

# The Evolution of Financial Innovation and Challenges for Small and Medium Enterprises: A Case Study from South Asian Economies

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## Abstract

Deprived of reluctance, SME sector has developed the considerable thump of constant, rapid and dynamic growth of South Asian Economies. Furthermore, serve as breeding ground for young entrepreneurs and sheltered the unemployed laborer force by providing them working opportunities. Beside all these facts, due to globalization the Small and medium-sized enterprises fronting incredible variation and concentrated competition. Thus, this research study primarily consists of analyzing the sources of financ available for Small and medium firms along with financing challenges confronted by small business traders with the objectives to exploit the innovative ways to improve financing streams for Small and medium enterprises in South Asian Countries. For accomplish this purpose, four major South Asian Countries, India, Pakistan, Bangladesh and Sri Lanka have been selected to analysis the growth of SMEs sector with the viewpoint of financial constrained and innovative financial provisions. This Study comprises of qualitative examination of secondary data gather from central banks of the respective countries along with SMEs development authorities in the country. This study suggest that the innovative entrepreneurs should be encouraged by government and financial institutions through the innovative technological education and financial literacy training programs. Moreover, the collaboration between Academia and researchers with innovative entrepreneurs are essential for growth of SMEs sector in the country because they provide referral and laboratory services to SMEs to promote innovation. Beside this, the need of establish business incubation centers are prerequisite in academia. The universities should have set up business centers with collaboration of SMEDA and Financial institutions to promote young entrepreneurs and enhance their business skills.

**Keywords:** Financial Innovation, Entrepreneurs, Small and Medium-Sized Enterprises.

## 1. INTRODUCTION

Small and medium enterprises (SMEs) is considered as contributing pillar of any economy. The evolution in the SME sector play prudent role to drive economic cycle efficiently. There are enormous SMEs firm operating around the world. These firms assist and provide upbringing ground for entrepreneur to curtail unemployment in the economy which ultimately encourage market growth. The evolution in SMEs sector have constructive influence on economic development in developed as well as emerging economies, while it makes available employment, increase in output, curtail poverty level and promote innovation and inventions to provide smooth ground for small business ventures. The study of (Eniola, 2014) argued that SME sector has been obligated extraordinary potential to sustain economic development in the economy.

The financing need is prerequisite to the growth of the any firm. Although there are number of ways firms can finance their business operations, but their financing decision would according to their preference and nature of business which likely to be differ from business to business. Even some countries SMEs sector volume is high in contrast with large firms. Whereas, SMEs sector has also ability to provide employment opportunities by creating new jobs and encourage young entrepreneurs to make investment and showcase their products in the local as well as foreign markets by acquiring innovative and spirited technologies in the country. Regardless of contributing facts, SMEs sector face numerous obstacles from their inception. Most of them are due to government policies and guidelines that extremely hinder this sector. But SMEs have also inherent barriers due to their small size.

Small and medium enterprises consider as the prerequisite of the south Asian countries because they have the capacity to engender opportunities if economic slam will be occurred in these economies. The Studies of (Fischer, 2003), (Subrahmanya., 2005) and (Mintoo, 2004) argued that the economic development of south Asian emerging economies exclusively relies on SME sector. Consequently, the government of South Asian emerging economies confidently patronage and make available a secure environment for small firms. Small and Medium Enterprises perform a significant role especially in developing economies. In Emerging Economies, the SMEs sector account for 60% of total employment and approximately 40% of GDP in emerging economies around the world.

According to World Bank financials, to grip the global growing workforce in Asia and Africa, around 60 billion jobs will be required in the next 15 years (World Bank Financial Sector Brief, 2017). Although most of the recognized jobs are created by SMEs in emerging economies but still difficulty to access fund is a foremost curb for SMEs. Hence, the growth of SMEs is stagnant and deteriorate. In Asian Economies, the SME sector mark a momentous contribution by adding devastating production volume as it has comprised of approximately 98% or even more in most of Asian countries. Most of the SMEs in this region promote domestic market by providing raw material for local market but some of them also produce goods for export market. These firms also facilitate regional as well as global value chain for large producers at domestic as well as global market (Pretorius, 2004). The Small and Medium Enterprises in Pakistan is nascent as evidence by other emerging economies in the world. Currently in Pakistan, The SME sector account for 99% business enterprises and create 35% share in value addition (Gélinas, 1998).

This Study have consisted of six sections. In section I, this study has given introduction of this research study along with its objective and significance. Section 2, explain background of this paper with detail background of SME criteria, its significance on economic growth of the economy and analysis of South Asian Economies in detail. Section 3, describe the sources of finance available for SMEs sector along with number of SMEs operating, commercial banks financing position to SMEs sector and position of SMEs defaults loan in South Asian Countries i.e. Pakistan, India, Srilanka and Bangladesh respectively. Section 4, has been describe the financial innovations to SMEs sector. This section is related to how many innovative financial options a firm or government must adopt to promote SMEs in the country. Section 5 highlight the four major challenges faced by SMEs in any country. In the last, Section 6 conclude this study.

### **1.1. Research Objective:**

The core objective for this paper is to highlight the sources of financ available for Small and medium firms along with financing challenges confronted by small business traders with the objectives to exploit the innovative ways to improve financing streams for Small and medium enterprises in South Asian Countries. For accomplish this purpose, four major South Asian Countries, India, Pakistan, Bangladesh and Sri lanka have been selected to analysis the growth of SMEs sector with the viewpoint of financial constrained and innovative financial provisions.

### **1.2. Significance of this Study:**

It is observed that SMEs sector is backbone for the countries economies. To finance and necessity to provide a regulatory environment is prerequist that will support it for the growth and advancement of this sector prospectively. Similarly, it is an essential strategy that would assist and provide paltform for entrepreneurs to remain much motivated towards promoting thier line of work. Moreover, it will assure an individual to become a successful entrepreneur and make successful his innovative idea.

