



A Study on Growth and Performance of Small and Medium Enterprises (SMEs) – A Study of Financing Strategies of Selected SME's

Vani.H

Research Scholar, Osmania University, Hyderabad

&

Dr.S.Vandana

Principal, Vidya dayini College of management Studies, Hyderabad.

&

Prof. Dr. R. Nageswara Rao

Professor and Director (Infrastructure), Osmania University, Hyderabad.

ABSTRACT:

Worldwide, the Micro, Small and Medium enterprises (MSMEs) play a leading role in propelling economic growth sustaining livelihood and in promoting equitable regional development. The MSMEs constitute over 90% of total enterprises in most of the developing economies and credited with generating the highest rate of employment growth and accounting for a major share of industrial production and exports. In India too, the MSMEs play a pivotal role in the overall industrial economy of the country. It is estimated that in terms of value, the sector accounts for about 39% of the Manufacturing output and around 33% of the total export of the country. Further, in recent years the MSME sector has consistently registered a higher growth rate compared to the overall industrial sector. (Shiralashetti, 2012).

This paper focuses on various financing strategies of selected SME's and overall growth and performance of SME's.

Key Words: SME's, FI, Financial Strategies.

INTRODUCTION:

Small and Medium Enterprises (SMEs) play a pivotal role in the development of the country. It has made significant contribution to industrial production, export and employment generation. In developing countries as well as developed countries they are important from the point of view of employment generations, which is very important in countries like India with huge backlog of unemployment in the urban sections of the economy. It has been observed that their composition depends upon the way the production is being organized in the economy. However in India Government deliberately planned the growth of SMEs to achieve certain economic and non-economic objectives. India has registered a consistent high economic growth (6-9%) over the last decade and was able to survive and sustain world recession triggered in 2008. For the sustainability of this kind of growth proper nurturing of SME sector is imperative.

SMEs are vital and of paramount importance in the development of any country especially developing country like India. Small and Medium Enterprises (SMEs) play a pivotal role and can be considered as a back bone of national economy (Peters and Waterman, 1982; Amini, 2004; Radam et al., 2008). SMEs in emerging markets rely on more labor-intensive production processes than large enterprises, boosting employment and leading to more equitable income distribution (Luetkenhorst, 2004). It is evident that nurturing the SMEs in any country would have fruitful results on the income generation and employment in an economy. The degrees to which the SMEs can flourish by overcoming obstacles are important for the expansion and upliftment of the economy. According to World Bank, SMEs account to 50 % of GDP and to quote EU, it highlights the role of SMEs as two-third of employment.



In India, SMEs has made significant contribution to the economy:

- Approximately 40% of the country's domestic production
- Almost 50% of India's total exports
- 45% of India's industrial employment
- 35-40% to the GDP and account for more than 90% of all industrial enterprises in India.

SMEs are able to make their presence felt mostly because of the simple structure of an they can respond quickly to changing economic conditions and meet local customers' needs, growing at times into large and powerful corporations or failing within a short time of the firm's inception. To manage, recognize, and mitigate the credit risks at the earlier stages can be beneficial for financial institutions in identifying possible defaults of the enterprise and reduce losses incurred by the financial institutions. Roopa Kundra, CEO Crisil, foresees Indian SMES as "SME will be a very big growth engine in India and adequate measures like proper rating assigned to them which will aid them to get access to bank loans".

Similar views are shared by Small and Medium Business Development K.J. Chamber of India (SMBDCI) which states that Indian SMEs also play a significant role for nation development through high contribution to Domestic Production, Significant Export Earnings, Low Investment Requirements, Operational Flexibility, Location Wise Mobility, Low Intensive Imports, Capacities to Develop Appropriate Indigenous Technology, Import Substitution, Contribution towards Defense Production, Technology – Oriented Industries, Competitiveness in Domestic and Export Markets and Generate new entrepreneurs by providing knowledge and training.

Rapid development and recent financial crisis in international financial markets lead regulatory bodies to establish some common supervisory standards for both financial institutions, providing credits to the firms, and non-financial companies, operating in a highly competitive environment, to accomplish the market discipline and effective global risk management all over the world. On this respect, Basel-II capital adequacy standards, was developed by the Basel Banking Committee on June 2004. The overarching goal for the Basel II Framework is to promote the adequate capitalization of banks and to encourage improvements in risk management, thereby strengthening the stability of the financial system. At the same time, they also forced the SMEs to establish a sound corporate structure for financing their operations, reporting the financial results and managing their risks so as to install a healthy relationship with their creditors.

