



Inclusive Growth through Access to Finance in Service Sector: A Policy Brief on Nano Enterprises in Pune

Introduction:

Businesses with annual revenues ranging from Rs 10 lakhs to 1 crore demonstrate resilience and offer promising growth opportunities. Understanding the specific dynamics and challenges of this segment is crucial. In rural or semi-rural areas, self-employed individuals with lower incomes often receive support from self-help groups and microfinance networks, while banks primarily focus on serving the higher end of the micro enterprise sector. However, nano entrepreneurs, who are perceived as urban and relatively affluent, often receive inadequate attention in policy frameworks, leading to a misconception that they are less vulnerable. It is essential to highlight their obstacles and provide them with the necessary resources to unleash their full potential.

Maharashtra, particularly Pune, holds the top position in India for registered micro businesses under the Udyam scheme, with Pune having the highest number of registered micro enterprises in the district, contributing to 13% of all such businesses in the country. These enterprises play a significant role in Maharashtra's employment, representing 25.9% of total employment, with the service sector dominating the micro-business segment at both the national (68%) and state (71%) levels. Therefore, deAsra Centre of Excellence in Nano Entrepreneurship, at the Centre for Excellence in Entrepreneurship & Development (CEED) at the Gokhale Institute of Politics & Economics conducted a survey among small businesses in the service sector in Pune, with an annual turnover ranging between Rs 10 Lakh and 1 Crore. The study was based on in-depth interviews with more than 500 randomly selected nano entrepreneurs to understand their unique business challenges.

This policy brief aims to highlight the challenges identified in access to finance in the survey study and present actionable policy recommendations to address these obstacles effectively. By implementing the suggested measures, policymakers, financial institutions, and stakeholders can create an enabling environment that supports the growth and sustainability of nano enterprises, fostering economic development at the grassroots level.

Study Findings:

The study revealed that a significant majority of respondents, comprising 92.5%, rely on self-funding and borrowing from friends and family as their primary source of financing for their businesses. This pattern of self-funding and informal finance remains consistent across various business segments, irrespective of factors such as gender, education, or age. It is evident that nano entrepreneurs predominantly depend on

informal sources of finance, including personal networks. Surprisingly, this trend persists regardless of gender, annual turnover, business sector, or formal education level. The study further highlights that a significant proportion of women entrepreneurs, approximately 46%, encounter challenges when seeking investments. Despite the availability of numerous banks in Pune, nano entrepreneurs exhibit reluctance in applying for bank loans. This exposes a critical gap in the current system and the government's efforts towards financial inclusion and lending support to priority sectors. Consequently, a fundamental policy change becomes imperative to address this issue effectively. Some of the significant challenges in access to finance discovered through the survey were:

- Lacked sufficient collateral to secure the desired loan amount, which hindered their access to finance.
- Loan application challenges such as uncertainty about obtaining the desired loan amount
- Nano entrepreneurs prefer informal sources of credit, such as friends and family, due to either lacking the necessary documentation or wanting to avoid submitting it when applying for bank loans
- Formal sources of finance entailed high interest rates, possibly influenced by the strict interest and repayment terms associated with such sources

Policy Recommendations

Bank Mitra and Bank Sakhi for Urban Nano Entrepreneurs: Urban nano entrepreneurs often encounter difficulties when seeking loans from traditional banks due to various reasons. They may lack the necessary documentation required by banks or be unfamiliar with the complex loan application processes. As a result, they may turn to informal sources of credit, which can be costly and less reliable. Bank Mitra and Bank Sakhi programs aim to bridge this gap by extending the reach of formal banking services to urban areas and specifically targeting micro-businesses with turnover less than 2 Crore. These programs, which have already been successful in rural areas through self-help group networks, can be adapted and implemented in urban settings. Bank Mitra refers to individuals or entities acting as banking agents or representatives, while Bank Sakhi refers to female banking agents. These intermediaries work closely with urban nano entrepreneurs, providing them with guidance, assistance, and support in accessing bank loans. They simplify the loan application process, assist in documentation, and facilitate communication between entrepreneurs and banks. By introducing Bank Mitra and Bank Sakhi programs, urban nano entrepreneurs gain easier access to formal financial services. They can benefit from lower interest rates, improved loan terms, and a more structured lending process. This promotes financial inclusion, encourages formalization of businesses, and reduces reliance on costly informal credit sources.

