

**ACCESS OF FINANCE TO MSMEs: AN ANALYSIS OF GROWTH OF MSMEs IN INDIA**

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**ABSTRACT**

Micro, Small and Medium Enterprises constitute the backbone of an economy in maintaining an appreciable growth rate and in generating employment opportunities. The Small and Medium Enterprises has been regarded as an engine of economic growth and social development in many developed and developing countries. Contribution of MSMEs to the Indian economy in terms of employment generation, containing regional disparities, fostering equitable economic growth and enhancing export potential of the country has been quite phenomenal. Despite some infrastructural deficiencies and challenges like flow of institutional credit and inadequate market linkages, this sector has registered remarkable success with regard to increase in number, quantum of investment, scale of production and overall contribution to national GDP. The study makes an attempt to focus on the huge growth potential and opportunities available in India for development of MSME sector, to identify important issues and challenges and offer suggestions to address the same.

**KEY WORDS:** MSMEs, Global MSME Sector

**INTRODUCTION**

The MSMEs has emerged as the rapidly growing sector and shown a stable growth over many years and is contributing at large. MSME does act as a very important part of country and being one of the many growth drivers of the economy. When we look at today's scenario the MSME represents around 38% of GDP and it has proven itself being the prime source for the skills, innovation and providing jobs. MSME is the most lucrative sector. And, the focus it has received in the past years has led it to rapid growth. The Government of India is also supporting all the entrepreneurs throughout the nation by helping and motivate them to setup their own business and run it. To make this happen

government has launched various schemes under the name of Make in India, Startup India and Skill India. These all schemes and their benefits are going to be very helpful in long as well as short run in both the aspect of societal and economical.. Now, when we look at some recent examples, after introduction of various schemes to assist start-ups in India, many have received tax exemptions, many are recognized to get the advisories for business plans, pitching and mentoring support. Many have received the benefit of 80% reduction in patent fees and income tax sops. The MSME department is constantly working very actively to have a healthy eco system for entrepreneurs, so that they can develop the MSME Sector.

The MSME sector also plays a key role in developing rural India and has unlocked many roads of growth for the rural peoples in India. Amplified investment and attention on this sector will ultimately lead to the development and growth of industries in rural India.

The following is an excerpt from the MSME report from MSME Dept.

*“The SME sector can play an important role in India’s growth story through their contribution in achieving various socio-economic objectives such as employment generation, higher growth of output, exports promotion, enabling entrepreneurial spirit and fostering innovation. The SME sector as the driver of these socio-economic objectives are set to witness certain trends such as growth of E-commerce, adoption of SMAC technologies and role of FinTech companies. Comprehending the urgency for accelerating the growth of the SME sector, the government has introduced various initiatives such as Public Procurement Policy, Pradhan Mantri Mudra Yojana, Start-up India, Skill India and GST Implementation. The GST Implementation seems disruptive in the short run, but it will be beneficial for SMEs in the long run. These initiatives along with the advent of new technologies and innovation will create multiple opportunities for the Indian SME sector in the time to come.”*

#### **MSMEs IN INDIA**

Micro, Small and Medium Enterprises (MSMEs) has been a key sector in the socio-economic development of India. The sector is considered to be the growth driver of the Indian economy for not only its input in employment generation, but also for the part it has played in the industrialization of rural and backward areas. Today, MSMEs are functioning in both formal as well as the informal segments of the economy, starting from rural industries to the precision engineering segment.

#### **DEFINING MSMEs**

*MSMEs have been defined in the Micro, Small and Medium Enterprises Development (MSMED) Act,*

2006 passed by the Indian government to address the policy issues affecting SMEs, and to extend the coverage and investment ceiling of the sector. The Act further categorizes these enterprises into *micro, small and medium enterprises, based on their investment in plant & machinery (for manufacturing enterprises) or investment in equipment (for services enterprises).*

**Table 1.1:** Criteria for Classification of Micro, Small and Medium Enterprises, All figures in INR

| <b>Manufacturing Sector</b> | <b>Investment in Plant &amp; Machinery</b> | <b>Service Sector</b> | <b>Investment in Equipment</b>      |
|-----------------------------|--|-----------------------|-------------------------------------|
| Micro                       | Up to 2.5 Million                          | Micro                 | Up to 1 Million                     |
| Small                       | Above 2.5 Million & up to 50 Million       | Small                 | Above 1 Million & up to 20 Million  |
| Medium                      | Above 50 Million & up to 100 Million       | Medium                | Above 20 Million & up to 50 Million |

Source: Ministry of Micro, Small and Medium Enterprises, Govt

**GROWTH OF MSMEs**

It is true to say that the MSME sector is the backbone of the economy. When we look at the numbers we find that an estimated 90% of all enterprises belongs to MSME sector. The MSME sector amounted to 6% of the GDP, 33% of the manufacturing sector output and about 45% of the country’s exports.

