

جمعية البنوك في فلسطين
Association of Banks in Palestine



Banking sector role in the
SMEs
development in Palestine

Seminar in Accounting

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Summary

The economic conditions and the growing numbers of SMEs in Palestine in addition to their role in the economic development require cooperation between all related parties in order to improve their conditions and create a suitable environment that enables them to grow and survive. SMEs constitute the majority of institutions in all countries. Moreover, they contribute to a large proportion in the GDP and providing job opportunities and lower prices products and services.

SMEs face several barriers and obstacles that affect the development and growth for them. The major obstacle they face is the financial aspects which reduce their abilities to growth and compete against foreign products. From this point, the role of financial institutions is to facilitate the accessibility of funds. This study showed the banking sector role in the SMEs development. Moreover, the facilities they can provide to SMEs to overcome the consequences that they facing.

CHAPTER ONE
INTRODUCTION

1.1 Introduction

Palestine is a developing country with an emerging economy characterized by some features that distinguish it from other economies. These features include the absence of local currency and the use of the three major currencies, U.S. dollar, the Jordanian dinar and the Israeli Shekel. In addition to these features, its dependence on foreign aids, and the fact that the Palestinian economy is a service economy which contributes to 68% of the GDP; the total Palestinian GDP is 6,797.3 million dollar in 2012 (Palestinian central bureau of statistics). The majority of Palestinian firms are family business which in many cases create management conflicts and lead to liquidation especially in the third generation (Sabri, 1999) thus, the economic development will not come from normal conditions, but rather by joint efforts among all parties to create a strong economy that is capable to meet the domestic requirements.

We do not deny the fact that the Palestinian economy is suffering from serious conditions. Nevertheless, human development index is moderate in Palestine due to the employment in Israel, The Gulf States and The United States. On the one hand, Employment in Israel has helped to acquire experience and bring some equipment. On the other hand, the employment in the Gulf States and The United States have brought remittances to the country (Sabri, 2008). This has encouraged some entrepreneurs and innovators to invest in this experience and remittances in projects in Palestine. The importance of these projects begins with their functions in the economic development and the fair distributions of income as they offer opportunities for workers from poor families and so, it alleviates poverty. Moreover, they spread in a wide geographic area, unlike large enterprises, which are concentrated in the city centers and employs only qualified employees.

According to the Palestinian Center for Statistics the total number of establishments operating in Palestine in 2007 was 132,874 enterprises 90.7 of them are a private ownership, the percentage of SMES around 90% of Palestinian enterprises. The economic distribution indicates that the wholesale and retail and the vehicles repair accounted for 53.9% from these enterprises followed by the manufacturing sector by 14%. SMEs in Palestine contribute more than 55% to the GDP, and employ 85% of the private sector labor force (PIF) which is considered as a high percentage. From this point, we can say that any hit to these projects will significantly affect the country's economy. On the other hand, any progress in this sector will revive the economy.

The Palestinian banking sector consists of 17 banks with 232 branches and offices 7 of them are local banks, and 9 are Arab banks and one is a foreign bank. The number of commercial banks is 15 banks and 2 Islamic banks (association of banks in Palestine). The banking sector has a dynamic role in the SMEs development by providing the necessary financial support and the effortless procedures as well as providing some features in collaboration with government and all the related parties. Wherefore, borrowing is difficult in most cases because of the lack of requirements and guarantees. Banks undertake these procedures in order to minimize risk and insure repayment. However, the existence of joint support between all parties will reduce this risk.

This research will talk about the SMEs in Palestine and its importance in the economy in addition to the banking sector role in the SMEs development so as to assist these enterprises in order to help create a favorable environment which enables growth and development for both of them.

1.2 topic statement

What are the banking sector roles in the SMEs Development and growth?

1.3 objectives

This study aims to investigate the role of banking sector in the development of SMEs and spurring entrepreneurial and innovative projects. Moreover, it seeks to know the facilities that SMEs need, so they can grow and survive.

1.4 research question

1. What are the facilities that banking sector can provide to SMEs?
2. What are the roles that banking sector played in the development of SMEs?
3. What is the common strategy that must be set by the government with the banking sector to develop SMEs?
4. What are the Consequences that SMEs faces?

1.5 Need for the study

SMEs plays an effective role in the economic development since it offers lower prices products and services and reducing unemployment by providing job opportunities, but in most cases these enterprises do not successes or develop because of the shortage of the financial support and the government incentives from the other side. From this point, the government and the banking sector should cooperate and work together in order to improve the conditions that enable them to grow and survive as well as increasing their abilities to compete against foreign products.

