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## INSTITUTIONAL FINANCIAL TO MICRO, SMALL AND MEDIUM ENTERPRISES (MSMES) IN INDIA: A CASE STUDY OF ANDHRA PRADESH

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### **ABSTRACT**

*Micro, small and Medium Enterprises (MSMEs) play a very significant role in almost all countries of the world irrespective of their stage of development. Developed countries like Japan, China, Malaysia, Taiwan, the United States of America and the United Kingdom have developed through developing many aspects of MSMEs business such as employment generation, exports, tax, income, innovation and competitiveness. The recent wave of globalization has influenced the overall business of the world. The MSMEs have prospered better under this wave of globalization. Particularly in India, they have made a significant impact on income distribution, social stability, domestic resources utilization technique, structural and regional development, exports, employment and creation of a broad entrepreneurial base. Hence, the MSMEs' are rightly regarded as the backbone of modern Indian economy. With the advent of a planned economy in 1951, and the subsequent industrial policy of the Government of India, both planners and the Government have earmarked financial resources for small and medium industries that play a special role in the economy. The MSMEs form the backbone of the Indian manufacturing sector and have become engines of economic growth in India. It is estimated that the MSMEs account for almost 90 per cent of the industrial units in India and 40 per cent of value addition in the manufacturing sector. It is increasingly recognized that the MSMEs play a crucial role in employment creation and income generation in the Asian Region. The MSMEs can be easily established since their requirements in terms of capital, technology, management and even utilities are not as demanding as it is in the case of large enterprises. This paper is main focus on institutional finance to micro small and medium enterprises in India: A Study of Andhra Pradesh.*

**Key Words:** *Micro, Small and Medium Enterprises, Manufacturing Sector, Economic, Growth*

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### **INTRODUCTION**

The Micro, Small and Medium Entrepreneurs, by and large, represent a stage in economic transition from traditional to modern technology. The variation in the transitional nature of this process is reflected in the diversity of Small-Scale Industries. Most Small-Scale Industries use simple skills and machinery. As well as playing an important role in the country's economic development, small enterprises, because of their unique economic and organizational characteristics, play a social and political role in local employment creation, balanced resource

utilization, income generation and in helping to promote change in a gradual and peaceful manner. Socio-economic factors affecting small-scale industrial entrepreneurs came to the forefront during the industrial revolution, with nations of entrepreneurial importance gaining favour by the mid-twentieth century. During the 1960's, the behaviour of the individual came to be highlighted as a major factor contributing to small-scale industrial entrepreneurship. Thus, the supply of small-scale Entrepreneurs came to be recognized as critical to development of small-scale industries.<sup>1</sup>

### **Definition**

Definition of Micro, Small and Medium Enterprises changed over the years with the changing circumstances and serious problems of the Indian economy. Various institutions, government agencies and individuals had defined small industrial units in different ways.

- i) **Small Industrial Units (1948):** The factory sector units registered under the Factories Act of 1948 constitute the organized sector. All traditional units and the remaining units of small industries segment, not covered under the Factories Act of 1948, constitute the unorganized sector. Such units generally employ fewer than 10 workers, if power is used and fewer than 20 workers, if power is not used.
- ii) **Small Industrial Units (1966):** The small enterprises definitions have changed in terms of the capital investment, that is, when the fixed capital investment is less than Rs. 5 lakhs and ancillary units with a fixed capital investment of Rs. 10 lakhs.
- iii) **Small Industrial Units (1972):** The investment in fixed assets in plant and machinery whether held on ownership basis or by lease or by hire purchase not exceeding Rs. 35 lakhs are defined as small industrial units. In the same year Ancillary and Tiny Industries were defined as those industries in which investment in plant and machinery did not exceed Rs. 45 lakhs and Rs. 2 lakh respectively.
- iv) **Small Industrial Units (1990):** According to Industrial Policy Statement 1990, the investment ceiling in plant and machinery for small industrial units (fixed in 1985) had been raised from Rs. 35 lakhs to Rs. 60 lakhs and, correspondingly, for ancillary units, from Rs. 45 lakhs to Rs. 75 lakhs. The investment for tiny units had been increased from Rs. 2 lakhs to Rs. 5 lakhs. According to the modified definition, an ancillary unit is one which sells not less than 50 per cent of its manufactures to more industrial units.
- v) **The Union Budget (2002-03):** The Union Finance Minister announced the change for the small industries definition i.e., enhancement of small industries investment ceiling for specified hosiery/hand tool items. The investment limit in plant and machinery with regard to industrial undertakings manufacturing specified items in the hosiery and hand tool sub-sectors was enhanced from Rs. 1 crore to Rs. 5 crores.
- vi) **Micro, Small and Medium Enterprises (MSMEs) Development Act, (2006)**  
The Micro, Small and Medium Enterprises (MSMEs) sector has been recognized as an engine of growth all over the world. Many countries have established SME Development Agencies as the nodal agencies to coordinate and oversee all Government interventions in respect of the development of this sector. In India, the term medium establishment has, for the first time, been defined in terms of a separate Act, governing

