A Study Of Banks Lending Facilities To MSMEs In Goa

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ABSTRACT

Banks in India by the mere fact are commercial in nature and because of the level of risk involved, are forced to charge high interest rates, require high value collateral from Micro, Small Medium Enterprises (MSMEs), financial statements and bank statements for the facilities sought, which eventually increase the transaction cost for the MSMEs. This has brought in a daunting challenge for banks in the provision of the credit to the MSMEs. The study found that banks selected for this study appear inconsistent in their lending practices for MSMEs in Goa. Marked differences in lending facilities such as fund based facilities, non-fund based facilities and requirements of loan documents were reported between MSME loan managers at bank branches and head offices within banks.

Key Words : Bank Experience, Lending, Bank Facilities, MSMEs, Fund based and Non-fund based facilities and Loan documentation

INTRODUCTION

Fair access to credit and banking services act as a ladder to the development and poverty reduction world over. Access to a bank account gives MSMEs greater control and security over their money, and a loan from a credit organization can be vital in promoting development of an enterprise (Kauffmann, 2010). Banks need to address the needs of these MSMEs so that they can grow and expand and therefore be a major driver in the growth of the Indian economy. Most commercial banks have been hesitant in lending to the MSME sector due to lack of collateral, credit history, financial statements and banking history. Most commercial banks in the recent past have developed different financial products to consumers in business banking, retail banking and MSME banking.

Banks in India by the mere fact are commercial in nature and because of the level of risk involved, are forced to charge high interest rates, require high value collateral from MSMEs,
financial statements and bank statements for the facilities sought, which eventually increase the transaction cost for the MSMEs. This has brought in a daunting challenge for banks in the provision of the credit to the MSMEs. 

In view of the above development, the study attempts to identify the fund based and non-fund based facilities available to MSMEs and the documents required to be submitted to bank by MSMEs in Goa.

**Figure No. 1.1 Classification of fund and non-fund based facilities**

![Diagram]

*Source: Drawn by Researcher*

MSME sector offers good scope for bank finance through its diversified base, backward and forward linkages with other sectors. Risk is also diversified and there are regulatory supports in the form of various subsidies, guarantee cover, technology support and infrastructure support from Central and State Governments.

Credit facilities provided by banks are classified into two categories viz. fund based and non-fund based. The figure 1.1 shows the further classification of selected fund based and non-fund based facilities considered for the analysis.

**Fund Based Facilities**

a. **Loan**

   This is disbursed by way of single debit/stage-wise debits to the account. It is repaid in lump-sum or in instalments. It is called Demand Loan if the repayment period is less than three years. It is called Term Loan in case the repayment is three years and above.

b. **Overdraft**

   When a customer is maintaining a current account, it is allowed to be drawn beyond the credit balance in the account; such a facility is called an ‘Overdraft’ facility. Regular overdraft limits are sanctioned against certain securities.
i. All rules applicable to a current account are applicable to overdraft accounts.

ii. Overdraft is an operational and active account and hence debits and credits are freely allowed.

iii. Interest on overdraft is applied on a daily product basis and debited to the borrowers’ account on a monthly basis. In case of temporary overdraft by borrowers, interest is applied by banks as and when the temporary overdraft is adjusted or at the end of the month, whichever is earlier.

iv. Overdrafts are generally granted against the collateral of government securities, shares and debentures, National Savings Certificates, LIC policies and banks’ own deposits etc. and also on an unsecured basis.

c. **Cash Credit**
   A cash credit is a short term working capital facility provided to MSMEs. Banks establishes a credit limit and allows the customers to borrow money up to a certain limit. Under this system, the customer is allowed a drawing limit against the security of stipulated assets i.e. stocks, book debts etc. It is a running account like a current account which functions with a cheque book facility.

d. **Bills Finance**
   Banks provide Bill finance facilities to customers. Finance is made available to customers against Bills drawn by them on their clients for goods supplied or service rendered. Such bills can be routed through the banker of the buyer for effective control and payment.

e. **Export Finance**
   It is the endeavour of the Bank to give all possible encouragement for promoting exports from the country. Apart from other benefits offered by the Government of India, banks grant export credit on very liberal terms to meet all the financial requirements of exporters.

