

# “A STUDY OF ACCESS TO INSTITUTIONAL FINANCE BY MSMEs IN AHMEDABAD DISTRICT”

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## Abstract:

The paper will analyze the accessibility of finance by MSMEs in Ahmedabad district to throw light on how the financing through different institutional sources is undertaken and utilized. The Study will draw the relationship between formal financing practices and challenges faced by MSME sector in Ahmedabad based on the information available. The growth of every economy largely depends on the progress of MSME sector. Companies those are in the growing phase today will impact employment and derive revenue tomorrow. In a developing economy like India, MSMEs and entrepreneurship have a significant role to play in the decades to come. Previous studies have revealed that MSME sector prefers informal financing optional available to them due to number of reasons.

According to the previous studies, access to formal finance options for MSMEs also remains a demanding concern. Although formal interest rates generally decreased, the formal channel for financing is again a suffering for MSMEs in Ahmedabad. MSME non-performing loans, as well as bankruptcies, continued to increase over the period of time. The provision of credit guarantees continues to be the most widely proficient policy instrument. Public financial institutions should have a leading role in promotion co-participation of the private sector in the lending markets through managing securities and in inspiring new public-private collaboration in equity instruments.

By enlightening focus and concern on MSME finance in Ahmedabad district, this is a step forward in increasing our awareness about the complications that MSMEs and entrepreneurs' meet in real life, and benefits governments and financial institutions design suitable reactions. Better access to finance can make all the difference in achieving a vibrant and energetic business sector, for the benefit not only of entrepreneurs, but society more largely.

**Key Words:** MSMEs, Institutional Sources of Finance for MSMEs, Formal Vs. Informal Financing, Angel Finance, Venture Capital, Bank Financing, Other available Sources of Finance

## INTRODUCTION:

MSME- an abbreviation of Micro, Small & Medium enterprises- is the pillar of economic growth in many developed, and developing countries in the world. Often rightly termed as “the engine of growth” for India, MSME has played a prominent role in the development of the country in terms of creating employment opportunities-MSME has employed more than 50 million people, scaling manufacturing capabilities, curtailing regional disparities, balancing the distribution of wealth, and contributing to the GDP-MSME sector forms 8% of GDP. Though India is still facing infrastructural problems, lack of proper market linkages, and challenges in terms of flow of institutional credit, it has seen a tremendous growth in this sector.

Under Section 7 of the Micro, Small and Medium Enterprises Development Act, 2006, the micro, small and medium enterprises are defined as under:-

Type of Industry	Investment in Plant & Machinery/Equipment excluding Land & Building	
	Manufacturing Enterprises	Service Enterprises
Micro	Upto Rs.25 Lakh	Upto Rs.10 Lakh
Small	Rs.25 Lakh – Rs.5 Crore	Rs.10 Lakh – Rs.2 Crore
Medium	Rs.5 Crore – Rs.10 Crore	Rs.2 Crore – Rs.5 Crore

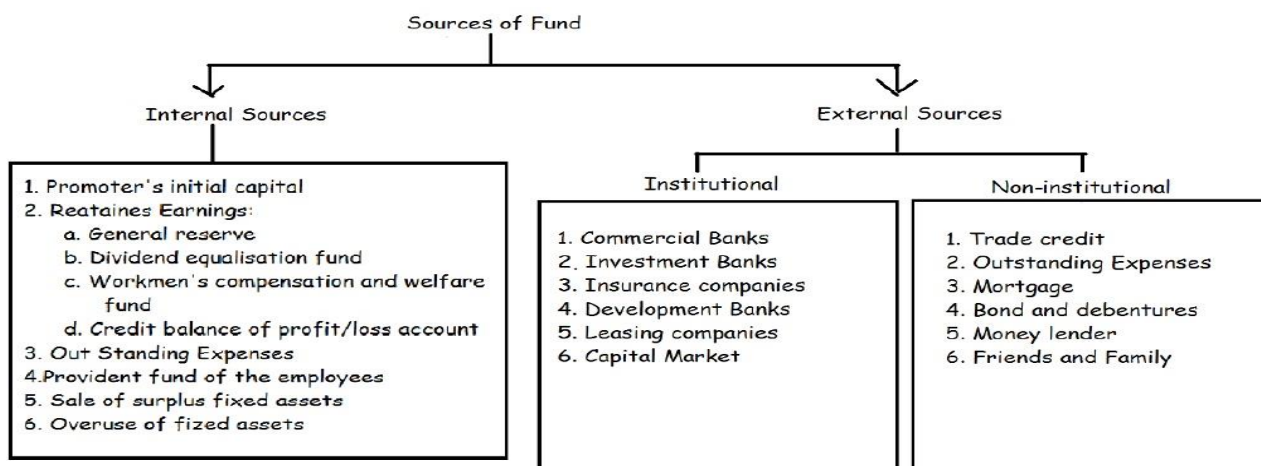
The advantage of this sector is it requires less investment, thus creating employment on a large scale, and reducing the employment and underemployment problems. Moreover, this sector has survived almost all threats emerging out of still completion from both domestic and international market. The contribution of MSME to other sectors has been immensely instrumental. It is the biggest employer after agriculture sector, despite the fact that agriculture sector's contribution to GDP is less than MSME. While it contributes about 45% to manufacturing sector, and perhaps 40% to Exports, it forms the highest share of Employment sector in India, contributing around 69% to it.

