

**THE IMPACT OF CREDIT CONSTRAINTS ON SMALL AND
MEDIUM SCALE ENTERPRISES. A CASE STUDY OF
ISLAMABAD**



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M.PHIL. DEVELOPMENT STUDIES

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ISLAMABAD, PAKISTAN

SEPTEMBER 2019



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CERTIFICATE

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Date of Examination: April 10, 2020

ACKNOWLEDGEMENTS

First of all I would like to thank Allah (SWT) for blessing me with good health. Then my supervisor Dr. Jehangir Khan, not just he supervised me he taught me how to work as well. Then all my teachers of Pakistan Institute of Development Economics (PIDE) , who made me capable enough that today i am able to complete my thesis. I would also like to thank to my husband who helped me for data collection and helping me to made it possible.

Finally, I would like to thanks all my friends and family members for their continuous support and encouragement.

Nida Zainab

Mphil Development

studies

PIDE2017FMPHILDS22

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Abstract:

The present study examines the impact of credit constraints on small and medium enterprises in Islamabad. Small and Medium size Enterprises (SME's) are very important part of the economy. There are four types of enterprises in a country micro small and medium and large. Small and medium enterprises contribute 40% to the GDP. Since they generate 60 -70 percent employment in low income countries. According to the Economic Census of Pakistan (2005), there were almost 2.96 million units in Pakistan, 90% of total businesses in Pakistan are either Small or Medium size Enterprises. But SMEs are facing a lot of credit constraints that are creating problems for their economic growth and development. Primary data were collected through interviews. descriptive research design has been use in this study. Units of data collection for this study were SME Executives, SMEDA, Chamber of Commerce and government and commercial Banks. The results show that major constraints faced by SMEs in term of financing are high tax rates, legislative framework, high interest rates, high transaction costs, high collateral requirements, lengthy procedure and less government support. Policy recommendations are also provided in this study that government should take serious measure to reduce high tax rates and interest rates. She should take steps to restrict banks to reduce their collateral requirements and their documentation procedure should not be lengthy it should be easy to read.

Chapter 1

Introduction

1.1. What are SMEs

SME stands for Small and medium-sized enterprises (SMEs) or small and medium-sized businesses (SMBs) are business whose personnel numbers fall below certain limits. Actually the SME sector plays an extremely important part in modern economy, proving to be the most attractive and tremendous innovative system. The number of employees in SMEs vary from industry to industry. The CEOs of SMEs often are the founders, owners, and manager of the SMEs. A CEO needs to strategically allocate her/his time, energy, and assets to direct the SMEs. CEO is the reason of whether the SMEs is going to develop or going to fail

Small and Medium-sized Enterprises (SME's) are very essential part of the economy. There are there types of enterprises in a country micro small and medium. They give 40% to the GDP. Since they generate 60 -70 percent employment in low income countries (Amaad and Sadaf, 2017). The definition of SME'S is contested, it varies from context to context. For instance, in USA SME'S are defined as enterprises having an employee strength of less than 500 while in European union the employee strength of SME'S is said to be 250¹. SME's are also defined on the basis of financial assets that they own. For example SMEs balance sheet should not surpass than forty three million EURO and should not surpass than fifty million EURO in turnover.

As we know that there is difference in SMEs definition in different countries. Its definition also differs in Pakistan that are creating problems for the businessman. As

¹ OECD 2005, OECD SME and entrepreneurship 2005, OECD Paris , page 17

according to SBP (state bank of Pakistan) SMEs are also defined differently. Small enterprises are those having an employee strength fewer than fifty staff with an annual sales turnover of one hundred and fifty million rupees, while medium enterprises are those having an employee strength of fifty to hundred staff in the case of a trading establishment or having fifty to two hundred staff in the case of a manufacturing establishment. The annual sales turnover should be between 150 million to 800 million Pakistani rupees². While federal bureau of Pakistan defines SME's in a way that small enterprises are those that employ less than 10 persons .). So as we know in Pakistani context SME definition varies from context to context. so my definition of SME is the companies with less than 50 workers with an annual turnover of 10 million Pakistani rupees will come under small enterprises and companies with more than 250 workers personnel with an annual sale turnover of 50 million rupees will come under medium enterprises

But the contest over the definitions is of little value considering the impact SME'S have on an economy. For instance, as quoted above according to some studies SME's account for 60 to 70 % total employment in low income countries.

Role of SMEs in Pakistan:

Pakistan is 24th largest economy in term of purchasing power parity. and 42 largest in its nominal GDP. Pakistan is a country of 207 million populations with \$1641 nominal GDP per capita who rank on 147th all over the world. SMEs are very significant part of economy in which there are almost thirty-eight million small enterprises and medium enterprises in Pakistan where 8 lacs are industrial units, 12 lac service sectors, 18 lac commercial and retails shops. in which 41% of industrial units are in urban areas while 59% are in rural areas. The provisional GDP growth rate for Fiscal year 2019 is accessed at 3.29% which is based on 0.85, 1.40 and 4.71% growth in agricultural, industrial and services sectors separately. Where SME sector donates 40% to the GDP. The provisional agriculture sector growth is determined at 0.85%. The crops sector has a negative growth of 4.4% in FY2019

² DAR.M.S , Ahmed S and Raziq 2017 Small And Medium Size Enterprises in Pakistan definition and critical issues, Pakistan business Review 19(1) 46-17

mostly due to negative growth of -6.6% of important crops. in 2019 The temporary growth in the industrial sector was estimated to be only 1.40% mainly due to 2.06% reduce in the large scale industrial sector and 1.96% reduce in mining and quarrying sector. Provisional growth in service sector is assessed at 4.71%. While Wholesale and Retail Trade sector grew at a rate of 3.11%.

According to Pakistan's Economic Census (2005), there were approximately 2.96 million units in Pakistan, 90% of Pakistan's total enterprises are either small or medium-sized enterprises. Where Establishments were 2.8 million (93.9 percent) and Household Units were 0.18 million (6.1 per cent). Punjab was the one with the highest share of the total establishments in 2005 of 65.26 percent, The share of Sindh (17.82%), the NWFP (14.21%), and the share of Baluchistan (2.09%). In the major industry sector of wholesale and retail trade and hotels / restaurants, government, social and personal services (22.3 per cent), the sum of 2,96 million institution and household units was approximately 53 per cent (Bizomer, 2009). With 19.72 percent of the total Institutions, manufacturing sector is third largest among other household units. the highest share is that of manufacturing sector (66.5%), Community, Social and Personal Services (20.5%), Agriculture, Poultry Farming, Fishing etc. (8.7%), and Wholesale and Retail Trade, etc., (about 4.00%). (Bizomer. (2009).

SMEs are playing a very essential role in economic growth of a country Pakistan. it plays a very important role in employment generation, poverty reduction, and als improve the living standards of a poor societies. There are almost 90% of the enterprises are SMEs in most of the countries that are creating economic growth and development in a country. To give support for strengthening SMEs sector, the government has created the SMEs Policy 2007; this policy main aim was to make more advancements in SME sector and to implement it for providing an environment of economic growth for a whole country. This policy covered the areas that include financial access, human development, technology un-gradation, a good business atmosphere and all of them are directly intertwined with a SMEs sector who has will to improve the economic conditions of Pakistan. And the SMEs have an ability to improve the economic growth in many ways; by reducing poverty, creating

employment, providing innovation to the economy, increasing exports and also contribute to increase the GDP of a country. (dr Akhter Hussain shah, 2018)

According to Farid (2016), there are 3.2 million enterprises in Pakistan of about 99% and also having value added share of 35%. According to Pakistan today (2018) SMEs are contributing 30% to GDP , 25% to the exports and 78% to industrial employment which had established very significant role in the country's economic growth and development. Accordingly, SME growth has an ability to make a progressive economy. Private businesses in the industrial sector employ almost 78 percent of non-agricultural labor force, 25 percent of manufactured goods exports besides sharing 35 percent of added value in manufacturing.

According to Pakistan Economic Survey (2012-13), however, economy of Pakistan is constantly facing problems due to energy crises, rains and floods, weak law and order situation and many other systemic barriers that are creating problems in country's development. Pakistan's economy over the past five years has grown up at an average percentage of 2.9 per annum. Industrial sector has 20.9 per cent share of GDP has sub-sectors: manufacturing, construction, mining & quarrying, distribution of electricity and gas. The trade sector has a GDP share of 13.2 per cent. Trade sector growth is assessed at 3.5 per cent compared with last year's 2.1 per cent growth (Muhammad Wasim Jan Khan et al, 2014).

The features & the importance of small and medium-size enterprises:

SMEs are jobs creators for employees where the motivation and flexibility are better. Also, SMEs have created the competitive state of the market which lead to better satisfaction of consumer's needs. SMEs also contribute in supplying certain activities to help big enterprises in a way of producing goods and services efficiently. Another important feature of SMEs is Focusing on innovative processes, both in technology and in management. Thus, they help in forming the GDP and increasing the national export and play role in maintaining the social-political stability in a country

SME's have a significant impact on the reduction of poverty through employment generation but SME needs quick and affordable credit as well. (Ali 2013) (Sharafat et al 2014). SME's contribute to economic growth in form of incentivizing innovation and entrepreneurship as discussed by Agyapong (2010). The study also found that major portion of exports was held by the SME sector in the case the west African country of Ghana. The SME contribution to employment is supported by statistical reports such the US Census 2001 which reported that the SME sector employed 57.3 million of 115 million total employed workers in the US alone. Emphasizing the role of SME's in the development of economic conditions of a country Kongolo (2010) report that more than half of the total Agriculture farm output in South Africa was accredited to SME's working in the agriculture sector. Studies such as Beck et al 2005 have given a cross country analysis rather than single country case. The OLS regression estimates showed a positive relationship between SME's employment and growth. In case of Pakistan the prominent studies such as Syed et al 2012, and shah 2018 along with Ali 2013 and Sharafat et al (2014) also support the results of Agyapong 2010 Kongodo 2010 and beck et al 2014 reveals in their studies that there is a positive relationship between economic growth, output, employment poverty alleviation and SME's. while most of these studies have taken the case of specific countries or cross country any analysis some have also dug deep and taken states/provinces within countries. For instance, Answer Ali Shah G, Syed et al 2012, took the case Sindh and found that SME sector of Sindh has positive impact on GDP through valuable Foreign Exchange inflow.

