India Exim Bank

Promoting Exports from the MSME SECTOR

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Export-Import Bank of India

Occasional Paper No. 227

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India Exim Bank's Occasional Paper Series is an attempt to disseminate the findings of research studies carried out in the Bank. The results of research studies can interest exporters, policy makers, industrialists, export promotion agencies as well as researchers. However, views expressed do not necessarily reflect those of the Bank. While reasonable care has been taken to ensure authenticity of information and data, India Exim Bank accepts no responsibility for authenticity, accuracy or completeness of such items.

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Executive Summary

The Micro, Small, and Medium Enterprises (MSME) sector in India serves as a backbone of the economy, as also the bedrock of entrepreneurship and innovation in the country. As per the National Sample Survey (NSS) 73rd round, conducted by National Sample Survey Office, Ministry of Statistics and Programme Implementation, there were 633.88 lakh unincorporated non-agriculture MSMEs in the country engaged in different economic activities during 2015-16[1]. Further, as per data from the Udyam Portal, there were 2.4 crore registered MSMEs in India, as of April, 2024.

MSMEs contribute significantly to various facets of the economy, including employment generation, economic output and exports. As per the latest information from the Ministry of Statistics and Programme Implementation, MSMEs contributed to 29.2 percent of India's Gross Domestic Product (GDP) during 2021-22. The share of MSMEs in the manufacturing output of India during 2021-22 stood at 36.2 percent.

Contribution of MSMEs to Exports

MSMEs serve as crucial drivers of exports, contributing substantially to India's foreign exchange earnings. As per the Ministry of MSME, Government of India (GOI), the share of exports of select MSME-related products in India's merchandise exports during 2022-23 was 43.6 percent.

As per data from the Directorate General of Commercial Intelligence and Statistics (DGCIS), exports by MSMEs is estimated at US$ 127.6 billion during

[1] Excluding those MSMEs registered under (a) Sections 2m(i) and 2m(ii) of the Factories Act, 1948, (b) Companies Act, 1956 and (c) construction activities falling under Section F of National Industrial Classification (NIC) 2008.

2023-24, accounting for about 29.2 percent of India's total merchandise exports during the year[2]. The principal commodity of gold and other precious metal jewellery accounted for the largest share in total exports by MSMEs in 2023-24, estimated at 6.2 percent. Other top exported products by MSMEs include pearl, precious, semiprecious stones (share of 4.9 percent), marine products (4.3 percent), readymade garments (RMG) of cotton including accessories (4.1 percent), products of iron and steel (3.6 percent), and basmati rice (3.6 percent), among others. In terms of direction of exports, the USA was the topmost destination for MSME exporters in India, accounting for a share of 19.7 percent in total MSME exports during 2023-24, followed by UAE (share of 9.8 percent), China (4.8 percent), the UK (3.7 percent), and Germany (3.1 percent), among others. State-level analysis indicates that Gujarat is the largest state of origin for MSME exports from India, accounting for a share of 21 percent in total MSME exports in 2023-24, followed by Maharashtra (share of 19.2 percent), Tamil Nadu (9.8 percent), UP (8 percent), and Haryana (7.5 percent), among other states.

Considering the pivotal role of MSMEs in India's exports, achieving the ambitious exports target of US$ 2 trillion by 2030 set by the GOI would hinge on unleashing the full potential of this sector. This would entail addressing the specific challenges faced by these exporters and creating an enabling environment for their growth. Against this backdrop, the study discusses the challenges faced by Indian MSMEs in their export endeavours, the opportunities for growth and the strategies to alleviate the challenges.

ANALYSIS OF CREDIT FLOWS TO THE MSME SECTOR

Credit flows to MSMEs by Scheduled Commercial Banks

Scheduled commercial banks (SCBs), comprising public sector banks (PSBs), private sector banks (PVBs) and foreign banks (FBs), are among the largest sources of credit for MSMEs in India. Analysis of data on the number of MSME loan accounts in SCBs indicates that the number of MSME loan accounts

[2] This data is based on the active Udyam status of the MSMEs and valid IEC status. However, indirect export through merchant traders is not included in this data.

across all categories of SCBs has nearly halved from 420 lakh accounts in 2020-21, to 213 lakh accounts in 2022-23. The decline in total MSME loan accounts could be partly attributed to MSME units becoming larger with the rise in economic activity, thereby crossing the threshold of ₹ 250 crore turnover as per the new definition of MSMEs[3]. It is noteworthy that despite the decline in the number of MSME loan accounts in SCBs, the credit flows to MSMEs by SCBs, has exhibited a steady growth over the recent year. During the period between 2018-19 to 2022-23, outstanding credit to MSMEs by SCBs has recorded a compound annual growth rate (CAGR) of 10.6 percent to reach an outstanding value of ₹ 22.6 lakh crore as on March 2023, up from ₹ 15.1 lakh crore as on March 2019.

Credit to MSMEs has particularly accelerated since 2020-21, recording an average annual growth rate of nearly 12.6 percent during 2020-21 to 2022-23. Incentives provided by the Emergency Credit Line Guarantee Scheme (ECLGS), coupled with lower Gross Non-performing Assets (GNPA) ratios have helped in boosting credit to MSMEs[4]. Further, increase in overall credit to the MSME sector can also be attributed to the addition of wholesale and retail trade in the MSME category since July 2021.

Since 2018-19, growth in MSME credit extended by PVBs far exceeded that of PSBs. During 2018-19 to 2022-23, MSME loans by PVBs recorded a robust CAGR of 17.9 percent, despite the sharp decline in the number of MSME loan accounts in PVBs during recent years. Meanwhile, MSME loans by PSBs and foreign banks also recorded healthy CAGRs of 5.4 percent and 6.3 percent during the same period.

Trends in Credit Disbursement to MSMEs

Data from the RBI highlights a steady growth in credit disbursements by SCBs to MSMEs over the recent year. During 2020-21 to 2022-23, credit disbursements to MSMEs by SCBs recorded a robust CAGR of 24.1 percent,

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[3] SBI Research (2023), "The rise of the prodigal: How the MSME Sector is charting a new story post pandemic and simultaneously getting bigger"

[4] Ibid.

to reach an estimated ₹ 17.0 lakh crore in 2022-23. Among MSMEs, credit disbursements to micro enterprises held the highest share of 37.9 percent in total credit disbursements to MSMEs by SCBs during 2022-23, followed by small enterprises, with a share of 34.2 percent. It is noteworthy that over the recent years, credit disbursements to medium enterprises have registered a stronger CAGR of 45.2 percent during 2020-21 to 2022-23, while that of small and micro enterprises witnessed CAGRs of 19.2 percent and 17.2 percent, respectively during the same period. As a result, the share of medium enterprises in total credit disbursements to MSMEs witnessed a sharp increase to reach 27.9 percent in 2022-23, up from nearly 20.4 percent share in 2020-21.

Data from SIDBI-TransUnion CIBIL also shows a healthy growth in disbursements of working capital term loans to MSMEs over the recent year. During 2020-21 to 2022-23, disbursements of working capital term loans to MSMEs recorded a robust CAGR of 22.3 percent, to reach an estimated ₹ 9.8 lakh crore in 2022-23. It is noteworthy that the average loan size for small enterprises has declined from ₹ 47.2 lakhs in Q4-FY22 to ₹ 44.2 lakhs in Q4-FY23, while that of medium enterprises has declined from ₹ 1.1 crore in Q4-FY22, to ₹ 98.4 lakh in Q4-FY23. As per SIDBI-TransUnion CIBIL report, the decline in average loan size is attributable to the conservative approach by lenders, particularly banks, their low-risk appetite and the higher cost of collections at both public sector and private banks.

Credit Flows to MSMEs through NBFCs

Apart from SCBs, NBFCs also play a crucial role in meeting the credit needs of MSMEs. Between end-March 2021 and end-March 2023, NBFC's outstanding credit to MSMEs recorded a robust CAGR of 31 percent to reach ₹ 2.7 lakh crore as on end-March 2023. Loans by NBFCs to MSMEs registered a strong growth of 42.9 percent in 2022-23, which is more than three times the growth in lending by SCBs to MSMEs. The co-lending framework for priority sector lending has facilitated flow of credit by NBFCs to the MSME sector, leveraging on the low cost of funds of banks and greater reach of NBFCs[5].

[5] Ibid.

Under the framework, banks are permitted to co-lend with all registered NBFCs (including Housing Finance Companies) based on a prior agreement.

It is noteworthy that MSMEs engaged in services accounted for nearly two-third of NBFC credit to the MSME sector, while the share of MSMEs engaged in industries stood at 33.4 percent. Within industrial sector, the share of NBFC credit to MSMEs is concentrated in the micro and small enterprises segment, which jointly accounted for a share of 78.1 percent in total NBFC's outstanding credit to MSMEs in the industries sector as on end-March 2023.

Credit Flows to MSMEs through Other Financial Institutions

In addition to SCBs and NBFCs, there are several other financial institutions like Urban Co-operative Banks (UCBs), Regional Rural Banks (RRBs), Small Finance Banks (SFBs) and Small Industries Development Bank of India (SIDBI), that also cater to the MSME sector. As on end-March 2023, outstanding credit to MSMEs by these institutions[6] jointly amounted to ₹ 2.45 lakh crore, accounting for a share of nearly 8.8 percent in total outstanding credit to MSMEs.

