

A Study on MSME – Availability of Finance and Way Forward in India

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Abstract: Objective: The research aims to assess the Credit Gap to MSME and also to measure the impact of Digital Finance to MSME. The research also aims to suggest measures to increase Finance to MSME in India.

Methodology: The Study was based on both Primary and Secondary Data. The secondary data was obtained from several credible sources of data, research literature, industry publications. The primary data was obtained by conducting primary interviews for evaluating size of the MSME finance market and the results validated with various stakeholders.

Findings: The overall finance demand by MSME is 69.30 trillion, with 70% of the requirement attributed to meeting working capital requirements. It is imperative to address huge credit gap that exists in meeting urgent fund requirements. Non availability of MSME - focused products. FinTech's are using technology to eliminate market inefficiencies, making lending more accessible, affordable, and contextual for MSMEs. The shift brought about by digital lending is changing the optics of MSME lending. What was once an onerous and time-consuming task is becoming an easily accessible business decision with the synergy of new age players, banks and government regulations.

Conclusion: Regulated entities (RE) are to provide a Key Fact Statement (KFS) to the borrower before the execution of the contract • RE's must disclose all inclusive costs of digital loans in form of annual percent rate (APR). Loan disbursements and repayments are required to be executed only between the bank accounts of the borrower and the regulated entity without any passthrough/pool account of the loan service provider or any third party. RE's must ensure that all loan service providers engaged by them have a suitable nodal grievance redressal officer to deal with digital lending-related complaints • Any complaint must be dealt within 30 days, borrowers have option to escalate it to the Ombudsman.

Keywords: SME's, Start-Up India, SME Finance, Digital Lending.

1. Introduction

The Micro, Small and Medium Enterprises (MSME) is one of the vibrant and dynamic sectors of the Indian Economy since 1980s. It played a vital role in economic and social development of the Nation by encouraging entrepreneurship there by creating huge employment opportunities with low capital cost. MSME is employing the most numbers next to agriculture in the country. MSME sector in India is playing a vital role in reducing regional imbalances and ensuring equitable distribution of Income and wealth across the country. The MSME's are committed to deliver an array of product and services meeting the domestic and global market demands. The MSME sector had witnessed a steady growth of over 10% during the past few years. It is representing the innovative nature of the Indian entrepreneurs providing solutions to various problems despite social, resource and logistic challenges across the country. The share of MSME in India's GDP (Gross Domestic Product) during FY 2021-2022 was at 29%. It contributes 36.20% of the country's manufacturing output during FY 2023. MSME contributes 49.40%, 45.00% and 43.60% of total exports of the country during FY 2020-21, FY 2021-22 and FY 2022-23 respectively. This research is directed by the following objectives.

1. To assess the Credit Gap to MSME in India
2. To assess the impact of Digital Finance to MSME in India
3. To suggest measures to increase Finance to MSME in India.

2. Literature Review

According to International Finance Corporation (2018), the demand for debt and equity finance of MSMEs were estimated at INR 87.7 trillion with INR 69.3 trillion of debt and INR 18.4 trillion of equity demand. After

excluding sick enterprises, startups and micro enterprises that prefer finance from the informal sector, the net debt demand is estimated at INR 36.7 trillion, which forms 53% of the total demand. The study revealed that 84% of the total debt demand was financed by informal sources. Only 16% of the debt requirement was met by the formal sources. Out of which, only 81% of the formal source of fund was provided by scheduled commercial banks. The rest of the debt fund was provided by NBFC, Small Finance Banks, Urban Co-operative Banks and Regional Rural Banks.

The Gap in meeting the credit needs were estimated at INR 25.8 trillion and the same is expected to be funded by the formal sources. It is also of the view that the enterprises getting its debt requirement from the informal sector can be included in the viable financial sector with appropriate policy interventions. The report further provides that, the medium enterprises in India are relatively well financed.

Three main pillars of the enabling the environment as per the study are; (a) legal and regulatory framework (b) government Support (c) financial infrastructure support.

Huang & Brown (1999); Chow & Fung (2000); Berger et al. (2001); Berger & Udell (1998, 2002); Radelet and Sachs (2001); Bracker et al. (2006); Mandal et al. (2008); Zeffane & Zarooni, (2008); Thevaruban, (2009); Rahaman,(2011) , Researchers found that because of bankruptcy there is a high risk of failure of enterprises. Studies conducted by researchers found that an inadequate financial resource is the main problem of SMEs which creates hurdles in the growth and development of MSMEs. MSMEs can obtain debt with the sufficient level of collateral. MSMEs owners should follow financial management practices then financial institutions can lend loan to them.