SMEs in fact do have the potential and momentum to inculcate innovations, competition-both domestic and international, job creation and stability in an economy. From time to time Indian Government have realized the importance as well as the potential these SMEs can unfold and therefore has been quite proactive in protection and nurturing of these budding SMEs. (Zaidi, 2013)

FINANCING OPTIONS FOR SMEs:

There are many organizations that have been set by the central governments and state governments and banks to support the development of the small scale enterprises as shown below :-

Central government

1. Central Board for Micro, Small and Medium Enterprises.
2. Small Industries Development Organization.
3. National Small Industries Corporation Limited Etc.
4. National Institute for SMEs.
5. Entrepreneurship Development Institute of India.

State government

1. District Industries Centers.
2. State Financial Corporations.



OBJECTIVES:

The Objective of the study is three fold:

- 1) To analyze the financing strategies presently used by various SME's.
- 2) To analyze the Growth and Performance of Small & Medium Enterprises (SME's).
- 3) To analyze the problems of the small and medium scale industries and a way out in deciding in the best mix of financial strategies.

NEED OF THE STUDY:

To highlight the growth, performance and contribution of the small and medium scale industries in the development of the country and also the problems that small and medium scale industries are facing relating to project implementation, relating to production, marketing, and finance so that government can take important steps for small and medium scale industries.

METHODOLOGY:

Both primary and secondary data has been used. For primary data Questionnaires were used to collect data from SMEs. SMEs were randomly selected from various places like Balanagar, Jeedimetla, Cherlapally, District industry centre, MSME's etc. Simple correlation coefficient has been used as a statistical tool to show the dependency of SMEs on formal and informal sources of finance. For correlation coefficient used other statistical tools like standard deviation, covariance, and correlation, and sum. Sample Size taken for the study 50 Sme's randomly selected.

REIVIEW OF LITERATURE:

Berry , Edgard, and Henry (Jun 2010) in their work on small and medium enterprise dynamics in Indonesia, have mainly focused on the development of small and medium enterprises (SMEs) in Indonesia before and during crises and argued that SME productivity has risen substantially, at rates not far from those of larger firms. They also argued that rather than providing direct assistance to smaller firms, government should concentrate on creating a business environment conducive to small and medium business growth, and promoting provision of business development services by the private sector.

Bala (July 2003) in his research paper (Pattern of technological innovations in small enterprises: a comparative perspective of Bangalore (India) and Northeast England (UK) has mainly focused on the comparative perspective of the pattern of technology innovations carried out by small enterprises in the engineering industry in Bangalore of India and Northeast England of the UK. However, the two regions have similar features but the insufficient spread of previous inventions and innovations and some other factors explained the lesser extent of radical and incremental innovations of small enterprises in Bangalore relative to that of Northeast England.

Sikka (April 1999) in his research paper, Technological Innovations by SME's in India, while surveying the current Indian scene has mainly focused on the need for SME's to utilize the technical facilities available at the S&T infrastructure created in the country and vice-versa. He has also highlighted the entrepreneurship capabilities which are being developed by SME's in India for producing quality products as well as undertaking ancillarization and sub-contracting activities for the larger firms in India.

Raju (January 2008) in his work on Small and Medium Enterprises (SMEs) in India: Past, Present and Future, has focused on the growth and development of the Indian small scale sector from opening of the economy in 1991 and the present scenario of SMEs and the problems they face like lending, marketing, license raj issues in detail . He also has discussed micro, small, and medium enterprises Act, 2006 in his study.



The aim of **Pradhan (February 2010)** research paper on R&D Strategy of Small and Medium Enterprises in India Trends and Determinants, work was to contribute to the literature on Indian R&D by analyzing the trends and patterns of R&D investment by Indian manufacturing SMEs during the period 1991–2008 and exploring various factors that determine their R&D behavior. The results show that Indian SMEs have lowest incidence of doing in-house R&D and their R&D intensities have fallen in the last decade Bakker, Marie, Gregory, and Leora (May 2004) in their study on Financing Small and Medium-Size Enterprises with Factoring: Global Growth and its Potential in Eastern Europe) have explored the advantages of factoring over other types of lending for firms in developing economies, and discuss the informational, legal, tax, and regulatory barriers to its growth. They also examined the role of factoring in the eight Eastern European countries that became EU members on May 1, 2004 - The Czech Republic, Estonia, Hungary, Latvia, Lithuania, Poland, the Slovak Republic, and Slovenia, referred to as the EU 8.

Cull, Lance, Naomi, and Jean (July 2006) in their research paper on historical financing of small-and medium-size enterprises, mainly focused on the economies of the North Atlantic Core during the 19th and early 20th centuries and found that an impressive variety of local financial institutions emerged to supply the needs of SMEs wherever there was sufficient demand for their services and, in addition, by raising the return to savings for local households, they helped to mobilize significant new resources for economic development.

