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Chapter I

Introduction

1.1 Introduction

India has made an attempt in the second five year plan to transform Indian economy into an Industrial economy. No doubt, Agriculture is the backbone of Indian economy, yet Indian agriculture is gambling with monsoon. Time and again government is making herculean efforts to derive some output from Industry to its Gross Domestic Product (GDP).

In the recent past, Indian economy witnessed nearly 8 percent of the country’s GDP, 45 percent of the manufacturing output and 40 percent of the exports from the Small Scale Industrial sector. Though second five year plan was termed as Industrial Plan the results of the plan was not up to the expectations of the government. It was the beginning of the beginning for visionary industrial scenario of the country. This Philip to industrial sector gave an impetus to the rise of many Small Scale Industries throughout the country. Time and again the government is marching ahead of expectation to derive maximum benefit from this sector in the form of output, employment generation and self-sustainability, keeping this vision in mind the economy of the country stepping forward to have robust growth of industry.

As mentioned earlier, Small Scale Industries (SSIs) are contributing their mite to the expected norms. Though there are many advantages for SSIs, their disadvantages are outnumbering the advantages. They face some common problems, such as, lack of availability of adequate and timely credit; High cost of credit; Collateral requirements; Limited access to equity capital; Problems in accessing government departments and agencies; Procurement of raw materials at a competitive cost; Problems of storage, designing, packaging and product display; Lack of access to global markets; Inadequate infrastructure facilities, including power, water, roads, etc.; Low technology levels and lack of access to modern technology; Lack of skilled manpower for manufacturing, servicing, and marketing, etc.; Multiplicity of labour laws and complicated procedures associated with
compliance of such laws; Absence of a suitable mechanism which enables the quick revival of viable sick enterprises and allows unviable entities to close down speedily; and Issues relating to taxation, both direct and indirect, and procedures thereof. Among these said problems lack of adequate and timely credit, high cost of credit, collateral requirements and limited access to equity capital are the major problems for Small Scale Industries.  

Especially, the financial requirement, which is considered to be the vital component of investment and churning process of business, mobilization of such required finance for the starting and management of the same has become mirage for Indian business organizations. Since, Small Scale Industries are facing financial problems at every successive stage of their firm’s development, government of India and State Governments have been established many national and state level financial institutions respectively to infuse finance to Small Scale Industrial Sector. Such institutions are, Small Industries Development Bank of India (SIDBI), National Small Industries Corporation (NSIC), Khadi and Village Industries Commission (KVIC), Export and Import Bank (EXIM Bank), National Bank for Agricultural and Rural Development (NABARD) and Small and Medium Enterprises Exchange (SME Exchange) at national level and State Finance Corporations (SFCs) at state level.

Financial institutions have been established to infuse financial resources to the Small Scale Industrial Sector. But, as per the Fourth all India census of Micro Small and Medium Enterprises (MSMEs) it is evidenced that, out of 15,52,492 registered Small Scale Industries only 1,74,034 (11.21 percent) SSIs have availed loan from Financial Institutions, majority (87.77 percent) of the SSIs have financed their ventures with informal sources of finance. Remaining 1.02 percent of the SSIs are availed finance from Non-Banking Financial Institutions. Perhaps, it seems financing institutions are miserably failed to infuse the finance to Small Scale Industrial Sector.

The reasons behind abstaining from availing finance from financing institutions by the small scale industries entrepreneurs are unknown and at the mean while the factors which made them to relay on informal sources of finance are also unknown.

1 Report of Prime Minister Task Force on MSMEs 2010.
To dig out the attitude and perceptions of the entrepreneurs about institutional financing researcher has made an attempt to study the perception of Small Scale Industries entrepreneurs towards the institutional finance for Small Scale Industries.

**Concept of Institutional Finance:**

The term *Institutional finance* is understood in many ways. In a narrow sense, it refers to injection of funds by financial institutions to new and existing enterprises which are lacking finance.

Institutional finance for small scale industries refers to the injection of funds by the national and state level financing institutions to the needy small scale industries at every successive stage of the firm’s development, Such as, *Start-up stage, Modernization stage, Up-gradation stage and Expansion stage.*

**Definitions of Institutional Finance:**

Ledgerwood, J defines Institutional Financing as “providing financial services by a variety of financial intermediaries that are part of the financial system”.

