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Challenges Faced by Entrepreneurs: An Empirical Study of India

Sivakumar Venkataramany¹, Balbir B. Bhasin², and Lee Keng Ng³

¹Ashland University, ²University of Arkansas at Fort Smith, ³Curtin University

*Corresponding email: svenkata@ashland.edu¹, balbir.bhasin@uafs.edu²,
lilee.ng@postgrad.curtin.edu.my³

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Abstract

The government of India considers its policy of financial inclusion a compulsion and not a choice. Its sole purpose is to achieve inclusive growth thus ensuring equality of economic opportunities. Entrepreneurs in the Micro, Small and Medium-sized Enterprises (MSMEs) have been identified as potential target for promoting financial inclusion. The need for assisting MSMEs is seen in them engaged in the formation of MNCs of tomorrow. Despite an overwhelming institutional response, India recognizes the need for bringing unregistered entrepreneurs under a supporting microfinance environment. This paper attempts to identify challenges faced by small firms and entrepreneurs, governmental response and possible solutions to their problems through an empirical study of the success factors for entrepreneurs.

INTRODUCTION

Globalization has paved the way for family-owned conglomerates such as the Tata Group become multinational corporations (MNCs) and technology-oriented entrepreneurial start-up firms such as Infosys become global provider of tailor-made business solutions. While technology wave has been responsible for growth, the challenges faced by entrepreneurs remain yet to be fully addressed. This paper attempts to identify challenges faced by small firms and entrepreneurs, governmental response and possible solutions to their problems. The government of India considers its policy of financial inclusion a compulsion and not a choice. Its sole purpose is to achieve inclusive growth thus ensuring equality of economic opportunities. Entrepreneurs in the Micro, Small and Medium-sized Enterprises (MSMEs)¹ have been identified as potential target for promoting financial inclusion. The government has also set up a policy making body known as the National Commission on Enterprises in the Unorganized Sector (NCEUS). Its role is to suggest policies and programmers to address the wide range of issues affecting the productive potential of the large segment of the unorganized micro and small productive units. The need for assisting MSMEs is seen in them engaged in the formation of MNCs of tomorrow [Chakrabarty, 2011]. Policymakers see Microenterprise development projects to serve four major

¹ The MSMEs' original investment in plant, machinery and equipment ranges between \$20,000 and \$2,000,000 to fit into this classification.

objectives: poverty reduction; the empowerment of women; employment generation, and enterprise development as an end in itself. Policymakers of the Reserve Bank of India warn entrepreneurs to beware of four pitfalls. First, products may serve better in a different role from what it was designed for. Secondly, entrepreneurs need to understand the importance of cash flows without focusing on profits. Thirdly, exponential growth raises stress and so, requires keen attention. Lastly, the entrepreneur learns to concentrate when the business brings success.

MSMEs in INDIA: ROLE, SIZE, and CREDIT FACILITIES

Table I presents the important role played by MSMEs in India and their growing importance in the country's progress. Estimates suggest that there are more than 26 million working enterprises in the country employing nearly 60 million laborers. Yet, only 1.5 million units are registered leaving data pertaining to about 24.5 million units out of enumeration.