Young (March 1993) in their work on Policy Biases, Small Enterprises and Development, have mainly focused on the performance and contribution of the small scale industries in the development of country in terms of employment and productivity. They also have revealed that small firms are often more efficient in total resources use than the larger firms. Moreover, small enterprises are often productive in spite of policies that are biased against them, particularly agricultural, financial, and trade policies.

Hutchinson Patrick's (Oct, 2003) in his paper has shown that how much does growth determine SMEs' capital structure. Main focus was to examine the extent to which growth determines the capital structure of small and medium-sized enterprises (SMEs). This is done by considering some theories of capital structure in relation to SMEs and then testing the resulting ideas empirically. A key feature of the empirical studies reported in this paper is that they utilize the same database of SMEs. The data were analyzed using ordinary least squares regression. The results show that growth is not consistently a major determinant of SMEs' capital structure but is more important in some circumstances than others.

Pandey, Prasad , and Shivesh (December 2007) in their work on Routes of Survival of SSI in India and its Futurity - a study of pre and post reform period have compared the performance of SSI in pre and post liberalized period and focuses on policy changes which have opened new opportunities for this sector. Technology development and strengthening of financial infrastructure is needed to boost SSI and thus growth target can be achieved.

Tewari & Pandey (2010) in their research paper on Conservation Of Energy in Small Scale Industries in India have focused on the prominence of the small-scale sector in the Indian economy & the need to improve the energy and environment performance of units operating in the sector. It drew upon the results of a major program initiated by TERI (Tata Energy Research Institute) in 1995 in the small-scale sector with the support of SDC (Swiss Agency for Development and Cooperation). The program aims at finding solutions to the energy problems of the SSI through technology up gradation and human and institutional development in some small scale energy intensive sectors.

Jha and Agarwal (June 2010), authors in their work on A Case Study of the Marketing Problems of Small Scale Industries have examined the marketing problems of small scale industries working in the district of Varanasi. The study opines that the marketing problems has arisen mainly due to cut throat



competition from other industries, adoption of cost oriented pricing, lack of advertisement, non-branded products etc.

INFORMAL AND FORMAL SOURCES:

Informal sources of finance are mostly those which do not require written and formalized agreements as given below:-

Own Saving

Some avenues to gaining finance for a new business might include internal sources such as an owner's personal money. Where this is used in conjunction with external financial help, this can demonstrate that the owner has some confidence and commitment to the venture and might make it easier to gain money from others.

Family and Friends

To meet the financial requirements of a start-up through funding from family and friends might have the advantage of being interest free or carry a lower cost compared to that of a bank loan.

Credit from suppliers

It is possible that by taking longer to pay creditors that the company might be able to use such delays to fund its operations in part. Many business start-ups find it difficult to gain extended credit terms from suppliers who are naturally suspicious of their lack of trading history.

Formal sources of finance are those which require written and formal agreements. There are many organizations and banks for that like SIDBI, NABARD, regional banks, commercial banks, and cooperative banks. SIDBI, that is small industries development bank of India, it is a kind of refinancing institution which refinances the SMEs if they fail to pay back to the others which are instituted by RBI.

RESULTS AND FINDING:

There are few findings through a questionnaire filled by the respondent which are represented graphically.

TOOL USED FOR THE STUDY:

Question no 1: Has the company ever applied to borrow money from the bank? (YES/NO)

Question no 2: Has the company ever applied to borrow money from the bank, if 'NO' than why?

Question no 3: What was the highest amount your company ever borrowed from a bank?

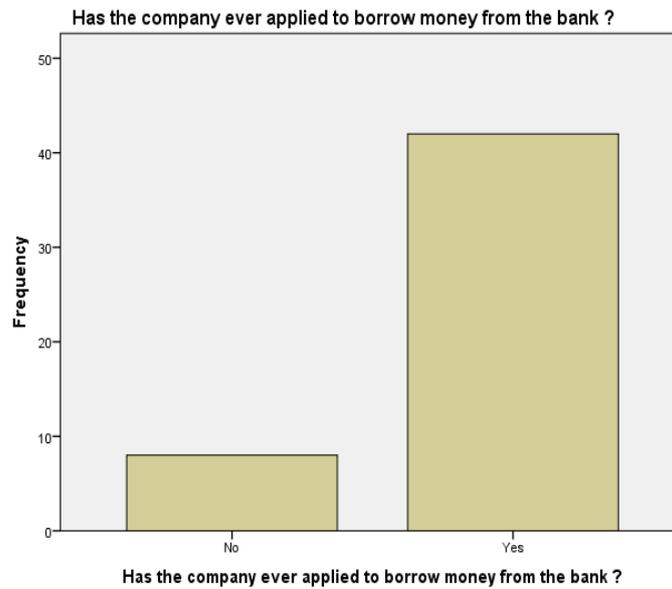
Question no 4: Have you ever had problem repaying a bank loan? (YES/NO)

Question no 5: How many employees you had in last 7 years?

