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INCREASING ACCESS TO FINANCE FOR MSMEs

A Policy Paper by Wadhwani Institute of Technology & Policy

Author- Sayantani Satpathi

EXECUTIVE SUMMARY

India’s path to a USD 5 Tn. (~INR 410 Tn.) by 2026-27, can be paved with investments leading to increase in employment generation, firm productivity, and export growth. At present, MSME sector employ 110 Mn. people, contributing ~27% to the national Gross Domestic Product (GDP). Additionally, MSME exports stood at ~43% of the country’s total exports.

Policymakers have identified unmet financial gaps from institutional sources as a significant stressor to MSME growth. Currently, the government has been working towards policy interventions to improve access to institutional sources of finance. Access to credit interventions can be categorized into three broad areas: novel financing channels, improving access to existing formal credit, and technological interventions. Majority of the existing policies in India fall under the second category. While the central government has introduced reforms to create novel financial channels and enable technological interventions, the efforts on the same from states have been very limited.

This white paper reviews existing policy interventions to increase access to finance for MSMEs, assess gaps, and examine policies from countries around the globe and Indian states. Drawing fromt this analysis, the paper makes a few key recommendations:

- Formalize the adoption of Open Financial Networks for credit, payments, insurance, investments, and tax filing.

- Promote the use of blended finance instruments for state level MSME ecosystem to ensure that public funds are supported by impact investment and private sector funds, thereby improving operational efficiency.

- Promote the creation of cooperatives and microfinance lending institutions, which have better geographical reach and community buy-in than commercial banks.

- Establish technical training programmes to ensure that banks and NBFCs have sector specific knowledge to serve MSMEs.

- Create a platform to enable voluntary enrollment by MSMEs that are not registered with the GST, EPFO, or ESIC, to allow MSMEs to take advantage of the Open Financial Networks.

1. INTRODUCTION

There are ~660 Mn Micro, Small, and Medium Enterprises (MSMEs) in India employing ~110 Mn. of the workforce, accounting for less than one-third (~27%) of the total Gross Value Added (GVA) in goods and services, and ~43% of the country's total exports (Economic Survey 2021- 22; MSME, 2022). The majority (52%) of MSME units were based in the rural areas (IBEF website), which enables entrepreneurship and employability opportunities across the country.

Therefore, if the country needs to achieve her goal of becoming a USD 5 Tn. (~INR 410 Tn.) economy by 2026-27 (The Economic Times, January 26, 2023), she needs to create an enabling ecosystem for the growth of the MSME sector. The MSME ecosystem in the country is dominated by micro enterprises[1] (96%) (IBEF website). These units are operated by an individual proprietor operating with one and three hired help or family-run businesses. According to government sources, as of FY 2021-22, 13% MSMEs were registered on the Udyam portal (Invest India, March 31, 2022). When MSMEs fail to register they are automatically denied access to institutional credit, tax exemptions, infrastructure (e.g., uninterrupted supply of water and power, subsidized land), and technology (e.g., R&D, e- commerce platform) (KPMG-IMC 2017, p,36). However, access to financial resources is the biggest stumbling block for MSMEs, which was exacerbated in the COVID years (ET Times, June 18, 2021). A post-pandemic survey (2021) of MSME entrepreneurs on the impacts of the pandemic reconfirmed financial access as one of the key stressors for small businesses[2] . The same survey noted that the majority (59%) of small business owners would like government interventions to improve financial access during the post-pandemic era (Dun and Bradstreet, April 2021, p.10).

Given the lack of financial inclusion as a significant stressor for MSMEs, the Wadhwani Foundation's Wadhwani Institute of Technology Policy (WITP) felt it necessary to produce this paper to create an enabling environment for fostering MSME growth. The paper is in line with the previous three papers authored by the Wadhwani Foundation team on addressing cluster development, global best practices, and a model MSME policy for the states. The paper is divided into five sections with the first section presenting an overview of the MSMEs in states. The second part looks at the status of MSME financing, its importance, and the challenges for MSME financing globally and in India. In the third part, global examples of MSME financing measures have been presented. The fourth part of the paper explores existing policy landscape of MSME financing at the center and the state level in India. The final section consolidates our findings and recommends viable policy interventions.

[1] A micro enterprise, where the investment in Plant and Machinery or Equipment does not exceed 10 Mn. rupees and turnover do not exceed 50 Mn. rupees. See: https://msme.gov.in/sites/default/files/MSME_gazette_of_india.pdf

[2] The survey respondents stated that the top three impediments for a small business owner to decide scaling up their operations include, inadequate financial access, market access and improving productivity (Dun and Bradstreet, April 2021, Executive Summary).

2. MSMEs IN STATES

To catalyze the transformation of Indian MSMEs into globally competitive entities, it is imperative to emphasize the adoption of innovation, world-class technologies, and a skilled workforce (KPMG, 2015, p.2). However, achieving these objectives is contingent upon securing unrestricted access to capital, which remains a critical challenge for MSMEs operating in the shadow of informality.

2.1 Overview

Under the Micro, Small and Medium Enterprises Development Act (MSMED) (2006)[3] , an entrepreneur registers with the Ministry of MSME through the Udyam portal. As of March 31, 2022, 13% of MSMEs registered with the Ministry of Micro, Small and Medium Enterprises (MSMEs) (Udyam portal). Once an enterprise has been registered, it is able to access funding (e.g., grants and loans) and direct/indirect tax exemptions (KPMG, 2015, p.3).

Central policymakers provide financial support, in the form of grants, funds, or access to low- interest loans, to catalyze MSME growth. However, individual states have yet to offer targeted interventions to promote MSME growth.