Total credit flows to the MSME sector by all financial institutions is estimated at ₹27.8 lakh crore, as on end-March 2023. After SCBs and NBFCs, UCBs accounted for the highest share of 4.8 percent in total outstanding credit to MSMEs as on end-March 2023, followed by RRBs and SFBs, with shares of 1.8 percent and 1.6 percent, respectively in the total outstanding credit to MSMEs as on end-March 2023.

UCBs, RRBs, and SFBs are required to lend a substantial portion of their credit to priority sectors, which includes MSMEs. It is interesting to note that UCBs, RRBs and SFBs have not only exceeded their priority sector lending targets in the recent years, but have also developed a niche in priority sector lending areas, particularly MSME. The better delivery of credit to MSMEs by these institutions could be due to factors such as better outreach of RRBs and UCBs and increasing implementation of digital lending models by SFBs.

[6] Comprising UCBs, RRBs, SFB and SIDBI. For SIDBI, only direct lending to MSMEs has been considered in this analysis.

MSME Financing through Trade Receivables Discounting System (TReDS)

In additional to traditional credit, Trade Receivables Discounting System (TReDS) also plays a crucial role in meeting the short-term financing needs of MSMEs. During 2018-19 to 2022-23, the number of invoices financed under TReDS recorded a remarkable CAGR of 82.2 percent, while the amount financed under TReDS has witnessed an even greater CAGR of 90.2 percent, to reach ₹ 76.6 thousand crore in 2022-23. The success rate of financing through TReDS has also been remarkably high since 2018-19, and stood at around 93.9 percent in 2022-23, indicating the significance of the platform as a reliable source for MSMEs in meeting their working capital needs.

Delinquencies in MSME Loans

There has been a steady decline in both the value and share of gross NPAs in MSME loans by SCBs over the recent year. In absolute terms, the Gross NPAs in MSME loans by SCBs have declined from ₹ 1.64 lakh crore as on end-March 2019, to ₹ 1.32 lakh crore as on end-March 2023. The share of GNPAs in total MSME loan outstanding has also declined from 10.8 percent as on end-March 2019, to 5.8 percent as on end-March 2023. This is indicative of the steady improvement in asset quality in MSME lending portfolio of SCBs, partially attributable to better end-to-end tracking due to increasing use of digital tools.

GOVERNMENT SCHEMES FOR MSMEs IN INDIA

The Study also highlights the government schemes aimed at boosting the MSME sector and traditional industries in India, including initiatives for addressing finance related issues, supporting marketing and capacity building efforts, and strengthening the existing infrastructure.

Some of the major initiatives by the GOI for improving access to finance include the Credit Guarantee Fund Trust for Micro and Small Enterprises (CGTMSE) Scheme to address the critical challenge of collateral requirements; the Interest Equalisation Scheme for Pre- and Post-shipping Rupee Export

Credit to address the cost burden on export credit and enhance the global competitiveness of MSMEs; and the Credit-Linked Subsidy Support under the Prime Minister’s Employment Generation Programme (PMEGP) to incentivise the creation of new micro-enterprises in the non-farm sector.

Initiatives by the GOI for enhancing market access for MSMEs include the Market Development Assistance (MDA) under International Cooperation Scheme of the Ministry of MSME, for facilitating MSMEs’ participation in international trade events and providing market intelligence; the Capacity Building of First Time MSE Exporters (CBFTE) sub-scheme under the International Cooperation Scheme for reimbursement of costs associated with registration with export promotion councils, export insurance premiums, and quality certification to first time exporters; the Procurement and Marketing Support (PMS) Scheme for enhancing market access and capacity building of MSMEs; and the MSME Sustainable (ZED) Certification scheme for promoting the adoption of zero defect and zero effect manufacturing practices.

Some GOI schemes are also strengthening the infrastructure for MSMEs. This includes as the Micro & Small Enterprises - Cluster Development Programme (MSE-CDP) scheme for enhancing the infrastructure and collective capabilities of MSE clusters; and the Scheme of Fund for Regeneration of Traditional Industries (SFURTI), for revitalising traditional industries by organising artisans into collectives, enhancing production and adding value to their products.

While the GOI is undertaking a wide array of interventions for supporting MSMEs, it would be crucial to learn from the best practices from successful global models, in order to further bolster the support provided to MSMEs.

GLOBAL BENCHMARKING - CASE STUDIES OF FINANCING PROGRAMMES AND INCENTIVES

The Study attempts to map the various financing programmes and incentives offered by Governments across select countries. Analysis indicates that the support provided to SMEs across different markets exhibits some similarities, on account of the common challenges faced by the sector across countries. Globally, countries have implemented measures such as subsidised loans and credit guarantees, to alleviate the financing challenges for SMEs. Further, some countries have specific programmes for alleviating export marketing related challenges. There is also a focus on promoting entrepreneurship and innovation. Apart from these commonalities, there are some differentiated programmes and initiatives that address specific local needs in countries.

China

China supports MSMEs through initiatives like the SME Development Fund, which encourages innovation and technological development through equity investments and grants. Alongside, policies like "Made in China 2025" seeks to upgrade the manufacturing capabilities of Chinese MSMEs by promoting the adoption of advanced technologies and processes. Further, the Export-Import Bank of China has introduced innovative finance models such as risk-sharing model for government-bank cooperation called Yuan Mao Dai, support to cross-border logistics through Wu Liu Dai (logistics loans) and joint lending business plan to explore new ways to develop policy-based inclusive finance. Programmes like business incubators and technology parks also foster a supportive ecosystem in the country. The government has also extended targeted fiscal and logistical support, particularly for pandemic-affected service industries, through 43 policy measures until December 2024.

The USA

One of the primary pillars of support for MSMEs in the USA is the Small Business Administration (SBA). The 7(a) Loan Program of SBA offers loans to SMEs that might not qualify for traditional bank financing. Alongside, the 504 Loan Program, provides long-term, fixed-rate financing for major fixed assets such as land and buildings. Another notable initiative is the SBA's Paycheck Protection Program, which mitigated the impact of COVID-19 by offering forgivable loans. Further, Small Business Innovation Research (SBIR) program of the SBA provides funding and facilitates partnerships between small businesses and federal agencies, leading to commercial successes and creation of high-tech jobs . Additionally, tax incentives, Manufacturing Extension Partnerships, and Manufacturing USA programmes are some of the other measures to support MSMEs in the USA. The US Export-Import Bank also supports international trade by MSMEs through a wide array of risk protection and financing tools.

Japan

In Japan, the Japan Finance Corporation (JFC), provides long-term loans, credit guarantees, and equity financing tailored to small businesses. The Credit Guarantee Programme of JFC reduces lending risks for financial institutions, making credit more accessible to MSMEs. Another key institution is the Japan External Trade Organization (JETRO), which offers comprehensive support to MSMEs through the "Export Support Programme". Under the programme, JETRO offers subsidies for participating in international trade fairs, as also organises business matching events and trade missions. Further, the Small and Medium Enterprise Agency (SMEA) in Japan administers the "Monozukuri Subsidy", under which grants are provided to manufacturing MSMEs for investments in innovative production technologies and processes. MSMEs in rural and economically disadvantages areas are also supported through initiatives like the Regional Revitalisation Support Programme, which provides financial assistance to MSMEs engaged in projects that contribute to economic revitalisation of the regions.

Indonesia

The Indonesian government actively supports MSMEs' internationalisation through the Directorate General for National Export Development (DGNED), which offers market research, export training, and participation in global trade fairs. Programmes like the Export Coaching Program equip MSMEs with the skills needed to navigate international markets.

Indonesia also has programmes such as Kredit Usaha Rakyat and Jamkrindo, to enable access to affordable credit for MSMEs. Further, Indonesia Eximbank provides financing and guarantees aimed at supporting export-oriented MSMEs. MSMEs in rural and economically disadvantages areas are also being supported through the One Village One Product (OVOP) programme. Indonesia Exim Bank's "Go Export Village" programme supports the initiative through training, mentoring and assistance in production facilities.

Brazil

The Special Agency for Industrial Financing (FINAME), a subsidiary of the Brazilian Development Bank (BNDES) provides long-term loans at favourable interest rates for acquiring domestically produced machinery and equipment. The BNDES Automático programme supports investment projects of MSMEs in all sectors, mainly related to construction, expansion, or reform of facilities. For international trade, the PROEX programme managed by BNDES offers pre- and post-shipment financing and export credit insurance. BNDES has also developed a digital platform, Canal MPME to facilitate access to information for borrowers, automate procedures for loan applications and offer a range of online services. Apart from this, the Brazilian Trade and Investment Promotion Agency (Apex-Brasil) offers export training and business matchmaking services. The PEIEX (Export Qualification Programme) of Apex-Brasil equips MSMEs with the knowledge to develop export strategies and explore new markets.

South Africa

One of the key institutions supporting access to finance for MSMEs in South Africa is the Small Enterprise Finance Agency (SEFA), which offers loans, credit guarantees, and equity financing tailored to the needs of MSMEs. Programmes like the SEFA's Direct Lending Programme provide loans to MSMEs for various purposes at favourable interest rates and with flexible repayment terms. SEFA also administers the Credit Guarantee Scheme, which helps MSMEs secure loans from private financial institutions by guaranteeing a portion of the loan amount.

The Industrial Development Corporation (IDC) also extends financial support to industrial MSMEs. The Gro-E Youth Scheme of IDC particularly extends support to young entrepreneurs.

The South African government also prioritises export promotion for MSMEs through the Export Marketing and Investment Assistance (EMIA) Scheme, which covers costs related to participation in international trade fairs, exhibitions, and business missions. Further, MSMEs are provided training and technical assistance under the South African Export Development and Promotion (SAEDP) Programme to facilitate entry into global markets and increase export revenues. The Export Credit Insurance Corporation (ECIC) also offers export credit insurance and pre- and post-shipment financing, for MSMEs to fulfil export orders and expand into international markets effectively.

