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MSME Enterprises and Bank Finance: An Investigation of Loan Advancement Policies

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Abstract

The micro, small, and medium-sized enterprise (MSME) sector is now playing a crucial part in India's economic growth. A driver for socio-economic development of the country, the sector is crucial in accomplishing the national goals of producing employment, alleviating poverty, and preventing rural-urban migration. These businesses not only encourage the use of local technology, but also contribute to the development of a flourishing entrepreneurial eco-system. The industry has also showed sustained growth over the previous several years, but it has done so in a limited context frequently subsequent in incompetentmeansutilisation. Small and medium-sized businesses (SMBs) are more susceptible to economic downturns because of the numerous obstacles in their way, including limited access to financial resources. Some businesses play pivotal roles in the value chains of many sectors. Issues that have an effect on the establishment, development, and maintenance of businesses in the sector are, therefore, of the utmost importance. The significance of the part played by credit advancingestablishments in the current growth of the MSME sector cannot be overstated. The government and financial institutions in India have made significant contributions to the growth and success of the MSME sector. This study provides an in-depth examination of the steps taken by Indian micro, small, and medium-sized enterprises to expand and flourish as a result of the recent economic liberalisation. The second half of the article examines the current situational involvement of different financial institutions in the nationwide growth of MSME's. This study's secondary objective is to assess the prospects for and barriers to raising capital via different financial institutions in the industry, a factor that policymakers need to take into account for improved, long-term outcomes.

Keywords: MSME, India's Growth, Financial Institutions, Economic Liberalisation

Introduction:

Small and medium-sized businesses (SMEs) in India rely deeply on support of the nation's financial institutions. SMEs are vital to India's economy because of the jobs they create, the goods they manufacture, and the goods they ship overseas. The expansion of SMEs in India may be traced back to the support of financial institutions in a number of ways. Money Availability: Access to capital is provided to SMEs by financial institutions such as banks and non-banking financial firms (NBFCs). Working capital, growth, adoption of technology, and capacity development are just few of the many uses for which this money is crucial. Small and medium-sized enterprises (SMEs) may use loans and credit facilities to finance capital expenditures including new projects, equipment purchases, and operations costs. This, in turn, stimulates corporate growth and adds to the general economic development.

Contingency Planning: In order to assist SMEs in managing and minimising risks, financial institutions often provide a range of financial products and services. Financial goods and services designed to address the unique challenges and dangers encountered by SMEs. Financial institutions assistance SMEs by making them more robust to economic uncertainty by offering instruments for risk management. Adopting New Technologies: Banks and other lenders may help SMEs adopt new technologies. They aid in the modernization of small and medium-sized business operations by providing financial solutions that facilitate the use of cutting-edge technology including digital payment systems, and enterprise resource planning (ERP) software.

Technology advancements boost a small or medium-sized enterprise's (SME) ability to compete in both home and international markets. Strengthening Institutions and Expanding Capabilities: Some banks provide courses and other resources to help SMEs recover their capabilities and professional skills. The goal of these courses is to provide company owners with the tools they need to manage and grow their enterprises. Small and medium-sized enterprises (SMEs) benefit from capacity development because it allows them to remain competitive in the face of changing market circumstances. Economic Equality: Reaching out to SMEs that are underserved or otherwise unbanked is one way in which financial institutions promote financial inclusion. This entails extending banking and related financial services to demographics who have hitherto had less access to mainstream financial institutions.

As a result of increased financial inclusion, SMEs are better able to join the formal economy, have access to loans, and take part in economic activities. Promotion of Policy: Banks and other financial organisations often lobby for pro-SME measures. Specifically, this means pushing for tax breaks, simplified regulations, and other policies that help small and medium-sized enterprises thrive. In essence, the influence of financial institutions on the development of India's SMEs is diverse. Financial institutions play a crucial role in fostering the development and sustainability of small and medium-sized enterprises in India by providing access to capital, mitigating risks, encouraging the adoption of technology, bolstering capacity building, promoting financial inclusion, and engaging in policy advocacy.

Literature Review

"Micro, Small and Medium enterprises" is anpart of countlessattention for numerousinvestigators. This is because the industry is becoming more vital in sustaining the livelihoods of a sizable portion of the people. Both public and private employers have failed to keep up with rising demand for workers. So, for millions of unemployed individuals, the rise of entrepreneurship is a welcome sign. MSMEs are highly productive, even when compared to bigger companies and they have a firm position notably in emerging countries (Agyapong, 2020).