## **2. BACKGROUND OF STUDY**

### **2.1. Small and Medium Enterprises:**

The SMEs has been considered as one of business segment in the domestic market. This business segments term different names in different countries. In United State Market, any firm that is originated as a small-office or Home-office to a large firm can be called SMEs. However, European Union specified SMEs criteria in four categories; Firstly, a firm which is employed 50 to 250 workers.

Secondly, A firm annual turnover should not exceed between Euro 7 to 40 million. Third, A firm total assets should not exceed Euro 27 million and fourth, a firm hold not more than 25% ownership of the large corporation (Canadian Business council, 2017) .

Furthermore, The International Chamber of Commerce (ICC) clarified SMEs, A firm having 100 – 2000 employees can be considered as Small and Medium Enterprises. On the contrary, When the SMEs based on business annual turnover and total assets rather than number of employees, it is hard to equate SMEs criteria among different economies. Although there is no formal recognized definition for SMEs in South Asian economies but due to similar macro environmental factors like political, economic, socio-cultural and norms and Technological advancement, they almost on the same track to define SMEs in this region (SAARC Chamber of Commerce and Industry, 2006).

**Table I: Conceptual Details of Micro, Small and Medium Enterprises**

| Indicator / Country | Micro Enterprises  |                | Small Enterprises    |   | Medium Enterprises   |                                  |
|---------------------|--|----------------|----------------------|---|----------------------|----------------------------------|
|                     | Employment   | Total Assets   | Employment           | Total Assets                              | Employment           | Total Assets                     |
| Afghanistan         | -  | -              | -                    | -   | -                    | -                                |
| Bangladesh          | Industry household-based family labour   |                | Workers in firms     | Investment of less than Takka 100 million | 50-99 workers        | Between Takka 100 to 300 million |
| Bhutan              | Investment of 100 million is categorized as micro or cottage, small and medium enterprises based on invested capital                       |                |                      |   |                      |                                  |
|                     | -  | -              | Up to 10 million     | -   | -                    | Between Rs 10-1000 million       |
| India               | The hire or purchase of plant and machinery does not exceed Rs 10 million.   |                |                      |   |                      |                                  |
| Maldives            | -  | -              | -                    | -   | -                    | -                                |
| Nepal               | -  | Upto Rs 200000 | -                    | Upto Rs 30 million                        | -                    | Between Rs 30 to 100 million     |
| Pakistan            | SME means an entity which employs less than 250 persons and total assets of Rs 50 million and with manufacturing concern of Rs 300 million |                |                      |   |                      |                                  |
|                     | -  | -              | 10-35 employees      | Assets upto Rs 20 million                 | 36-99 employees      | Between Rs 20 to 40 million      |
| Sri Lanka           | Up to 10 employees   | -              | Upto 10-49 employees | -   | Upto 50-99 employees | -                                |

Source: Conceptual details of Micro, Small and Medium Enterprises, World Bank, 2004

## 2.2. Significance of SMEs in the Economy Growth:

In developing economies, the Small and Medium enterprises endorse growth of economic industrialization. Because, by investing low amount of investment and time, an entrepreneur can start its business operations through skilled workforce. Most of the time the resources employed by entrepreneurs are unutilized in the economy. Hence, utilization of idle resources in an effective way can lead economic growth at front. Although SMEs perform a dynamic role for attaining economic development in the country, but they also relieve from the burden of poverty level especially in the developing and emerging economies. The Study of (Hussain, 2010) and (Wang, 2010) argued that the development in the SMEs sector in the emerging economies is prerequisite in today's world because they not only deliver abundant labor but also facilitate young entrepreneurs to flourish their business ideas.

Mostly the local SMEs use raw material which is locally produced. They are contributed towards the betterment of the society by introducing many innovative ideas and technological advancement to fill the gap in the domestic market. The expansion of these industries ultimately valuable to the developing nations as they would positively contribute and enlightening their financial and social welfare.

The SMEs contributions in the economic development of the South Asian economies cannot be denied. This sector has potential to create employment opportunities and have leading source of innovative ideas to provide gear of the economic engine of the country. The SMEs are measured comparatively labor intensive and their employment creation feature help to reduce poverty level and facilitate them towards equitable distribution of resources. These firms are significantly important source of employment for youth and specially to encourage Women Entrepreneurship and consequently, contributes towards sustainable economic growth.

The South Asian researchers (Eniola, 2014; Fischer, 2003), (Mintoo, 2004), (Subrahmanya., 2005) revealed that the SMEs sector in India, Pakistan, Nepal and Bangladesh are contributing most of the industrial output in the country. And the respective governments are encouraging and patronage this sector of the economy. Regardless of absence of clear definition of SMEs, the contribution of this sector in GDP is enormously high in South Asian Region. Subsequently, hustle struggle is required to overcome these challenges by encouraging investment in education, health and commerce to promote industrial sector in the country.

According to the Pakistan Economic Survey 2015-2016, The SME sector account for 99% business enterprises and create 35% share in value addition currently in Pakistan (Pakistan Economic Survey, 2015-2016). The Small and Medium Enterprises in Pakistan is promising as evidence by other emerging economies in the world.

## 2.3. Analysis of South Asian Economies:

The South Asia is positioned in the south of the continent Asia. South Asia encompasses of eight Countries;

Pakistan, India, Srilanka, Bangladesh, Bhutan, Nepal, Maldives and Afghanistan. The World Bank statistics revealed that almost 1/5<sup>th</sup> of the world population occupant in this region. After Africa, this region is found 2<sup>nd</sup> poorest region in the world. South Asian nations since their freedom are facing many challenges such as illiteracy, scarce resource, unemployment and low per capita income. To accomplish these objective between south Asian nations, the Regional cooperation body named Association for Regional Cooperation (SAARC) was established in 1985 (Desh, 1996).