1.6 definition and key terms

- SMEs: small and medium enterprises ,small enterprises are projects that have 6-15 workers and the capital invested in fixed assets less than \$ 15,000, The medium is a project, which employs 15 -50 workers and invests from \$15000 to \$25000 in fixed assets
- Banking sector: the 17 banks operating in Palestine, 7 of them are local banks, and 9 are Arab banks and one is a foreign bank.
- Family business: a business managed and owned by more than one member from the family and the ownership is transferred to the children.
- Entrepreneurial: is a person who managed the business and assumes all risks.

CHAPTER TWO

LITERATURE REVIEW

2.1 Introduction

SMEs comprise the largest percent of all enterprises in most countries and also, a large part of private sector; they form 98% in Palestine. In general, the importance of these enterprises comes from its dynamic role in the economic development and their contribution in the GDP as they considered the engine of the economy. Moreover, it is a source of new job opportunities, low prices products and services, income distribution besides the creation of innovative products and services. By reviewing previous studies, we find several facts relating to SMEs. Firstly, they are often a family business or a partnership with simple structure. Secondly, SMEs are more flexible than large enterprises so they can respond to adverse action and take advantages from opportunities. Thirdly, they face several obstacles and risks that affect the development and growth for these enterprises. As we will see in the literature review, the financial aspects are the major barriers they have faced. Due to the importance of SMEs to the economy since the Palestinian economy needs to grow and develop, especially in the productive sectors. We need to create a supportive system and clear strategy that includes the government; banking sector and other institutions in order to create a suitable environment that enable them to obtain the necessary funds that will activate their role.

2.2 Palestinian economy

The Palestinian economy has passed through several stages, we notice that after the establishment of the Palestinian National Authority, the Palestinian economy has experienced a recovery in several aspects where income rose by 6% and unemployment levels fell by 3.5%. In that time, the SMEs form 92% from Palestinian enterprises they had simple and undeveloped structure and produced basic consumer goods. Nevertheless, the Palestinian economy is suffering from inherent weakness as a result of the Israeli occupation. Despite these conditions the Palestinian economy continues to operate because of the aids they have received from donors. The total Palestinian GDP was 6,797.3 million dollar in 2012 grew by 5.9% than 2011, the services sector contributes to 68% of the GDP and the total number of employees was 858 in 2012 grew by 2.5% compared with 2011 but the number of unemployment rate increases to 23% (Palestinian central bureau of statistics) (UNCTAD, 2004).

In a study conducted by D. Sabri he has summarized the most dynamic problems of the Palestinian economy, one of them is the closure policies and crossing points which impede the movement of goods and workers. The second problem is the lack of infrastructure and the use of outdated technology which increase total costs. Third, most raw materials are imported and controlled by the Israelis. The fourth one is the financial aspects where the majority of enterprises use the outstanding account with high interest rate. The last but not least is the inflexibility of the credit financing because of the warranties and guarantees requested by banks (Sabri, 1999).

2.3 SMEs definition

Small and medium are words with concepts differ from one country to another; the SMEs definition also differs across countries as a result of the variation in the criteria used to define it. However, the most common variables used are the number of employees, net assets and the productions and sales level. The reasons behind the definition differences are the countries and business cultural, population, industry and the economic. Therefore, when we compare developed and developing countries we will notice that there is a difference in the definition and criteria used (Thorsten & Demirgüç, 2003).

International Finance Corporation (IFC) defined SMEs as a registered business with less than 250 employees. These enterprises contribute heavily to employment and GDP; they also grow in ways linked to the formalization of an economy. Often SMEs have great difficulty accessing financial services in many emerging markets (IFC, 2011). According to the European Commission, SMEs definition has derived from three elements which are; the number of employees, the financial year, net turn over and the balance sheet total (EC, 2012).

Size and capital

In a study conducted by the Palestinian Ministry of Economy it defines small enterprises as projects that have 6-15 workers and the capital that invested in fixed assets is less than \$ 15,000. The medium is a project that employs 15 -50 workers and invests from \$15000 to \$25000 in fixed assets (Alsos, 2010). According to the PMA SMEs are enterprises staffed by less than 25 employees, their annual sales not exceeding seven million dollars or equivalent (PMA, 2013).

Characteristics

Despite that SMEs differ from state to state, they share common characteristics summarized in six points:

1. SMEs are often a sole proprietorship or family business.
2. They have simple structures since they are managed directly by the owners.
3. The simplicity of their products and quality levels where they use simple technology and non qualified workers. Therefore, they offer low prices.
4. They have limited production levels, which help them to adopt with market changes.
5. SMEs are easily established in terms of the capital since they rely on the individuals' savings.
6. SMES are financially more constraint than large companies and have less access to finance which is the major obstacle they face (Beck & Demirguc, 2006)(Lu & Beamish, 2001).