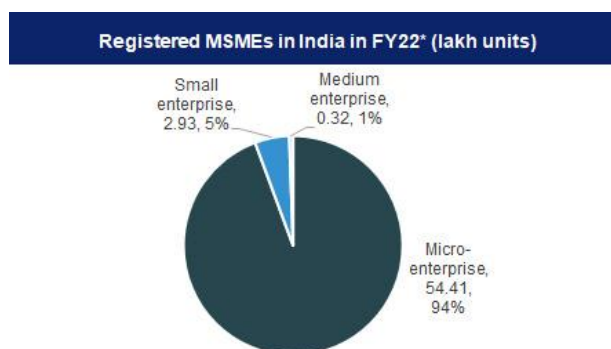
Noorinasab, Seifabad & Zarei, (2016), Entrepreneurs face problems like for startup how to raise capital, inadequate fund. Many entrepreneurs are unable to access external funds because of inadequate security and credit in market. The process of loan availing facility is time consuming .Other problems is decrease in profit because of competition, financial statements are not properly maintained by entrepreneurs of MSMEs, inadequate guarantees for raising loans, through equity problem in raising capital, dependent on money lenders for loans which are high cost.

Siddiqui, (2018), During early growth stages micro, small and medium enterprises need timely and sufficient capital. MSMEs rely on various sources of finance. Various financial problems are inadequate and non-timely credit, limited knowledge and capital, collateral security requirement, not sufficient working capital, recovery from debtors, for availing loan from financial institutions excessive paper work is required.

Definition of MSME

In accordance with the provision of Micro, Small & Medium Enterprises Development (MSMED) Act, 2006 the Micro, Small and Medium Enterprises (MSME) are classified as below:

- (i) a micro enterprise, where the investment in plant and machinery or equipment does not exceed one crore rupees and turnover does not exceed five crore rupees;
- (ii) a small enterprise, where the investment in plant and machinery or equipment does not exceed ten crore rupees and turnover does not exceed fifty crore rupees; and
- (iii) a medium enterprise, where the investment in plant and machinery or equipment does not exceed fifty crore rupees and turnover does not exceed two hundred and fifty crore rupees.



Source: Annual Report 2023, Ministry of Micro and Small Industries.

3. Methodology

The Study was based on both Primary and Secondary Data. The secondary data was obtained from several credible sources of data, research literature, and industry publications. The primary data was obtained by conducting primary interviews for evaluating size of the MSME finance market and the results validated with various stakeholders.




MSMEs borrow from informal sources for financing their needs due to lack of documentation or credit footprint. Credit access can help unorganized MSMEs integrate into the formal economy, compete with the global players and gradually transition into the organized formal sector.

The overall finance demand by MSME is 69.30 trillion, with 70% of the requirement attributed to meeting working capital requirements. Working Capital finance is an important aspect of fledging MSME business. It is imperative to address huge credit gap that exists in meeting urgent fund requirements. Non availability of MSME - focused products. The Government had revised the definition of MSMEs by providing a composite criterion of Investment in plant and machinery and the Annual Turnover, to fuel the rising financial needs of the MSMEs. On the other hand, the rise in Digital Lending provides opportunities for the MSMEs further growth which enables them even to market their product in GeM (Government E-market place).

MSME Credit Landscape in India

Retail Lending	<ul style="list-style-type: none"> ➤ Personal Loans ➤ Credit Cards ➤ Consumer Durable loans ➤ Two-wheeler Loans ➤ Home Loans ➤ Auto Loans ➤ Business Loans
Micro-Finance Lending	<ul style="list-style-type: none"> ➤ Increasing per-capita income ➤ Loans for small entrepreneur ➤ Towards medical emergency by way of consumption loans ➤ Home construction & extension / renovation loans
Commercial MSME lending	<p>Working Capital Loans:</p> <ul style="list-style-type: none"> ✓ Overdraft Facility ✓ Reducing OD ✓ Kissan Credit Credit ✓ TReDS (Trade Receivables Discounting) ✓ Bank Guarantee ✓ Letter of Credit
	<p>Term Loans:</p> <ul style="list-style-type: none"> ✓ Secured Term Loan ✓ Loan for acquisition of Fixed Assets ✓ Addressing long-term working capital gap ✓ Project Loan ✓ Loans backed by CGTMSE (Credit Guarantee Trust for Micro and Small Enterprise) guarantee.

Source: Prepared by Authors (2024).