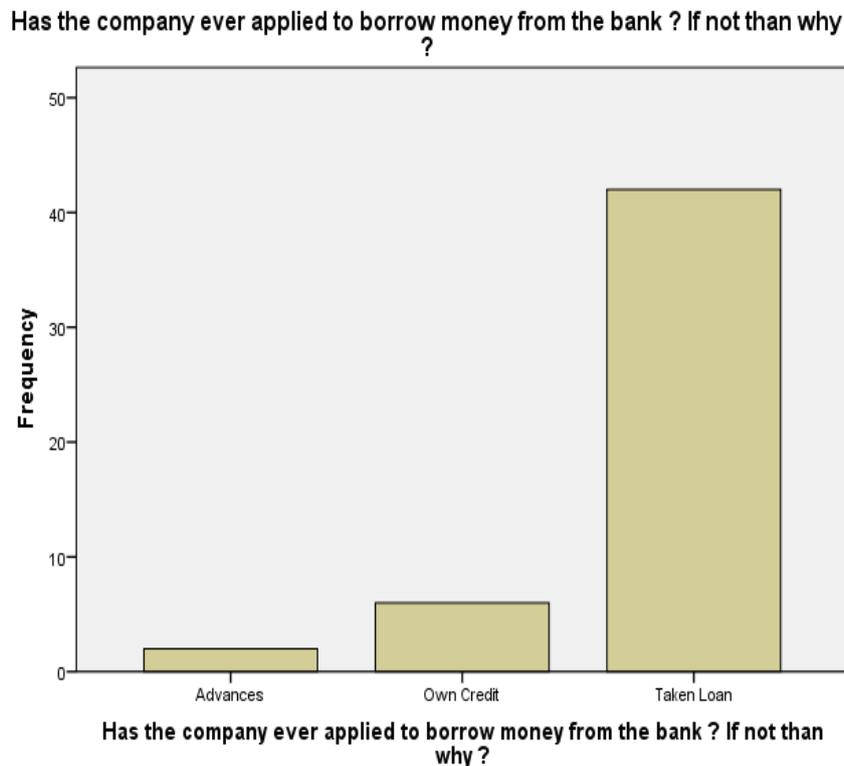
Question no 6: How many employees you have today?



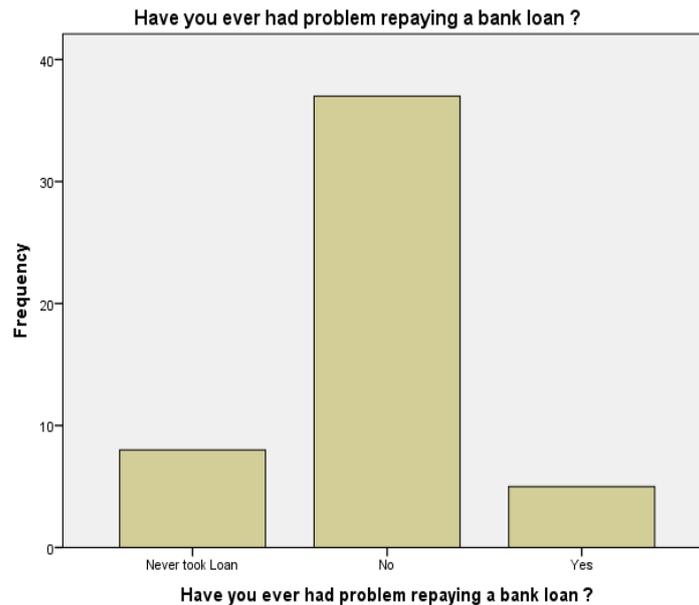
GRAPHICAL REPRESENTATION:



- From the sample taken for study the above graph depicts that 84% of SME sector have applied for finance through Formal source i.e.; approaching bank rather than Informal sources
- The rest 16% of SME sector of selected sample had not applied for the loans
- It concludes that the majority of SME's approach Formal source of financing for their Growth and Production



- From the sample taken for study the above graph depicts that 84% of SME sector have applied for finance through Formal source i.e.; approaching bank rather than Informal sources
- The rest 16% of SME sector of selected sample had not applied for the loans
- Of them 12% of the SME sector had their own credit and 4% have taken advances
- It concludes that the majority of SME's approach Formal source of financing for their Expansion and Production