In Gujarat, Ahmedabad district leads with the highest number of SSI units with 64,916 units, constituting almost 22% of the total SSIs in the state as per the report.

#### MSME Financing:

MSME Finance is the funding of Micro, small and medium sized enterprises and represents a major function of the general business finance market – in which capital for firms of types is supplied, acquired, and priced. Capital is supplied through the business finance market in the form of bank loans and overdrafts; leasing and hire-purchase arrangements; equity/corporate bond issues; venture capital or private equity ; and asset- based finance such as factoring and invoice discounting and trade credit.

MSMEs in India and in Gujarat have universal problems like helplessness to provide quality data and display formal systems and practices and lack of asset cover. This has resulted in the unwillingness of banks to increase their SME lending. Legal and regulatory compliance has also been inadequate. Conventional weaknesses like dense and uneven data and low capital base continue to characterize MSME sector balance sheets. This problem is further compounded due to supremacy of a large cash economy and informal lending practices in this segment. MSME lending has thus met with partial success. The lending in the past has not been hugely successful and self-sustaining also due to the lack of forward and backward networks in the economy due to which MSMEs had a low survival rate. MSME banking space has also been lopsided by major Indian banks whether public or private, which account for most of the capacities in MSME business, restricting them to low cost but inflexible lending with no focus on flexibility. Following is the chart represents the sources of institutional and non-institutional finance:



## REVIEW OF LITERATURE:

According to *Sinha Akinchan Buddhodev, 2008*, Small and Medium enterprises are like growth engine of Indian economy. In view of this, Government of India has initiated numerous measures to develop the sector, like, erstwhile definition of 'Small Scale Industries' was enlarged by enhancing investment ceiling in plant and machineries from INR 1 crore and trading activities have taken in the ambit of MSMEs by enactment of Micro, Small & Medium Enterprises Development (MSMED) Act from 2nd of October, 2006. Also the act recognizes the term 'Enterprises' instead of 'Industry' to cover service in MSME segment.

(*yourstory.com, 2019*). Why is procuring a loan still a challenge for MSMEs? Expensive means of procuring credit, complicated procedures legacy institutions still hold on to, information asymmetry, lack of documents to prove creditworthiness, and lack of awareness about the existing products and services are some of the primary reasons. When it comes to addressing lack of credit accessibility using advanced technologies, conventional and legacy banks are yet to pick up pace as compared to new-age fintech startups and alternative lending platforms.

*The Economic Times Jan 2, 2019*, MSMEs need more access to formal finance, Tensions are defusing between the government and the Reserve Bank of India. A proof of rapprochement is the RBI's latest decision on concessions to micro-small and medium enterprises (MSMEs). The reprieve in the form of a one-time loan restructuring scheme will ease the stress that has been building up in the SME segment. That is fine, but the need is to go beyond short term fixes. The substantive reform would be to ensure that SMEs have better access to long term finance.

*Das, K. (2008)* says that there are many constraints faced by SME's are credit facilities, technology up gradation, inadequate infrastructure, poor transportation facilities etc. *Adrian Wilkinson, (1999)* says that recruitment in SME's are carried out through their networks. Informal network of people will be involved in recruitment process. He also describes that SME's do not follow any job description and job specification methods for recruiting people. On the other hand a USA based study finds that because of lack of importance on human resources is the major reason for SME's failure *McEvoy (1984)*. *Mukund Chandra Mehta (2013)* says that lack of finance, low on production capacity, lack of skilled man power, lack of infrastructure facilities, lack of industrial estate facilities etc. He concludes that government should consider these factors influencing SME's in formulating of any schemes or programs.

