge range of goods and services to the Bangladeshi population, especially in the rural areas, alongside providing vital support in the production chain to large industries. This present study may focus on role of SME loan performance, procedure for the banking sectors especially in BRAC Bank limited. However, the study is likely to provide interesting practices to academic scholar, policy maker, executives and potential entrepreneurs with the theories and principles of Small and Medium Enterprises (SME) areas.

## **Justification of the Study**

Most of the developing countries suffer from extreme economic imbalance, resulting in political and economic instability. Bangladesh is one of the poorest and most densely populated countries in the world. Apart from its low economic status, major impediments to growth have included frequent floods and other environmental degradations like water, land, and air pollution. Besides, the inefficiency of its state-owned enterprises and the slow implementation of required economic reforms are also hampering the development of Bangladesh. Traditional industries, however, will

not provide sufficient opportunity for the majority of job seekers. Enabling of small and medium enterprises is embraced as a key strategy of wealth creation and employment especially in Bangladesh. Many organizations (both government and nongovernment) are working with micro finance program in Bangladesh. In this regard the present study is helpful to unfold the hidden momentum especially for SME loan in one of the important commercial banks in Bangladesh and it will also facilitate the future researchers in SME sectors.

## Literature Review

A good number of studies have been done on SMEs sector in Bangladesh; some of the notable ones are; Uddin (2008), Chowdhury (2007), Ahmed (2006), Bhattacharya and Chowdhury (2003) MIDAS (2004), Mahmud (2006), Hossain (1998), Rosen (2003), Chowdhury (2007), Hallberg (2002), MIDAS(2004) and so on. 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 (2006) opined that SME development, as 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. Nevertheless, the small scale industries (SSIs) including the cottage industries are of special consideration as these. Chowdhury (2007) highlighted that 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 Daily Star in its editorial (2006) mentioned that many SME owners are to face difficulties when they require bank loans. In fact, SME financing has recently been identified by experts as one of the major problems faced by SMEs in Bangladesh. Mahmud (2006) said that the SMEs have very limited bank finance, which is only around 10 percent, while self-finance remains the major source of their finance contributing 76.5 percent of fixed capital and 51.8 percent of working capital. Bhattacharya and Chowdhury (2003) mentioned that Bangladesh Bank encourages banks to give loans to projects for diversified industrial development. From the point of view of limiting the credit risk exposures of the banks having a higher level of classified loan, the new rule is justified. However, to consider large loans as risky loans (by the new rule) is not reasonable. Moreover, for increasing the volume of lending to the SME sector, this sort of supply-side policy is not adequate. In fact, under both directed lending (before 1990) and deregulated lending (after 1990) regimes, the demand-side factors were not considered; consequently, resource allocation suffered. Ranjit & Rashid, (1996).In Bangladesh, small and medium enterprises have been facing multifarious problems related to raw materials, power, land, marketing, transport, technical facilities and finance. Bari, & Ali & Haque (2005) examined the key constraints faced by the SMEs sector in Pakistan, including lack of access to credit, excessive government regulation, an arbitrary and exploitative tax administration system, a weak technological base and the lack of business support

services. It also provides a set of concrete strategic recommendations to address such constraints in order to promote SMEs growth for greater income generation and employment creation. Rani and Rao (2008) have found in their study that SMEs need special treatment through devising special instruments of credit for strengthening their competitiveness. Pasanen (2007) has mentioned that there is a strategic difference between organic and non-organic group regarding SMEs<sup>2</sup> growth strategies in the light of their scale of operation, firm age, founders, and product and customer structures. Pullen, et al (2009) have found in their study that companies which give emphasis on incremental innovation that achieve high overall innovation performance indeed share a pattern in their internal organization, while controlling for innovation type . Hossain (1998) has also identified some constraints in developing SMEs in Bangladesh. Why commercial banks are so reluctant to extend loans to this sector? That is because of the high risk and supervision cost associated with this type of financing. Hossain (1998), furthermore, the loan application forms for investment financing from banks are long, tedious, and redundant. Bhattacharya, *et.al.* (2000) and Sia (2003) identified that banks are shy to lend to SME activities, as they do not consider them as attractive and profitable undertakings. SMEs are also regarded as high risk borrowers because of their low capitalization, insufficient assets, and high mortality rates (Sia,2003) and consequently, they are not offered any attractive deals in terms of loans and interest rate. Banks charge high rate of interest from SME loan because of high cost of supervision. For example, in secured credit transactions, interest rates vary from 14% (subsidized in cases defined by Bangladesh Bank policies) to 22% or more. Bhattacharya and Chowdhury (2003) mentioned that Bangladesh Bank encourages banks to give loans to projects for diversified industrial development. From the point of view of limiting the credit risk exposures of the banks having a higher level of classified loan, the new rule is justified. Shahadan et al (1990) also identified the inability of SMEs to raise capital and limited access to institutional credit as the two typical problems of SMEs.