Use of digital ledger apps: Facilitating financial literacy and increasing access to credit through innovative lending by connecting fin-tech with banks: Digital ledger apps play a significant role in connecting fin-tech platforms with traditional banks. Fin-tech companies leverage advanced technologies, such as artificial intelligence and data analytics, to develop innovative lending models. These models assess the creditworthiness of nano entrepreneurs based on alternative data sources, such as their digital transaction history, online sales records, and customer reviews. By integrating digital ledger apps with banking systems, fin-tech companies can provide a seamless and efficient lending experience for nano entrepreneurs. This integration enables quick loan application processes, streamlined document verification, and faster loan disbursement. It helps to overcome the traditional barriers faced by nano entrepreneurs, such as lack of collateral or formal credit history, by considering their digital footprint and business performance. The use of digital ledger apps in facilitating financial literacy and connecting fin-

tech with banks leads to increased access to credit for nano entrepreneurs. They can access loans tailored to their specific needs, receive competitive interest rates, and benefit from flexible repayment terms.

It is also important to consider several other interventions that could play a role in catalyzing better access to finance for the nano segment. Firstly, introducing solid fringe benefits for Udyam Registration, such as free capacity building, digital training, and membership in market-linked associations, can incentivize registration and indirectly facilitate access to finance by providing resources and support. The provision of free capacity building and digital training equips nano entrepreneurs with essential skills and knowledge to manage their businesses effectively. This can improve their financial literacy, business acumen, and ability to present their business plans and financial statements to lenders and investors. When entrepreneurs demonstrate a solid understanding of their business operations and financial management, it instills confidence in financial institutions and makes them more likely to extend financial support.

Secondly, the use of digital ledger apps can promote financial literacy and increase credit accessibility by connecting fin-tech with banks, enabling innovative lending practices. Online platforms that match and connect Indian SMEs with global companies can provide assessment and ranking services, improving the quality and value of nano enterprises and potentially opening doors to finance opportunities.

Additionally, implementing gradation and accreditation systems for service sector businesses, recognized by the government, can rationalize pricing and identify high-quality services, which can aid in accessing finance. Gradation and accreditation systems can also help rationalize pricing in the service sector. With official recognition, businesses can differentiate themselves based on their quality and value proposition, rather than engaging in price competition. This enables businesses to command fair prices for their services, which is attractive to lenders as it indicates a higher potential for sustainable profitability and repayment capacity. Furthermore, accreditation may also open up additional avenues for financing, including equity investments, venture capital, and strategic partnerships.

Lastly, establishing business turnaround support centers can provide comprehensive assistance to SMEs, including scaling up support, indirectly contributing to improved access to finance. By offering scaling up support, these centers help SMEs enhance their business operations, expand their market presence, and improve their financial performance. This, in turn, strengthens their creditworthiness and makes them more attractive to lenders and financial institutions. When SMEs demonstrate a solid growth trajectory and financial stability through the support received from business turnaround centers, they become more likely to access various forms of finance. Lenders and investors are more willing to provide loans, credit lines, or equity investments to businesses that have a clear plan for growth and a track record of successfully implementing strategies to improve their operations.

It is essential to prioritize the inclusion and support of nano entrepreneurs to unlock their full potential and ensure a more inclusive and vibrant economy. Therefore, the policy recommendations provided in this brief aim to assist policymakers in creating an enabling environment that supports and promotes the growth of nano enterprises through improved access to finance.