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Certificate

This is to certify that (**NEHA KIRAN PHATAK)** has worked and duly completed her Project Work for the degree of Master in Commerce under the Faculty of Commerce in the subject of **(ENTREPRENEURSHIP MANAGEMENT)** and her project is entitled, (**EFFECT OF CREDIT AVAILABILITY ON SMALL BUSINESS)** under my supervision.

I further certify that the entire work has been done by the learner under my guidance and that no part of it has been submitted previously for any Degree or Diploma of any University.

It is her own work and facts reported by her/his personal findings and investigations.

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Declaration by learner

I, the undersigned **(NEHA KIRAN PHATAK)** declare that the work embodied in this project work hereby, titled **(EFFECT OF CREDIT AVAILABILITY ON SMALL BUSINESS)**, forms my own contribution to the research work carried out under the guidance of **(DIPIKA GUPTA)** is a result of my own research work and has not been previously submitted to any other University for any other Degree to this or any other University.

Wherever reference has been made to previous works of others, it has been clearly indicated as such and included in the bibliography.

I, here by further declare that all information of this document has been obtained and presented in accordance with academic rules and ethical conduct.

Name of the learner: Neha Kiran Phatak

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Signature of the Student

(NEHA KIRAN PHATAK)

CHAPTER ONE

1.0 INTRODUCTION

For both developing and developed countries, small and medium scale firms play important roles in the process of industrialization and economic growth. Apart from increasing per capita income and output, Small Medium businesses create employment opportunities, enhance regional economic balance through industrial dispersal and generally promote effective resource utilization considered critical to engineering economic development and growth. However, the seminal role played by Small Medium businesses notwithstanding its development is everywhere constrained by inadequate funding and poor management. The unfavourable macro economic environment has also been identified as one of the major constraints which most times encourage financial institutions to be risk-averse in funding small and medium scale businesses.

The reluctance on the part of financial institution to fund Small Medium businesses can be explained by the insufficient capital base of banks and information asymmetry that often exists between Small Medium businesses and lending institutions. This study critically examines the availability of business credit to small business , and how more funding can be made to support small businesses. However, this chapter, forms the basic foundation for this study as it presents the objectives of the study, and the statement of problem that motivated the researcher to undertake the study.

The access to bank credit and its availability is one of the key factors to be considered development of a company. Many Polish companies use bank loans as the main source of external capital. Credit availability varies according to many factors related to enterprises and the operating banks. One of the features which may be described as differentiating the terms of credit availability is the size of the enterprise. Small and medium-sized enterprises, despite their importance for economic development, encounter many difficulties in searching for capital due to an insufficient amount of information forwarded to banks and its asymmetry. However, the better the economic condition of an enterprise and the more information about an enterprise available, the easier it is to gain access to bank funding. The aim of the research was the determine the differences in the access to bank loans in terms of the length of the relationship with the bank institution, the size and age of the companies, along with other characteristics. Among the factors determining credit availability the ones that characterize enterprises (e.g. company's age, its financial results, the length of the relationship with the bank, the number of operating banks), as well as the features characterizing the banking sector (i.e. concentration ratio of the banking sector, interest margin indicator) were analyzed. A model approach to enterprise cooperation with banks is presented. On the basis of the logit model results and on the panel data, the factors significant for credit availability are presented, both the ones lying on the side of an enterprise as well as the banking environment. The research was carried out considering small and medium-sized enterprises (SMEs), as well as young and mature companies. Additionally, on the cross-sectional data, there was an analysis of the factors influencing the denial of credit by a leading bank and the factors influencing the inclination to use the services of many banks.

1.1 BACKGROUND OF THE STUDY AND ORGANIZATIONAL PROFILE

During the 1990s, a number of studies documented that lending to small businesses and the economic activity of small businesses were affected by financial sector disruptions, such as the widespread merging of banks of all sizes and the capital shortfalls occasioned by large loan losses. Although not much previous research has examined discrimination in small business credit markets, there has been an active debate on the question of whether banks discriminate against minority applicants for mortgages. In an influential study in that area, researchers at the Federal Reserve Bank of Boston tried to collect any information that might be deemed economically relevant to whether a loan would be approved along with the borrower's Raceland financial status (Munnell et al., 1996). In the raw data larger firms had 10 percent of their loans rejected versus rejection rates of 28 percent for small scale businesses. After controlling for the large number of variables collected to establish the credit-worthiness of the borrowers (including, the amount of the debt, debt/income ratio, credit history, loan characteristics, etc.) small scale businesses were still percentage points less likely to be granted the loan.

A variety of criticisms have been launched at this study (see, for example, Horne 1994;Day and Liebowitz, 1998; Harrison, 1998); responses to these criticisms are found in Browneand Tootell (1996). The most common critique indicates that we cannot make a determination of discrimination unless those small businesses whose loans are approved have a greater likelihood of repayment. This argument rests critically upon an implied assumption that the distribution of repayment probabilities for large companies and small businesses is identical. His figure indicates that if this assumption is met and if firms discriminate against small businesses by setting a higher bar for loan approval, then the mean rate of repayment among small businesses conditional upon loan approval will be higher for large and smaller firms.

In most cases, small businesses appear to have been able to meet their credit needs. However, in some cases, small businesses may have wanted more credit than they were able to obtain. Data from the ASE indicate that in 2014 the majority of firms did not apply for a new loan of any type, although, for those that applied, success rates were relatively high. Among the 13 percent of firms that applied for a bank loan, nearly threefourths received the full amount for which they applied. Credit card applications were slightly less frequent than bank loan applications, although a bit more likely to have been approved. New home equity loan applications for businesses were even less common, with slightly more than 30 percent of applicants not receiving all of the funding they sought from this source.

Some firms that may have wanted additional credit may not have applied for it because they anticipated that their applications would be denied. Such firms are known as "discouraged borrowers." The ASE asks firms whether there were times during 2014 when the business needed additional financing but the owner chose not to apply. Almost 10 percent of firms fell into this category. The reason most commonly stated for not applying for additional credit was that the firm did not want to accrue debt, with nearly two-thirds of discouraged firms providing that response.

Usage of different types of small business credit varies by the age and industry of the firm as well as by the gender, race, and ethnicity of the owners. However, the usage represents the intersection of what firms would like to use to finance their firms with what providers are willing to supply. The additional questions in the ASE on loan applications and forgone applications would indicate that--at least for some firms--demand exceeds supply. But it is important to keep in mind that not all credit applications should be approved. There is a great deal of fluctuation in the small business population, and determining which businesses are a good credit risk is a challenge that small business credit providers need to carefully evaluate.

