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Barriers and Strategies of Financial Inclusion of SMEs: A Lender and Borrower Perspective of Khyber Pakhtunkhwa

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***Abstract*:** Fostering SMEs financial inclusion of is also one of the top priorities of State Bank of Pakistan and the Government of Pakistan. In this way, the State Bank of Pakistan has announced National Financial Inclusion Strategies (NIFS) under the banner of the NIFS 100days agenda in order to attain various targets including financial inclusion of SMEs by 2023. In this regard the research study is conducted to explore the barriers (demand and supply side) in the main stream of financial inclusion of Small and Medium-sized Enterprises (SMEs) and to provide comprehensive ways and strategies for greater financial inclusion. To fulfill the research aims, the research used a qualitative technique followed by thematic approach. Semi-structured interviews with SMEs and banks were used to acquire primary data. The report reveals a number of demand side constraints that SMEs encounter, such as financial illiteracy, lack of collateral, lack of financial statements, lack of information about accessible financial products and services, and many others; the supply side barriers are arise from financial institutions while supporting SMEs include lengthy and complex procedure, demand of collateral, high transaction costs, and so on and other constraints. These demand-sides, supply-sides and other sides' barriers contribute to SMEs' reluctance to participate with formal financial channels. In response to these impediments, the research developed a number of formal financial channels. In response to these barriers, the research established various strategies that incorporate both demand-side, supply-side factors in order to form a flourishing environment for SMEs' inclusion in formal financial system.

Key words: Financial Inclusion, SME's, Demand Side Barriers, Supply Side Barriers

1. Introduction

1.1 Background of the Study

Global economic and financial developments are going side by side. New concepts and reforms are introducing in these disciplines. Financial inclusion is another well-liked strategy for lowering market friction—which keeps markets from acting in the oppressed and impoverisher's best interests (Aduda & Kalunda, 2012). It has gained more currency after the introduction of UN Millennium Development Goals and then Sustainable Development Goals. United Nations (UN) set 17 various targets under Sustainable Development Goals to be achieved in 2030. The 8th goal is universal financial inclusion to attain the target of, eradicating poverty, promoting economic growth and decent jobs and supporting industry. Financial inclusion has been identified as an essential development priority by international and national governments (Alliance for Financial Inclusion, 2013; World Bank, 2013). It is the process by which all members of society have easy access to, and use of, financial products and services" (Sarma, 2008). In 2010, the G20 Toronto summit declaration established criteria for creative financial inclusion. Among these concepts include fostering financial literacy, as well as creating an institutional structure with clear lines of accountability and cooperation across government. Furthermore, in 2015, the United Nations General Assembly emphasized the importance of financial inclusion as a policy target in financial regulation in accordance with national agendas and legislation. Financial inclusion is the provision of a sufficient range of safe, convenient, and affordable financial products and services to disadvantaged and other vulnerable groups, such as low-income, rural, and undocumented individuals, and SMEs, who have been underserved or excluded from the formal financial sector (FATF, 2011). Financial inclusion strives to bring the "unbanked" people into the formal financial system so that they can receive credit and insurance as well as financial services including savings, payments, and transfers (Hannig and Jansen 2010). At the 2010 Millennium Development Goals Summit, these elements were combined to create the definition of financial inclusion, which is "universal access; at a reasonable cost; to a range of financial services for everyone in need, provided by a diverse range of sound and sustainable institutions" (Maxima, 2010). There are five main areas of the financial inclusion: Banking, credit, insurance, savings, and financial suggestion (Maxima 2010). It is basically all about availability, access and usage of financial services and products to both individuals and SMEs. Small and Medium Enterprises (SMEs) is playing an important role in economic development of a country. Many governments and development organizations have concentrated on promoting SMEs as a means of encouraging more people to participate in the private sector (Kushnir, 2010). SMEs account for 60-70 percent of jobs in most developed and developing nations, and numerous African countries have emphasized investment in SMEs to produce the majority of new jobs (Iddris, 2012).

In Pakistan, over five million SMEs account for around 90 percent of the country's enterprises, contributing 35 percent to GDP and more than 30 percent to export revenues. In fact, it is a crucial pillar of the national economy, employing over 40% workforce with diverse skills. These diverse businesses are involved in a wide range of industrial, commercial, and service operations. Textiles, leather, plastic, sports goods, handicraft, IT, building, materials, consumer products, horticulture, fisheries, jewels, healthcare, agricultural produce, and energy are among the numerous industries. (INTERNATIONAL THE NEWS). Small and Medium Enterprises Development Authority – SMEDA, a Premier Institution of the Government of Pakistan under the Ministry of Industries and Production, was founded in October 1998 to address the challenge of promoting Small and Medium Enterprises (SMEs) in Pakistan.. Despite too much importance of SMEs in overall development of the country, it remains excluded from the main stream of financial services and products. Various studies show that the majority of SMEs fail due to a lack of proper funding and financial services (Amyx, 2005). Despite rising recognition of the significance of SMEs for the creation of job and economic development, SMEs claim that lack of access to funding is one of the most significant hurdles to their expansion. In emerging markets, half of SMEs are credit limited. 70% of micro, small, and medium-sized firms (MSMEs) do not have access to external funding, while another 15% are under-financed (IFC, 2013). All of this adds up to an estimated $2 trillion credit gap. Similarly, in Pakistan the state of SMEs in the mainstream of financial inclusion is not up to the mark. Commercial banks and other financing institutions fail to adequately and effectively disseminate the several funding schemes introduced by SBP. It includes a variety of subsidized loans and credits for SMEs, such as a refinance scheme to meet working capital requirements, a credit guarantee scheme for small and rural enterprises, an export finance scheme, a refinance facility for SMEs to modernize, a long-term financing facility for plant machinery, an agriculture credit scheme, financing for agricultural produce storage, and recently introduced financing for renewable energy (wind and solar). The SBP has established a refinance and credit guarantee initiative aimed specifically at women entrepreneurs. Under this initiative, SBP will give commercial banks with interest-free funding, and women entrepreneurs would be able to borrow up to Rs5 million over a five-year period. The Prime Minister's interest-free Youth Loan Scheme is offered for youth-owned enterprises and other similar ventures. To mitigate the negative effects of the COVID-19 and lockdowns, the government recently launched an economic stimulus plan, with an emphasis on SMEs. Recently, during COVID-19, State Bank of Pakistan (SBP), in support of Asian Development Bank (ADB) has provided Rs1.3 trillion relief packages to the industries and the SMEs but it remained under-utilized due to the issue of financial inclusion. Therefore, SMEs' financial inclusion is also the main objectives under NIFS 100 days agenda issued by state bank of Pakistan. In Pakistan limited studies are available highlighting the barriers in financial inclusion of SMEs. In addition established strategies to address the issue of financial inclusion of SMEs. The study is conducted to add the present body of literature to fill the gap.

1.2 Research Problem Statement

Both SMEs and Financial inclusion have a decisive role in socio-economic growth and development of a country. In Pakistan, SMEs contribute 40 to GDP, 40pc to export 80pc to non-agricultural employment and 35pc to total value addition. Despite, too much vitality, the sector is lag behind in the main stream of financial inclusion. State bank Pakistan 2020 report shows that SMEs share in overall loans to private sector is low i.e. 7.74pc however the target was 17 pc by year 2023.