2.2 Challenges

In recent years, policymakers both the central and state government have prioritized startups over MSMEs. States have formulated independent startup policies that provide 360-degree support to startup entrepreneurs in the form of regulatory, financial, and capacity-building incentives. This supportive policy environment catalyzed the Indian startup ecosystem, which now ranks third largest globally with over 80,000 registered startups and 107 unicorns (Startup India, Invest India, September 7, 2022).

The role of MSMEs in the Indian economy is undeniable, yet state-level policymakers have failed to design adequate policies to address their needs. This is partly due to the information asymmetry created by the informality of the MSME sector. While states with higher levels of industrialization tend to have dynamic MSME sectors that complement larger industries as ancillaries, standalone MSME policy interventions are lacking, except for a few states.

[3] Under the MSME Development Act (2006) (revised on May 13, 2020), anyone wishing to register their businesses as a Micro, Small, or Medium enterprise, relies on investment and annual turnover. For additional information, check: https://pib.gov.in/PressReleasePage.aspx?PRID=1628925

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3. MSME FINANCING

3.1 Overview

Access to finance presents a critical roadblock for MSMEs across the globe. It is estimated that in developing countries with MSMEs regarded as engines of growth-the current credit gap stands at USD 5.2 Tn. (~INR 426 Tn.) (19% of the gross GDP) (IFC Report, 2017). In addition, there is a potential demand for an estimated USD 2.9 Tn. (~INR 238 Tn.) (10% of the GDP) from informal SMEs in developing countries (Ibid). While the problem of lack of access to finance is not endemic to India, it is particularly regretful. MSME demand for capital was estimated to be USD 1.4 Tn. (~INR 115 Tn.) a major part (67%) met through the non-institutional sources (e.g., family, friends, money lenders and chit funds) (IFC, 2018). The credit gap in MSME sector was estimated to be around ~INR 20,000 to 25,000 Bn. with ~40% of MSMEs depending on informal sources (Standing Committee on Finance, April 8, 2022).

3.2 Challenges

Small businesses grow through family loans, personal investments, government grants, working capital loans, collateral funding, short and long-term investment secured from a bank or NBFC (KPMG-IMC, 2017, p. 9). Securing formal credit for a small business is a lengthy process characterized by information asymmetry and procedural complications. From the lenders' perspective, financing a small business is complicated due to a combination of "high transaction costs, low ticket sizes and high risks involved" (KPMG-IMC, 2017, p.15). More specifically, the early-stage businesses are unable to provide collateral (e.g., physical assets), consistent cash flow in their books, or credit history against which the loans can be processed (Ibid, p.15).

To alleviate these concerns, the government directly offers credit to MSMEs through state-owned banks and restructured the mandates for banks and NBFCs to ensure ease in credit allocation. Nevertheless, a significant hurdle to MSME financing, as highlighted by a World Bank study (2017), is the issue of "transparency". MSMEs require working capital and term loans (RBI, 2019), and lenders assess their creditworthiness through credit appraisal systems (e.g., Score Card Models for small loans and Credit Risk Assessment for bigger loans). However, assessing the creditworthiness of MSMEs is challenging due to information asymmetry resulting from the lack of publicly available data on their financial performance (RBI, 2019).

While MSMEs in India face similar challenges to those in other developing countries, there are a few distinct challenges that are unique to Indian MSMEs. According to a Reserve Bank of India (RBI) (2019) study, MSMEs in India face higher costs associated with accessing credit, even though the central bank has issued guidelines stating that collateral is not required for loans up to INR 1 million. First-time entrepreneurs often cannot access loans due to a lack of documentation, such as income tax returns from past years. From the lenders' side, banks lack the human resources and tools required to effectively evaluate loan applications for small businesses. Instead, they rely on basic indicators such as cash flows to assess the feasibility of small businesses, which is an unreliable proxy for assessing a company's performance (Ibid). Stringent monitoring requirements of existing government schemes, such as those found in the Credit Guarantee Fund Trust for Micro and Small Enterprises (CGTMSE) scheme, have occasionally caused delays in the allocation of funds to companies. In addition to these challenges, MSMEs in India remain at the lowest end of the payment flow in the supply chain. This means that whenever the supply chain is impacted, the cash flow to MSMEs is relatively more impacted.

The lack of novel financial solutions (i.e., equity and venture capital, angel investment, crowdfunding, and ***Peer to Peer*** (P2P)[4] funding) to meet the financial needs of MSMEs increases their dependence on banks and non-banking financial companies (NBFCs) (Saini, 2016). Typically, a small business requires funding for its entire growth cycle, which is classified into four stages: start-up, survival, growth, and sustenance (GoAP Discussion Paper, 2017). In the initial phase, an MSME relies on personal fundings or financial support from both families and friends. In the later stages of growth and sustenance, which are more capital-intensive, entrepreneurs require access to formal credit and innovative financial products/services. In the absence of innovative or novel financial products, MSMEs rely on a combination of personal funds, family wealth, friends, moneylenders, and banks.

According to a study by the Asian Development Bank (ADB), 57% of all MSMEs surveyed were not aware of any government schemes meant to support them financially. This lack of awareness explains why MSMEs are so dependent on informal sources of credit, which makes them vulnerable to predatory practices and increases their risk of insolvency and bankruptcy. Additionally, the lack of formal credit made it difficult for the MSMEs to ensure a stable supply chain and labor flow, and to implement expansion and diversification plans.