CHALLENGES AND STRATEGIES

Analysis in the study highlights that only 1 percent of Udyam-registered MSMEs are currently exporting. This highlights the substantial untapped export potential in the sector. However, MSMEs face a myriad challenges that hinder their growth and sustainability.

Results of the Survey of MSMEs

With the objective of understanding the needs of the MSME sector and identifying the key obstacles faced by them, Exim Bank conducted a survey of MSMEs across various industries. As per the survey, lack of information on export opportunities is one of the major challenges faced by Indian MSMEs in exports, with 51.4 percent of the respondents considering this as a challenge. Lack of relationship with foreign distributors, agents and customers is another hindrance for Indian MSMEs in realising the export potential, with 49.5 percent of respondents considering this as a challenge. MSMEs also reported significant difficulties in marketing their products internationally (44.9 percent of respondents), which is essential for gaining visibility and finding customers. Around 43 percent of respondents also faced challenges in obtaining the necessary financial support for exports. Navigating the complex regulatory frameworks of different export markets can also be a barrier, with nearly 28.0 percent of the respondents highlighting challenges in complying with regulations in export markets

Focus Products and Markets for Diversification of MSME Exports

Analysis of MSME's export patterns indicates a significant concentration on resource-intensive and low value-added products in MSMEs' exports basket. For instance, only 3 out of the top 10 products (non-oil) exported by MSMEs in FY24 were high value-added/ high technology intensive products, while the rest were either resource-intensive or low value-added goods. In contrast, 6 out of 10 top non-oil exported products from India were high value-added/ high technology intensive products during the same period. Enhancing production capacities in higher value-added products would be crucial for a substantive increase in exports from the MSME sector and imparting resilience to India's exports basket.

An attempt has been made to identify focus products and destinations for diversification of MSME exports from India. Some of the segments identified for product diversification are lab grown diamonds, organic aquaculture, processed cereal products, spice oleoresins, biosimilar, synthetic textiles and technical textiles, strategic and defence electronics, parts and components for electric vehicles, among others.

An attempt has also been made to identify markets for enhancing exports from MSMEs. An analysis of the share of MSMEs in India's non-oil exports to major markets indicates that several of India's key destinations for non-oil exports remain under-tapped by MSMEs. These include destinations such as the USA, Saudi Arabia, Hong Kong, the Netherlands, Italy, Singapore, Belgium, among others. There is substantial scope for MSMEs to enhance their exports in these top markets.

Strengthening Marketing and Branding Efforts

As per the survey, one of the most pressing concern for MSMEs is marketing. MSMEs face marketing-related problems due to their limited size and scale of operation. Intense competition from established brands is a challenge for MSMEs. Further, unlike large enterprises that can allocate substantial budgets to marketing and branding activities, MSMEs often operate on tight financial margins with limited marketing budgets.

Digital marketing offers a cost-effective way for MSMEs to reach a broad audience and compete with larger enterprises. However, nearly 11.9 percent of MSMEs in the survey indicated inadequate knowledge about this. Clearly, several MSMEs in India are unable to keep pace with the technological advancements that can ease their marketing efforts.

To effectively support the growth and international competitiveness of MSMEs, the GOI could consider consolidating and streamlining existing schemes such as the market development assistance and the market access initiative. A unified, streamlined programme would be easier for MSMEs to navigate and access. The consolidated scheme could be made exclusively available to MSMEs, to ensure that the resources are focused on those businesses that need them the most. Moreover, the scope of consolidated scheme could be extended beyond just participation in events and conducting market studies, to include funding support for critical areas such as brand building, preparation of marketing materials, etc.

Alleviating Financing Related Challenges for MSMEs

Analysis in the Study indicates that nearly 53 percent of the respondent MSMEs found it challenging to obtain financing for their businesses from the banking sector. Majority of the respondent MSMEs found high interest rates as the topmost challenge in securing financing. Besides high interest rates, some of the other key challenges faced by MSMEs in securing financing included lack of collateral, complex application process, lack of awareness about products and lack of proper documents.

Rationalising Interest Rates for MSMEs

With a view to rationalise interest rates for MSMEs, the Study recommends reinstating the Interest Subvention Scheme, which was operational until March 2021. Under the scheme, a 2 percent interest subsidy was extended to GST-registered MSMEs on fresh or incremental loans up to ₹100 lakh, covering both working capital and term loans. The scheme was facilitated through SIDBI, which acted as a nodal agency to channel the benefits to various lending institutions. Reviving this programme would provide immediate relief to MSMEs by lowering borrowing costs, enabling them to enhance their capital expenditure and production capacity, thereby generating surplus for exports.

Additionally, the government could consider reinstating the 5 percent interest equalisation support for MSME exporters that was available under the Interest Equalisation Scheme (IES) for Pre- and Post-Shipment Rupee Export Credit. The benefit has been reduced to 3 percent for MSME exporters. This would help reduce the cost of export credit and enhance the global competitiveness of MSME exporters. Further, ensuring the timely extension of IES without retrospective approvals would prevent operational disruptions for banks and improve the predictability of benefits for exporters.

Enhancing Availability of Working Capital for MSMEs

Approximately 70 percent of the debt requirements of MSMEs pertain to working capital, yet only a quarter of this demand is met through formal financial channels. With a view to bridge the unmet need for working capital from formal sources by MSMEs, the Export-Import Bank of India (Exim Bank) has proposed a Working Capital Guarantee Programme (WCGP), in line with similar schemes implemented by Export Credit Agencies in other countries such as the USA, the UK, and Canada. Under the programme, Exim Bank would extend guarantees to banks for enhancing credit flow to MSMEs. The Bank is currently awaiting approval from the RBI for the programme. The Government of India could provide a backstop facility to enable Exim Bank to consider higher guarantee amount and scale up the support under the programme.

Strengthening the CGTMSE Scheme

The CGTMSE is an important scheme for facilitating collateral-free loans for micro and small enterprises. However, the number of guarantees issued under the scheme remains substantially low when compared to the total number of MSMEs in the country. As of December 2023, only 11.02 lakh guarantees, amounting to ₹1.36 lakh crore, had been approved under the scheme, while there are nearly 2.9 crore registered MSMEs in India. Expanding the scheme's coverage to include medium enterprises could improve access to credit, allowing more MSMEs to scale their operations and contribute to exports.

Support for Scaling up Exim Bank's Trade Assistance Programme to Bridge the Financing Gaps

The global trade finance gap has widened to US$ 2.5 trillion in 2022. Recognising the challenges, Exim Bank has developed a new, first-of-its-kind trade facilitation initiative in India, the 'Trade Assistance Programme' (TAP) to address the trade finance gap, particularly in the MSME sector. The Bank has so far supported over 640 export transactions under TAP till date across 43 countries, leading to nearly US$ 2.4 billion worth of incremental exports by more than 150 exporters, in 42 cities across 16 states of India. With the slowing demand in advanced economies, support under TAP will gain further salience for diversification of exports across non-traditional markets. TAP is increasingly receiving enquiries for supporting exports to high-risk countries. Given that Exim Bank's risk appetite is constrained due to the possibility of high default risk and challenging forex situation in select countries, the Government of India may consider risk sharing under TAP through a designated fund. Further, assistance from Indian embassies abroad could be instrumental in facilitating introductions, providing market insights and fostering collaborations with potential overseas banking partners, to enhance the reach and effectiveness of the programme. Moreover, to amplify the reach and impact of the programme, the GOI could encourage scheduled commercial banks in India to partner with Exim Bank under TAP.

Creating Awareness for Leveraging Existing Credit Support Schemes

Analysis in the Study indicates that more than two-third of the MSME respondents were unaware of the existing support schemes for MSMEs. As per Exim Bank's discussion with banks and exporters, MSMEs lack awareness about crucial schemes such as the CGTMSE. There is a need to create awareness about CGTMSE, portal for 59-minute loans from PSBs, and FinTech enabled innovative financing solutions such as the GST Sahay portal, through outreach activities and awareness campaigns.

Strengthening Receivables Financing for Trade Finance

Fostering a Robust Operating Environment for International Trade Financing Services (ITFS) Platform

The Study notes that the flow of receivables financing to MSMEs through the TReDS platform recorded a robust growth in the recent years. On similar lines, there is a need for strengthening receivables financing in cross-border transactions. To that end, the ITFS platform was launched by the International Financial Services Centres Authority (IFSCA) in 2021, to facilitate trade financing for exporters and importers through services such as import and export factoring, reverse factoring, forfaiting, and credit guarantees. There is substantial scope for enhancing the scale and quantum of export finance from ITFS. To enhance ITFS's impact, the Study suggests fostering a supportive operating environment with simplified processes and transparent regulations to attract financial service providers and international participation. Additionally, the platform must focus on educating and supporting MSMEs, many of which have limited technological capabilities, to ensure continued participation and success.

Regulatory Easing for Fostering Factoring Services from IFSC

Exim Bank has established its subsidiary, Exim Finserve, in GIFT City to bridge financing gaps for exporters through trade finance products, with a focus on factoring. Factoring is a valuable tool for MSME exporters as it provides a combination of three essential services to exporters: receivables financing, coverage of the risk of non-payment, and management of accounts receivable. It is particularly beneficial for MSME exporters as it is primarily based on the quality of accounts receivable rather than collateral. It also has the potential to improve export competitiveness as it enables exporters to offer competitive credit terms to their buyers.