According to Bhaird and Lucey (2021), "firms in the nascent stages of development are largely dependent on resources of the firm owner, friends, and family" in Ireland. With indirect financial systems predominating in Asia, Shinozaki (2021) argues that improving the efficiency of bank lending to small and medium-sized enterprises (SMEs) should be a top policy goal. In addition, he says, "the number of growth-oriented SMEs is expected to increase, and they will seek increased access to the formal financial system." Supporting growth-oriented SMEs necessitates boosting financial accessibility via a wider range of funding options and improved infrastructure. Due to the difficulty of the application procedure, Saini (2014) discovered that commercial banks are not the major source of financing for most MSMEs in New Delhi. They cannot get loans since they do not have sufficient collateral or positive balance sheets. "not only does it discourage aspiring entrepreneurs but also plays a huge role in holding back the growth of existing firms," the author writes.

Based on their research, Osotimehin et al. (2021) concluded that "a vast majority of the respondents indicated that lack of financial support from the government and financial institutions are problems hindering the establishment of small and medium enterprise in many states in Nigeria." The most significant barrier to entry for new small and medium-sized businesses is a lack of initial funding. It was suggested that "the government should re-introduce the small business credit scheme so that beneficiaries can use them to run the micro, small, and medium enterprises" (MSME) since it was what the research indicated was needed.

"the association between business finance sources ranging from finance provided by friends and family to British government sourced finance and e-commerce as a trading activity" was evaluated by Pickernell, Jones, Packham, Thomas, White, and Willis (2021). It was shown that engaging in e-commerce had a positive effect on both private wealth and public coffers.

Major objectives of the study:

Following are some of the primary goals of this research:

- To Learn About and Analyse MSME's Role in India's Economy.
- To observe the function of banks in the development of Indian SMEs.
- To examine the potential and threats facing India's micro, small, and medium enterprises.

Research Methodology:

All of the necessary information for this investigation has been gathered from secondary resources. The information used in the research comes from two sources: i) annual reports of MSMEs and ii). Reports on MSME from SIDBI, version iii). Fourth document from the Ministry of Small and Medium-Sized Enterprises. Bureau of Indian Affairs Annual Reports v). Numerous topic-specific online resources.

Discussion

MSMEs in India are becoming more relevant as a result of the important roles they play in the Indian economy. More than 90% of India's industrial units are micro, small, and medium-sized enterprises. The government is implementing a number of measures to encourage the manufacturing sector, which will benefit the economy as a whole. The establishment of multiple organisations for policy creation and funding allocation via Five Year Plans provides insight into the government's commitment to industrialization. Formation of National Manufacturing Competitiveness Council by Government offers strategies to promote competitiveness in the manufacturing sector to make it internationally competitive. In order to increase manufacturing's contribution to GDP to 25% by 2021, the government has launched the National Manufacturing Policy. The new government of India declared Make in India in September 2014 with the intention of turning India into a major manufacturing centre in the world.

RELIABLE FUNDING SOURCES FOR SMALL AND MEDIUM-SIZE ENTERPRIS

Most Indian small and medium-sized enterprises (SME) fund themselves. Fourth MSME sector census finds 87.23 percent of businesses fall into "self-finance/no finance" category. This significant reliance on "self-finance/No finance" may be attributable to the prevalence of "Micro enterprises" among the sampled units. In India, micro enterprises account for 94.94% of all MSME units, with small firms making up 4.89% and medium-sized businesses making for just 0.17%.

Receivables management via factoring services may help small and medium-sized enterprises (SMEs) who lack access to sufficient finance options. Concern about late payments from corporate buyers has long been a major problem for micro, small, and medium-sized businesses. The Indian financial sector has to be more aggressive in financing factoring receivables. When it comes to gaining access to working capital, small and medium-sized enterprises (SMEs) throughout the world choose factoring. In 2011, India passed the Factoring Regulation Act, which is widely anticipated to increase demand for factoring services in the country. The open account capability that comes with factoring allows the company's credit limit to expand in tandem with its sales, if the company has a good payment history.