S. no.	Parameters	 Retail	 Micro Finance	 Commercial	Overall
1	Portfolio as of Mar'22 (in INR T)	85.2	2.9	86.3	174.4
2	Growth (% FY21-22)	13.6%	10%	8.6%	11.1%
3	Contribution to total lending (%)	48.9%	1.6%	49.5%	
4	Originations Value (FY22, in INR T)	42.3	2.3	66.5	111.1
5	Growth (% FY21-22)	22.9%	23.2%	73.2%	
6	Originations Volume (FY22, in L)	2310.7	614.8	22.2	2947.7
7	Growth (% FY21-22)	38.5%	13.1%	-4.3%	

Source: CRIF, Secondary Research, 1 Latice Analysis.

4. Factors Impacting Adequate Finance:

Collateral Requirement: The MSME does not have fixed / movable assets to hypothecate for the proposed loan to be availed by them. It prefers unsecured loans to meet the business needs at a competitive rate to meet the market expectations by offering cost effective services and products.

Financial Literacy: Due to non-availability of financial awareness, they often tend to borrow at high costs or sourcing short term finance for long term needs there by creating liquidity problems and ending up in resorting to high cost debts available in the informal segments. At times they also fail to chose the right lender for the working capital / term loan requirements which results in high borrowing costs.

Limited Penetration: Bank's and Non-Banking Finance Companies still finding difficult to address the credit requirements of the entire nation in terms of geography. Still major part of rural and semi-urban areas are being under banked. Though, the fintech and digital lending parterns are trying to bridge the gap, still a considerable population is left un-banked both in terms of lending and savings.

Complicated Process and Documentations: Often the financial institutions lending to the MSMEs need variety of documents to be produced and executed to avail the loan. The MSME units were not able to avail the immediate requirement of funds, since they were not able to comply with the requirements on time.

Schemes floated by Government of India to Increase the access of Finance by MSMEs

1. Pradhan Mantri Mudra Yojana (PMMY)
2. Credit Facilitation through Banks by NSIC
3. Prime Minister Employment Generation Programme (PMEGP)
4. Credit Guarantee Trust Fund for Micro & Small Enterprises (CGTMSE)
5. SIDBI Make in India Soft Loan Fund for MSMEs (SMILE)
6. Credit Linked Capital Subsidy Schemes (CLCSS)

Way Forward:

- ❖ Fintech and NBFCs can help banks overcome information asymmetry regarding MSMEs
- ❖ Demonetization, followed by COVID-19 encouraging the units to go digital
- ❖ Improved access of high-quality data from credible sources like GSTN
- ❖ Implementing efficient underwriting process by verification and validation of transactional information.
- ❖ Data analysis and technology to assess digital foot print and establish creditworthiness of MSMEs with lack of credit history
- ❖ Fintech lending with contactless, paperless, cashless and consent based.

5. Conclusion

The majority of the credit deficit will be required to be filled by structural, market-driven solutions. As a result, fintechs/new age players are using technology to eliminate market inefficiencies, making lending more accessible, affordable, and contextual for MSMEs. The Indian government intends to increase annual MSME financing disbursements to roughly INR 6 lakh crore by 2023. Banks have sanctioned loans worth Rs 3.1 lakh crore under the ECLGS for the MSME sector. The shift brought about by digital lending is changing the optics of MSME lending. What was once an onerous and time-consuming task is becoming an easily accessible business decision with the synergy of new age players, banks and government regulations. As MSME lending in India is still at its nascent stages, there is a need to regulate the landscape. The holes in the system were highlighted during Covid, as unregulated lenders flouted consumer protection norms putting MSME borrowers at more financial risk than they started with. Open digital ecosystems in India like Aadhar & India Stack are the springboard for the proliferation of digital lending. As a guardrail for this rapid growth, the RBI introduced the Account Aggregator framework which aims to further simplify the process of disbursing credit digitally. Digital lending business can be carried out only by entities that are - either regulated by the RBI, or - entities permitted to do so under any other law. The MSME Samadhaan portal allows MSMEs to directly register cases of delayed payments against buyers of goods/services with the Micro and Small Enterprise Facilitation Council (MSEFC). Regulated entities (RE) are to provide a Key Fact Statement (KFS) to the borrower before the execution of the contract • RE's must disclose all inclusive costs of digital loans in form of annual percent rate (APR). Loan disbursements and repayments are required to be executed only between the bank accounts of the borrower and the regulated entity without any passthrough/pool account of the loan service provider or any third party. RE's must ensure that all loan service providers engaged by them have a suitable nodal grievance redressal officer to deal with digital lending-related complaints • any complaint must be dealt within 30 days, borrowers have option to escalate it to the Ombudsman.

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