



Empirický výzkum vazeb mezi malými a středními podniky a ekonomickým růstem Srí Lanky

An Empirical Investigation on the Association between Small and Medium Enterprises and the Economic Growth of Sri Lanka

Sinnathurai Vijayakumar

Abstract:

Purpose of the article: SMEs play important role in both developed and newly industrialized countries in terms of boosting economic growth and alleviating poverty. Despite there are vast numbers of SMEs in Sri Lanka, people do not enjoy stable economic growth and good living standard so far. Therefore, the prime intension of this study is to find out the association between economic growth and SMEs in Sri Lanka and also nexus among the economic growth, poverty and SMEs.

Methodology/methods: This study analyzes the impact of small and medium enterprises in the economic growth and poverty in addition to role of SMEs in consonance with employment generation and value added in Sri Lanka. The secondary data have been employed for the analysis. The simple multiple regression model was employed to analyze the data. Heteroskedasticity and serial correlation problems were detected with the help of statistical soft ware (E-views).

Scientific aim: The aim of study is to scrutinize the association between economic growth and SMEs and the relationship among the economic growth, poverty and SMEs. It strived to bring about the general behavior of SMEs in Sri Lanka.

Findings: The finding clearly shows that there is positive relationship between economic growth and SMEs but, impact of SMEs on economic growth is not significant in Sri Lanka. Even though the co-efficient of SMEs is 0.02 indicating that there is positive relationship between economic growth and SMEs, the impact of SMEs on economic growth is statistically insignificant. Another finding is that there is vast number of industrial establishments of SMEs in total establishments which do not significantly contribute to the employment generation and value added in Sri Lanka.

Conclusions: Notwithstanding several literatures related to SMEs have articulated the fact that SMEs can play important role in boosting economic growth, employment generation, accumulation of capital and poverty reduction, this experience is not consistent with Sri Lanka. The output of this study clearly proves the conclusion that SMEs don't play significant impact on economic growth of Sri Lanka while poverty has significant effects on economic growth. Furthermore, public private participation (PPP) is sine qua none to the effective promotion of SMEs which leads to economic growth and poverty reduction. Visionary government can launch effective PPP which is remedy for the successful promotion of SMEs and thereby boosting economic growth.

Keywords: small and medium enterprises, economic growth, employment, value added, public private participation

JEL Classification: L25, L26, I30, O40, O43

Introduction

Sri Lanka is conducive to start up micro and small enterprises for socio-economic development because it has labor abundance in nature. Small and medium enterprises can play crucial role in every one's life because most of the day to day economic activities are related to SMEs. In other words, it is the thought that SMEs have potential capabilities to boost the economic growth, reduce the poverty and enhance the export and innovation rat in developing countries particular and developed countries in general. The small industries in rural areas are source of employment and production of food in addition to agriculture .Since independent, successive governments in Sri Lanka have been giving great attention to develop the small and medium industries which is backbone for the economic growth and thereby reducing poverty .Sri Lanka is an island found in the South East of India surrounded by Indian Ocean with total land area of 65610 square kilometers in which total population is 21.2 million in 2011. Sri Lanka's human development index is by far the highest in South Asia and exceeds that of the rich countries. This level of human development has been achieved through the provision of universal access to health, education and continued investment in the social sectors. Economic development however has lagged consistently behind social development (Vijayakumar, 2010). In terms of production, Sri Lanka is primarily an agricultural country. The main crop is rice. Tea, rubber, coconut, and spices are important commercial agricultural crops. The contribution of the agriculture sector to GDP was 12 % although 24.6%R and D expenditure is spent on agriculture research and development. However, over the past few years the manufacturing industry has grown significantly. Textiles, wearing apparel and leather products are the major industrial products (Central bank of Sri Lanka, 2008). For example, textile, wearing apparel and leather products constituting 44 percent (in 1998) have accounted for the largest value of industrial production. The service sector, which included transport, tourism, Communication, trade, financial services, public administration, defense and other services, contributed 50.7 percent of the growth in GDP in 2010. Tourism and financial services play a major role in the service sector. As mentioned above, in recent years the manufacturing sector appears to have played a prominent role in the economy relative to the other economic activities; especially in terms of expanding production, export, and employment since the introduction of the liberalized economic policies in Sri Lanka in 1977. Accord-