However, India's international factoring volumes are significantly lower than China's, highlighting the need to improve the regulatory and operational framework for factoring services in GIFT City. Currently, IFSCA guidelines restrict factoring service providers from using credit insurance from outside the IFSC, making insurance expensive and inadequate. To align GIFT City with leading global financial hubs, IFSCA could consider allowing overseas insurance for factoring entities or permitting domestic insurers to cover transactions within the IFSC. These changes would support the growth of factoring in GIFT City and attract more businesses to establish a presence there.

Interest Subvention for Factoring

Globally, several governments provide interest equalisation support to enable competitive credit for exporters and bolster export competitiveness. In India as well, the Interest Equalisation Scheme for Pre and Post Shipment Rupee Export Credit, reduces the cost of borrowing through banking channels for exporters. Similar interest subvention support can be extended for export factoring, at least till the time substantial revenues are generated by the factoring business in India and economies of scales are achieved. This would help reduce the cost of international factoring for exporters and enable more MSMEs to benefit from export factoring.

Promoting Fintech for Supply Chain Finance

Fintechs and alternative finance providers can play a crucial role in bridging trade finance gaps, particularly through collaborations in supply chain financing (SCF). Scaling SCF volumes through fintechs requires technological capabilities, resources, and awareness. GIFT City offers a conducive regulatory environment for innovation, with its IFSCA FinTech Sandbox allowing testing of blockchain-based SCF solutions. To further boost SCF adoption, IFSCA could introduce incentive schemes focused on supply chain finance. Besides, IFSCA could consider developing a multi-funder platform to encourage participation in SCF by lenders who may otherwise be unable or unwilling to develop their SCF platforms, including commercial banks. IFSCA could develop an enabling regulatory framework for SCF and advise and support commercial banks in developing new products.

Capacity Building of MSME Exporters

Several MSMEs face challenges in meeting international quality standards and understanding the complex regulations, certifications, and packaging requirements. To that end, the Study suggests strategies for capacity building of MSMEs to enable them to integrate into global value chains.

Reimbursement of Certification Costs

The cost of certifications is a significant barrier for MSME exporters, especially small enterprises, to enter international markets. To alleviate this, the Government of India has launched the CBFTE scheme, which reimburses costs related to registration, insurance, and testing for first-time exporters. There is a need to expand this scheme to include all MSMEs. Besides, to improve market access for existing exports, State Governments could also consider introducing a scheme for providing refund of expenses incurred by MSMEs on obtaining standards and certifications. This could help make certifications more affordable, particularly for high-cost certifications like CE and US-FDA, thus boosting MSME competitiveness in global markets.

Decentralisation of Product Testing and Quality Management for MSMEs

The Ministry of MSME currently operates four accredited testing centres and seven MSME testing stations across India, but the varying certification needs of different sectors make decentralisation essential. To meet export standards, the Study suggests development of sector-specific testing facilities in MSME clusters.

Institutional Mechanism for Supporting MSME Exporters

As part of the District Exports Hubs (DEH) initiative, the GOI has already established State and District-level Export Promotion Councils in all States/ districts, which are playing a crucial role in bolstering export activities. To further strengthen the institutional mechanism, MSME internationalisation centres could be set up across key export clusters. Such centres may provide end-to-end support to MSME firms for conducting exports, including logistics support, guidance for trade compliance, order and lead management services, finance and insurance related consultancy etc .

Capacity Building/Awareness Programmes for MSME Exporters

Creating awareness among exporters about export procedures, regulations and standards related to various products is a crucial aspect of enhancing exports for MSMEs. In this regard, the GOI, in collaboration with State Governments, could conduct regular district-level workshops/ seminars/ conferences on various aspects of international trade and covering different sectors. Industry associations and agencies, in coordination with State-level Export Promotion Councils and the proposed MSME international centres can help in organising such programmes. Training and awareness drives could also be conducted in major production hubs for dissemination of information on certifications required for exports, including process of application and support provided by the government.

Creation of a Single-Window Trade Information Portal for Exporters

MSMEs often struggle with accessing comprehensive and reliable information on export opportunities, procedures, and government support programmes. To address this, a unified, user-friendly platform should be created to centralise all relevant trade-related information. In this regard, the Trade Connect e-Platform has been recently launched by the Government of India to serve as a one-stop portal offering detailed export information and streamlining the export processes for MSMEs. The Study suggests that this portal could be further enhanced on similar lines as the USA's International Trade Administration (ITA) portal, which not only provides information on trade trends, tariffs, export procedures, documentation, and trade agreement related information, but also provides comprehensive market research, and information on financing options for exports. In addition, the ITA portal also provides compliance and risk management support, access to networking events and support for grievance redressal.

Leveraging e-Commerce for Enhancing MSME Exports

Promoting Exports of GI Products through e-Commerce

India has comparative advantage in certain products and focusing on these products for e-commerce exports would enable the sellers to garner greater revenues and establish their brand identity. The DGFT's e-Commerce Exports Handbook for MSMEs identifies a list of such products where India has comparative advantage, that may be targeted by MSMEs aspiring to export through e-commerce mode. In addition to these products, the Government of India could also consider promoting Indian products with Geographical Indications (GI) through e-commerce by collaborating with leading e-commerce platforms. A similar approach is being adopted by the Government of Italy, which has signed a memorandum of understanding with the e-commerce platform Amazon, to promote Italian products that have a protected designation of origin (PDO) or protected geographical indication (PGI). The collaboration also aims to strengthen the protection of such products sold on the e-commerce platform, through identification and reporting of violations of intellectual property rights of products with PDO or PGI, as well as through checking unfair practices related to sharing of incorrect product information. The agreement also allows Amazon to promptly remove counterfeit products. Similar collaboration could be considered by the Government of India to help improve consumer confidence on quality and authenticity of GI products, and enhance sales and exports of these products through e-commerce mode.

Expanding the ITPS to Cover more Countries

The International Tracked Packet Service (ITPS) is a competitive service for transmission and delivery of packets. The ITPS has been designed by India Post to meet the cross-border shipping requirements of e-commerce exporters including MSMEs, small businesses and merchants, and promote exports using local post offices. India Post already provides the service for 41 destinations. However, several of India's top export destinations are currently not covered under the ITPS. Going forward, key export destinations like Bangladesh, Saudi Arabia, the UK, could also be considered for collaboration under the ITPS. Besides, there is also a need to consider rationalising the postage fee charged under the ITPS. Currently, the ITPS provides shipping solution to exporters for packages weighing up to 2 kgs, along with pick-up and volume-based discount to contractual customers. The postage fee for such packages stands at an average of nearly ₹ 341 for the first 50 gms and an average of ₹ 32.8 for every additional 50 gms , exclusive of GST. This could be cost prohibitive for small value exporters. As postal e-commerce routes are used predominantly for small value exports by MSMEs, the government could consider rationalising/ waiving the postage fee for MSME exporters.

Promoting ONDC for International Trade

The Open Network for Digital Commerce (ONDC) is an initiative of the Department for Promotion of Industry and Internal Trade (DPIIT), Ministry of Commerce and Industry. The platform creates new opportunities and limits e-commerce monopolies by supporting MSMEs and small traders to get on online platforms across various segments. The network has successfully conducted its first cross-border transaction in January 2024, with Singapore and is progressing towards scaling up this initiative. In order to scale up ONDC beyond the borders of India, the Study suggests a few key enablers, such as i) seamless cross-border payment settlements; ii) robust grievance redressal systems; iii) awareness about country-specific guidelines; and iv) collaboration with international e-commerce platforms.

Addressing Regulatory Complexities

Currently, there are host of regulations in India for e-commerce, involving multiple government agencies and departments governing different aspects of e-commerce operations. For instance, the Consumer Protection Act, 2019 and the Consumer Protection (e-Commerce) Rules, 2020 deal with the responsibilities and liabilities of the sellers and e-commerce platforms to protect the consumers. Meanwhile, the Competition Act, 2000 keeps in check anti-competitive practices. Besides these, the Sale of Goods Act, 1930, the Legal Metrology Act, 2009, the Foreign Exchange Management Act, 2000, and the Payments and Settlement Systems Act, 2007, among others, also govern various aspects of e-commerce. Such multiplicity of regulations and regulatory bodies increases compliance burden and may affect the ease of doing business, particularly from the perspective of MSME e-commerce players. A single, comprehensive e-commerce policy is therefore important for supporting growth of e-commerce exports. While the DPIIT has released the draft e-Commerce Policy in 2018-19, the policy is still in its draft stage and yet to be adopted. There is a need to expedite the finalisation of the national e-commerce policy. The policy should include short-term and long-term strategies to promote the growth and development of the sector, in line with domestic priorities and international best practices. Regulations related to e-commerce must also be aligned with the national policy to avoid ambiguity and conflicting regulations.

