

## Disparity between Demand and Supply of Finance to MSMEs: Dilemma Faced by Financial Service Providers

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### Abstract

Availability of ample and timely credit at reasonable rate of interest is vital for the development of MSME sectors. The major problem Indian MSMEs face is unavailability of adequate amount of finance. There seems to be a gap between demand for and supply of the bank credit to the MSMEs. Priority sector lending scheme with the advent of nationalization of banks is being revised periodically in order to diminish this credit gap. But the public sector banks are unable to reach the prescribed targets to priority sector due to various reasons. Credit constraints continued to prevail over the years. It has been reported that the constraints faced by the bankers with regard to deployment of credit to priority sector are lack of viable credit products, implying lack of demand for credit etc. If MSMEs are to improve, bank lending to MSMEs is to be improved. Hence, the need for examining various issues related to this gradually widening credit gap arises.

**Keywords:** MSMEs, Priority Sector Lending, Credit Gap

### Introduction

MSMEs occupy a position of strategic importance in the development of Indian economic structure since independence. India accorded high priority to MSMEs from the very beginning and pursued various support policies to make these enterprises viable and vibrant and over time these have become major contributors to the GDP. MSMEs are consistently playing crucial role in providing large employment opportunities at comparatively lower capital cost than large industries; MSMEs, in fact, are complementary to large industries as ancillary units (MSME Annual Report, 2016-17). Despite holding one of the major planks in India's economic development, MSMEs remained mostly small, technologically backward and lacking in competitiveness (Raju, 2008; Siddiqui, 2015). Availability of timely and adequate bank credit to MSME sector has been a matter of intense policy focus across countries. With the employment generation potential of the Micro, Small and Medium enterprises sector, the sector is getting a lot of attention to meet the 'inclusive growth' objective of the country. The concept of priority sector lending to the hitherto neglected sectors was introduced with the nationalization of banks. Small scale industries were brought under the purview of priority sector lending in order to

ensure maximum credit flow to such a promising sector. Recognizing the significance of adequate supply of bank credit for the upliftment of MSMEs and thereby the overall development of the economy, the present study has been conducted.

MSMEs in the North East region of India are facing huge challenges in order to contribute to the development of regional economy and national economy as well as to remain competitive in an increasingly globalized era. Keeping in mind the potential of MSME sector, it becomes all the more important to give special attention for growth of MSME sector in the region since they hold the promise of providing highest wage employment for the labour force next to agriculture and to provide goods and services at a lower cost (Munda & Swain 2014). Availability of ample and timely credit at reasonable rate of interest is vital for the development of these sectors. As is elsewhere in the world, the major problem Indian MSMEs face is unavailability of adequate amount of finance (Thampy, 2010; Salwan; 2012). There seems to be a gap between demand for and supply of the bank credit to the MSMEs.

Priority sector lending scheme with the advent of nationalization of banks is being revised periodically in order to diminish this credit gap. But the public sector banks are unable to reach the

prescribed targets to priority sector due to various reasons. Credit constraints continued to prevail over the years (Ahmed, 2009). It has been reported that the constraints faced by the bankers with regard to deployment of credit to priority sector are lack of viable credit products, implying lack of demand for credit etc (Shete, 2002).

If MSMEs are to improve, bank lending to MSMEs is to be improved. Hence, the need for examining various issues related to this gradually widening credit gap arises.

### Objectives

The study has been undertaken with the following objectives:

1. To analyze the imbalance between demand for finance and supply of finance to MSMEs.
2. To identify the problems of financial service providers in extending credit to MSMEs.

### Research Hypotheses

The hypothesis formulated for the study is:

**H<sub>0</sub>1:** There is no significant difference between the demand for finance and the supply of finance to MSMEs.

### Research Methodology

The present research has been carried out in the periphery of Jorhat district of Assam with a view to assess the scenario of credit availability to MSMEs