dingly, Sri Lankan policy makers have emphasized the private sector participation in boosting the economy of Sri Lanka and are giving more important to that of it in their decision making. Thus, Successive governments in Sri Lanka have taken various steps from time to time to promote Small and Medium Enterprises which is backbone of economic growth and reduction of poverty. SMEs are more appropriate to the countries where population is high. Sri Lankan economy was liberalized to encourage the private sector participation for achieving economic development and reducing poverty in 1977. The most of the policy makers believe that Small and medium industries will play crucial role in boosting the economic growth and alleviating poverty in Sri Lanka because of its capacity of employment generation, contributing growth, and alleviating poverty, bringing about improvement of income distribution, increasing share of export earnings and embarking on innovation. Particularly, in Sri Lankan context, it is expected by the government that chronic poverty can be reduced via employment generation, increasing export income, contribution of GDP and income distribution of SMEs. In other words, generally, in Sri Lanka, contributions of Small and medium enterprises to the development of education, health and infrastructural facilities which are inevitable factors in boosting social and economic development are questionable and should be explored. There is ample empirical evidence that countries with a high share of small industrial enterprises have succeeded in making the income distribution (both regionally and functionally) more equitable. This in turn is a key contribution to ensuring long-term social stability by reducing re-distributional pressure and by reducing economic disparities between urban and rural areas. In this study author strives to find out the contribution of SMES in boosting economic growth and its trend in Sri Lanka.

1. Objective of Study and Methodology

Generally, the developing countries like Sri Lanka are confronting severe problems in respect of having stable economic growth and other favorable macro economic performance indicators. Therefore, to make stable economy, these countries strive to transform their economy from primary agricultural products to industrial products. It is the fact that industrial products are elastic which generate more income and profit rather than agricultural products which have inelastic demand. This is not different in the case of Sri Lanka. This study tries to focus on the

fact that how small and medium enterprises perform on Sri Lankan economy, particularly on economic growth. Furthermore, this study analyzes the trend of small and medium enterprises in employment generation and value added. In addition to this objective, the study tries to explicate the remedial measures taken by government to promote small and medium enterprises in Sri Lanka.

Secondary data have been used for the analysis. The data has been gathered from reports such as Central bank of Sri Lanka, Department of Census and statistics in which data from 2000 to 2010 were taken for the analysis. Furthermore headcount index and SMEs employment data have been interpolated because of non-availability of some data. The simple multiple regression model is employed to analyze the data. Heteroskedasticity serial correlation problems were detected by using Eviews option. The entire analysis has been carried out with the use of statistical package of Eviews.

2. Definition of Small and Medium Enterprises

Enterprise development is almost universally promoted in developing countries, and is often justified on the grounds that the emergence of enterprises is an important mechanism to generate economic growth. As a developing country in Sri Lanka, many enterprises are small and medium scales. SMEs have been identified as an important strategic sector for promoting growth and social development of Sri Lanka. Over the years SMEs have gained wide recognition as a major source for employment, income generation, poverty alleviation and regional development. The SMEs cover broad areas of economic activities such as agriculture, manufacturing, mining, constructions and service sector industries. In the present competitive and challenging global environment, a viable and dynamic SME sector is essential for economic development of developing countries. For the survival of the SMEs sector in developing countries, support from other sections of society is needed. Most success stories of developed countries come with the private-public synergy. Therefore the private-public cooperation is very important to achieve the success of SMEs. It is the fact that in developing countries, most important and crucial issue is to generate tremendous employment opportunities for the vast labor forces because unemployment problems vitally affect the people that lead to severe poverty ridden condition. Amararatne (2003) mentioned that employment ge-