Enhancing Access to Export Credit for e-Commerce Exporters

In recent representations made to the Government of India, firms had highlighted the non-availability of pre-shipment and post-shipment export credit for e-commerce exporters. As per Exim Bank's discussion with select commercial banks, the main challenge with export credit to e-commerce players is the unavailability of confirmed orders/Letters of Credit. Besides, it was also noted that the banks found it challenging to conduct due diligence of buyers as also to ascertain the nature of sales (domestic/overseas), as the transactions are done online. Further, banks also found it challenging to track the realisation of export proceeds in e-commerce, as it may not be routed through traditional banking channel. In order to address the issues of e-commerce exporters in availing export credit, it would first be important to distinguish between the traditional modes of trade and e-commerce, and their distinct financing requirements. Unlike the traditional mode of transaction, where payment is usually made after the receipt of goods by the buyer, e-commerce exports typically allow upfront payments to sellers through payment gateways at the time of placing the order. Moreover, the frequency of shipments is higher in e-commerce exports as compared to offline exports. Additionally, a seller may forward deploy inventory to an overseas warehouse, and a single shipment may get sold over a period of months, with the seller receiving multiple remittances against one shipping bill. These complexities increase the documentation burden on e-commerce exporters and also lead to reconciliation problems. Therefore, a thorough assessment of the financing requirement of e-commerce exporters, perhaps through a Working Group approach, would be crucial to highlight specific challenges faced by e-commerce exporters in obtaining export credit and design tailored financing programmes for e-commerce exporters. It is noteworthy that, the Export-Import Bank of Thailand (Exim Thailand) has introduced a separate financing programme viz. e-Commerce Financing Loan. Under the programme, Exim Thailand extends short term revolving credit (including pre and post-shipment) for a period of up to 10 months for business operators who trade through e-commerce platforms viz. Alibaba, Thai Trade and Amazon. On similar lines, a specific programme could also be designed to support e-commerce exporters in India by scheduled commercial banks.

CONCLUSION

MSMEs play a vital role in India's exports, contributing around 29.2 percent of merchandise exports in 2023-24. Despite their importance, MSMEs face several challenges in participating in exports, including lack of information, difficulty in building relationships with foreign distributors, marketing challenges, financial constraints, and regulatory compliance issues. Addressing the challenges faced by MSMEs requires a holistic approach with interventions targeted at supporting marketing efforts, bridging financing gaps, bolstering export capacity, strengthening of support programmes and institutions, and promoting innovative modes such as e-commerce.

1. Overview of MSME Sector in India

INTRODUCTION

The Micro, Small, and Medium Enterprises (MSME) sector in India serves as a backbone of the economy, as also the bedrock of entrepreneurship and innovation in the country. With the vast network of enterprises spread across various industries and geographical regions, the MSME sector contributes significantly to the country's economic development. The sector plays a crucial role in generating employment opportunities, especially in rural and semi-urban areas, thereby alleviating poverty and fostering socio-economic empowerment. With their ability to generate jobs at a rapid pace, these enterprises play a crucial role in addressing the challenge of unemployment and underemployment. The widely dispersed nature of MSMEs positions them as key drivers for balanced regional development and inclusive growth. Serving as ancillary units to large industries, MSMEs contribute significantly to inclusive industrial growth, complementing the efforts of major player.

MSME CLASSIFICATION

MSMEs in India are defined based on their investment in plant and machinery or equipment, as well as turnover. The earlier classification was amended in 2020, with the new classification coming into effect from 1st July, 2020. The earlier criteria of classification of MSMEs under MSMED Act, 2006 was based on investment in plant and machinery / equipment. It was different for manufacturing and service units. It was also very low in terms of financial limits. As a result, businesses were reluctant to expand and invest in better technology or increase their workforce because they feared losing the benefits associated with MSME classification. This led to under-utilisation of potential and stagnation. The adverse incentives for scaling up and accessing new technologies meant that MSMEs were often unable to compete effectively with larger businesses, both domestically and internationally.

The latest classification of MSMEs is presented in Table 1.1. The distinction between manufacturing and service sectors has been removed. Also, a new criterion of turnover has been included in addition to the criterion of investment in plant and machinery. The new criteria is expected to catalyse growth of MSMEs, as they can expand without concerns about losing the status of being an MSME and associated benefits. It has also been decided that the turnover with respect to exports will not be counted in the limits of turnover for any category of MSME units whether micro, small or medium.

Table 1.1: Revised Definition of Micro, Small and Medium Enterprises

Parameters	Micro	Small	Medium
Investment in Plant and Machinery	< ₹ 1 Crore	< ₹ 10 Crore	< ₹ 50 Crore
Annual Turnover	< ₹ 5 Crore	< ₹ 50 Crore	< ₹ 250 Crore
No. of MSMEs (Based on NSS data)	6.3 Crore	3.3 Lakh	5 thousand
No. of MSMEs (Based on Udyam data as on 12 April 2024)	2.4 Crore	6.1 Lakh	55.9 thousand

Source: Ministry of Micro, Small and Medium Enterprises, Exim Bank Research

MSMEs IN INDIA

As per the National Sample Survey (NSS) 73rd round, conducted by National Sample Survey Office, Ministry of Statistics & Programme Implementation during 2015-16, there were 633.88 lakh unincorporated non-agriculture MSMEs in the country engaged in different economic activities (196.65 lakh in Manufacturing, 230.35 lakh in Trade and 206.85 lakh in Other Services)[7]. Micro sector had 630.52 lakh estimated enterprises, accounting for more than 99 percent of the total number of MSMEs. Small sector

[7] excluding those MSMEs registered under (a) Sections 2m(i) and 2m(ii) of the Factories Act, 1948, (b) Companies Act, 1956 and (c) construction activities falling under Section F of National Industrial Classification (NIC) 2008.

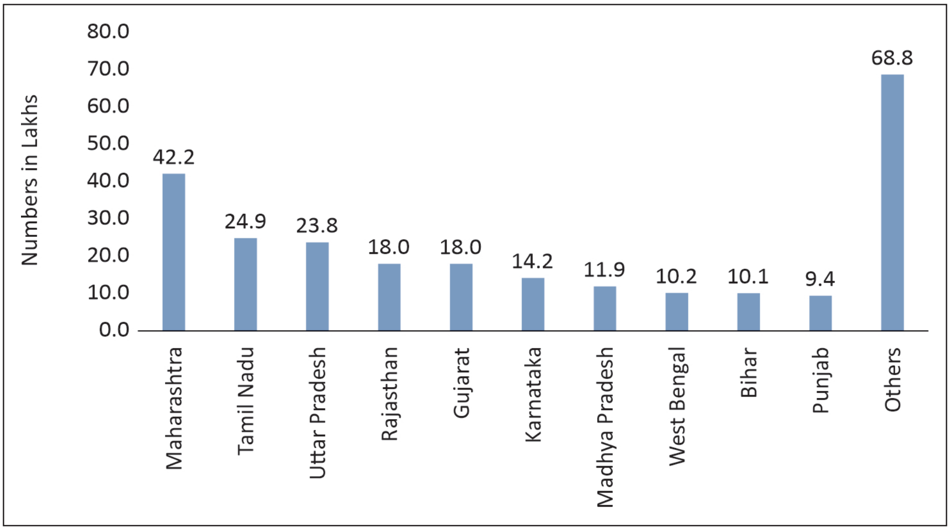
with 3.31 lakh enterprises and Medium sector with 0.05 lakh estimated enterprises accounted for 0.52 percent and 0.01 percent of total estimated MSMEs, respectively. Around 51.3 percent of the MSMEs were in the rural area, while the remaining were in the urban areas.

Data indicates that 608.41 lakh (95.98 percent) MSMEs were proprietary concerns. There was dominance of males in ownership of proprietary MSMEs, with 79.6 percent of such MSMEs being male-owned and 20.37 percent of such enterprises owned by female. The dominance of male owned enterprises was slightly more pronounced in urban areas compared to rural areas (81.6 percent as compared to 77.8 percent).

The Ministry of MSME has introduced a new registration process called 'Udyam' to replace the previous method of filing the Udyog Aadhaar Memorandum. It is beneficial for the MSMEs to apply for this registration as this is a mandatory requirement for availing benefits under the various schemes of Ministry of MSME such as Credit Guarantee Scheme, Public Procurement Policy, protection against delayed payments, etc. Registration is also required for MSMEs to be eligible for priority sector lending from banks[8]. This new process is facilitated through an Udyam portal developed by the Ministry of MSME. As per the Portal, there were 2.5 crore newly registered MSMEs in India, as of April 2024. Out of the total, 2.4 crore belonged to micro, 6.1 lakh to small, and 55.9 thousand to medium sector. Maharashtra state had the maximum Udyam registrations with 42.2 lakh units, followed by Tamil Nadu (24.9 lakh), Uttar Pradesh (23.9 lakh), Rajasthan (18.0 lakh), and Gujarat (18.0 lakh) (Exhibit 1.1).

[8] Ministry of Micro, Small and Medium Enterprises, Government of India

Exhibit 1.1: State-wise Top Udyam Registration as of April 2024



Source: Ministry of Micro, Small & Medium Enterprises, Exim Bank Research

Contribution of MSMEs to Gross Output

MSMEs contribute significantly to various facets of the economy, including employment generation, economic output and exports. As per the latest information from the Ministry of Statistics & Programme Implementation, the contribution of MSMEs to all-India Gross Domestic Product (GDP) during the years 2019-20, 2020-21 and 2021-22 were 30.5 percent, 27.2 percent, and 29.2 percent, respectively. The share of MSMEs in the manufacturing output of India during the years 2019-20, 2020-21 and 2021-22 were 36.6 percent, 36.9 percent, and 36.2 percent, respectively.