**Non-Fund Based Facilities**
The credit facilities given by the banks where actual bank funds are not deployed are termed as 'non-fund based facilities'. Letters of credit, Guarantees are examples of non-fund based facilities.
a. Bank Guarantees

Section 126 of the Indian Contract Act, 1872, defines a Contract of Guarantee as a contract to perform the promise or discharge the liability of a third person in case of his/her default. The contract of guarantee has three principal parties which have to perform or discharge the liability.

i. Principal debtor, the person who has to perform or discharge for whose default the guarantee is given.

ii. Principal creditor, the person to whom the guarantee is given for due fulfillment of the contract by the principal debtor. Principal creditor is sometimes referred to as the beneficiary.

iii. Guarantor or Surety is a person who gives the guarantee. Banks come across a ‘Guarantee' in two capacities; one is as a beneficiary i.e. when somebody guarantees the payment of a debt of bank's borrower in case of default. The other one is as a guarantor when the bank itself promises to pay the dues or discharge the liabilities of its customers in favour of a third party. While in the former case, the Bank is the creditor and in the latter case, Bank’s liability is coextensive with that of the debtor.

b. Letter of Credit

Letter of Credit (LC) is a method of settlement of payment of a trade transaction and is widely used to finance the purchase of machinery and raw material etc. It contains a written undertaking given by the bank on behalf of the purchaser to the seller to make payment of a stated amount on presentation of stipulated documents and fulfilment of all the terms and conditions incorporated therein. All Letters of Credit in India relating to the foreign trade i.e., export and import letters of credit are subject to provisions of Uniform Customs & Practice for Documentary Credits’ (UCPDC 600).

Banks may also issue Inland Letters of Credit subject to the provisions of UCPDC and it is, therefore, important that the borrowers should be fully aware of these provisions. The borrowers shall also understand the complete mechanism of Letter of Credit as these transactions will find increasing use in the coming days.

Documentation

Documentation starts with a written loan application with preliminary project report by the borrowers followed by signed loan covenants like, right of set off, right to enforce collateral / securities on default, right to debit account for charges, right to freeze operation on misuse of
facilities, right to receive statements of business like Audited financial statement, Cash flow and fund flow statement etc. NOC from local authorities should also be obtained.

LITERATURE REVIEW

Chera E. D. (2014), in the paper titled “MSMEs Access for Finance in Zambia” examined the level of MSMEs access to Bank Finance in order to determine the demand for and supply of financial services to the MSME sector, and the potential for broadening and deepening existing linkages between the banking community and MSMEs in Zambia. The finding of the study shows that MSME operators understand little about the basic principle of commercial bank lending and borrowing practices. The survey also shows that commercial banks have limited experience with the MSME sector and lacks the knowhow to assess the associated credit risks, and are therefore unwilling to meet the sector’s growing demand for financial services. As far as Banking institutions are concerned, many MSMEs do not understand how to work with the financial institution. As a result, these historical perspectives, both the supply of and demand for MSME financial services are not being adequately addressed in Zambia.

Nishanth P. and Zakkariya K. A., (2014), identified the various barriers faced by MSME units in raising finance and also tried to identify the various sources of finance other than banks. The study was based upon primary data from the MSME owners in Kozhikode District of Kerala. The study found that major portion of respondents (69.89%) availed credit from public sector banks only a meagre portion (2.74%) of respondents availed credit from private sector banks. It is also found that only 11% of the respondents availed multiple loans from banks and 81% of respondents used both owned and borrowed funds in their capital. Further, it was observed that 8.43% of firms use relatives as their sources of borrowed funds and 74.70 % of respondents use a bank as their sources of borrowed fund. From these findings, the study recommended that District Industries Centre must give proper training regarding the maintaining of accounts, getting various licenses and clearances which will help the MSME units to increase the managerial capacity of the owner of these units.