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[4] Peer to Peer (P2P) lending model refer to a digital marketplace connecting borrowers with lenders allowing quick access to low-cost loans
(See: https://uncitral.un.org/sites/uncitral.un.org/files/media-documents/EN/wasme_access_to_credit_for_indian_msmes.pdf)

Figure 1: Financial Gap for Micro Enterprises-India v. Global

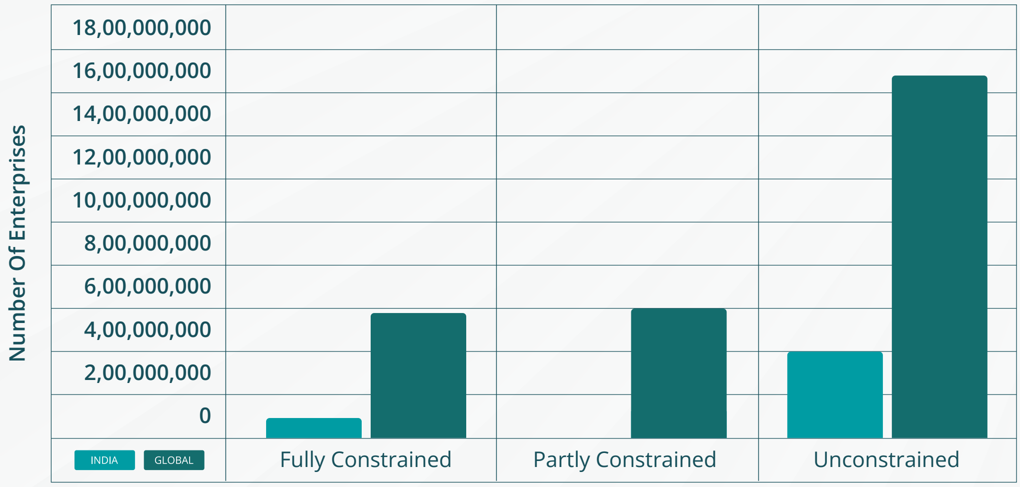


Figure 2: Financial Gap for Small and Medium Enterprises-India v. Global

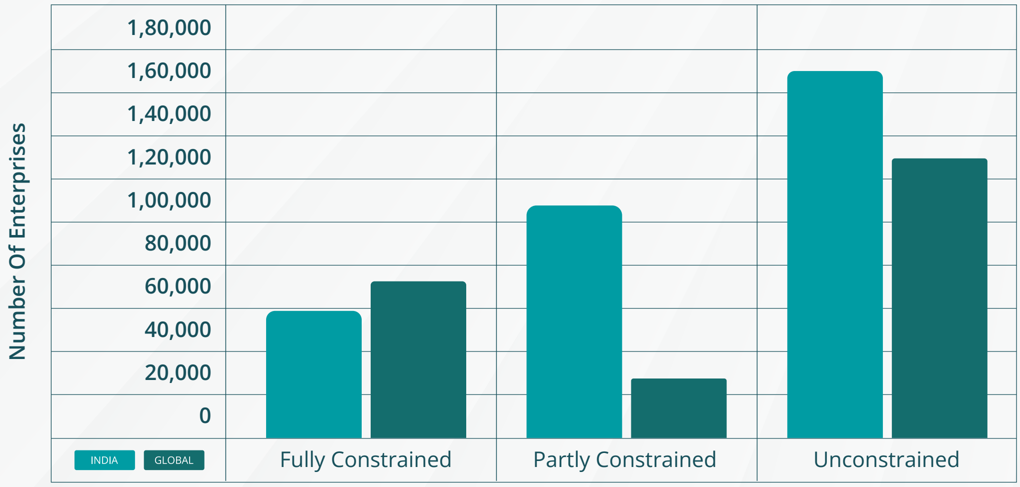
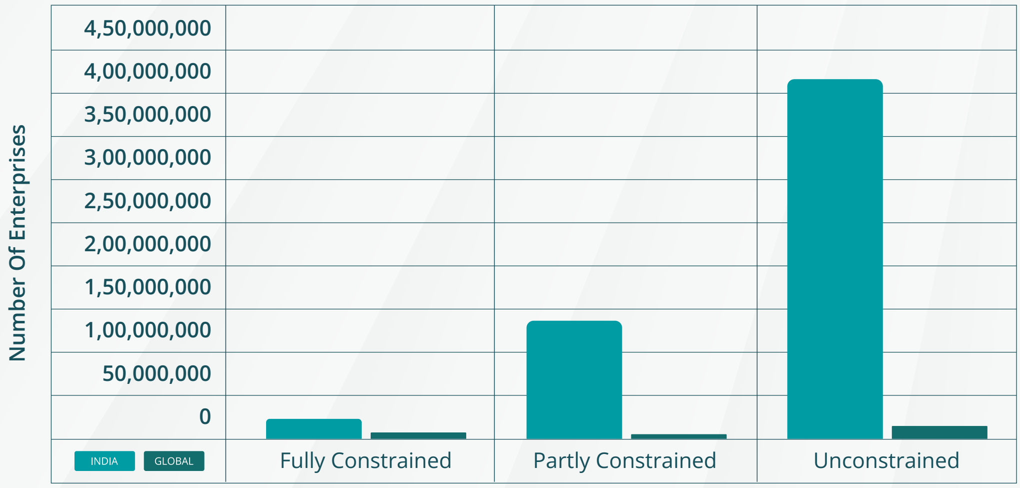


Figure 3: Financial Gap for Micro, Small and Medium Enterprises-India v. Global



Source: SME Finance Forum

4. MSME FINANCING
GLOBAL EXPERIENCE

Countries across the globe have adopted several innovative techniques to address the access to finance challenges for MSMEs. These interventions can be divided into three broad categories: novel financing channels, increasing access to formal credit, and technological interventions. Some noteworthy examples are listed below:

4.1 Novel Financing Channels

4.1.1 Colombia

The National Training Service (Servicio Nacional de Aprendizaje) in Colombia launched the ***Emprender Fund*** (SENA website). Funds worth USD 137.1 Mn. (~INR 11,234 Mn.) were disbursed for 4,141 projects between 2005-14. Furthermore, Colombia also brought existing angel investors and venture capital funds into the fold to help with financing of business activities.