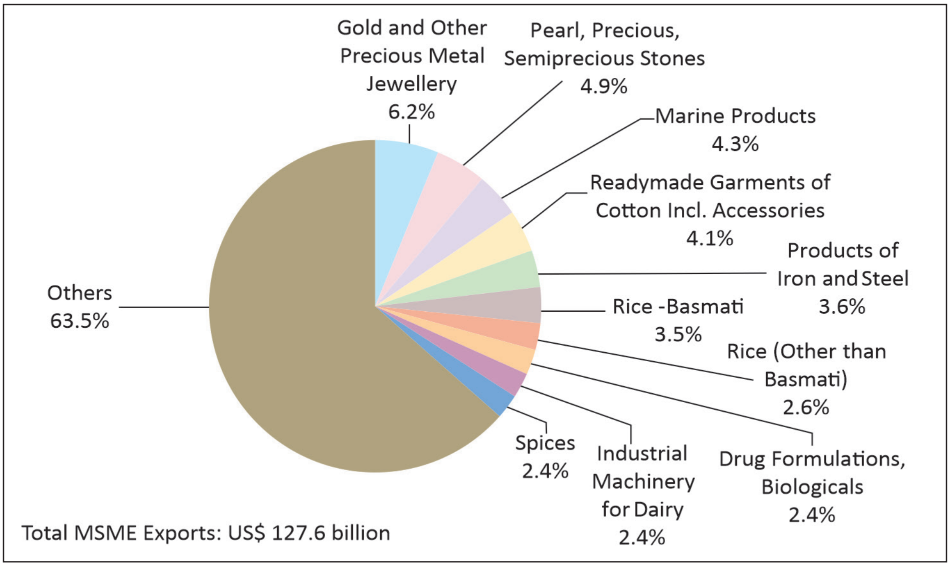
Contribution of MSMEs to Exports

MSMEs serve as crucial drivers of exports, contributing substantially to India’s foreign exchange earnings. Many MSMEs engage in export-oriented activities, leveraging their competitive advantages in terms of low-cost production, niche expertise, and innovative solutions to access international markets. As per the Ministry of MSME, Govt. of India, share of exports of select MSME related products in India’s merchandise exports during the years 2020-21, 2021-22 and 2022-23 were 49.4 percent, 45.0 percent, and 43.6 percent, respectively.

As per the information received from the Directorate General of Commercial Intelligence and Statistics (DGCIS), exports by MSMEs is provisionally estimated at US$ 127.6 billion during 2023-24, accounting for about 29.2 percent of India's total merchandise exports during the year. This data is based on the active Udyam status of the MSMEs and valid IEC status. However, merchant traders can source their products from MSMEs and then export them, which is not included in this data. Therefore, overall contribution of MSMEs to exports, including direct and indirect exports, may be higher.

Out of the total provisional exports by MSMEs, the exports of gold and other precious metal jewellery[9] accounted for the largest share at 6.2 percent in total exports by MSMEs in 2023-24. Other top exported products include pearl, precious, semiprecious stones (share of 4.9 percent), marine products (4.3 percent), readymade garments of cotton including accessories (4.1 percent), products of iron and steel (3.6 percent), and basmati rice (3.6 percent), among others (Exhibit 1.2).

Exhibit 1.2: Principal Commodity-wise Exports by MSMEs (2023-24)

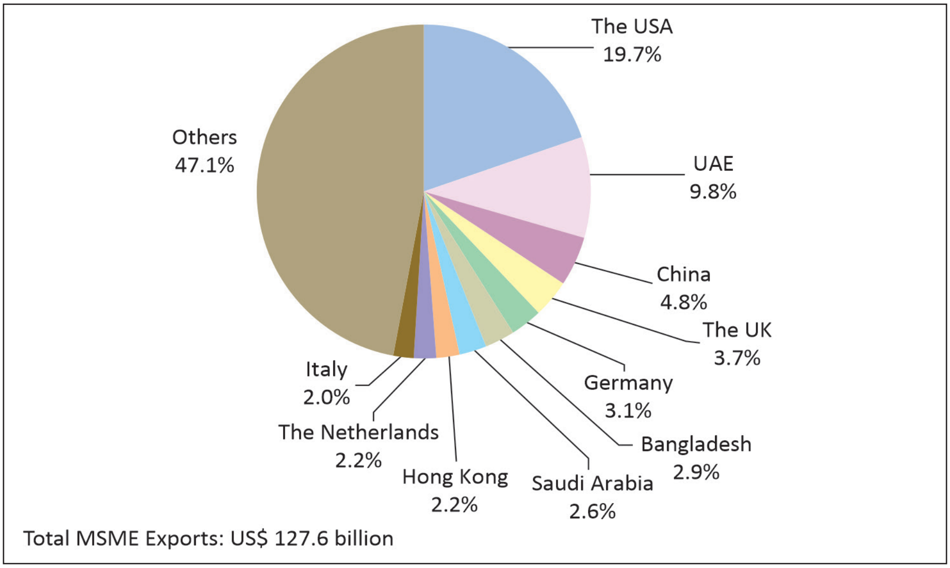


Source: DGCIS, Ministry of MSME, Exim Bank Research

[9] Principal Commodity classification by DGCIS

In terms of direction of exports, the USA was the topmost destination for MSME exporters in India, accounting for a share of 19.7 percent in total MSME exports during 2023-24, followed by UAE (share of 9.8 percent), China (4.8 percent), the UK (3.7 percent), and Germany (3.1 percent), among others (Exhibit 1.3). It is noteworthy that the top 10 export destinations for MSME exporters accounted for nearly 52.9 percent of total MSME exports during 2023-24. This is slightly higher compared to all-India level, wherein the top 10 export destinations accounted for nearly 49.1 percent of India's total merchandise exports.

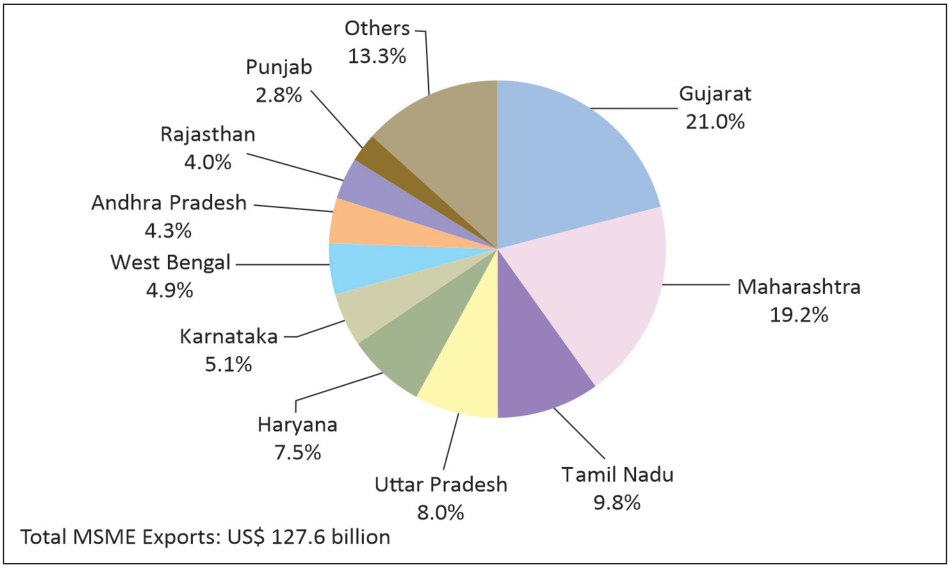
Exhibit 1.3: Direction of Exports by MSMEs (2023-24)



Source: DGCIS, Ministry of MSME, Exim Bank Research

State-level analysis of exports data indicates that Gujarat is the largest state of origin for MSME exports from India, accounting for a share of 21 percent in total MSME exports in 2023-24, followed by Maharashtra (share of 19.2 percent), Tamil Nadu (9.8 percent), Uttar Pradesh (8 percent), and Haryana (7.5 percent), among other states. It is noteworthy that while the top three states remain the same for MSME exporters as compared to all-India exports, their joint share at nearly 50 percent of total MSME exports in 2023-24 is lower than all-India level of 56.1 percent during the same period.

Exhibit 1.4: State-wise Exports by MSMEs (2023-24)



Source: DGCIS, Ministry of MSME, Exim Bank Research

SCOPE OF THE STUDY

Considering the pivotal role played by MSMEs in exports, achieving the ambitious exports target of US$ 2 trillion by 2030 set by the Government of India (GOI) would hinge on unleashing the full potential of this sector. This would entail addressing the specific challenges faced by these exporters, and creating an enabling environment for their growth.

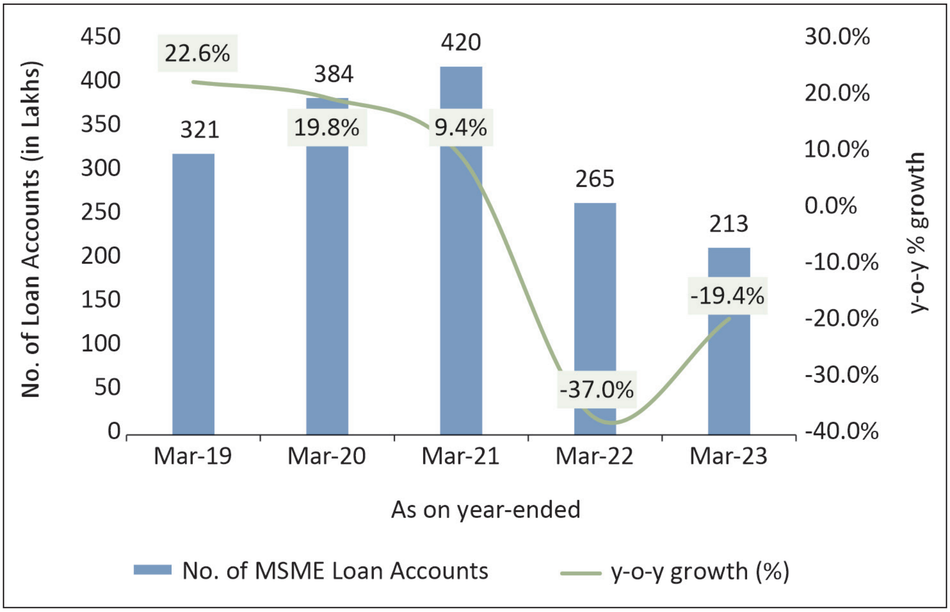
Against this backdrop, the study discusses the challenges faced by Indian MSMEs in their export endeavours, the opportunities for growth and the strategies to alleviate the challenges. In the study, a survey-based approach was employed to identify the challenges faced by the MSMEs. The method involved structured questionnaires to a representative sample of MSMEs registered with various Export Promotion Councils and across various regions. As export finance is a critical component of competitiveness, the study particularly examines the dynamics of credit flows to the sector, explores the global best practices in MSME financing, and recommends strategies for alleviating the financing challenges faced by MSMEs. Additionally, the study suggests a holistic approach to address challenges related to marketing and branding, and leveraging e-commerce, among other areas.