the promotion and development of Micro, Small and Medium Enterprises (MSMEs). This came into force from 2<sup>nd</sup> October, 2006.

The MSMEs are broadly classified into two: Manufacturing and Servicing. It is a known fact that the service sector has fast emerged and is becoming a good contributor to the economy. Therefore, manufacturing and service sectors have been defined separately. The concept of “Enterprises” as against “Industries” has been brought out in this Act.

**The definitions given by the Act are as follows**

MSMEs in India are defined on the basis of investment in Plant & Machinery and equipments under the MSME Act, 2006. The present investment limit for MSMEs is as under. The classification of micro small and medium enterprise in India is presented in table.1

**Table – 1**  
**Classification of Micro Small and Medium Enterprises in India**

Classification	Manufacturing Enterprise Investment in plant and Machinery	Service Enterprises Investment in Equipment
Micro Enterprises	upto Rs. 25 lakh	up to Rs. 10 lakhs
Small Enterprises	Between Rs. 25 lakh and Rs.5 crore	From Rs. 10 laksh to Rs. 2 crore
Medium Enterprises	Between Rs. 5 crore and Rs. 10 crore	Between Rs. 2 crore and Rs. 5 crore

**Source:** MSME Annual Report 2015-16

**(a) For Manufacturing Enterprises**

- i. A micro enterprise is one where the investment in plant and machinery does not exceed Rs.25 lakh;
- ii. A small enterprise is one where the investment in plant and machinery is more than Rs.25 lakh but does not exceed Rs.5 crore;
- iii. A medium enterprise is one where the investment in plant and machinery is more than Rs 5 crore but does not exceed Rs 10 crore.

**(b) For Servicing Enterprises**

- i. A micro enterprise is one where the investment in plant and machinery does not exceed Rs.10 lakh;
- ii. A small enterprise is one where the investment in plant and machinery is more than Rs.10 lakh but does not exceed Rs.2 crore
- iii. A medium enterprise is one where the investment in plant and machinery is more than Rs.2 crore but does not exceed Rs.5 crore

**REVIEW OF LITERATURE**

The available relevant literature on Micro, Small and Medium Enterprises is reviewed with reference to their financial as well as other related aspects. Following are the important reviews mentioned in the present study.

**Dr. Aanjaneya (2019)**, in his study titled “A Research paper on role and Problems of Micro, Small and Medium Enterprises”, concluded that the role of MSMEs helps in economic restructuring and development of India. Empirical data revealed that hurdle like financial constrain and issues relating to power, raw material procurement should be more effectively dealt with by the government. Further, the data collected revealed that overall, globalised business environment of India has been favourable for the growth of micro and small scale industries. There has been lack of effective co-ordination among the various support organizations set up over the period for the promotion and development of these industries. Quality consciousness has not been generated to the desired level despite various measures taken in this regard. Some of the fiscal policies pursued have resulted in unintended splitting up of these capacities into uneconomic operations and have inhibited their smooth transfer to the medium sector.<sup>2</sup>

**Kwadwo Boateng, Naveen Sodem and Y. Nagaraju (2019)**, in their article “The Contribution of MSMEs to the Growth of the Indian and Global Economy”, It was also found that, even though all states and union territories have their share of the MSMEs, the states of Uttar Pradesh, West Bengal followed by Tamil Nadu, Maharashtra, Karnataka, Bihar, Andhra Pradesh, Gujarat, Rajasthan, and Madhya Pradesh, are the 10 states with the highest number of MSMEs. The findings again indicated that, MSMEs that engage in trade activities dominate the industry. In addition, as much as 51 per cent of Indian MSMEs operates from the rural areas whereas 49 per cent operates from the urban cities. The consistent growth of India’s economy cannot be mentioned without acknowledging the contribution of the MSMEs. The MSMEs sector contributes as much as between 40 and 50 per cent of India’s total export. Again, an average of 30 per cent share of the Gross Domestic Product (GDP) of India is contributed by the MSMEs sector, and an average of 32 per cent to the Gross Value Added (GVA).<sup>3</sup>