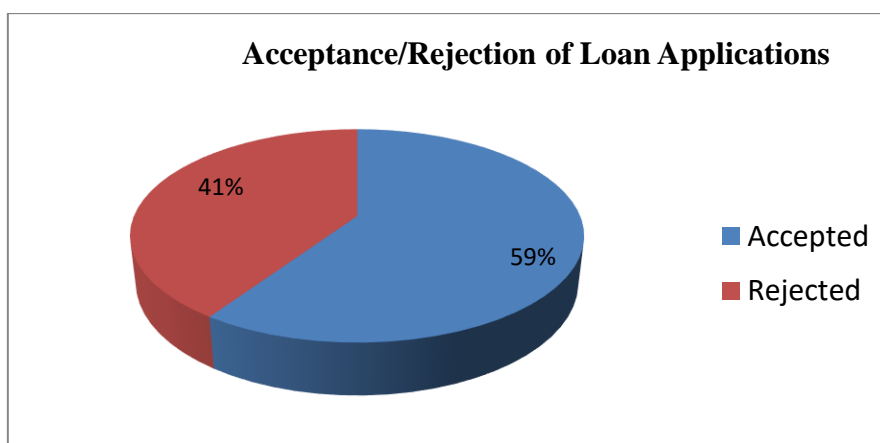
in the district. Having massive ability for development of new manufacturing and service enterprises as well as upliftment of existing enterprises in terms of infrastructural development, Jorhat is an encouraging industrial district of Assam.

The selected commercial bank for the present study is State Bank of India which has established itself as a pioneer in MSME financing. With wide array of products and services catering to the needs of MSMEs, SBI has established 15 branches in the study district. The concern of the present study is to analyze credit disbursements for the establishment, expansion, and modernization of micro, small and medium enterprises. Hence, the data was collected from RASMECCC (Retail Assets and Small and Medium Enterprises City Credit Centre), a specialized cell dealing exclusively in MSMEs loans. MSME applications for credit in all the other SBI branches are forwarded to this cell for loan disbursement.

### Findings & Discussion

For the purpose of our study, loan applications under priority sector lending are considered. Upon scrutiny it was found that, a total of 624 applications were submitted for grant of loan under priority sector lending during the study period 2019 to 2021. Out of which 370 applications were accepted for sanctioning loans. Figure 1 shows 370 loan applications were granted loan whereas 254 were rejected.

Figure 1 Chart showing number of accepted and rejected application (in percentage)



Source: Field Data

Also, it was found that bank loans to enterprises are not always granted in full against requirement. There exists gap between proposed amount and

actual loan granted. Table 1 shows the cross tabulation between amount of loan sanctioned and amount of loan proposed amount.

**Table 1 Proposed & Sanctioned Loan by RASMECCC, SBI**

(Figures indicate ₹ in lakhs)

Loan Sanctioned	Amount of Loan proposed						
	Up to 1.00	1.001 to 10	10.001 to 20	20.001 to 30	30.001 & above	Total	
Up to 1.00	Count	30	4	0	0	0	34
	% within Amount of Loan proposed	100.0%	1.5%	0.0%	0.0%	0.0%	9.2%
1.001 to 10	Count	0	260	5	0	1	266
	% within Amount of Loan proposed	0.0%	98.5%	9.6%	0.0%	9.1%	71.9%
10.001 to 20	Count	0	0	46	2	0	48
	% within Amount of Loan proposed	0.0%	0.0%	88.5%	15.4%	0.0%	13.0%
20.001 to 30	Count	0	0	1	10	4	15
	% within Amount of Loan proposed	0.0%	0.0%	1.9%	76.9%	36.4%	4.1%
30.001 & above	Count	0	0	0	1	6	7
	% within Amount of Loan proposed	0.0%	0.0%	0.0%	7.7%	54.5%	1.9%
Total	Count	30	264	52	13	11	370
	% within Amount of Loan proposed	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%

Source: Field Study

**Interpretation:** Table 1 exhibits the amount of loan sanctioned against the amount of loan proposed by the applicant. It is seen that a total of 34 applicants were granted loan up to ₹ 1 lakhs amongst which 4 applied for loan between ₹1 lakhs to ₹10 lakhs. A total of 266 applicants were granted loan between ₹1 lakhs to ₹10 lakhs amongst which 5 applicants proposed for loans between ₹10 lakhs to ₹20 lakhs and 1 applicant proposed for loan above ₹30 lakhs. A total of 48 applicants were granted loan between ₹10 lakhs to ₹20 lakhs amongst which 2 applied for loan amounting between ₹ 20 lakhs to ₹30 lakhs. Again, 15 applicants were granted loan between ₹20 lakhs to ₹30 lakhs amongst which 4 applied for loan above ₹30 lakhs and 1 applied for loan

between ₹10 lakhs to ₹20 lakhs. Out of 7 applicants who proposed for loan above ₹ 30 lakhs, one applicant was granted loan between ₹20 lakhs to ₹30 lakhs. Thus, we may interpret that the study bank does not disburse the same amount of loan which the applicant proposes.