The government realized that more concrete steps are needed to make full use of the SME sector's potential and lead it to growth; State Bank of Pakistan (SBP) has advised all banks to provide their input in formulating an action plan for SME promotion policy. This is the product of SBP's recognition that strong institutions are a pre-requisite for a productive SME sector that also requires a strong industry structure that could provide the necessary support to make it easier for SMEs to achieve financial objectives and competitiveness. A strong sector of SMEs will in the long run reduce the need for costly imports and boost the economy. In addition, SBP has also set a goal to complement the financial inclusion of SMEs by 2020 to enable substantial growth and development for the SME sector witnesses. (Dr Akhter Hussain shah, 2018)

While the studies agree that SME's have a optimistic effect on the key economic indicators such as GDP employment and incomes there is one problem on which most studies have a consensus too. And that is of low credit availability. For instance, Sharafat et al 2014, Ali 2013 report that SME sectors faces considerable credit constraints in Pakistan. Agyapong (2010) while doing a study for Ghana reported that that the biggest hindrance that the SME's faced was that of non-availability of credit. Shah (2018) extensively argues about the absence of credit availability, credit guarantee schemes and the overwhelmingly complicated financial system which is highly regulated when it comes to SME's as the major hurdle in the growth of Pakistan SME's sector. While studies have focused on the effect of SME's on Economic growth and their role on poverty alleviation and most studies have diagnosed lack of credit availability as the major hurdle faced by SME sector both in Pakistan and elsewhere there has been no work on identifying the specific credit constraints faced by SME's, the nature of those constraints and the best ways to remove them. How does the banking industry, the government and the SME sector coordinate among themselves and what are the dynamics of this trio? This is the gap that this study intends to fill.

Previous work on the SME's has focused on quantitative techniques. Studies have relied on co-integration techniques and regression models. But there has been little attempt at approaching the issue from an angle wherein we can have a holistic picture and what the problems of the SME's really are. This study will focus on the problems of the SME and will attempt to approach it from qualitative angle. Reason being that the regression models as applied by other studies do not have the ability to capture the problems of SME's as a whole rather they just show dependence and in some case causation. But in reality there are a lot of barriers like for example credit constraints. The regressions models as adopted by previous studies are not able to explain the issues that the SME industry is facing and the possible solutions that could solve credit availability problems. It is for this reason that the study will adopt qualitative research methodology and ethnographic methods such as Interviews and Questioners and methods to collect primary data.

1.2. Operational definition of SMEs:

SME meanings aren't unique; they vary from country to country. Some countries identify very different types of SMEs. Others define SMEs based on their employment and some define SMEs based on their revenue and assets capitalization. In Pakistan SMEDA describes small and medium-sized companies on the basis of employee's strength and total production assets. While SME bank describes SME as the metric, based on total asset numbers. Whereas SBP describes SMEs based on company character, number of workers, net sales per annum and the amount of capital employed. (Dar, M. S., Raziq, A. & Ahmed, S. (2017). The concept of SMEs in Pakistan lies in the number of employees up to 250 people, up to Rs.25 million of paid-up capital and annual sales up to Rs.250 million (Kureshi et al., 2009). So as we know in Pakistani context SME definition varies from context to context .so my operationalize definition of SME is the companies with less than 50 workers with an annual turnover of 10 million Pakistani rupees will come under small enterprises and companies with more than 250 workers personnel with an annual sale turnover of 50 million rupees will come under medium enterprises. This definition should be applied in Pakistani context to target the goals and needs that the enterprise is going to fulfil. If this definition will be applied throughout the country, it will be helpful for a country to separate the enterprises and the problems that enterprises are facing and how a government can resolve them. The definition should be advanced in ways that achieve not only the national objectives but also the international perspective

Institution	Criteria	Medium Scale	Small Scale
SMEDA	No of employees less than 250 Productive assets	Between 36 -99 20-40 million	Between 10-35 2-20million pkr
SME BANK	Total assets Number of employees	Over 100 million PKR NA	<100 million <10 employees
SBP	Nature of business (service, manufacturing) No of employees Capital employed Sales per anum	Less than 250 employees and less than 100 million PKR assets for manufacturing. Less than 50 employees and less than 50 million PKR for trade/services. Net sales less than 300 million PKR	Less than 250 employees and less than 100 million PKR assets for manufacturing. Less than 50 employees and less than 50 million PKR for trade/services. Net sales less than 300 million PKR

In Pakistan context there is no standardize definition of SME which is also affecting the performance of SMEs. Pakistan government and political regimes are failed to provide the definition of SME. A consistent and synchronized definition of small medium enterprises will help for the development and growth of SME. So therefore as a academicians a proposed definition of SME is given below which is projected to advantage Pakistan for their development and growth.

1.2.1. Proposed Definition of SMEs:

	ENTERPRISE CATEGORY	NUMBER OF EMPLOYEES	TOTAL ASSETS
PROPOSED DEFINITION OF SME	Small scale enterprises	Between 5-24	Less than 50 million PKR
	Medium scale enterprises	Between 25-99	Over 50 million PKR

1.3. Research Objectives

- 1) To understand the problems of non-availability of credit faced by the SME's in Pakistan.
- 2) To Find out the problems of Banking sector that limit availability of credit to the SME's sector and that how can SME sector be made more attractive investment option
- 3) . To find out the Government policies and regulations that may hinder credit availability to SME's.

1.4. Research Questions

The central theme of this study is to find out the impact of credit constraints on SMEs in Islamabad Pakistan. In this backdrop, following are the research questions have been upraised:

- 1) What are the specific credit constraints faced by SME's and how does the Banking sector and banking sector regulations limit credit to SME's?

In this research question I will find out the constraints that are facing by SMEs by interviewing the SMEs bank Executives, SMEDA and chamber of commerce. We will interview them about SMEs that why SMEs are facing credit constraints and what initiatives government should take to solve these problems.

- 2) What are the successful models of Credit availability to the SME's around the world?

In this research question we will find out what are the successful models of Credit availability to SMEs are followed by different countries and how we can follow these model to solve our problems of SMEs.

- 3) What can the Government Do to Solve these problems which are facing by SMEs? In this research question by interviewing our UDCs and knowing the actual issue that are facing by SMEs in Pakistan we will give precautions that a government should follow to solve the credit problems of SMEs in Pakistan. If these steps will be taken it will make SMEs of a country to be able to improve country economic growth and development.

1.5. Units of Data Collection

In this proposed thesis following UDCs are used to collect data.

UDC 1- SME Executives:

These are the founders, owners and managers of SMEs. they are accountable to run an organization, although the nature of their roles varies depending on the organization. This UDC will help me in getting information about what constraints are facing by small and medium enterprises and what they think about this problem and how it Can be resolved. What are their opinion about the steps that government should take to improve this sector of Pakistan and create the economic growth of a country?

UDC 2- SME banks:

These are sections of bank that are dealing with SME'S such as SME Division which is the focal point of all SME related issue in State bank of Pakistan and SME financing divisions

of commercial banks like summit bank, SME bank, Faysal band, Bank of Punjab. they will help us in getting information about the problems of low availability of credit that are facing by SME's and how it can be resolved and what hurdles do they face in the disbursement of loans to SME's

UDC 3- government:

SMEDA is Pakistan's government institution, under the Ministry of Industry and Production. The main focus of this institute is to provide Small and Medium Enterprises with enabling environment and business development services. The key goal is the growth of a globally competitive small and medium-sized enterprises market, through business and support services, as a driver of sustainable growth for the country." this UDC will help me in getting information about the constraints that are facing by SMEs and what initiatives government should take to resolve these issue to make sustainable growth for economy of Pakistan.

UDC 4- chamber of commerce:

It is a type of business network whose main focus is to promote the interest of businesses. They serve as spokespeople and representatives of business community. they are business owners in cities and towns to fund these local societies on behalf of the business community. They will help us in getting information about the local businesses that are established in Islamabad and what are the credit constraints faced by them. What obstacles they are facing in getting finance.

1.6. Significance of the study

Most of the previous work on SME's has focused on the effect of SME's on the Economy and major Economic Variables such as the GDP, Employment, Poverty reduction, and innovation. Very little attention is paid to the problems faced by SME's. for example, many studies agree that low credit availability is one of the major hurdles faced by SME sector around the World. Yet a detailed analysis of the credit constraints is missing. This creates a gap in the academic and policy researches and the current study aims to fill that gap by

attempting to analyse the type of credit constraints the SME face and how can those issues be understood and what solution can be recommended.

Chapter 2

Review of Literature

2.1. SMEs and poverty:

Sharafat Ali et al. (2014) study the impact of Small and Medium Enterprises on poverty alleviation. This study focused on the impact of small scale industries on poverty in Pakistan. They use autoregressive model where Inflation, health expenditure, population growth rate, income inequality and one year lagged value of poverty head count index as explanatory variables. They use Annual time series data for the period of 1972-2007 The data of small scale industries' output as percentage of GDP (SME) and Health Expenditure as Percentage of GDP (HE) for the 1972-2004 has been obtained from the Statistical Handbook (2005) of State Bank of Pakistan and the data for these variables for the period of 2005-07 has been taken from the State Bank of Pakistan Annual Report (2008). Annual poverty Head Count Ratio (HCR) and income inequality measured by Gini coefficient (GINI) has been obtained from Annual Economic Survey of the Ministry of Finance, Government of Pakistan. The population growth rate (P) and consumer price index (CPI) has been taken from the World Development Indicators (WDI) (2008) of the World bank. The result of the study shows negative impact of small scale industries output on the poverty level of Pakistan. So the results of this study is significant that small scale enterprises are playing very important role for poverty reduction, employment generation and economic growth. They also give the recommendations to the economic policy makers to pay attention on the financial problems faced by SME'S and give credit rights and reduce the credits costs to help the SME'S sector in Pakistan

Sharafat Ali, (2013) did an empirical analysis on the impact of small and medium enterprises on poverty. His study reveals that SME's are very important for reducing poverty and employment generation and for economic growth, they use the time series data from 1972 to 2008 to check the impact of SME'S on poverty, they employed Johansson cointegration and correction error mechanism to see the impact of SME's on poverty and

they came to the fact that SME's are reducing poverty. They also give the recommendations to the economic policy makers to pay attention on the financial problems faced by SME'S and give credit rights and reduce the credits costs to help the SME'S sector in Pakistan.