neration has been first choice than improving technology because poverty reduction can be achieved only by generating new employment opportunities. Thus, small enterprises are a key source to generate more employment not only for skill labor but also non-skill labor. What is the important fact is that labor productivity and labor quality could be greater in medium and large scale industries in practice. Accordingly, for rural population, small and medium enterprises should provide the significant size of employment opportunities of which unskilled labor force could be benefited and thereby increasing living standard of that people. In other words the generation of employment through small industries among the rural poor will be fostering of spirit of people's entitlement and capabilities. Generally, 75% to 80% population of county is living in rural areas in developing countries that mainly rely on agriculture and allied services for their livelihood. Also, in Sri Lanka, 80% of people inhabit in rural and estate sector depending primary sector of agriculture. Even though Sri Lankan government has been spending huge money for poverty alleviation, rural and estate people are still living very low level living standard and poverty stricken nature. Therefore, promotions of cottage, small and medium enterprises have been emphasized by policy makers, government, non-governmental organizations and international aid agencies as strategy to achieve high economic growth and poverty reduction. The faith on small industries in economic development other than large scale once that has commenced to emphasize a fresh labor intensive from 1980s. In the context of reducing capital cost in employment generation small and medium industries are more cost less source compared with the large enterprises. Though small and medium enterprises can play crucial role in boosting economic growth, export income and reducing poverty in developed countries in general and developing countries in particular, developing countries where around 80 percentage of population live in rural areas should give their attention for the promotion of the small and medium enterprises in general and small enterprises in special because Small enterprises can be launched with very few knowledge of modern management, finance controlling and minimum skills. Furthermore, crucial issues like balance of payment deficit can be easily solved by export oriented small and medium enterprise. This is the one of the reasons for failure of small enterprises and for ineffective performance of SMEs. In practice, role of small enterprises don't play vital role in alleviation poverty and boosting economic growth in Sri Lanka. In comparison with

small enterprises, medium enterprises are providing more employment but not significant in general. Nevertheless, compared to large scale enterprises, a role of small and medium enterprises do not have significant contribution in boosting economic growth and employment generation in Sri Lanka.

The definition of SMEs varies country to country, region to region, sometimes within one nation. SMEs can be defined as in terms of many parameters such as the number of persons employed, amount of capital invested, amount of turnover, or a combination of the two or more. It is the fact that there is no single or unique definition in regard to SMEs. The European Union defines SMEs the following way: Small scale businesses consist of fewer than 50 employees and the annual turnover is less than EUR 7 million or the annual balance-sheet total must not exceed EUR 5 million. Medium scale businesses are considered 50–250 people and annual turnover must be less than EUR 40 million or the annual balance-sheet total must not exceed EUR 27 million. In consonance with aforesaid definition, employment, assets and turnover are highlighted. In countries where there are strong SMEs sectors, they are as a rule defined by using the number of employees and size of capital. Japan defines SMEs under three categories including manufacturing sector SMEs, wholesaling sector SMEs, retailing and service sector SMEs. In India, Small Scale Industry (SSI) can be defined as in terms of limits on investment in plant and machinery, excluding investment in land and buildings, testing equipments and anti-pollution measures. As said above, various departments, institution in Sri Lanka also define poverty based on various criteria. The criteria for SMEs based on number of persons employed are reasonable because they distinguish between enterprises regardless the line of business, and the amount of capital investment must be revised frequently due to inflation (Ponnamperuma, 2000). Industrial Development Board (IDB) defines a small industry as an establishment whose capital investment in plant and machinery does not exceed Rs.4 million and the total number of regular employees does not exceed 50 persons (Central Bank of Sri Lanka, 1998). The Department of Small Industries (DSI) classifies enterprises with capital investment of less than Rs. 5 million (US\$ 52500) and fewer than 50 employees as SMEs. In accordance with World Bank definition, in Sri Lanka, those with fewer than 49 employees are small; those with 50–99 employees are medium enterprises. Generally, the number of employees as a criterion can be more acceptable because other criteria can be affected by inflation. In accordance with above

said definitions, it is the fact that there are no unique criteria or a unique definition for the small and medium enterprises in Sri Lanka like other countries. In other words, there is no universally accepted definition of SMEs. Apart from the different criteria, various types of definitions were adopted by different official agencies for administrative and statistical purposes (Lakshman, *et al.*, 1991).