- From the sample taken for study the above graph depicts that 74% of SME sector have no problem in repaying the bank loan
- 10% of SME sector of selected sample had problem in repaying the loan amount
- 16% of the SME sector had their own credit and taken advances
- It concludes that the minority of SME's have problem in repaying the bank loan

DATA ANALYSIS:

Performance of SMEs Units, Employment, Investments, Production and Exports

Sl. no	Year	Total working SMEs	Employment	Fixed Investment	Production (current prices)	Exports
		(Lakh numbers)	(Lakh Persons)	(Rs in crores)		
1	2001 - 2002	105.21	249.33	154349	282270	71244
2	2002 - 2003	109.49	260.21	162317	314850	86013
3	2003 - 2004	113.95	271.42	170219	364547	97644
4	2004 - 2005	118.59	282.57	178699	429796	124417
5	2005 - 2006	123.42	294.91	188113	497842	156242
6	2006 - 2007	361.76	805.23	868543.79	1351383.45	369694
7	2007 - 2008	377.37	842.23	917437.49	1435179.26	419799
8	2008 - 2009	393.7	881.14	971407.49	1524234.83	487596
9	2009 - 2010	410.82	922.19	1029331.46	1619355.53	569839
10	2010 - 2011	428.77	965.69	1094893.42	1721553.42	602467
11	2011 -	447.73	1012.59	1176939.36	1834332.05	693481

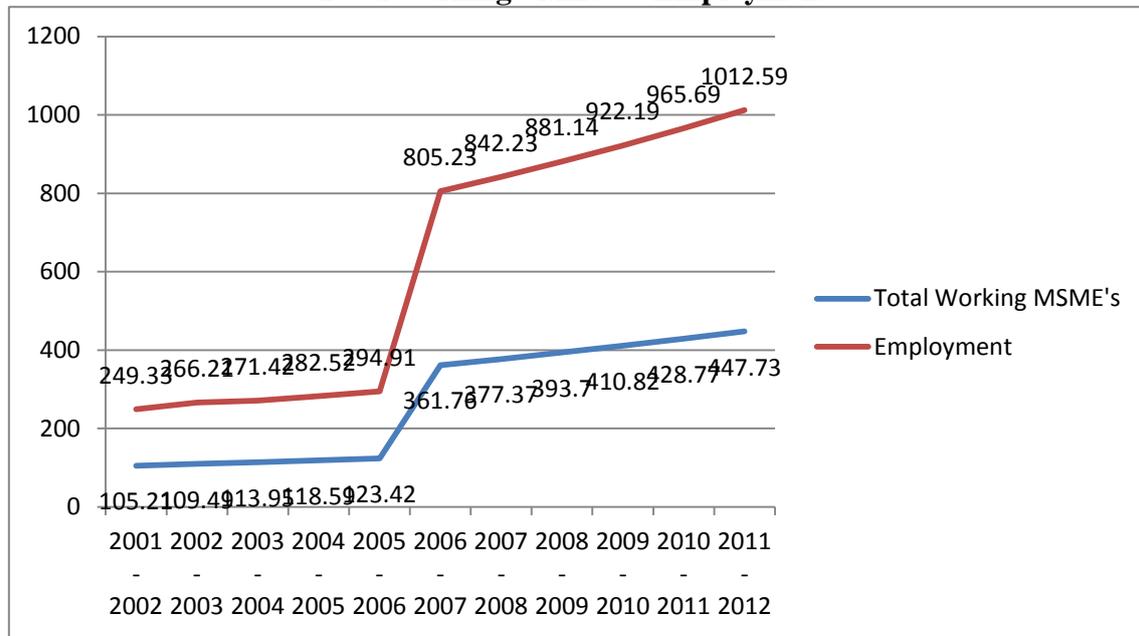


2012

CONTRIBUTION IN THE GROSS DOMESTIC PRODUCT (GDP)

Year	Contribution of SMEs(%) at Prices in	
	Total Industrial production	Gross domestic Production(GDP)
2001 – 2002	39.12	5.77
2002 – 2003	38.89	5.91
2003 – 2004	38.74	5.79
2004 – 2005	38.62	5.84
2005 – 2006	38.56	5.83
2006 – 2007	45.62	7.2
2007 – 2008	45.24	8
2008 – 2009	44.86	8.72
2009 – 2010	46.22	7.96
2010 – 2011	47.51	7.6
2011 – 2012	48	8