Daniel Agyapong, (2010) study the importance of SME's for economic growth and reducing poverty in Ghana. They study the views of pro and anti pro SME'S where pro MSME'S (micro, small and medium enterprises) believe that small businesses are creating the economic growth while anti SME's believe on the large organizations that are increasing economic growth. So from all of above discussion they concluded that the small businesses play a very key important role in creating job, contributing in taxes, increases the imports and exports, also creates the innovation and entrepreneurship reducing poverty. They also give the policy recommendations to the government to give the credit support and non-financial business services to MSME'S

Thorsten Beck et al, 2005 in his study find out the relationship of SME's economic growth and poverty alleviation. They take the data of 45 countries to find out the share of SME labor on manufacturing labor force. They did the OLS Regression that shows that there is positive relation among the SME's and economic growth. But through the cross country analysis they don't get the evidence that SME's are reducing poverty. Their results do not found any relationship among SME's and poverty. And the results do not show the empirical supports to the SME's development to poverty Alleviation and increase growth.

2.2. SMEs and economic growth/ development:

Mukole kongolo, 2010 study the role of SME's on the economic development in south Africa. He tells us in his study that SME'are playing a very importance role in economic growth and development by different ways, by generating employment for rural labor force and urban labor force and by providing the continuity and innovation to the economy. His study shows that SME's represents a big part of businesses in developing countries. About more than half of the non-farm output are produced by SME's by making the contributions to economy in south Africa and other developing countries. and these SME's are also playing a main role in creating employments. Despite all this he also talked about the challenges faced by SME's in south Africa. They says that it will be a good approach

to focus on the development of SME's sector because SME's are very important source for the country growth and development of their economy.

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Dr. Syed Akter Hussain shah (2018) did a study on the SME'S sector development in Pakistan. His study shows that SME'S are very significant for the growth of the country. All nations in the world are improving their economy and national development through their strong SME sector. His study shows that SME's are growing economy of Pakistan through creating employment opportunities, innovation and the human resource development He use the secondary data collection sources of Pakistan government organizations such as SMEDA and the industrial development board for analysis and he use both the quantitative and qualitative techniques. He interviewed the employees and businessmen that are involved in SME business. His study additionally discusses the problems and challenges that face the SME sector of Asian nation. these over-regulated business surroundings; complex human resource development surroundings, which includes shortage of masterful manpower and lack of efficient technological framework; market constraints, covering restricted disclosure of SMEs to international market and incapability to faucet new market and resources; lack of business undertakings, portraying the necessity for brand remarkable new schemes and incubators to help in new businesses development; and refined money facilities, that could be a key challenge to the SME sector. he provides the strategy to beat these challenges that face by SME sector of Asian nation. The strategy framework provides the commendations for the Judicial surroundings, Regions Development Approach, Institutional Framework, Sectors Development Approach, Access to Finance, that suggests steps within the style of Credit Guarantee Schemes and Equity Participation Fund.

Towards the tip, the paper outlines the expected outcomes and impact that might be achieved through materializing the recommendations.

Subhan et al, (2014) empirically study the effect of innovation prevailing in SME's on the economic development from the period of 1980 to 2013. They show that innovations are very important for the economic development. They use national and international sources to collect the data such as Asian development outlook 2013, Pakistan economic survey, government of Pakistan and key indicators 2013. To measure the effect of SME's performance on economic development and the impact of innovation on performance of SME's they use the log linear regression model. They construct two equations to know the impacts and their outcomes shows that there is a positive relationship between economic development and innovation that prevails in SME's. And shows that by making improvements in process of innovation these will be increase in SME growth and that will enhance the economy of Pakistan.

G. Syed et al, (2012) did a study on the effect of SME'S on the economic development of Pakistan. They have taken the case of Sindh. In this study to analyse the data they have used descriptive statistics, paired sample t test, Pearson product moment correlation analysis. They follow the questionnaire research design. The questionnaire were used to collect data There results show that SMEs have positive impact on the economic growth of Pakistan, on their foreign exchange earnings, exports and GDP. Their study reveals that SME's are also playing a very significant role in employment generation of the rural area of Sindh in Pakistan. And they also suggest government to take measures for developing the SME sector of Pakistan.

Hussain, I., Farooq, Z., & Akhtar, W. (2012) empirically examines the recent developments of SMEs and the importance of public private partnerships for development of SMEs. They use questionnaires to get data from SMEs owners and top managers to get the status of their enterprises and also examines SME development strategies follow by them. They used linear regression to analyze data and take sample form 72 SMEs. They said that SMEs are playing very important role in the economy of developing counties as they are taking more than 90% of the firms outside the agriculture sector. They also find out the constraints that are faced by SMEs that include lack of funding, low human resource abilities, and

technological abilities. After studying different development strategies that are used by SMEs they came to the result that there is a positive relationship between public and private partnerships and growth performance of SMEs and said that PPPs is the best development strategy for the future. They also gives policy recommendation for the SMEs development in Pakistan.

2.3. SMEs and employment:

G. Syed et al, (2012) did a study on the effect of SME on the employment in textile industry of Pakistan. They use simple random technique to collect data. They develop the structural questionnaire and collect data from 100 respondents from 30 organizations The data were collected from the various sources included All Pakistan Cotton Mills association, the export promotion bureau. Cotton central research institute, Multan and WTO. All the study reveals that SME'S play a very important role for foreign exchange earnings, to increase the country GDP, to boost up the entrepreneurial strength and these SME'S are the key feature of alleviating poverty through employment generation. Their result also shows that that SME's services and products are very good in quality and are more proficient in resource Distribution than the large businesses.

2.4. SMEs and credit constraints:

Abubakr Saeed et al (2015) did an empirical study on the impact of bank market concentration of financial constraints on firm investment, they did cross-industries panel of 368 listed Pakistani non-financial firms over the period of 2001-2009. And they use generalized method of moments estimation technique to estimate the panel data model. And they came to the result that SMEs are facing credit constraints due to reduction in bank concentration. And their results also show that opaque firms are facing more credit constraints due to less bank concentration.their results give support to the market power hypothesis that more bank competition lead to reduce credit constraints on firm level investment. The positive effect of bank market concentration is more prominent for small enterprises. When we alternate the bank market concentration variable for different measure (three-bank concentration), the results persist unchanged. – The results, first, measure the usefulness of current financial improvements in Pakistan and, second, offer

suggestions for other economies that show economic development similar to that of Pakistan.

Thorsten beck (2007), shows that SMEs are facing more financial constraints than the large enterprises because of the flaws in monetary systems of many emerging countries. Their conceptual framework shows that unsymmetrical information and transaction costs between lender and borrower are the main factors that are explaining the financial constraints that are facing by SMEs in developing countries. They argue strategies and improvements that can lead financial institutions to lend to SMEs and also give comments on the government role in establishment building and also in providing the controlling framework and take policies that are friendly to market such as credit assurance schemes. They also points out the difficulties in government involvement in SMEs financing.

TAHAR HANEEF (2010), did an empirical study in lahore on the obstacles to growth in SMEs. These obstacles include capital shortage, high production cost, unpaid accounts receivables, high markup rates and difficulties in getting finance. They collect primary data through questionnaire and did multiple regression and Pearson correlation to analyze the data through SPSS. And their result shows that these obstacles have a negative effect on the SMEs Growth in Lahore. They also give commendations that government should take serious steps to provide capital to SMEs and also make a legal system who takes the legal action against the delayed actions to improve the growth of SMEs

Syed Manzur Quader et al (2008) did a study on impact of credit constraints on SMEs and they show that SMEs play a significant role in development and underdevelopment of a economy. They shows that there are many problems that SMEs are facing related to raw materials, power, land, marketing, transport, technical facilities, and finance. And these problems are creating issues for the SMEs to increase the GDP ad growth of a country. They use varimax normalization method based on primary questionnaire survey and rank the factor constraints according to their level of severity to find out the constraints that are facing SMEs in Bangladesh. the study have shown that there are seven main factor that are the main weaknesses to SMEs growth and its development in which high rate of markups, controlling constraints of government, small size of maket domestically, collateral needs for getting finance and availability of very less technical skilled labors are one the highest.

RA Cole, A Dietrich (2017), did a study on the credit availability of SME's all around the world. To test the importance of government for the accessibility of credit They use data from the World Bank's Enterprise Surveys of 133 countries over the period from 2006 – 2014. They take data from firms who have fewer than 500 employees as per the united states SMEs definition. They see the credit availability process to SMEs in three steps. By following these three steps, they distribute small businesses into four clusters according to their needs of finance. In a first step, they examine which firms need credit and which firms do not. In the second step they analyze that which firms are dejected. And in the third step they analyze that the firms that applied for the credit either get deprived of or get accepted. From all of the above discussion they came to the result that governance on country level play a very serious role in availability of finance to SMEs for both developed and developing nations.