4.1.2 Germany

Germany worked on aggressively expanding its equity financing ecosystem. For instance, in 2017, Germany launched the *INVEST-Venture Capital Fund*, which extended 20% grant support to investors willing to acquire stakes in young and innovating startups (European Foundation website). In 2018, the state-run development bank, KfW had announced its decision to double the co-investment in venture capital funds by 2020 (GTAI website). KfW also established the "*Venture Tech Growth Financing Scheme*," through which it expanded its VC loans to tech companies. Unlike the Indian counterpart, the German investment strategy adopt the use of novel financing mechanisms for extending incentive funds to both the small and medium businesses.

4.1.3 Canada

The state led *Venture Capital Action Plan* (VCAP) has pledged a sum of CAD 400 Mn. (~INR 24,835.6 Mn.) to encourage private companies to invest in early-stage small and medium businesses. Between 2013 and 2016, the VCAP initiative had backed four private sector led funding of CAD 900 Mn. to support 100 companies (bdc website).

4.1.4 Mexico

In 2000s, Mexico reoriented its national finance organization Nacional Financiera (NAFIN) to focus on SME financing. The idea was to promote low-cost products, and a credit guarantee (NAFIN website). NAFIN also launched the "productive chain scheme", whereby it acts as an intermediary and provides factoring services. As a reliable intermediary, it connects financiers with suppliers, while simultaneously maintaining a secondary credit market. This had led to the creation of 584 productive chains, with 39 financial intermediaries, 68,000 suppliers, and 10,000 daily transactions.

4.1.5 Ethiopia

Ethiopia launched its Women Entrepreneurship Development Project (WEDP) to provide individual liability loans to female entrepreneurs. The first ever women-entrepreneur focused line of credit, it extended USD 3 Mn. in loans and supported capacity building of 600 women entrepreneurs (WEDP website). The dedicated funding for female entrepreneurs was able to increase the average amount of loans availed by women. The WEDP fund also show an increase in profit margins of 40% and added 56% of net new jobs (WEDP website).

4.1.6 Lebanon

Lebanon currently runs the Innovative Small and Medium Enterprises (iSME) project (Ministry of Economy and Trade website). The project is worth USD 30 Mn. (~INR 2,458 Mn.) is based on equity financing (along with seed and venture capital) for startups and the SMEs. Using the funding from the iSME, firms raised USD 13.1 Mn. (~INR 1,074 Mn.) of fresh capital, resulting in leveraging ratio of 5.3 times (World Bank). Lebanon also has the International Finance Corporation's (IFC) "Banking on Women" (BoW), which provide financial access of USD 130 Mn. to women entrepreneurs through six banks, while five banks offer capacity building training for the women entrepreneurs (World Bank.org). This is a great initiative as small businesses in Lebanon are controlled by women (60%), and female participation in entrepreneurship activities continues to rise, when financial access to support SMEs through loans are restricted to mere 3% (IFC-World Bank, 2016, p.12).

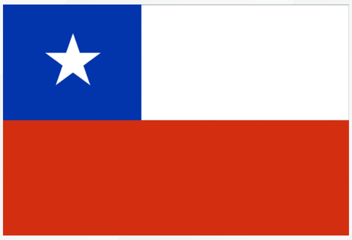
4.2 Increasing Access of Formal Credit

4.2.1 China

China pioneered the concept of decentralized credit guarantee by creating both regional and local level credit guarantee agencies. While the central government supported these agencies, they operated at an independent level. This allowed the agencies to become responsive towards addressing the local needs of the SMEs. In 2015, China announced the setting up of the *National SME Development Fund* worth USD 2,100 Mn. (~INR 172,086 Mn.), which was supported by an additional USD 6.35 Bn. (~INR 520 Bn.) of private capital funding to meet the financial needs of the seed and early stages SMEs (China Daily website).

4.2.2 Nigeria

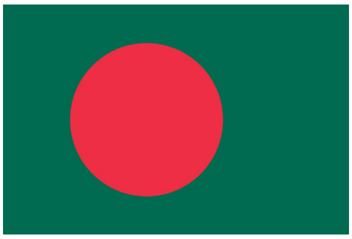
The state led *Development Bank of Nigeria* (DBN) working with global partners extended credit to the MSMEs. To date, DBN extended USD 250 Mn. (~INR 20,484 Mn.) of financing and partial credit guarantees to the 50,000 MSMEs and small corporates in the country (DNB website).



4.2.3 Chile

The Production Development Corporation of Chile (CORFO) launched the Innova Chile programme in 2005. This programme merged capacity building training and capital disbursement efforts with the objective of promoting innovations, investment, and entrepreneurship (CORFO website). Under this programme, selected entrepreneurs received seed capital support for designing an innovative startup and suitable mentoring. Companies under the scheme have generated effective sales in one year and have grown at 44% on average. Chile also operated the *Fondo Etapas Tempranas* (Early Stage) Fund to provide equity financing to firms.

4.2.4 Bangladesh



Bangladesh has undertaken a comprehensive overhaul of its MSME financing infrastructure. Apart from launching six MSME specific schemes in the past five years, Bangladesh eased the provisioning norms and risk weights of unrated assets. This increased the flow of collateral in the credit market. Additionally, Bangladesh designated 30% (as of 2021) of loan disbursement to MSMEs, and made the licensing of new bank branches, contingent on meeting this target. This was combined with easing of the loan sanctions procedure, which led to a reduction in the time of disbursement. Bangladesh also has an "*Access to Finance for Women SME*" (WSME) project, which extends credit guarantee to female entrepreneurs (World Bank).