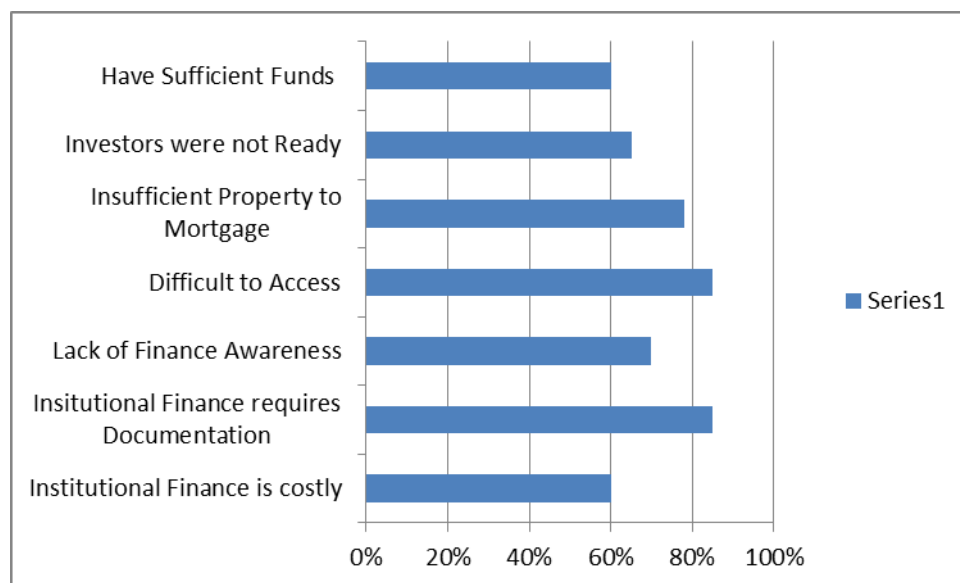
**RESEARCH METHODOLOGY:**

This study is based upon the descriptive research methodology. Both primary and secondary sources of information have been used for this research. The primary data for this study was collected from the owners of MSME in Ahmedabad through a planned questionnaire. The respondents were more comfortable responding to the survey telephonically and physically in some cases. In few of the cases, the interviews were conducted on telephone and the researchers met few entrepreneurs personally in Ahmedabad for survey purpose. The survey time period was from Jan 2017 to April 2018. Without exception, majority of the business owners approached for the survey were forthcoming with their response and shown significant interest and involvement. In total, it was possible to generate the responses from 58 enterprises from the state. These respondents are from Ahmedabad district of Gujarat which is termed to be an entrepreneurship center of the state.

**Table of Development Stage of MSME and Sources of Financing:**

Stage of an Enterprise	Institutional Sources of Finance	Non-Institutional Sources of Finance	Total
Early	6	16	22
Survival	4	2	06
Expansion	15	12	27
<b>Total</b>	<b>25</b>	<b>30</b>	<b>55</b>

**Reasons for Not Availing Institutional Finance:**



**Descriptive Statistics of Perception of Respondents towards Financing:**

Parameters	Mean Score	Standard Deviation
Institutional Finance is costly	3.52	0.62

Institutional Finance requires Documentation	3.45	0.87
Lack of Financial Knowledge	4.02	0.71
Not Accessible	3.68	0.65
Insufficient Properties to Mortgage	3.25	0.87
Investors were not Ready	3.15	0.88
Have Sufficient Funds Internally	3.45	0.52

## CONCLUSION & FINDINGS:

Based upon the survey outcomes of the above study in Ahmedabad, the following conclusions emerged:

**Lack of credit scoring:** MSMEs are often time neglected by credit scoring assistances. This singular act of the credit scoring agencies created a space in one of the most important criteria required by banks, non-banking financial institutions and other financial institutions. And because of the uncertainties involved, banks always insist that their small business clients must provide an acceptable credit score and base their decision on this system so as to follow regulations.

**Lack of adequate documentation:** Because banks and other financial institutions cannot get useful information that will give them insight into the activities of these MSMEs, they force the small businesses to provide a detailed business plan, list of the firm's assets, details of the experience of directors and managers and show how they intend to provide security for the amount advanced- you can imagine the stress.

**Maturity gap:** It is particularly difficult for small businesses to obtain medium term loans due to a mismatching of the maturity of assets and liabilities. Longer term loans are easier to obtain than the medium and short term loans. The reason is because longer term loans are secured with hypothecations against assets.

**Interest rate discrimination:** In general, banks and other financial institutions tend to ask for personal securities from owners of small businesses and will set interest rates at higher levels than those charged to big and reputable companies.

**Equity finance:** Lack of market trust in MSMEs even when they have, they tend to lay or attach little value to it and this will make the firm to issue out more number of shares (just to raise little amount) that will in turn further dilute the small company's earnings.

A considerable fraction of the MSME sector do not possess the security required for conservative collateral based bank lending, nor high enough revenues to attract formal institutions and other risk investors. Furthermore, markets may be characterized by lacking information (limiting the effectiveness of financial statement-based loaning and credit scoring). This has led to claims of an "MSME financing gap". The MSMEs that fall into this group have been defined as Small Growing Businesses (SGBs) at a workshop in Geneva in July 2008, held by The Network for Governance; Entrepreneurship & Development (GE&D). There have been at least two distinguishing approaches to try to overcome the so-called SME finance gap. The first has been to widen the collateral based approach by inspiring bank lenders to finance MSMEs with insufficient collateral. This might be done through an external party providing the collateral or guarantees required. Regrettably, to the extent that the schemes concerned run counter to basic free market principles they tend to be unsustainable. Thus, the next possible approach has been to broaden the feasibility based approach. Since the feasibility based approach is concerned with the business itself, the aim has been to provide better general business development support in terms of accessibility to finance to reduce risk and increase returns of the units located in Ahmedabad district.

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