



Institutional Financing for MSMEs in Odisha: Key Issues

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Abstract

The MSME sector is an important pillar of Indian economy as it contributes significantly to growth of Indian economy with a vast network of around 30 million units, creating employment of about 80 million, registering about 37 per cent share of the GDP, manufacturing more than 6000 products, contributing about 45% to manufacturing output and about 40% of exports directly and indirectly. Despite significant contribution, this sector has been suffering from many problems and most particularly the issues relating to financial aspects including lack of adequate institutional credit, high cost of debt capital, collateral requirement and poor access to equity fund. Keeping in view the problem of poor delivery of institutional finance to MSMEs, this paper is an attempt to identify the key issues in the flow of institutional financing to MSME sector with special emphasis on the role of Commercial Banks in the state of Odisha.

Key Words: Formal Financial Institutions (FFIs), Human Development Index (WDI), Priority Sector Lending.

Introduction

During more than four half and decades after nationalisation of banks in India, the Indian Credit delivery system has witnessed a revolutionary improvements in all its laps and bound. There has been much improvement in all major aspects of banking developments including the expansion of bank network in unbanked regions, mobilisation of deposits and credit deployment. Since then many favourable measures have been taken from time to time under the active guidance of the Reserve Bank of India in the form of targeted programmes and policy measures to bring the banking services to the reach of all segments of the people and more particularly the poor not having access to formal banking

services including the establishment of Regional Rural Banks(RRBs), lead Bank Scheme, Priority Sector Lending and financial inclusion among others. All these measures were intended to ensure easy flow of timely and adequate institutional credit to rural sector of the country including agriculture and allied activities, small-scale industries and poverty alleviation programmes. The emphasis was on spread of branch network and introduction of new instruments, credit packages and institutional benchmarks to make the banking sector responsive to the needs of the poor and vulnerable groups of the society living below the socio-economic pyramid.



There has been a considerable quantitative improvement with many-fold increase in the network of bank offices in the country. The number of bank offices of the Scheduled Commercial Banks which was 8262(out of which 1833 rural branches) in 1969 has registered a 15.21 times increase to 125672 (45175

rural offices) in 2015. Despite many fold increase in the number of bank offices, deposit mobilisation and credit expansion; there has been little impact of banking services in the socio-economic improvement of the economically marginalised rural poor.

Table- 1: Distribution of Bank offices according to population Group(as on March 2014)

Centre	Odisha	India
1	2	3
Rural	1744	36481
Semi-Urban	105	6383
Urban	8	387
Metro	-	34
Total	1857(100.000)	43285(100.00)

Note- Figures within the brackets indicate percentage to total. Source- *Basic Statistical Returns, Vol- 43, Summary Table, RBI.*

Keeping in view the problem in the delivery of credit to rural poor, a sincere attempt in this paper has been made to investigate the role of bank credit in the promotion of rural entrepreneurship with special reference to Jajpur district of Odisha.

Objectives of the Study:

This paper is based on the following objectives.

1. To study the growth and development of Commercial banks in India viz.-a-viz. Odisha.
2. To analyse the role of bank credit in promotion of rural entrepreneurship.
3. To investigate the problems of rural entrepreneurship.

Scope of the Study

The present study is a macro level study of growth and development of rural entrepreneurship and flow of bank credit to different sectors of rural economy and most particularly the small-scale industrial sector. The data are used to investigate the impact of bank credit in promotion of rural entrepreneurship and the problems involved in it.

The Rural Poor

Poverty and poor Human development continue to be big challenges in a civilised society. One of the significant socio-economic problems that the entire Globe is encountering is economic deprivation leading to poverty and hunger. The problem is more acute in south Asian nations. And India is not an exception to it. India officially houses more 350 million poor (about 30 per cent) living below poverty line.



So far as the causes of rural poor are concerned, these are more complex and multi-dimensional and involve among others the socio-economic factors, culture, climate, gender, market and public policy.