O Arsalan, MB Karan (2009) focuses on the important factors that are causing credit risks to the SMEs in turkey. They did a study on two types of firms domestic and international. Domestic are those that make local sales and international firms are those that also make sales abroad. they provide evidence in this study that credit risk aspects of national firms differ from those of international firms. They did regression analysis by using linear probability model. Their results show that domestic firms are more in need to reduce unavailability of credit. Because there is a positive relationship between their proportion of economic expenditures to total assets and the possibility of financial risks. They have found that off-the-record transactions are playing an incidentally vital role in increasing the credit risks of both the national and international SMEs.

I Ahmad, K Alam (2015) did a study on flow of credit manufacturing sector of Pakistan. The data shows that credit availability to manufacturing sector of Pakistan increases from December 2006 to December 2014, Though, its part of total industry credit to government and non-government sectors declined from 35 to 16 percent during this period. Moreover, the results show that asses to credit to manufacturing sector increases while its share to overall industry credit has been decreases over a nine-year period. this obtainability of finance is focused in a few subsectors both in the manufacturing sector overall as well as among manufacturing SMEs. This imitates the low level of change where funding is

concerned. Having recognized numerous aims for this low level of funding, we observe the role of the central bank and suggest what actions it could take to improve the loaning marketplace for SMEs. They conclude that funding to manufacturing sector primarily decline and then enlarged over a six years period of time.

Ahmed, k and Chowdhury T.A (2009) did a study on evaluation of the enactment of SMEs in Bangladesh. They said that SMEs development playing a very vital role in in poverty alleviation, employment generation and the rapid industrialization. They did a desk research in which they collect data from secondary sources. In this study author tried to find out the problems that are facing SMEs. They said that SMEs performance of Bangladesh are below the international standards in terms of turnover rate of a worker, funds distribution, superiority assurance and in marketing activities. Government is not paying much attention to this sector they said that government should more focusses on this area. They also give some suggestions to overcome the problems that are the hurdles in development of SMEs in Bangladesh.

Sherazi, S. K et al (2013) investigates the problems that are fronting SMEs in Pakistan. They collect data by from 107 SMEs firms that are located in Rawalpindi Islamabad. The data were collected by using questionnaire survey. They have use principal component analysis approach to rank the lowest and highest difficulties aspects for doing business in SME part of Pakistan they have found six major obstacles that are facing SMEs in which financial constraints are on highest and the Secord highest is Corruption. The other 4 obstacles are “public and technical obstacles, Training obstacles, Supervision and Infrastructure obstacles. They also give recommendations to the government and rule makers to overcome the problems of SME in Pakistan.

Ullah, M. S. et al, (2016) This study shows that globally SMEs are considered to be financially stressed. According to small and medium enterprises authority (SMEDA) most of the SME startup fails within 4 years due to financial constraints and stress. This study surveys the rate of SMEs failure due to financial stress. The primary data has been collected form 433 SMEs that are randomly selected from market committees list. They came to the result that 90% of the entrepreneurs get finance from up to rotated savings and credit Associations (ROSCAs). Respondents considered non availability of finance is a lesser

problem than the issues like defaulted customers, competition and supply to electricity. High failure rate was not detectable in any age group.

Qureshi, J., & Herani, G. M. (2011) discover out the problems that are faced by SMEs in financing that are a big hurdle in their growth and financial position. These constraints are faced by SMEs not only in Karachi but also in the other areas of Pakistan. They did a quantitative and qualitative research and their study is exploratory in nature. Their methods of data collection were Questionnaires that were taken from 500 SMEs respondents in Karachi. And the interviews were taken from businessmen and bankers. Their finding shows that most of SMEs do not get agree to take finance from bank due to their high mark up, prolonged documentary process or from professional negligence to some extent. Their preference is always to lending the large enterprises. Their Results shows that SMEs in Karachi are unable to enjoy the financial advantages due to the credit constraints, no government support, internal flaws and weakness of SMEs in their business management. They also give recommendation to the government and policy makers to improve the SMEs financing issues In Karachi Pakistan.

Khawaja, S. (2006) did a study on the potential of SMEs and the improvement in productivity. They show that SMEs play very significant role in creating employments, poverty reduction and income generation and how it transforms the economy from low to middle income group. They also talked about the constraints that are faced by SMEs and the efficiency of government policies to solve that problems for the SME growth. They also give a snapshot of the present strategies that are adopted for the growth of SMEs and also give comments on the possibilities of interventions that they can make to improve SMEs growth and development.

World Bank Enterprise Survey Report (2013). This survey was done to obtain feedback from enterprises on the state of the private sector as well as to help in building a panel of enterprise data that will make it possible to track changes in the business environment over time, thus allowing, for example, impact assessments of reforms. Through interviews with firms in the manufacturing and services sectors, the survey assesses the constraints to private sector growth and creates statistically significant business environment indicators

that are comparable across countries. The standard Enterprise Survey topics include firm characteristics, gender participation, access to finance, annual sales, costs of inputs/labor, workforce composition, bribery, licensing, infrastructure, trade, crime, competition, capacity utilization, land and permits, taxation, informality, business-government relations, innovation and technology, and performance measures. Data from 1,247 establishments was analyzed. Stratified random sampling was used to select the surveyed businesses. Data was collected using face-to-face interviews. The enterprise survey have found the major constraints that faced by SMEs are corruption, electricity, political instability, tax administration, crime theft and disorder, tax rates, inadequate educated work force, asses to finance, custum and trade regulations, transportation.

2.5. SMEs and human resources:

Khan, Awang, & Zulkifli (2013) did a research in Pakistan on human resource practices and SMEs. they show that SMEs plays a positive role in the economic development and growth. Their study also discusses the universal views of SMEs that are operating in Pakistan and human resource practices in SMEs. Their results show that SMEs have a great will to increase the social and economic development. And they also address the issues that are facing SMEs in Pakistan regarding HR practices. Having no proper competency implement human resource practices because of the shortage of HR practitioners becomes the major difficulties, faced by these SMEs, to increase their results. According to them significant steps to be taken is necessary to improve the sources of organizational proficiencies to achieve the SME performance.

2.6. SMEs and finance:

Khan M.M (2015) did a study on the sources of finance that are available for SME sector in Pakistan. They show that SMEs are play important role in the economic development of country, poverty reduction, generate employment, income equality and entrepreneurial culture. Keeping in view the importance of SME sector in Pakistan, stockholders achieved many milestones along with establishment including Small and Medium Enterprises

Development Authority (SMEDA), but at the same time SMEs faced many other problems such as the problem of improper infrastructure, difficulties in regulatory requirements, lack of skilled HR, having not good competitive products, and have lack of expertise in entrepreneurial department. little range of business and threat of failure to pay but from all of above access to credit is the major hurdle that are facing SMEs (especially small businesses because of their high risk and small scope of business and non-availability of financial statements) for their growth and development. This study focus on the sources of finance that are available for SMEs and also the problems that are facing by SMEs in getting financial facilities. They conclude that availability of finance is a key factor of success to SMEs in Pakistan.

Khan, S. (2015) shows that SMEs have very important role in the generation of employment, poverty improvement income distribution. This study empirically investigates about the impact of diverse types of answer on the Small and medium enterprises growth and development in rising counties by using of Pakistan's case. They did panel data analysis and using 78 SMEs data in Pakistan over the 3 years including the years 2002, 2007 and 2010. results show positive role of bank in growth of SME in the sample given period. But on another side other informal sectors did not play a positive role in growth of SMEs in Pakistan plus the property scatter among the years of 2007 and 2010 indicate the positive impact on the policies of government. They also give recommendation to the government to take steps to reduce the problems of SMEs while availing finance from banks.

Ullah, M. S. et al, (2016) This study shows that globally SMEs are considered to be financially stressed. According to all these small and medium enterprises authority most of the SME startup fails within 4 years due to financial constraints and stress. This study shows that the rate of SMEs failure due to financial stress. The primary data has been collected form 433 SMEs that are randomly selected from market committees list. They came to the result that 90% of the entrepreneurs get finance from up to rotated savings and credit Associations (ROSCAs). Respondents considered require of accessibility to finance is a lesser problem than issues like defaulted customers, competition and supply to electricity. High failure rate was not detectable in any age group

Chapter 3

Methods and Methodology

Methodology is the abstract, methodical examination of the techniques useful to a arena of study. This includes the academic study of the collection of procedures and values associated with an information branch. It usually includes academic models, stages and quantitative or qualitative techniques (Irny, S.I. and Rose, A.A. (2005)).

3.1. Research Strategy:

There are three kinds of research strategies in social sciences that are qualitative, quantitative and mixed research strategy. (Creswell, J. W., & Creswell, J. D. (2017)) In our research we were following a qualitative research technique. it is a research in which we collect the non-empirical data. This research refers to meanings, concepts and description of things. It does not include the numeric things.) The studies conducted on SME's both domestically and internationally have focused on quantitative techniques and quantitative methodologies. In this research thesis we are following a qualitative technique because most of the studies I have read are quantitative in nature. As according to my point of you we can't get to know the problems of SMEs and their constraints that they are facing without knowing their problems face to face. Interview is a only method through which we can know the problems of the person completely. In this method we deeply understand the things. But in quantitative technique we can't understand the thing deeply. we only depend on numerics. Most of the studies have found the effect of SME's on employment, poverty alleviation poverty reduction and its contribution to GDP. but all those studies such as (Sharafat Ali et al 2014) (Sharafat Ali 2017) both of them agreed that credit constraints and lower ability of credit facilities to SME's is a main hurdle to the development of SME'S both domestically and internationally. Soo to investigate this problem we cannot only rely upon quantitative techniques. We have SME's Bank and Government nexus and to find

out the real reasons behind the low availability of credit and how this problem can be resolved for this reason this study has to use qualitative methodology.

3.2. Research Design:

Research design for this thesis is a case study in which we do in-depth investigation of a specific problems. A case study can be can be descriptive, explanatory and exploratory. Creswell and Creswell (2017) in his study defines a case study in a way whose main approach is to capture the context based realities of a case under investigation. In this proposed thesis. We had followed a descriptive research design to know the credit constraints that are facing by SMEs in a case of Pakistan.