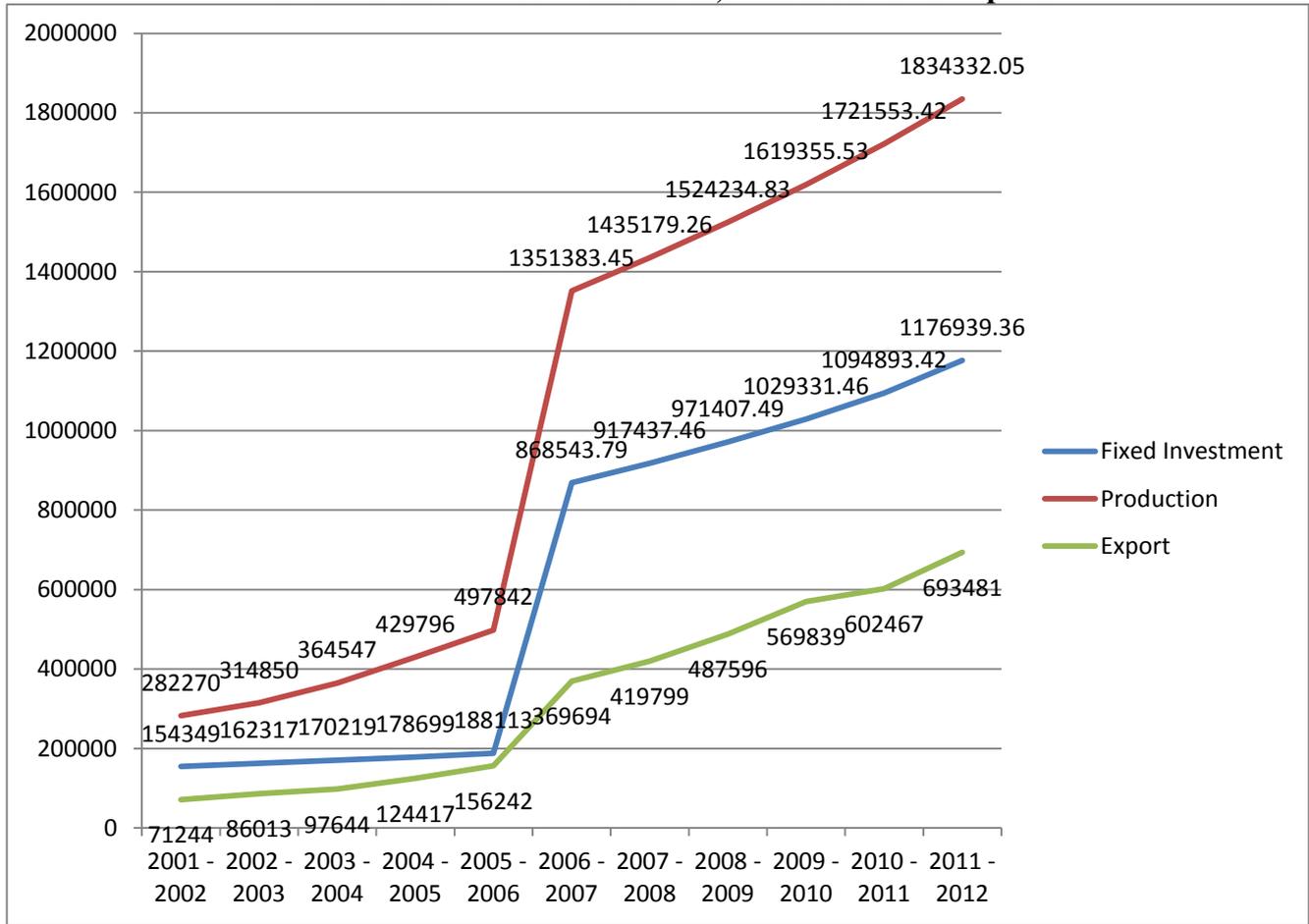
Total working SMEs Vs Employment:



- From the Performance of SMEs in Units and Employment, the above graph depicts that there is a sudden increase in the Total working SMEs in turn increasing the Employment.