Table- 2 :Percentage of People below poverty line

Year	Reference Period	Odisha(%)			India(%)		
		Rural	Urban	Total	Rural	Urban	Total
1	2	3	4	5	6	7	8
Expert Committee Methodology							
1973-74	URP	67.28	55.62	66.18	56.44	49.01	54.88
1977-78	URP	72.38	50.92	70.07	53.07	45.24	51.32
1983	URP	67.53	49.15	65.29	45.65	40.79	44.48
1987-88	URP	57.64	41.53	55.58	39.09	38.20	38.36
1993-94	URP	49.72	41.64	48.56	37.27	32.36	35.97
2004-05	URP	46.80	44.30	46.40	28.30	25.70	27.50
Tendulkar Committee Methodology							
1993-94	MRP	63.00	34.50	59.10	50.10	30.80	45.30
2004-05	MRP	60.80	37.60	57.20	41.80	25.70	37.20
2009-10	MRP	39.20	25.90	37.00	33.80	20.90	29.80
2011-12	MRP	35.69	17.29	32.59	25.70	13.70	21.92

Note- URP_ Uniform Recall Period Method, MRP_ Mixed Recall Period Method. Source- Planning Commission, GOI, New Delhi.

Odisha no doubt has made significant improvement in poverty reduction between 2004-05 and 2011-12 with a substantial fall in rural poverty from 60.80 per cent in 2004-05 to 35.69 per cent in 2011-12. However, there has been high concentration of poverty in rural sector of the state with official poverty ratio of 35.69 per cent which is much high than the national figure of 25.70 per cent.

Again, Odisha has been performing poorly in all round Human Development. Table- 3 HDI of Odisha and India

The state has been performing poorly in improving the quality of life of the people of the state as reflected in the Human Development Index (HDI). HDI is an average of health index, education index and income index. In all counts, the performance of the state is very poor. Infant mortality rate of Odisha is estimated to be 51 in comparison to national average of 40 in 2013. Life expectancy of state is 71.6 years against national figure of 72.3.



	1981	1991	2001	2011
Odisha	0.267	0.345	0.404	0.442
India	0.302	0.381	0.472	0.504

Source- UNDP.

Why Rural Enterprises?

Poor people residing in villages, who make up the majority of India's population, are mainly dependent on agriculture. They get only 2 to 3 months work in a year, either in their own fields or to work as agricultural labourers. During the rest of the year they look for some other source of income. It was very difficult for them to meet their day to day expenses and they continued to remain in the vicious circle of poverty from where they could just dream of savings besides earning for their survival.

The poor require finance for both production and consumption purposes. Production loan may be of three types, viz. (a) short term (for periods up to 15 months), (b) medium term (from 15 months to 5 years) and (c) long term (for periods above five years). Economic activity in rural areas may relate to the various sectors of crop husbandry, animal husbandry, poultry, fishery, cottage & village industries, handicrafts, transportation, repair shops, and trade & services. But the recent strategy is to ensure flexibility in lending and in repayment based on the capacity of the borrower to earn enough to repay-whether it is daily, weekly, monthly or seasonal. Short term loans may be required by the poor for purchasing (HYV) seeds, fertilizer and for irrigating a leased-in land etc. Medium term loans may be required for purchase of bullocks (or a boat) and for purchase of machinery and equipment. Long term loans may be required for repayment of loans, for

constructing a shed/shop and for purchase of land etc. What needs to be appreciated is that all the three kinds of production loans are relevant to the poor.

About two-thirds of the estimated credit requirement of the poor is said to be on account of consumption needs. Nearly three-quarters of this consumption need (Rs.25, 000 crore) is stated to meet emergencies like illness and household expenses during the lean seasons. It is worth mentioning that due to lack of employment, and incomes during the lean seasons, the poor are often not in a position to buy subsidized food grains from the Targeted Public Distribution System (TPDS). If consumption loan could be made available through the formal banking sector, the poor will benefit not only by way of lower interest rate but also in terms of realizing the subsidy on food grains/items of TPDS. Alternatively, food grains credit could be provided directly under TPDS. It is important to note that consumption loans are also as relevant to the poor as production loans.

Availability of finance, moreover, tilts the employment scenario in favour of self-employment vis-à-vis wage employment. An added dimension is the empowerment of women with easier availability of micro-finance to them. Going by the estimates provided earlier, the demand for production credit in the country today is equal to Rs.17000 crore per annum whereas the total credit outstanding under micro-finance is merely Rs.5000 crore. Thus, there is definitely a need to



increase the flow of credit, both for consumption and production, to the rural sector.