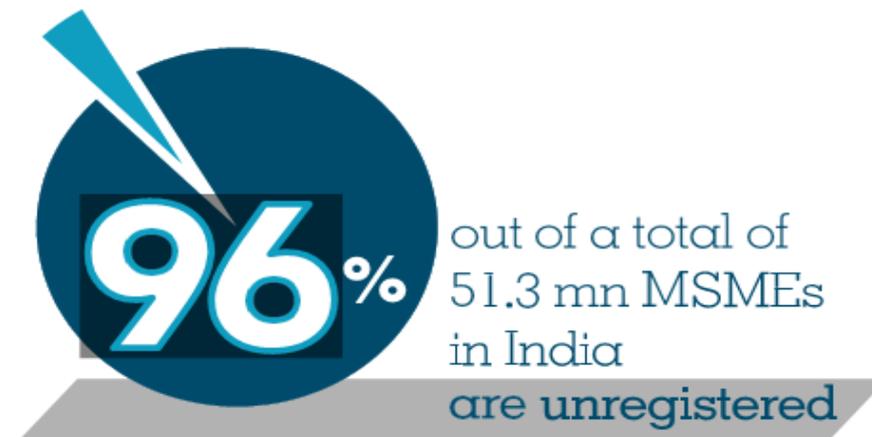


**Figure1.1: Growth of MSMEs**

As per estimates made using results of the Sixth Economic Census, 2013, (results of which were published on 31 March 2016), the Fourth all-India Census of MSMEs, 2006-07 and the Fifth Economic Census, 2005, the number of working MSMEs in India stands at around 51.3 mn. Out of these, a

whopping 96% are unregistered.

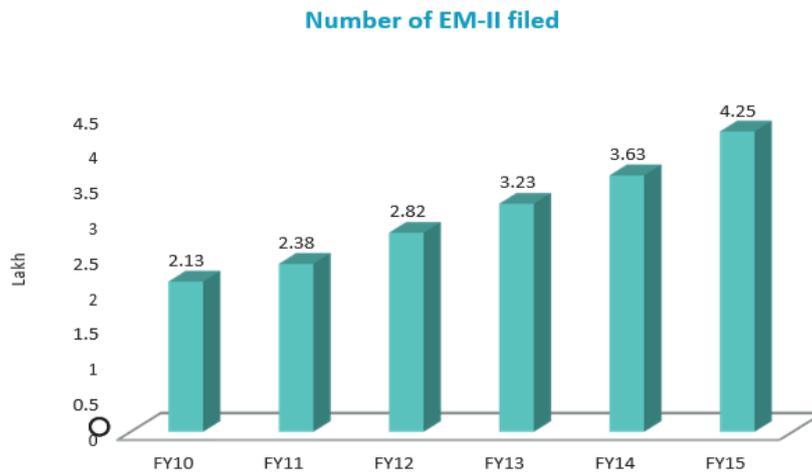
**Figure 1.2: MSME registration statistics**



**Key benefits of getting registered**

- Avail the benefits from Ministry of MSME
- Easy access to finance
- Improve reputation with customers