3.3. Sampling techniques:

There is no hard and fast rule of sampling in qualitative research soo researcher has a liberty for sampling

3.3.1. UDC 1 – SME Executives:

In this unit of data collection, I did a convenient sampling because it was very difficult for us to take a time from them

3.3.2. UDC 2 – SME Banks:

There are many banks that are dealing with SMEs that includes, SME bank, faysal bank, the bank of Punjab, summit bank , Al Baraka Bank and many other soo for this UDC I did random sampling. The reason behind that is, the nature of the UDC's. the bank sections that deal with SME's are easy to reach and they have specialized sections for SME's credit and other financial affairs relating to SME's

3.3.3. UDC 3 – Government:

Head offices of SMEDA are present in different provinces of Pakistan. So For this UDC I did convenience sampling. I had collected data from the head office of SMEDA that is based in Rawalpindi which is very convenient for me to collect data.

3.3.4. UDC 4 – Chamber of Commerce:

For this UDC I did convenient sampling. Because offices of chamber of commerce are based in different areas of Pakistan. For this UDC I had collected data from Chamber of commerce that is based in Islamabad.

3.4. DATA COLLECTION TECHNIQUES:

I had done semi structured interview as my research tools. the interviews were recorded and transcribed and then they were analyzed.

3.5. Research Methods:

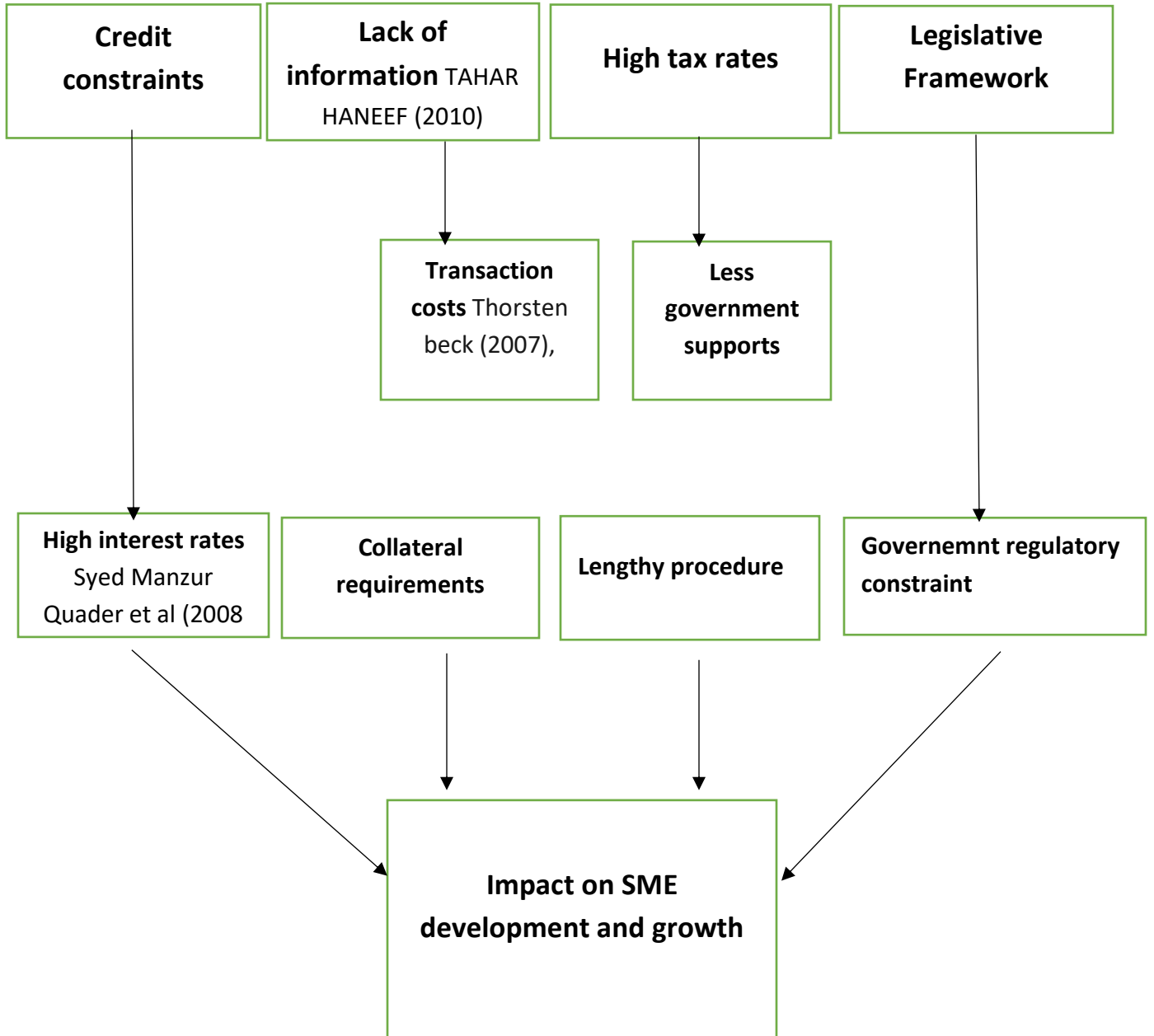
Research methods are the data collection tools which are used in social research. These tools include different forms of data that are generated questionnaires and interviews, naturally occurring observational techniques, focus group discussions, oral history and documentation analysis. In this proposed thesis our research methods were following

3.5.1. Semi structure Interviews:

A semi structured interviews are those in which we do not follow the official list of questions. In these type of interviews, we will ask an open ended questions. In this method we are allowed to have a discussion rather than asking a to the point questions and answer format. Semi-structured or hybrid in-depth interviews which is basically a mix of close ended and open-ended questions was used to gather information from the SME Executives and SME Banks and for other UDCs. The goal was to have an in-depth look into the problems that are facing by SMEs. And to know their views regarding this issue and how this issue can be resolved.

CHAPTER 4

Conceptual Framework:



The study shows that SMEs have a great potential to increase country economic growth and development. But there are many credit constraints are faced by SMEs. As we know that asses to Financing is the backbone of SME and lack of this aspect can lead SMEs to the big problem. Therefore by under mining the importance of credit and finance there is need to find this issue and how it can be resolved because there is a big gap in the study of literature regarding this aspect and we need to highlight this issue and conduct a research on it. Islamabad which is the capital of Pakistan has a great impact on the economy of Pakistan. In this area there is a big problem of credit constraints that are facing by SMEs. Soo this study have tried to explain the current scenario that is running in Islamabad Pakistan.

To understand the difficulties confronted by SMEs, I will borrow the information from TAHAR HANEEF (2010), which says that there area lot of constraints faced by SMEs which have a main influence on SME development. **Non-Availability of Actual Data on the SME sector and Pakistan's Economy:** This causes many challenges for institutions to deal with the small enterprises and medium enterprises market, as there are many economic declarations and the explanations of various SMEs are inexistent. The shortage of information is in itself a main difficulty for SMEs, which adversely effects their performance. **Non-Conducive Regulatory and Legislative Frameworks:** Small and medium-sized companies in Pakistan have to do a lot to get register their enterprises, arrange with tax authorities, follow documentation requirements and so on. This non-conductive supervisory and judicial framework is causing difficulties for SMEs and negatively affecting them. **High Tax rates:** it is also a big issue for the growth and development of SMEs. Government has set high taxation on them; Pakistan's people are unwilling to set up new ventures because much of the benefit is eaten by the government's taxes on them.

Moreover to gain the understanding of how high interest rates and other factors that are the biggest constraints for SMEs are creating problems for their growth and development. I will use the concept of Syed Manzur Quader et al (2008) who did a study on impact of credit constraints on SMEs and shows that how SMEs are playing very vital role in growth and underdevelopment of economy. They shows that there are many problems that are facing

by small and medium enterprises related to raw materials, power, land, marketing, transport, technical facilities, and finance. Their study have found some major factors that are work as impairments to SME growth that include high loaning rate, regulatory constraint of governemnt, lengthy document process, collateral requirement for financing and many more. He said that Sme are having credit constraints due to high interest rates which is the biggest constraint in the growth of SME. they demonstrate the requirements for collateral and small national market size, non availability of skilled technicians non availability of physical production. (Raw materials), Lack of funding and high rate of equipment, Absence of protection measures and vagueness also shows a no support of government to help SMEs globally.

To gain the understanding regarding how financial constraints are facing more by Small and medium enterprises than the large enterprises and what are the main factors that are creating financial problems for SMEs. For that I am borrowing the concept of Thorsten beck (2007), who shows that SMEs are facing more financial constraints than the large enterprises because of the flaws in monetary systems of many emerging countries. Their conceptual framework shows that unsymmetrical information and transaction costs between lender and borrower are the main factors that are explaining the financial constraints that are facing by SMEs in developing countries. They argue strategies and improvements that can lead financial institutions to lend to SMEs and also give comments on the government role in establishment building and also in providing the controlling framework and take policies that are friendly to market such as credit assurance schemes. They also point out the difficulties in government involvement in SMEs financing. They also give comments on role of government in building of institution and in giving the supervisory framework and take policies that are market friendly such as credit guarantee schemes. We also shown that policy plays a major role in changing the institutional atmosphere, establishing supervisory frameworks and promoting productivity. However, worldwide experience shows widespread failure of financial institutions that are kept and managed by government focusing on definite sets of borrowers or lending programs. Government role in interfering by advanced programs, like loan guarantee schemes, is less clear.