Government's initiative to reduce poverty by improving access to financial services to poor started since independence. India's overwhelming majority of poor is located in rural areas and this motivated the government to give special attention to rural credit. Following the report of All India Rural Credit Survey in mid-1950's, the State took crucial steps in reviewing Cooperative structure including the partnership of State in cooperatives. Also the policy initiative of 'social banking' concept described as "the elevation of the entitlements of previously disadvantaged groups to formal credit even if this may entail a weakening of the conventional banking practices" led to the nationalisation of commercial banks in 1969, adoption of direct lending programmes to rural areas and development of credit institutions such as Regional Rural Banks (RRBs). Government initiatives during the Fourth Plan focused on marginal farmers and agricultural labourers bringing individual family as the basic borrowing unit. Integrated sustainable income generating activity was promoted through subsidized lending under Integrated Rural Development Programme (IRDP) and its subsequent variations including the current self-employment programme known as Swarnajayanti Gram Swarozgar Yojana (SGSY).

Credit to Small and Medium Enterprises (SMEs)

Credit to SMIs is an important segment of priority sector lending of the commercial banks. Micro, Small and Medium Enterprises (MSMEs) contribute

37.54 per cent of the total GDP of the country, 45 per cent the industrial output and 40 per cent of the export. Also, this sector is the second largest employer of the country next to agriculture providing employment to about 80 million persons in 30 million enterprises.

The Prime Minister's Task Force on MSMEs (2010) has identified 14 basic problems that these small enterprises are facing and out of which four belong to capital viz.

1. Lack of Capital
2. High Cost of Capital
3. Collateral requirements
4. Limited access to equity capital

Some facts about Credit to SMEs

- Out of the total 41.83 million establishments, 37.63 million (about 90 per cent) do not have any source of finance.
- According to the Fourth Census of MSME sector (September 2009), only 5.18 percent of the units had availed of finance through institutional sources while 2.05 percent of them had finance from non-institutional sources and the majority of units (92.77 percent) had no finance or depended on self-finance.
- Only 1.41 million (3.37 per cent) get credit from formal financial institutes (FFIs).
- 0.62 million (1.49 per cent) borrow fund from the moneylenders.
- 52 million people are employed in 25.5 million establishments in rural sector.
- Majority of the SMEs belong to unorganized sector.



- By the end of 2006-07, MSEs have contributed 39 per cent of nation's manufacturing output, 34 per cent of export and employment to 29 million people of the country.

Entrepreneurship Development in Odisha

Odisha is endowed with rich natural resources including precious mineral reserves including coal, bauxites, iron ore, manganese and forest reserves among others which led the state for the growth of mineral based large and medium –scale industries. The impacts of economic reforms in early 1990s in the country coupled with a series of favourable state Industrial Policies have made the state an industrial as well as services hub in the last decade and significantly contributing the gross state

domestic products. The manufacturing and mining sub sector's share is about 26 per cent of GSDP which was instrumental in maintain a higher annual GDP growth in the last decade despite a global slowdown.

So far as the MSME sector is concerned, this sector is not far behind the manufacturing and mineral based activities. MSME sector in the state are proved to be a key driver of economic growth with a sizable contribution to GDP, 2nd largest employer next to agriculture and proper use of man power and other resources and skill. As of 2015, 1.60 lakh numbers of MSME units are operating in the state with an investment of Rs.7906.25 crore with direct employment to a tune of 8.46 lakh persons

Table-4: District-wise Distribution of MSME Units, Capital Investments and Employment Generation in Odisha as of 2014-15

SL. No.	District	No. Of Units	Capita Investment (Rs. in Lakh)	Employment Generation(in no)
1	2	3	4	5
1.	Anugul	1011	68386.94	7447
2	Balasore	1602	5328.43	4879
3	Baragarh	877	10154.80	3496
4	Bhadrak	1160	8476.03	2398
5	Bolangir	1270	5976.75	5337
6	Boudh	201	583.38	684
7	Cuttack	2190	11434.93	10382
8	Deogarh	180	658.99	730
9	Dhenkanal	1062	4473.61	2439
10	Gajapati	291	1588.17	803



11	Ganjam	1854	8724.90	5694
12	Jagatsingpur	740	5428.65	2761
13	Jajpur	2008	10952.76	7179
14	Jharsuguda	621	4421.90	1867
15	Kalahandi	841	4825.78	3561
16	Kandhamal	136	394.64	360
17	Kendrapada	641	1920.14	1830
18	Keonjhar	901	6067.06	2652
19	Khurda	2187	10870.89	7176
20	Koraput	874	5563.22	3097
21	Malkangiri	160	436.67	722
22	Mayurbhanj	1375	3611.42	3963
23	Nabarangpur	428	2691.86	1658
24	Nayagarh	342	2211.81	883
25	Nuapada	220	1787.15	945
26	Puri	1270	4880.37	3961
27	Rayagada	978	6498.75	3196
28	Sambalpur	945	7228.77	2898
29	Subarnapur	272	699.66	934
30	Sundargarh	3229	20445.13	13079
	TOTAL	29866	226723.56	107011

Sources: District at a Glance-2016, Directorate of Economics and Statistics, Government of Odisha, Bhubaneswar.