4.2.5 Turkiye

Turkiye has combined the preferential rates with priority lending for certain demographic. The country offered preferential rates for women entrepreneurs and provide small businesses with non-financial institutional support including training, and guidance. Turkey also operates the ***Turkish Credit Guarantee Fund***, under which it accepts programme specific funding from international organizations such as the ***European Bank for Reconstruction and Development*** (AECM). This fund extends guarantees and collaterals for SMEs and non-SMEs, which fail to access bank loans in the absence of collaterals (Finance Office, Turkiye Government website). The fund extended TKY 353 Bn. (~INR 3,212 Bn.) as guarantees, and TKY 404 Bn. (~INR 3,676 Bn.) to 545,000 thousand entrepreneurs by end of 2019 (Finance Office, Turkiye Government website).

4.3 Technological Interventions

4.3.1 Brazil

The *National Bank for Economic and Social Development* (BNDES) offers support to SMEs through financial access, public procurement, innovations, capacity building of entrepreneurs, managerial and workforce skilling, and training programmes for women entrepreneurs (OECD.org). The BNDES has also launched the e-BNDES card (2004) to address the challenge of ease of availability of working capital for firms. Issued through public and private sector financial intermediaries, the BNDES card have pre-determined credit limit to support SMEs to purchase accredited products and services. When the cardholder makes a purchase using the card, the sales revenue generated from the transactions are linked back to the card or associated with the project or investment for which the financing was provided (BNDES website).

4.3.2 Singapore

The *National Monetary Authority of Singapore* created a regulatory sandbox to encourage and enable digital solutions for delivering financial products and services (Monetary Authority of Singapore website). The *FinTech Regulatory Sandbox* allowed FinTech players to experiment with innovative financial products while safeguarding the interests of the overall financial system (Monetary Authority of Singapore website).

5. POLICY LANDSCAPE IN INDIA

In India, the center and the state governments have several policy interventions targeting MSME access to finance problems. Apart from a targeted MSME policy, the central government operates several programmes focused on specific demographics (e.g., women, socio-economically marginalized communities) and industries. In addition, the *Small Industries Development Bank of India* (SIDBI), set up in 1990, operate programmes that are run either independently or in conjunction with the government to address finance inclusion for the MSMEs.

5.1 Central government schemes

5.1.1 Prime Minister Employment Generation Programme (PMEGP)

Under the programme, financial assistance is provided for setting up micro-enterprises in the non-farm sector, to facilitate employment opportunities for the unemployed youth. The bank sanctions up to 95% of the project costs (60-75% as bank term loan, and 15-35% as margin money or PMEGP subsidy). The beneficiary can apply for maximum project cost of INR 5 Mn. for the manufacturing sector, and INR 0.2 Mn. for the services sector.

5.1.2 Credit Guarantee Scheme for Micro and Small Enterprises (CGTMSE)

The CGTMSE provides guaranteed credit to first-time, as well as existing entrepreneurs. Under the scheme, the entrepreneurs could avail collateral-free guarantee of INR 50 Mn., while reducing the guarantee fee for securing loans up to INR 10 Mn. to 0.37% per annum. The scheme is run jointly by the Government of India, and the SIDBI.

5.1.3 Stand-Up India Scheme

The scheme was launched in 2016 and extended to 2025, to promote entrepreneurship among women, Scheduled Castes (SC) & Scheduled Tribes (ST) categories. The scheme prioritized economic empowerment and job creation by extending access to finance to these groups (INR 1-10 Mn. to woman or SC/ST per branch of the bank) to help them start a greenfield enterprise in manufacturing, service, trade, or activities allied to agriculture.

5.1.4 Credit Linked Capital Subsidy Scheme (CLCSS)

This scheme facilitates technological upgradation for the plants and machineries in the MSEs by extending a capital subsidy of 15% (on institutional finance of up to INR 10 Mn.) across 51 sub-sectors/products.

5.1.5 Trade Receivables Discounting System (TReDS)

MSMEs in India continue to suffer from delayed payments. The TReDS system allows MSMEs to leverage their existing trade receipts for receiving liquid funds from third party investors. It also shifts the onus of fund recovery from smaller firms who may lack the capacity to larger investors specializing in recovery.

5.1.6 Raising and Accelerating MSME Performance (RAMP) scheme

The Government of India in partnership with the World Bank plans invested INR 60,000 Mn. with the objective of supporting MSME recovery, post-COVID. By collaborating with the state governments, the RAMP scheme aims at improving formal access to credit for the MSMEs, strengthen institutions and governance structures, improve collaborations between the central and state governments, and address the dual challenges of delayed payments for the MSMEs and greening of MSMEs.

5.1.7 Micro Finance Programme

Under the scheme, the Government of India provides capital to SIDBI for maintaining and running a microfinance specific fund called the "Portfolio Risk Fund". In this scheme, NGOs, and Monetary Financial Institutions (MFIs) were expected to provide 2.5% of the loan amount as security deposit, while the balance (7.5%) was to be funded through the Portfolio Risk Fund. The scheme was expected to improve access to capital for women, and citizens from underserved areas such as the Northeast.

5.1.8 Securitization and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002 (SARFAESI)

The SARFAESI Act allows banks and NBFCs to recover their dues exceeding INR 0.01 Mn. against secured assets of the borrower or guarantor, without intervention of the court or tribunal. This act helped to reduce the *Non-Performing Assets* (NPA) burden on lenders and free up more capital for lending. It also eases the collateral takeover process.

5.1.9 Sub target for MSME loans

Under the current RBI norms, domestic commercial banks are required to have an exposure of at least 7.5% to micro enterprises. This scheme targets access to finance for the MSMEs to ensure their growth, development and sustainability, and employment generation.