TABLE I: ROLE of MSMEs in INDIA

Year ending March 31	Production (millions of units)	Value of Production (\$, millions)	Employment (millions)	Value of Exports by Small Scale Industries (\$, millions)	Percentage of Value of Exports to Total Production
1974	0.42	\$9,000.00	3.97	\$500	5.56%
1975	0.50	\$12,475.20	4.04	\$678	5.43%
1976	0.55	\$13,530.00	4.59	\$615	4.55%
1977	0.59	\$13,283.50	4.98	\$857	6.45%
1978	0.67	\$17,642.63	5.40	\$987	5.59%
1979	0.73	\$18,715.82	6.38	\$1,303	6.96%
1980	0.81	\$27,324.00	6.70	\$1,518	5.56%
1981	0.87	\$36,494.88	7.10	\$2,078	5.69%
1982	0.96	\$35,844.48	7.50	\$2,309	6.44%
1983	1.06	\$37,030.00	7.90	\$2,116	5.71%
1984	1.16	\$39,576.73	8.42	\$2,093	5.29%
1985	1.24	\$43,167.40	9.00	\$2,137	4.95%
1986	1.35	\$49,462.71	9.60	\$2,263	4.58%
1987	1.46	\$57,257.58	10.14	\$2,851	4.98%
1988	1.58	\$66,903.55	10.70	\$3,372	5.04%
1989	1.71	\$73,319.27	11.30	\$3,790	5.17%
1990	1.82	\$79,710.75	11.96	\$4,579	5.74%
1991	6.79	\$43,918.42	15.83	\$5,386	12.26%
1992	7.06	\$32,703.57	16.60	\$5,632	17.22%
1993	7.35	\$29,143.94	17.48	\$6,140	21.07%
1994	7.65	\$31,496.67	18.26	\$8,068	25.62%
1995	7.96	\$38,905.39	19.14	\$9,258	23.80%
1996	8.28	\$44,159.69	19.79	\$10,903	24.69%
1997	8.62	\$47,269.98	20.59	\$11,056	23.39%
1998	8.97	\$50,374.44	21.32	\$11,958	23.74%
1999	9.34	\$50,023.59	22.06	\$11,642	23.27%
2000	9.72	\$53,945.94	22.91	\$12,508	23.19%
2001	10.11	\$57,195.80	24.09	\$15,278	26.71%
2002	10.52	\$59,184.62	24.93	\$14,938	25.24%
2003	10.95	\$65,057.95	26.02	\$17,773	27.32%
2004	11.40	\$79,331.65	27.14	\$21,249	26.79%
2005	11.86	\$95,654.54	28.26	\$27,690	28.95%
2006	12.34	\$112,447.04	29.49	\$33,935	30.18%
2007	26.10	\$156,652.99	59.46	\$40,309	25.73%
2008	27.28	\$196,506.65	62.63	\$50,202	25.55%
2009	28.52		65.94		
2010	29.81		69.54		

Source: Ministry of Micro, Small & Medium Enterprises, Government of India

Unregistered MSMEs are not desirous of cooperating with data collection as they fear that information might be leaked to the regulators and bureaucrats². They have thus voluntarily chosen to be operating in a world of financial exclusion denying themselves privileges of credit, export & import license, marketing support, financial literacy tools, and a nurturing ecology. MSMEs contribute to national income, provide employment opportunities especially to the village artisans and rural people, and prevent economic concentration in the hands of a few. The labor intensity in the MSME sector is higher than in the MNCs. So, the government agencies at the federal and state levels treat this sector as a priority. Entrepreneurship thrives with access to credit which paves way for empowerment. India's overwhelming response in favor of institutionalized lending to SMEs is a focused effort [Venkataramany & Fox, 2009].

A wide range of financial institutions exist in the country to provide credit to various sectors of the economy. These include (not counting the branches or affiliates) 183 commercial banks, 133 regional rural banks (RRBs), 13,014 non-banking financial companies, and 1,853 urban cooperative banks. In addition to these sources of credit, short-term rural credit at the grass root level is emphasized through 31 state co-operative banks, 367 district central co-operative banks (DCCBs), 108,779 primary agricultural cooperatives. State cooperative and agricultural rural development banks (20) and primary cooperative and agricultural rural development banks (727) serve long term credit needs in rural India. Table II shows the volume and share of credit extended by scheduled commercial banks to MSMEs.

TABLE II: CREDIT ASSISTANCE BY COMMERCIAL BANKS to MSMEs

Year	Number of Accounts (millions)	Outstanding Credit	Ratio of Credit to SMEs to Total Credit
2010	8.5	\$ 80,509.11	13.40%
2011	9.3	\$107,660.67	9.90%

Source: The Reserve Bank of India Annual Report, August 25, 2011

Security based credit has proved to be a major constraint since the late 1960s as it relies upon collateral and guarantees. The current shift in the paradigm to resource-based credit (evaluation of cash flows discounted at the cost of credit) is dynamic and focused on the entrepreneur. Besides, the infrastructure needs improvement in the areas of lending by financial institutions, technical skills development programmes, assistance with technological up-gradation, marketing, consulting and capacity building. Only 5% of the MSMEs seek credit from commercial banks thus, leaving the remaining 95% reliant on self-finance. While major players have joined the network of multinational corporations, the small units tend to be either self-employed or part-timers or those catering to ancillary business units. Little development has taken place in decades in the adoption of technology due to lack of financial resources, skill and awareness.³ Liberal credit guarantee facilities are also made available by the government to facilitate smooth credit assistance to entrepreneurs. For instance, 85% of credit in default of a total bank loan of \$10,000 to an SME and 80% of credit in default of a total loan of \$100,000 accorded to women entrepreneurs are unprecedented.

