

# Challenges Faced by Small and Medium-Sized Enterprises in India

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## ABSTRACT

*The present article deals with micro, small and medium enterprises in India. MSMEs are credited with generating high rates of employment growth and account for a major share of industrial production and exports but still they are facing many problems i.e. Finance problems, shortage of raw material, lack of demand, shortage of working capital, power shortage, management and equipment related problems etc.*

## 1. Introduction

Micro, Small and Medium Enterprises (MSMEs) play an important role in the development of country. Micro, Small and Medium Enterprises have been accepted as the engine of economic growth and for promoting equitable development. The MSMEs constitute over 90 per cent of total enterprises in most of the economies and are credited with generating the highest rates of employment growth and account for a major share of industrial production and exports. As per available statistics, this sector employs an estimated 31 million persons spread over 12.8 million enterprises and labour intensity in the MSMEs sector is estimated to be almost four times higher than the large enterprise (<http://www.msmedikarnal.gov.in/>).

However, these industries face difficulty in accessing adequate finance for their businesses. Scarcity of finance is a major obstacle in the development of Micro, small and medium enterprises. The capital base of small entrepreneur is usually weak and often he has to procure credit at a high rate of interest. Securing bank credits, difficulties in documentations for bank loans and lack of collateral security are bigger problems in India. Large enterprises have access to various sources of finance; small sector depends primarily on finance from banks and other financial institutions (Vijayarani, 2011).

### Meaning and Definition of Micro, Small and Medium Enterprises

According to MSME Development Act, 2006 Micro, Small and Medium Enterprises are defined based on their investment in plant and machinery (for manufacturing enterprise) and on equipment' s for enterprises providing or rendering services.

According to the Ministry of Micro, Small and Medium Enterprises, recent ceilings on investment for enterprises to be classified as micro, small and medium enterprises are as follows:

For manufacturing sector, an enterprise is classified as:

- Micro enterprise, if investment in plant and machinery does not exceed Rs. 25 Lakhs.
- Small enterprise, if investment in plant and machinery is more than Rs. 25 Lakhs but does not exceed Rs. 5 Crore; or
- Medium enterprise, if investment in plant and machinery is more than Rs. 5 Crore but does not exceed Rs. 10 Crore;

In case enterprise is engaged in providing or rendering services, it is classified as:

- Micro enterprise, if investment in equipment does not exceed Rs. 10 Lakhs.
- Small enterprise, if investment in equipment is more than Rs. 10 Lakhs but does not exceed Rs. 2 Crore.
- Medium enterprise, if investment in equipment is more than Rs. 2 Crore but does not exceed Rs. 5 Crore.

According to Micro, Small and Medium Enterprises Amendment Bill, 2015, a recent ceiling on investment for enterprises to be as follows:

For manufacturing sector, an enterprise is classified as:

- Micro enterprise, if investment in plant and machinery does not exceed Rs. 50 Lakhs.
- Small enterprise, if investment in plant and machinery is more than Rs. 50 Lakhs but does not exceed Rs. 10 Crore; or
- Medium enterprise, if investment in plant and machinery is more than Rs. 10 Crore but does not exceed Rs. 30 Crore;

In case enterprise is engaged in providing or rendering services, it is classified as:

- Micro enterprise, if investment in equipment does not exceed Rs. 20 Lakhs.
- Small enterprise, if investment in equipment is more than Rs. 20 Lakhs but does not exceed Rs. 5 Crore.
- Medium enterprise, if investment in equipment is more than Rs. 5 Crore but does not exceed Rs. 15 Crore (Jain, 2017).

**2. Literature Review:**

**Tucker and Lean (2003)** conducted a questionnaire survey to collect data concerning small business awareness and use of informal finance and to identify issues concerning difficulties encountered in gaining access to finance. They found that debt finance gap may exist for a minority of firms, though an equity finance gap may represent a more significant issue for small firms.

**Satija (2007)** found that credit ratings are being institutionalized into the regulatory framework of banking supervision. This raises four important issues that need to be looked into. These are – the quality of credit rating in India, the level of penetration of credit rating, lack of issuer ratings in India and last but not the least, the effect of the credit rating scheme on Small and Medium Enterprises (SMEs) and Small Scale Industry (SSI) lending.

**Zeng et al. (2008)** observed that Chinese MSMEs still face serious financial problems related to operational needs and business expansion. In China, at start-up, MSMEs mainly raise funds from the owner’s personal savings and the savings of immediate families and friends. In the growth stage, MSMEs have strong financial needs and gain access to intermediated finance such as bank loans. They found that the proportion of small businesses using bank loans is higher.