Srinivas K T (2014), studied the financial assistance provided to MSMEs in Karnataka by Canara bank. The data was collected for a period of 5 years and it is analyzed based on the information provided by bank officials and available annual reports. The study found that government is continuously supporting the MSMEs to grow, however, it should consider the present business environment and exposure level of the entrepreneur in the country and focus
should be made on increasing the lending of banks to MSMEs, which are one of the traditional and trusted ways to finance the business.

**Harsha T. and Hegde Desai P. (2015)**, in the paper titled “Lending to Micro Small and Medium Enterprises: An Analysis of Bank Approaches and Risk Perceptions” attempted to identify the approaches used by banks to finance MSME sector thereby finding out whether these approaches differ across banks, type of units and loan types. The study also identifies and evaluates important criteria in different lending approaches. The study found that in Public and Private sector banks the lending is based on the financial data, however, the lending based on the relationship has been given equal importance. For Micro enterprises, the character-based lending has been considered the most important evaluation technique after financials. In character-based lending, Quality of Management has been identified as the most essential factor.

**Allen N. B. and Gregory F. U. (1995)**, examined the role of relationship lending in small firm finance. It examined the price and non-price terms of bank lines of credit extended to small firms. The focus on bank lines of credit allows the examination of a type of loan contract in which the bank-borrower relationship is likely to be an important mechanism for solving the asymmetric information problems associated with financing small enterprises. The study found that the borrowers with longer banking relationships pay lower interest rates and less likely to pledge collateral. These results are consistent with the theoretical argument that relationship lending generates valuable information about borrower quality. The result of the study suggested that the impact on small business lending may be limited because of the value of the relationship associated with bank lending.

**IDENTIFICATION OF RESEARCH PROBLEM**

It is being learned from the literature review that the number of studies have been carried out in the area of banking in India and Abroad. There has been ample research done on the banking sector especially in terms of its lending practices and constraints in providing and managing finance. However, no research has been found in the area of banks lending facilities to MSMEs by banks.

The present study makes an attempt to find the various fund based and non-fund based lending facilities provided to MSMEs across types of banks and the documents required to be submitted to the bank by MSMEs in Goa.
OBJECTIVES OF THE STUDY
The main objective of the study is to analyse the lending facilities provided by banks to MSMEs in Goa. However, the specific objectives of the study are as follows.
1. To study the fund based and non-fund based facilities provided by Banks to MSMEs in Goa.
2. To study the documents required to be submitted to the bank by MSMEs in Goa.

HYPOTHESIS OF THE STUDY
H01(a) – There is no significant difference with regards to fund based facilities provided by banks to MSMEs across type of banks in Goa.
H01(b) – There is no significant difference with regards to non-fund based facilities provided by banks to MSMEs across the type of banks in Goa.
H01(c) – There is no significant difference with regards to loan documents required to be submitted by MSMEs across the type of banks

RESEARCH METHODOLOGY
Universe and Sample Size
There are 41 Commercial banks and 15 Cooperative banks functioning in the State of Goa as on 31st December 2015. These commercial banks have a network of 644 bank branches and cooperative banks have a network of 164 bank branches (Economic Survey, 2015-16, Govt. of Goa). These 41 Commercial banks and 15 Cooperative banks together having a network of 808 bank branches represent the universe of the study.
For the purpose of this research study, a total of 100 bank branches, both from Commercial and Co-operative banks are selected and studied.

Sources of Data
The data source for this part of the area of research is both Primary and Secondary sources. The primary data is derived from the response to the well designed open-ended and close-ended questionnaire administered on Bank Managers. The result of semi-structured interviews conducted on bank managers is used as supplementary data for those obtained from the questionnaire.
Secondary data is collected from the internet, books, research papers, research articles and newspapers.
Period of Study
This part of the study is survey based. The survey was conducted from March 2017 to May 2018. Hence, the period of the survey is considered as period of study.