### **3.0. SOURCES OF FINANCING TO SMEs SECTOR:**

Finance is basic determinant on which all factors of business operations rely. For SMEs, the Credit/Loan assist as major source of funds that can be employed to attain the business objective of the enterprise (Eisenhardt, 2000). This Study explained financing according to its sources available in the country.

Internal financing is the first preference of the financing source to generate fund for the business operations. In internal financing, a firm can take fund from their retained earnings or contingencies saving. With regards to SMEs financing, the studies of (Gélinas, 1998) and (Pretorius, 2004) found that there are two foremost sources of financing in SMEs sector, 1. internal financing and 2. external financing. Business fund can either be generated through bank financing, investors and crowdfunding. The Study of (Fischer, 2003) argued that although external source of finance is essential for rapid growth of the enterprise but most of the SMEs acquire fund from their existing internal sources of financing and therefore, pay cost of their choice. There are several debts financing sources available for businessmen. Informal source consists of family, friends, partners and directors etc. Recognized formal source of financing to SMEs are Financial institutions like Commercial banks, DFIs and Micro finance banks etc. that are the major fund provider to the SMEs sector in the economy. The Financial institutions mobilize their deposits as a loan to the young entrepreneurs or businessmen to attain productive use of their money. The above-mentioned literature revealed that borrowing through commercial banks can be significant component for start-up and efficient operation of any business venture. The Size and nature of venture does not matter because, the financial need is the identical with availability of all factors of production. Bank's lending to SMEs sector can positively impact firm productivity by increasing firm overall performance that push the economic cycle towards recovery phase.

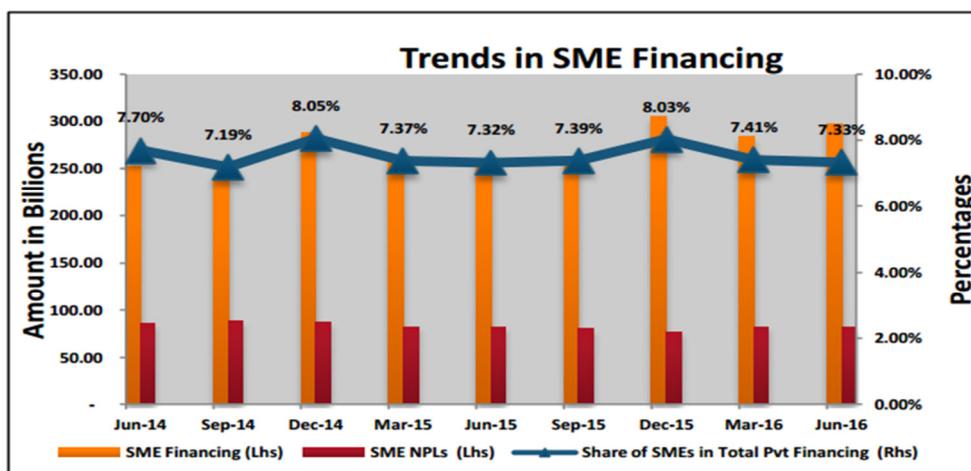
According to the study of (Keasey, 1994) observed that the Small firms face difficulty of raising sufficient capital to finance their business operations and looking forward short-term finance at high cost rather than long term loan from Commercial banks.

### **3.1. SMEs Financing Situation in South Asian Economies:**

#### **3.1.1. Pakistan:**

The previous literature along with above mentioned literature observed that SMEs are a principal contributor of the sustainable economic growth and responsible to reduced poverty level in the country. Although there is difference in the contribution of the SMEs sector in numerous economies, but their significance cannot be denied by any of them. The economy of Pakistan constitutes almost 90% of all economic institutions. The SME sector in Pakistan significantly contribute Gross Domestic Product and a considerable source of export earnings (Review & SBP, 2007). This sector persistent growth remarkably gears up economic engine towards sustainable economic development. According to the International Financial Corporation 2012, almost 3.2 million business enterprises operating in Pakistan and around 3 million of them are Small and medium Enterprises. That contribute 30% to countries' GDP and 25% countries' earning depends on SMEs sector. Furthermore, this sector employing around 70% labor force in the Country (IFC, 2012).

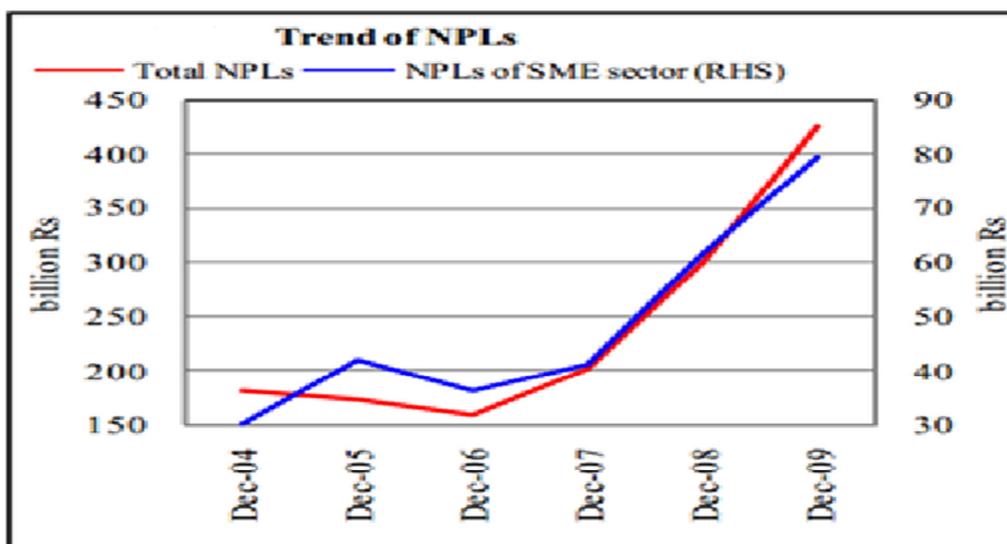
While all stakeholders of SMEs sector believe that deficiency to access finance is a key obstacle for growth of this sector. In Pakistan, this sector face challenge as shown by very small share of SMEs loan in total loan portfolio of banking sector in Pakistan. According to the SBP, the SMEs sector account for 11.8% of overall loan portfolio whereas, this sector loan consists of 7% of GDP (SBP, 2010).