1.2 RESEARCH OBJECTIVES

This paper is aimed at the following objectives:

. To examine the relationship that exist between small scale businesses and financial institutions that grant business credits.

. To identify the challenges faced by small businesses in securing business credit.

. To examine the degree of business credit availability to small businesses.

. To identify the effects of businesses credit availability on small businesses.

1.3 SIGNIFICANCE OF THE STUDY

This study is very important because it is aimed at examining the effects of business credit availability and its effect on small businesses. The paper will provide some relevant recommendations for policy makers, development agencies, entrepreneurs, and small business managers to help seek better ways to increase business credits to small businesses, and appropriate strategies to improve the small business sector in Nigeria. Secondly, the study is also vital since it suggest to small businesses certain strategies they can adopt before seeking business credits, to make their borrowing process easier and more effective. This will go a long way to increase the efficiency and profitability level of small businesses. Any time these strategies are put in place, access to business credit increases, and the participation of more people in entrepreneurial activities will also increase, hence the economy of India will be improved.

1.4 SCOPE OF THE STUDY

The area chosen for this study is Mumbai Suburbs in Maharashtra. The study is limited to the effects of business credit availability on small businesses , using various small businesses in India as a focus point.

CHAPTER 2

2.1 What is Small Business Credit?

Just like you have a personal credit score, your business also has a credit score. Business credit is a track record of a business's financial responsibility that companies, investors, or financial organizations use to determine whether or not that business is a good candidate to lend money to or do business with.

There are a number of agencies that calculate business credit, and each agency has a different calculation method, but typically this is a ranking from 0 to 100. The higher the number, the lower your calculated risk. Maintaining a score of 80 or higher is a good rule of thumb.

Common factors that impact your small business credit are public records, such as liens or bankruptcies, credit, such as outstanding balances and payment habits, and demographic information, such as business size and years on file.

2.2 Why is Business Credit Important?

Strong business credit can help you grow your company. Many banks, investors, and companies rely on your business creditworthiness when setting loan terms, determining insurance premiums, increasing lines of credit, or considering you as a viable partner.

According to the Small Business Administration (SBA), insufficient or delayed financing is the second most common reason for business failure. Because anyone can view your business credit score—it's not confidential—it's important to establish business credit from the start receive better interest rates, loan terms, and negotiation leverage on payment periods with suppliers.

As a small business owner, separating personal credit and business credit is also important. Think of your small business credit as a wall dividing your business decisions from your personal credit history. Rather than being linked to your name and Social Security number, business credit is linked to your business entity and separate Tax ID number.

This separation can remove potential funding obstacles that could prevent your business from growing. Likewise, it limits your personal liability while running a company—in the event your business went under, your personal credit would be protected.

2.3 How is Business Credit Calculated?

Major business credit bureaus include Dun & Bradstreet, Experian, and Equifax. Each agency uses slightly different indicators and methods to calculate a score.

- Dun & Bradstreet uses PAYDEX, a score ranging from 1 to 100 based on the payment history information Dun & Bradstreet has on file. The higher the score, the better your payment performance is.
- The Equifax business credit score compiles three different factors to determine the risk level of your business: a payment index, which is reflective of making on-time payments, a credit risk, which considers the likelihood of your business becoming severely delinquent, and a business failure score, the likelihood of your business closing.
- Experian uses, a statistically based credit score with a 1 to 100 rage that takes multiple factors into account such as years in business, payment history, and new lines of credit opened.

Small businesses should also be aware of (SBSS), which ranks businesses on the likelihood of making on-time payments. SBSS scores are used for term loans, lines of credit, and commercial loans up to $350,000 from the SBA. Scores range from 0 to 300, the higher the score the better. To pass the SBA's pre-screen process you need a minimum score of 140.

2.4 About Small and Medium-sized Enterprises (SME) Loans

Small & Medium scale industries play an important role in the economic development of a country. Apart from strengthening the exports of a country, they provide employment to millions of Indians. The Indian Government has many schemes in place for the establishment and development of the Micro, Small &Medium Scale industries all over the country.

Initial capital and working capital are required to run any industry smoothly. Numerous industrial financing institutions and banks, both public sector and private sector, have customized Small &Medium-sized Enterprises (SME) loan products to aid the MSME sector in their growth.

2.6 What is an SME loan?

SME Loans are given to entrepreneurs, either aspiring to set up a new business or modify and expand a current establishment. SME loans can be availed even for technological up gradation of a particular process. Some businesspersons would like to avail an SME loan to upgrade their manufacturing unit to adapt greener energy alternatives. These are some of the purposes for availing an SME Loan.

Where to get an SME loan?

1. Government Banks or PSU Banks (SBI, Bank of Baroda, Punjab National Bank, etc)

2. Private Banks (ICICI Bank, HDFC Bank, AXIS Bank, etc)

3. NBFCs (Mahindra Finance, Bajaj Capital, Fullerton, Tata Capital etc)

The government disburses financial loans to various SMEs through dedicated schemes built for this purpose. Entrepreneurs can approach various PSU Banks that are authorized to give loans under these schemes. Banks also have their own MSME loan products.

2.7 How is an SME loan processed?

As mentioned earlier, proprietor of an established business or an aspiring entrepreneur can approach a bank or an NBFC for an SME Loan. While applying for an SME loan, one should have done the basic groundwork with regards to the type of loan, the amount required, the eligibility criteria etc. The process usually consists of the below steps:

1. Prepare a comprehensive summary of the business and purpose of the loan

2. Attach supporting documents to establish the worth of your business idea or establishment

3. Briefly explain the benefits you are expecting to derive out of the loan

4. Promptly fill the necessary forms required by the financial institution and duly submit it to the authorized person

The SME Loan process is quite simple and straightforward in most banks. With sufficient documents to support the purpose of your loan, it would be processed quicker and the funds disbursed to your account. Banks look into a few eligibility criteria while processing your SME loan

- Proprietorship of the firm – Sole or Partnership
- Nature of the holdings – Private limited company or Public limited company
- Nature of business – Manufacturing or service units
- Profitability of existing businesses – steady profit for 2 or more years
- Monetization factors of new business – how soon can a new business become profitable
- Registration and recognition of the establishment under Government norms

The above factors help the banks/NBFCs in deciding the creditworthiness of the business and hence the approval of loan. The applicant should take special care in highlighting these factors in their loan application.

2.8 Small Scale Industries Loan Procedure

India’s small-scale business segment contributes approximately 40% to the country’s GDP (Gross Domestic Product). Also known as the SME (Small and Medium Scale Enterprises) sector, it is a key source of employment and income. Stiff competition in this sector requires entrepreneurs to scale-up, innovate and upgrade their existing setups. Business expansion is key to succeed as an SME in India.