Data Analytical Tools
The ANOVA test is used to analyse the significant difference in the fund based and non-fund based facilities provided by banks and documents required to be submitted by MSMEs in Goa. Further, fund based, non-fund based facilities and documents required are considered as dependent variables. Whereas, type of banks, as independent variables.

ANALYSIS OF BANKS’ EXPERIENCE IN LENDING TO MSMEs IN GOA
In this part of the study, the banks’ experience in lending to MSMEs in Goa is analyzed with respect to fund based and non-fund based facilities provided to MSMEs by banks. Further, the study analyses loan documents to be submitted by MSMEs.

Sample Size Description
The responses derived from 100 bank branches operating in the State of Goa are used to analyze the experience of banks with respect to the above variables. Table 1.1 gives a description of 100 bank branches selected for this part of the study.

Table No. 1.1: Sample Distribution of Banks

<table>
<thead>
<tr>
<th>Type of Banks</th>
<th>Frequency</th>
<th>%</th>
</tr>
</thead>
<tbody>
<tr>
<td>Private</td>
<td>34</td>
<td>34.0</td>
</tr>
<tr>
<td>Public</td>
<td>52</td>
<td>52.0</td>
</tr>
<tr>
<td>Co-operative</td>
<td>14</td>
<td>14.0</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>100</strong></td>
<td><strong>100.0</strong></td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>District</th>
<th>Frequency</th>
<th>%</th>
</tr>
</thead>
<tbody>
<tr>
<td>North Goa</td>
<td>37</td>
<td>37.0</td>
</tr>
<tr>
<td>South Goa</td>
<td>63</td>
<td>63.0</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>100</strong></td>
<td><strong>100.0</strong></td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Years of Experience in MSME Loan</th>
<th>Frequency</th>
<th>%</th>
</tr>
</thead>
<tbody>
<tr>
<td>Upto 5 years</td>
<td>32</td>
<td>32.0</td>
</tr>
<tr>
<td>&gt;5 years to 10 years</td>
<td>53</td>
<td>53.0</td>
</tr>
<tr>
<td>&gt;10 years</td>
<td>15</td>
<td>15.0</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>100</strong></td>
<td><strong>100.0</strong></td>
</tr>
</tbody>
</table>

*Source: Compiled from Primary Data*

Table 1.1 connotes that out of the 100 bank branches, 52% are public bank branches, 34% are private bank branches and 14% are cooperative bank branches. 63% of the selected bank branches are from South Goa and 37% are from North Goa. Further, it is found that 53% of
the bank branches have 5 to 10 years of experience in MSME loan, 32% have 1 to 5 years of experience and 15% have 10 years and more experience in MSME loans. The study examines if there is a significant difference in banks’ experience with respect to the fund based and non-fund based facilities provided to MSMEs across the type of banks i.e. public sector, private sector and co-operative banks.

ANALYSIS OF BANKS’ EXPERIENCE WITH RESPECT TO FUND BASED AND NON-FUND BASED FACILITIES

Fund based facilities under the study shall include some of the important facilities provided by banks to MSMEs in Goa like term loan, cash credit, overdraft, bill finance and export finance. Some of the important non-fund based facilities provided by banks to MSMEs in Goa such as bank guarantee, letter of credit, bill discounting and buyer credit are considered for the present study. The data used in the study with reference to the above 09 variables has a cronbach’s alpha of 0.741. Since an alpha value of 0.7 is the minimum acceptable standard for demonstrating internal consistency (Kennedy et al, 2002), the data used in the study is reliable. The following hypothesis is framed to test significant difference between the fund based facilities and type of banks in Goa.

**Ho1(a) – There is no significant difference with regards to fund based facilities provided by banks to MSMEs across the type of banks in Goa.**

One way ANOVA test result indicating a significant differences in fund based facilities provided to MSMEs across the type of banks is given in Table 1.2.