² Goel, Deepak, "MSMEs not co-operating with us during data collection for 4th MSME Census": <http://www.smetimes.in/smetimes/face-to-face/2008/May/27/msmes-not-co-operating-with-us-deepak-goel.html>

³ <http://www.smetimes.in/smetimes/editorial/2012/Jan/31/technology-adoption-an-achilles-heel-indian-smes80001.html>

CHALLENGES FACED BY THE MSMEs

While the government fulfills its responsibility in terms of ecology by providing a congenial climate for growth, the entrepreneurs need to start accessing all the available channels for development. Registration of business enterprises may add to the tax burden leading to an increase in prices and eventual losses, the entrepreneurs have to assert their right to be taxed only to qualify for numerous privileges, promotional programmes and incentives. The benefits obviously exceed the costs. In the end, these entrepreneurs do not need to operate in a world of informal economy any more. Small firms can manage their operations during growth but, are forced to access bank credit during lower business activity [Manna, 2009].

The MSMEs' primary problem lies in their production and marketing of their products. They have limited scope in advertising and marketing research. They lack the necessary financial resources to face competition from large firms, both domestic and foreign. Inadequate infrastructure, inability to secure long-term funding for the purchase of plant, machinery, and equipment pose a huge threat against survival during a growth stage. Shortage of working capital leads to paucity of raw materials and value adding components. They do not have the ability to adopt modern methods of organization, recruit experts, and competitive managers. Technology obsolescence, managerial inadequacies, delayed payments, poor quality, incidence of sickness, lack of appropriate infrastructure, marketing network, raw materials, credit, technology human resource, infrastructure, managing exports, and increasing competition are identified by the government as common challenges for MSMEs.

GOVERNMENT'S RESPONSE

Entrepreneurship Development Programmed (EDPs) set up by the government aim to assist new entrepreneurs in setting up micro and small enterprises. Skill development programmes (SDPs) and entrepreneurship-cum-skill development programmes (ESDPs) are also being organized by various public and private training institutions. The Ministry of Micro, Small and Medium Enterprises regularly collects data on MSMEs engaged in manufacturing and services. The data is analyzed to understand the constraints and challenges faced by the MSMEs amidst opportunities available to them. The results are used for policy research and designing appropriate strategies and measures of intervention by the Government. Micro, Small and Medium Enterprises Development Act, 2006 has been enacted to facilitate the promotion and development of MSMEs. It provides the first-ever legal framework for recognition of the concept of 'enterprise' which comprises both manufacturing and service. De-reservation of products in the MSMEs is aimed at providing opportunities for technological upgradation, promotion of exports and economies of scale, with a view to encourage modernization in the sector. The total number of items reserved for exclusive manufacture in the micro and small scale sector is at present 35. The National Manufacturing Competitiveness Programme (NMCP) has been launched to provide support to the manufacturing sector. Credit Linked Capital Subsidy Scheme (CLCSS) was launched to facilitate technology upgradation by upfront capital subsidy to small, micro and medium enterprises.

METHODOLOGY

India is still a factor-driven economy in Asia along with Iran, Philippines, and Vietnam while China, Indonesia, Malaysia, Thailand, and Turkey have transformed themselves into efficiency-driven economies. Global Entrepreneurship Monitor considers the following twelve factors for entrepreneurial success: the availability of financial resources, public policies supporting entrepreneurship, taxes or regulations encouraging SMEs, programs assisting SMEs, training in creating or managing SMEs, programs incorporated within the higher education system, national research and development that lead to new commercial opportunities for SMEs, property rights, commercial, accounting and other legal and assessment services and institutions that support or promote SMEs, levels of change in markets from year to year, freedom to enter markets, ease of access to physical resources, social and cultural norms that encourage increase of personal wealth. Table III displays the pattern of growing success factors for entrepreneurs in India.