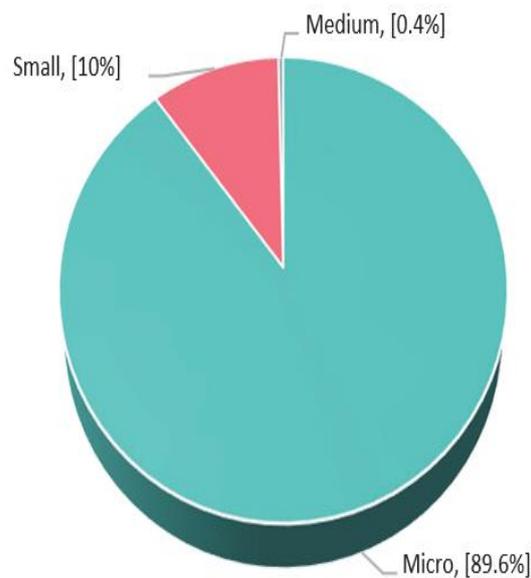
Nonetheless, the growth of MSMEs can be assessed from the rapid increase in the number of registrations in the past few years. The number of Entrepreneur Memorandum Part-II (EM-II) filed with State/UT Commissionerate/Directorates of Industries (DICs) during FY15 almost doubled to 0.43 mn as against 0.21 mn during FY10, reflecting a CAGR of 14.8%. From Sep 2015 onwards, the EM-II was replaced by the Udyog Aadhaar Memorandum (UAM). Since then, a whopping 3.7 mn enterprises have been registered under UAM till date, out of which 89.6% are micro enterprises, 10% are small enterprises and 0.4% are medium enterprises. The state-wise distribution reveals that Bihar, Uttar Pradesh, Tamil Nadu, Maharashtra and Gujarat are the top five states which collectively accounted for 63.4% i.e. of the UAM filings made, whereas the bottom ten states and UTs contributed to a minuscule 0.24% of the UAM filings.



Source: Development Commissioner Micro, Small and Medium Enterprises

**Figure 1.3: Statistical data of EM-II Filing**

**Distribution of Micro, Small and Medium Enterprises as per UAM Filings (as on 12th Nov 2017)**



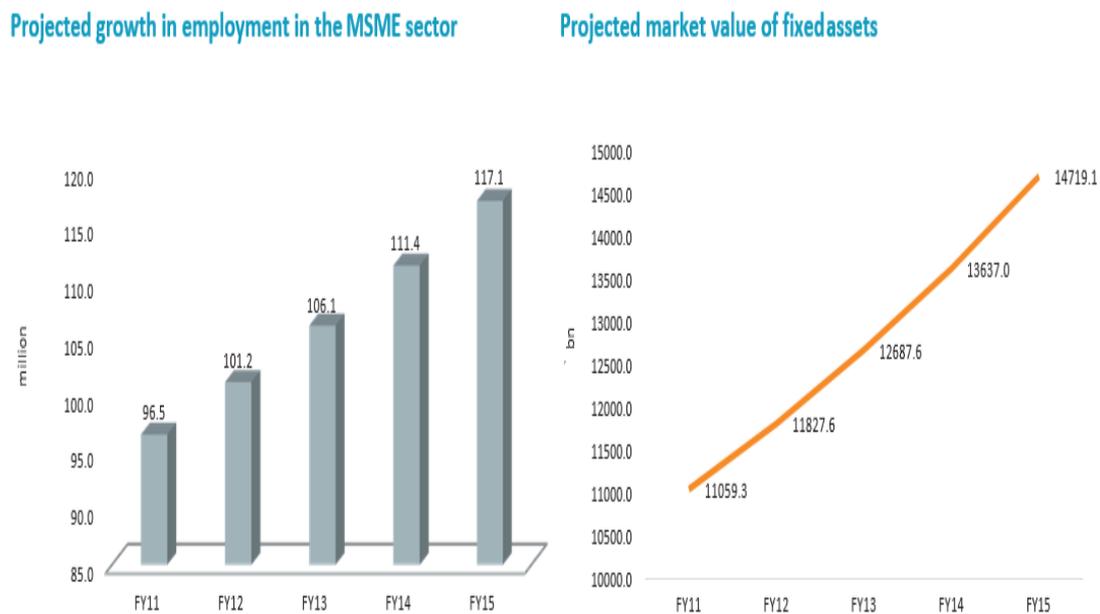
Source: Udyog Aadhar Website, Ministry of MSME

**Figure 1.4: Distribution of MSMEs as per UAM Filing**

On the employment front, the MSME sector gave employment to 117.1 mn persons in FY15, showing a growth of 5.1% as compared to the previous year. Employment in MSMEs rise by 4.9% per annum during FY11-FY15.