Hassan (1992) pointed that SMEs are not able to gain access and utilize available funding due to interrelated factors such as inadequate collateral and lack of performance record to convince the financial institutions into providing them with the loans. Other studies in developed countries like United States of America and United Kingdom also suggested that SMEs operating in these countries faced financial problems. Broom & Longenecker (1975) indicated that one problem of major significance to many small businesses is lack of capital and credit. Most bankers associate loans to SMEs with low returns and high risk. Thus, SMEs businesses are not only having problems in obtaining bank finance, but they also claim that the costs are too high. Ranjit & Rashid, (1996). Point out that in Bangladesh, Small and medium enterprises have been facing multifarious problems related to raw materials, power, land, marketing, transport, technical facilities, and finance. From the above discussion, it can be seen that while the availability of finance is unquestionably important, their accessibility is even more crucial.

## **Objectives of the Study**

The main objective of the study is to analyze the importance of SME loan of BRAC Bank limited and the specific objectives are as follows:

- a. To identify the SME loan procedure and performance of BRAC Bank ltd.
- b. To highlight the SME loan utilization pattern and examine the impact of SME loan of BRAC Bank ltd.
- c. To give some recommendations in the light of respondents opinion.

## **Methodology of the Study**

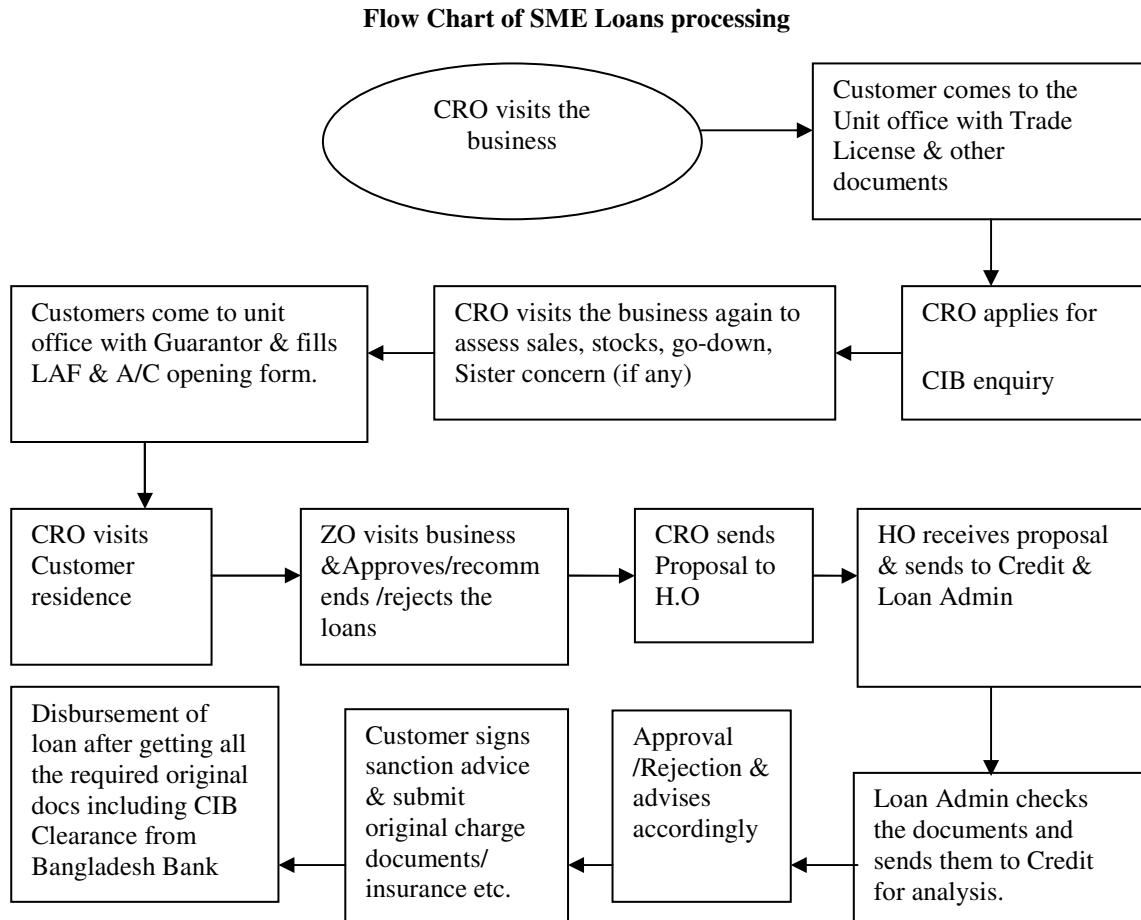
This study is based on both primary and secondary data. Primary data were collected through personal interview with a structured questionnaire and direct observations. Forty employees and twenty borrowers of BRAC Bank Limited, Rajshahi Branch were used as the respondents and the sample units were drawn through convenience non-probability sampling method. Questionnaire was pre-tested and further improvement was done before conducting the survey. Respondents were assured of anonymity by asking them not to reveal their identity anywhere in the survey instrument. They were also told that neither their immediate supervisors nor their headquarters officials will have access to the individual questionnaire. Secondary data were collected from the published official statistics, reports documents, laws, ordinance, books, articles, periodicals of different domestic and international agencies, annual reports of concerned bank, different reports and statistics of Bangladesh Bank, Ministry of Finance, websites etc. The study was conducted between June 2013 to May 2013 with 60 SMEs borrowers and employees of BRAC Bank Ltd. of Rajshahi city corporation area. For proper editing, the field interview scheduler were sorted, scrutinized and checked to avoid laps and gaps. Then the data were transferred to Microsoft word and excel sheet in order to facilitate analysis.