TABLE III: Twelve Factors of Entrepreneurial Success in India

Year	2007	2012	2013	2014	2015
Financing for entrepreneurs	3.37	3.09	2.82	3.11	5.74
Governmental support and policies	2.73	2.92	1.89	3.00	5.50
Taxes and bureaucracy	2.31	2.18	1.84	2.43	3.94
Governmental programs	2.42	2.79	2.05	2.94	4.52
Basic-school Entrepreneurial Education and training	2.12	1.92	1.50	2.33	4.11
Post-school entrepreneurial education and training	2.91	2.73	2.42	3.09	5.09
R&D Transfer	2.89	2.54	1.94	2.86	4.29
Commercial and professional infrastructure	3.99	3.10	2.95	3.40	4.96
Internal market dynamics	3.02	3.13	3.51	3.45	5.72
Internal market openness	3.12	2.85	2.49	2.87	4.75
Physical and services infrastructure	4.07	3.71	3.68	3.96	6.15
Cultural and social norms	3.41	3.20	2.69	3.43	5.45

Source: Global Entrepreneurship Monitor

Financing is the key ingredient for success of entrepreneurs and how it is being impacted by the other eleven factors is the methodology of our analysis. Table IV includes the correlation matrix among these twelve variables.

TABLE IV: Correlation Matrix for Factors for Consideration for Financing To Entrepreneurs

	Financing	Govt Support	Taxes	Govt Programs	Education & Training	Post-school Training	R&D Transfer	Commercial Infrastructure	Market Dynamics	Market Openness	Physical Infrastructure	Cultural-Social Norms
Financing	1.000											
Govt Support	0.793	1.000										
Taxes	0.705	0.773	1.000									
Govt Programs	0.792	0.846	0.809	1.000								
Education & Training	0.721	0.645	0.646	0.672	1.000							
Post-school Training	0.740	0.715	0.649	0.772	0.752	1.000						
R&D Transfer	0.853	0.791	0.757	0.880	0.745	0.803	1.000					
Commercial Infrastructure	0.836	0.710	0.701	0.791	0.717	0.820	0.821	1.000				
Market Dynamics	0.647	0.614	0.453	0.502	0.494	0.572	0.581	0.558	1.000			
Market Openness	0.837	0.776	0.777	0.837	0.749	0.813	0.857	0.870	0.577	1.000		
Physical Infrastructure	0.775	0.723	0.730	0.787	0.578	0.758	0.799	0.832	0.641	0.812	1.000	
Cultural-Social Norms	0.758	0.691	0.680	0.702	0.715	0.799	0.738	0.746	0.615	0.774	0.715	1.000

Data for the aforesaid twelve factors for 62 countries for the period between 2007 and 2015 is analyzed to understand the path to success for entrepreneurs. Our hypotheses are presented below:

Hypothesis 1 (overall):

$$\text{Financing} = \alpha (\text{constant}) + \beta_1 (\text{governmental support}) + \beta_2 (\text{taxes}) + \beta_3 (\text{government programs}) + \beta_4 (\text{entrepreneurial education}) + \beta_5 (\text{post-school training}) + \beta_6 (\text{R\&D transfer}) + \beta_7 (\text{commercial infrastructure}) + \beta_8 (\text{market dynamics}) + \beta_9 (\text{market openness}) + \beta_{10} (\text{physical infrastructure}) + \beta_{11} (\text{cultural and social norms})$$

Hypothesis 2: (India)

$$\text{Financing} = \alpha (\text{constant}) + \beta_1 (\text{governmental support}) + \beta_2 (\text{taxes}) + \beta_3 (\text{government programs}) + \beta_4 (\text{entrepreneurial education}) + \beta_5 (\text{post-school training}) + \beta_6 (\text{R\&D transfer}) + \beta_7$$

(commercial infrastructure) + β_8 (market dynamics) + β_9 (market openness) + β_{10} (physical infrastructure) + β_{11} (cultural and social norms) + β_{12} (dummy variable for India)

Hypothesis 3 (other countries):

Financing = α (constant) + β_1 (governmental support) + β_2 (taxes) + β_3 (government programs) + β_4 (entrepreneurial education) + β_5 (post-school training) + β_6 (R&D transfer) + β_7 (commercial infrastructure) + β_8 (market dynamics) + β_9 (market openness) + β_{10} (physical infrastructure) + β_{11} (cultural and social norms) + β_{12} (dummy variable for other countries)

Table V presents the results of the regression analysis of the data for our hypotheses.