The European Central Bank describes, “It is an act of resident financial institutions to accept the deposits and channelizing the deposits as finance into the industrial sector”.

International Finance Corporation (IFC) defines Institutional Finance as “financing to the entities as equity, loans, and mezzanine finance through formal financial intermediaries”.

In Business Dictionary the term Institutional Finance is defines as “Loan or equity capital provided by a financial institution(s), instead of by one or more individuals”.

A plausible definition of Institutional Financing would be “Facilitating finance to the new and existing Small Scale Industries to reap the capital and credit needs of the small scale Industries at every successive stage of firm’s development through financial Institutions”.

3
Determinants of Small Scale Industries Access to Institutional Finance

Finance is the life blood of business. It is an integral part of every business entity. Every second minute every business affirms availability of financial resources to keep the business operations intact. Perhaps, proper access to financial resources ensures harmony in firms operations.

Financial resources play a vital role in operational efficiency, irrespective of the age, size, nature of activity, type of ownership and location of the business entity. SSIs access to formal sources of finance is determined by institutional (lenders) level and firm level factors such as, Documentation, Collateral security, Restricted quantum of loan, Business information disclosure, Interest rate, Accruing cost, Business plan, Timeliness of loan sanction and Location of the firm, Size, Age, Ownership type, Type of industry, Business information disclosure, Education level of owners, Experience level of owners and Collateral security respectively.

Firms finance their operations and growth in a variety of ways, to some extent it depends on the preferences of entrepreneurs but also on what is available to them. Hence, every entrepreneur has to finance his business in a unique way. Perhaps, firm level and institutional level factors play an important and strategic role in SSIs accessibility to institutional sources of finance to obtain required finance at each phase of entity’s development.

Access to Finance: An overview

Access to finance is one of the several factors influencing the performance of the small scale industries. It plays a vital role in achieving its intended objectives. Access to finance is a pre-requisite and fundamental for every business entity, it is a difficult task comprising capabilities of small scale industries such as, managerial experience, collateral security, debt servicing ability, accountability and transparency in maintaining books of accounts. It is therefore essential to have strong commitment by the small scale industries to maintain good entrepreneurial and enterprise track record in their functional performance. Further, access to finance results in influencing on other business activities for the achievement of desired objectives. Access to finance enables an enterprise to maintain harmony in
business activities at every phase of firm’s development. It should concern primarily with the firm’s characteristics and capability. However, firm’s age, size, type of ownership, type of business, business planning, firm’s innovativeness, profitability, tangible assets, turnover, liquidity, on one side and on the other side institutional level factors such as, lending norms, lines of credit, risk taking ability, cost of funds, collateral requirement, margin on average loan, efficiency of sanctioning authority constitute major role in SSIs accessibility to institutional finance. It’s therefore the study considers the entrepreneurs perception on accessibility of institutional finance.

**Determinants of Access to Formal (Institutional) Sources of Finance:**

Financial accessibility is a complex act. The level of financial accessibility is determined by various firm and institutional level factors. The following are the major determinants of access to institutional finance by the small scale industries. Basically these determinants can be classified as firm level and institutional level factors as shown below.

**Figure No.1.1**

**Figure Showing Firm Level and Institutional Level Determinants of SSIs Access to Institutional Finance**

**Institutional level determinants**
- Documentation
- Collateral security
- Restricted quantum of loan
- Business information disclosure
- Interest rate
- Accruing cost
- Business plan
- Timeliness of loan sanction

**Firm level determinants**
- Location of the firm
- Size
- Age
- Ownership type
- Type of industry
- Business information disclosure
- Education of owners
- Experience of owners
- Collateral security
i. Firm level determinants

In spite of the statistical difficulties in defining SSIs and defining business failure in different countries, there is general agreement that lack on access to debt financing cause difficulties for businesses’ development. Pretorius and Shaw (2004)\(^2\) observed that accessibility to external finance is essential to solve shortage of SSIs cash flows. Financing is required for SSIs’ to set up and enlarge their business operations, human resource development, new product development, research and development and acquirement of up-to-date production equipments and technology. Most of SSIs rely on informal sources of finance since they can’t afford external finance easily only prioritized source become informal sources of finance but still informal sources of finance is inadequate for SSIs’ development and profitability. Failures of SSIs to access debt financing result into an inadequate capital structure. Shane (2008)\(^3\) pointed out that external equity from stock exchange (capital markets) usually never exists for SSIs. Majed et al., (2010)\(^4\) pointed out that firm characteristics have an impact on access to debt financing, capital structure and performance of SSIs. In this study researcher has considered, firm characteristics such as firms’ location, type of industry, firms’ size, firms’ age, firms’ legal status, Education level of owners, Experience level of owners, the availability of both collateral and business information.

