

**The impact of credit on the success of  
SMEs: Study on People's Bank  
customers in Colombo District**

By

**RATHEEPA RAVEENDRA**

A research submitted to the University of Sri Jayewardenepura in  
partial fulfillment of the requirements for the Degree of Master  
of Business Administration

The work described in this research was carried out by me under the supervision of Mr.R.N.Weerasinghe and a report on this has not been submitted in whole or in part to any university or any other institution for another Degree or Diploma.

*R. Rathepa*.....

R.Rathepa

I certify that the above statement made by the candidate is true and that this research is suitable for submission to the University for the purpose of evaluation.

03/05/2016  
Mr.R.N.Weerasinghe

# Table of Contents

Page

<b>1. INTRODUCTION .....</b>	<b>1-9</b>
<b>1.1 Background of the study .....</b>	<b>1</b>
<b>1.2 Research problem .....</b>	<b>5</b>
<b>1.3 Objectives of the study .....</b>	<b>5</b>
<b>1.4 Significance of the study .....</b>	<b>5</b>
<b>1.5 Methodology .....</b>	<b>7</b>
1.5.1 Hypotheses of the study .....	7
1.5.2 Research sample .....	7
1.5.3 Data collection techniques.....	7
1.5.4 Method of analysis .....	8
<b>1.6 Organization of the study .....</b>	<b>8</b>
<b>2 LITERATURE REVIEW .....</b>	<b>10-31</b>
<b>2.1 Introduction .....</b>	<b>10</b>
<b>2.2 The Definitions of SMEs.....</b>	<b>10</b>
<b>2.3 SMEs and Finance .....</b>	<b>13</b>
<b>2.4 SMEs development in Sri Lanka .....</b>	<b>15</b>
<b>2.5 SMEs and People's Bank .....</b>	<b>19</b>
<b>2.6 Empirical literature on role of credit on SMEs performance .....</b>	<b>22</b>
<b>2.7 Summary .....</b>	<b>31</b>
<b>3 RESEARCH DESIGN AND METHODOLOGY .....</b>	<b>32-39</b>
<b>3.1 Introduction .....</b>	<b>32</b>

3.2	Conceptual model .....	32
3.3	Operational frame work .....	34
3.4	Variable of the study .....	34
3.5	Population and Sample .....	35
3.6	Sampling Techniques .....	36
3.7	Source of Data .....	36
3.8	Data collection .....	37
3.9	Data Analysis .....	38
3.10	Summary .....	39
<b>4</b>	<b>DATA ANALYSIS AND PRESENTATION.....</b>	<b>40-59</b>
4.1	Introduction to the chapter .....	40
4.2	Validity and Reliability analysis in the study .....	41
4.3	Analysis and presentation of profile and credit behaviour of the respondents .....	42
4.3.1	Types of business .....	42
4.3.2	Legal structure of business .....	43
4.3.3	The period of business.....	44
4.3.4	No of employees.....	45
4.4	Type of Bank facilities and their patronage .....	46
4.5	Utilization of granted loan .....	50
4.6	Hypotheses testing in the study .....	52
4.7	Conclusion .....	59
<b>5</b>	<b>SUMMARY, CONCLUSION AND RECOMMENDATION .....</b>	<b>60-66</b>
5.1	Introduction .....	60

5.2	Summary of findings.....	60
5.3	Achievement of Research Objectives .....	62
5.4	Conclusion and Recommendations.....	63
5.5	Limitations of the Research .....	65
5.6	Suggestions for future researchers .....	66
6	REFERENCES .....	67-77
7	APPENDIX .....	78-82

<b>List of Table</b>	<b>Page</b>
1. Table 3.1: Operational Framework .....	34
2. Table 4.1: Reliability test for the items .....	41
3. Table 4.2: Summary of the validity and reliability testing results .....	42
4. Table 4.3: Type of bank facilities .....	47
5. Table 4.4: Summary of credit rating .....	52
6. Table 4.5: Model summary .....	53
6. Table 4.6: Anova table .....	54
7. Table 4.7: Coefficients table .....	54
8. Table 4.8: Anova table .....	55
9. Table 4.9: Coefficients table .....	56
10. Table 4.10: Correlation matrix .....	58