3. Literature review

The small and medium industries play significant role in generating employment and has generated eight out of ten employments in America (Birch, 1979). Armington and Odle (1982) indicated that Birch had not controlled for the fact that many new small business, owned by large firms, play an important role in generating job. Davis, Haltiwanger and Schuh (1993) identified several more flaws in the statistical logic underlying Birch's analysis. Moreover, in newly emerging economies of south East Asia such as South Korea, Taiwan, Malaysia, and Singapore have fruitful experience about SMEs which played crucial contribution to boost the economic growth and thereby reducing poverty. In Korea, large firms provided only 0.7 million jobs while SMEs in this country generated 2.5 million jobs, representing 80% of the total employment in the secondary sector in 1996. Biggs and Shah (1998) put forwarded the view from panel data of five countries in sub-Saharan Africa that large firms in the early 1990s emerge as a dominant source of net job creation in manufacturing in all the countries where there had been net job addition. Many small firms are created as a last resort rather than as first choice and have therefore limited growth potential (Liedholm, Mead, 1987). In fact, there are contradictory arguments in regard to role SMEs. In the one hand, SMEs play significant role in boosting economic growth, reducing poverty and rising living standard of their employees i.e America, Germany, South Korea, Taiwan. On the other hand, SMEs does not play the significant role in boosting economic growth, reducing poverty and increasing living standard of workers in many developing countries such as Sri Lanka, Pakistan, and Kenya. Therefore one can observe the fact that the growing body of studies with regard to SMEs indicate that SMEs does not boost employment generations even quality jobs. According to the empirical evidence of micro economic studies, large firms are generating more better and stable employment opportunities, higher wages and non wage benefits compared to small firms in de-

Table 1. Relative size of SMEs in Sri Lanka.

Size of class	1983			1996			2006			2008		
	No of Esta (%)	No of Emp (%)	Val add (%)	No of Esta (%)	No of Emp (%)	Val add (%)	No of Esta (%)	No of Emp (%)	Val add (%)	No of Esta (%)	No of Emp (%)	Val add (%)
Small	86.6	29.2	11.3	70.7	8.6	4.1	65.9	12.2	5.7	63.0	10.2	4.7
Medium	11.4	19.4	19.8	20.1	14.0	8.4	25.9	27.5	26.1	30.0	19.4	15.6
Large	2.0	51.41	68.9	9.2	77.4	87.4	8.4	60.2	68.2	7.0	70.4	79.7
Total	100	100	100	100	100	100	100	100	100	100	100	100

Source: Department of Census and Statistics (Various report).

Abbreviation: No of esta-number of establishment, No of emp-number of employment, val add-value added.

veloped and developing countries (Brown, Medoff, Hamilton, 1990). Further, most of the studies about contribution of SMEs in the national economy conducted in the developing countries do not support to SMEs in accordance with its offering good salary and stable jobs. Moreover, a wide array of evidence rejects the view that small firms are the engine of job formation (Dunne, Roberts, Samuelson, 1989; Sleuwaegen, Micheline, 2002). In India, over the last 15 years, growth of SMEs has significantly been increasing and there is considerable increase in employment generation and economic growth. Many small firms are more capital intensive than large firm in the same industry (Little, Mazumdar, Page, 1987; Snodgrass, Biggs, 1996). This suggests that SMEs are not necessarily more suitable to the labor abundance and capital shortage characteristics of developing countries. In terms of job quality, microeconomic evidence does not support the pro-SME view that small firms create better quality job than large firms. Empirical evidence shows that large firms offer more stable employment, higher wage and more non- wage benefits than small firms in developed and developed countries, even after controlling for differences in education, experience (Brown, Medoff, Hamilton, 1990). Although the pro-SME view argues that small firms are more innovative than large firms, the micro economic evidence is at the best inconclusive. Financially more developed countries tend to have large firms (Beck, Ross, Norman, 2000). This suggests that financial development eases financial constraints on successful firms and allow them to grow. Therefore, in consonance with existing literature, it is can be concluded that Small and medium enterprises are in success in boosting economic growth and reducing poverty and providing quality and better job in developed and newly industrialized countries while SMEs are not in more success in that of most of the developing countries. As said above, SMEs are significantly