The growth of the MSME sector can also be measured from stable growth in the investment in fixed assets. A 7.2 % of growth is reflected in market value of fixed assets of MSMEs during FY11- FY15.

Figure 1.5: Projected data for growth and fixed assets



Source: Ministry of MSME, Annual Report 2016-17

## GLOBAL MSME SECTOR – KEY H

### HIGHLIGHTS

- The most widely used variable for defining an MSME is the number of employees, followed by turnover and assets.
- There are about 162.8 mn formal MSMEs, employing more than 508 mn employees. Out of this, about 96.3 mn MSMEs and 231.4 mn employees operate in emerging markets.
- Formal MSMEs account for a median share of employment totaling 67.1%. MSME's contribution to employment in high- income economies surpasses 65%, while in upper-middle income economies it is about 60% and in low-income economies it is approximately at 75%.
- Globally, MSMEs have registered a growth rate of around 5.2% annually since 2000. The lower-middle-income economies (for example, in the Europe and Central Asia region) have the highest growth rates of MSMEs.

- Overall, the median MSME density stands at 32.18 MSMEs per 1,000 people. The five economies with the highest formal MSME densities are the US (89.96), Czech Republic (89.31), Liechtenstein (80.69), Iceland (79.2), and Portugal (78.7).
- The density of MSMEs largely depends upon higher levels of GNI per capita, better access to finance, streamlined business environments, a more competitive landscape, adequate institutional frameworks, less poverty, and greater shared prosperity.

*Source: MSME Country Indicators 2014, International Finance Corporation*

### **RECENT GOVERNMENT INITIATIVES TO BOOST MSMEs**

In view of the pivotal role played by MSMEs, the Government has introduced several initiatives to provide impetus to the sector. Some of the key policy measures taken by the government for the MSME sector are as follows:

- Augmentation of the corpus of Credit Guarantee Trust Fund from INR 25 bn to INR 75 bn, to be fully funded by the Government of India
- Increased coverage of the loans under the credit guarantee scheme from INR 10 mn to INR 20 mn.
- Increased coverage of the Credit Guarantee Scheme for loans being extended to micro and small enterprises by NBFCs as well.

Post the demonetization, the Government took several steps to promote digital transactions amongst MSMEs. Some of them are as under:-

- In the Union Budget FY18, the Government proposed that under the scheme of presumptive income tax for small and medium tax payers with turnover up to INR 20 mn, 6% of their turnover which is received by non-cash means will be counted as presumptive income as against 8% of their turnover earlier.
- To promote cashless transactions, it was proposed in the Union Budget FY18 to exempt BCD, Excise/CV duty and SAD on miniaturized POS card reader for m-POS, micro ATM standards version 1.5.1, Fingerprint Readers/Scanners and Iris Scanners.

The government has implemented various schemes for the promotion of MSMEs. The total expenditure on these schemes as on JUNE 31, 2016 was INR 33.5 bn as against INR 4.5 bn till JUNE 2016.

**Table 1.2: Government assistance data to MSMEs**

| Scheme                     | Expenditure (INR mn) |           | Physical Performance (number) |           |           |
|----------------------------|----------------------|-----------|-------------------------------|-----------|-----------|
|                            | Upto JUNE            | Upto JUNE |                               | Upto JUNE | Upto JUNE |
|                            | 2016                 | 2016      |                               | 2016      | 2016      |
| Technology Upgradation     | 80.8                 | 145.3     | Trainees                      | 1037      | 1030      |
| Credit Support Programme   | 177.8                | 28018     | Credit Proposals              | 161696    | 305903    |
| Marketing Development      | 16.9                 | 19.5      | MSMEs                         | 4822      | 5531      |
| Promotional Services       | 139.5                | 346.7     | Trainees                      | 1         | 5         |
| Infrastructure Development | 1689.1               | 2222.1    | MSMEs                         | 20946     | 19159     |
| NMCP - CLCSS               | 2273.9               | 2552.8    | No of MSMEs                   | 3553      | 4027      |

Source: Office of Development Commissioner, MSME

### IMPACT OF DEMONETIZATION ON MSMEs

While Indian companies have witnessed significant level of digitization in the past few years, a large number of MSMEs continue to operate completely offline. Even those with an access to digital infrastructure haven't fully leveraged its benefits. Consequently, the sector was hit hard when the Government of India announced that the Five Hundred and One Thousand Rupee notes would cease to be legal tender from the midnight of Nov 8, 2016. The demonetization caused short-term disruption in terms of working capital, fall in consumer demand, supply disruptions, and debt repayment, especially in rural and semi-urban areas.