### **OBJECTIVES**

The objectives of the present study are as follows;

1. To examine the significance of Micro, Small and Medium Enterprises in the economic development of the India;
2. To ascertain the role of institutional finance for the development of Micro, Small and Medium Enterprises in Andhra Pradesh;

### **IMPORTANCE OF FINANCE**

Blood is crucial to body and the leading financial institutions are as crucial as blood to the large and medium scale sectors. The transfusion of blood enriches the recipient but does not impoverish the donor. Financial support from institutional sources is not only essential for the growth of industry but is perhaps even necessary for its very survival. When finance is easily available, industrial development can be accelerated as there is a source of access to funds on reasonable terms and conditions.

Financial needs of small scale industries may be broadly divided into two categories i.e. fixed capital and working capital. The first category (i.e. fixed capital) needs resources to be deployed for a long period and the second category involves resources for a short period. The long term finance is needed for creating assets like land and buildings and plant and machinery. The

short term finance is needed for purchasing of raw materials and for meeting the day to day requirements of business. The fixed capital requirements are met usually by issue of shares and debt securities. In small scale units the equity capital is generally provided by the entrepreneurs themselves. The entrepreneurs often supplement their own contribution with funds raised from their friends and relatives. The small entrepreneurs also borrow on long term basis from the financial institutions and others to meet their fixed capital requirements. The working capital needs are met by drawing on; (a) owner funds; (b) funds from operation; (c) long term borrowings; (d) spontaneous financing (trade creditors), and (e) short term borrowings from commercial banks and others. The working capital is needed to purchase raw material, stores and to maintain required level of inventory. It is also required to maintain cash balance and also to make credit sales to customers. Moreover, the present day financial requirements of the business are met out of the funds drawn on working capital. The level of working capital in any organization depends upon the operating cycle, nature of the business and the capital market situation.<sup>4</sup>

### **DEVELOPMENT OF FINANCING INSTITUTIONS**

The development depends upon various, micro, small and medium enterprise factors like availability of raw materials, skilled labour, advanced technical know- how, adequate, easy and cheap finances and right type of management. Among these, finance plays a vital role in the development of micro, small and medium enterprises. Non availability of finances at the right time and in right quantities with low rate of interest poses a serious threat to the development of micro, small and medium enterprises. With the availability of adequate finances, it is easy to run the unit successfully without any hindrance.

The, small and medium enterprises main sources of finances are promoters, institutional agencies, and non-institutional agencies. Because of their poor financial background, the capacity of the promoters to invest in their respective units is limited. Likewise, the non-institutional agencies are always reluctant to invest in these micro, small and medium enterprises because of their limited earning capacity as well as poor reputation of the entrepreneurs. Hence, the institutional financial agencies have to play a greater role in financing the development of the micro, small and medium enterprises. There are different financial institutions to cater to the financial needs of the micro, small and medium enterprises. Working capital financial needs are mostly met by the commercial banks, regional rural banks and co-operative banks. Sometimes, these institutions may also participate in the long-term financial needs along with State Financial Corporation (SFCs), but on a limited scale. Financial assistance is also available to the small and medium enterprises from the State Small industries Development Corporations (SSIDC). At the national level, the Industrial Development Bank of India (IDBI), the Small Industrial Development Bank of India (SIDBI), National Bank for Agriculture and Rural development (NABARD) and other national level development banks provide refinance facilities to banks and other grassroot level agencies for financing, small and medium enterprises. The Deposit Insurance and Credit Guarantee Corporation (DICGC) assists the small and medium enterprises by guaranteeing advance to these industries. Moreover, the Export-Import (EXIM) Bank of India facilitates

external debt by rediscounting the bills of these industries. Likewise the Industrial Reconstruction Bank of India (IRBI) assists in rehabilitating the sick units of these industries.