contributing to the economic growth and poverty reduction in developed countries in general and developing countries in particular. This is not different in case of Sri Lanka but its potential contribution on Sri Lankan economy is questionable because of various flaws that occurred in the country. As being India and other developing countries, SMEs account for high percentage of establishments in the total number of establishments in Sri Lanka. But contribution of SMEs to the employment generation and value added in India is very high in comparison with that of Sri Lankan economy. In other words, even though Sri Lanka has vast number of industrial establishments of SMEs in total establishment, its contribution to employment generation and value added is very low which hinder the economic growth and poverty reduction. Therefore, large scale enterprises located in urban areas, especially in western province, play significant contribution to the employment generation and value added in Sri Lanka. Thus, it is the fact that full potential capacity of SMEs has not been used to the development of the country. The Table 1 clearly shows the contribution of SMEs to the economy in terms of employment, value added in years of 1983, 1996, 2006 and 2008.

It is the fact that SMEs play crucial role to the economic growth in developed countries in general and developing countries in particular. But, in Sri Lanka, there is difference experience in regard to contribution of SMEs to the economic growth of the country. In other words, contribution of SMEs on the Sri Lankan economy is not significant which does not lead to high economic growth and reduction of poverty. According to the Table 1, small enterprises account for 86.6% of total establishments in 1983. But, even though there is significant number of small enterprises in Sri Lanka, its contribution to the employment and value added is 29.2% and 11.3% respectively. There are 11.4% of medium industries which account for 19.4 %of total

employment and 19.8% of value added. According to this statistics, in 1983, 98% of small and medium enterprises only account for 48.6% of total employment and 31.1% of value added. It is the important fact that only 2% of large enterprises account for 51.4% total employment and 68.9% of value added in 1983. On the one hand, successive years, contribution of SMEs has decreased in Sri Lanka. On the other hand, contribution of large enterprises has continuously increased. In 2006, percentage of establishment of small enterprises is 65.9% and its contribution to the employment is 12.2% and 5.7% for value added. There are 25.9% medium enterprises which have accounted for 27.5% of the total employment and 26.1% of total value added. Though percentage of large enterprises is 8.4% in 2006, its contribution for employment and value added is 60.2% and 68.2% respectively. It is the general observation that there are 91.5% of small and medium enterprises which account for 39.7% of employment and 31.8% of value added in 2006. However, 93% of small and medium enterprises account for 29.6% total employment and 20.3% of value added in 2008. But, only 7% of large enterprises in 2008 account for 70.4% of total employment and 79.4% of value added. In consonance with this statistical analysis, even though small and medium enterprises have accounted for vast percentage of establishment in Sri Lanka, its contribution to the economy is very low. In comparison with small business, contributions of medium enterprises are somewhat significant and insignificant compared with large enterprises in Sri Lanka. What is the important fact is that India is a neighbor country of Sri Lanka in which SMEs play crucial role in the economy, particularly; small sectors' growth is significant in India. Therefore, it can be concluded that although there are significant number of SMEs in Sri Lanka, their contribution to the national economy in terms of employment, output, value added has been very low. However, in

developed countries and newly developed countries, SMEs have contributed significantly to the economic growth and poverty reduction. Particularly, role of SMEs in boosting economic growth and reducing poverty of Sri Lanka is to be analyzed with giving great attention for determinants of poverty.

4. Model, Empirical results and Discussion

As already mentioned above, this study focuses on the impact of SMEs on economic growth and status of SMEs in generating employment and value added. Even though there are number of determinants of economic growth, author tries to find out the relationship between SMEs and economic growth, other things remaining same. On the other hand, the relationship between economic growth, SMEs and poverty has been scrutinized while other things remain constant. In this study, it is expected that there is positive and significant impact of SMEs on economic growth. Furthermore, based on second equation, it is expected that there is negative and significant relationship between economic growth and poverty. The two basic models are, thus illustrated below. In equation (1) Eco. growth refers to economic growth rate. SME refers to employment share of SMEs and ε is stochastic error term. Further, the important assumption is that other factors determining the economic growth remain constant while analyzing the relationship between economic growth and SMEs.

$$\text{Eco. growth} = \beta_1 + \beta_2 \text{SMEs} + \varepsilon_t \quad (1)$$

Based on this equation, output was obtained which is illustrated in Table 2.

Time series data for 2000–2010 time period were used for the estimation using Eviews software. The summarized results of regression are shown in Table 2. The value of R^2 of 0.03 means that about

Table 2. Ordinary Least Square Regression results.