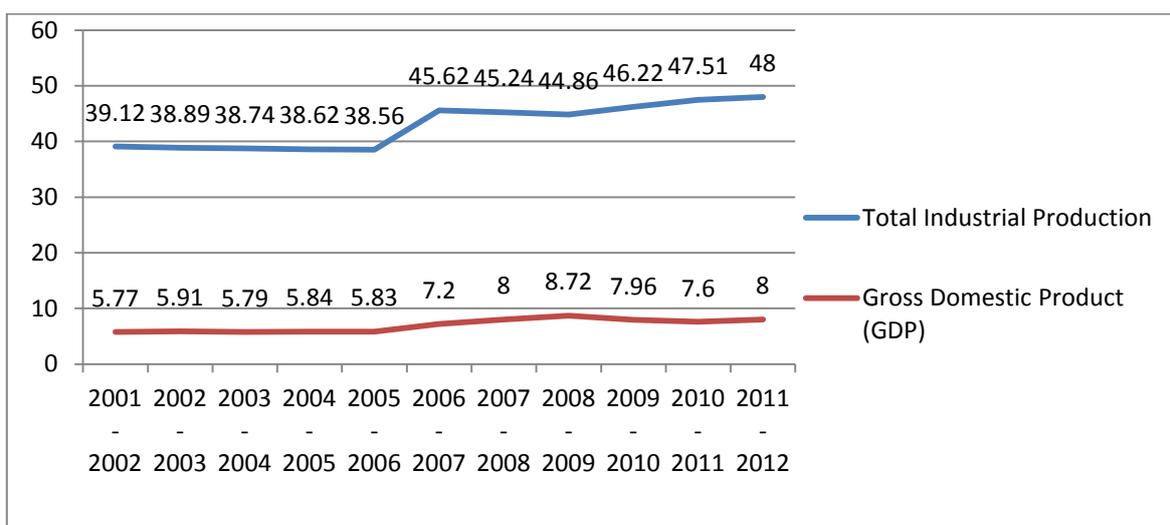


Performance of Fixed investments, Production and Exports



- From the Performance of SMEs in Fixed investments, Production and Exports, the above graph depicts that there is a sudden increase in the fixed investments of SMEs in turn increasing the Production and Exports.

Performance of Total Industrial Production and Gross Domestic Product (GDP)



- From the Performance of Total Industrial Production of SMEs and Gross Domestic Production, the above graph depicts due to the increase in the Total Industrial Production of SMEs there is an increase in Gross Domestic Production (GDP)



FINDINGS

- It is found that there are various financing options for SMEs but access to these funds has been difficult in spite of government initiatives
- Most of the SMEs which are taken in our survey raise funds from the informal source. As it is flexible and no need to pay monthly installments.
- It is also found that most of the SMEs raise funds from both by keeping a certain percentage

SOME LIMITATIONS OF INFORMAL SOURCE:

In case if person requests that the money is repaid at short notice and this in turn causes working capital shortages for the business.

SUGGESTION:

While not every SME turns into a big multinational, but they all face the same problem in their early as well as subsequent days – finding the finance to enable them to start and build up their business and test their products or services. In majority, while the financing for SMEs was being provided by informal sources, financial institutions, commercial banks extended working capital. Besides the traditional needs of finance, the changing environment has generated demand for introduction of new financial services for SMEs. SMEs should consider all financing options that maximize the value of the business enterprise.

CONCLUSIONS:

The Growth and Performance of Small & Medium Enterprises (SMEs) has been increased in factors like SMEs Units, Employment, Fixed investments, Production and Exports. There is also an increase in Total Industrial Production which in turn increases the Gross Domestic Production (GDP) of SMEs. The financing strategies of selected SMEs are presently based on Formal and Informal Sources. The problems which SMEs mostly face these days are relating to project implementation, finance, production, marketing, and management, etc.

REFERENCES:

- David Deakins, (. E. (1998, June 8). Emerald. Retrieved June 8, 2013, from Emerald: <http://www.emeraldinsight.com/journals.htm?articleid=882552&show=abstract>
- David Smallbone, (. f. (1995, June 8). Emerald. Retrieved June 8, 2013, from Emerald: <http://www.emeraldinsight.com/journals.htm?articleid=872004&show=abstract>
- Dr.K.D.Raju. (2008, January 5). Papers.ssrn. Retrieved June 8, 2013, from Papers.ssrn: http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1080505.
- Duhan, Levy, & Powell. (2001, June 8). Ingenta connect. Retrieved June 8, 2013, from Ingenta connect: <http://www.ingentaconnect.com/content/pal/0960085x/2001/00000010/00000001/3000379>
- Kapoor, A. (2012, December 4). SSRN. Retrieved June 8, 2013, from SSRN: http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2116978
- M.H. Bala Subrahmanya, (. o. (2007, June 8). Emerald. Retrieved June 8, 2013, from Emerald: <http://www.emeraldinsight.com/journals.htm?articleid=1626517&show=abstract>
- Mel Hudson, (. f. (2001, June 8). Emerald. Retrieved June 8, 2013, from Emerald: <http://www.emeraldinsight.com/journals.htm?articleid=849357&show=abstract>
- MSME. (2013, June 8). MSME Hyd. Retrieved June 8, 2013, from MSME: <http://msmehyd.ap.nic.in/About%20Us%20-%20MSME-DI%20Hyderabad.htm>
- Murthy, H. N. (2012, April 14). Indian Faculty. Retrieved June 8, 2013, from Indian Faculty: http://www.indianfaculty.com/Faculty_Articles/FA11/fa11.html
- Rajesh K. Singh, (. E. (2008, June 8). Emerald. Retrieved June 8, 2013, from Emerald: <http://www.emeraldinsight.com/journals.htm?articleid=1742532&show=abstract>