Location:

Location of the firm determines the firms requirement of finance and availability of the same where in which the venture locates, if the firm is in urban area they may probably access financial institutions and on the other hand if the firm is located at the rural area they are less in accessing institutional finance since, majority of the financial institutions are located in urban areas than rural areas. Therefore, location of the business is also a factor which determines the small scale industries accessibility to institutional finance.


\(^3\) Shane, S., 2008. The importance of angel investing in financing the growth of entrepreneurial ventures. (January 24, 2012).

Size

Firm size can also influence access to finance by SSIs. First, the informational asymmetry between insiders and outsiders can be more severe. Therefore, smaller firms seek proportionately less debt. Second, profitability positively relates to firm size. If this is the case, size can be negatively associated with debt. In addition, given there is a positive relationship between size and age, start-up or early stage SSIs are more likely to seek equity. Therefore, size of the business is also a determinant of small scale industries access to institutional finance.

Age

Firm’s age largely corresponds to the business cycle of SSIs. Start-up and early-stage SSIs may then resort to external equity, particularly private investors and business angels. One reason is the restrictions in informal sources of equity. At the starting stage of a SSI, retained profits are scarce, and the personal sources of the owner and firm-connections are very limited. A second reason is associated with a combination of information asymmetries and potential agency problems related to the lack of a trading history. The lack of collateralisable assets can aggravate the problem of restricted access to finance. From this perspective, firm age positively relates to institutional finance seeking. However, as SSIs move from the start-up or early-stage to the middle-stage, they can source more finance from retained profits. SSIs can then replace external equity with informal sources of equity. Consequently, firm age should negatively relate to external equity.

Ownership

Ownership type can also influence access to finance by SSIs. The finance mobilization pattern and preference differ between proprietary concerns, partnership firms, private Ltd. companies and other forms of business. Firstly, family controlled and sole proprietary SSIs entrepreneurs are not willing to share the control, partnership firms are not go for external finance since they are partners they arrange finance within the firm by hand to hand lending and private limited companies financing pattern is also differs based on the entrepreneur’s preference. Though, the proprietary concerns constitute greater part of SSI sector in numbers their
accessibility to institutional sources is very less, compare to other forms of business. Therefore, type of ownership is also a factor which determines the small scale industries accessibility to institutional finance.

**Type of Industry**

Industry type display diverse debt levels. The manufacturing industry is capital intensive and requires large investments in fixed assets derived from both debt and equity while the retail sector needs relatively less short-term debt. Firms in the service industry are less likely to use family loans, and family businesses in the manufacturing industry are less likely to use capital and retained profits. However, for the most part firm-specific characteristics are more important than industrial effects in the firm’s financing decisions.

**Financial Statement**

A financial statement (or financial report) is a formal record of the financial activities of a business, person, or other entity. It reveals relevant financial information to the users. Many investment decisions are based on the financial position of the entity. Since, financial statements are the mirror of financial position of the firm. So that, it plays significant role in determining accessibility to finance from institutional sources.

**Education level of Owners**

Management level or key personnel educational qualification also a key factor, which is considered by the lenders, person with the higher qualification deserves much debt than the person who is less educated; this is the notion of the lenders. So that, education level of owners level is also an important factor which determines the accessibility of finance from the institutional sources.

**Experience Level of Owners**

Management experience is also one of the important factors. It has been considered by the lenders, person with the higher expertise deserves much debt than the person who is not having much expertise in the field of business; So that, owners experience is also an important factor which determines the accessibility of finance from the institutional sources.
Collateral

An entity with the collateral security will certainly have the accessibility to the institutional finance, on the other side the entity with less collateral security will have to struggle a lot to avail finance from the institutional sources. Therefore, collateral security is one of the important factors to determine the accessibility to institutional finance.

ii. Institutional level determinants

To avail financial assistance from financial institutions, a set of comprehensive norms or conditions should be satisfied by the Small Scale Industries entrepreneurs as they are the major obstacles and determinants of SSIs access to institutional finance.