Businesses operating in this sector thus require external financing as small scale industries loan from lenders. They can avail these loans from both government and private financial institutions. Such funds are commonly utilized to meet daily operations, expand the business, and fulfil such other requirements. GOVT Loan Schemes for Small Scale Industries

The Government of India also extends these advances through govt. loan schemes for small scale industries like –

- PMMY (Pradhan Mantri Mudra Yojana)
- CGSMSE (Credit Guarantee Scheme for Micro and Small Enterprises)
- SMILE (SIDBI Make in India Loan for Enterprises)

Additionally, private lenders also facilitate the financing of small scale industries through various loans and advances. For instance, Bajaj Finserv brings its SME and MSME loan of up to Rs.20 lakh to help businesses meet their financing requirements at ease.

2.9 Use of Small Scale Industries Loan

Avail an industrial loan for small scale industry to fulfil multiple funding requirements of your business.

i. Expand the firm's infrastructure.

ii. Install new equipment, plant & machinery.

iii. Fulfil your business's working capital requirement.

iv. Meet operational expenses like overhead payments, inventory purchase and more.

v. Maintain cash flow of the business with external financing availed under small scale industries loan scheme.

2.10 Eligibility Criteria for Small Scale Industries Loan

Eligibility requirements vary depending on the Central Government small scale industries loan scheme availed. Check out the basic eligibility requirements to look for when availing such advances.

- **Business type –** The business should fall under microenterprise category engaged in manufacturing, trading and services industry. The loan is also available for professionals like doctors, engineers, CAs, etc.
- **Residential status –** He/she should be a resident of India.
- **Age requirement –** Borrower must also meet the age requirement laid down by the concerned financial institution.
- **Business status –** Meet the business vintage requirement for a minimum of 3 years to avail a small scale industries loan from NBFCs like Bajaj Finserv.

Credit score – Fulfil the minimum credit score requirement of 750 with zero payments default for improved chances of loan approval. Also, fulfil the documentation requirements of the lender for faster processing of your loan application. Keep the following documents handy before applying.

- KYC documents including proof of identity and proof of address, like Aadhaar card, voter ID card, PAN card, etc.
- Financial documents like profit and loss statement, balance sheet, tax returns and audit reports, etc.
- Bank account statements.

Submit any other necessary documents required by your lender to avail the loan.

India has more than 40 million registered and unregistered SMEs engaged in varied sectors including IT, manufacturing, packaging, and food processing. This sector is one of the key growth drivers of the country, contributing about 40% to India's GDP. Recognising the importance of this sector, the government has started the 'Make In India' initiative to encourage more SMEs to become a part of India's growth journey.

2.11 Challenges of SEM's Loans

Owing to their small size, SMEs and MSMEs, as compared to big firms, are burdened with many challenges that come in the way of their growth. The most important are accessing finance at the right cost and getting the support of labour at the right time. Here are some of the other common challenges that this business sector has to deal with in order to increase their efficiency and output.

- Trained talent migrates from SMEs to higher paying jobs as soon as a lucrative opportunity comes along, which undermines the firms' stability.
- In order to survive in the market and stay relevant, SMEs tend to drop the prices of their services and products below profitable levels. This shakes up the market prices for competitors too and leads to overdependence on existing clients.
- Unlike bigger firms, who have ready cash to fall back on, SMEs have to rely on their working capital to fund every need of the hour. Sometimes this is not enough given their recurring expenses. This is especially a challenge when it comes to investing in new technology to fuel their growth.
- Another bigger point of contention for start-ups is that they have to eye growth keeping their USP intact. Maintaining the same quality of goods and services while they grow into bigger firms is difficult for most start-ups as they don't enjoy the finances required for rapid expansion, be it hiring best-in-class talent or buying state-of-the-art equipment.

SMEs can deal with these challenges with adequate and timely funding, which government loans aim to provide to different sectors. As a business owner, here are the top government business loan options you can choose from.

CHAPTER THREE

3.1 GOVERNMENT SCHEME FOR SES

1. **MSME *Government Business Loan Scheme***

The Indian Government launched the MSME business loan scheme as a working capital loan. As an MSME, you can get a loan sanction of up to Rs.1 crore within just 59 minutes. The best part is you get this loan at 8% rate of interest, keeping the repayment easy on your pocket. A reservation of 3% is available for women entrepreneurs, so as to offer a quick sanction to the increasing number of women helming their own business today.

When applying for the loan, follow these basic steps:

- Enter your business’s GST's identification number.
- Upload the income tax returns for your business in XML format
- Upload the bank statements of your business account for the last six months in PDF format.
- Enter the director/owner’s details for your business. This will include all details related to personal, educational, and ownership criteria.
- Submit the application to enjoy an on-principle sanction within 59 minutes!

Features:

- You can avail a loan of up to Rs5 crore where the amount will be deposited to your account in less than 60 minutes.
- Minimum documents required. You only have to upload the scanned versions of the required documents and upload it online for you to avail the loan.
- You can avail a loan between Rs.1 lakh and Rs.5 crore under this loan scheme. Since you have the option of availing this loan from any of the lenders, the rate of interest levied may differ. The rate of interest however starts at 8.5%.

2. **MUDRA Business Loan**

Established by the current government, Micro Units Development and Refinance Agency (MUDRA) has envisioned the idea of 'funding the unfunded' and put it into action with a funding scheme. Small business entities and start-ups are given financial support in the form of low-cost credit. MUDRA Loans are financed through public and private sector banks, co-operative societies, small banks, scheduled banks.
Broadly, any MSME operating in the manufacturing, trading and services sector is eligible for the MUDRA loans. Your firm can avail funds via the government business loan scheme under three subheads.

- Sishu Loans up to Rs.50,000
- Kishor Loans up to Rs.5,00,000
- Tarun Loans up to Rs.10,00,000

To facilitate easy funding, the government has recently introduced the MUDRA Card. This innovative product provides a working capital facility as a cash credit arrangement. This card is given to you as a debit card against your MUDRA loan account. Based on your sanction, you can withdraw funds from your MUDRA loan account multiple times. Until and unless you use a portion of the sanction, you will not be charged interest on it. You can use your MUDRA card for POS purchases or to withdraw cash from any ATM across the country.

