Third Party Evaluator's Opinion on
Fund for Small and Medium Scale Industries

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Relevance

The conclusion that this project continues to be relevant remains basically sound. However, the Government has since launched the 9th Malaysia Plan, 2006-2010 (9MP) and the 3rd Industrial Master Plan, 2006-2020 (IMP3). While the 9MP seeks to create high performance and resilient SMEs, IMP3 also emphasizes their need to strengthen intra-firm linkages and participate in international supply chains. The new focus is for SMEs to adopt technology to raise efficiency and to harness their potential in services. For the first time, IMP3 stresses that financial support for SMEs should be market driven, based on performance. 5 strategic thrusts are set under IMP3 for SMEs in the next 15 years: (i) enhancing competitiveness; (ii) capitalizing on outward investment opportunities; (iii) driving growth through technology and innovation; (iv) instituting a more cohesive policy, regulatory and institutional framework; and (v) enhancing growth in the services sector. In particular, IMP3 pledges continuing financial support, including new and improved credit facilities by the SME bank. A Services Sector Development Fund for SMEs is being considered to help up-grade skills and professionalism. Commitment with its drive to deepen human resource development, the Government will ensure that SMEs have ready access to all forms of finance at reasonable cost, including extended trade finance, working capital and venture promotion. To be helpful, it may be worthwhile for the second generation fund to move increasingly towards providing more credit to SMEs in non-traditional areas to support their drive to actively participate in the globalization process, especially in services activities adding value in particular to tourism, health & education exports, integrated logistics and ICT.

Efficiency

The conclusions in the report are reasonable enough. While the problems listed are centered on the borrower, these were imposed (some unreasonably) by the lender. Standardization of SME definition has helped, while the use of 3 development banks acting as executing agencies has worked out reasonably well. Future assistance would be better placed at the new SME bank. Its holistic approach should make it more efficient in lending although it does need help to build capacity and capability. Future focus should include equity financing, extended working capital and trade finance, hire purchase, leasing & factoring, contract finance and guarantees all of which would require flexibility given rapidly changing circumstances, and evaluation based on commercial viability. While the listed reasons for delays are real, many borrowers find the lengthy loan process too bureaucratic, too time consuming and too demanding & inflexible for their needs. Disbursement conditions do not lend themselves to early compliance: e.g. many on the long list of conditions precedent cannot be readily met in practice; complex legalities often reflect lawyers' rather than bankers' concerns; and lack of sensitivity to real market conditions adversely affect efficient implementation. Both lenders and borrowers need to work at bridging this gap to reduce cost in doing business. The issue of credit concentration will be resolved with the new strategic direction under IMP3. In the end, borrowers will trade-off higher cost for greater credit access. To be helpful, working capital finance should be made more flexible and allow for broader coverage and adequate access to accommodate rapidly changing business conditions mostly beyond their control. New fund flows should be extended with greater sensitivity to borrowers' needs. Moves to strengthen credit management should reflect practicable realities, while project scope should be broadened, consistent with new initiatives under the National SME Blueprint, 2006.