The following figure briefs about comprehensive norms or conditions of financial institutions to be fulfilled by the small scale industries entrepreneurs.

**Figure No.1.2**

*Figure Showing Lending Norms of Financial Institutions*
Documentation:

Entrepreneurs should furnish many documents along with the application, before the sanction of loan, after sanction before disbursement of loan and even after the disbursement of loan frequently entrepreneur has to provide some documents to the financial institutions. Some of the applicants may ever never heard and saw a set of documents of that kind. It is one among the lending norms or conditions should be fulfilled by the Small Scale Industries Entrepreneurs.

Collateral Security:

In lending agreements, collateral is a borrower's pledge of specific property to a lender, to secure repayment of a loan. The collateral serves as protection for a lender against a borrower's default—that is, it can be used to offset the loan to any borrower failing to pay the principal and interest under the terms of a loan obligation. If a borrower does default on a loan (due to insolvency or other event), that borrower forfeits (gives up) the property pledged as collateral, with the lender then becoming the owner of the property. 5

Collateral, especially within banking, traditionally refers to secured lending. More complex collateralization arrangements may be used to secure trade transactions. It is one among the lending norms or conditions should be arranged by the Small Scale Industries Entrepreneurs.

Restricted Quantum of loan:

Maximum and minimum Size of the loan amount differs and restricted based on the purpose, scheme of finance, credibility of the finance aspirants and so on. It is one among the lending norms or conditions should be agreed by the Small Scale Industries Entrepreneurs.

Business information

Fund seeking SSIs should disclose and satisfy some norms of financial stability such as, Debt Equity Ratio, Assets Coverage Ratio, Current Ratio, and

some other ratios which depict the financial soundness of the enterprise. It is one among the lending norms or conditions should be fulfilled by the fund seeker.

**Interest Rate:**

The amount charged, expressed as a percentage of principal, by a lender to a borrower for the use of assets. Interest rates are typically noted on an annual basis, known as the annual percentage rate (APR). The assets borrowed could include cash and cash equivalents. The interest rate is sometimes known as the "lease rate". When the borrower is a low-risk party, they will usually be charged a low interest rate; if the borrower is considered high risk, the interest rate that they are charged will be higher. It is one among the lending norms or conditions should be agreed to pay by the Small Entrepreneurs.

**Accruing cost**

Financial institutions charge many types of charges to process the application, to grant the loan and even for disbursement of loan. Such as, commitment charges, application process fees, upfront fees and legal fees etc.

A fee charged by a lender to a borrower for an unused credit line or undisbursed loan. A commitment fee is generally specified as a fixed percentage of the undisbursed loan amount. The lender charges a commitment fee as compensation for keeping a line of credit open or to guarantee a loan at a specific date in future. The borrower pays the fee in return for the assurance that the lender will supply the loan funds at the specified future date and at the contracted interest rate, regardless of conditions in the financial and credit markets.

A commitment fee is different from interest; although, the two are often confused. A commitment fee is separate from the interest rate that is charged by the lender on the loan. A key distinction is that the commitment fee is charged on the undisbursed loan amount, while interest is charged on the disbursed amount of the loan.

A fee charged to process an application for a loan, such as a home mortgage from a lender or mortgage broker. Loan application fees are charged to cover some
of the costs involved in processing the application including credit checks, property appraisals and basic administrative costs.

An up-front fee charged by a lender for processing a new loan application, used as compensation for putting the loan in place. Origination fees are quoted as a percentage of the total loan and are generally between 0.5% and 1% on mortgage loans.

**Business plan**

An entrepreneur seeking finance should prepare and present a business plan to the financial institution. If the plan is innovative, viable and profitable financial institution approves the loan based on the business plan. This is the very basic step fund seekers should be alert. However, preparation and presentation of business plan is a difficult task for small scale industries. Since they are unaware and they would have been experienced many problems in preparing and presenting business plan. So that, business plan is also one of the lending norms should facilitate by small scale industries entrepreneurs to avail institutional finance.

**Timeliness of loan sanction**

Time is a very important factor which insists an entrepreneur to acquire financial resources from the amenable sources where finance can be assured on time. But, financial institutions have not been giving value for the time of entrepreneurs, simply they follow some procedures and drag the process long way, it harms the operational efficiency of the small scale industries. Therefore, one who seeks finance form financial institutions should wait till they grant the loan. This is also one of the lending norms of financial institutions, entrepreneur should agree.