So from all of above studies we have found that there are many credit constraints that are face by SMEs in which these are on the top that include, lack of information, high tax rates, legislative framework, high interest rates, high transaction costs, high collateral requirements, lengthy procedure and less government support. These are the major impacts that SMEs have on their growth and development. If all these constraints will be removes this will lead us to the growth of Small and medium enterprises

CHAPTER 5

Data Analysis and discussion:

This chapter provides findings and discussion based on the selected themes mentioned in the previous chapter for the interpretation and information collected from data from interviews. The findings and discussion are based on the analysis of the data under the following major categories with selected sub-themes:

- I. Role of government on the development of SMEs
- II. Role of banks on the development of SMEs
- III. SMEs Executives and credit constraints
- IV. Private equity firms and awareness
- V. Kamyab Jawan Program

5.1. Role of Government on the development of SMEs:

Policy makers selected for the study comprised of stakeholders from Government side including Federal and Provincial authorities in which our first most important stakeholder was Small and Medium Enterprises Development Authority Head Office, Rawalpindi (SMEDA) who work as a policy making and facilitating bodies for SMEs on provincial level respectively. Another important stakeholder; Islamabad Chamber of Commerce and Industry (ICCI) is a contact organization on provincial level for other organizations such as SMEDA and Punjab Small Industries Corporation (PSIC).

The role and observation of these stakeholders in the context of SMEs and their credit constraints are discussed as follows according to the sub-themes.

the definitions of SMEs being followed by the selected organizations. There are two definitions of SMEs being followed by the institutions and organizations in the country, one is the definition proposed by SME Policy 2007 and the other one is proposed by State Bank of Pakistan. SMEDA follows the definition of SME Policy 2007. When asked about the difference of definition of SME Policy and definition proposed by SBP, the respondent

from SMEDA told that; “SMEDA is not bound to follow the definition of SMEs declared by State Bank of Pakistan, we are an independent organization and have the right to follow definition of our own based on the research and international practices. However, in order to avoid confusion among the organizations, we are planning to align our definition of SMEs with the definition given by SBP in our upcoming SME Policy.” (Respondent from SMEDA Head Office Islamabad)

5.1.1. Facilities provided by SMEDA to SMEs:

the facilities provided to SMEs by SMEDA, it was laid out that the Head Office, SMEDA deals with all kinds of facilitation that include Providing business support/ promotion to the SMEs, extending marketing support, Advisory services for government on fiscal and monetary issues relating to SMEs, Conducting seminars, workshops and training programs for SME, Donor assistances for SME development through programs and projects.

It also deals with SME policy making, amending and revising process. However, Regional Business Centers (RBCs) of SMEDA are a ‘One Man Office’ i.e., only one person is leading RBC in the region. There are total twelve RBCs of SMEDA all over the country which includes Abbotabad, Dera Ismail Khan, Lahore, Faisalabad, Gujrat, Multan, Gujranwala, Sialkot, Rawalpindi, Rahim Yar Khan, Dadu and Ghotki.

RBCs provide facilitation only and do not have Research and Development (R&D) unit or policy role, but the rest of the functions are similar as of the Head Office, SMEDA. a) Financial Services On financial front, SMEDA Head Office and RBC do not provide direct financial services or loans to SMEs. However, it has ‘Financial Services under the department of Business & Sector Development Services (B&SDS). The respondent from SMEDA head office Rawalpindi also tells us that financial role of SMEDA is divided in to four sub-categories that are ‘Supportive role, Advisory services, and SME Financing Products and Financial publications’. SMEDA is playing supportive role for SMEs in terms of conducting ‘Financial Analysis’ or pre-feasibility studies in their sector studies which includes historical status of that particular sector in business market, competitive analysis and source of financing in that sector. SMEDA also prepare ‘Financial models’ or business plans for their clients on their request. Respondent from SMEDA Head Office

told that; “We have prepared up to 200 pre-feasibility studies published so far which are also available on our official website. Whenever a client visits SMEDA and asked which business he/she should start, we give them briefing on these pre-feasibility studies for their information.” (Respondent from Islamabad Head Office, SMEDA).

When we asked them about what is your role in recent kamyab jawan program scheme then the respondent tells us that they are also working as a advisory body about the recent Kamyab jawan program scheme. They tells us about how hey can apply for this scheme and which banks are working under this scheme. And which bank wil provide loan after applying to this scheme.

When we asked about SME Financing then the respondent from SMEDA Rawalpindi tell us that For SME financing, SMEDA guides the financial institutions about the demands of SMEs regarding loan facilities. It also updates the information of banking services related to SME financing on its website periodically and make it accessible through one portal on its website named as ‘SME Financing Products Database’ they tell us they also written the book named how to approach bank in 2007 in which SMEs can easily get approach to banks and their procedure of giving loans to them. (Respondent from, SMEDA rawalpindi)

When we asked them about what are their business development services for SMEs we were told that for business development, SMEDA works on a classified agenda. First, a sector is identified, then within that sector, sub- sector is formed and under a sub -category, cluster is formed. For these clusters, SMEDA conducts diagnostic studies (complete profile of that district as well as that sector/ cluster), available for everyone on the website so that the clients and new participants should have complete information of that region/ district before starting a business. SMEDA guides its clients on the spot regarding their queries about business start-up, investment plan, feasibility studies, legal matters, or refers them to other resource persons as well. It also creates Customized Business Plans on subsidized cost for the new entrants. (Respondent from SMEDA head office Rawalpindi) they tells us that they have design Customized Business Plans for the clients for which Rs.10,000-35,000 are charged, but for pre-feasibility studies, nothing is charged but it is a time consuming process. If they approach market for the business development plan, they would face cost of Rs. 60,000 to 80,000 which is not affordable for many of the SMEs. We charge

them because only serious clients will then approach us and they will take their business seriously once they invest some of the amount for business plans. Facilities provided for free are generally taken for granted by SMEs.” (Respondent from the SMEDA head office Rawalpindi)

When we asked them about what are the legal facilities you are providing to SMEs for their business then we were told that For legal facilities, SMEDA provides contracting services for the SMEs in which SMEs are informed about the regulation related to businesses and also provides legal opinions for their issues. Regional Business Coordinators are trained for legal purposes so that they can guide their clients. SMEs have an easy access to legal and commercial contracts in a separate section ‘Regulatory Procedures’ on our official website where clients can get all the information regarding legal matters. There are also help desks for one to one information for the SMEs where they can get information about company formation, registration or other services. Moreover, there is a ‘legal cell’ in which legal experts and lawyers are available in every RBC and Head Office. (respondent from SMEDA Rawalpindi)

When we asked them about that what they think government is facilitating SMEs in a way they should then the respondent told that the government is working on the development of SMEs sector. They are giving different schemes, training programs for SMEs development.

When we asked then about what are the major constraints are facing SMEs then they said that there are number of constraints for SMEs in the market such as unfriendly business environment due to complicated process of registration which may irritate new participants for business startup, lack of financial support because banks provide loans to SMEs on the basis of collateral which many of the SMEs may not be able to provide, lack of skilled labor, lack of complete or adequate knowledge, lack of experience and technological constraints. “There are two major constraints for SMEs that are incomplete information and lack of financing. (Respondent from SMEDA head office Rawalpindi)

5.1.2. Facilities provided by Chamber of Commerce to SMEs:

Since its beginning in 1950, the FPCCI has supported and pronounced the shared opinion, concern and ambition of the personal sector and offered useful recommendation and solid help to the government. in its efforts to push exports, encourage foreign investment and stimulate economic activities within the country. The FPCCI has its fingers on the heart beat of the economy and is a bond between the personal sector and also the Government. The FPCCI is playing lively role in promoting economic activities still as distinguishing issues of trade, industry, services, investments, atmosphere and safeguarding the interest of the personal sector through constant dialogue with the government.

Every city of a country has its own chamber of commerce. Every industrialist, traders and corporate firms are member of these chambers. Company in Islamabad will be a member of Islamabad chamber of commerce or company in Rawalpindi will be a member of Rawalpindi chamber of commerce. There are 58 chamber of commerce offices in Pakistan. We have 4500 total members in Islamabad chamber of commerce. All shop owners, multinational companies, industries are members of chamber of commerce. (respondent from FPCCI Islamabad)

Government is facilitating SMEs through giving loans through banks. These loan are giving according to rules that are given by state bank of Pakistan. Markup is decided by state bank of Pakistan, as bank rate increase markup increase. There are also some microfinance bank that are also giving loans to small and medium enterprise if they eligible in bank criteria of loan. (respondent from Islamabad chamber of commerce Islamabad) The high markup rate is due to the worse economic conditions of a country. There is very less variation between banks because markup is already decided by the state bank of Pakistan.

When we asked about do government is facilitating SMEs then the respondent tells us that Government have made different skill development institutions to facilitate SMEs. Like SMEDA (Respondent from FPCCI Islamabad)

When I asked them about what is your link with Kamyab Jawan Program the respondent tells us that for kamyab jawan program Government have taken some input from their

members of president regarding different sector about what are their demands. (Respondent from FPCCI Islamabad)

Then I asked that what initiative government should take for SMEs then The respondent said take government should take initiative like youth program to give loans to bank on lower interest rates and they should take some steps for women's for their skills development. (Respondent from FPCCI Islamabad)

5.2. Role of banks on the development of SMEs:

The banks play an important role in providing loans to SMEs. They are the only sources for the financial facilities for SMEs. The role of Government led banks and commercial banks differ from each other in terms of facilitation to SMEs. Therefore, the interviews were conducted from both categories in order to get views from both sides. Government-led banks include SME Bank, SME Bank is the government entity which facilitates SMEs only. It was officially established in 2001 when three organizations; Youth Investment Promotion Society (YIPS), Regional Development Finance Corporation (RDFC) and Small Business Finance Corporation (SBFC) were merged in to one entity as 'SME Bank'. The mission of SME Bank includes financial and technical assistance to SMEs, promotes SME sector for value addition and exports and to provide entrepreneurship and employment opportunities

The commercial banks including summit bank and Bank Alfalah were also involved in this study based on convenience sampling both government owned and privately owned banks this perspective will give us information about how they are helping SMEs

All the selected banks follow SBP's definition of SMEs that is SE has up to 50 employees and annual sales turnover up to 150 million whereas, ME has 51 -250 number of employees for manufacturing and services and 51 - 100 number of employees for trading services and annual sales turnover of 800 million. "Like all other banks, we also follow definition of SMEs by SBP because it is the regulatory authority whereas SECP is the registering authority for SMEs." (Respondent from SME Bank, Head Office, Islamabad)

5.2.1. SME bank and SMEs:

There are only 13 branches of SME Bank in the country out of which three branches are in Karachi, three in Lahore, one in Sialkot, one in Quetta, one in Faisalabad, one in Rawalpindi, one in Peshawar, one in Islamabad and one in Gujranwala. The SME Bank offers financial as well as technical services to SMEs. The main difference between lending services of commercial banks and SME Bank is the ease of SME lending that SME Bank offers to them because SME Bank gives loans on cash base lending. Commercial banks do not lend easily to the SMEs without financial guarantee or collateral. The main lending products and services for SMEs include loans based on personal references. SME Bank does cash based lending instead of an asset based lending. SME Bank provides loans of Rs. 50,000 - 200 million. “We do not take fresh clients for loans, actually we cannot take them because we already have very few clients and giving loans to fresh clients is risky for our bank. Credibility of the client is important here.” (Respondent from SME Bank, Head Office, Islamabad)

When we asked them about their procedure of giving loans to SMEs then we were told that we give loan to SME whose business must be running to a year. And we take their property as a security which is the rule of bank to give loans.