Issues with Micro, Small, and Medium-Sized Enterprise Financing:

It is impossible to increase lending to MSMEs deprived oftalking the reluctance of traditional financial institutions similar banks to do so. MSMEs are viewed as high risk mortgagors owing to reasons such as limited properties and low capitalization. Companies with a high susceptibility to economic and marketing volatility tend to fail at a higher rate. The number of failing businesses in India's MSME sector rose by 16% from March 2017 to March 2018 (from 77,723 to 90,141). If a unit has been in commercial production for at least two years and one or more of its borrower accounts remains substandard for 6 months, or if the unit's net worth declines as a result of accumulated cash losses totaling more than 50% of its net worth during the previous accounting year, then the unit is considered sick under the current definition. There was a 9.8% share of MSEs in banking system loans during the 2017–18 fiscal year, and a 17.9% proportion of MSEs in banking system Non Performing Assets (NPA) during the same time period. The increasing trend of nonperforming assets and the large number of small and medium-sized enterprises going bankrupt both constitute a serious threat to financial institutions. Credit flow to the industry is hampered by the knowledge asymmetry that emerges when lending to MSMEs. Since it is not financially viable for banks to gather data on a significant number of small businesses, access to credit information on them is limited. As a consequence, the cost of knowledge asymmetry is often included into loan rates. Lenders have trouble determining which projects are viable and which are risky due to information asymmetry. According to the latest MSME sector census, 90.08 percent of businesses are privately held. Lenders are wary about the industry as a whole since so many businesses are solely reliant on their founders and lack adequate succession plans. Smaller businesses depend too much on the owners since they lack the resources to engage sufficient staff. Most MSMEs cannot provide sufficient security, thus lenders must place more faith on the technical, managerial, and marketing expertise of borrowers in order to recoup their loan losses. Lack of openness and reliable data, lack of financial discipline, and inability to produce strong financial track record are additional issues that lenders face when working with MSMEs.

M&S Contribution to Production and GDP:

More than 45 million units, or more than 90% of industrial units, contribute significantly to the country's economic development. MSMEs manufacture has constantly expanded over the span of previous several years and reached at Rs. 671910 Crore i.e. 37.52% of total industrial output at the end of FY19. MSME have also shown their efficacy as an engine of job generation, with a total of 1011.8 Lakhs employed as of the end of FY19 and a yearly rate of employment creation of roughly 1.5 million.Financial planning for micro, small, and medium-sized enterprises: money is what keeps the wheels turning. Most small and medium-sized businesses in India are part of the unorganised economy and have trouble getting access to consistent funding. While it was formerly difficult for start-ups to get seed money, today's entrepreneurs are often able to do so via other, less formal means. Term loans and working capital loans are particularly important for growing and established small and medium-sized businesses. The following have been the primary funding mechanisms for Indian MSMEs:

Money put aside over time, inherited wealth, loans from loved ones, and funds from unchecked markets. Institutional finance from schedules commercial banks Venture capital funds / seed funds Retained profits, funding's from sale of important assets. The federal government, individual states, and financial institutions have all established organisations to foster the growth of MSME.

Minority- and women-owned MSMEs in India have emerged as a driving force behind the country's economic growth. The government recognises the importance of MSMEs and periodically takes measures to foster their growth and expansion. Analysis shows that the government has poured a lot of money into the manufacturing, service, and retail (MSME) sector over the course of five year plans to help it become more competitive. Key success factors need special attention in a country like India, whose economy is still maturing. The same thing has happening to Indian MSMEs, and it has caught the attention of policymakers and academics.

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Comparison of Bank Loans to Fixed Investments and Output at MSME:

The performance of Indian MSMEs throughout time shows great development in output. Policymakers and financial institutions have taken notice of production since it accounts for 45% of industrial output and 40% of exports. Various measures undertaken by Government of India and Small Industrial Development. Bank of India (SIDBI) led to financial inclusion and development of MSME sector in recent years. Bank loans for fixed asset investment and manufacturing by MSME are also on the rise, at 33% and 22%, respectively. The rise in the availability of financing is a reflection of policymakers' attention to the importance of a flourishing MSME sector to the national economy.