As stated earlier, the conventional banker, being purely security oriented, does not show interest in the development of small scale industries. Hence, during the Second Five Year Plan, it was felt that the commercial banks had to take interest in financing small scale enterprises. For the first time, the State Bank of India, had instituted a pilot scheme to meet all types of credit requirements of small scale industries fully under liberalized rules and procedures. In 1969 when the 14 major commercial banks were nationalized, other commercial banks also had made efforts to support the development of small scale industries.

**The SIDBI was established in 1990 as the apex refinance bank. The SIDBI is operating different programs and schemes through 5 Regional Offices and 33 Branch Offices. The financial assistance of SIDBI to the small scale sector is channelized through two routes-direct and indirect.** The Small Industries Development Bank of India (SIDBI) was established, in 1999 – 2000 as a subsidiary of IDBI. The SIDBI administers both the small industries development and the national equity funds for providing equity support to tiny and small scale industrial units, in addition to providing developmental finance to small scale industries. The financial institutions including commercial banks have taken over a large number of functions like development of entrepreneurship, provision of technical and management consultancy and other related activity.

The Industrial Finance Corporation of India Limited (IFCI), the first development finance institution was set up in 1948 and since July 1, 1993, it has been brought under Companies Act, 1956. The IFCI extends financial assistance to the industrial sector through rupee and foreign currency loans, underwriting direct subscription to shares debentures. It guarantees and also offers financial services through its facilities for equipment procurement, equipment leasing and finance to leasing and hire-purchase companies. It also provides merchant banking. The IFCI has started new promotional schemes, such as (a) interest subsidy schemes for women entrepreneurs (b) consultancy fee subsidy schemes for providing marketing assistance to small-scale industry and (c) encouraging the modernization of tiny, small-scale industries.

The Entrepreneurship Development Institute of India (EDII) is the principal financial institution for promotion, financing and development of small scale industries in the economy. It aims to entrepreneurship development of Micro, Small and Medium Enterprise (MSME) sector with a view to contributing to the process of economic growth, employment generation and balanced regional development.

**State Financial Corporation Act 1951 was brought into force to enable all the state governments (except Jammu and Kashmir) to set up State Financial Corporations as regional development banks. State Financial Corporations provide long term finance to industrial entrepreneurs, subscribing equity and debentures of industrial entrepreneurs, providing financial assistance to small and medium enterprises engaged in service sector and providing working capital loans and meeting various short term needs of their clients.**

Scheduled commercial bank is a different type of bank which provides services such as accepting deposits, making business loans and also offering basic investment products. Scheduled commercial bank is a public sector bank which can refer to the bank or a division of a bank that deals with deposits and loans from corporations or large business. In a developed country like United States the term scheduled commercial bank was used to distinguish it from an investment bank due to a different bank regulation. After great depression, through the Glass-Seagull Act, the United State Congress required the commercial banks to be engaged only in banking services sector activities.<sup>5</sup>

#### **ANDHRA PRADESH STATE FINANCIAL CORPORATION (APSFC)**

**State Financial Corporation Act 1951 was brought into force to enable all the state governments (except Jammu and Kashmir) to set up State Financial Corporations as regional development banks. State Financial Corporations provide long term finance to industrial entrepreneurs, subscribing equity and debentures of industrial entrepreneurs, providing financial assistance to small and medium enterprises engaged in service sector and provide working capital loans and meet various short term needs of their clients.** Andhra Pradesh. In spite of the researcher's best efforts, the entrepreneurs could not provide 100 per cent information at the time of collecting the primary data. Secondary data was collected from more than one source. Hence there may be slight discrepancies between one source and another on the same variable. The reliability and correctness of calculation and findings depend upon the information to calculate few ratios. Nevertheless, these limitations do in no way act as a deterrent in drawing effective and meaningful inferences from the study.

#### **CONCLUSION**

The Indian industrial economy is characterized by a dynamic and versatile set up enterprise actors, who are micro, small and medium in terms of scale of operation. This MSMEs category has been lending a typical competitive advantage to Indian industry in terms of controlling sufficient markets globally, because of the enterprises their ability to make available low-volume customized products, flexible response and lower fixed overhead costs. The other typical behaviour of these MSMEs is that in most cases, depending upon their specialization, they have evolved as clusters. The importance of MSMEs as compared to Corporate Enterprises with regard to their contribution towards Indian economy can be best understood by the fact that they have a share of 40 per cent in terms of volume, 80 per cent in terms of employment, 60 per cent in terms of exports and 92 per cent in terms of number of enterprises. The figures indicate their economic significance.

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