## List of figures

Page

1.	Figure 3.1: Conceptual model .....	33
2.	Figure 4.1: Type of business in the sample .....	43
3.	Figure 4.2: Legal structure of business.....	44
4.	Figure 4.3: Period of business .....	45
5.	Figure 4.4: No of employees .....	46
6.	Figure 4.5: Type of bank facilities .....	49
7.	Figure 4.6: Utilization of granted loan .....	50

## **ACKNOWLEDGEMENTS**

Pursuing a Master Research is both interesting and pleasurable experience. The experience during the research period is like hardships, encouragement and confidence with great people's support. First of all, my sincere thanks belong to our Professor K.D.Gunawardene, who initiated me to search topic while emphasising the importance of the research work for MBA degree program. Secondly my special thanks to my advisor Mr.R.N.Weerasighe, who accepted me as his student without any hesitation. His experience in his academic life and industry exposure assisted me throughout my research period. Further I will be thankful to the coordinator Dr. P.J.Kumarasinghe, helped me to finish this research work. I must thank for the non academic staffs of Postgraduate unit as well, they too supported during the tenure of my research. Special thank goes out to my family, relatives and friends who supported me during the study though several ways, such as arranging references list, formatting, editing and proof reading. Finally my sincere thanks belong to all who supported me at different capacities. Moreover, I hope that this research fulfils a practical knowledge on impact of credit facility on SMEs' success.

Ratheepa Raveendra

Colombo, December 2015.

# **The impact of credit on the success of SMEs: Study on People's Bank customers in Colombo District**

**Ratheepa Raveendra**

MBA General (Student)  
Faculty of Graduates Studies,  
University of Sri Jayawardenepura.

## **ABSTRACT**

Small and Medium Enterprises (SMEs) are the catalyst for economic growth in most economies thus, the fundamental objective of this study is to investigate the impact of loans on Small and Medium Enterprises in Colombo District. The purpose of this research is to evaluate the impact of credit availability on SMEs success. This study give an insight in identifying better and poor performance of the credit on SMEs success or failure, and a clue of measurements to be taken in order to improve the credit availability strategy and implementation. Data were collected from primary sources which were collected from Colombo district people's bank 100 customers, while correlation, non parametric chi -square statistics and multiple comparison tests were used for analysis of data. Simple random sampling technique was employed in selecting the 100 SMEs that constituted the sample size of the research. It is recommended that Banks should review their interest rate downwards and also share best practices with their SME customers especially on the efficient use of loans; this will boost their productivity and support SMEs in Sri Lanka. The study concluded that there is a strong relationship between bank credit facility and SMEs success. It means, if the bank increases the rate of granting SMEs loan facility, it helps to make the success of the SMEs. Then, it is recommended for the banks to increase the loan amount to SMEs for developing the SMEs to accelerate the economic growth.

Key Words: Small and Medium Enterprises Success, Credit facilities, financial contribution of bank to the business.

# CHAPTER 01

## INTRODUCTION

### 1.1 Background of the study

Small and Medium Enterprises (SMEs) contribute a large part of Sri Lanka's economy, accounting for 80 per cent of all businesses. These are found in all sectors of the economy, primary, secondary and tertiary and provide employment for persons of different skills: skilled, semi-skilled and unskilled. There are SMEs in the agri-business sector engaged in growing spices, fruits and vegetables and in the manufacturing sector engaged in numerous industrial activities accounting for about 20 percent of industrial establishments. In the service sector SMEs accounts for more than 90 percent of business establishments. SMEs are an essential source of employment opportunities and are estimated to contribute about 35 percent of employment (NHREP, 2012). The SMEs play an important role in promoting inclusive growth.