Variable	Coefficient	Std. Error	t-Statistic	Prob.
SME	0.021681	0.156617	0.074582	0.5422
C	4.973857	5.178648	0.960455	0.3619
R-squared	0.030618		Mean dependent var	5.354545
Adjusted R-squared	0.009370		S.D. dependent var	2.752222
S.E. of regression	2.900201		Akaike info criterion	5.132652
Sum squared resid	75.700340		Schwarz criterion	-5.202747
Log likelihood	-26.217220		F-statistic	0.005562
Durbin-Watson stat	1.746616		Prob (F-statistic)	0.041179

Source: Author's own.

Table 3. Ordinary Least Square Regression results.

Variable	Coefficient	Std. Error	t-Statistic	Prob.
SME	0.082312	0.162830	0.547187	0.5992
POV	-0.240883	0.187585	-1.284126	0.0020
C	6.950873	5.233061	1.328260	0.2257
R-squared	0.020140		Mean dependent var	5.354545
Adjusted R-squared	0.110420		S.D. dependent var	2.752222
S.E. of regression	2.800971		Akaike info criterion	5.124810
Sum squared resid	62.763520		Schwarz criterion	-5.233270
Log likelihood	-25.186460		F-statistic	0.827471
Durbin-Watson stat	1.696976		Prob (F-statistic)	0.031369

Source: Author's own.

3 percent of variation in economic growth is explained by SMEs. In accordance with this regression result, as predicted, SMEs has positive relationship with economic growth but not significant. Thus, as SMEs increase, economic growth also increases and vice versa. According to the Table 2, co-efficient value of SMEs is 0.02 indicating 1% increase in SMEs' employment leads to increase in economic growth by 0.02%. But, its p-value is greater than 0.05 indicating that there is insignificant impact of SMEs on economic growth. Further, the model is goodness of fit because p-value of t-statistics (0.041) is less than 5% in the model. Even though R^2 is very low, p-value of t-statistics (0.041) is less than 5% in the model which indicates the goodness of this model. Durbin-Watson value confirms the fact that there is no autocorrelation. From this statistical analysis, one can understand that there is no significant impact of SMEs on economic growth in Sri Lanka. As a matter of fact, many studies about economic growth and SMEs of developed countries and newly industrialized countries show the positive and significance of SMEs. Unfortunately, the same studies in many developing countries indicate that SMEs don't have significant impact on economic growth. This study also proves the above said conclusion that SMEs don't have significant impact on economic growth of Sri Lanka. What is the important observable fact is that we assumed that other factors determining the economic growth remain constant when analyzing the relationship between SMEs and economic growth.

In equation 2, there are two independent variables such as SMEs and poverty head count index. Due to the strong relationship between growth and poverty in many literatures, author has added one more variable, say poverty in this model, other things remaining same.

$$\text{Eco. growth} = \gamma_1 + \gamma_2 \text{SMEs} + \gamma_3 \text{POV} + \varepsilon_1. \quad (2)$$

Same time series data for 2000–2010 time period were used for the estimation using Eviews software. Poverty and SMES are explanatory variables. The value of R^2 of 0.2 means that about 20% of variation in economic growth is explained by SMEs and poverty. In this regression analysis, what is the observable fact is that when adding poverty with variable SMEs, R^2 value has increased by 17% implying poverty is important determinant of economic growth in Sri Lanka. Many empirical studies express the view that poverty both negatively and significantly affects the economic growth. Therefore, significant improvement of living standard of people will lead to considerable reduction of poverty. SMEs in developed and newly industrialized countries prove the fact that SMEs have had significant improvement of poverty and living standard of workers who are working in SMEs. Thus, the growths of SMEs are effective remedial measures to solve the problem of poverty and stagnant economic growth. In accordance with regression result of Table 3, as predicted, economic growth has positive relationship with SMEs and negative relationship with poverty. According to the Table 3, co-efficient value of SMEs is 0.08 indicating 1% increase in SMEs' employment leads to increase in economic growth by 0.08%. But, its p-value (0.590) is greater than 0.05 indicating that there is insignificant impact of SMEs on economic growth of Sri Lanka. Furthermore, co-efficient value of poverty is -0.24. Thus, 1% decrease in poverty leads to 0.24% increase in economic growth and vice versa. Its p-value is 0.002 that indicates the significance of variable-poverty in determining economic growth. Further, the model is goodness of fit because p-value of t-statistics (0.03) is less than 5% in the model. Even though R^2 is very low, p-value of t statistics (0.03) is less than 5% in the model which indicates the significance of this model. In comparison with SMEs, poverty has more significant impact