When we asked them about what are the constraints faced by SMEs to Approach SME banks then the respondent said that are the lack of awareness about SME Banks and psychological barrier because SMEs avoid banking relations due to complicated documentation procedures.

When we asked them about what interest rate do you charge to SMEs for getting loan then the respondent tells us that we charge 7.5 % markup for term finance and 8.5 % for running finance and the markup charge by state bank of Pakistan is 21 % which is very high. The respondent said that the high markup rates is a very major problem for SMEs. Government should reduce this markup rate for SME development and for the growth of country. Respondent said that only SMEs have an ability to increase the economic growth of a country. (respondent from SME Bank Islamabad)

5.2.2. Commercial banks and SMEs:

Bank Alfalah has the highest ratio of financing SMEs among all other banks. Deposit ratio of SMEs is beyond 66%. There are credit hubs for SMEs in all over the country and six such credit hubs are located in Multan only. In Multan, SMEs from sectors of trading, fertilizers, cotton ginning, textile and weaving are among the clients. For loans, clean financing to SMEs is provided that is loan is given to SME without collateral or security. However, financial strength is considered, previous relation with other banks is also considered. The bank gives businessmen loans and even services like cars, passenger vehicle, trading services for business support and chain financing. The sector specific focus of bank is more towards women financing in Multan. However, manufacturing sector is preferred over other sectors for services due to their financial guarantee.

Habib Bank Limited (HBL) has separate credit hubs for SMEs and in Multan, there are two credit hubs. The services for SMEs include provision of loans related to export oriented businesses, normal working loans, conventional financing, small business financing, and HBL Business finance. Loans for SMEs are given as per rules by SBP that is up to 25 million loan for SE and up to 200 million for ME. HBL have a sector-specific focus in dealing with SMEs preferring mostly SMEs involved in trading, shoe-making and leather businesses in Multan.

5.3. SME Executives and credit constraints:

SME Executive for the study were selected randomly. In which we have interview 3 to 4 small and medium enterprises executives. We have interview them about what are their credit constraints and did they take loans from banks. Do government is facilitating them or not ?

The respondent from travel agency based in blue Area Islamabad. He said that they have started this business in 2016. When researchers asked about the employees they have then we were told that They have 5 to 6 workers. They have around 20 to 30 employers who are working in their enterprise. When we asked about their business Revenue then the respondent said Their business revenue is more than a crore. When we asked about did they even take loans from bank then the respondent tells us that They have not ever take

loan from bank. They start their business by taking loan from their friends and family. They said that they don't believe in bank system. Their interest rates are very high. When asked about did they apply in recent kamyab jawan program scheme then the respondent said that They have not apply on recent kamyab jawan program scheme. They said that government is not facilitating Small and medium enterprise. If they are giving loans, then their interest rates are very high and their procedure of giving loans is very lengthy. Respondent also give recommendation to government that they should work on the awareness of loans and should not take a high interest rates.

The respondent from real estate and construction a company based in Islamabad. respondent said that they have started their business 20 years before. When research asked them about total employees they have then the respondent tells that they have 5 to 10 employees that are working now but when they get a project their employees increases more than 50 employees. . When we asked about did they even take loans from bank then the respondent tells us that They have not ever take loan from bank. They start their business by taking loan from their friends and family (informal loan). They said that bank is taking very high interest rates. They don't care about the people. They just care about their own benefits and their procedures. When researcher asked about did they apply in recent kamyab jawan program scheme then the respondent said that this kamyab jawan program scheme is rubbish. They said government will not give loans. Did anyone get loan from bank yet? no one then how we can believe on this. This is only the government method to play with the people. They have never facilitated to the SMEs. Respondent said that all fault is of government who is not taking paying much attention to their institutions. The corruption is on peak. FBR and CDA are on the peak of corruption. Tax rates are not affordable. If we pay that much high taxes, then what we will earn. Government should do some serious action for all these problems. She should facilitate to SMEs because SMEs have a power to increase the economic growth and development of a country.

The respondent from hotel based in Islamabad. respondent said that they have started their business in 2013. When researcher asked them about total employees they have then the respondent tells that they have 30 to 35 employees. When we asked about did they even take loans from bank then the respondent tells us that They have not ever take loan from

bank. They start their business by taking loan from their friends and family (informal loan). They have never applied in any financing scheme. And said that they have never take loan from banks because bank are taking very high interest rates. When researcher asked about did they apply in recent kamyab jawan program scheme then the respondent said that this kamyab jawan program scheme is not more than a drama that is made by government. Respondent said that they have not applied in this kamyab jawan scheme because they know that they will not provide loans. The Respondent said Tax rates are very high. They said they give 17% tax rates for hotels Which is very high and not affordable. If we pay that much high taxes, then what we will earn. Government should do some serious action for all these problems. She should restrict bank to reduce interest rates for providing loans and should reduce tax rates. Because these are the main problems for SMEs that are a big hurdle in their growth and development.

Then from all of the interviews about we have found that most of the SMEs of Islamabad showed no satisfaction with the facilities provided by the Government organizations including SMEDA, FPPCI, FBR and others. they have complained that government is not providing facilities for SMEs for the expansion of theory businesses. They also complained of lack of incentives in terms of tax exemptions specifically for SMEs. In order to avoid taxes, these SMEs avoid to get registered with the SECP they also have complained that banks are providing loans to SMEs but on very high interest rates. they said that their procedure of documentation is also very lengthy. Some of the SME Executives said that government should provide loans to SMEs on a free interest rates. Most of the SMEs are not well-educated, so there are several misperceptions that they have regarding government organizations like SMEDA and SME Bank

Most of the SMEs Executive were not aware of the SME Policy due to lack of education and access to information. Some of them were somewhat aware of the SME Policy but disappointed for the failure of its implementation. In terms of financial assistance, the SMEs are not satisfied with the services because commercial banks ask for collateral for loans and SEs do not have such guarantee.

Most of the SMEs were also not aware about the recent scheme for SMEs. Like Kamyab Jawan Program. Some of them said them if were aware they not apply for loan because

they don't believe in government. because their interest rates will be increase with the time. And the documentation process is also very lengthy. They said that banks ask for collateral for loans and SMEs do not have such guarantee.

SME executive also give recommendations to the government that government that they should work on the awareness of loans and should not take a high interest rates. they should reduce their tax rates because these are the major constraints that are facing SMEs.

5.4. Private equity firms:

Private equity is an alternative form of investment and is made up of capital not listed on a public exchange. Private equity consists of funds and creditors actively investing in private enterprises or participating in public sector buyouts, resulting in the exclusion of public equity. Institutional and retail investors provide private equity funding, and this can be used to fund new technologies, buy, increase working capital, and improve and enhance a balance sheet.

Private equity has always played a pivotal role in the development of small and medium-sized enterprises (SMEs) globally by providing not only capital but also operational expertise, managerial bandwidth, leadership and vision.

A number of local and international players showed keen interest in the private equity space in the mid-2000s, when many of the local brokerage houses and investment banks such as Arif Habib, AKD, BMA and JS looked at setting up private equity businesses, however, most of the local investment houses dropped the idea either due to the unfavorable regulatory regime or later due to the global financial crisis in 2007-08 JS was the only local player to set up a fund at the time, however, the fund was registered offshore due to the low tax, superior regulatory regime and the double tax treaty with Pakistan.

Currently, there are three domestically registered private equity funds which include Ijarah Capital, Lakson Investments Private Equity (similar to Tribune, a Lakson Group company) and PNO Capital.

5.4.1. Private equity firms in Pakistan

There are three private equity firms in Pakistan.

I. Ijara group:

It is a Pakistan based private equity firm that helps people to grow their business. They help their co companied in their difficult situations. Their criteria is given below.

1. They prefer to give opportunities to health care, education, technology, real state, FMGC, hospitality and also to the other sectors.
2. they prefer the companies based in Pakistan.
3. they invest on the company having EBITDA (earnings before investment taxes, depreciation amortization) of approximate 350 million PKR and have been operating over 5 years.
4. They give investment of 500 million PKR. And it vary from deal to deal.

II. PNO capital:

- PNO Capital is a specialist investment and advisory company. Working with a wide range of assets, from a diverse range of industries, they take a diverse approach to creating value from each investment for their investors. Their work varies from growth investments, SME investments, joint ventures and even the creation of new businesses.
- They seeks to invest in great companies and increase the value of their businesses, their partnership with management teams have been built upon teamwork, shared values and truth
- They only give money to the enterprenurs who have a great business plan and want to take his business to the best level. It protect the buisnesses financially who have a potential to grow.