- Rajesh K. Singh, (. E. (2010, June 8). Emerald. Retrieved June 8, 2013, from Emerald: <http://www.emeraldinsight.com/journals.htm?articleid=1827992&show=abstract&>
- Roy Rothwell, W. Z. (2009, June 8). Social Science Research Network. Retrieved June 8, 2013, from Social Science Research Network: http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1496714
- Shiralashetti, A. S. (2012, July 2). SSIJMAR. Retrieved June 8, 2013, from SSIJMAR: <http://ssijmar.in/Vol.%201%20No.%202%20PDF%20for%20Website/A.%20S.%20Shiralashetti.pdf>
- Srinivasan, V. (2010, May 13). African Journal of Business Ethics. Retrieved June 8, 2013, from African Journal of Business Ethics: [www.ajobe.org/article.asp?issn=1817-7417;year=2009;volume=4;issue=2;spage=32;epage=36;aulast=Srinivasan#Definition of SMEs](http://www.ajobe.org/article.asp?issn=1817-7417;year=2009;volume=4;issue=2;spage=32;epage=36;aulast=Srinivasan#Definition%20of%20SMEs)
- Zaidi, L. (2013, March 20). International Conference on Technology and Business Management. Retrieved July 8, 2013, from International Conference on Technology and Business Management: <http://www.icmis.net/ictbm/ictbm13/proceedings/pdf/D3116-done.pdf>
- Bakker Marie-Renee, Klapper Leora , and Udell Gregory F., (2004). "Financing small and medium-size enterprises with factoring: global growth and its potential in Eastern Europe", Policy Research Working Paper Series 3342, The World Bank
- Berry Albert, Edgard Rodriguez, and Henry Sandee. (2001). 'Small and Medium Enterprise Dynamics in Indonesia', Bulletin of Indonesian Economic Studies, 37(3):363-84
- Cull, Robert and Davis, Lance E. & Lamoreaux, Naomi R. & Rosenthal, Jean-Laurent, 2006. "Historical financing of small- and medium-size enterprises," Journal of Banking & Finance, Elsevier, vol. 30(11), pages 3017-3042, November
- Hutchinson, P. (2003). "How Much Does Growth Determine SMEs' Capital Structure?", paper presented at the 16th Annual Conference of Small Enterprise Association of Australia and New Zealand.
- Jha N.S. and Agarwal K.N. (June 2010). "A Case Study of the Marketing Problems of Small Scale Industries", Management Convergence, Vol. 1, No 1 (2010)
- Pandey, Prasad Adya & Shivesh (December 2007). "Routes of Survival of SSI in India and its Futurity", MPRA Paper No. 965
- Pradhan, J. P. (2002), 'R&D strategy of small and medium enterprises in India: Trends and determinants', MPRA Paper No. 20951
- Raju, K. D (2008). "Small and Medium Enterprises (SMEs) in India: Past, Present and Future," Working Paper for PHD Chamber of Commerce and Industry, New Delhi available at < http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1080505>
- Sikka, P. (1999). "Technological Innovations by SME's in India", Technovation 19 (1999), pp. 317-321
- Subrahmanya, Bala MH (2005), Technovation, 25 (3), pp. 269-280
- Young, Robert C. (1993). Policy Biases, Small Enterprises and Development, "Small Enterprise Development", Volume 4, Number 1, March 1993, pp. 4-15 (12)
- http://www.dcmsme.gov.in/publications/msmed_actx.html
- <http://www.dcmsme.gov.in/publications/PoliciesSchemesProgramme.html>
- http://www.legalpundits.com/Content_folder/SMEArti150610.pdf
- <http://www.driems.ac.in/mba/Download/10%20INNOVATIONS%20AND%20CHALLENGE%20IN%20MSME%20SECTOR.pdf>
- <http://msme.gov.in/>
- http://www.dcmsme.gov.in/ssiindia/defination_msme.htm
- http://www.dcmsme.gov.in/ssiindia/MSME_OVERVIEW09.pdf
- <http://www.rbi.org.in/scripts/FAQView.aspx?Id=84>