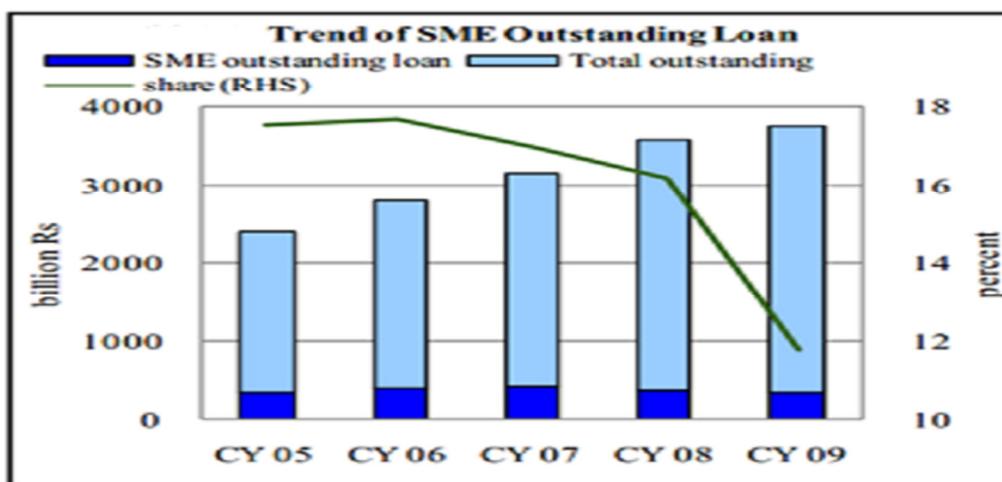
**Figure I: Trend of SME Financing in Pakistan**

During the 2008 economic crunch, the SMEs sector financing declined as compare to total outstanding loans. The above-mentioned Figure indicated that the trend of SMEs financing situation in the country during 2005 – 2009. In 2005, the trend was slightly increased but it was suddenly drop and persistently continue declined trend till 2009.

During this period, the rising trend of Nonperforming loans was diffculted the financing decisions. According to the SBP quarterly bulletin 2012, The NPLs of SMEs sector was bounced from Rs.30 billion in 2004 to Rs. 79 billion in 2009. However, the financial institutions were reluctant to finance SMEs sector



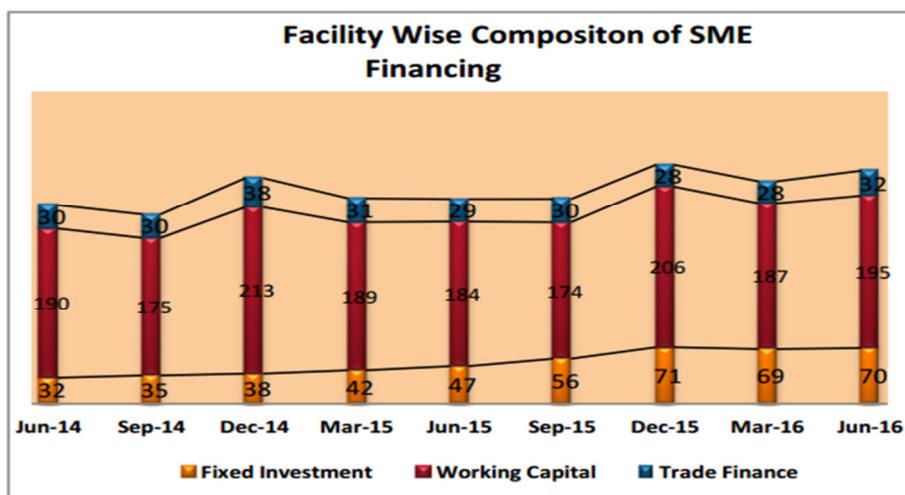
At the same period, around 70% of the total SMEs financing facility consist of Working capital (Figure). It is evidence by previous literature that startup venture face difficulty to access capital to start their business operations as compare to established firms. Besides this working capital financing is an effective financing option for startup venture and financing SMEs working capital depicted towards startup venture to support their growth and development.



**Figure III: Trend of SME Outstanding Loan**

Source: SBP Quarterly Bulletin 2012.

Although SMEs sector consider as economic engine to boost up GDP growth, export earnings and employment level. But government policies could not support SMEs sector in past. However, SBP has taken footstep for preferment and growth of SME banking that has caused to increase around 20% SMEs financing Outstanding in 2015 as compare to period 2006 – 20014.



**Figure IV: Composition of SME Financing**

Source: SBP Quarterly Bulletin 2012.

During that period, the NPLs witnessed declined by almost 30% because of conservative lending approaches and banks tried to clean their overdue loans to SMEs sector. This positive trend, encourage Banks/DFIs to lend more in SMEs sector. The Figure, depict that financing to working capital constituted almost 74% to total SMEs financing.

### 3.1.2. India:

The MSMEs, predominantly for developing economies, considered as backbone of the economy that cause significantly to appreciate export earnings with constructive GDP. The growth of SMEs sector in India is commendable. According to (Indian SMB Sector , 2013) India has the 2<sup>nd</sup> highest number of micro, small and medium sized enterprises (MSMEs) in the World with 48.8 million enterprises. Beside this, China is the largest SMEs homeland worldwide.