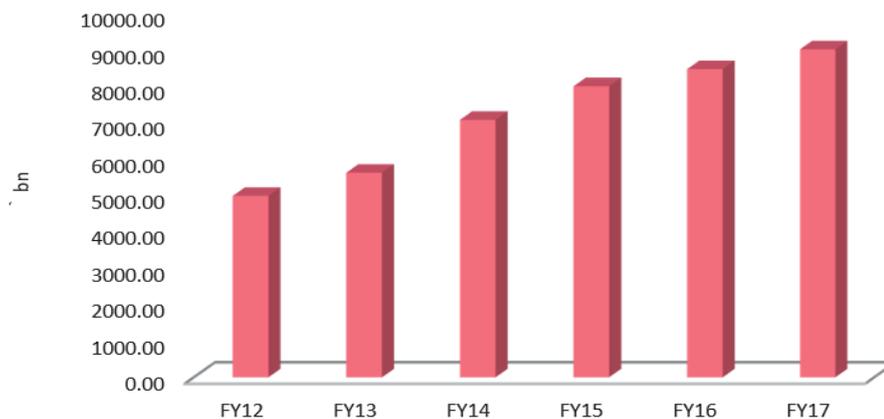
However, post demonetization there has been a substantial shift away from cash transactions to cheque or electronic payment channels, especially in traditional cash-sensitive sectors such as textiles, agricultural products, electrical equipment, steel consumer durables and automobiles. Further, with liquidity and working capital drying up in the immediate aftermath of the demonetization, the unbanked MSMEs had to approach banks for loans. Thus, while demonetization has resulted in short term disruptions for SME business, it has also provided significant impetus for digital transactions, which in turn will benefit SMEs by way of easier record keeping, expansion to other geographical markets and quick processing of payments.

### ACCESS OF FINANCE TO MSMEs

Access to finance is one of the main problems faced by the MSME sector in India. The MSME Census of 2006-07 showed that almost 87% of relied on their personal sources like friends, families, relative and loans from private lenders, despite they know various other options available to them.

The main reason behind this is that it is generally perceived that MSME financing have credit risk involved in it. This occurs due to negligence from MSMEs in case of producing invoice and trade related information on time. And, due to this a higher collateral is demanded from MSMEs for financing which they cannot provide. In order to mitigate this credit risk, higher collateral is sought, which cannot be brought in by many SMEs. Further, due to their small size and local presence, the transaction costs involved in financing them are very high. In order to tackle this issue, SME lending is being treated as priority sector lending. The priority sector lending to SMEs reached INR 9 trillion in FY17 as against INR 8.5 trillion in FY16, registering a growth of 6.5%.

In addition to various efforts by the Ministry of Small and Medium Enterprises, Small Industries Development Bank of India (SIDBI) and the RBI, a World Bank project has been initiated to address the SME financing issue. Approved in 2015, the USD 550 mn World Bank project supports innovative financial products, frameworks and tools for MSME financing. This is the World Bank's first loan to support start-up debt development and franchising finance to India. The World Bank is working with the SIDBI for providing a credit line of USD 500 mn and supporting SIDBI's efforts in direct and indirect financing. As of March 2016, the MSME project of the World Bank has disbursed USD 265.38 mn to facilitating SME finance.



Source: RBI

**Figure 1.6: Priority sector lending to MSMEs**

## CONCLUSION

The MSME sector in India has shown remarkable resilience amidst the challenging economic environment in the past few years. They have emerged as the backbone of the Indian economy due their contribution in terms of job creation and boosting economic growth. In view of its significance

for the economic growth and poverty elimination, the Government of India has taken various initiatives to support the growth of MSMEs. Despite this, MSMEs continue to suffer some critical challenges like unavailability of adequate, timely and low-cost credit, lack of digitization, lack of skilled manpower, inadequate marketing support and infrastructure facilities, etc. These challenges have turned out to be the major dampener for the growth of MSMEs in India, and hence need to be resolved.

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