**Table No. 1.2: ANOVA result for Fund Based Facilities provided by Banks to MSMEs across Type of Banks.**

<table>
<thead>
<tr>
<th>Type of Banks</th>
<th>Mean Square</th>
<th>df</th>
<th>F</th>
<th>Sig.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Term loan</td>
<td>.042</td>
<td>2</td>
<td>1.425</td>
<td>.245</td>
</tr>
<tr>
<td>Cash credit</td>
<td>.009</td>
<td>2</td>
<td>.225</td>
<td>.799</td>
</tr>
<tr>
<td>Overdraft</td>
<td>.065</td>
<td>2</td>
<td>1.355</td>
<td>.263</td>
</tr>
<tr>
<td>Bill finance</td>
<td>2.402</td>
<td>2</td>
<td>14.390</td>
<td>.000</td>
</tr>
<tr>
<td>Export finance</td>
<td>1.641</td>
<td>2</td>
<td>8.176</td>
<td>.001</td>
</tr>
</tbody>
</table>

*Source: Computed from Primary Data*
Table 1.2 shows the result of one way ANOVA test conducted to analyze significant difference with regard to fund based facilities such as term loan, cash credit, overdraft, bill finance and export finance provided by selected banks in Goa across type of banks. Since the p-value is less than 0.05 indicating significant mean difference exists in the fund based facilities with regards to bill finance and export finance analyzed across type of banks whereas, for term loan, cash credit and overdraft, p-value is more than 0.05 indicating no significant difference exist. Thus, the null hypothesis $H_{0(a)}$ is rejected with respect to bill finance and export finance and accepted with respect to term loan, cash credit and overdraft as a fund based facilities analyzed across type of banks. It can be thus inferred that there is a significant difference in bill finance and export finance as a fund based facilities provided by the selected public sector, private sector and co-operative banks in Goa to MSMEs in Goa. This can cause a hindrance in obtaining working capital for MSME units as bill finance meets the short term requirements of MSME. On the other hand, non availability of export finance means a shortage of short term funds to export oriented units.

$H_{0(b)}$ – There is no significant difference with regards to non-fund based facilities provided by banks to MSMEs across type of banks in Goa.

Table No. 1.3: ANOVA Result for Non-Fund Based Facilities Provided by Banks to MSMEs across Type of Banks, Years of Experience of Banks in Lending to MSMEs and District Wise Location of Banks

<table>
<thead>
<tr>
<th>Type of Banks</th>
<th>Mean Square</th>
<th>df</th>
<th>F</th>
<th>Sig.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Bank guarantees</td>
<td>1.267</td>
<td>2</td>
<td>9.559</td>
<td>.000</td>
</tr>
<tr>
<td>Letter of credit</td>
<td>.846</td>
<td>2</td>
<td>3.533</td>
<td>.033</td>
</tr>
<tr>
<td>Bills discounting</td>
<td>.090</td>
<td>2</td>
<td>.628</td>
<td>.536</td>
</tr>
<tr>
<td>Buyers credit</td>
<td>.492</td>
<td>2</td>
<td>2.612</td>
<td>.079</td>
</tr>
</tbody>
</table>

Source: Computed from Primary Data

The ANOVA test result shown in Table 1.3 indicates that there exists a significant difference with regard to non-fund based facility provided by selected banks in Goa across type of banks, years of experience of banks in lending to MSMEs and district wise location of banks. The p-value for non-fund based facilities like bank guarantees and letter of credit is less than 0.05 and it is significant at 5% level of significance indicating significant mean difference exist among public sector, private sector banks and co-operative banks whereas for bill discounting and buyers credit the p-value is more than 0.05 signifying no mean difference exist among public sector, private sector banks and co-operative banks.
Thus, the null hypotheses $H_{01(b)}$ is rejected with respect to bank guarantees and letter of credit and is accepted with respect to bill discounting and buyers credit. Hence, it can be inferred that, there is a statistically significant difference with regards to bank guarantees and letter of credit as the non-fund based facility provided to MSMEs across type of banks.