## **Research Framework**

SME is the most emerging sector to expand and BRAC Bank has every potentiality to explore the SME business throughout the country. It plays gigantic role in developing SME sectors in all areas in Bangladesh. This study mainly conducted the role of SME loan in BRAC Bank Limited. BRAC Bank Ltd (BBL) is one of the fastest growing banks in Bangladesh. Established in 1999, BRAC bank achieved spectacular growth in loans, assets and deposits in the last few years. The bank focuses principally on lending to small and medium enterprise (SME). By specializing in a business sector that is underserved by financial institutions, BBL has curved out a very attractive niche for itself. It has created a countrywide network of SME service centers. These service centers keep operating costs low by complementing BBL branches and generate and monitor SME loan portfolio. BBL is managed by a relatively young, innovative and ambitious management team. The bank has invested significant resources to develop state of the art IT systems. BBL has internationally reputed institutions as shareholders, and a board representing these institutions ensures excellent corporate governance and minority investor protection. This is

a very important issue in a country where owner/director meddling has been the bane of once-formidable banks. The entrepreneurs behind them could and should play a much larger role in development, but too often are held back by a lack of ready access to financing from local formal sector financial institutions (Rosen (2003). The bank's investments, during the year 2008, were made mostly in government securities which stood at BDT 8,245 million as on December 2008. BBL did not have a capital markets operation. BRAC Bank proud to be the pioneering and largest SME bank in Bangladesh is discharging over 14,500 core taka in SME loan and helping fulfillment of more than 320,000 dreams that change hundreds and thousands of lives every day (Noman, 2011). However, BBL seems ready to participate in the capital markets in a significant way. It has acquired a 51% stake of BRAC-EPL Investments and BRAC EPL Brokerage Ltd. in 2009. We expect a significant growth in investment and fee income in coming years. BBL also has acquired 124,796 shares (approximately 5%) of Dun & Bradstreet (Bangladesh) that will participate in credit rating and debt advisory. SME sector, the main concentration area for the bank financing since its inception, comprises over 50% of the total loans and advances. Major portfolio of BRAC Bank belongs to commercial sector.

Since SME loan providing is one of the main business operations of BRAC Bank Limited so here it should be mentioned about the SME loan processing flow chart.