2.4 SMEs in Palestine

A study conducted by the UNICTAD shows that 92 % of the SMEs in Palestine are small which accounted for 76% of workforce, 71% of total value added, 69 %of total output and 68 %of total employment (UNICTAD, 2004).

Size

According to the 2012 establishments' census the total number of establishments in Palestine were 151,066 with an increase by 19% compared to 2007 census,102,344 of them located in west bank and 48,722in Gaza strip. The census indicate that 89% are small with less than 5 employees, 9.9 % are medium enterprises that have 5-19 employees and 1.1 % have 20 employees or over(PCBS, 2012).

Location

The geographic distribution of establishment shows that two thirds of them are in the West bank, 21.3 % of enterprises are concentrated in Hebron followed by Nablus then Ramallah and Jenin with 16.1%, 14% and 12.3% respectively (PCBS, 2012).

Ownership

The Palestinian establishments are dominant by the private sector by 90.8% (PCBS, 2012). Also we found that most SMEs in Palestine are family business managed directly by the owner and transmitted to their offspring.

Distribution

SMEs distribution in Palestinian economic sectors shows that wholesale, retail and repairs represent 51.1%, followed by the manufacturing 12.4%, services activities come in the third place by 11.1% ,then the food sector accounted for 4.8% ,health activities 4.0%, education activities 3.9 ,and the rest is distributed to other sectors (PCBS, 2012).

2.5 SMEs role in the society development

SMEs play a critical role in the economic growth and self-sufficiency in various aspects, as we see SMEs contribute to a fair income distribution by employing unqualified employees since on the one hand; their wages are less than qualified ones and their abilities usually do not allow them to give high wages on the other hand. SMEs also provide low prices local products and services by the exploitation of domestic resources to meet the Palestinian society needs and reduce the Israeli dependency. It is noticeable that the majority of entrepreneurship and the literal and professional projects are small and medium, these projects create innovative products and services and respond to the consumer needs (عطياني و الحاج علي, 2009) (Rothwell & Zegveld, 1982).

2.6 Problems that SMEs facing

SMEs in Palestine face several difficulties and barriers, at the outset the Palestinian economy is suffering from instability which increases the risks due to the difficulty of predicting the future and the inaccuracy of the financial and accounting data. Nevertheless, the majority of SMEs begin working based on family experiences without performing a feasibility study. The lack of necessary infrastructure and the absence of clear legal and legislative environment are another problem that increases the start up and the production costs. Moreover, the crossings problems that we mentioned about it above lead to increases the raw materials costs and to impair the ability to export (Abdel karem,). The taxes system in Palestine has many problem and need to be changed also the absence of local Palestinian currency affect SMEs development. Doing business in Palestine is not easy because Palestinian economic is complex, the world bank ranked the economies on their easy of doing business from 1 to 189, in the 2013 survey Palestine ranked 138 (Sabri, 2010).

Palestine rank in easy of doing business index

Easy of doing business rank	Starting a business	Dealing with constructing permit	Getting electricity	Registration property	Getting credit	Protecting investors	paying taxes	Trading across borders	Enforcing contract	Resolving insolvency
138	153	131	87	122	165	80	62	123	88	198

Source: World Bank (2013), doing business (2013) available online at www.doingbusiness.org/rankings

The financial aspect is the major obstacle that SMEs is faced; there are two reasons that restrict the growth and continuity for them. The first reason is the limited capital they have since SMEs owners usually depend on their personal savings which in many cases inadequate. Second, it is difficult to obtain the needed funding and concessional loans from financial institutions. The financial side effects include the lack of the required inputs on time and the depending on unqualified employees and simple technology. For that they resort to borrowing from financial institutions at high interest rates, or by trade credit which means buying on debt for specific time period from suppliers at high interest rates (Beck & Demirguc, 2006).

The social aspect also has an impact on the SMEs development as consumers often prefer foreign products because they believe that they have higher quality; the government and media role here is to encourage the local production and promote them. As we have found, the family business in Palestine form the majority of SMEs while the large firms are non-family business, when we compare the management performance between family and non-family business we will notice that non family are better and have higher profit than family business they also can access finance more easily. The main problem that has faced family businesses is the management conflict between family members particularly, in the third generation, as long as the founding father is still in job the business remains on control, but the problems begin at his death when the management transmitted to his children. Then, any conflict on management or profit sharing will lead in many cases to business liquidation in order to divide the shares among members (Sabri, 2008).