The above result indicates that non-fund facilities like bank guarantees and letter of credit are not provided by all the selected public sector, private sector and co-operative banks in Goa. Bank guarantees and letter of credit are important financial instruments, required to transact overseas without availing bank loan. These facilities are usually available to only large enterprises in Goa subject to some conditions including individual bank board policy, customer credential verification and credit appraisal. There is a need to extent these non-fund based facilities to MSMEs in Goa.

ANALYSIS OF BANKS’ EXPERIENCE WITH RESPECT TO LOAN DOCUMENTS REQUIRED TO BE SUBMITTED BY MSMEs

In this part of the analyses, the study covers the experience of banks with respect to loan documents required to be submitted by MSMEs in Goa. The loan documents such as, audited financial statements, cash flow and fund flow statements, project report and NOC from local authorities are some to the important documents required to be submitted by MSMEs to banks. The study analyses the significant difference in the loan documents required to be submitted by MSMEs across type of banks in Goa. The reliability of the data for this part of the study is tested using cronbach’s alpha and the data is found to be reliable with an alpha value of 0.80.

For the purpose of this study the loan documents such as audited financial statement, cash flow and fund flow statements, project report and NOC from local authorities are considered as dependent variables whereas, type of banks, years of experience of banks in lending to MSMEs and district wise location of banks in Goa as independent variables. The one way ANOVA is found to be an appropriate statistical tool to test the significant difference between independent and dependent variables.

The following hypothesis is framed to test the significant difference between independent and dependent variables.
Ho_{1(c)} – There is no significant difference with regards to loan documents required to be submitted by MSMEs across type of banks.

The Table 6.4 below gives the one way ANOVA result for loan documents required to be submitted by MSMEs analyzed across type of banks, years of experience of banks in lending to MSMEs and district wise location of banks.

Table No. 6.4: ANOVA result for Loan Documents Required to be Submitted by MSMEs across Type of Banks, Years of Experience of Banks in Lending to MSMEs and District wise Location of Bank

<table>
<thead>
<tr>
<th></th>
<th>Mean Square</th>
<th>df</th>
<th>F</th>
<th>Sig.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Audited financial statement</td>
<td>.416</td>
<td>2</td>
<td>8.387</td>
<td>.000</td>
</tr>
<tr>
<td>Cash flow and fund flow statement</td>
<td>.039</td>
<td>2</td>
<td>.678</td>
<td>.510</td>
</tr>
<tr>
<td>Project report</td>
<td>.166</td>
<td>2</td>
<td>3.037</td>
<td>.050</td>
</tr>
<tr>
<td>NOC from local authorities</td>
<td>.222</td>
<td>2</td>
<td>1.979</td>
<td>.144</td>
</tr>
</tbody>
</table>

Source: Computed from Primary Data
Table 6.4 shows output from One-way ANOVA using different loan documents as a variable across type of banks. The variance of group is not same as the p-value is less than 0.05, indicating significant mean difference exist in the loan documents with regards to project report and audited financial statement where as for cash flow and fund flow statements p-value is more than 0.05 indicating no significant difference exists across type of banks. Thus, the null hypothesis $H_{0\text{(c)}}$ is rejected with respect to the project report and audited financial statement and it is accepted with respect to cash flow and fund flow statement and NOC from local authorities.

Hence, it can be interpreted that, there is a statistically significant difference with regards to project report and audited financial statement as the loan documents required to be submitted by MSMEs across type of banks. Thus, it can be inferred that, there is no uniformity in the selected private sector, public sector and cooperative banks with regards to different loan documents required to be submitted by MSMEs in Goa.

**CONCLUSION**

The banks selected for this study appear inconsistent in their lending practices for MSMEs in Goa. Marked differences in lending facilities such as fund based facilities, non-fund based facilities and requirements of loan documents were reported between MSME loan managers at bank branches and head offices within banks. As a result, there is no consensus as to whether certain banks are less likely to provide finance than other banks. Co-operative banks are not empowered in their lending decision to MSMEs in Goa and their role in MSME finance is insignificant.

**References**


11. Das Keshab-SMES in India-Issues & Possibilities in times of globalization Chapter-3