*Source: Website of Bracbank*

From the above flow chart the researchers see the procedure of SME loan system of BRAC Bank Limited. It should be mentioned here that for the security of the SME loans sanctioned by the bank to the customers it is required to have some written documents. For this bank collect necessary documents for supporting loan sanction process. After completing these types of total process bank serve SME loans.

## Data Analysis, interpretations and observations

An analysis is generated from the questionnaire to fulfill the objectives of the study. The number of respondents was 60 loan takers and employees of BRAC Bank Limited, Rajshahi Branch. From the responses of Bank's questionnaire, the researcher has taken the highly affecting responses and tries to find out the bank's problems in designing proper financial products for the SME. For the convenience of analysis the researcher has calculated the percentage of the responses. Several judgments are being made from the responses of the employees of BRAC Bank Ltd. to authenticate the objectives of the study. The results are presented below.

### Types of Facility

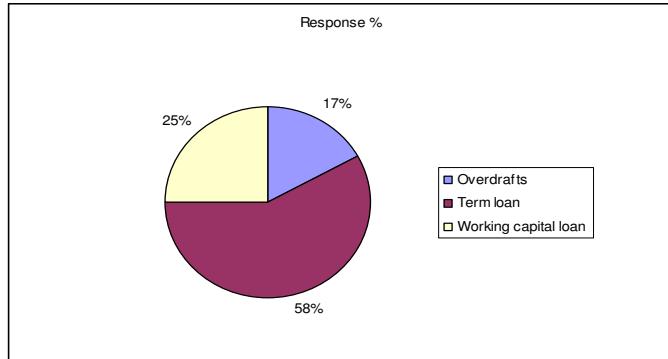
For achieving the purpose of this article, at first the researchers have tried to find out the types of facilities regarding the loan sanction of BRAC Bank Limited of Rajshahi Branch. The findings are given below by using table and chart.

**Table- 8.1: Facilities**

Types of Facility		
Types of facility	Response	Percentage
Overdrafts	10	17%
Term loan	35	58%
Working capital loan	15	25%
<b>Total</b>	<b>60</b>	<b>100%</b>

*Source: Field Survey*

**Graph: 8.1: Facilities Provided by BBL**



The above Table 7.1 shows the percentage of distribution of the different types of methods of loan taking facility with respect to the respondents. There is a clear indication that the distribution is not skewed to just one type of facility. A business can have more than one type of facilities depending on the purpose of the loan takers. About 58% of term loan is used by the loan taker to finance their capital expenditure. Then 25% of working capital loan is used by the loan taker to

finance their working operations of their firm performances. Nevertheless overdraft followed with 17%, a type of loan that attracts daily interest (restricted to the amount utilized) and it has a short term period of one year.

### **Effect and Contribution of SME Loan Performance**

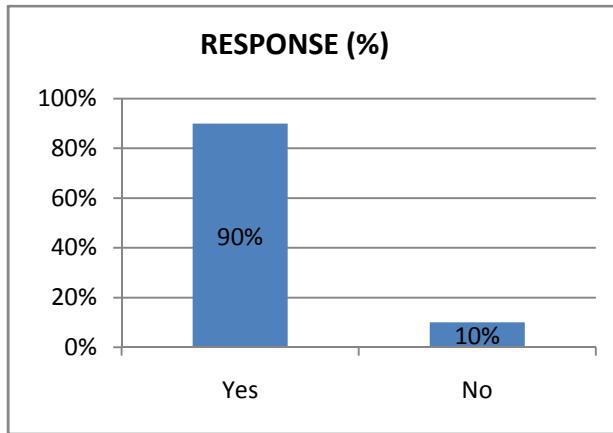
For attaining the objectives of this paper, the researchers find out the effect and contribution of SME loan performance which are showed on the following table and graph.