2.7 How to develop the Palestinian SMEs

SMEs are the engine of the economy; these businesses have greater opportunities to grow when the environment encourages them so we have to look at them as an essential sector in the economy that create an effective system which involve all related parties (Toleston & Asli, 2006). From a financial point, we can encourage SMEs by providing them the necessary financial support for capital financing which will accomplished by encouraging the banking sector to first, finance them at low interest rates. Second, grants some privileges. Third, reduce the required guarantees. Also there must be a role for lending institutions to provide loans to SMEs under concessional terms. The financial institution role should not be limited to provide the fund only but also help them to reach a suitable level which enables them to compete in the market. We should not forget the importance of training and development which also requires financing (Boocock & Shariff, 2005) (Valverde & Fernandez & Udell, 2009).

Government plays a significant role to SMEs development sometimes its role is most important and powerful than banking sector role. Banks request collateral to ensure repayment as they are profit corporations aim to earn profit. But when government provides a suitable environment and setting effective policy that supports the SMEs growth and progress by granting those taxes exemptions and incentives, also by facilitating the registration procedure and providing the necessary infrastructure in addition to the enactment of laws and regulations for commercial disputes. The government can stimulate banks by different ways, it can offer them tax exemptions on the profits that generated from SMEs supportive activities or by establishing a guarantee funds for SMEs loans to reduce the risks. Finally government can set up special lending institutions for SMEs to purchase the needed machinery and equipment on favorable terms and low interest. These facilities will reduce the lending risks which encourage financial institution to facilitate their procedures (عطيانى و الحاج) 2009, (abdelkarem, 2010).

2.8 SMEs and the banking sector in Palestine

The Palestinian banking sector consists of 17 banks with 232 branches and offices, 7 of them are local banks and 9 are Arab banks. Further, there is only one foreign bank which is the HSBC. The total number of commercial banks is 15 banks, the rest are Islamic banks (association of banks in Palestine). Banking system plays an important role in the community since they provide several services for individuals and institutions so as to facilitate their business and trade. Each bank has his own policy, but they subject to the PMA instructions and adopt a general policy that Commensurate between the credit, capital and business. If we look at the Palestinian banks, we can find that there is a gap between the value of deposits, amounting 95% and loans which did not exceed 32% in 2009 (عبد الكريم, 2010).

Each project needs financing in all its life stages in order to achieve the needed goals and objectives. The funding sources are either informal such as personal savings or formal ways from financial institutions. Banks often refrain from financing SMEs to avoid the risk of nonperforming loans in case of failures. These risks can be reduced by following certain actions. Firstly, they can develop special banking products and programs for SMEs. Secondly, setting particular credit policy aimed to liquidity, profitability and safety by analyzing the financial and credit condition. Thirdly, establish a special department to follow-up with SMEs and provide advisory services which will reduce the likelihood of failure. Fourthly, cooperate with other institutions, whether governmental, non-profit or private to provide a common platform for these enterprises. Finally, the SMEs loans should be secured by one of the of the guarantee funds (wall street journal, 2013) (Valverde & Fernandez & Udell, 2009).

According to Sabri, there are three financing sources available for private sector in Palestine; the primary source is the internal fund which includes paid in capital, retained earnings and the reserves followed by the credit payment. The last source is bank loans that accounted for only 8% of the financing sources which considered low percent needs to raise since in many cases the lack of financing lead to business liquidate (sabri, 2008).

In April 2013, the PMA issued circular 53/2013 entitled developing and enhancing lending opportunities for SMEs to adopt a definition of SMEs by depending on two criteria, the number of workers that not exceeding 25 workers, the annual sales volume does not exceed seven million dollars. The circular issued based on the fourth Banking Conference results that aim to enable SMEs to reach the necessary funding, also to motivate financial institutions to grant them the needed credit through two recommendations.

First: Exempt all SMEs that are working in Palestine from the requirement to make advanced cash payment amounting to 10% of debt for one time under certain conditions, including that the loans should be guaranteed by not less than 60% from acceptable guarantee funds.

Second: Exempt the Palestinian banks from 1.5% of the required risk reserve from SMEs credits under the same conditions in the first point (PMA, 2013).

In a study conducted by D. Abdel karem he has found that 62% of SMEs need financing. The personal contributions formed 87.1% from total financing, while the loans accounted for 8.2%. This indicates that the role of banking system is not effective because they pursued a complex lending policy. He also points that the business owners prefer to finance their projects from their private funds. The second option is the short-term loans followed by the long-term loans, and the last option is the entry of new partners (Abdel karem, 2010).

2.9 Credit risks that related to SMEs

The financial institutions refrain from financing SMEs because there are many types of risks associated with them come from internal and external factors. The external factors include political, economic and natural disasters and unfortunately these risks can't be controlled. The internal risks are related usually to the firm itself. In fact, we cannot ignore these risks but fortunately they can be controlled and avoided or mitigated.