TABLE V: Regression Results for Financing To Entrepreneurs (2007-2015)

Dependent Variable: Financing	Model 1 (overall)	Model 2 (India)	Model 3 (Other Countries)
Constant	-0.153 (-2.295)*	-0.149 (-2.247)*	0.266 (1.752)*
Government Support	0.219 (5.619)***	0.210 (5.414)***	0.210 (5.414)***
Taxes	-0.071 (-2.085)*	-0.061 (-1.809)*	-0.061 (-1.809)*
Government Programs	-0.023 (-0.455)	-0.013 (-0.267)	-0.013 (-0.267)
Education and Training	0.096 (2.308)*	0.100 (2.408)*	0.100 (2.408)*
Post-school Training	-0.230 (-5.264)***	-0.221 (-5.079)***	-0.221 (-5.079)***
R&D Transfer	0.366 (6.813)***	0.358 (6.715)***	0.358 (6.715)***
Commercial Infrastructure	0.328 (7.495)***	0.325 (7.483)***	0.325 (7.483)***
Market Dynamics	0.093 (3.964)***	0.094 (4.036)***	0.094 (4.036)***
Market Openness	0.118 (2.167)*	0.106 (1.963)*	0.106 (1.963)*
Physical Services Infrastructure	0.002 (0.070)	0.005 (0.161)	0.005 (0.161)
Cultural and Social Norms	0.119 (3.764)***	0.113 (3.571)***	0.113 (3.571)***
India Dummy		0.415 (3.072)**	
Other Countries Dummy			-0.415 (-3.072)**
Adjusted R ²	0.835	0.838	0.838
Number of observations	471	471	471

t-statistics appear in parentheses for each variable;

* = significant at 90% confidence level

** = significant at 95% confidence level

*** = significant at 99% confidence level

DISCUSSION OF RESULTS

Our analysis indicates that financing for entrepreneurs is significantly dependent upon government support for entrepreneurs, favorable policies of taxes and regulations, education, training programs beyond formal education, intellectual property rights, presence of commercial infrastructure, market dynamics, market openness, and norms based upon cultural and social values. The negative sign for the highly significant variable

of the availability of post-school training programs for entrepreneurs emphasizes the need for entrepreneurial education in the first place. The variable for the availability of government sponsored programs turned out to be insignificant thereby explaining the wasteful resources of the government, the lack of knowledge of entrepreneurs in accessing and utilizing such programs, and the inability of the government to propagate the information. The analysis produced similar results in our separate analyses in the context of India and in that of the other countries.

CONCLUSION

Corporate entrepreneurship is shown as the prescriptive method to increase competitiveness in large organizations in the era of globalization [Bhardwaj, Sushil & Momaya, 2007]. The challenges are similar for both real production and service sectors. Suitable policies will help India's service sector shape the nation into a knowledge based economy [Jauhari, 2007]. The protective environment that shielded India's MSMEs is now withdrawn in the era of liberalization and they are exposed to cross-border competition [Kulkarni, 2008] and so policy changes are necessary. A strong commitment to internationalization and the ability to leverage human capital influence the international success of Indian SMEs [Javalgi & Todd, 2011]. Imparting fundamental skills is a critical factor in mentoring entrepreneurs [Manimala, 2006]. India stands out as an example in policy-making decisions for several emerging economies, particularly in Southeast Asia [Venkataramany & Bhasin 2010]. The lack of confidence in Indian entrepreneurs in countering foreign competition stems from a lack of flexibility and bureaucratic obstacles [Rajan, 2009]. Once these shortcomings are addressed, India will become and remain a global hub.

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