The researcher has made an attempt to brief very important determinants of small scale industries access to institutional finance. In the study area it is significant to identify the influence of these factors on the small scale industries access to institutional finance.
1.2 Small Scale Industries - A Bird’s eye view:

Small Scale Industrial (SSI) sector has emerged as a highly vibrant and dynamic sector of the Indian economy over the last five decades. SSIs not only play a crucial role in providing large employment opportunities at comparatively lower cost than large industries but also help in industrialization of rural and backward areas, thereby, reducing regional imbalances, assuring more equitable distribution of national income and wealth. SSIs are complementary to large industries as ancillary units and this sector contributes enormously to the socioeconomic development of the country.  

Small Scale Industries (SSIs) contribute nearly 8 percent of the country’s GDP, 45 percent of the manufacturing output and 40 percent of the exports. They provide the largest share of employment after agriculture. They are the nurseries for entrepreneurship and innovation. They are widely dispersed across the country and produce a diverse range of products and services to meet the needs of the local markets, the global market and the national and international value chains.

Performance of Small Scale Industries (SSIs) sector is assessed by conducting periodic All India Census of the Sector. The latest census conducted was Fourth All India Census of MSME. The Census was conducted with reference year 2006-07, wherein the data was collected till 2009 and results published in 2011-12. Fourth All India Census of MSME is the first census conducted post implementation of the Micro, Small and Medium Enterprises Development (MSMED) Act, 2006.

As per the quick estimates of 4th All-India Census of MSMEs, the number of enterprises is estimated to be about 26 million and these provide employment to an estimated 60 million persons. Of the 26 million SSIs, only 1.5 million (6 percent) are in the registered segment while the remaining 24.5 million (94%) are in the unregistered segment.

The State-wise distribution of SSIs show that more than 55% of these enterprises are in 6 States, namely, Uttar Pradesh, Maharashtra, Tamil Nadu, West Bengal, Andhra Pradesh and Karnataka. Further, about 7% of SSIs are owned by women and more than 94% of the SSIs are proprietorships or partnerships.

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6 Ministry of MSME - Annual Report 2013-14
SSIs in the country manufacture over 6,000 products. Some of the major subsectors in terms of manufacturing output are food products (18.97%), textiles and readymade garments (14.05%), basic metal (8.81%), chemical and chemical products (7.55%), metal products (7.52%), machinery and equipments (6.35%), transport equipments (4.5%), rubber and plastic products (3.9%), furniture (2.62%), paper and paper products (2.03%) and leather and leather products (1.98%)\(^8\).

**Figure No. 1.3**

*Figure showing Leading Industries in SSI sector*

*Source: Ministry of MSMEs Annual Report 2013-14*

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Definition of MSMEs:

Micro, Small and Medium Enterprises Development Act, 2006 defined Enterprises as Micro, Small and Medium based on the investment of an enterprise in fixed assets as follows,⁹

<table>
<thead>
<tr>
<th>Enterprise</th>
<th>Investment in Fixed Assets(P&amp;M)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Micro</td>
<td>Upto Rs. 25,00,000</td>
</tr>
<tr>
<td>Small</td>
<td>Rs. 25,00,001 to Rs.5,00,000,000</td>
</tr>
<tr>
<td>Medium</td>
<td>Rs. 5,00,00,001 to Rs.10,00,00,000</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Enterprise</th>
<th>Investment in Equipments</th>
</tr>
</thead>
<tbody>
<tr>
<td>Micro</td>
<td>Upto Rs. 10,00,000</td>
</tr>
<tr>
<td>Small</td>
<td>Rs. 10,00,001 to Rs.2,00,00,000</td>
</tr>
<tr>
<td>Medium</td>
<td>Rs.2,00,00,001 to Rs.5,00,00,000</td>
</tr>
</tbody>
</table>

Source: MSMED Act 2006

Prior to implementation of MSMED Act, 2006, the sector was defined as per the provision of Industrial Development and Regulation Act, 1951 as Small Scale Industries (SSI) sector and its constituent, tiny and auxiliary units as per periodic revision of criteria for defining such units. The Third All India Census of SSI was conducted with coverage and concepts as prevailing during 2001-02. The scope and coverage of the SSI sector were broadened significantly under the MSMED Act, 2006, which recognized the concept of “Enterprise” and to include both manufacturing and services sector, besides defining the medium enterprises under the SSI sector. Thus, the entire non-agricultural sector of the economy was brought under the coverage of MSME sector subject to the revised criteria prescribed for defining Micro, Small and Medium Enterprises separately for manufacturing and services sectors.¹⁰