Type of internal risks:

- Managerial risks that are related to the manager of the firm, number of managers, qualification and experience, organization structure.
- Production risks particularly in manufacturing sector and the type of technologies they used beside the quality.
- Supplier risks related to the number of supplier and if the firm depends on one supplier beside the purchase policy.
- Payment risks: to avoid nonoperational loans.
- Guarantees risks, the types, values and quality of the collaterals and the ability to liquidate it.
- Financial risks by analyzing the financial position of the firm.
- Currency exchange risks if the firm depend on import and deal with more than one currency.
- Operational risks which related to the internal control system and the fraud.
- Market and competition risks, the firms market share and the competitors in the market in addition to market conditions that affected the firm.
- Technological risks which important when the firm need update technology.

(Dietsch & Petey, 2002) (Altman & Sabato, 2007).

2.10 Palestinian institution that support the SMEs

There are several formal and informal institutions that support SMEs in Palestine. In this section we will address some of these institutions and their role in the SMEs development.

1. The ministry of national economy

The Ministry providing several services to help developing the local economy and improving the productive sectors. It also protects businesses and creates new job opportunities. Further, it places and applies policies and laws in order to achieve stability and economic efficiency. In 1992, the ministry approved the Investment Promotion Law, which accordingly the Palestinian investment promotion agency was established in order to apply the law by attracting investment and providing them with needed services, the agency facilitates the communication between public and private sectors by providing the necessary information and licenses in addition to giving incentives exemptions for investment. Its activities are concentrated on three key areas which are; providing guarantees to investors then offering them incentives and finally, creating a suitable investment environment. In addition to the three major activates, the agency also designs programs to finance small profitable projects and non-profitable housing projects.

In 2008 the agency established a government program to support small enterprises by providing interest-free loans in cooperation with several banks to developing existing projects and financing and support new projects, which in turn will create economic activities and jobs opportunities that will decrease poverty levels (Palestinian investment promotion agency, The investment promotion law (1) (1992)).

2. Palestinian standards institution

The institution established in 1994 to apply the Standards and Metrology Law (6) (2000), it aims to builds and develops international specifications and standards in several areas though cooperation with local and regional institutions to develop infrastructure. They provide inspection services, incentives and promotion to the Palestinian enterprises. The Palestinian standards institution activities are important to increase consumer awareness, and improve the quality to comply with the specifications that will enable them to compete they are also working on the rehabilitation of many factories, whether small or large. (Palestinian standards institution, Standards and Metrology Law (6) (2000)).

3. Palestinian federation of industries

The PFI is a national institution was found in 1999 as a private sector to represent the industry sector at a local and international level. They follow a strategy that aimed to develop and support the Palestinian industrial enterprises by providing several services to the members that help them to achieve their goals. The Palestinian industrial sector includes more than 14000 registered enterprises in West Bank and Gaza. The family businesses form the majority of these enterprises. The contribution of industry sector in GDP is 17% and absorbs around 17% of the total work force.

PFI focuses on four major projects. The first one is to improve the social and economic conditions of the Palestinian women in Bethlehem Area. The second one is The Industrial Rehabilitation Project. The third is related to bar coding. And the fourth, Small and Medium Industrial Enterprises Rehabilitation Program which aims to provide loans from €100,000 to € 500,000to industrial sector with cooperation between ministry of national economy and the Italian government, this project requires the beneficiaries to purchase Italian machines to develop their business (Palestinian federation of industries).

4. Palestinian investment fund

PIF runs several projects to support SMEs under SHARAKAT fund which include all PIF activities related to SMEs by financing new and existing projects and loans guarantee. SHARAKAT fund fo-

cuses on existing projects in Palestine that their market value less than 20 million dollar in addition to new projects that have promising plane. These projects have to match several conditions that are:

1. Legal and registered firm.
2. Have the ability to growth.
3. Have experts and management team.
4. Using new technologies and mechanisms.
5. Organization structure.
6. The ability to finish the loan within five years.
7. The minimum return on investment should be 10 %(PIF).

5. Bank of Palestine

To see the banking sector role in the SMEs development, Bank of Palestine has been selected as a sample. Bank of Palestine is a national bank established in 1960. The bank has 48 branches in Palestine and employees more than 1200 employees, the market share of BOP is 23% of the deposits and loans, The bank plays an active role in the SMEs and micro finance, this section focuses on the programs that were offered by the bank to these institutions.

Bank of Palestine designed SMEs financing program to support the productive projects through developing the existing projects and established a new one. This program provides loans with a grace period and concessional terms, the loans value Commensurate with the project size and revenues or 85% of the purchased goods or equipments. There are several types of credit programs addressed to this category which includes the banks' loans and foreign agreements programs that belong to foreign agreements, these programs are dedicated to specific purposes, for example, Italian loans are intended to support SMEs through financing the purchase of Italian machines, equipments and services.