3. Credit Guarantee Fund Government Business Loan Scheme

CGTMSE has been in action for 18 years now. Since its inception, the Credit Guarantee Fund Trust for Micro and Small Enterprises has been facilitating collateral-free loans for MSMEs. Any scheduled commercial bank and regional rural bank can become a part of the scheme by empanelling itself as a lending authority. The agency sanctions loans to eligible Micro and Small Enterprises basis their credit standing via the lending agencies in question. The scheme provides working capital loans up to Rs.10 lakh and has provisions for bigger sanctions as well. However, to get approval for an amount exceeding Rs.10 lakh, you will need to mortgage your business assets and land.

Features:

- The scheme was launched with an intent to offer collateral-free credit to the micro and small enterprise sector.
- Both working capital facility and term loans are eligible to be covered under the scheme.
- Under the scheme, guarantee cover can be availed up to 85% of the sanctioned amount of the credit facility.
- For microenterprises seeking a loan of up to Rs.5 lakh, MSEs owned and operated by women, and loans in the North-Eastern region, guarantee cover of up to 80% will be provided.

4. National Small Industries Corporation Subsidy

Established in 1955, NSIC offers MSMEs two kinds of funding benefits: raw material assistance and marketing assistance. Any business qualifying as a micro and small enterprise having EM Part-II (Optional)/ Udyog Aadhaar Memorandum (UAM) is eligible to register for this government business loan scheme under its Single Point Registration Scheme (SPRS). Once you qualify, you can opt for the raw material assistance scheme, where funding for both indigenous and imported raw material is covered. Under the marketing support, you can avail funds and use it to enhance your competitiveness and the market value of your offerings. The NSIC also overlooks the functioning of an MSME and supports it in its endeavour to enrich production and quality.

5. Credit Link Capital Subsidy Scheme

This government business loan scheme funds technological up gradations. Under the varied facets of the scheme, you can access finance to enhance your technology and equipment. You can use the funds from your sanction to undertake a revamp related to numerous processes for your business, like manufacturing, marketing, and supply chain. Through this scheme, the government plans to reduce the production cost borne for creating and providing goods and services by small and medium enterprises. This will pave the way for a more competitive local and international market ecosystem. Under this scheme, you can get an upfront 15% capital subsidy for your business. However, the maximum amount you can avail as subsidy is capped at Rs.15 lakh. In order to be eligible for a loan under this scheme, you need to apply as a sole proprietorship business, partnership firm, and co-operative or private and public limited company.

6. SIDBI Make in India Soft Loan Fund for MSMEs (SMILE)

Launched in 2015, SMILE is governed by Small Industries Development Bank of India (SIDBI). The aim of this scheme is to provide soft loans, to meet the required debt-equity ratio for the establishment of new MSMEs and also to enable the growth for existing ones. The interest rate offered under SMILE scheme is 8.36% onwards.

Eligibility: New enterprises on board along with the existing manufacturing and services sectors can apply for this scheme. Existing enterprises undertaking up-gradation or starting other projects for expanding their business will also be covered under this scheme. The maximum loan repayment tenure is 10 years with 36 months of moratorium period.

Fiscal incentives:

- The loan amount offered under SMILE scheme is minimum Rs. 25 lakh and onwards

3.2 SMALL ENTERPRISES IN INDIA

1. The Rationale For Promotion Of Small Enterprises

Support schemes for small enterprises form an important development strategy in many economies. Since the late 1950s, the Indian government has supported small enterprises to generate employment and to promote balanced regional development. Various preferential schemes such as credit assistance, tax exemption, purchase preference by the government agencies and preferential access to raw materials have been provided for small enterprises. The most important scheme, however, was the reservation policy.[3] The schemes of protection and promotion of small enterprises were designed on the presupposition that small enterprises cannot obtain adequate credit due to asymmetric information and that they cannot enjoy scale economies in material purchases and marketing. Since the economic liberalisation began in 1991, the environment surrounding small enterprises has changed. On the one hand, small enterprises have faced severe competition from imported products. On the other hand, small enterprises have been increasingly expected to act as a growth engine due to their flexible and innovative nature.

The definition of small enterprises varies across countries and sectors. In India, micro and small manufacturing enterprises have been defined in terms of the value of investment in plants and machinery since 1966, and the investment ceiling in plants and machinery has been revised from time to time. As per the Micro, Small and Medium Enterprises Development (MSMED) Act 2006, micro and small manufacturing enterprises are defined in terms of enterprises whose investment in plants and machinery does not exceed Rs. 50 million.[4] These enterprises produce over 6000 products and account for approximately 45% of India's total manufacturing output. In this paper, we confine our analysis to micro and small manufacturing enterprises ("small enterprises" hereafter). This is partly because lending to medium enterprises is not included for priority sector lending described below and partly because manufacturing enterprises have more nature and potential for creating jobs.

2. Credit Policies For Small Enterprises In India

The Government of India and Reserve Bank of India (RBI) have been instrumental in devising a multi-agency approach to extend financial services to small enterprises. These include commercial banks, co-operative banks and development financial institutions. Commercial banks with their extensive networks of branches accounted for 91.2% and co-operative banks accounted for 6.5% of the total formal credit for small enterprises, and development financial institutions such as the Small Industries Development Bank of India (SIDBI) and State Financial Corporation (SFC) accounted for 2.3% of the total formal credit as of March 2008.

Commercial banks have been the most important source of formal credit to small enterprises. In particular, public sector banks have been playing a dominant role in disbursing credit to small enterprises since the nationalisation of major commercial banks in 1969 and 1980. In 1972, small enterprises and agriculture were identified as a priority sector, which might not receive timely and adequate credit in the absence of this special dispensation. Although there was initially no specific target fixed in respect of priority sector lending, in 1974 commercial banks were asked to direct 33.3% of their credit to the priority sector by March 1979. Subsequently, commercial banks were asked to direct 40% of their credit to the priority sector by March 1985. A sub-target for agriculture was also fixed at 18% by March 1990, while a specific sub-target was not fixed for small enterprises. Over the years, private sector indigenous banks and foreign banks have also been asked to get involved in the priority sector lending.

Since the financial sector reform began in the 1990s, the definition and scope of the priority sector was expanded, although the quantitative target for the sector has remained unchanged. New sections such as housing loans and micro credit have been introduced, and ceiling limits on advances to education and housing loans have been raised, especially since the early 2000s. More affluent borrowers who are not considered to be among the vulnerable were included in the priority sector because the upward revision of the loan ceiling would not have been justified on the grounds of inflationary pressures. Such expansion of the coverage of the priority sector seems to have adversely affected the credit availability of small enterprises. Demonstrates, the share of small enterprises' advances in net bank credit by public sector banks has been decreasing since the early 2000s, while the share of others including housing loans in net bank credit has been increasing.