2. Analysis of Credit Flows to the MSME Sector

CREDIT FLOWS TO MSMEs BY SCHEDULED COMMERCIAL BANKS

Scheduled commercial banks (SCBs), comprising public sector banks (PSBs), private sector banks (PVBs) and foreign banks (FBs), are among the largest sources of credit for MSMEs in India. Analysis of data on the number of MSME loan accounts in SCBs indicates that there has been two consecutive years of decline in the number of MSME loan accounts across SCBs since 2020-21. Number of MSME loan accounts has nearly halved from 420 lakh accounts in financial year end (FYE) 2020-21, to 213 lakh accounts in FYE 2022-23 (Exhibit 2.1).

Exhibit 2.1: Trends in MSME Loan Accounts in Scheduled Commercial Banks

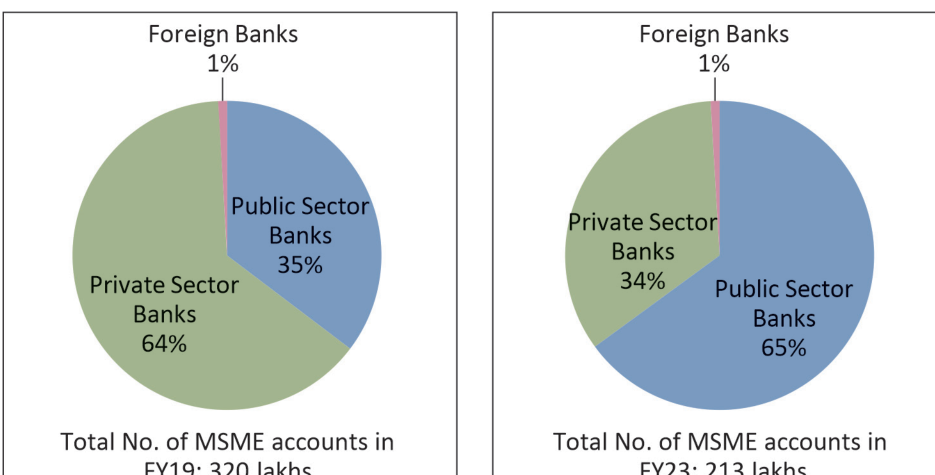


Source: RBI; Exim Bank Research

The decline in MSME loan accounts in SCBs was witnessed across all categories of SCBs. However, there was a particularly stark drop in MSME loan accounts in PVBs, with an average annual decline of (-) 46.5 percent during 2020-21 to 2022-23. The number of MSME accounts in foreign banks also witnessed a sharp decline, recording an average annual decline of (-) 22.7 percent. However, PSBs recorded a relatively lower average annual decline of (-) 4.1 percent in MSME loan accounts during the same period, underscoring the salience of these banks for inclusive growth.

On the back of the sharp decline, the share of PVBs in total MSME loan accounts across SCBs declined to 34 percent in 2022-23, from 64 percent in 2018-19, while that of PSBs increased to 65 percent in 2022-23, from 35 percent in 2018-19. The share of foreign banks remained unchanged during the period under consideration (Exhibit 2.2). The decline in total MSME loan accounts could be partly attributed to MSME units becoming larger with the rise in economic activity, thereby crossing the threshold of ₹ 250 crore turnover as per the new definition of MSMEs[10].

Exhibit 2.2: MSME Accounts By Type of Banks



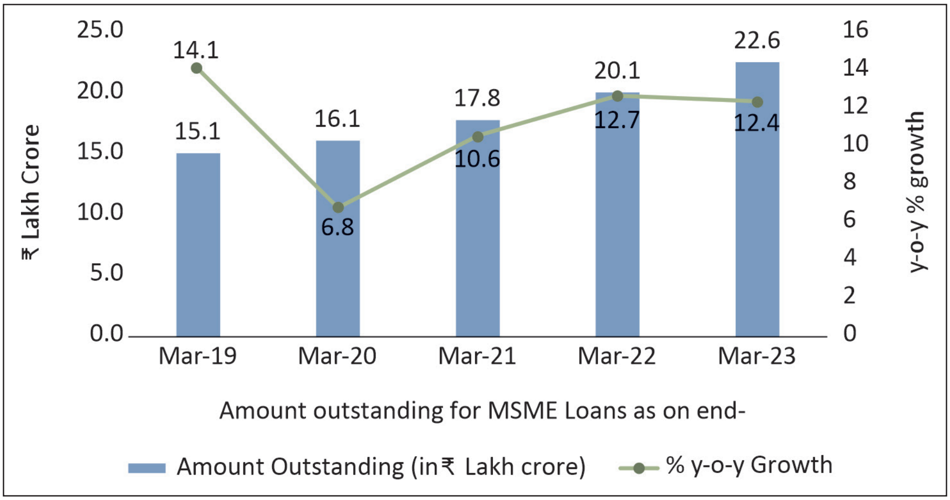
Source: RBI; Exim Bank Research

[10] SBI Research (2023), "The rise of the prodigal: How the MSME Sector is charting a new story post pandemic and simultaneously getting bigger"

It is noteworthy that despite the decline in the number of MSME loan accounts in SCBs, the credit flows to MSMEs by SCBs, has exhibited a steady growth over the recent year. During the period between 2018-19 to 2022-23, outstanding credit to MSMEs by SCBs has recorded a CAGR of 10.6 percent to reach an outstanding value of ₹ 22.6 lakh crore as on March 2023, up from ₹ 15.1 lakh crore as on March 2019.

Credit to MSMEs has particularly accelerated since 2020-21, recording an average annual growth rate of nearly 12.6 percent during 2020-21 to 2022-23. Incentives provided by the Emergency Credit Line Guarantee Scheme (ECLGS), coupled with lower Gross Non-performing Assets (GNPA) ratios have helped in boosting credit to MSMEs[11]. Further, increase in overall credit to the MSME sector can also be attributed to the addition of wholesale and retail trade in the MSME category since July 2021.

Exhibit 2.3: Trends in Credit Flows to MSMEs by All Scheduled Commercial Banks



Source: RBI; Exim Bank Research

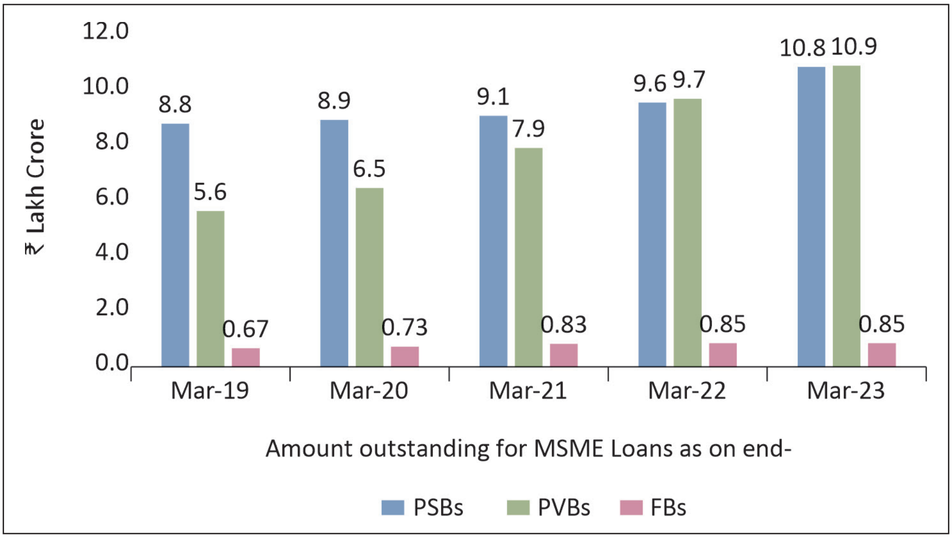
It is noteworthy that during 2021-22, credit growth to MSMEs in the industrial sector was distinctly higher on a year-on-year basis, as well as in

[11] Ibid.

comparison with credit growth to large industries. Although the growth rate decelerated since March 2022, it remained higher than the credit growth to large industries[12].