In India, the micro, small and medium sized enterprises (MSMEs) has been defined according to their investment in plant and machinery under the Act of Micro Small and Medium Enterprise Development 2006 (MSMED, 2006). According to this Act, those firms who are investing not more than Rs. 100 million in the head of plant and machinery are categorized as MSMEs in the manufacturing sector. However, in services sector, firms investing not more than RS. 50 million are classified as MSMEs in India.

**Table II. Number of MSMEs in India**

| Item   | 2007 | 2008 | 2009 | 2010 | 2011 | 2012  | 2013  | 2014* |
|--|------|------|------|------|------|-------|-------|-------|
| <b>Number of MSMEs</b>                                   |      |      |      |      |      |       |       |       |
| MSMEs—registered and unregistered (mil.) <sup>1</sup>    | 36.2 | 37.7 | 39.4 | 41.1 | 42.9 | 44.8  | 46.8  | 48.8  |
| Total number of enterprises (mil.) <sup>2</sup>          | --   | --   | --   | --   | --   | --    | 58.5  | --    |
| MSMEs to total enterprises (%)                           | --   | --   | --   | --   | --   | --    | 79.9  | --    |
| Growth (%)   | --   | 4.3  | 4.3  | 4.3  | 4.4  | 4.4   | 4.4   | 4.4   |
| <b>Employment by MSMEs</b>                               |      |      |      |      |      |       |       |       |
| MSME employees—registered and unregistered (mil. people) | 80.5 | 84.2 | 88.0 | 92.1 | 96.5 | 101.1 | 106.1 | 111.3 |
| Growth (%)   | --   | 4.6  | 4.6  | 4.7  | 4.7  | 4.9   | 4.9   | 4.9   |

Sources: Annual Report of MSMEs for the financial Year 2013-2014.

The SMEs sector play significant role in industrial sector in India that create jobs and provide raw material to the large manufacturing sector in the country. Beside this, Indian government support and assist this sector with lenient term and condition. Therefore, approximately three million SMEs units operating in India that produce almost 8000 variety of products in differentiated industries (Indian SMB Sector , 2013). The Ministry of MSMEs in India announced the annual results of MSMEs sector. This report estimated that the MSMEs in India has grown at average 4.4% rate every year. While, at the end of first quarter of 2014, the total number of MSMEs in India was projected at 48.8 million.

The number of employees in MSMEs in India has grew at fast pace equivalent to MSMEs sector growth. In first quarter of 2014, the total number of employees employed by MSMEs in India was around 111.3 million which was grew at the pace of 4.9% for consecutive three years.

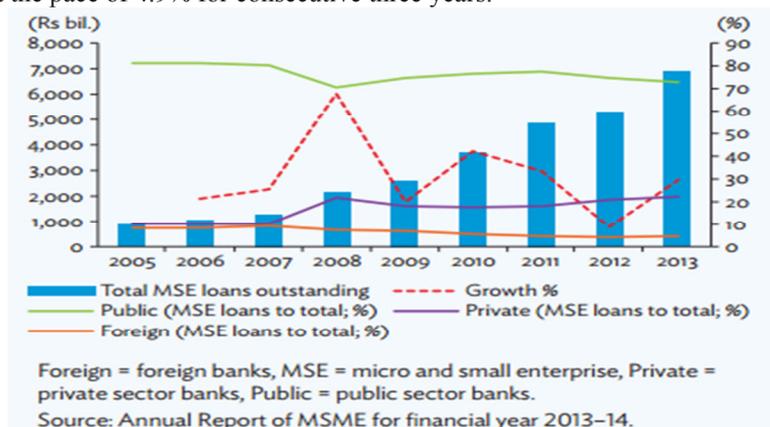
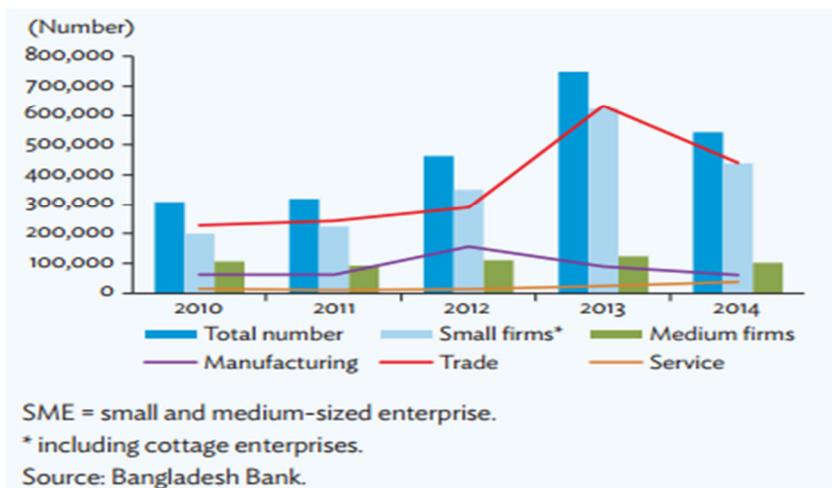