5.1.10 Credit Enhancement Guarantee Scheme for the Scheduled Castes (CEGS)

The CEGS guarantee loans to SC entrepreneurs motivated by innovations and technological growth. The scheme was allocated a corpus of INR 2,000 Mn. fund and provided up to 100% requested loans.

5.1.11 Emergency Credit Line Guarantee Scheme (ECLGS)

The ECLGS was launched by the government as a pandemic relief measure for MSMEs to meet their operational liabilities and restart their businesses. Under the scheme, 100% guarantee coverage to banks and NBFCs to enable them to extend credit to SMEs, in view of the COVID-19 pandemic, to meet their additional loans or working capital needs.

5.1.12 Financial Support to MSMEs in ZED Certification Scheme

This scheme has an objective of enabling MSMEs adopt "Zero Defect and Zero Effect" (ZED) practices, which entail reduction of wastages, adopt eco-friendly practices, save energy, optimal use of natural resources, improve productivity, and expand scope of market operations. To this end, MSMEs would receive both subsidies and monetary aid to help them achieve ZED solutions and certifications. The subsidies were extended to cover the costs of ZED certification (i.e., micro enterprises-80%; small enterprises-60%; and medium enterprises-50%, with additional subsidies available for women run enterprises and those operating in Northeast, Aspirational Districts, Islands, Left Wing Extremism affected states, and SFURTI or Micro & Small Enterprises – Cluster Development Programme (MSE-CDP)). To encourage MSMEs to take the ZED Pledge, would receive a joining bonus of INR 10,000. Furthermore, financial assistance of up to INR 0.5 Mn. will be provided to enable handholding, and consultancy support for assisting MSMEs in adopting and implementing ZED solutions.

Name of Schemes	Period	Number of Projects/Cases	Amount in (INR in Mn.)
Prime Minister Employment Generation Programme (PMEGP)	2023-24	22,050	9,002.3 (As subsidy)
Scheme of Fund for Regeneration of Traditional Industries (SFURTI)	2015-16 to 2023-24	513	13,361 (As grants)
Credit Guarantee Scheme for Micro and Small Enterprises (CGTMSE)	2014-15 to 2022-23	4,378,275	2,668,194 (As credit guarantee)
Credit Linked Capital Subsidy Scheme (CLCSS)	2016-17 to 2021-22	47,100	32,535 (As subsidy)
Bank Credit Facilitation to MSMEs	2016-17 to 2021-22	NA	16,607,980 (As credit)
Stand-Up India Scheme	2016-17 to 2021-22	133,995	301,605 (As credit guarantee)

Table 1: Status of Schemes

5.2 State-level landscape

To help MSMEs and startups access finance states have developed independent policies. However, substantial variations exist within states based on state's economy measured by the Gross State Domestic Product (GSDP) and political motivations for creating an enabling ecosystem for the MSMEs and startups.

5.3 Novel Financing Channels

Bihar: Bihar provides co-investment in startups through a trust run VC fund.

Gujarat: Gujarat runs the Gujarat Venture Finance Limited Fund for small ticket funding ranging from INR 0.5 Mn. to 30 Mn. for pre-series companies.

Karnataka: Karnataka provides a one-time grant up to INR 0.5 Mn. to startups under the Idea2POC scheme.

Odisha: Odisha runs INR 1,000 Mn. (~USD 12 Mn.) Fund for Funds, through which it invests in other MSME focused investment vehicles.

Punjab: Punjab runs INR 1,000 Mn. (~USD12 Mn.) fund through which it invests in VC backed projects and runs its own INR 1,500 Mn. (~USD18 Mn.) VC fund.

Tamil Nadu: Tamil Nadu runs an Alternative Investment Fund (AIF) called the Tamil Nadu Emerging Sector Seed Fund for MSMEs. This initiative was set up with the objective of investing in startups and undertakings in the sunrise/emerging sectors. The investment is extended in the form of financial and non-financial support.

Telangana: Telangana runs INR 2,000 Mn. (~USD 240 Mn.) VC fund called the Telangana Innovation Fund.

Uttar Pradesh: The state has dedicated ~INR 39,310 Mn. (USD 480 Mn.) for creating an innovation fund, and ~INR 9,827 Mn. (USD 120 Mn.) as startup fund.

5.4 Increasing Access of Existing Formal Credit

Andhra Pradesh: The government has partnerships with private sector banks to increase the MSME credit access by measures such as establishing MSME bank branches in underserved regions.

Gujarat: Gujarat provides support to access collateral free loan under the CGTMSE scheme.

Jharkhand: Jharkhand has created "Industrial Credit Plans" to assess ways to improve credit facilitation in underserved areas

Maharashtra: Maharashtra provides viability gap funding up to INR 0.5 Mn. (~USD 60,000) under the Chief Minister's Employment Generation Programme.

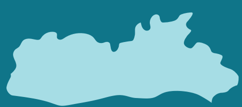
Rajasthan: Rajasthan provides support for the creation of MSME specific bank branches.

The table further provides a comprehensive review of noteworthy state level interventions for improving MSME access to finance:

SN	State	Policy
1.	Andhra Pradesh 	• 3% interest subsidy on fixed capital investment for term loans up to 5 years. • 15% investment subsidy on fixed capital investment of up to INR 0.20 Mn. • Working capital loans of INR 0.02 to INR 0.10 Mn. with a capped interest rate of 6 to 8%. • Seed capital assistance for EV manufacturing units. This includes, 25% of fixed capital investment of up to INR 0.15 Mn., 20% FCI of up to INR 0.40 Mn. for small, and INR 0.50 Mn. for medium industries. • Agreements with private banks to increase MSME credit access. • Loan restructuring mechanisms under the *"YSR-Navodayam"* scheme.
2.	Arunachal Pradesh 	• District industries centres to facilitate access to MSME credit. • Reimbursement of annual interest-80% of up to INR 0.05 Mn. for micro, 50% interest of up to INR 0.15 Mn. for small, and 50% interest up to INR 0.20 Mn. for medium industries. • Interest subsidy of 3% on outstanding working capital loan for all new industries in the state.
3.	Assam 	• Credit availability schemes targeting tea workers. • Project financing (up to 55%) for projects led by the youth under the "***SVAYEM***" Scheme. • Loan subvention scheme of 5% per annum for all the MSME units, with a maximum loan amount of INR 0.10 Mn. under the "Startup Assam" programme.