In addition to the priority sector lending requirement, public sector banks have been mandated to open at least one specialized branch for small enterprises in each district to ensure sufficient credit flow for small enterprises. Public sector banks have also been asked to open specialized small enterprises' branches in identified clusters with a dominance of small enterprises to enable entrepreneurs to have easy access to bank credit and equip bank personnel with the requisite expertise since 2005.

3.3 FACTORS AFFECTING ACCESS TO FORMAL CREDIT BY SMALL ENTERPRISES

In spite of the longstanding supply side credit policies, the share of credit flow to small enterprises appears to be deteriorating, as economic liberalization proceeds. The cost and availability of credit is a major issue facing small enterprises in India. It may be interesting to consider why lenders will not give loans to small enterprises and investigate the demand side factors affecting access to formal credit. To look into the factors that could affect small enterprises access to credit, we review the literature on credit constraints.

1. The Literature On Credit Constraints For Small Enterprises

Weise argue that credit rationing may be an equilibrium situation when there is imperfect information. This is because information asymmetries exist between lenders and borrowers in the ex-ante screening of projects (adverse selection) and ex-post monitoring of loan contracts (moral hazard). If a rise in the interest rate to clear the market lowers average borrowers' quality, lenders will choose to ration their credit.

Although credit rationing is not unique to small enterprises, small enterprises are more likely to face restrictions in the credit market due to higher transaction costs of lending to small enterprises. Transaction costs of lending to enterprises comprise administrative costs and default costs. Administrative costs are those that are attributable to the processing, delivering, and administrating of loans. Default risk costs are those expenses for provision for losses, loan guarantee fees paid, and actual bad debts.

Even if the administrative costs are constant regardless of the loan size, the costs as a percentage of loan size decrease as the loan size increases. Assuming that the size of a loan is positively correlated with the size of an enterprise, the per unit transaction costs of lending to a small enterprise are higher than those of lending to a large enterprise. However, in practice, the default costs and the administrative costs are not constant but higher for small enterprises than those for large enterprises for the following reasons.

It is well known that the provision of collateral may reduce the problems of information imperfection and cover losses through default, but small enterprises do not own sufficient assets for collateral. If any, because pledged land or building is often of a personal nature, some costs may be present in arranging and foreclosing such collateral . Reliance on such personal assets may discourage a lender's investment. Lenders may also utilize financial statements and enterprises' performance such as sales and profits to assess repayment prospects. However, small enterprises in developing countries may not have complete financial statements, and more time is therefore required to evaluate their creditability. Earlier studies on Indian small enterprises have found that a large number of owners do not maintain formal accounts. Moreover, in a number of cases, there is no clear separation between the account of the owner's household and that of the enterprise. In addition, small enterprises may show relatively more volatility in the face of economic slowdowns because they have less diversified products.

These factors taken together lead to the higher transaction costs of lending to small enterprises. Estimate the real costs of lending to small enterprises are approximately twice those of lending to large enterprises in the Philippines.

In addition to the above hard information, some studies argue that lenders may utilize alternative soft information such as the age of an enterprise, the relationship with banks, past communication with contractors, and other sources of finance in the case of informationally opaque small enterprises. Conditional on its past experience with the borrower, the lender now expects loans to be less risky. This could reduce the transaction costs of lending. It is also possible that lenders could obtain information on an enterprise's ability to serve claims by observing its past interactions with contractors.

There is some evidence that small enterprises that are linked as suppliers to successful large enterprises usually succeed in their ventures in many economies find that small enterprises in the auto component industry acquire knowledge and technology spillovers through continuing relationship with assemblers and large auto component enterprises in India. Their finding may be understandable because Japanese major assemblers and parts makers have entered into capital and technical tie-ups with Indian enterprises in the automobile industry, and therefore, the Japanese method of supply-chain systems has penetrated. Considering these studies, it may be expected that if a small enterprise has a contractual relationship with a large enterprise, it may then face less credit constraints. However, find that in the case of small enterprises in India, while working under sub-contract with larger enterprises has been increasing in recent years, enterprises working under contract do not perform better than those not working under contract. In other words, it may be concluded that on average, small enterprises working under contract may be driven to subcontracting under distress and eventually do not gain significantly from this relationship. In addition, the relationship has been found to be exploitative with the issue of delayed payment. Thus, the effect of small enterprises' sub-contracting relationships with large enterprises for availability of formal credit is not unambiguous in the case of India.

2.Other Factors Affecting Access To Formal Credit In India

Looking at other variables that could affect the credit availability of small enterprises in India, enterprises that register under an act/agency are likely to have better access to formal credit as being registered in practical terms makes it easy to access the government's support schemes for small enterprises. In addition, by the process of registration, the registered enterprises give their information to agencies and can therefore be expected to be more transparent than non-registered enterprises, and can hence be expected to have less information asymmetry. Thus, registration status should be positively associated with the probability of access to formal credit.

Enterprises with more educated owners can be expected to have easier access to formal credit than enterprises with less educated owners. This is because less educated owners tend to have more difficulty with application procedures and expect to be rejected. In addition, educated owners are more likely to have managerial skills in finance, marketing production, and international business that would lead to the enterprise's growth.. Further, the gender of the owner of an enterprise may play some role in access to formal financing, as the literature shows that female owners are more likely to be financially excluded.

As note, banks may prefer enterprises of specific industries such as growing industries. Further, enterprises engaged in capital-intensive industries with higher credit needs for initial project scale and continuing investment may face relatively greater constraints.

There may be regional effects because enterprises belonging to more developed regions with a high density of bank branches will have easier access to banking services.

3.4 CREDIT AVAILABILITY AFFECTS BUSINESS VALUATION

The credit debacle in August brought the large, syndicated leveraged-loan market to a standstill. While we are still assessing the full impact of these events on the middle market, it is clear that credit spreads have widened and the leverage allowed to borrowers has declined. Knowledgeable commentators in the field, including Zachary Scott, have predicted that a restriction on the availability of credit would dampen the prices paid for businesses. This is perplexing, as it flies in the face of accepted corporate finance theory.

The chart below shows the relationship between allowed leverage, as measured by debt-to-cash flow covenants required by leveraged lenders, and the prices paid for middle- market businesses, as measured by the ratio of enterprise value-to-cash flow. The data appear to be highly correlated and our experiences in recent years support that conclusion. However, accepted corporate finance theory says that the availability of credit should not influence valuation conclusions, so what is going on?