1.3 Need for the study

One of the most important developments in Indian business scenario has been the growth of Small Scale industrial financing institutions. In India, Small Scale Industries financing institutions help the entrepreneurs in various ways to nurture the business entities, such as providing Start-up finance, Modernization finance and up-gradation finance, finance for expansion of the business and providing working capital facilities as well.

Government of India and all State Governments have been assisting finance to SSIs through many National and State level financial institutions. But, majority (88.79 percent) of the registered SSIs and 95.20 percent of unregistered SSIs are not accessing these financial institutions as per the Statistics of Fourth All India census of MSMEs, there arise a need to study the perception of Small Scale Industries Entrepreneurs on Financing Institutions. Hence the study is to evaluate and analyze the institutional Financing for Small Scale Industries in Karnataka. Moreover no significant study has been carried out in Karnataka with special reference to demand side perceptional analysis on Institutional Financing for Small Scale Industries.

Table No. 1.1

Table Showing Percentage of SSIs Availed Financial Assistance from Institutional Sources

<table>
<thead>
<tr>
<th>Source of Finance</th>
<th>Registered</th>
<th>Unregistered</th>
</tr>
</thead>
<tbody>
<tr>
<td>No Finance/Self Finance</td>
<td>87.77</td>
<td>93.08</td>
</tr>
<tr>
<td>Finance through Institutional Sources</td>
<td>11.21</td>
<td>4.8</td>
</tr>
<tr>
<td>Finance through Non-Institutional Sources</td>
<td>1.02</td>
<td>2.12</td>
</tr>
<tr>
<td>Total</td>
<td>100</td>
<td>100</td>
</tr>
</tbody>
</table>

*Source: Fourth all India Census of MSMEs*
1.4 Statement of the Problem

The scarcity of credit and finance is the major obstacles in the development of Small Scale Industries. “In a growth hungry economy with a scarce funding environment, Financing Institutions offer finance for fueling the economic engine”. Financial institutions are the avenues for Small Scale Industries to mobilize finance to their Short term, Medium term and Long term financial needs.

During the course of exhaustive review of literature prominent questions which strike the mind are what are the formal avenues of finance for SSIs? What are the lending norms of formal financial institutions? Which group of SSIs having some defined characteristics have greater accessibility to financial Institutions? How lending norms influence the accessibility to financial institutions? What other sources of finance for small scale industries? Is there any relationship with formal source of financing and growth of business and vice-versa? Hence, there arises a need to address the aforesaid questions. The following table explains the overall finance gap in MSME sector.

### Table No.1.2

<table>
<thead>
<tr>
<th>Particulars</th>
<th>(in INR Trillion)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Total Finance Demand</td>
<td>32.5</td>
</tr>
<tr>
<td>Entrepreneur’s Contribution</td>
<td>4.6</td>
</tr>
<tr>
<td>Potential Finance Demand</td>
<td>27.9</td>
</tr>
<tr>
<td>Formal Supply</td>
<td>7</td>
</tr>
<tr>
<td>Total Finance Gap</td>
<td>20.9</td>
</tr>
<tr>
<td>Total Debt Gap</td>
<td>19</td>
</tr>
<tr>
<td>Total Equity Gap</td>
<td>1.9</td>
</tr>
</tbody>
</table>

*Source: Compiled from MSME Census, RBI Reports, SIDBI Reports, IFC Intellecap Analysis*

This shows the need for the study to meet the financial gap or expectations.
1.5 Objectives of the study

Objectives of the study are as follows.

1. To identify the formal and informal sources of finance for Small Scale Industries.

2. To study the relationship between characteristics of Small Scale Industries and access to institutional finance.

3. To study the relationship between Small Scale Industries accessibility to institutional finance and institutions lending norms.

4. To examine the entrepreneurs’ perception regarding institutional financing for Small Scale Industries.

5. To explore the policy implications for strengthening institutional financing for Small Scale Industries in Karnataka.

1.6 Hypotheses for the study

The following Hypotheses have been enlisted for the study.