**Table 8.2: Effect and Contribution**

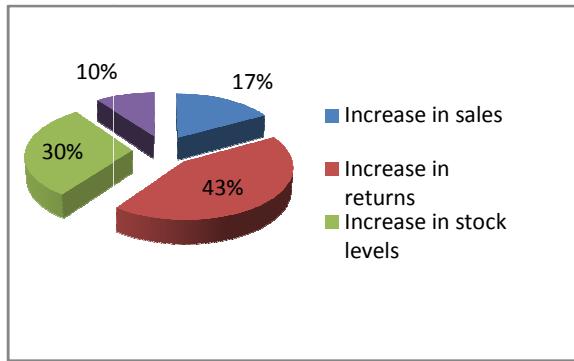
Effect			Contribution		
Level of Respondents	No. of Respondents	Percentage (%)	Performance Scale	No. of Respondents	Percentage (%)
<b>Highly</b>	54	90%	Increase in sales	10	17%
<b>Medium</b>	6	10%	Increase in returns	26	43%
<b>Lower</b>	0	0	Increase in stock levels	18	30%
<b>Nil</b>	0	0	Increase in profitability	6	10%
<b>Total</b>	60	100%	Total	60	100%

*Source: Field Survey*

**Graph- 8.2.1: Effect of SME Loan on Firm Performance.**



The above Table 7.2 and the histogram graph 7.2.1 indicate the percentage of respondents that the type of loan they have taken from the Bank either improved the overall firm performance or not. According to the findings of the table, 90% of total respondents are improved their total small and medium enterprises performance by the loan. On the other hand 10% has indicated that the loan did not improve the overall performance of their firm.

**Graph- 8.2.2: Effect of SME Loan on Firms' Performance**

The Table 7.2 and the pie chart 7.2.2 indicate the contribution of loan to respondents' firm performance. The table and the chart indicate that loan help business overall firm performance in diverse ways. Respondents chose taking loan for contributing to their firm's financial performance because of more than one reason. Percentage wise, most respondents (43%) opted for increase in returns with respect to improvement in overall firm performance. Increase in stock levels, that is inventory (30%) also on the high side implied that loan taken are used to purchase materials for production, thus businesses are able to increase their stock to mitigate demand. Definitely, with an increase in stock levels of (30%) of sample, it's not surprising that increase in sales is 17%, because an increase in stock levels with all things being equal increase sales. Also 10% of respondents agreed that the loans increase their profitability.

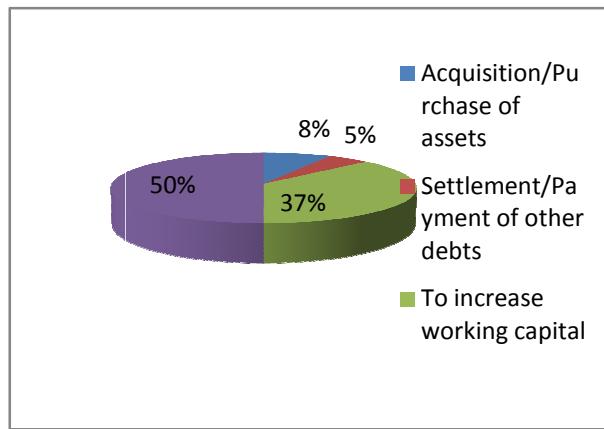
### **Utilization of SME Loans**

To focus the objective of this paper, the researchers find out the utilization of SME loan which is showed on the following table and pie chart.

**Table 8.3: Utilization of SME Loans**

Loan utilization	Respondents	Response %
Acquisition of assets	5	8%
Settlement/Payment of other debts	3	5%
To increase working capital	22	37%
Procuring raw materials	30	50%
<b>Total</b>	<b>60</b>	<b>100%</b>

*Source: Field Survey*

**Graph- 8.3: Utilization of SME Loan.**

The above Table 7.3 and the chart indicate how respondent utilized their accessed loan from the Bank. Majority percentage of the respondents (50%) utilizes the loan for procuring raw material to enable production. Respondents with 37% invest the loan in their business with the rational of increasing working capital. That is 8% of the total respondents who utilize loan in the acquisition of assets for their firms. Of the 5% of respondents which chose the utilization of loan for settlement of other debts.

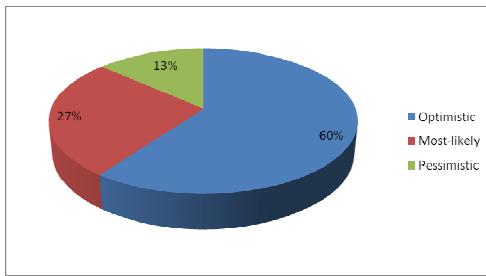
### **Result of Using SME Loan**

According to the field survey, the researchers have tried to find out the outcomes of using of SME loan. Here the researchers have focused on the types of facilities provided by the bank about the loans terms and conditions, whether the loans taken by the respondents satisfied their purposes or not and the respondents are satisfied or not by the interest rate charged by the bank. The findings regarding the outcomes of using of SME loan by respondents are given on the below table and charts.