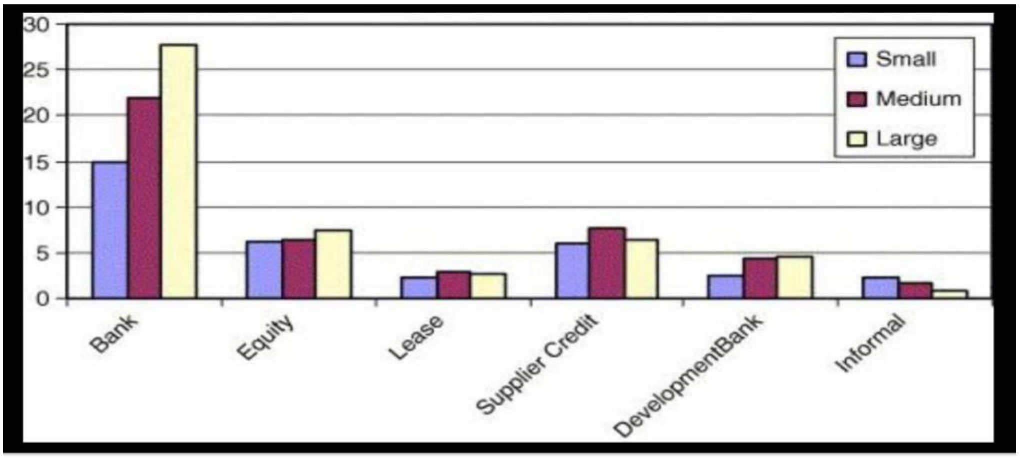
THE THEORY

There are two corporate finance principles that tell us that the availability of high levels of leverage should not affect value.

- The first principle is that the risk of an asset, as measured by the variability of the cash flow generated by it, corresponds to a specific expected rate of return appropriate for that level of risk. In other words, each business has its own distinct discount rate that reflects the operating risks of the underlying business, exclusive of its capitalization. The value of any business is the present value of its expected future after-tax cash flow stream, discounted by the rate that reflects the risk of that business.

- The second principle is that, as a result of taxes (and the tax deductibility of interest expense), a modest amount of debt in the capital structure enhances the returns to the equity holder. As leverage increases, the risk of insolvency and the costs of bankruptcy correspondingly outweigh the advantage of the tax deductibility of interest.

Without trivializing the nuances of these principles, our observation is that real world practices differ from accepted theory.



CHPATER FOUR

4.1 REVIEW OF LITERATURE

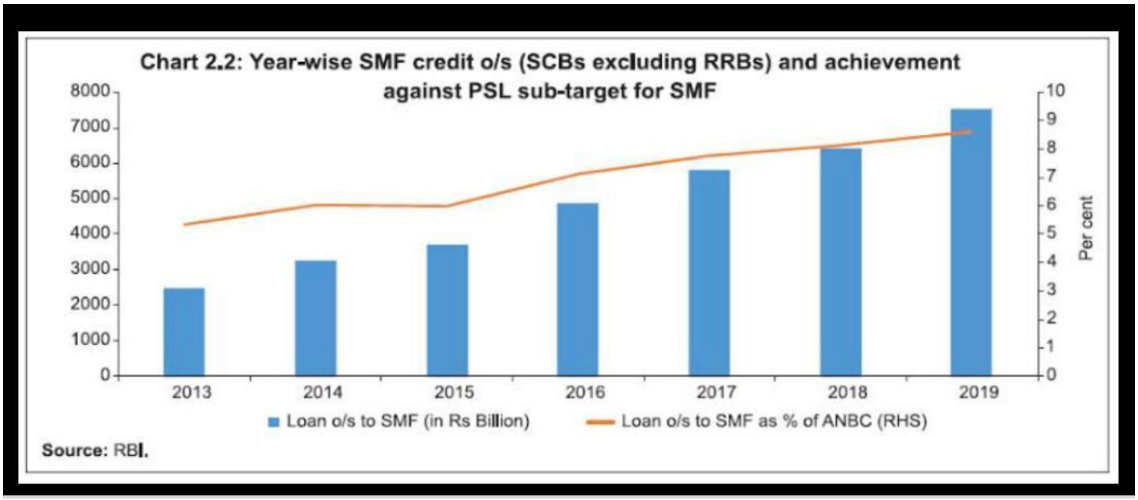
The predominant sources of finance used by MSMEs are bank loans; loans from institutions (e.g., NBFCs); venture capital; microfinance institutions; loans from family, relatives, and friends; equity finance; and own funds (Mallick et al. 2010; International Finance Corporation 2012; Asian Development Bank 2014). According to International Finance Corporation (2012), the supply of finance to the MSME sector is estimated to be 32.5 trillion Indian rupees (Rs). This total comprises contributions from informal finance, formal finance, and self-finance. Informal sources and self-finance contribute Rs25.5 trillion to the sector, of which informal finance accounts for Rs24.4 trillion. In other words, 78% of the finance used by MSMEs is met by informal sources and self-finance. The remaining 22% (Rs6.9 trillion) is provided by banks and NBFCs, of which banks provide the bulk (91.8%). It is unlikely that the financial services offered by banks sufficiently address the requirements of early-stage small and medium-sized enterprises (SMEs) (Banerjee 2006). There are several conditions that hinder the provision of bank credit to early-stage SMEs in India. Early-stage SMEs do not have an established credit history and have unstable equity patterns. Biswas (2014) noted that access to external finance apart from banks is costly and limited, and poses a challenge to SMEs, although it is essential for the maintenance of long-term opportunities and targets. These external loan products also require collateral and are highly priced. SMEs use finance from NBFCs and informal sources at higher rates of interest, particularly in the early stages.

The dominance of the informal sector in addressing the financial requirements of MSMEs is due to the inherent limitations of formal sources of finance. The Asian Development Bank (2014) has pointed out that barriers to accessing finance by SMEs in India from formal institutions include the requirement for collateral or a guarantee, inflexible policies, high rates of lending, complicated procedures, and entrepreneurs lack of financial knowledge of applicable schemes. Ambrose (2012) also identified barriers to effective financial assistance to SMEs, which included absence of collateralized security, and the regulatory framework. In addition, the unavailability of skilled workers, the lack of infrastructure, and an inability to raise capital through the stock market (especially for MSMEs with a net worth of less than Rs100 million (about $1.5 million) are other challenges (Lahiri 2012). Barriers have also been examined in the context of gender (Irwin and Scott 2010), firm size, the length of a lending relationship, and the use of overdraft credit (Bebczuk 2004). The Reserve Bank of India (2005) identified the following issues in financing SMEs: (i) inadequate access to finance by tiny firms due to lack of financial information and nonformal business practices, with a lack of access to private equity, venture capital and secondary market instruments; (ii) fragmentation of markets with respect to their inputs as well as vulnerability of products due to market fluctuations; (iii) lack of easy access to interstate and international markets; (iv) limited access to technology and product innovations, and lack of awareness of global best practices; and (v) considerable delays in settlement of dues and payment of bills by large-scale buyers.