Figure V: MSMEs Loan Outstanding

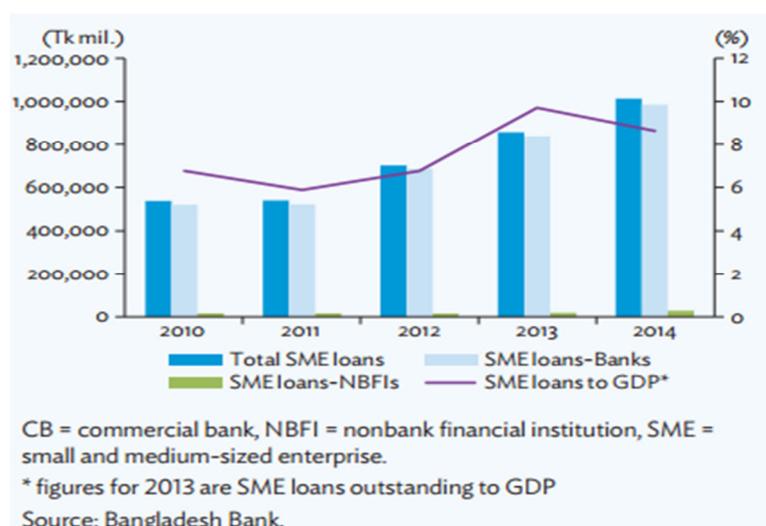
The Small Industries Development Bank of India (SIDBI) was originated in 1990 with an aim to encourage, financing and expansion of the MSMEs sector in India. In India, the commercial banks issued around Rs. 8,460 billion outstanding loans to MSMEs sector as of the end of first quarter of 2014. The growth rate of outstanding loans has been increased at 23.1% as of the end of March 2013. Beside this, in 2013, the public-sector banks provided around 73% of the total loans outstanding to MSMEs with 22.3% and 4.7% followed by Private and foreign banks respectively. However, for MSMEs, the total credit demand was RS. 28 trillion at the end of first quarter of 2014 in which almost 70% would be required for maintaining working capital requirements (ADB, 2014).

### 3.1.3. Bangladesh

Regardless of challenging global economic environment, the economy of Bangladesh grew at 6% during the year end 2014 including 9% growth rate of micro, small and medium-sized enterprises (MSMEs). Among the fastest-growing emerging economies, the Bangladesh stood at fourth ranked (IMF, 2014). According to the Bangladesh Bureau of Statistics, 2013 the SMEs sector constitute 90% of the private sector enterprises including 7.2 million firms. Moreover, SMEs sector employed 70%-80% of the workforce in Bangladesh and contribute 40% of industrial output with 25% contribution in GDP in the country (BBS, 2013).

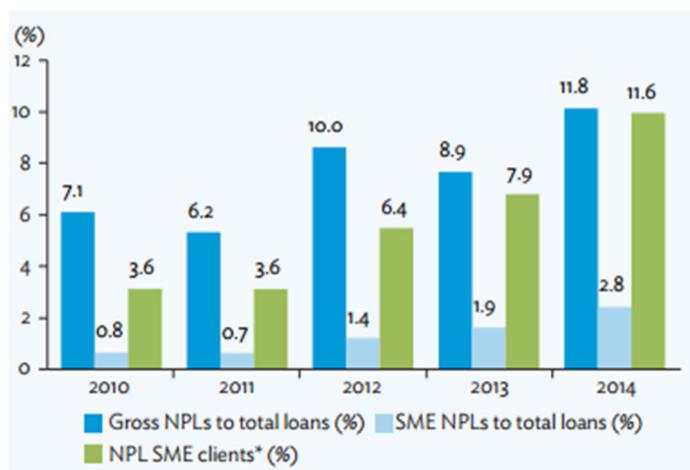


**Figure VI: SMEs Borrows**



**Figure VII: SMEs Loan Disbursed**

The Bangladesh industrial policy in 2010, define SMEs criteria that is based on number of employees or value of fixed assets. The manufacturing firms considered as MSMEs when they employed less than 250 employees or their fixed assets not exceeding TK 300 million. Whereas, in services sector MSMEs, the fixed assets are not more than TK 150 million and employed not more than 100 employees (Industrial Policy for SMEs, 2010).



**Figure VIII: SMEs Nonperforming Loans**

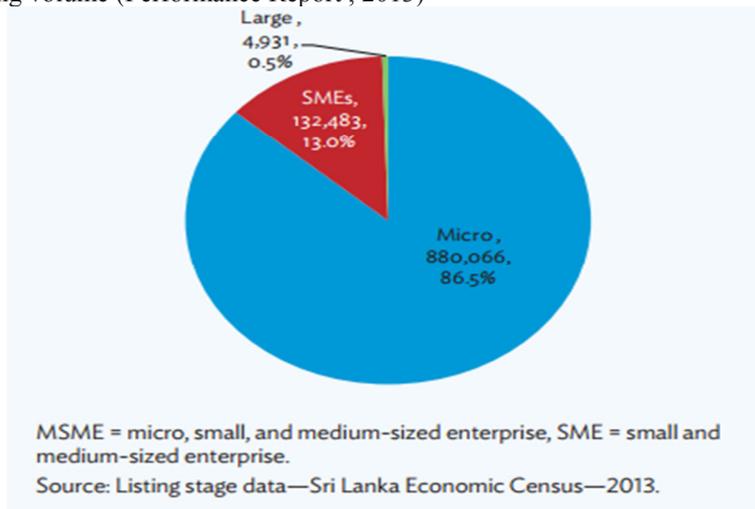
The growth of SMEs sector's loan was growing at the rate of 18.3% in 2013-2014. In 2014, the small firms received 52% of total loan disbursement in Bangladesh. Though, Medium-sized firms got 48% loan in

Bangladesh (Bangladesh Bank, 2013-2014) . While because of worse political conditions in country during 2013 to 2014 caused to grew SMEs sector default rates. During the specified period, the NPLs to SMEs sector ascended to shocking 11.8% in the country.

However, to deal with this phenomenon, the Bangladesh Bank directed all financial institutions and NBFIs to rescheduling SMEs loans to this sector. Furthermore, with the assistance of Asian Development Bank, Japan International Cooperation Agency and the International Development Association the Bangladesh Bank has offered refinancing facility to the Banks and NBFIs against their SME loans (ADB, 2014).