2.11 Conclusion

After reviewing previous studies, the researcher finds that nearly all studies have emphasized the importance of SMEs and their active role in economy as they accounted for more than 90% from all enterprises in most countries which mean that any hit or recovery in this sector will reflect on the economy. Therefore, we cannot overlook their problems, especially the financial aspect which is the major obstacle they face that impede their growth. SMEs development cannot be achieved from one party. Instead it needs a joint effort from all relevant parties in order to set effective strategy that will empower the role of these institutions in the community, and also to give them growth and development opportunity. The role of financial institutions in this strategy is to facilitate the process for obtaining the necessary fund, which in turn will positively reflect all aspects in the economy and society.

CHAPTER THREE
METHODOLOGY

3. Methodology

3.1 To measure the objectives of the study through designing sectional descriptive study.

3.2 Population and sample

The population of this study is defined according to PMA circular 53/2013 to adopt a definition of SMEs based on two criteria, the number of employees that not exceeding 25 workers, and also their annual sales volume which do not exceed seven million dollars or equivalent. The researcher has selected a sample of 40 SMEs though following a simple random sample selection method in selecting the sample members; the sample includes four sectors which is services, trading, restaurants in addition to industry and textiles.

3.3 Data collection

To accomplish the purpose of the study, The researcher depends on two types of data; Secondary data, through conducting a literature review for number of books, journals, readings & internet sites that were conducted about this topic, and Primary data through designing a survey that is attributed to the study .Furthermore, through interviewing credit department at Bank of Palestine and with selected SMEs in various sectors in Palestine.

Sample Distribution

	Distribution
Field	15.0% restaurants, 2.5% textiles, 27.5% trading, 20.0% industry and 35.0% services.
Number of employees	90.3 % less than 15 employees, 9.7% from 15 to 25 employees.
Ownership	37.5% family business, 30% sole proprietorship, 22% partnership, 10% other.
Education level of the owner	15.0% high school or lower, 12.5% Diploma, 42.5% BA degree, 30.0% post graduate.
Advanced technology	42.5 yes, 57.5 no
Organization structure	42.5 yes,57.5 no
(\$)Annual sales	70% less than one million, 12.5% from 1 to less than 3 million, 5.0% from 3 to 5 million,2.5% from 5 to less than 7 million.

3.4 Questionnaire Design

The questionnaire was divided into five sections. The first section is the demographic information that includes general information about the firm; the second one contains Yes\ No questions since it aims to find out. In Section three, respondents ranked the constraints that have impact on the success and continuation of their business. Section four is a 5-point Likert scale, in which 1 = strongly agree and 5 = strongly disagree with 15 statements .In section five, the respondents ranked the most priority banking services that need further facilitation. The last section includes open question.

3.5 Validity and Reliability Analysis

A planned questionnaire was designed for achieving the goals of this study.In order to ensure its validity credit manager and sub-branch manager at Bank of Palestine in addition to course professor have checked the instrument and its content to give their opinion. Cronbach alpha was found to be .656 suggesting satisfactory internal consistency among items.

Reliability Statistics	
Cronbach's Alpha	N of Items
.644.	15

3.6 Analytical Tools

The questionnaires returned back from customers and then the results were analyzed by SPSS program V20 to set reasonable conclusions and recommendations related to the study.

3.7 Limitations

1. This study was conducted with SMEs customers at one particular bank (bank of Palestine), so we cannot compare the results among banks in order to compare between customers opinion.
2. Some applicants didn't give very accurate answers that were provided in the questionnaire specially the financial issues.
3. There are no formal or published lists that illustrate the number of small and medium-sized compared with large companies at the Bank of Palestine in order to analyze the difference between them.

CHAPTER FOUR
FINDING AND ANALYSIS

4. Data analysis

4.1 What are the facilities that banking sector can provide to SMEs?

One of the research objectives is to find out the facilities that banks can provide to SMEs, the majority of applicants assume that they need more facilities in most banking services where they remark that most banking services are not flexible and need some simplification, Particularly loans and overdraft which considered complex in terms of the required guarantees and interest rate. About 32% lacks the assets to meet loan collateral requirements beside 75 % found that the interest rate is high. Around 65% couldn't receive a loan because of banks procedures which they consider complex; they also need more facilities to cover checks.

Applicants have been asked to rank the banking services that need more facilities terms of importance to their business, they consider that cover checks are the most important service where most SMEs owners work on checks not cash. However, in some cases they suffer from inadequate funding to cover it or to pay their daily obligations. Loans come in second place where they believe that the lending procedures are complex, in most cases it is the only fund source so if SMEs owners cannot received the loan, they may liquidate the business. The third position is the overdraft which allows them to cover checks or withdrawal to specific limit which help them to pay their daily obligation. Transfers beside credit and warranty come in the last place. They are important for enterprises that imported from abroad.