The perception of an SME as a high-risk and commercially unviable proposition to lend to has resulted in only a few SMEs receiving formal financial assistance (Ambrose 2012). Prasad (2006) highlighted that Indian banks in particular are not inclined to finance small enterprises, due to reasons such as the inability to provide collateral, high levels of nonperforming assets, high transaction costs, and the inability to verify the creditworthiness of applicants.Grant Thornton and FICCI (2011) concluded that the cost of capital is high for MSMEs, and that there is a need to reduce the time and documentation required for procuring finance. Lahiri (2012) pointed out that with MSMEs' rising need for short-term and long-term capital, banks should move toward more innovative methods of lending to provide for those firms' financial needs. In light of the abovementioned barriers, the Government of India (2015b) initiated several policy measures: (i) achievement of universal financial inclusion of MSMEs in a time-bound manner, ensuring that every registered MSME has a bank account linked to the Udyog Aadhaar; (ii) operationalization of an Rs100 billion equity fund for the MSME sector; and (iii) expanded coverage and enhanced utilization of credit guarantee schemes with inclusion of a wider set of credit providers such as NBFCs and microfinance institutions, which could involve a sevenfold increase in the corpus from Rs40 billion to Rs280 billion.

CHAPTER FIVE

Data Analysis



This survey was developed by Industry of Maharashtra and is commissioned to monitor changes in lending conditions. It was conducted in 2009 and 2010 and will be conducted in years when the Survey on Financing and Growth of Small and Medium Enterprises is not conducted. Analysis focuses primarily on debt financing as it is by far the largest source of financing for small businesses. A representative sample of over 3500 respondents is normally collected.

For the purpose of both surveys, a small business was defined as a business that:

Operates in the manufacturing; retail/wholesale trade; professional, scientific and technical services; accommodation and food services; agriculture; construction, mining; transportation; or other services industries;

Employs between 1 and 99 employees; and

Generates between $30 000 and $50 million in annual revenues.

Exclusions from the target populations include sole proprietorships, non-profit and government organizations, schools, hospitals, subsidiaries, co-operatives, and financing and leasing companies.

What Is a Credit Report?

A credit report is a detailed breakdown of an individual's credit history prepared by a credit bureau. Credit bureaus collect financial information about individuals and create credit reports based on that information, and lenders use the reports along with other details to determine loan applicants creditworthiness.

In the United States, there are three major credit reporting bureaus: Equifax, Experian, and TransUnion. Each of these reporting companies collects information about consumers' personal financial details and their bill-paying habits to create a unique credit report; although most of the information is similar, there are often small differences between the three reports.

Understanding Credit Reports

Credit reports include personal information such as the individual's current and previous addresses, Social Security numbers, and employment history. These reports also include a credit history summary such as the number and type of bank or credit card accounts that are past due or in good standing, and detailed account information related to high balances, credit limits, and the date accounts were opened.

Credit reports also list credit inquiries and details of accounts turned over to credit agencies such as information about liens and wage garnishments. Generally, credit reports retain negative information for seven years, while bankruptcy filings typically stay on credit reports for about 10 years.

How Does The CIR Affect You As A Customer?

The biggest impact of the CIR is that it makes your payment history (or ‘creditworthiness’) available to a lender, when you apply for a new loan or credit card. In the diagram above, a consumer applies for a credit card to a bank. To gauge his credit eligibility (i.e. will he make the monthly payments regularly?), the bank requests CIBIL for his Credit Score and CIR. The information in the CIR contains details of all the loans and credit cards availed by him and how he has been repaying his installments or dues. The consumer, for instance, may have existing home or auto loans with different banks. Banks submit monthly reports of their customers’ payment histories to CIBIL, making it easier for banks to judge customers’ creditworthiness.

Lenders would generally treat all loan-seekers equally. Each applicant, if approved by the lender's internal credit policy, would get charged the same interest rate for a particular loan size and purpose. The lenders would charge a higher interest rate to all borrowers to compensate for the possible default of a small portion of the loans disbursed. In other words, it is similar to a college professor (the lender) punishing an entire class of students (borrowers) for the mischief of a few (defaulters).

Today, the Credit Score and CIR may help lenders differentiate between consumers who have honoured their financial obligations responsibly and those who have defaulted. Individuals who meet their obligations appropriately thus build 'reputational collateral' with lenders. This reputational collateral- in turn- helps individuals to avail of better terms with a lender.

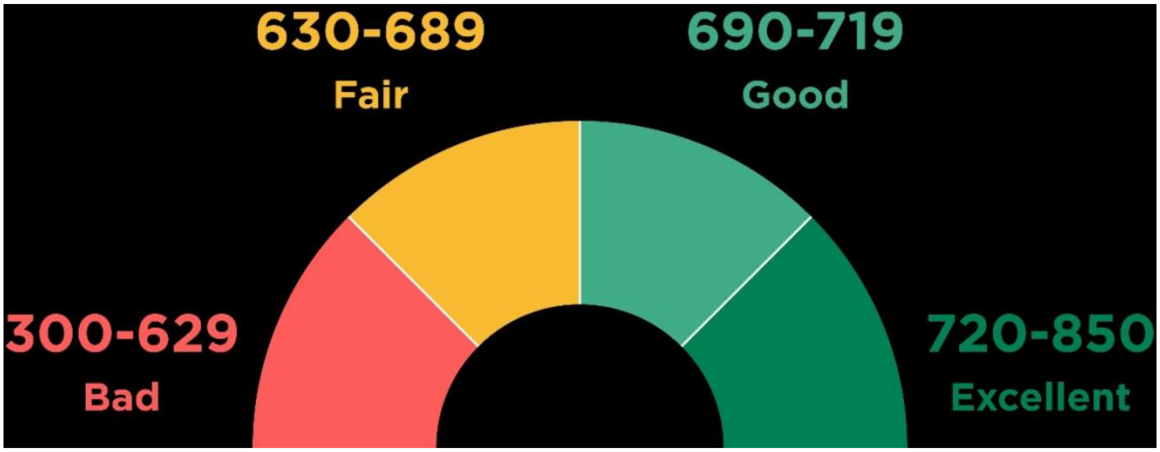
Hence, it is advisable for you to purchase and review your CIR (and Credit Score) before commencing loan application. Firstly, it helps you understand what the lender will review while evaluating your application. Secondly, it is important to identify and rectify discrepancies, if any, on the CIR to prevent any disruptions or delays to the loan evaluation process. While a high score doesn't guarantee loan approval, it does significantly improve the chances of approval, and helps you take control of your financial health.