### 3.1.4. Sri Lanka

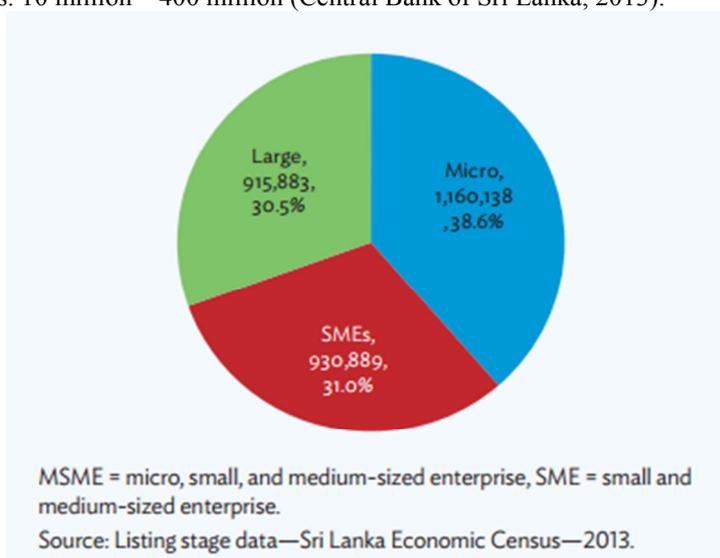
In Sri Lanka, for attaining sustainable economic growth with dropping unemployment rate and poverty in the country, the small and medium enterprises is considered significant and contributing sector. In 2013, The SMEs sector in Sri lanka has contributed 30% to GDP, 35% of national labor force and its 20% total export consist of SMEs manufacturing volume (Performance Report , 2013)



**Figure IX: Number of MSMEs**

The Sri Lankan government has permitted some privileged rights to the SMEs sector operating in the country including providing credit at lenient term and conditions, Tax subsidy and make available conducive business set-up to promote innovation, technological advancement and competitiveness in the country.

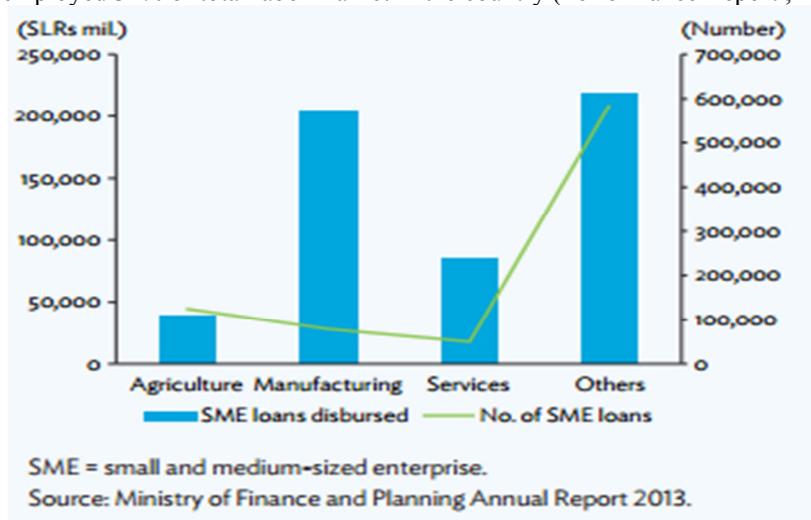
The Central Bank of Sri Lanka (CBSL) has defined SMEs according to the two diverse constraints; the one parameter defines SMEs according to the value of net assets without land and building cost. According to these criteria, the Assets value should not exceed SLRs.50 million. Whereas, the second standard define SMEs in term of annual turnover. For SMEs, the standard turnover value should be between SLRs.100-2000 million and fixed assets worth between SLRs. 10 million – 400 million (Central Bank of Sri Lanka, 2013).



**Figure X: Employment by MSMEs**

The Sri Lankan Census department in 2013, has defined firms according to the number of employees in the firm. According to the criteria, for manufacturing sector, the firm employees less than 10 workers are considered

as Micro Enterprises, whereas those employed between 10 to 100 workers are considered as SMEs. For services sector, the Micro firms can be employed less than 3 workers While, SMEs consist of between 3 to 29 employees. In Sri Lanka, there are 86.5% firms were Micro enterprise while only 13% were SMEs and 0.5% of Large firms operating in Sri Lanka in 2013. The Micro Enterprises provide employment of around 38.6% workforce, Whereas, SMEs employed 31% of total labor market in the country (Performance Report , 2013).



**Figure XI: SMEs Loan Disbursed by Sectors**

In Sri Lanka, the bank's lending to SMEs sector were increased sharply by approximately 106% in 2013-2014. While, loan disbursement by manufacturing SMEs were 37.2% of total SMEs loan disbursement and for service sector SMEs account for 15.6% of total SMEs loan in Sri Lanka ( Annual Report, 2013).

#### 4.0. FINANCIAL INNOVATION TO SMES:

As we discussed earlier that for economic development of the developed as well as emerging economies, the SMEs perform a vital role. But financing constrained is the leading hurdle for growth of this sector. Financial institutions perform a intermediary role between lender and borrow. Financial institutions propose several financial services to SMEs to facilitate their business operations. Not only funding facility, the institutions also offer advices regarding management issues, employees trainings and how to mitigate risk while trade at domestic as well as international level. However, SMEs are more financial constrained as camper to large firm due to access of finance that is crucial impediment to their growth. Financial sector perceived that financing to SMEs are challenge because irregular information, lack of collateral and high risk curtails their growth.

According to the World economic forum report, innovation is the chief pillar to determine the country's global competitiveness (WEF, 2008) . Although innovation and risk taking have usually restrained in developing nations including South Asian Economies and traditionally business sector capitalization focused on rent-seeking rather than entrepreneurship. Beside this, for growth of SME sector, Entrepreneurship is essential and continued process.