4.2 What are the roles that banking sector played in the development of SMEs?

The researcher finds that banks role should not be limited to provide loans but also it should follows up with these institutions and cooperate with institutions that provide consulting and training services to business owners who get loans from the bank. They ask banks to provide financing programs as needed. In which if the purpose of the loan to buy equipment the program should be dedicated to provide equipment at lower prices.

Through the interview with the Department of credit and loans, we found that Bank of Palestine designed SMEs financing program to provide loans with a grace period and concessional terms support the productive projects through several credit programs, the first type is the banks loans for example:

- Green Loans Program, that aims to fund environmentally friendly projects to encourage customers to optimize the use of natural resources and recycling.

The micro projects financing loans to finance working capital and fixed assets for micro productive projects.

- Fishermen loans and others.

The second type is the. The foreign party supports these loans when tripping. This support encourages banks to provide concessional loans and reduce the required guarantees, such as:

- Italian loans that signed between the Italian Foreign Ministry and the Palestine Liberation Organization. Through this agreement, the Palestinian banks provide maximum 5 years concessional loans with one year grace period to SMEs from 50 to 500 thousand euro at 5 % interest rate. The total value of these loans is 25 million euro. This program aims to support SMEs through financing the purchase of Italian machines, equipments and services to develop the production lines in food and services industries.70% of the loan value should used to import Italian equipment, and the rest can be used to purchase non Italian or to cover other costs.

- French development loans which are agreements between Bank of Palestine and the French government. The agreement energizes the SMEs loans with non specific period and value at 5%

interest rate on dollar and 6% on euro to support the Palestinian SMEs and create job opportunities.

German operational loans that signed in 9th September 2009 between Bank of Palestine and the European credit guarantee fund which funded from three parties the European commission, the European investment bank and the Republic of Germany through the German Development Bank to guarantee loans risks. The loan values should not exceed \$100,000 with 9 % interest rate in addition to 1% loan fee and 1% loan managing fee. The loan term should not exceed 3 years to finance fixed assets or investments and 5 years to finance working capital.

- French grant loans, under this agreement the French government provides aid to the Palestinian private sector in order to finance the purchase of materials and equipment. The agreement focuses on the development of industrial, agricultural, tourism and services sectors. The beneficiary firms have to use French materials and equipment.

4.3 What is the common strategy that must be set by the government with the banking sector to develop SMEs?

The majority believe that the government role to support SMEs is more important than the banking sector role. First, the taxes system do not support or spur entrepreneurs and business owners so it needs some modifications. Second, they claimed that SMEs does not receive government incentives that facilitate their development and growth. Third, Business owners emphasized the importance of judicial courts where the absence of it increases the complexity of commercial disputes. Fourth, the majority said that the government facilities don't support SMEs access to fund sources.

4.4 What are the Consequences that SMEs faces?

Applicants have been asked to rank constraints according to the degree of their impact on their business success and continuation; they consider that economic instability is the most barriers the facing in which it affect all aspect in the business. Second, they believe that the lack of funds sources have a great impact on the business development and growth and in many cases lead to liquidation. This is what most researcher indicate in their in their articles. For example, Beck & Demirguc said in their article that SMES have difficulty to obtain the needed funding and concessional loans from financial institutions which lead to lack of the required inputs on time and limited capital to invest.

The government support and the taxes system come in the third and fourth place. They believe that the government role is more important than the banking sector role; also they said that the government did not support SMEs and provide incentives to them. In addition, they think that the taxes system needs some modifications and changes, the majority claimed that they did not receive taxes incentives or exemption. Dr sabri in his article "MSMEs in Palestinian; challenges and potential" talked about his opinion in the said effect of the Palestinian taxes systems.

Arabs usually prefer foreign products because they believe that they have higher quality which comes in the fifth place. SMES owners think that the Israeli and foreign competition form a challenge to their business. The government should support local products by different methods and convince customers to support local products. Although the crossing problem comes in the last place but it has a great impact on the overall Palestinian economy, it leads to an increases in the cost and time of input which causes a delay in the production.

5. Conclusions and recommendations

CHAPTER FIVE
**CONCLUSIONS
AND RECOMMENDATIONS**

Throughout this study the researcher finds the conclusions and recommendations mentioned below:

5.1 Conclusions

Throughout this study we can say that the government role is more significant than the banking sector role in the SMEs development. Moreover, the government support is inadequate in developing SMEs in addition to the taxes system that needs modification which means that SMEs needs more incentives and taxes exemption from the government.

This study shows that the banking procedures are characterized by complexity and need some flexibility regarding SMEs transaction as well as the loan guarantees are always difficult which complicate the borrowing process to obtain the needed funds. We also find that lack of funds and costumers preference of foreign products beside the government support and the economic conditions in Palestine are the most significant variables that affect SMEs development and growth. Therefore, the government and the banking sector have to cooperate together so as to solve their difficulties and facilitate the funding issue which enable them to grow and improve quality to compete with foreign products.