Moreover, of 3.2 million SMEs in the country, approximately 188,000 have banks outstanding loan. Recently, during COVID-19, State Bank of Pakistan (SBP), in support of Asian Development Bank (ADB) has provided Rs1.3 trillion relief packages to industries and SMEs but it remained underutilized. All of the above missing targets were due to low financial inclusion of SMEs. Therefore, financial inclusion of SMEs is one of the top priorities of SBP and government of Pakistan. In this regard State Bank of Pakistan has issued National Financial Inclusion Strategies (NIFS) under the flagship of NIFS 100 days agenda to achieve various targets by 2023. One of them is financial inclusion of small and medium enterprises (SMEs) in Pakistan. Similarly, "Pakistan Vision 2025", the long-term development plan aims to achieve "sustainable, inherent, inclusive growth" and "private sector-led growth".

In fact, this topic is the top priority of SBP (NIFS 100 days agenda and Pakistan Vision 2025). However, limited literature is available in Pakistan on exploring the factors effecting financial inclusion of SMEs, strategies that smoothen the way for greater financial inclusion of SMEs. Thus, it is high time to conduct a study in order to explore the constraints of SMEs' financial inclusion and suggest various promising strategies for address these constraints. This study will serve as a foundation for the development of successful financial inclusion frameworks, policies, and initiatives throughout the country.

1.3 Research Objectives

i. To explore the barriers of financial inclusion of SMEs in Pakistan
ii. To develop the strategies that address the issues of SMEs' financial inclusion in Pakistan

1.4 Research Questions

i. What are the barriers of financial inclusion of SMEs in Pakistan?
ii. What are the strategies that address the issues of SMEs' financial inclusion in Pakistan?

1.5 Purpose and Significance of the Research

The goal of this research is to figure out the causes of dwindling SME growth. The study revealed that, improving the financial inclusion of small and medium-sized enterprises (SMEs) in developing nations is a crucial approach to mitigating poverty, expanding job prospects, and fostering economic expansion and advancement. In Pakistan as well as most other emerging nations, one issue that has received little attention is SMEs financial inclusion stimulation. Since SMEs are crucial to a nation's socioeconomic development (Morgan & Pontines, 2014). As a result, the Government of Pakistan and SBP released several policies and assistance initiatives like NFIS 100days agenda and Vision Pakistan 2025 to include SMEs in the mainstream of financial inclusion.

Pakistan is currently facing socio-economic issues ranging poverty (39%), unemployment, a illiquidity and high debts of about US$ 122 billion (World Bank 2020). To tackle these issues financial inclusion of SMEs is imperative. By identifying the constraints of SMEs' financial inclusion will aid to the policy makers and other stake holders to devise strategies and policies for grater inclusion of the sector. It is also pertinent to note that this study will gain the attention SMEs owners and managers regarding the consequences of financial inclusion on firm's performance. In this way they will strive for financial inclusion and SMEs sector is transforming from informal to formal sector of the economy.

Thus, in the light of this study government and SBP will formulate strategies and policies in order to achieve the targets of NIFS100 day's agenda and of Vision Pakistan 2025.

1.6 Contributions of the Study

The study has both theoretical and contextual contribution to existing literature on financial inclusion/exclusion with respect to SMEs. For the first time an exploratory study will be conducted in Pakistan to explore the factors affecting financial inclusion of SMEs and establishing strategies for greater financial inclusion.

2. Literature Review

2.1 Theoretical Background

The underlining theories of the study are: theory of financial growth perspective, financial inclusion theories, free market model (FMM) and theory of asymmetric information.

2.2 Empirical Studies

2.2.1 Concept of Financial Inclusion

Oruo (2013)'s definition of financial inclusion is utilized to operationalize the concept of financial exclusion. As a result, it is regarded as an individual's ability to gain access to and use fundamental financial services. Savings, loans, and insurance are examples of such services that are reasonably convenient, dependable, and versatile in terms of access and design. The traditional concept of financial inclusion, according to Nwanko and Nwanko (2014), is the provision of access to and utilization of diverse, easy, and inexpensive financial services. Access to the utilization of financial services is a fundamental driver of economic growth. Financial inclusion refers to long-term, relevant, cost-effective, and meaningful financial services for the disadvantaged population, particularly rural people. Financial inclusion, as defined by the World Bank (2012), is the range, quality, and availability of financial services to the underserved and financially excluded.

According to FATF (2011), financial inclusion is giving the underprivileged and vulnerable groups, such as low-income, rural, and undocumented individuals, access to sufficient range of safe, convenient, and affordable financial services. On the other side, it is also about providing a greater range of financial services to consumers who today only have access to basic financial items. Financial inclusion, according to the Centre for Financial Inclusion (2013), is defined as a situation in which all people who can use financial services have access to a complement of quality financial services that are delivered at cheap costs, in a convenient manner, and with dignity for the clients.

2.2.2 Challenges of Financial Inclusion

According to Pallavi and Bharti (2013), the following are main causes of financial exclusion:1) High cost: Providing and utilizing financial services is not free for both the service provider and the service user. (i) Service provider costs: Establishing branches in rural locations is often not advantageous due to high costs and poor business. (ii) Service user cost: It has been noticed that the poor in rural areas are hesitant to use these services due to high costs, such as minimum balance requirements in savings accounts, fixed charges in credit cards and debit cards, loan processing charges, and so on. 2) Non-monetary barriers: Access to formal financial sources necessitates paperwork proving a person's identification, postal address, income, and so on. Poor people, in general, lack these documentation and are consequently denied financial services.

According to the World Bank (2012), more than half of the world's poor adults do not have a bank account, leaving them exposed to loss, theft, and exploitation. More than half of the world's population, particularly those living in rural areas, have difficulties to accessing banking and other financial services due to bureaucracy, travel distance, and cost. Similarly, Ibeachu (2010), as referenced in Onaolapo and Odetayo (2012), identified six categories of financial exclusion: (i) Physical access exclusion: According to them, this is caused by the closure of local banks or building societies, as well as a lack of dependable transportation to reach alternatives. (ii)Access exclusion: This sort of access is limited through risk assessment, with persons being denied a product or service because they are deemed high risks.(iii) Condition exclusion: When conditions are linked to items or services, they become inaccessible to some people. (iv) Price exclusion: This occurs when things are available but at an unaffordable price. (v) Marketing exclusion, in which sales and marketing efforts are directed at specific groups or places at the expense of others. (vi) Self-exclusion occurs when people do not seek financial products and services for a variety of reasons, such as fear of failure, fear of temptation, or a lack of awareness.

2.2.3 Small and Medium Enterprises (SMES)

SMEs are defined differently by each country. SMEs are classified by the World Bank as businesses within a maximum of 300 employees, $15 million in annual sales, and $15 million in assets. According to the Inter-American Development Bank, SMEs have a maximum of 100 employees and less than $3 million in revenue.
Similarly, there is no clear definition of SMEs in Pakistan. SMEs are defined differently by different agencies like; SME Bank, Small and Medium Enterprises Development Authority (SMEDA), Federal Board of Revenue (FBR), and SBP etc. The criteria employed in their definitions differ amongst companies, with SME Bank, for example, citing only total number of assets as the criterion that is total assets up-to Rs20 million is small and up-to Rs 100 million is medium, while SMEDA and SBP set both number of employees and annual sales as criteria for SMEs. According to State Bank of Pakistan the number of employees up to 50 is small while employees 51-250 with annual turnover of Rs150-800 million are SMES. As for SMEDA employees up to 250 and annual turnover up to PKR 250 million are SMES.