By the end of 31st March 2015, 160167 number of MSME units have been set up in the state with a tune of investment of Rs.2267.24 crore and cumulative employment of 107011 persons. Table- 5 depicts MSME units in Odisha between 2004-05 and 2014-15.



Table- 5 MSME Units in Odisha

Year	MSME Units set up(cumulative)	SSI/MSME Units set up during the yr	Investment (Rs. In Crore)	Employment generated(persons)
1	2	3	4	5
2004-05	83075	4507	245.59	21898
2005-06	87861	4786	270.44	25142
2006-07	92417	4556	271.14	20839
2007-08	97127	4710	295.51	23301
2008-09	101933	4806	227.92	10996
2009-10	106840	4907	292.34	23195
2010-11	111856	5016	395.02	24451
2011-12	117361	5503	500.73	30387
2012-13	123292	5931	432.90	27104
2013-14	130301	7009	669.41	321.36
2014-15	160167	29866	2267.24	107011

Sources: Economic Survey of Odisha- 2015-16, Directorate of Economics and Statistics, Government of Odisha, Bhubaneswar.

Sector-wise distribution of MSME units in the state of Odisha is concerned, highest number of 70024 units have been set up in Repairing and services sector followed by 28551 units in food and allied sector by the end of 2014-15. A low of 478 units have set up in Livestock and leather sector. Sector-wise distribution of MSME units in Odisha by the end of 2014-15

Table-6 Sector-wise MSME Units in Odisha by the end of 2014-15

Category	No. of Units set up	Investment (Rs. In Crore)	Employment (persons)
1	2	3	4
Food & Allied	28551	1716.99	153415
Chemical & Allied	3131	270.31	24295
Electrical & Electronics	1287	78.86	7972
Engineering & Metal based	14559	1072.38	104301
Forest & Wood based	3574	119.40	49670
Glass & Ceramics	9516	685.10	145185
Livestock & Leather	478	8.33	2646
Paper & Paper products	3299	147.97	18073
Rubber & Plastic	1888	264.64	11818
Textiles	10584	240.58	58890
Misc. Manufacturing	8276	332.63	39276
Repairing & Services	70024	2969.06	229945
TOTAL	160167	7906.25	845489

Sources: Directorate of Industries, Odisha.



Financing MSMEs in Odisha

MSME financing is a key function of the financial institutions as part of their priority sector lending in Odisha and commercial banks are committed to extend all financial helps in promoting small industries in the state. By the end of 2014—15 a sum of Rs. 21455.04 crore has been advanced to MSMEs in the state by all scheduled commercial banks of which the share of commercial banks is Rs.21,762.85 crore and of the co-operative banks Rs.92.19 crore. Among the Public Sector Banks have shown their leadership in financing different sectors

of the economy of the state. The credit-deposit(C/D) ratio of public sector banks in the state by the end of 2014-15 is estimated to be 73.55, followed by private sector banks with C/D ratio of 62.97 and 59.34 in case of co-operative banks. Of the total credit of Commercial banks to MSMEs, the share of Public sector banks is estimated to be 80.77 per cent, followed by private sector banks with 11.48 per cent and 7.77 per cent in case of RRBs. Table-7 depicts the sector-wise key indicators of bank financing to MSMEs in Odisha by the end of 2014-15.

Table- 7 Bank-wise Key Indicators at the end of 2014-15

(Rs. in Crore)

Banks	Total Branches	Deposits	Advances	CD Ratio	Advance to Agri	Advance to MSMEs	Adv Services to
1	2	3	4	5	6	7	8
Public Sector	2889	153828.69	113136.04	73.55	9570.30	17254.10	12970.70
Private Sector	457	23285.98	14663.99	62.97	2146.28	2452.83	624.88
RRBs	983	11942.22	7086.71	59.34	3195.74	1655.92	847.04
Total Commercial Banks	4329	189056.89	134886.74	71.35	22566.03	21362.85	14442.62
Total Co-operative Banks	343	7175.05	8727.02	121.63	7390.73	92.19	734.49
Grand Total	4672	196231.53	143613.76	73.19	29956.76	21455.04	15177.11

Sources: 139th Issue, SLBC, Odisha, March 2015.