5.2 Recommendations

To develop SMEs we need to set an effective strategy which includes government, banking sector and other parties to support SMEs growth and progress. The government role is to facilitate the lending process through Stimulate banks by different ways; it can offer them tax exemptions on the profits that generated from SMEs supportive activities. In addition to provide taxes exemptions and a suitable environment that supports them. Furthermore, they have to set up special lending institutions for SMEs to purchase the needed machinery and equipment on favorable terms and low interest.

The banking sector role should not be limited in providing loans. In other words, to support SMEs they should establish a special department to follow-up with SMEs and provide advisory services by Cooperation with companies specialized in the field of training to assist business owners acquire the needed skills which will reduce the likelihood of failure.

Finally, future research may focus on the shared role between the government, banking sector, unions and agencies to develop a common strategy that can support the Palestinian SMEs.

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Appendix (1)



BIRZEIT UNIVERSITY

Lina Issam Mosallem

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I am currently conducting banking sector role in the SMEs development research for my Masters degree from Birzeit University “MBA program”. Where SMEs are enterprises staffed by less than 25 employees, their annual sales not exceeding seven million dollars or equivalent.

I would appreciate your cooperation by filling these sheets to give me your opinion about ho banking sector can contribute in the SMEs development and growth, all the information provided will be confidential and for research uses only where all my work will be under the supervision of Doctor “Nidal Sabri “.

Thank you in advance for your cooperation

Part 1: Demographics

1. Field (s) of activity

- a) Restaurants
- b) Textiles
- c) Trading.....
- d) Industry.....
- e) Services.....

2. Number of employees

- a) Less than 15
- b) From 15 to 25

3. Type of ownership

- a) Family business
- b) Sole proprietorship
- c) Partnership
- d) Other.....

4. Annual sales in dollar

- a) Less than one million
- b) 1-less than 3 million
- c) 3- less than 5 million
- d) 5-less than 7 million
- e) More than 7 million

5. Education level

- a) High School or lower
- b) Diploma
- c) B.A Degree
- d) Post Graduated education

- 1. Number of branches.....
- 2. Year established.....

Part 2: Yes or No questions

Yes no

1. The government provides facilities that support the development and growth for your enterprise.
2. The banking sector provides facilities that support the development and growth for your enterprise.
3. Did you receive a loan from a Palestinian bank?
4. If you received a loan you founded that the bank's procedures are simplified.
5. I/we started the business from my/ our personal fund/s.
6. Did you suffered from delay in receiving input due to lack of funding.
7. Your enterprise using modern technology.
8. Your enterprise has clear organization structure.
9. The enterprise owner is the manager.
10. The enterprise employs staff with simple expertise qualifications.

Part 3: Rank these constraints according to the degree of impact on the success and continuation of your business, where 1 is the most important and 7 is the least important.

Constraint	#
Lack of financing sources	
Lack of government facilities	
The crossings problems	
Preference of foreign products	
Economic instability	
The Palestinian taxes system	

Part 4: to what extent do you agree or disagree with the statements about SMEs.

	Strongly Disagree	Disagree	Neutral	Agree	Strongly Agree
I believe that the government facilitation is useful in supporting SMEs access to fund sources.					
I think that SMEs receive a government support that facilitates their development and growth.					
In my opinion, the government role to support SMEs is more important than the banking sector role.					
The absence of commercial courts makes increase the complexity and difficulty of commercial disputes.					
I think that there are several financing and lending programs dedicated to SMEs.					
I believe that the taxes system in Palestine supports SMEs , they receive taxes incentives and exemptions					
I think that the SMEs lending policies differ from bank to bank					
The financial problem are the major obstacle that SMEs facing.					
I believe that decrease the interest rate is more important that decrease the required collaterals.					
Your enterprise lacks of assets to meet loan collateral requirements.					
The banking sector role should not limit to provide loans but also to follow up with SMEs.					
The cooperation between banks and training & development institutions will contribute to improving the performance.					
I believe that SMEs banking services are flexible in terms of time and requirements.					
I think that borrowing from relatives better than borrowing from banks.					
I think that credit Trade better than banks loan.					

Part 5: What are the most priority banking services to your business, where 1 is the most important and 7 is the least important.

	1 Most important	2	3	4	5 Least Important
loans					
check cover					
overdraft					
Transfers					
credit and warranty					

Part 6: In order to support SMEs development there must be a joint plan between several parties, mainly the government and the banking sector, from your opinion what are the most important procedures that must be followed by the government and banking sector to support these SME.

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