2.2.4 Financial Inclusion and SMEs

Garang (2014) looked into how the growth of the financial sector affected SMEs' access to financing in Kenya. The results showed that financial inclusion significantly affects the expansion and improvement of SMEs. Ndege (2012) studied the correlation between Kenya's economic growth and the deepening of the financial sector and found that the two were positively correlated. The World Bank (2018) highlights the benefits of policy reforms aimed at supporting the growth of SMEs by establishing credit bureaus across the country, which would promote citizens' financial inclusion. According to Beck and Cull (2014), financial inclusion is important for the growth of SMEs in Sub-Saharan Africa. According to Bassey Ina Ibor Amenawo Ikpa Offiong and Enyeokpon Samuel Mendie (2017), financial inclusion and the growth of micro, small, and medium-sized firms in Nigeria have a substantial relationship.

3. Research Methodology

3.1 Introduction

Research technique, according to Silverman (1998), "is a general approach to studying a research topic that establishes how to go about studying any phenomenon and how the research should be designed."

3.1.1 Research Design

Research design or research strategy is an approach for answering a series of questions (McCombes, 2019). It is a framework for collecting, evaluating, and interpreting data that includes many techniques and protocols. Qualitative method will be used whereby a researcher first conduct interviews and then develop the themes from the transcribed interviews. Qualitative technique and primary data will be used. Data collection method is interviews by exploring the barriers in the main stream of SMEs' financial inclusion and established strategies to address these barriers.

3.2 Sampling

The population frame of the study is composed of SMEs and Banks of Khyber Pakhtunkhwa. Researcher will use A-theoretical sampling method for obtaining primary data from SMEs (demand side) and financial institutions (supply side) in Khyber Pakhtunkhwa. The data is collected from 8 SMEs of different sectors, 3 different institutions related to SMEs like SMEDA, chamber of commerce, small industrial development board and 17 banks including government, Islamic, micro finance and conventional banks.

3.3 Data analysis plan

3.3.1 Thematic analysis

First the researcher will conduct thematic analysis to a set of text, such as interview transcripts. Here the researcher will closely examine the given data to find out common themes-ideas and patterns. From thematic analysis researcher will develop a frame work to identify factors.

4. Results and Findings

After conducted thematic analysis barriers (demand side and supply side) are identified in the mainstream of SMEs' financial inclusion. Along with this, strategies are also established to improve the current state of SMEs' financial inclusion.

4.1. Demand Side Barriers

4.1.1. Default Risk

Default risk acts as a formidable barrier to achieving the financial inclusion objectives of SMEs. These enterprises, despite their potential to fuel economic growth and innovation, often confront difficulties in accessing formal financial services due to concerns surrounding their ability to fulfill repayment obligations (Beck & Demirgüç-Kunt, 2006). Lenders tend to perceive SMEs as carrying a higher default risk due to factors such as their limited scale, insufficient financial history, and vulnerability to economic fluctuations (Klapper & Love, 2011). Respondent in interview said:

"*By taking credits from banks, there is a risk of default if we do not manage the fund properly.so due to this fear we have limited approach to formal credits". (Participant: SMEs owner)*

4.1.2. Religious Factor

Religious issues are a significant impediment to SMEs reaching their financial inclusion goals. Religious beliefs and practices can influence financial behaviours and choices in some cultural contexts, affecting SMEs' access to and utilization of credit. Karim and Tarazi (2009) define formal financial services. Interest-bearing obligations are prohibited by religion. Usury, which is common in Islamic finance, might make it difficult for SMEs to get financing. Iqbal and Molyneux (2005) define conventional loans as "credit products." Likewise, cultural conventions and money management and risk-taking characteristics may lead some SMEs to rely on the integration of informal financial networks into the formal financial system is limited Babajide and Raji (2013). The reply stated as follows:

"Dealing with formal financial channels involves the payment of interest, which is a serious sin and is outlawed in most jurisdictions. Because of Islam, we are able to survive in the informal sector."(Participant: owner of a small business)

"Due to lack of interest and awareness, SMEs are hesitant to interact with banks."(Participant Bank manager)

4.1.3. Conservative Culture in Khyber Pakhtunkhwa

The prevalent conservative culture in Khyber Pakhtunkhwa (KP) is a key impediment to reaching financial inclusion targets for the region's SMEs. Traditional values, practices, and social conventions that characterise KP culture can impact the mindset of SMEs and attitudes towards traditional financial services (Afridi et al., 2016). Conservative perspectives on Interest-based transactions based on religious beliefs and local norms could result in SMEs' reluctance to work with traditional financial institutions that offer interest-bearing loans (Khattak et al., 2020). Furthermore, cultural standards about gender roles and Interactions may hinder women's participation in financial decision-making and entrepreneurship, limiting SMEs' access to loans and other financial services even more. (2018) (Qureshi et al.).

"Dealing with formal financial channels involves the payment of interest, which is a serious sin and is outlawed in most jurisdictions. Because of Islam, we are able to survive in the informal sector."(Participant: SMEs owner)

"Due to the presence of interest and lack of awareness, SMEs are hesitant to interact with banks". (Participant: bank manager)

4.1.4. Limited Usage of Fintech

Fintech provides innovative digital tools and platforms that can increase access to financial services for disadvantaged SMEs, but widespread adoption is preventing these benefits from being realized (World Bank, 2020). Factors such as SME owners' lack technological literacy, insufficient digital infrastructure, and security and privacy concerns may all contribute to their reluctance to accept Fintech solutions (Aterido et al., 2016). Furthermore, regulatory difficulties and a fragmented Fintech environment can stymie the development and deployment of user-friendly and accessible financial technology to meet the demands of SMEs (Kumar & Thakur, 2021).

"In remote locations, Fintech resources, awareness training, and financial literacy are lacking. Because the majority of us are illiterate, we are unable to use these services effectively."(Participant: SMEs owner)

"SMEs cannot use Fintech and other financial services due to several reasons and utilize informal channel. Therefore it is requires to arrange comprehensive awareness and training program related to formal financial product and services." (Participant: bank manager)

4.1.5. Undefined source of income

The undefined source of income among SMEs serves as a notable barrier to their financial inclusion. In many cases, SMEs operate in the informal sector and lack clear documentation of their income sources, making it difficult for formal financial institutions to assess their creditworthiness (Demirgüç-Kunt & Klapper, 2012). This hampers their ability to access loans and other financial services, as lenders often require verifiable proof of income to mitigate default risks. Many SMEs, particularly those in the informal sector, are hesitant to engage with formal financial institutions for fear of attracting the attention of tax authorities such as the FBR (Ahmed & Din, 2019). The perception of stringent tax regulations, potential penalties, and the bureaucratic challenges associated with tax compliance often deter SMEs from entering the formal financial ecosystem. Respondent said that:

"While dealing with banks and FBR, they demand for proper source of income with complete records, most of the SMEs don't have definite sources of income and they prefer informal market and services though this market is not that much reliable".(Participant: bank manager)

4.1.6. Lack of Proper Financial Statements

The absence of proper financial statements among SMEs is one of the barriers to their financial inclusion. Financial statements that are well-prepared provide critical information about a company's financial health and performance, assisting lenders in determining creditworthiness (Klapper et al., 2006). However, many SMEs, especially those operating in informal sectors or lacking adequate financial literacy, struggle to maintain accurate and comprehensive financial records. This lack of transparency limits their access to formal financial services, as financial institutions require reliable data to assess risk. Interviewer response:

"Most of the SMEs are unregistered, illiterate and do not hire proper accountant, so they do not maintain proper financial record and other related documents". (Participant: bank manager)