**Kyaw (2008)** found that MSMEs have to deal with a number of constraints that hinder their development potential, such as the shortage in power supply, unavailability of long term credit from external sources, and many others. Among them, the financing problem of MSMEs is one of the biggest constraints.

**Singh et al. (2008)** found that MSMEs are facing so many problems due to their limited resources and lack of innovation in capability development like securing finances for establishing and running MSMEs, lack of entrepreneurial and management competences, problems in finding the markets, limited opportunities for promotion, and limited amount of government and institutional support.

**Fumo et al. (2011)** highlighted on the main barriers faced by Mozambique micro, small and medium enterprises and their implications in respect to the support policies available for these enterprises. They found that financial and competitive barriers are the main barriers faced by analyzed MSMEs. These barriers vary according to the field of activity of enterprises.

**Venkateswarlu and Ravindra (2012)** found that a major problem faced by MSMEs in South Asian countries is lack of finance to advance business growth. MSMEs lack setup capital, liquid capital, working capital and investment capital to survive and grow in a dynamic business environment.

**Jain and Madan (2012)** observed that most of the MSMEs are underutilized due to the paucity of funds. Main objective of this article was to study the challenges for future growth and development in the Textile Industries (MSMEs) of Panipat region of Haryana. They found that MSMEs in the Textile Industries generally face critical problems related to

the finance and government policies are not adequate to meet the requirement of the entrepreneurs.

**Naidu and Chand (2012)** in their study concluded that financial problems faced by the MSMEs could be divided into three broad categories-financial problems, operational and administrative problems, and sales and debtors problems. The 19 financial obstacles tested in this research falls under these broad categories. The study involved conducting a survey of 200 MSMEs in Fiji and Tonga.

**3. Objective of the Paper**

- To find out different Challenges and Problems faced by Micro, Small and Medium Enterprises in India

**4. Credit flows to Micro, Small and Medium Enterprises and Sickness**

The overall availability of credit to small and micro enterprises as percentage of net bank credit (NBC) of the Scheduled Commercial Banks (SCB) has declined from 15.5 per cent in 1996-97 to 6.6 per cent in 2007-08. Analysis of data reveals that only 12.77 per cent (199706 enterprises) of the total registered enterprises have obtained loan either from financial institutions or non- financial institutions or both with amount of loan Rs 46520.23 crore. As on September 2012, the outstanding loan by the bank to the SME segment stood at Rs 15,784 crore (**The Hindu: Business Line, October 31, 2012**).

Sickness in MSMEs sector is a cause of concern because of the different reasons like inadequate finance, limited marketing, and R&D facility, accessing credit on easy terms, skills about decision making and good management etc. Conditions of MSMEs sickness are given here below in table 1:

**Table-1: Position of Sick MSMEs Units**

Year	Sick MSMEs Units	Amount Outstanding (crore)
2006	126824	4981
2007	114132	5267
2008	85187	3083
2009	103996	3620

For the enterprises falling under the category sick and not working satisfactorily, reasons were elicited in below table. “Lack of Demand” and “Shortage of Working Capital” was the main reasons for sickness in MSME sector.

**Table-2: Major reasons reported by sick units**

Reasons for Sickness	Proportion of Sick
Lack of Demand	41.94%
Shortage of Working Capital	20.49%
Non- Availability of raw material	5.11%
Power shortage	5.71%

Labour problems	5.64%
Marketing problems	11.48%
Equipment problems	3.17%
Management problems	6.46%

(Sources: Annual Report of MSMEs, 2015-16).

The MSME sector today faces competitive environment owing to: (a) liberalisation of the

Investment regime during the 1990s, favouring foreign direct investment (FDI); (b) the

Formation of the World Trade Organization (WTO) in 1995, forcing its member-countries (Including India) to drastically scale down quantitative and non-quantitative restrictions on imports, and (c) domestic economic reforms. Labour market rigidity is considered as a barrier to the overall growth of the economy.

After the liberalisation of the economy, government's attitude towards the MSME sector Changed and many of the products exclusively manufactured by these units earlier got dereserved. Presently, only 20 items are reserved for exclusive manufacturing in the MSE sector. These include bread, pickles

& chutneys, wooden furniture, wax candles, exercise books and registers, safety matches, incense sticks, fireworks, and stainless steel and mustard oil, laundry soap, fireworks etc. The phased deletion of products from the list of items reserved for the exclusive manufacture by micro and small enterprises is being continued. In October 2008, the government deleted 14 items from this list.

### 5. Suggestions for better functioning of MSMEs-

1. SMEs need IT-based solutions in terms of multi-tasking, expanding customer base, raising productivity, controlling cost, working remotely, fast and accurate decision-making and facilitating collaboration.
2. More support is needed for MSMEs from the government in the form of priority sector lending, government procurement programme, credit and performance ratings and marketing support.

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