SN	State	Policy
4.	Bihar 	• Scale up funding under the "Bihar Startup Policy" (2022). A trust run Venture Capital Fund to co-invest in start-ups in Bihar. The trust would also facilitate the listing of companies in SME and national exchanges. • Providing seed grants of up to INR 0.10 Mn. in the form of interest free loans, which is to be repaid in 10 years. • Providing cash subsidies and interest-free loans of total INR 0.10 Mn. under the "*Mukhyamantri Yuva Udyami Yojana*". The cash subsidy is up to INR 0.05 Mn., and interest-free loans of up to INR 0.05 Mn. by state government. • Interest free loan of INR 0.05 Mn. under the "*Chief Minister Scheduled Castes and Scheduled Tribes Entrepreneurs Scheme*".
5.	Chhattisgarh 	• *No notable policy intervention*
6.	Goa 	• Interest subsidy of up to 30% of loan interest, up to INR 0.05 Mn for 2 years, under the state start-up policy. • Priority payment from state departments to MSMEs, with assured payment under 60 days, failing which departments are liable to pay 0.75% penalty per month, under the "*Preferential Purchase Incentives for Micro and Small Enterprises Scheme*" (2008).
7.	Gujarat 	• 25% subsidy on MSME capital investments • 7% subsidy on MSME interest payments. • "*Gujarat Venture Finance Limited*" provide small ticket funding ranging from INR 0.5 Mn. to INR 30 Mn., which is dedicated for pre-series companies, under the "*Gujarat Industrial Policy*" (2020). • State support to access collateral free loan under the CGTMSE scheme.

SN	State	Policy
8.	Haryana 	● 75% reimbursement of up to INR 0.2 Mn. for credit rating when conducted by SIDBI, or other government affiliated credit rating agency under the “Haryana MSME scheme”. ● State contribution of INR 1,000 Mn. to the CGTMSE fund. This is aimed at providing loans of up to INR 10 Mn. for existing Micro and Small enterprises in the state. ● 20% support of up to INR 0.05 Mn. on expenditure incurred for listing on SME exchange after successfully raising funds.
9.	Himachal Pradesh 	● Up to 3% interest cost reimbursement.
10.	Jharkhand 	● 5% interest subsidy for MSMEs, with a maximum limit of INR 0.40 Mn. ● Preparation of “Industrial Credit Plans” and extension of state banking infrastructure for underserved areas to ensure speedy credit facilitation.
11.	Karnataka 	● Interest subsidy scheme for loans at 4% for SC/ST entrepreneurs. ● Start-up funding in the form of a onetime grant up to INR 0.50 Mn. under the Idea2POC scheme. ● Under the “Vishwakarma Loan Scheme”, entrepreneurs pursuing occupation other than traditional occupations, receive financial assistance of up to INR 40,000 and 30% subsidy of up to INR 10000.

SN	State	Policy
12.	Kerala 	● Under the "Entrepreneur Support Scheme", provide subsidies for fixed assets. For general category, the assistance is 15% of capital investment (limited to INR 0.30 Mn.). Youth, women, and SC/ST entrepreneurs are eligible for 25% assistance up to INR 0.40 Mn. ● Under the "Kerala Self Employment for the Registered Unemployed (KESRU) Scheme", provide bank loan of up to INR 0.01 Mn. for unemployed youth to start a business. ● Dedicated Credit Facilitation cell for MSMEs.
13.	Madhya Pradesh 	● Loan of up to INR 0.50 Mn. at 3% interest subsidy for young people under the "Madhya Pradesh Mukhyamantri Udyam Kranti". ● 5% interest subsidy, up to INR 0.50 Mn. over 7 years, under the Madhya Pradesh IT/ITES policy. ● Subsidized loans up to INR 0.10 Mn. under the "Mukhyamantri Yuva Swarozgar Yojana" with15% subsidy, up to INR 0.01 Mn. for general, 30% subsidy, up to INR 0.02 Mn. for women, SC/ST/OBC candidates. ● 7% subsidy of MSME interest payments
14.	Maharashtra 	● Provide up to INR 0.04 Mn. in seed money.15% project cost assistance (+5% for SC/ST/OBC candidates), and interest subsidy of up to 3% on loaned capital under the state seed money scheme. ● Viability gap funding for projects up to INR 0.50 Mn., with subsidized interest rate (2%) under the "Chief Minister's Employment Generation Programme". ● Subsidized loans up to INR 60,000 provided under the "District Industries Centre Loan Scheme". ● Creation of an advisory cell focused on bankruptcy resolution for MSMEs.
15.	Meghalaya 	● *No notable policy intervention*