on economic growth, as said many existing literature of developing countries in regard to studies of SMEs and poverty. Further Sri Lanka is also lower middle income country and as a result, most of the rural and estate people are living very poor condition. Durbin-Watson value confirms the fact that there is no autocorrelation. From this Table 3, one can understand that there is not significant impact of SMEs on economic growth in Sri Lanka. But, poverty significantly affects the economic growth. As a matter of fact, many studies about the relationship among the economic growth, poverty and SMEs of developed countries and newly industrialized countries show the significance of SMEs and their promotion. The same studies in many developing countries indicate that SMEs don't have significant impact on economic growth. The output of this study also proves the above said conclusion that SMEs don't have significant impact on economic growth of Sri Lanka while poverty has significant effects on economic growth.

5. The private-public participation (PPP) and its benefits to SMES

Above analysis clearly indicates the fact that promotion and encouragement of SMEs are important to accelerate the economic growth and thereby reducing poverty. Further, government and other public and private organizations should play massive role in promoting SMEs and thereby boosting economic growth and alleviating poverty. Natural resource endowment, technology, policies, help of institution determine nation's industrial composition and growth (Kumar, Raghuram, Randzinglaes, 2001). Even though poverty negatively affects the economic growth, it is the remedy for this issue is private public co-operation which will induce the growth of SMEs and thereby reducing poverty ridden condition. If it has happened properly, economic growth will be automatically accelerated which leads to reduction of poverty. Therefore, one can understand that there is causal relationship among the variables. It needs to be further analyzed.

Minna (2007) emphasized a Policy and Operational Guidelines for PPP for growth of SMEs. The guidelines points out what PPP is and its special features, ways of PPP and its benefits etc. The concept of PPP has evolved for centuries in the USA and Europe but has become more prominent in recent decades in local economic development. PPP is the idea of bringing in private finance to finance public sector infrastructure originated with the early occurrences of PPP. It is further referred to as a

contractual arrangement between a public sector agency and a for-profit private sector concern, whereby resources and risks are shared for the purpose of delivery of a public service or development of public infrastructure. PPP arrangements are growing in use and acceptance as an alternative and effective method to organize additional financial resources and benefits from private sector efficiencies. There is no private sector participation in building up infrastructural facilities in Sri Lanka. Generally, small and medium and large enterprises in Sri Lanka think that government has full responsibility in the poverty alleviation, infrastructural development and social development. It is entirely wrong notion which hinder the overall development of country. There has been no macro-level policy for the development of the sector although there have been some incentives provided by different programs until late 1950s. However, recently there have been a large number of institutions directly involved in the promotion of the small business sector in Sri Lanka. Their assistance vary from formulating policies, strategies, and programs such as providing credit, training, technology, marketing sub-contracting, and management. In addition to the government organizations, there are a large number of NGOs involved in the promotion of the small business sector by providing various types of assistances. Many of them were set up after the 1977 reforms. Government of Sri Lanka has taken various measures to promote the SMEs.

Ministry of youth affairs and sports which is main policy making body relating youth development conducts some small enterprise development programs, especially focused on the youth of the country in which the Small Entrepreneurship Development Division and National Youth Co-operatives (NYSCO) are playing role in the development of small business. Ministry of traditional industries and small enterprise development which has several sub-councils and boards is also providing various promotion and assistance for the small business in Sri Lanka. In addition, some government departments and boards such as Department of Rural Development and Cottage Industries, Industrial Development Board (IDB), Department of Textile, Sri Lanka Handicrafts Board (SLHB), National Design Center (NDC), Ceylon Institute of Scientific and Industrial Research (CISIR) are providing facilities such as financial technical and marketing, management assistances to develop the SMEs. So as to increase the export income of SMEs and national contribution of SMEs, export development board and above said departments have offered various facilities for SMEs. For the loan facilities

