

## Yaseen Anwar: SME banking

Keynote address by Mr Yaseen Anwar, Governor of the State Bank of Pakistan, at a roundtable on “SME Banking”, jointly organized by the State Bank of Pakistan and the International Finance Corporation (IFC), Karachi, 16 January 2013.

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Mr. Kaiser Naseem & Mr. Andrew McCartney from IFC, Distinguished Presidents of commercial banks Ladies and gentlemen, Good morning!

Let me extend a very warm welcome to all of you to this Roundtable on the important subject of “SME Banking”, jointly organized by State Bank of Pakistan and IFC. I would like to especially welcome and thank the SME Banking experts from IFC who have traveled from abroad to conduct this important session for the top management of the banking industry of Pakistan.

This Roundtable is indeed a significant event as we have representation of all the major banks that contribute more than 90% of the total SME Lending in the country. The objective of today's proceedings is twofold; *first*, to take stock of the issues confronting the SME sector, and *second*, to learn and deliberate on the various successful strategies and SME Banking models practiced globally by lending institutions.

I am sure everyone around the table believes that SME development plays a key role in the economic development of a country. In Pakistan, the sector contributes 30 percent towards GDP, employs more than 70 percent of the non-agricultural workforce and generates 25 percent in export earnings. The sector has huge potential in generating employment and poverty alleviation in the country. Therefore, SBP is actively promoting SME finance under the broader agenda of increasing Financial Inclusion in Pakistan.

The governments around the world support small scale agriculture, services and manufacturing sectors through a number of initiatives because of their labor-intensiveness and employment generation potential for poverty reduction. These countries have also successfully integrated their SMEs with the large corporate sector through sub-contracting which has proved an extremely useful way of integration across size and scale.

In Pakistan, despite the immense significance of the SME sector, it remains largely financially excluded, as reflected from the declining trend in SME finance over the years, constituting only 8% of the banks' total advances as of June 2012, down from 16% in June 2007. Unfortunately, this ratio is quite low compared to our regional peers such as in India, Sri Lanka and even Bangladesh.

A closer look at the SME sector reveals that there are various issues on both demand and supply side that constrain the SME's access to finance and other banking products and services. *On the demand side*, these issues can be tackled through a more systematic documentation and disclosure of information by SMEs and better business planning. *On the supply side*, bankers' reluctance to lend to SMEs can be addressed through innovative credit assessment tools and techniques like credit scoring and better capacity building efforts for the financial service providers.

Among various stakeholders that have to play their role for SME development, I think, State Bank of Pakistan and Commercial Banks both need to play a proactive role in improving access to finance for SMEs. As far as SBP is concerned, it has taken a number of important initiatives for improving access to credit for SME sector. These measures include a provision of specialized Prudential Regulations (PRs) for SMEs, Refinance Schemes for SMEs, Credit Guarantee Scheme for Small and Rural Enterprises and cluster development surveys.

Further, SBP has been assisting banks through a holistic IFC technical assistance and capacity building initiative encompassing areas of Strategy Formulation, Product

Development, Risk Management and HR Development etc. for SME lending. Presently, Bank Alfalah Ltd. is being supported for capacity building to boost SME banking, while many other mid-tier banks are being considered for similar IFC technical assistance. IFC is in direct dialogue with a number of banks. We hope that this project will revitalize SME lending by participating financial institutions and will be a prototype for other financial institutions which could see financing to SMEs as profitable business ventures. Aside from the boost SME provides to employment and overall growth to the economy, it also provides diversification to a bank's balance sheet and in turn a stable revenue stream to support long term shareholder value.

Given the huge potential for this sector, I encourage all the commercial banks to review their SME strategies and assume a greater role in SME lending. Ultimately it has to be the private sector which has to take the lead role in lending to the SME sector given their critical positioning and greater capacity in terms of their outreach and availability of funds.

As I earlier mentioned, the actual statistics for lending to SMEs have not been encouraging in recent years. Banks' credit to SMEs has declined over the last 4 years from Rs 437 billion in 2007 to Rs 248 billion in June, 2012.

Although, this decline can be partly attributed to adverse economic conditions during the period and growing NPLs, a more risk-averse posture of banks remains a major factor responsible for their low exposure to SMEs. In recent years, banks have increasingly invested in safer havens – opting for government paper and increased financing for commodity operations, rather than lending to private sector that would offer better returns and is the main driver of economic activity.

I would encourage the financial industry to break-out of this tendency and move towards promoting SMEs by formulating strategies to overcome the challenges presented by the market as well as by the cyclicity in economic conditions. Banks need to shift from traditional banking approach towards SMEs to the provision of more customized and differentiated financial products and services.

Let me re-iterate the objective of this program i.e. to share with you the successful SME banking models and their important Building Blocks, such as Strategy Formulation, Product Development, Risk Management tools, and HR & IT requirements. We are lucky to have with us today's lead presenter Mr. Andrew McCartney from IFC who is a renowned international expert on SME Banking.

I hope this event will help top management of the banks to take critical stock of their existing approaches towards the SME sector; and, accordingly develop a more robust and focused strategy for meeting the banking needs of this important sector of economy, leading to better and improved banking solutions for their SME customers. I would hope that when you walk out after this roundtable, a voluntary commitment to increase lending to this sector will be forthcoming. This prudent decision will be in the interest of both the banking sector and the economy.

Thank you.