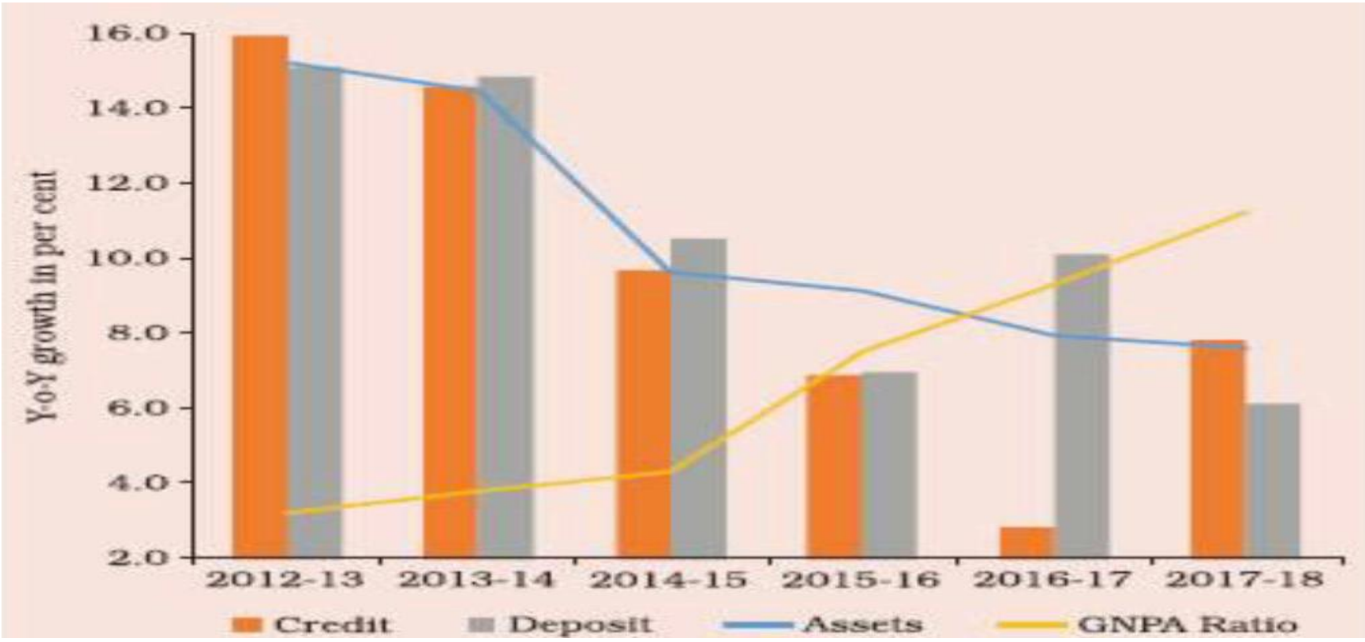
What information does your CIR contain?

The CIR is a month-on-month record of your loan-related EMI payments and/ or credit card payments. It does not include your investment or savings details. Loans include home loans, personal loans, automobile loans and overdraft facilities.

Other information included in a CIR:

- Personal information such as your name, date of birth, address and identification numbers like PAN, passport number, voters number and telephone number as reported by member banks and credit institutions.
- Account information such as type of credit availed (various loans, credit card etc), the size of loan/ credit card limit, outstanding current balance, overdue amount, number of days a payment is overdue, status (written off/ settled), etc.
- Number of 'Enquiries' made by banks about your credit profile- An "Enquiry" is created on your CIR every time the lender requests CIBIL for your CIR (this usually happens when a consumer applies for credit).





As per above table, Credit ratio from 2012 of the Bhagirathi Enterprises which is located in Bhiwandi. The company is entitled as a food corporation. Since 2012 Bhagirathi launching their products with the taste and quality. As per given table orange colour showing credit of the company, grey colour showing deposits, blue line showing assets of the venture and the growing yellow line showing GNPA ratio of the company. It was conducted in the year 2017-2018.

CHAPTER SIX

Conclusion

The results of the research on the influence of credit availability for small and medium-sized companies are in line with those obtained in previous studies. The reapplying the cross-sectional analysis in 2015 has only confirmed the initial results, reinforcing the importance of identified factors of influence. The first conclusion is that in Poland, similarly to other European countries, it is more difficult for small and medium-sized or companies to obtain a credit than the large ones. At the same time, it ought to be stressed that in recent years in both groups of enterprises the number of rejected loan applications had diminished. Most likely, this change is due to the increased willingness of banks to lend money on the background of general improvement of macroeconomic parameters, but also the change for the better of the economic and financial performance of the companies. The main reasons for denying a credit for the enterprises from both the groups remains the lack of proper liquidity and the limited rate of profitability. The result was confirmed by the quantitative studies which were carried out. From the panel and cross-sectional studies, it can be concluded that together with the deterioration of a company's financial situation and the decrease of profitability, the possibility of a credit being denied by both the leading bank as well as any other has increased. The banks' attitude towards the companies having financial difficulties during the period of their cooperation has served to improve the company's situation; at the same time, banks have protected their business. This is why it can be said that banking institutions have played a certain role in supporting and strengthening the economic and financial performances of companies, together with financial discipline and financial communication. As far as large companies are concerned, the banks have decided to continue crediting provided that the enterprises have supply additional collateral or information about the enterprise in order to better monitor its situation. Relative to small and medium-sized enterprises, banks conditioned further crediting upon providing additional information about the company in order to improve the process of monitoring or they decided to increase the previous amount of credit in order to prevent financial problems. For bank lending relationship the situation in the banking sector proves to be very important. The results of the panel analysis showed that, and according to the literature concerning this research area, a better situation in the banking sector and smaller competition between banks (involving greater concentration of assets and a greatergreater interest margin indicator) influenced the increase of the probability that the crediting of a company would be denied. As well as regarding this factor, the results obtained from this study are in line with the results previously obtained. Finally, the results of the analysis of multiple relationships proved that bigger companies cooperate with a greater number of banks more frequently than small and medium-sized enterprises. The hypothesis was also confirmed by the results of the logit study, which showed that the probability of an enterprise using the services of more than one bank increases together with the growth of the enterprise and its debt, and are in line with the results of the previous research.

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