to be facilitated there is two important government banks such as people bank and bank of Ceylon in Sri Lanka. The establishment of People's Bank and the nationalization of Bank of Ceylon in 1961 were land marks in providing institutional credit to SMEs. Bank of Ceylon branches and its sub offices at Agrarian Services Centers provided credit facilities under special programs to SMEs. National development bank and Samurdhi bank are also providing loan facilities for development of SMEs. In addition to this, some domestic private banks have also introduced special facilities to these industries with the expansion of their branch network. In accordance with a national strategy of development of SMEs, Enterprise Promotion Bank (SME Bank) was recently established by the government. The government of Sri Lanka has realized the importance of SMEs for its economy and as a result, it has taken the initiative in setting up a new licensed specialized bank called the SME Bank in year 2005. The purpose of establishing the SME Bank is to promote the micro, Small and Medium enterprises via the provision of financial and technical assistance on a vigorous and sustainable basis. What is the observable fact is that enterprises in initial stage or poor small businesses are still undergoing financial difficulties having launched several special banks and credit facilities. Notwithstanding the number of institutions have been established to promote the SMEs, it is the fact that there is no significant co-ordination of activities among the existing organizations in Sri Lanka. Particularly, even though there are many government departments and boards, they have not had common effective policy or effective coordination for the development of SMEs in comparison with developed countries. This is significant flaws that have been decreasing the effectiveness of the various activities and programs related to SMEs. Thus, effectiveness of SMEs on economy is not considerable. Further, a strong relationship exists between the quality of business environment and long-term national economic performance, including pace of poverty.

Conclusion and Recommendation

Notwithstanding several literatures related to SMEs have articulated the fact that SMEs can play important role in boosting economic growth, employment generation, accumulation of capital and poverty reduction, this experience is not consistent with Sri

Lanka. In other words, direct contribution of small and medium enterprises in changing poverty status and boosting economic growth is questionable in Sri Lanka. For instance, in 1983, 98% of small and medium enterprises only account for 48.6% of total employment and 31.1% of value added while 2% of large enterprises accounts for 51.4% total employment and 68.9% of value added in 1983. However, 93% of small and medium enterprises account for 29.6% total employment and 20.3% of value added in 2008. But, only 7% of large enterprises in 2008 account for 70.4% of total employment and 79.4% of value added. In consonance with this statistical analysis, even though small and medium enterprises have accounted for vast percentage of establishment in Sri Lanka, its contribution to the economy is very low. Further, despite there is positive relationship between economic growth and SMEs, impact of SMEs on economic growth is not significant in Sri Lanka. The co-efficient of SMEs is 0.02 indicating that there is positive relationship between economic growth and SMEs but impact of SMEs on economic growth is insignificant. Same conclusion in regard to relationship between economic growth and SMEs is derived in Table 3. It is the fact that as expected, negative and considerable impact of poverty on economic growth has been in Sri Lanka.

The output of this study clearly proves the conclusion that SMEs don't play significant impact on economic growth of Sri Lanka while poverty has significant effects on economic growth. In consonance with general believes, SMEs can simultaneously play double role in boosting economic growth and alleviating poverty. Thus, as remedial measures, government and other non-governmental organizations should assist for existing small and medium enterprises as well as its new establishment in effective manner. Even though there are number of government organizations for promoting SMEs in Sri Lanka, co-ordination among them is questionable and ineffective. Furthermore, public private participation (PPP) is sine qua non to the effective promotion of SMEs which leads to economic growth and poverty reduction. Visionary government can launch effective PPP which is remedy for the successful promotion of SMEs and thereby boosting economic growth.

Therefore, active private public participation is needed to accelerate the growth of SMEs and improvement of SMEs and thereby, its contribution to the economy can be enhanced like developed countries.

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Dr. Sinnathurai Vijayakumar

Faculty of Economics and Management

Tomas Bata University

Mostni 5139, 760 01 Zlin

Czech Republic

Senior Lecturer, Department of Economics

University of Jaffna

Sri Lanka

e-mail: vijai114@gmail.com