H1: “Small Scale Industries in Karnataka are funded significantly by informal sources of finance than formal sources”.

H2: “There is a significant relationship between characteristics of Small Scale Industries and access to institutional finance”.

H3: “There is a significant relationship between the lending norms of financial institutions and access to institutional finance by Small Scale Industries”.

H4: “The level of perception of entrepreneurs about the effectiveness of institutional financing is low”.
1.7 Scope of the Study

The scope of the present study is confined to Registered Small Scale Industries located in Karnataka state. Out of 20,19,000 registered Small Scale Industries in Karnataka, 1363 registered (at District Industries Centers since 2007 to 2012), Small Scale Industries consisting Micro, Small and Medium Enterprises have been chosen for the study.

Operational Definitions of Important Concepts

To evaluate the study in a precise manner the researcher has used the following operational definitions.

Financial Institutions

For the present study ‘Financial Institutions’ are defined as, “Central and State government financing institutions, specially established for the up-liftment of Small Scale Industries. Such as, Small Industries Development Bank of India (SIDBI), National Small Industries Corporation (NSIC), Khadi and Village Industries Commission (KVIC), National Bank for Agriculture and Rural Development (NABARD), Export and Import Bank (EXIM Bank), Small and Medium Enterprises Exchange (SME Exchange), State Financial Corporations (SFCs).

Formal Sources of Finance

For the present study ‘Formal Sources of finance’ is defined as “National level and State level, formal or organized sources of finance (Financial Institutions) specially established for the up-liftment of Small Scale Industries. Such as, Small Industries Development Bank of India (SIDBI), National Small Industries Corporation (NSIC), Khadi and Village Industries Commission (KVIC), National Bank for Agriculture and Rural Development (NABARD), Export and Import Bank (EXIM Bank), Small and Medium Enterprises Exchange (SME Exchange), at national level and Karnataka State Financial Corporation (KSFC) at state level.
Informal Sources of Finance

For the present study ‘Informal Sources of finance’ is defined as “Informal or unorganized sources of finance which fulfil the financial needs of Small Scale Industries. Such as, Personal Savings, Angel investors, Friends, Family, Relatives, Supply chain credit, Customer Advances and Crowd funding, etc.”

Angel Investor

For the present study ‘Angel Investor’ is defined as, “Entrepreneur's family members, friends and relatives who inject seed money for continuous support to carry out the operations of the company through difficult times”.

Lending Norms

For the present study ‘Lending norms’ is defined as “a set of rules or norms to be fulfilled by the Small Scale Industries entrepreneurs to avail financial services of financial institutions. It includes collateral norms, documentation, business plan, accruing cost, rate of interest, Loan processing time (procedure), and quantum of loan.

Small Scale Industries

For the present study ‘Small Scale Industries’ are defined as “all registered Micro, Small and Medium Enterprises with investment ceiling prescribed under the MSMED Act 2006”.

Manufacturing Enterprise

<table>
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<th>Enterprise</th>
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Service Enterprise

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</tbody>
</table>

Source: MSMED Act 2006
1.8 Research Methodology

Area of study

Karnataka is the chosen locale for the study.

Population of the study

Population of the study consists of 20,19,000 Small Scale Industries which are manufacturing goods and providing services in Karnataka as on 2012.

Sample of the Study

In this study data has been pooled from selected 1363 Small Scale Industries registered during 2007-08 to 2011-12. Sampling design is as follows.