#### Test of Hypothesis

The results of test of significance of the formulated hypothesis are as follows:

To test the null hypothesis, Mann-Whitney U Test is performed using software SPSS (version 25.0.0.0). The result of the test is given in Table 2.

Table 2 shows the summary of the Mann-Whitney U Test performed to test the null hypothesis. The Asymptotic significance is 0.000, which is less than

the significance level 0.05. Hence, the null hypothesis is rejected.

**Table 2 Test of Significance: Difference between Bank Credit to Manufacturing and Service sector MSMEs**

Null Hypothesis	Test	Asymptotic Significance	Decision
The distribution of loan sanctioned is the same across categories of Loan proposed	Independent-Samples Mann-Whitney U Test	0.000	Reject the null hypothesis

Source: SPSS Output Table, Version 25.0.0.0

### Problems In Extending Credit To MSMEs

The importance attached to development of priority sectors and thereby development of rural India had put significant pressure on banks. With the advent of nationalization the agenda of social banking enabled neglected sectors to become the priority sectors in availing credit not only in adequate quantity but even at the right time. Post nationalization, the performance of commercial banks regarding flow of credit to priority sectors has been commendable over the years in reaching the targets set by the Government. However, after analyzing the lending practice by the study bank it is observed that there are several deficiencies in the sphere of credit delivery to MSMEs. These deficiencies in turn reflect certain problems that undermine the extensive bank credit to MSMEs in the study area. Hence, it would be pertinent to identify the problems and constraints faced by the study bank in extending credit to MSMEs.

To elicit information regarding the problems faced by the bank officer in lending to MSMEs, the bank officer was interviewed. Bank officials are facing problems before sanctioning loans, at the time of sanctioning loans and also after sanctioning loans. The response of the bank official on the criteria under the three sections is presented given as under-

#### 1) Pre-sanction problems

While scrutinizing the loan applications for business purposes, the study bank is facing certain

problems in qualifying the application to be eligible for sanctioning advances. The problems before sanctioning loans are listed below:

#### a) Improper documents

Banks are directed to accept only Officially Valid Documents (OVD) for KYC (know your Customer) purpose. These include Passport, Driving License, PAN Card, Voter's identity card, Aadhaar Card, Job Card issued by NREGA duly signed by an officer of the state government. Applicants sometimes submit documents other than these which creates problem for the bank.

#### b) Illiterate applicants

Bank lending to illiterate applicants poses great risk of increase in NPAs. Therefore, extending credit to such applicants is a major hindrance in credit delivery.

#### c) Already financed

Financing MSMEs which are already financed by other financial institutions is a major problem because sometimes application of promising business venture is rejected due to this reason.

#### d) Negative credit story

Non repayment of previous loans by the beneficiaries restricts in sanctioning future loans to the same applicant.

#### e) Political Interference

Political pressure on bank for sanctioning a particular application is also a difficult situation for the sanctioning authority.

## 2) During Sanction before disbursement problems

After qualifying applications for priority sector lending there are certain issues which needs to address before disbursing the final amount. Constraints faced by bank in the process of disbursement are listed below:

### a) Visiting MSME site

In case of loans applied for the purpose of expansion of business venture, bank staff visits the MSME for inspection. During such inspection, the false information provided to the bank by the applicant puts trouble in disbursement of the final amount.

### b) Area outside jurisdiction of SBI

Sometimes while disbursement it is known that the firm appears to be outside the jurisdiction of SBI. Such situation imposes restriction on credit delivery.

### c) Delays on the end of the applicant

Delays in obtaining pollution certificate, industrial clearance, etc curtails disbursement of loans.

## 3) Post Sanction problems

The complication arising while follow-up action and supervision by the bank authority are discussed below:

### a) Misutilization of fund

Utilizing amount sanctioned to the beneficiary for personal use instead of starting business impose embarrassment for the bank officials.

### b) Launching non-sanctioned business venture

It is sometimes seen that the loan was sanctioned for a particular type of business but in reality the amount has been financed to another business. Such situation diminishes bank credit.

### c) Non repayment of loan

Non repayment of loans leads high NPAs of banks which in turn discourages priority sector credit.

## Conclusions

From the above discussion, it is evident that despite various arrangements made from end of

government and the study bank itself for extending priority sector credit to MSMEs; there are various issues which impose constraints in the process of credit disbursement. Such issues need to be addressed at length in the ground level.

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