III. Lakson private equity fund:

- The Lakson Private Equity Fund (' LPEF ') will provide growth capital for rapidly developing companies with a discernible competitive advantage, good management and reputable stakeholders seeking to grow their business.
- They invest in prominent marginal stakeholders and monitor stakeholders in private native businesses, as well as in visibly registered about-turns.
- Investments may be made by direct cash equity or a structured equity instrument, e.g. preferred equity, convertible etc. 5 to 10 portfolio investments with initial investment sizes ranging from 5% (minimum) to 20% (maximum NAV); 5-Year Investment cycle, 2-year Distribution period with a 25 percent goal IRR over the life of the Fund.
- The target fund size amounts to PKR 3 billion. And the minimum size of the funds is PKR 50 million

I did not take a detailed interview about private equity funds to small and medium scale enterprises because when I interviewed about private equity funds to the SME executive then I came to the result that they had no information about these private equity funds that how they are facilitating to Small and Medium scale enterprises. So for that there should be a awareness about these funds that how SMEs can avail these funds and what are their requirement for giving funds and how they are helping SMEs for their growth and development.

5.5. Kamyab jawan program:

This program is launched by prime minister Imran khan which is offering an opportunity to the Pakistani youth related to skill training, education, entrepreneurship and civic engagement. This program is giving loans worth rupees 100 billion to youth during five years. Under this kamyab jawan program loans will be provided to the youth for the SME sector development. They also give opportunity to the women entrepreneur to get loans to run their small businesses. They are giving 25% loans to the women entrepreneur. They are expecting 52% of the Pakistani population will be directly get benefit through this scheme. Applicant from the age between 21 to 25 can apply for the loans. Loans from

10,000 to 100,00 will be without any markup distributed on the priority basis. And the loans less than or equal to 500,000 will be given with an 6% interest rate while the loans more than 500,000 will be given with 8% interest rate. These loans will be given through three major banks, national bank of Pakistan, bank of Punjab, and bank of Khyber.

Eligibility criteria for kamyab jawan program scheme is For this loan only Pakistani citizen can apply. An applicant minimum age under this scheme of kamyab jawan is 21 years, and 45 years is the maximum age limit, minimum educational qualification is not required in general while for business, all genders have an equal opportunity to apply in this scheme but 25 % share of loan is kept only for females who want to do businesses it compulsorily need certain qualification, certifications, diplomas, authorizations or licenses, the same must be held by the applicant., private job employers can also apply for this scheme. Person can apply for not more than one loan, individually more than one person of same family can also apply for this loan. Anyone who is himself applying for the loan cannot give a guarantee to the other person. Person any family member can give guarantee for his loan and person only be given guarantee for only one loan not more than that.

For the loans less than 500,000 no collateral will be required but for the loans more than 500,000 collaterals will be required. And the collateral for these loans will be rests with the participating banks. However, they must include the following: Mortgage of Applicant Assets (Residential / Commercial / Agricultural etc.) Mortgage of Third Party Residential / Commercial Property etc.) Vehicle acquisition (Joint Registration) Connection to marketable securities / deposit certificates / National Savings Certificates etc.) Mortgage of existing and fixed assets like stocks and receivables, Pledge of gold ornaments, Registered charge on business assets in case of joint stock companies, Third party guarantees

I take a detailed interview about kamyab jawan program to small and medium scale enterprises, SME bank and SMEDA. As I mentioned about respondent from SMEDA said that they are working as a advisory body about the recent Kamyab jawan program scheme. They tells us about how people can apply for this scheme and which banks are working under this scheme. And which bank will provide loan after applying to this scheme. And when I asked to SME Executives about this scheme they were not much aware about this

scheme. They said that if they were aware they will not apply for this loan because they don't believe in government given scheme. Respondent said they know that all this scheme is a drama which is made by government to take attention of people. They will do nothing.

CHAPTER 6

Conclusion:

The study concluded that SMEs are very important part of the economy. They have a great impact of Poverty alleviation, employment generation and economic growth. The study reveals that SMEs are facing major credit constraints in terms of financing, high tax rates, legislative framework, high interest rates, high transaction costs, high collateral requirements, lengthy procedure and less government support. So to investigate the impact of credit constraints on SMEs we have interviews different SME executives to know the constraints faced by them and the facilities government is providing to them, SMEDA, Chamber of Commerce FPPCI to have knowledge about the facilities they are providing to SMEs, banks to know their facilities provided by them to SMEs.

Then the results show that government is not providing facilities for SMEs for the expansion of businesses. There are very less incentives have been given by government in terms of tax exemptions specifically for SMEs. Government has put a high tax rates on them; because of these taxes, people of Pakistan are not willing in making new projects because main part of the profit is always taken by the taxes that were imposed by the government on them. that's why In order to avoid taxes, these SMEs avoid to get registered with the SECP. banks are providing loans to SMEs but on very high interest rates Because of capital needs if people decide to take loan from a banks; they have to pay high markups rates to banks. That is why most SMEs do not apply for the loan because of their incapacity to pay such high markups in the current declining conditions in the country. Their procedure of documentation is also very lengthy. Some of the SME Executives said that government should provide loans to SMEs on a free interest rates. Most of the SMEs are not well-educated, so there are several misperceptions that they have regarding government organizations like SMEDA and SME Bank. guarantee. Most of the SMEs were also not aware about the recent scheme for SMEs. Like Kamyab Jawan Program. if they were aware they have not applied for loan because they don't believe in government. because their interest rates will be increase with the time. And the documentation process is also very

lengthy. They said that banks ask for collateral for loans and SMEs do not have such guarantee.

The policy recommendations are suggested on the basis of the findings that serious steps in terms of policy measures must be taken regarding inclusion of SMEs and strengthening their position in general for their growth and development. These are SMEs that can improve economic growth of a country. Government should take measures to reduce their tax rates. And should give loans to the low interest rates, because these are the major constraints that are facing SMEs. Bank documentation procedure should not be lengthy no one have a time to read their lengthy papers. Transaction costs should be low. Government should support to SMEs in building of institution and in providing the regulatory framework and take market friendly activist policies such as credit guarantee schemes.

Chapter: 7

Policy Implications and limitations:

7.1. Policy implications:

In order to strengthen the position of SMEs in all over the country for their growth and development, following are the proposed key policy implications;

7.1.1. Reduction of high Interest rates and high collateral:

In order to facilitate Small and Medium scale enterprises, government should reduce their interest rates. Because banks are providing loans to SMEs but on very high interest rates with high collateral. Because of capital needs if people decide to take loan from a banks; they have to pay high markups rates to banks. That is why most SMEs do not apply for the loan because of their incapacity to pay such high markups in the current declining conditions in the country. Government should make some policy implications to reduce these high interest rates to help SMEs for their growth and development. Because if the interest rates will be low and collateral requirement will be less than SMEs will take loans and will improve their enterprises this will result in their growth and development. If there is a growth of SMEs in a country this will increase the economic growth of a whole country.

7.1.2. Reduction of tax rates:

In order to facilitate Small and Medium scale enterprises, government should reduce their tax rates. Because of these high taxes, people of Pakistan are not willing in making new projects because main part of the profit is always taken by the taxes that were imposed by the government on them. that's why In order to avoid taxes, these SMEs avoid to get registered with the SECP. Government should make some serious policy implication to reduce tax rates for the growth of Small and Medium- Scale Enterprises.

7.1.3. Awareness on private Equity firms:

In order to facilitate Small and Medium scale enterprises, there should be a awareness regarding private equity funds. Private equity funds are playing a key role in the development of small and medium-sized enterprises (SMEs) globally by providing not

only capital but also operational expertise, managerial bandwidth, leadership and vision. These are the firms that help people to grow their business. They help enterprises in their difficult situations. So there must be a awareness platform where people know about these firms and the facilities they are providing to SMEs.

7.1.4. bank procedure of giving loans should be simple:

It was evident from the findings that all of the SMEs were facing problems of lengthy procedure. If they are applying for loans from the bank. They become afraid by seeing their procedure and their demands. They don't have much time of reading all the policies of bank that is written on the paper. Due to that fear they don't apply for the loans. So the bank procedure of giving loan should be simple

7.1.5. Awareness for facilities provides by bank to SMEs:

In order to facilitate Small and Medium scale enterprises, there should be a awareness regarding the facilities given by bank to SMEs. Most of the SMEs do not know about banks who are giving loans to SMEs and their facilities they are giving to SMEs. Steps should be taken to give awareness regarding banks and their facilities they are providing to SMEs

7.1.6. Non-Conducive Regulatory and Legislative Frameworks:

Small and medium-sized companies in Pakistan have to do a lot to get register their enterprises, arrange with tax authorities, follow documentation requirements and so on. This non-conducive supervisory and judicial framework is causing difficulties for SMEs and negatively affecting them.

7.1.7. Facilitation desk should be provided to SMEs:

To start a new business is becoming a more difficult process in Pakistan due to their complex registration process, getting permits, access to financial assistance and dealing with taxation process. In order to improve the ease of doing business, facilitation desk for the SMEs must be introduced in the light of revised SME Policy and the authority of this facilitation desk should be provided to SMEDA and SME Bank. Because these are the only organizations that are established by government to facilitate SMEs. In that way SMEs can

easily get all the facilities including registration, financial, legal business development services.

7.2. Limitations of the Study:

The study was based on primary data collection from the selected stakeholders and SMEs of Islamabad. Therefore, there are number of limitations regarding data availability. Following are the limitations faced during data collection and compilation of this study;

- I. The availability of SMEs for interviews was difficult because of time shortage or they hesitated to share details of their business, they were not willing to respond. Hence, only 3 to 4 SMEs were interviewed.
- II. The organizations like SMEDA, did not have complete list of SMEs, even if they had a list, the data was kept confidential.
- III. Due to time shortage data were only collected from Islamabad.

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