Figure No. 1.4

Figure Showing Sample Size of the Study
Table No. 1.3

Table Showing Sample Stratification for the Study

<table>
<thead>
<tr>
<th>Year</th>
<th>Micro</th>
<th>Small</th>
<th>Medium</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td>2007-08</td>
<td>13945</td>
<td>902</td>
<td>31</td>
<td>14878</td>
</tr>
<tr>
<td>2008-09</td>
<td>14812</td>
<td>869</td>
<td>24</td>
<td>15705</td>
</tr>
<tr>
<td>2009-10</td>
<td>16177</td>
<td>992</td>
<td>26</td>
<td>17195</td>
</tr>
<tr>
<td>2010-11</td>
<td>17408</td>
<td>998</td>
<td>28</td>
<td>18434</td>
</tr>
<tr>
<td>2011-12</td>
<td>19610</td>
<td>1370</td>
<td>41</td>
<td>21021</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>81952</strong></td>
<td><strong>5131</strong></td>
<td><strong>150</strong></td>
<td><strong>87233</strong></td>
</tr>
<tr>
<td>in Percentage</td>
<td>93.95</td>
<td>05.88</td>
<td>0.172</td>
<td>100</td>
</tr>
<tr>
<td><strong>No. of Sample Units</strong></td>
<td><strong>820</strong></td>
<td><strong>513</strong></td>
<td><strong>30</strong></td>
<td><strong>1363</strong></td>
</tr>
<tr>
<td>in Percentage (on Total)</td>
<td>01.00</td>
<td>10.00</td>
<td>20.00</td>
<td>100</td>
</tr>
</tbody>
</table>

Figure No. 1.5

Figure Showing Sample Stratification for the Study
Data has been collected from all the districts of Karnataka, 1363 units have been chosen and it consists of 820 Micro, 513 Small and 30 Medium Scale Enterprises.

Out of 820 Micro Enterprises, 290 enterprises from Bangalore district, 140 enterprises from Mysore district and 15 enterprises from each district have been selected.

Out of 513 Small Enterprises, 169 enterprises from Bangalore district, 84 enterprises from Mysore district and 10 enterprises from each district have been selected.

Out of 30 Medium Enterprises, 2 enterprises from Bangalore district, 2 enterprises from Mysore district and 1 sample unit from each district has been selected.

Sources of Data

Data has been collected from both primary and secondary sources.

**Primary Sources:** well-structured questionnaire and interview schedules were the primary sources of information.

**Secondary Sources:** Secondary data has been collected from the available sources of information such as; Annual Reports, Journals, Magazines, Reports of Special Committees, Working Papers, Government Gazettes, Websites, Brochures of Financing Institutions, E-Libraries and other Databases.

Tools Used for Data Analysis:

In this study for testing of hypotheses following statistical tools are used;

**Descriptive statistics:** With the help of Descriptive statistics such as percentage and graphs, researcher has been described the results of the study.

**Logistic Regression:** With the help of logistic regression analysis, researcher has studied relationship among independent and dependent variables.

**Chi-Square:** with the help of Chi-square test researcher has examined the level of perception of entrepreneurs towards effectiveness of institutional finance.
1.9 Chapterisation Scheme

The study has been presented in six chapters.

Chapter 1: Introduction – Deals with the introduction of the study. It explains the way in which the study has been carried-out. It contains, concept of institutional finance, definition of institutional finance, enterprise level and institutional level determinants of Small Scale Industries Access to Institutional finance, an overview of Small Scale Industries, need for the study, statement of the problem, objectives of the study, hypotheses for the study, scope of the study, operational definitions of important concepts, research methodology, chapterisation scheme and Limitations of the study.

Chapter 2: Review of Literature – This chapter consist literature survey as a process of developing an insight into both conceptual and research based studies available both at national and international arena has been covered.

Chapter 3: A Profile of Financing Institutions for Small Scale Industries– It deals with the Profile of Financing Institutions for Small Scale Industries. It gives clear picture of national level, State level and other informal financial sources of Small Scale Industries.

Chapter 4: Small Scale Industries in India: An Overview – A detailed overview of SSIs in India and Karnataka has been presented in this chapter. It has been classified into two parts. First part deals with the scenario of Small Scale Industries in India. Second part deals with scenario of Small Scale Industries in Karnataka.

Chapter 5: Data analysis and Interpretation – This chapter deals with analysis and interpretation of data collected from primary and secondary sources relating to perception of entrepreneurs towards institutional financing for Small Scale Industries has been covered and hypotheses have been tested.

Chapter 6: Summary of Findings, Suggestions and Conclusions - This chapter summarized the research findings with suitable suggestions. Further, identified the scope for further research and drawn conclusion.
1.10 Limitations of the study

1. The study mainly focused on 1363 Small Scale Industries in Karnataka; obviously the findings of the study may not be generalized for the entire Small Scale Sector of India.

2. This study was focused only on perception of Fund seekers (Entrepreneurs) towards the Accessibility of Finance from financing institutions and it was not focused on attitude of Funding agencies towards Small Scale Industries’ credibility.

3. Data analysis and interpretation is done based on the information provided by Small Scale Industries and reliability of the data may not be hundred percent accurate.