So far as flow of credit to different MSME units by commercial banks is concerned, all the commercial banks of the state have extended Rs.19774.25 crore to MSME units through 739814 numbers of accounts. Public sector banks of the state with 2754 offices by the end of September 30, 2014 have extended Rs.15874.08 crore through 393317 numbers of accounts. The private sector banks on the other hand have provided credit worth of Rs.2025.64 crore to MSME units followed by Rs.1874.54 crore by the Regional Rural Banks. Table-8 shows Bank- wise Credit flow to MSMEs as of 30.09.2014 in Odisha.



Table- 8 Bank- wise Credit flow to MSMEs as of 30.09.2014 (Odisha)

(Rs. in Crore)

Sl. No	Name of Bank	No. of Branches	Micro Enterprises		Small Enterprises		Medium Enterprises		Total MSMEs	
			A/C	Rs.	A/C	Rs.	A/C	Rs.	A/C	Rs.
1	2	3	4	5	6	7	8	9	10	11
1.	Public Sector Banks	2754	320773	7001.20	71347	6119.46	11197	2753.42	393317	15874.08
2.	Private Sector Banks	395	48089	528.22	8334	1956.37	437	441.05	56860	2025.64
3.	RRBs	957	203364	1133.03	86264	664.17	0	77.34	289637	1874.54
4.	Total CBs	4106	572226	8663.45	165945	7840.00	1643	3271.81	739814	19774.25

Sources: SLBC, U.CO Bank, Bhubaneswar.

Problems in MSME Financing in Odisha

Despite favourable industrial state of affairs like adequate inputs, power supply, favourable Government policies, abundant man power supply, stable Government, the MSMEs in the state do not exhibit required growth due to poor institutional funding and related issues. Some of the issues affecting the flow of institutional credit to MSMS sector are as follow;

1. Issue of Collaterals: The MSME units face the problem of either less or no collateral. A large proportion of the MSME loans are against Property(LAP) causing hindrance in the flow of institutional credit to this sector.
2. Lack of Government Supports: Despite being the second largest employer, huge potential for employment generation and

considerable contribution to GDP, MSME sector is lacking adequate support from Government and other development agencies.

3. Lengthy and Inflexible formalities: A big challenge that the MSMEs are facing is lack of flexibilities and unnecessary bank formalities in financing.
4. Apathy of Financial Institutions: The staff members of banks and other financial institutions lack interest in lending MSMEs and many cases cause unnecessary delay and huddles in financing.
5. Regional Disparity: There exists regional disparity in financing MSMEs by banks. Some of the industrially rich districts of Odisha get more bank credit than others.



6. Bank-sector-wise Disparity- Also, there exists disparity among the banks in financing small industries. The public sector banks outnumber their private sector and foreign banks in financing MSMEs.

7. Lack of Equity capital participation: MSMEs get mostly debt capital from the banks and other financial institutions. There is little scope for participation of equity capital for these small industries.

8. No access to Foreign instructional finance: Despite a series of economic and industrial policies measures to promote Globalisation and liberalisation, the access of MSME sector has little access to foreign capital.

9. Lack of Information: The MSME sector of the nation is mostly in unorganised sector, resulting poor information base. Many of the traditional entrepreneurs lack knowledge on developments in financial and other sector. It causes difficulty in smooth flow of institutional credit to MSME sector.

Suggestions:

1. The focus of the banks must be on flow of easy, timely and low cost credit to MSME units.

2. The banks are required to establish MSME financing units in identified clusters with dedicated staff members and proactive policy measures to support small entrepreneurs.

3. The private sector and foreign banks must increase their share in MSME financing at par with public sector banks.

4. Banks are required to provide more venture capital funds to new

generation industrial units with advanced technology and high degree of risk.

5. Financial institutions must follow cluster approach in financing MSMEs.

6. There must be proper co-ordination and data sharing between the banks, Government bodies and promotional agencies.

7. Besides, financing the banks should provide other promotional and supportive services to MSMEs including information, training and skill development, marketing of produce, leasing, project development and monitoring among others.

8. Banks must provide additional funds to sick units for revival and potential units for modernisation and up gradation.

9. There is urgent need to strengthen the credit delivery system of the financial institutions to improve the existing delivery mechanism and developing alternative sources of finance to MSMEs.

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