To cope with financial challenges, Innovative financing tactics are prerequisites for the growth of small and medium firms that enable small and medium enterprises to contribute in the economic growth of the country. Financial plans endorse innovation by the following ways;

- The innovative entrepreneurs should be encouraged by government and financial institutions through the innovative technological education and financial literacy training programs.
- The collaboration between Academia and researchers with innovative entrepreneurs are essential for growth of SMEs sector in the country because they provide referral and laboratory services to SMEs to promote innovation.
- The government should have fortified innovative ideas by allowing tax exemption to the SME sector.
- The need of establish business incubation centers are prerequisite in academia. The universities should have set up business centers with collaboration of SMEDA and Financial institutions to promote young entrepreneurs and enhance their business skills.
- Financial policies have been mobilized towards SMEs financing and government provide easing on institutional investment in domestic project funds.
- The government has taken decision to eliminate minimum capitalization to channel flow of funds to innovative MSMEs.

## **5.0. CHALLENGES FACED BY SMEs:**

Although it is observed that SME sector in South Asian Economies growing rapidly and it is worth mentioned here that SMEs contribution in the selected economies are notable in term of their contribution in GDP and Export surplus of the country. But this sector is facing several issues and challenges that restrain SME sector growth in this region. However, despite of several obstacles, most of the emerging economies are rely on SMEs sector.

In following section, the researcher is going to highlight major issues and constraints faced by SME sector in South Asian economies;

1. Financial Constraints
2. Weak Infrastructure for SMEs
3. Inadequate Use of Technology
4. Human Resource Restraints and Lack of Administrative Skills

### **5.1. Financial Constraints**

Along with many challenges, the accessibility of finance for SME sector is the significant issue for all the entrepreneurs and business participants (Sherazi S.K, 2013). The above literature evidenced that almost all the targeted South Asian economy's financial institutions lent to SMEs sector, but it is also fact that they are reluctant to finance SMEs sector due to many reasons like, limited scope, default risk, lack of collaterals and

lack of knowledge about borrowing process from financial institutions. Most of the financial institutions prefer large enterprises over small while lending credit. Because large firms have maintained their books of account according to the accounting principles and their financial data is audited that have low chance of defaults. Beside this, SMEs do not have clear accounting information of their business and in the view point of lenders it is risky to finance SMEs sector.

Regardless of the fact banks are mostly risk averse while lending to SMEs sector because increasing inflation in the economy laid on positive impact on interest rate that caused to fluctuate economic conditions and thus due to risk associated, small sector bear huge loss as camper to any other sector (Kousar R., 2012).

### **5.2. Weak Infrastructure for SMEs:**

In Developing economies, the Micro and Small enterprises contribution towards economic growth cannot be denied. The study of (Tamvada, 2012) found in their study that small enterprises have potential to grow fast as compare to large enterprises. But the reckless business infrastructure not supportive for small firms. The inadequate resources, administrative issues, Lack of prudent policy and regulations by the Government and deficient market information behind the economic growth of these economies and it is hard to sustain in today's business environment without technology (Zaidi, 2013).are the crucial obstacle that hinder SMEs sector growth.

### **5.3. Inadequate use of Information Technology:**

The use of modern technological is prerequisite in today's business arena. Technological advancement growing rapidly around the world. Therefore, most of the customers prefer buying online through e-commerce. The complications which avert future growth of small firms are negligence of technology usage while performing business operations. The low literacy rate in south Asian nations observed which limited the knowledge to attract towards technology which may ease the business operation by cutting cost and save time. However, some technological advancement is essential and consider as obligatory part of the business operations.

According to the study of (L. Poblete, 2010) the vulnerability to adopt the modern technology and skills consider as internal curb that can hurt growth of small enterprises. In India and Pakistan, the deficiency of technical education laid adverse impact on growth of small firms. Because lack of awareness about usage of technology legging.

### **5.4. Human Resource Restraints and Lack of Administrative Skills**

To recruit the workers, to manage them and to retain them is one of the major obstacles in the track of SMEs sector growth. Insufficient relevant expertise and poor administration can curtail and even stop the growth of small firms. According to the study of (Islam, 2011) inadequate business knowledge and lack of skilled labor force can ultimately affect the business operations. The study further explained that unskilled labor is the biggest challenge for the small firms because they can never take chance to lose their customers thus, lack of skilled labor force is obligatory for the growth of small enterprises.

## **6.0. CONCLUSION:**

The Small and medium enterprises have developed as imperative straight for sustainable and continuous growth of south Asian economies. Although there are several financing options available for SMEs from the financial institutions, but it is crucial for SMEs to choose appropriate financing options to resolve the firm financial

challenges. This research study primarily consists of analyzing the sources of financ available for Small and medium firms along with financing challenges confronted by small business traders with the objectives to exploit the innovative ways to improve financing streams for Small and medium enterprises in South Asian Countries. For accomplish this purpose, four major South Asian Countries, India, Pakistan, Bangladesh and Sri lanka have been selected to analysis the growth of SMEs sector with the viewpoint of financial constrained and innovative financial provisions.

In South Asian Economies, there are several financing sources available to SMEs but these firms due to their small-scale face challenges that make these firms higher risky financing decision. The SMEs contributions in the economic development of the South Asian economies cannot be denied. This sector has potential to create employment opportunities and have leading source of innovative ideas to provide gear of the economic engine of the country. These firms are significantly important source of employment for youth and specially to encourage Women Entrepreneurship and consequently, contributes towards sustainable economic growth.

This study suggests that the innovative entrepreneurs should be encouraged by government and financial institutions through the innovative technological education and financial literacy training programs. Moreover, the collaboration between Academia and researchers with innovative entrepreneurs are essential for growth of SMEs sector in the country because they provide referral and laboratory services to SMEs to promote innovation.

Beside this, the need of establish business incubation centers are prerequisite in academia. The universities should have set up business centers with collaboration of SMEDA and Financial institutions to promote young entrepreneurs and enhance their business skills.

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