"Our income is not that much to pay salary to accountant we are keeping informal records of various transaction in note book or personal diary". (Participant: SMEs owner)

4.1.7. Financial Illiteracy

Financial illiteracy stands as a formidable barrier to achieving financial inclusion for SMEs. The lack of knowledge about the basic financial concepts and practices among SME owners can hinder their ability to effectively navigate formal financial systems and access appropriate services (Lusardi & Tufano, 2015). Insufficient financial literacy often leads to suboptimal financial decisions, inadequate management of cash flows, and difficulty in assessing available financial products. This, in turn, reduces SMEs' attractiveness to lenders and limits their ability to secure credit for growth and investment. Respondent believe that:

"Majority of us are financially illiterate, few have some formal education. That is why we cannot use formal financial product and services. Feeling easy while dealing in informal financial market". (Participant: SMEs owner)

"SMEs are financially illiterate the feel hesitation while dealing with banks and to avail formal financial product and services." (Participant: bank manager)

4.1.8. Lack of Entrepreneurial Skills

The absence of essential entrepreneurial skills constitutes a significant barrier to achieve SMEs access to formal finance. The role of SMEs in economic development process is very crucial, but their success relies on effective management, strategic planning, and financial decision-making (Ameer et al., 2021). However, many SME owners lack the necessary entrepreneurial skills to navigate these challenges successfully. Limited knowledge in areas such as financial management, marketing, and business planning can hinder their ability to present themselves as creditworthy borrowers to formal financial institutions. Respondent believe that:

"Majority of the SMEs owners are operating their family business or businesses established by the fore fathers, they are just doing routine activities. So their entrepreneurial skills remain unpolished and relying on old tactics and strategies and do not avail modern financial product and services". (Participant: bank manager)

4.1.9. Risk of Disclosure

The risk of disclosure represents a significant barrier to achieving financial inclusion for SMEs. Many SMEs hesitate to disclose their financial information, such as business performance, revenue, and credit history, due to concerns about privacy, competition, and potential negative perceptions (Berger & Udell, 2006). This lack of transparency hinders their ability to establish credibility with formal financial institutions, which often rely on comprehensive financial data to assess creditworthiness. As a result, SMEs may face limited access to loans and financial services. Based on the interview response that:

"Many SMEs are unregistered, undocumented and have undefined source of income. In financial inclusion they will disclose their financial record which they do not want to disclose and resultantly the issue of FBR, FIA and NAB may arise. So due to this negative perception of SMEs deter to involved formal financial system." (Participant: bank manager)

"We do not want to share our financial records with any of the institution, because there is a risk that FBR, NAB and FIA may visit and ask for different questions and records. It is better to engage in informal sector".(Participant: SMEs owner) .

4.1.10. Misconception about Islamic Banking and Finance

Misconceptions about Islamic banking and finance among SMEs represent a notable barrier to their financial inclusion. In regions where Islamic banking is prominent, SMEs might lack a clear understanding of the principles and benefits of Islamic finance, leading to misconceptions that hinder their engagement with such financial services (Karim & Tarazi, 2009). Misunderstandings about profit-sharing models, risk-sharing mechanisms, and compliance with Sharia principles can deter SMEs from considering Islamic financial products as viable options as expressed by respondent that:

"Due to illiteracy and unawareness, a misconception about Islamic banking and finance has been developed in SMEs. They have the opinion that it is just change of names; both Islamic banking system and conventional banking and finance are the same. They deny availing Islamic financial products and services and surviving in informal sector". (Participant: bank manager)

4.1.11. Lack of Saving

The lack of savings among SMEs constitutes a significant barrier to their financial inclusion. Limited savings can impede SMEs' ability to build a financial cushion, manage cash flow fluctuations, and demonstrate financial stability to potential lenders (Kunt & Morduch, 2008). Many SMEs in the country struggle with limited savings, hindering their ability to manage cash flow fluctuations, make investments, and establish a stable financial base (Hussain et al., 2018). Without adequate savings, SMEs may struggle to meet sudden expenses or investment needs, leading to increased reliance on external financing. This can deter formal financial institutions from extending credit due to perceived risks. It has been also expressed by the respondent that:

"SMEs have limited formal saving to invest in formal financial system. The lack of saving is either due financial illiteracy or lack entrepreneurial skills". (Participant: bank manager)

4.1.12. Lack of Collateral

Lack of collateral is also a notable barrier for achieving financial inclusion of SMEs. Collateral is often required by formal financial institutions as a form of security against loans, providing lenders with assurance in case of default (Beck et al., 2005). The interviewee said that:

"SMEs cannot provide proper mortgage and security which in case of borrowing of formal credit they approached to informal credit market. Banks cannot take the risk in case of SMEs default or delay repayments. Collateral is type of security for recovery of credits". (Participant: bank manager)

4.1.13. Cash Based Transaction

Relying on cash-based transactions constitutes a significant barrier to achieving financial inclusion for Small and Medium-sized Enterprises (SMEs). Cash transactions are often associated with informality, lack of transparency, and limited access to formal financial services (World Bank, 2020). Due to issues such as a lack of awareness about digital payment choices or restricted access to banking infrastructure, many SMEs, particularly those working in the informal sector, participate in cash transactions. Cash transactions can make it difficult for SMEs to build a formal financial history, making it harder for them to acquire finance and grow various financial products. The respondent gave the same response that:

"*The majority of SMEs transactions are conducted in cash, avoiding conventional banking systems. Using the formal channel will necessitate a number of documents and evidences. As a result, cash-based The deal will result in the informality of SMEs."(Participant: bank manager)*

4.1.14. Lack of Awareness about Financial Products and Services

Small and medium-sized enterprises (SMEs) face a substantial barrier to financial inclusion due to a lack of awareness about financial products and services. Many SMEs may lack adequate knowledge of the range of financial solutions available to them. Loans, insurance, and investment alternatives, for example, or how these items could benefit them companies (Mia et al., 2021). Many Pakistani SMEs may be under-informed about the wide range of financial options open to them, such as loans, insurance, and investments, investment potential, as well as how these items might help their company (Pakistan) 2020, Telecommunications Authority). This lack of awareness can result in inferior results financial mistakes, missed opportunities for progress, and limited access to formal education financing. Respondent also stated:

"Due to a variety of factors, SMEs are unable to employ Fintech and other financial services informal channel. As a result, full awareness and training are required. Programed concerning formal financial products and services." (Participant: bank manager)

4.2. Supply Side Barrier

4.2.1. High insurance premium

The high premium of insurance policies represents a significant barrier to achieving SMEs' financial inclusion. Many SMEs are facing hurdles in accessing affordable insurance coverage due to the relatively high costs associated with insurance premiums (World Bank, 2020). Insurance serves as a critical tool for risk mitigation, safeguarding SMEs from various unforeseen challenges like property damage, liability claims, and business interruptions (Churchill & Matul, 2012). However, the high cost of premiums can deter SMEs; particularly those with limited financial resources, from subscribing to these essential services. It has been said by the respondent that:

"Formal financial market demand high premium for getting insurance policy which we cannot afford to pay". (Participant: SMEs owner)

4.2.2. Withholding Tax

Withholding tax is a significant barrier to financial inclusion for Small and Medium-sized Enterprises (SMEs). Withholding tax is levied on numerous financial transactions in many economies, including Pakistan, and the administrative complications connected with it. SMEs may be disproportionately affected by its application (Alif et al., 2021). Withholding taxes, which are frequently viewed as a tool for governments to enforce tax compliance, can incur upfront expenses on SMEs that are already working on thin margins (Kaplan & Zingales, 2000). The SMEs may be discouraged from participating in formal banking transactions if they face additional financial burdens or obtaining credit, as they may wish to reduce their tax liability or avoid complex tax issues processes. Respond believe that:

"*Withholding tax is prevalent in the formal banking system such tax makes the formal financial market further expensive for SMEs" (Participant: SMEs owner)*

4.2.3. High Interest Rates

High interest rates are a significant barrier in the way of financial inclusion SMEs. Interest rates represent the cost of borrowing, and when interest rates rise, SMEs, particularly those with narrower margins and fewer resources, may find it excessively expensive to obtain credit (Beck & Demirgüç-Kunt, 2006). In many cases SMEs experience difficulties in obtaining cheap finance due to high interest rates imposed by formal financial institutions (World Bank, 2020). These hefty borrowing costs can deter SMEs from requesting loans, particularly those with low profit margins. SMEs may also turn to informal lenders, who provide faster access to funds but at higher interest rates. Interest rates are rising, increasing their financial difficulties. The interviewee said that:

"As interest is one of the discourage factors of SMEs to avail formal financial product and services. It is considered in terms of cost and in religious aspect as well. As a result, to accomplish the goal of SMEs' financial inclusion, the government and SBP must launch interest-free financing initiatives for SMEs."(Participant: bank managers)

"Interest is a sin as well as a significant cost, thus we cannot approach to formal financial market. SBP must develop an interest-free loan package for SMEs". (Participant: SMEs owner)

4.2.4. Lack of Marketing of Financial Products and Services

The absence of marketing for financial products and services is a significant impediment to achieving the growth in financial inclusion for SMEs. SMEs frequently used are uninformed of the various financial options open to them, and they may not take advantage of them comprehend how these goods can help their company expand (Mia et al., 2021).Many SMEs in Pakistan are typically unaware of the various funding options available to them available to them, as well as how these services might benefit their enterprises (Pakistan).2020, Telecommunications Authority).Marketing may not be a priority for financial organizations efforts at SMEs, considering that small companies lack the means to participate with such offerings. This lack of marketing can lead to SMEs passing on possibilities access to credit, insurance, and other financial resources that could help them operations. Respondent expressed that:

"Due to a variety of factors SMEs cannot use Fintech and other financial services and utilize informal channel As a result, full awareness and training are required. Programed concerning formal financial products and services." (Participant: bank manager)

4.2.5. Relaxed Informal Financial Market

In Pakistan, the prevalence of a flexible informal lending market is a significant hurdle to achieving financial inclusion for SMEs. In many circumstances, SMEs in Pakistan rely on informal finance sources due to faster access, less verification requirements, and a lower cost of borrowing and reduced loan approval time as well (Ahmed et al., 2019). Informal lenders, often localized and community-based, provide quick, albeit sometimes at higher interest rates, access to capital without the bureaucracy and documentation required by formal institutions (Hassan et al., 2017). Many SMEs often resort to informal credit sources due to easier accessibility, less stringent documentation requirements, and quicker approval processes compared to formal financial institutions (Beck et al., 2005). This informal credit market, while providing short-term relief, often comes with high interest rates and lacks the regulatory protections associated with formal financial services. According to respondent that:

"While dealing in formal financial market it is too much expensive by charging various fee and charges on transactions and processes. So we utilize informal financial market which is seemed to be less expensive as compare to formal one." (Participant: SMEs owners)

"The current formal financial system is lengthy and complex. We cannot fulfill these requirements. And other the process is time consuming by passing an application from different personals. We need assistance on urgent basis. That is why we prefer informal financial market to avoid these formalities. So the government is required to make the procedure simple, easy and quick by reducing unnecessary documents etc."(Participant: SMEs owners)

4.2.6. Bankers' Default Risk

Bankers' fear of default risk serves as a significant barrier to achieving SMEs' financial inclusion. Financial institutions often perceive SMEs as riskier borrowers due to their limited financial history, information opacity, and vulnerability to economic shocks (Beck et al., 2015). Due to concerns over SMEs' limited financial history, information opacity, and susceptibility to economic volatility, financial institutions tend to perceive SMEs as higher-risk borrowers (World Bank, 2020). This perception often results in stringent lending criteria, demanding higher collateral, and charging elevated interest rates, making it challenging for SMEs to access formal credit facilities. The respondent believes that:

"SMEs cannot provide proper mortgage and security which in case of borrowing of formal credit they approached to informal credit market. Banks cannot take the risk in case of SMEs default or delay repayments. Collateral is type of security for recovery of credits". (Participant: bank manager)

4.2.7. Cyber Risk in Fintech

Cyber risk within the Fintech sector constitutes a significant barrier to achieve SMEs' financial inclusion. As SMEs increasingly rely on digital financial services for banking and payment, the possibility of cyber-attacks, data breaches, and online fraud becomes a major worry (World Bank, 2020). As financial technologies advance, the reliance on digital platforms and systems also increases which, although beneficial in many ways, but expose firms to cyber risks such as hacking, phishing, and data breaches (Zavolokina et al., 2016). The perceived vulnerability of digital financial services to cyber hazards may hinder SMEs from implementing these technologies and gaining access to formal financial services. Participant believes that:

"Cyber risk is involved by using Fintech". (Participant: bank manager and SMEs owners)

4.2.8. Geographical Discrimination

Geographical discrimination by bankers constitutes a significant barrier to achieving financial inclusion for Small and Medium-sized Enterprises (SMEs). Research has shown that financial institutions often exhibit a bias toward lending to businesses located in urban or economically developed regions, while neglecting SMEs in rural or less affluent areas (Coleman, 2007; World Bank, 2020; Ashraf et al., 2021). As a result, SMEs located in underserved regions are denied access to formal lending and financial services, hindering their growth prospects. According to respondent that:

"No doubt, government of Pakistan introduces various schemes through banks. But the bankers assigned these schemes to SMEs established in urban areas or to near and dears by passing the merit. We had applied for several financial schemes but couldn't avail. Therefore, it is required to abolish every type of discrimination and followed merit while devolving the schemes."(Participant: SMEs owners)

4.2.9. Lengthy and Complex Procedures

Research has indicated that SMEs, often lacking the resources and expertise of larger enterprises, can be deterred by the bureaucratic hurdles and time-consuming processes associated with formal financial institutions (World Bank, 2020; Aterido et al., 2011; Djankov et al., 2007). Empirical studies have highlighted that the bureaucratic challenges and intricate processes associated with formal financial institutions can deter SMEs, particularly those with limited resources, from accessing necessary credit and financial services (World Bank, 2020; Aterido et al., 2011; Shahbaz et al., 2019). Cumbersome loan application procedures, extensive documentation requirements, and extended approval times can hinder SMEs' ability to access credit and financial services. Respondent believe that:

"The current formal financial system is lengthy and complex. We cannot fulfill these requirements. And other the process is time consuming by passing an application from different personals. We need assistance on urgent basis. That is why we prefer informal financial market to avoid these formalities. So the government is required to make the procedure simple, easy and quick by reducing unnecessary documents etc.". (Participant: SMEs owners)

4.2.10. Demand for Comprehensive Financial Statements

In Pakistan, the demand for comprehensive financial statements by banks serves as a significant barrier to achieving financial inclusion for Small and Medium-sized Enterprises (SMEs). Research underscores that SMEs often strive hard to fulfill the documentation need set by formal financial institutions due to their limited resources, accounting practices, and unfamiliarity with complex financial reporting (World Bank, 2020; Aterido et al., 2011; Ghazali et al., 2017). Banks' insistence on detailed financial statements can disproportionately impact SMEs, particularly those in rural or informal sectors, are remained excluded from formal credit and financial services. It has been mentioned by respondent that:

"Most of the SMEs are unregistered, illiterate and do not hire proper accountant, so they do not maintain proper financial record and other related documents". (Participant: bank manager)

"Our income is not that much to pay salary to accountant we are keeping informal records of various transaction in note book or personal diary." (Participant: SMEs owner)

4.2.11. Demand for Collateral

The demand for collateral by banks poses a significant barrier to achieving financial inclusion for Small and Medium-sized Enterprises (SMEs). Extensive research highlights that SMEs, often characterized by limited assets and credit history, face challenges in meeting the collateral requirements set by formal financial institutions (World Bank, 2020; Beck et al., 2013; Ayyagari et al., 2014). Extensive research underscores that collateral requirements set by formal financial institutions can disproportionately hinder SMEs' access to credit, especially those with limited tangible assets (World Bank, 2020; Khan et al., 2017; Ayyagari et al., 2014). Banks typically require collateral to mitigate lending risks, but this practice disproportionately affects SMEs' access to credit. Collateral requirements can lead to exclusion, especially for newer and smaller enterprises that lack sufficient assets to pledge. According to the respond of interviewee:

"Banks demand for proper mortgage and security which SMEs cannot provide in case of borrowing of formal credit. That is why we approach to informal credit market. Therefore financial institutions are required to relax the collateral requirement and introduce collateral free schemes for the development SMEs". (Participant: SMEs owner)

4.2.12. Lack of a Separate Counter for SMEs in Banks

The absences of a dedicated counter or specialized guidance for SMEs within banks may be a notable barrier to achieving financial inclusion for these businesses. Research highlights that SMEs often face challenges in accessing appropriate financial services and advice due to their unique needs and limited resources (World Bank, 2020; Shahbaz et al., 2019; Beck et al., 2013). It is the opinion of participant that:

"There is lack of specific corner for SMEs in banks. Majority of us are illiterate and unaware form formal financial system. There it is required to establish a separate corner for us with trained personal to give us proper time and information related to SMEs. As we have bad experience with the general banking system and their personals". (Participant: SMEs owners)

4.2.13. High transaction cost

The high transaction cost is a significant barrier to financial inclusion for SMEs. According to research, the costs of executing financial operations, such as fees for moving funds and making payments, access to formal financial services, in particular, can have a disproportionate influence on SMEs.(World Bank, 2020; Shahbaz et al., 2019;

Beck et al., 2007). The financial burden of transaction charges can deter SMEs from utilizing formal financial services assistance and instead push them towards more informal, cash-based ways that may be more effective, inexpensive yet lack the benefits of formal banking ties. This practice may result in a SMEs are trapped in a cycle of restricted lending and savings possibilities. View point of the respondent:

"Dealing in the official financial market is expensive due to the different fees and charges levied on transactions and processes. As a result, we use the informal financial market, which appears to be less expensive than the legitimate one."(Participant: SMEs owners)

5. Strategies of Financial Inclusion

5.1 Training and Awareness of SMEs

Empowering SMEs through targeted training and awareness activities emerges as a strategic way to improving their financial inclusion. According to extensive studies, enhancing SMEs' financial literacy and knowledge of formal financial systems can help them gain access to financial services significantly (Karim et al., 2019; Shahbaz et al., 2019; World Bank, 2020). Increasing financial stability SME competence and knowledge improve their ability to leverage formal resources financial services, increasing financial inclusion and generating long-term economic growth (Karim et al., 2019; Shahbaz et al., 2019; World Bank, 2020). Because of the rapid evolution of Financial technology has heralded a new era of digital financial services. Businesses can benefit from transformative prospects (World Bank, 2020; Zavolokina et al., 2019). According to research, providing Fintech training to SMEs allows them to better understand and utilize digital payment systems, online lending platforms, and other financial technologies, allowing them to gain greater access to financial services (Goldstein & Turner, 2004; Claessens & Rojas-Suarez, 2016). Such programs not only improve SMEs' digital financial capabilities, but also encourage trust and confidence in using these platforms, supporting broader financial inclusion and generating long-term economic growth (World Bank, 2020; Zavolokina et al., 2019). According to the responder:

"SMEs cannot use Fintech and other financial services for a variety of reasons and must rely on informal channels. As a result, full awareness and training program are required concerning formal financial products and services." (Participant: bank managers)

5.2 Financial Literacy Program for SMES

Improving the financial inclusion of (SMEs) demands a diverse approach, with the development of a strong financial literacy program at its core. Empirical research reveals that SMEs frequently struggle to know the intricacies of banks, limiting its ability to access and successfully use financial services (World Bank, 2020; Klapper et al., 2016; Beck et al., 2007). These issues can be addressed with a thorough financial literacy curriculum designed specifically for SMEs. A program like this can provide SMEs with information about available financial products, credit procedure complexities, and successful financial management techniques, allowing them to make informed decisions (Beck et al., 2007; Aterido et al., 2011). Furthermore, these programs can help to bridge the information gap between SMEs and financial institutions, building mutual understanding and trust. SMEs are better positioned to exploit financial services, maximize their financial health, and contribute more effectively to economic growth by improving their financial literacy (World Bank, 2020; Klapper et al., 2016).

"As majority of SMEs owners are financially illiterate, so for enhancing financial inclusion of SMEs, State Bank of Pakistan is required to introduce financial literacy program for SMEs as it had already announced Financial Literacy Program for general public".(participant: bank manager)

5.3 Simple and Streamlined Procedures

Adopting simple and streamlined procedures appears as a critical method to improving financial inclusion for SMEs. According to research, regulatory difficulties, time-consuming paperwork, and complex financial processes frequently prevent SMEs from obtaining and fully utilizing formal financial services (World Bank,2020; Beck et al., 2007; Demirguc-Kunt et al., 2018). Financial institutions may make their services more accessible and appealing to SMEs by streamlining application procedures, decreasing documentation requirements, and accelerating approval processes. This shift toward improved speed and accessibility in financial procedures is critical for building confidence, lowering barriers, and eventually assuring greater financial inclusion for SMEs

(World Bank, 2020; Beck et al., 2007; Demirguc-Kunt et al., 2018). Response from interviewer:

"The current formal financial system is lengthy and complex. We cannot fulfill these requirements. And other the process is time consuming by passing an application from different personals. We need assistance on urgent basis. That is why we prefer informal financial market to avoid these formalities. So the government is required to make the procedure simple, easy and quick by reducing unnecessary documents etc". (Participant: SMEs owners)

5.4 Separate Corners for SMEs in Banks

Establishing specialized SMEs corners within banks emerges as a strategic strategy to promote financial inclusion of Pakistan's SMEs. Recognizing SMEs' distinct financial needs and concerns, such specialist corners can provide targeted services geared to this segment (World Bank, 2020; Beck et al., 2007; Khan et al., 2017). This type of initiative can help to reduce the informational asymmetry that SMEs frequently confront when dealing with larger financial structures (Beck & Demirguc-Kunt, 2006). One of the most significant issues that SMEs in Pakistan confront is navigating the complexity of the formal banking system, with many feeling ignored or misunderstood by conventional banking services (Khan et al., 2017; World Bank, 2020). Such a focused approach can create trust in SMEs, enabling them to interact more completely with the formal financial sector, resulting in broader financial inclusion and boosting long-term economic growth in Pakistan (World Bank, 2020; Khan et al., 2017). Similarly, respondent said:

"In banks, there is no separate corner for SMEs. The majorities of us are uneducated and have little knowledge about formal financial system. It is required to build a distinct corner for us with trained personnel to provide us with adequate time and information on SMEs. We have had a bad experience with the general banking system and its personnel". (Participant: SMEs owners)

5.5 Fixed Taxation

Consideration of fixed taxation for SMEs represents an innovative way to promoting their financial inclusion in Pakistan. A consistent tax structure in which SMEs are aware of the fixed tax amounts they owe regardless of shifting business profits can simplify their fiscal landscape (World Bank, 2020; Mahmood et al., 2018). This strategy eliminates the complexities and uncertainties associated with fluctuating tax requirements, allowing SMEs to better plan and manage their finances (Ayyagari et al., 2011). Fixed taxation can also reduce administrative requirements for both tax authorities and SMEs, resulting in more compliance and fewer conflicts (Khan et al., 2017). Pakistan can potentially encourage SMEs to engage more actively with formal banking systems by making the tax climate more predictable, hence promoting their financial inclusion. To accomplish this, policymakers, regulatory bodies, and industry stakeholders must work together to design and implement a transparent and feasible fixed tax regime that takes into account the operational realities of SMEs in Pakistan (World Bank, 2020; Mahmood et al., 2018; Ayyagari et al., 2011).). Respondents are also believed that:

"FBR has imposed various taxes on us(SMEs)and we cannot afford to pay these heavy tax, therefore FBR is required to imposed fixed tax on SEMs regardless of our income stream".(participant: SMEs owners)

"As SMEs are mostly undocumented, unregistered businesses and their source of income is undefined. Therefore, they have fear from FBR and mostly evade income tax and survive in informal sector. By consultation with SMEs and imposing fixed tax according to their affordability will be good step from informal towards formal sector". (Participant: bank manager)

5.6 Collateral Free Loan to SMES

Research consistently underscores the challenges SMEs face in providing collateral, as the main hurdle for getting formal financial services (World Bank, 2020; Beck et al., 2007; Khan et al., 2017). By introducing collateral-free loans, financial institutions can mitigate this barrier, making credit more accessible for SMEs. Providing unsecured financing options encourages SMEs to enter the formal financial sector, fostering trust and promoting financial inclusion. Policymakers in Pakistan should collaborate with financial institutions to design and implement a viable framework for collateral-free lending, balancing risk management with the needs of SMEs, thereby facilitating broader financial inclusion (World Bank, 2020; Beck et al., 2007; Khan et al., 2017). It is also suggested by the participant that:

"Banks demand for proper mortgage and security which SMEs cannot provide in case of borrowing of formal credit. That is why we approach to informal credit market. Therefore financial institutions are required to relax the collateral requirement and introduce collateral free schemes for the development SMEs".(Participant: SMEs owner)

5.7 Interest Free loan to SME's

Interest-free credit has a positive impact on SMEs, making it more accessible and affordable for them to access formal financial services (World Bank, 2020; Mahmood et al., 2018; Ahmed & Hussain, 2019). Interest-free loans can significantly reduce the financial burden on SMEs, encouraging their contribution in formal financial sector (Beck & Demirguc-Kunt, 2006; Khan et al., 2017). Policymakers in Pakistan should collaborate with financial institutions to design and implement effective interest-free loan programs, ensuring they are well-structured and responsive to the unique needs of SMEs (World Bank, 2020; Mahmood et al., 2018; Ahmed & Hussain, 2019).

"As interest is one of the most important factor that discourage SMEs to avail formal financial product and services. It is considered in terms of cost and in religious aspect as well. Therefore, government and SBP are required to initiate interest free financial schemes for SMEs to achieve the target of greater financial inclusion of SMEs". (Participant: bank managers)

"Interest is a sin as well as carries high cost, due which we cannot approach to formal financial market. SBP is required to launch interest free credit scheme for SMEs." (Participant: SMEs owner)

5.8 One Window Operation System for SME's

In Pakistan, implementing a one-window operation system for Small and Medium-sized Enterprises (SMEs) is a strategic goal to increase financial inclusion. This method streamlines and consolidates multiple processes, making it easier for SMEs to interact with formal financial services (World Bank, 2020; Mahmood et al., 2018; Ahmed & Hussain, 2019). A one-window operation removes bureaucratic barriers, allowing SMEs to access and engage in official financial channels more easily (Beck & Demirguc-Kunt, 2006; Khan et al., 2017). Policymakers and financial institutions in Pakistan should work together to build and execute successful one-stop shop solutions that are user-friendly and responsive to the unique needs of SMEs (World Bank, 2020; Mahmood et al., 2018; Ahmed & Hussain, 2019).

"The implementation of a single-window system for SMEs is essential. It will deliver more services to SMEs and enhance their access to products and services offered by banks". (Participant: bank managers)

5.9 Marketing of Financial Products and Services

Implementing successful marketing strategies for financial services and products aimed at SMEs in Pakistan is a critical strategy for increasing financial inclusion. According to research, specialized and focused marketing is critical for raising awareness and encouraging SMEs to connect with formal financial institutions (World Bank, 2020; Mahmood et al., 2018; Ayyagari et al., 2007). Marketing initiatives that are well-designed can fill knowledge gaps and dispel myths, creating increased trust in formal financial services (Beck & Demirguc-Kunt, 2006; Khan et al., 2017). In Pakistan, policymakers and financial institutions should work together to create and implement comprehensive marketing strategies that highlight the benefits of formal financial services for SMEs and promote financial inclusion (World Bank, 2020; Mahmood et al., 2018; Ayyagari et al., 2007). Respondent suggested that:

"Banks must start marketing campaigns regarding the products and services for SMEs especially in rural areas. The vast majority of SMEs are not aware of formal financial products and services. It will raise our awareness and allow us to contact the formal financial market". (Participant: SMEs owner)

5.10 Abolish Geographical Discrimination by Bankers

Numerous studies demonstrate the negative consequences of regional inequalities in access to finance and emphasize the necessity of treating SMEs fairly across geographical boundaries (World Bank, 2020; Mahmood et al., 2018; Ayyagari et al., 2007). Removing such discrimination requires concerted efforts from policymakers and financial institutions to ensure that SMEs in all regions have equal access to financial resources (Beck & Demirguc-Kunt, 2006; Khan et al., 2017). Policymakers should enforce regulations and guidelines that discourage discrimination based on geography, fostering a fair and inclusive financial landscape for SMEs in Pakistan (World Bank, 2020; Mahmood et al., 2018; Ayyagari et al., 2007). It is of the opinion of interviewee that:

"No doubt, government of Pakistan introduces various schemes through banks. But the bankers assigned these schemes to SMEs established in urban areas or to near and dears by passing the merit. We had applied for several financial schemes but couldn't avail. Therefore, it is required to abolish every type of discrimination and followed merit while devolving the schemes". (Participant: SMEs owners)

5.11 Efficient Role of SEMDA

SMEDA, being a key organization established for support and development of SMEs. It has the potential to significantly impact their financial inclusion. Several studies emphasize the pivotal role of government agencies and institutions like SMEDA in promoting SME growth and inclusion (Khan & Iqbal, 2019; Ayyagari et al., 2011). SMEDA can enhance financial inclusion by implementing targeted programs that provide financial literacy training, access to credit, and support in navigating formal financial channels for SMEs (SBP, 2021). Collaborative efforts between SMEDA and financial institutions can create synergies, promoting the growth of financial products tailored to the unique needs of SMEs (World Bank, 2019). By leveraging its expertise and network, SMEDA can act as a catalyst in creating an enabling environment for SMEs, fostering their financial inclusion and contributing to the overall economic growth and development of Pakistan. Respondent has also mentioned that:

"SEMDA is required to play its role effectively by investigating and resolving issues of SMEs and bringing SMEs under formal financial channel". (Participant: bank managers and SMEs owners)

5.12 Active Role of SME's Bank

SMEs banks, specialized in catering to the unique financial needs of small businesses, can contribute significantly to fostering financial inclusivity. Numerous studies highlight the usefulness of specialized SMEs financial institutions in improving access to finance for smaller businesses (World Bank, 2013; Batool, 2017). By adapting banking products and services to the individual needs of SMEs, SMEs banks can alleviate the barriers to standard banking services that these businesses confront (Majeed et al., 2019). The Financial Inclusion Strategy for 2020-2023 of the State Bank of Pakistan emphasizes the vital role of financial institutions, notably SMEs banks, in fostering financial inclusion (SBP, 2021). Collaboration between SMEs, banks, and regulatory organizations can help to create an environment that promotes SME growth and financial inclusion.

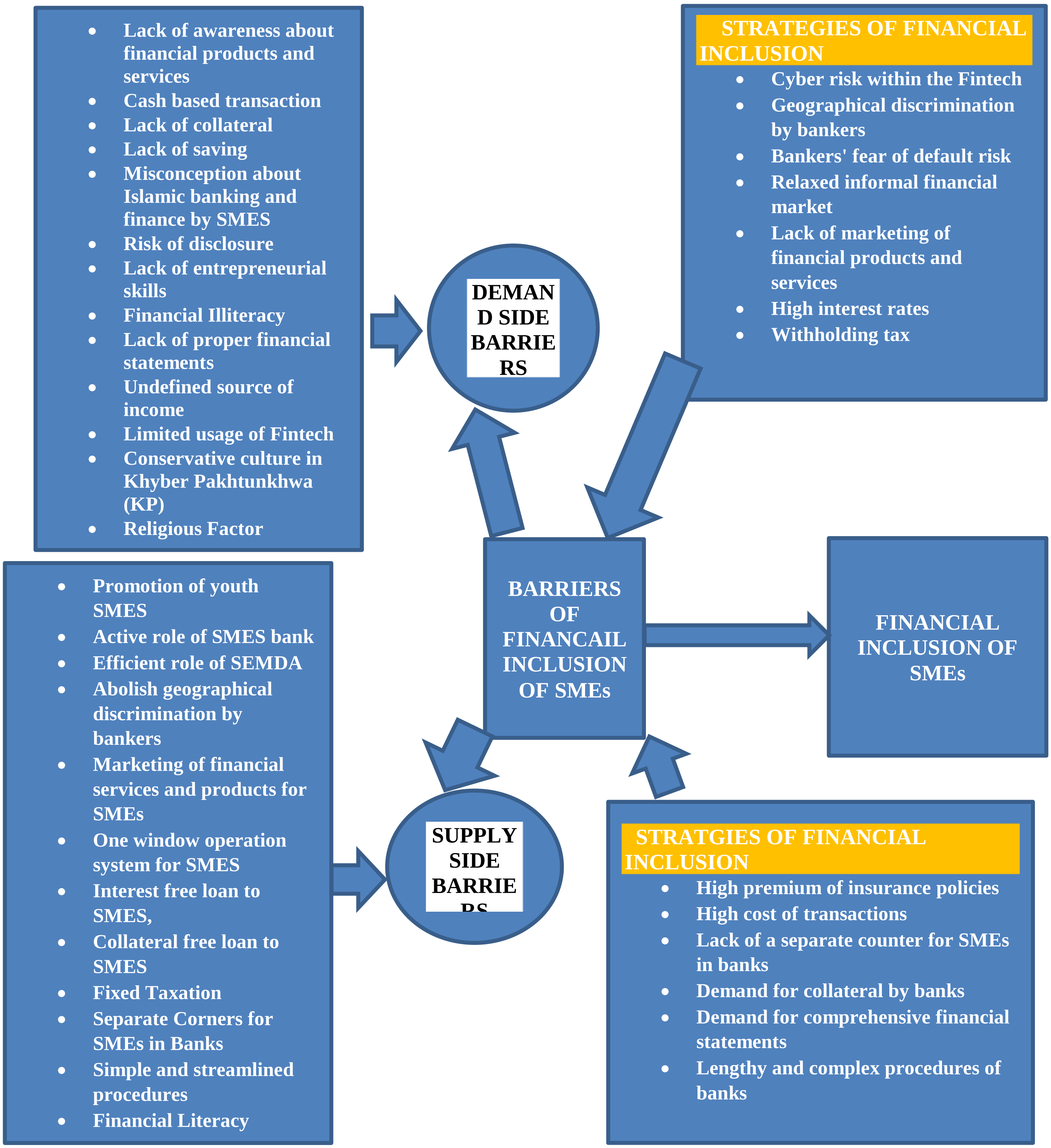
"SME banks must play an active role in providing various incentives and initiatives to SMEs. The bank was founded primarily to promote SMEs in the country". (Participant: bank managers)

5.13 Promotion of Youth SME's

Involving young entrepreneurs in business initiatives can boost economic growth and encourage innovation. Several studies emphasize the importance of encouraging young entrepreneurship for overall economic development (Amorós & Cristi, 2008; Bosma & Levie, 2010).The State Bank of Pakistan recognizes the significance of youth entrepreneurship in its Financial Inclusion Strategy for 2020-2023, emphasizing the need to create an enabling environment for the youth to engage in business activities (SBP, 2021). Additionally, initiatives such as the Investment Climate Program for SMEs as supported by World Bank, underscore the importance of fostering a friendly environment for youth-led SMEs to thrive (World Bank, 2013). By specifically targeting and promoting youth SMEs, Pakistan can harness the potential of young entrepreneurs, ultimately improving financial inclusion and fostering a vibrant entrepreneurial ecosystem. It has been suggested by the respondent that:

"SBP is required to initiate projects and schemes which are purely related to youth SMEs. Majority of our youth are educated and have the potential to become a successful entrepreneur. Such approach will improve SMEs financial inclusion in the country". (Participant: bank managers)

6. Conceptual Framework



Both Financial inclusion and SMEs have a significant impact on the socioeconomic growth of a country. Therefore, SMEs' financial inclusion of is one of the top priorities of SBP and government of Pakistan. Under this context State Bank of Pakistan has issued National Financial Inclusion Strategies (NIFS) under the flagship of NIFS 100days agenda to achieve various targets by 2023. This study was conducted in order to explore the barriers in the main stream of financial inclusion of SMEs and establish strategies to enhance SMEs financial inclusion. This research studied various demand-side and supply-side barriers are identified. Majority of the SMEs in Pakistan are unregistered and surviving in informal financial market. The main reason of their exclusion and informality is demand and supply side barriers. SBP and government of Pakistan have introduced various schemes for the uplifting of SMEs sector, but the sector is still lag behind in the development process. As a result the current study has established various strategies and ways to improve SMEs 'financial inclusion. By improving the state of SMEs' financial inclusion will lead to the development of formal economy and SMEs sector in the country which is one the main objectives of SBP, World Bank and government of Pakistan.

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