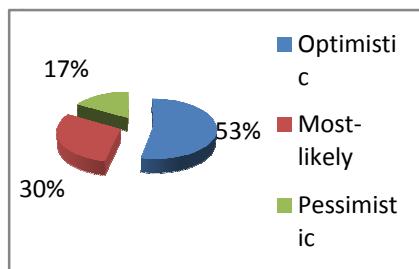
**Table- 8.4: Result of Using SME Loan**

Loan Satisfy its Purpose			Satisfaction of Interest Rate		
Loan purpose Satisfaction	Response	Percentage	Satisfaction	Response	Response
Optimistic	36	60%	Optimistic	32	53%
Most-likely	16	27%	Most-likely	18	30%
Pessimistic	8	13%	Pessimistic	10	17%
Total	60	100%	Total	60	100%

Source: Field Survey

**Graph: 8.4.1: Loan Satisfy its Purpose**

From Table 7.4 and the chart 7.4.1 shows that more than 60% of respondents expressed that they are mostly satisfied by using SME loan taken from the bank for their firm performance improvement, 27% respondents are averagely satisfied but 13% respondents are not satisfied by using SME loan taken from the bank for their firm performance improvement.

**Graph: 8.4.2 : Satisfaction of Interest Rate**

From the above Table 7.4 and the chart 7.4.2 we have found that the 17% of the respondents think that the interest rate of SME loan of BRAC Bank is high and 30% of the respondents think that the interest rate of SME loan on an average but 53% of the total respondent think that the interest rate is reasonable.

### **Conclusion and Policy Recommendations**

After observing all respondents the researcher concluded that BRAC bank is doing a great job in the SME sector. It is observed that the loan is not used by the clients for only one purpose rather it is used for meeting the capital expenditure and the working expenses as well; the loan given by the BRAC bank improving the overall performances of the small and medium enterprises of the respondents. Here it is also seen that by using the loan most of the respondents are experiencing increase return with respect to improvement in overall firm performance, they are also using the loan for purchasing raw materials for the purpose of increasing the inventory and their value of stock. And 53% of the respondents agree that this loan is improving profit of their small and medium enterprises. Most of the respondents are using their loan for the procurement of raw materials for their production and some are using for increasing working capital as well as acquisition of assets for their firms. At the very end of the analysis of this paper,

it is seen that 60% respondents are satisfied with loan given by BRAC bank and they are also satisfied with the interest rate which is charged by the BRAC bank for its loan.

But still it needs some adjustments; using SME loan most of the loanees have brought success. Similarly loan facility and utilization system is favorable to the clients but some clients realized that loan interest rate is not suitable for them. The researchers suggest some recommendations in this article from the aspect of bank employees and the borrowers for present and future sustainability of the SME loan of BRAC bank limited:

1. The loan sanction by the bank and its disbursement should be so easy and flexible so that different classes of people may consider for taking the loan for growth and sustaining of their small and medium enterprise.
2. BRAC bank should pay attention and revise its credit policy for the betterment and enhancement of the small and medium enterprises.
3. Barriers should be removed by taking advanced steps in mode of disbursement, charge documents and approval process.
4. The Bank should have more conference in overseas, work shop, symposium, and seminar for more expansion of SME loan.
5. BRAC Bank customer should be used SMEs loans in various sector rather than specific scheme.
6. In rural areas, BRAC Bank should want the SME Loan to alternate the poverty and also increase the self reliance.
7. Amount of loan can be increased in proportion to the existing demand of people in SME loan; SME loan can be popular among the small trader and lower income group people.
8. Interest rate should be reduced because most of their competitors are providing loans at a lower rate for example most of the competitor's banks providing loan at 12-15% interest rate.

Finally it can be told that Government, financial institutions and Non Government Organizations (NGOs) may take necessary steps to ensure uninterrupted financial support to the prospective SME loan in Bangladesh. Along with the discussion business power for sanctioning loans and advances can be increased at branch level and the Bank should have more conference in overseas, workshop and seminar for more expansion of the SME loan.

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