SMEs are normally privately owned establishments, partnerships or sole proprietorships. SMEs use several sources available for capital. It includes self financing by owner, loans from friends or relatives, grants from private foundations, personal savings, forming partnerships and banks. SME has an important place in the social economic development of the country. Most entrepreneurs start small and then develop as large industries. SME provides opportunities to enhance their skills and talents and to transform their ideas into goods and services needed by society.

According to the Central Bank of Sri Lanka(1998), the cottage and small scale industries sector plays an important role in economic development through creation of employment opportunities, the mobilization of domestic savings, poverty alleviation, income distribution, regional development, training of workers and entrepreneurs, creating an economic environment in which large firms to flourish and contribute to export earnings.

Over the years SMEs have gained wide recognition as a major source of employment, income generation, poverty alleviation and regional development (White paper, 2002). According to central bank of Sri Lanka (2009), SMEs sector plays an important role in economic development and therefore, institutional facilities for SMEs development continued in the year 2009. The Federation of Chambers of Commerce and Industries of Sri Lanka (FCCISL) continued to provide a wide range of services for the SMEs to be competitive, socially responsible and environmentally friendly and a program named “Enterprise Sri Lanka” is launched to provide support services to SMEs. Having understood the positive impact SMEs development and economic growth, successive governments in Sri Lanka, have taken various steps to develop this sector (Gamage, 2000). When compared to other developed and developing countries, the present contribution of this sector to the national economy is not up to the desired level. Lack of access to credit is one of the major constraints hindering the development of small businesses. So, there is vast opportunity for Sri Lanka to develop this sector by providing financial support.

Small and medium sized enterprises represent the lifeblood of local trade, commerce and industry. SMEs offer the best prospects in creating employment, generating incomes and

contributing to society. SMEs are in fact the very fabric of the economy. SMEs do not exist in isolation from the rest of the economy. They are integrated specific opportunities, sharing knowledge and know-how with SME's to increase their competitiveness, productivity and market shares.

Commercial banks have concentrated to providing financial facilities to small businesses. The People's Bank was established (1961) to fulfill banking requirements and to promote industrial development. People's Bank provides loans to the business customers by the name of "Development Banking". It includes loan scheme for upraise of micro and small entrepreneurs engaged in micro and small scale trading activities, Viskam (credit line for development of commercialized agribusiness), Micro finance loans (people's fast), Athamaru loan scheme, Provincial development loan scheme, Prosperity loan scheme. Micro, Small and Medium scale entrepreneurs constitute a high percentage of existing client base and the critical need to uplift this segment created a conducive platform for us to intensify our SME financing activities. Establishing a separate department empowered to carryout SME financing in 2006, resources were put in place by way of a Deputy General Manager and an Assistant General Manager to research, design, develop and implement strategies and methods for launching and managing the extensive, commercially viable SME business.

Recognizing the importance of uplifting the rural economy through the nurturing and development of the SMEs, which then results in reducing unemployment and bringing about social equality, People's Bank continues proactively the long-term vision of the

government in making the Sri Lankan SME sector globally competitive through developing a sustainable entrepreneurial culture in Sri Lanka. People's Bank defines SME financing, as a small scale business activity that creates or adds value in the areas of industry, agribusiness or services being a sole proprietorship, partnership or corporate venture. These enterprises may be a new project or an ongoing business activity with the characteristics of good product marketability, innovation, employment generation, local raw materials utilization and even more profoundly, export oriented.

People's Bank established a dedicated department to develop the SME banking business in a more structured and targeted manner drawing on the strength of branches equipped with strong capacities including competent and skilled branch managers and credit officers to appraise and disburse loans efficiently and effectively. Bank develops strategies of implementing a business model based on market needs and demands. Structured SME financing products, speedy credit evaluation and approval are the features of the approach. Appraising the specific requirements of these customers and addressing issues through specialized SME lending in tandem with building and strengthening relationships, will remain fundamental pillars in the approach which will then also pave the way efficiently for current Micro borrowers who move up the ladder of entrepreneurial success. The aim of this research is to examine effects of bank credit to SMEs on entrepreneurial success.