Table 1

Share of Gross Value Add (GVA) and Gross Domestic Product (GDP) of MSMEs in India (Figures in Rs. Crores adjusted for FISIMat current prices)

Year	*Total MSME GVA*	*Growth%*	*TotalGVA*	*Share of MSME in GVA (%)*	*All India GDP*	*Share of MSME-in All India GDP (in%)*
2012-13	2977475	14.99	9202597	31.24	9944102	30.01
2013-14	3343124	13.01	10363241	33.21	11233721	30.22
2014-15	3658217	9.61	11504369	30.99	12467875	30.81
2015-16	4059874	11.00	12574745	33.51	13771921	30.51
2016-17	4502259	11.21	13965451	33.91	15391784	30.27
2017-18	5086863	13.25	15513247	33.01	17098627	30.11
2018-19	5741978	13.74	17139899	34.10	18971945	31.01

Source: Annual Report MSME-2020-21

The following is a list of the products and services offered by financial institutions that provide loans to the MSME sector:

Banks that lend money to the micro, small, and medium-sized enterprise (MSME) sector may be broken down into two groups, depending on the kind of money they lend out. The loan supply from financial institutions to MSMEs has been boosted by the general government assistance and the competitive legal and regulatory environment. Boosting the availability of finance would help the MSME sector grow and become more competitive on the international stage. The government's target of a 25% manufacturing contribution to GDP by 2021 may be reached if MSME is provided with upgraded technology, tool room facilities, incubators, and entrepreneurial training facilities.

Major obstacles that the MSME sector must overcome include:

There is a massive disparity between the availability of credit and the demand from the MSME sector, notwithstanding the efforts of the government of India and the Reserve Bank of India. The expansion of the industry is impeded by more than just a lack of finance. The following are examples of such difficulties:The most pressing issue that MSMEs confront is financial exclusion. According to data gathered in a recent survey of the MSME sector, just 5.18 percent of businesses reported using institutional financing, 2.05 percent used non-institutional financing, and 92.77 percent were entirely self-funded via informal means. To make the MSME sector internationally competitive and to achieve GDP objectives or expectations, these issues must be resolved. To meet the demands of this industry, the government must take the initiative.

Infrastructure: India is striving to provide world-class support for MSME. The private sector is hampered in its efforts in this area by inadequate infrastructure. As a result, improving the infrastructure for MSME's should be a top focus.Advertising: The IT revolution has destroyed the previously presumed market for items made by MSME. Promotion of a wide range of IT-based product applications for use in marketing is warranted to boost MSME competitiveness.

Technology: Due to the significant up-front costs associated with adopting new technologies, MSMEs are falling behind their larger counterparts in this area. The promotion of the Sustainable Business Model approach to MSMEs should include a number of enticing packages.Need for trained work: The key restriction of MSME sector is availability of trained work force. The government should create a paradigm for bringing together academia and business to achieve this goal. Students' chances of gaining the theoretical background and practical experience valued by employers are boosted by this kind of instruction.

Small and Medium-Sized Enterprises' Role in Creating Jobs:

Micro-, small-, and medium-sized businesses are widely acknowledged for the positive impact they have on national economies. Some writers suggest that SMEs play a crucial role in creating jobs in developing nations because they: Use more labor-intensive production techniques than big enterprises, which increases employment and leads to more equal income distribution. Offer a means of subsistence in economies dependent on agriculture via basic value-adding processes. Support the development of systemic production capacity and the emergence of robust economic systems by encouraging collaboration between small and big businesses.

Conclusion

In various established and emerging economies across the globe, MSMEs have emerged as an engine of development. By significantly contributing to GDP, industrial output, and exports, they have also developed as a thriving and dynamic part of the economy in India. The creation of jobs, however, is the industry's most vital contribution, second only to agriculture. While job losses have been especially severe in the agricultural sector in recent years, they have also been felt in big businesses. Unorganised sectors, such as small and medium-sized businesses and the service industry, would be primarily responsible for employment generation under such conditions. The MSMEs industry has been tasked with increasing yearly growth by 12 percent and creating an extra 4.4 million jobs due to its potential and capacity. Also MSMEs in India will play a significant part in the country's economic growth. Creating work for young people is one way that MSME combat unemployment and poverty. It has created scope for regional growth and dismantling inequities. MSMEs are often regarded as a major economic driver of growth. Therefore, both the formulation and execution of policies in the industry need careful thought from policymakers. While banks and other financial institutions have helped small and medium-sized enterprises grow and thrive so far, more attention has to be paid to ensuring that these businesses are financially included. The findings and suggestions of the MSME sector analysis committees should be implemented by the government.

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