SN	State	Policy
16.	Mizoram 	• Interest subsidy scheme for up to 4%.
17.	Nagaland 	• Interest free loans up to INR 0.01 Mn. for women entrepreneurs under the "Women Entrepreneurial Development Initiative".
18.	Odisha 	• To foster entrepreneurship and innovations created a "Fund of Funds" under Odisha Startup scheme with an investment of INR 1,000 Mn. for 5 years. • "Odisha Youth Innovation Fund" with the provision to grant INR 50,000 for any new idea, INR 0.01 Mn. for any demonstrative product, and INR 0.03 Mn. for the development of any existing enterprise.
19.	Punjab 	• State support for the CGTMSE scheme in the form of covering 100% guarantee free, up to INR 0.01 Mn. under the "Punjab Industrial and Business Development Policy". • Seed funding grant, up to INR 0.03 Mn. • Provision of funding from INR 1,000 Mn. of state fund, contingent on raising 10% funds raised by VCs. • Venture Capital fund of INR 1,500 Mn., with 10% government equity.
20.	Sikkim 	• *No notable policy intervention*

SN	State	Policy
21.	Tamil Nadu 	● Up to 7% interest subsidy for MSMEs. ● Infusion of INR 10,000 Mn. into the like Tamil Nadu Industrial Investment Corporation Ltd (TIIC) for ensuring increased credit access, under the "MSME Policy 2021". ● "Tamil Nadu Start Up Fund for SC/STs" to promote equity financing. ● Alternative Investment Fund (AIF) called the "Tamil Nadu Emerging Sector Seed Fund" for MSMEs. ● Collaboration with banks, and NBFCs for creating MSME branches, and strengthening the TReDS system.
22.	Telangana 	● INR 20,000 Mn. venture capital fund to enable companies to connect with global investors called the "Telangana Innovation Fund".
23.	Tripura 	● 4% interest reimbursement, up to INR 0.03 Mn. per annum for 5 years, under the "Tripura Industrial Investment Promotion Scheme".
24.	Uttar Pradesh 	● 25% project cost subsidy under the state "One District One Product (ODOP) Scheme". ● The "UP Innovation Fund" of INR 40,000 Mn. ● The "UP Startup Fund" of INR 10,000 Mn. ● Creation of a dedicated "UP Angel Network" for the facilitation of angel funding in the state. ● 50% interest subsidy up to INR 0.25 Mn. for micro units. 60% subsidy for women, and SC/ST entrepreneurs.
25.	Uttarakhand 	● Loans of up to INR 0.05 Mn. for manufacturing, and INR 0.03 Mn. for business and services sector provided under the "Mukhya Mantri Saur Swarojgar Yojana" (Chief Minister's Self Employment Scheme). ● Monthly allowance of INR 10,000 (INR 15000 for women) for start-ups and INR 0.02 Mn. running costs under the "Uttarakhand Startup Policy 2018".

6. POLICY RECOMMENDATIONS

6.1. Main recommendation

1. Formalize the adoption of *Open Financial Networks* for credit, payments, insurance, investments, and tax filing. These *Open Financial Networks* will use digital public goods such as Aadhar, UPI and Account Aggregator (consent-based financial information sharing between the MSME entrepreneurs and financial product manufacturers) to deliver sachet financial services to the underserved. ***Open Network for Digital Commerce*** (ONDC) Financial Services enable credit, insurance and investments and the *Open Credit Enablement Network* (OCEN)[5] helps facilitate credit.

6.2. Novel Financing Channels

2. Promote the use of blended finance instruments[6] for state level MSME ecosystem to ensure that public funds are supported by impact investment and private sector funds, thereby improving operational efficiency.

3. Establish a distress asset fund by respective state governments to reduce the risk profiles of MSME lending for private sector lenders.

6.3. Increasing Access of Existing Formal Credit

4. Promote the use of movable collateral by MSMEs. The Central Registry of Securitization Asset Reconstruction and Security Interest (CERSAI) is currently expanding to include movable assets which can be augmented by states' intervention.

5. Promote the creation of alternate credit institutions such as challenger banks[7], and MSME focused fintech firms.

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[5] **Open Credit Enablement Network** is a set of open standards to facilitate the various aspects of the lending value chain. It creates a common language for collaboration and partnerships between lenders and digital platforms. OCEN, launched as part of IndiaStack in July 2020, aiming to change the way credit is distributed to the end-user by introducing new touchpoints for the distribution of financial services. It empowers new players (such as digital platforms) to play crucial roles in the lending value chain. It is a complete reimagination of the credit ecosystem in India. For details: https://www.pib.gov.in/PressReleasePage.aspx?PRID=1759602

[6] **Blended finance** instruments are classified into two premises: blended within transaction that is, concessional debt and equity or guarantees. The second, blended over time that is, grants or financial support to provide catalytic support (See: https://ibf-uzh.ch/wp-content/uploads/2022/02/Blended-Finance_When-To-Use-Each-Instrument_Phase-1-final.pdf)

[7] **Challenger banks** are digital banks that harness the power of modern technology to provide customers with the financial services they need, anywhere, anytime. These are digital banks without any physical branches, allowing for all services to be access through mobile apps. For details: https://www.banks.com/articles/banking/challenger-banks/

6. Establish technical training programmes to ensure that banks and NBFCs have sector specific knowledge to serve MSMEs.

7. Promote the creation of cooperatives and microfinance lending institutions, which have better geographical reach and community buy-in than commercial banks.

8. Supplement the central government credit guarantee cover by establishing state specific credit guarantee covers.

6.4.Technological Interventions

9. Create a platform to enable voluntary enrollment by MSMEs that are not registered with the GST, EPFO, or ESIC, to allow MSMEs to take advantage of the Open Financial Networks. The platform shall enable:

   - Access to information on various central and state schemes for the MSMEs. Central and State governments could push information on schemes to them.

   - Enable such units to get sachet financing using consent-based financial data-sharing between MSME entrepreneurs and lenders (e.g., banks and NBFCs).

   - The data on the informal sector will help governments to design new and innovative schemes for such units.

About the Author: *Sayantani Satpathi is a Policy Analyst with the Wadhwani Institute of Technology and Policy, Wadhwani Foundation in India.*

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