Since 2018-19, growth in MSME credit extended by PVBs far exceeded that of PSBs. During FYE 2018-19 to FYE 2022-23, MSME loans by PVBs recorded a robust CAGR of 17.9 percent, to reach an outstanding value of ₹ 10.9 lakh crore as on end-March 2023, up from ₹ 5.6 lakh crore as on end-March 2019. This is despite the sharp decline in the number of MSME loan accounts in PVBs during recent years (Exhibit 2.4). Meanwhile, MSME loans by PSBs and foreign banks also recorded healthy CAGRs of 5.4 percent and 6.3 percent during the same period, to reach an outstanding value ₹ 10.8 lakh crore and ₹ 0.85 lakh crore, respectively, as on end-March 2023. As a result, the share of PVBs in outstanding credit has increased over the recent years, from 37 percent in FYE 2018-19 to 48 percent in FYE 2022-23, while that of PSBs and foreign banks have shrunk (Exhibit 2.5).

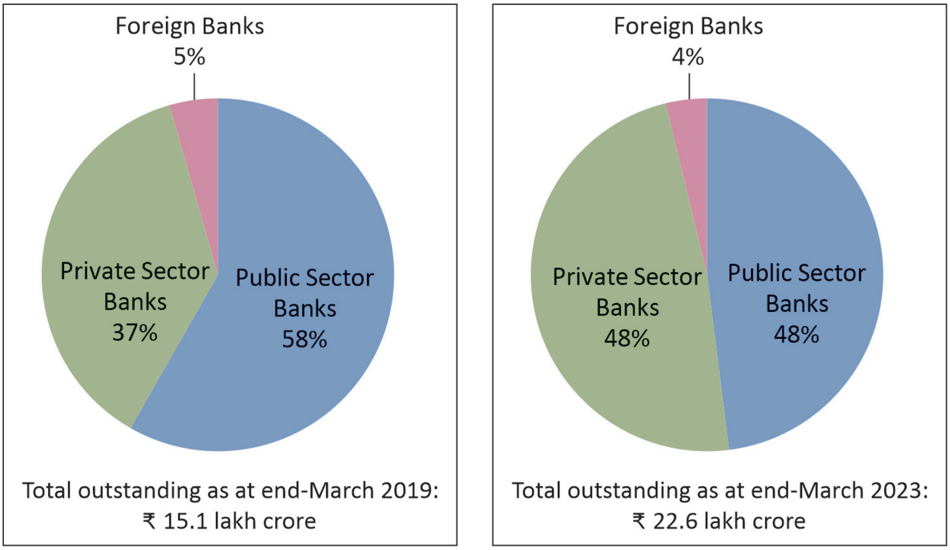
Exhibit 2.4: Trends in Credit Flows to MSMEs by Type of SCBs



Source: RBI; Exim Bank Research

[12] RBI (2023), Report on Trend and Progress of Banking in India 2022-23

Exhibit 2.5: Share in Credit Flows to MSMEs by Type of Banks



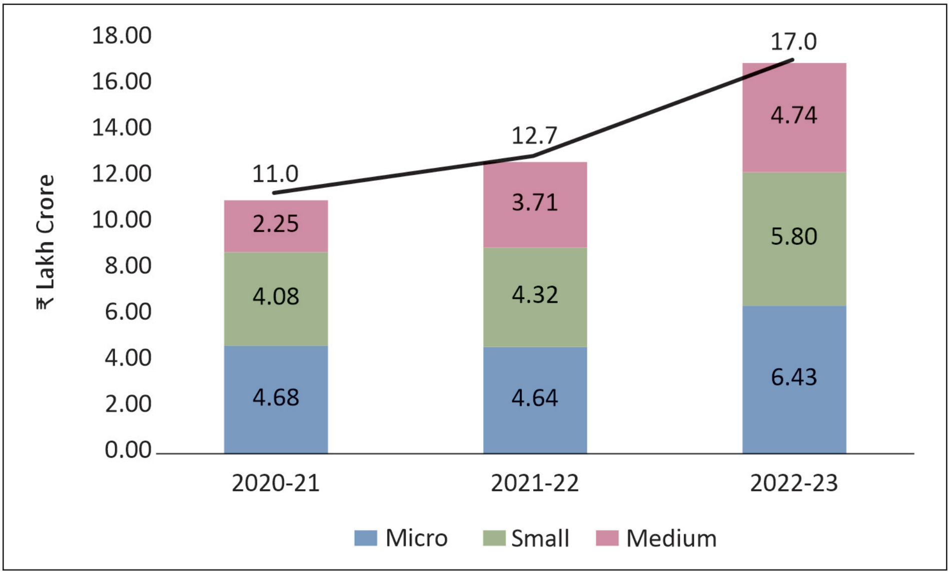
Source: RBI; Exim Bank Research

TRENDS IN CREDIT DISBURSEMENT TO MSMEs

Data from the RBI highlights a steady growth in credit disbursements by SCBs to MSMEs over the recent year. During 2020-21 to 2022-23, credit disbursements to MSMEs by SCBs recorded a robust CAGR of 24.1 percent, to reach an estimated ₹ 17.0 lakh crore in 2022-23, up from ₹ 11.0 lakh crore in 2020-21 (Exhibit 2.6). Among MSMEs, credit disbursements to micro enterprises held the highest share of 37.9 percent in total credit disbursements to MSMEs by SCBs during 2022-23, followed by small enterprises, with a share of 34.2 percent.

It is noteworthy that over the recent years, credit disbursements to medium enterprises have registered stronger growth. In fact, during 2020-21 to 2022-23, credit disbursements to medium enterprises by SCBs recorded a CAGR of 45.2 percent, while that to small and micro enterprises witnessed CAGRs of 19.2 percent and 17.2 percent, respectively, during the same period. As a result, the share of medium enterprises in total credit disbursements to MSMEs witnessed a sharp increase by nearly 7.5 percentage points to reach 27.9 percent in 2022-23, up from nearly 20.4 percent share in 2020-21 (Exhibit 2.6).

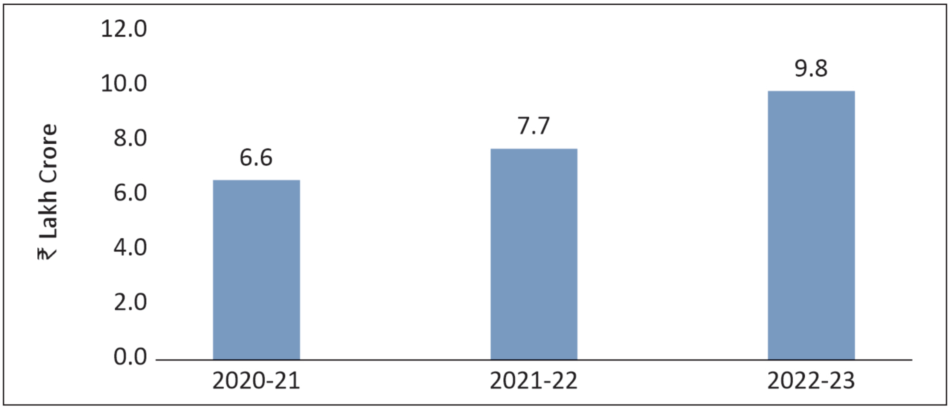
Exhibit 2.6: Trends in Credit Disbursement to MSMEs by SCBs



Source: RBI; Rajya Sabha unstarred question no. 1231 dated July 2023; Exim Bank Research

Data from SIDBI-TransUnion CIBIL also shows a healthy growth in disbursements of working capital term loans to MSMEs over the recent year. During 2020-21 to 2022-23, disbursements of working capital term loans to MSMEs recorded a robust CAGR of 22.3 percent, to reach an estimated ₹ 9.8 lakh crore in 2022-23, up from ₹ 6.6 lakh crore in 2020-21 (Exhibit 2.7). Among MSMEs, credit disbursements to small enterprises had the highest share of 40.6 percent in total credit disbursements to MSMEs during 2022-23, followed by medium enterprises, with a share of 35.0 percent, while the share of micro enterprises in total credit disbursements stood at 24.4 percent (Exhibit 2.8).

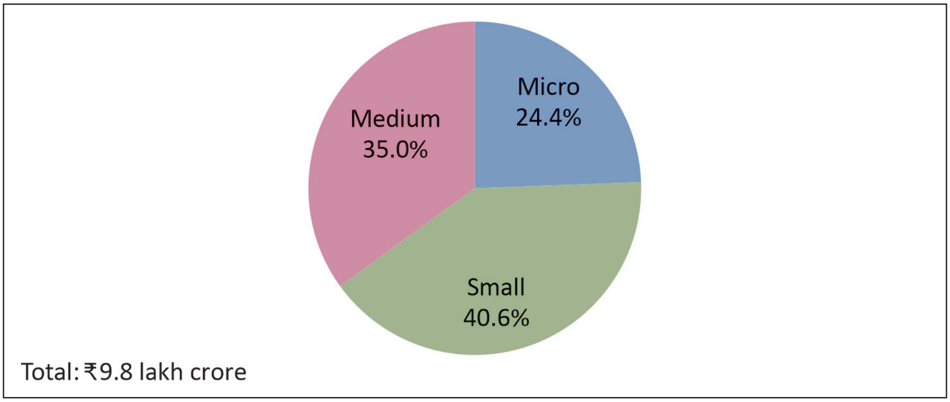
Exhibit 2.7: Trends in Disbursement of Working Capital-Term Loans to MSMEs



Note: All MSME fund-based (WC-TL) Originations considered excluding Renewals; Micro Exposure upto ₹ 1 crore; Small: Exposure between ₹ 1 crore and ₹ 10 crore; Medium Exposure between ₹ 10 crore and ₹ 50 crore

Source: SIDBI- TransUnion CIBIL Limited MSME Pulse; Exim Bank Research

Exhibit 2.8: Disbursement of Working Capital - Term Loans by Type of Enterprise (2022-23)

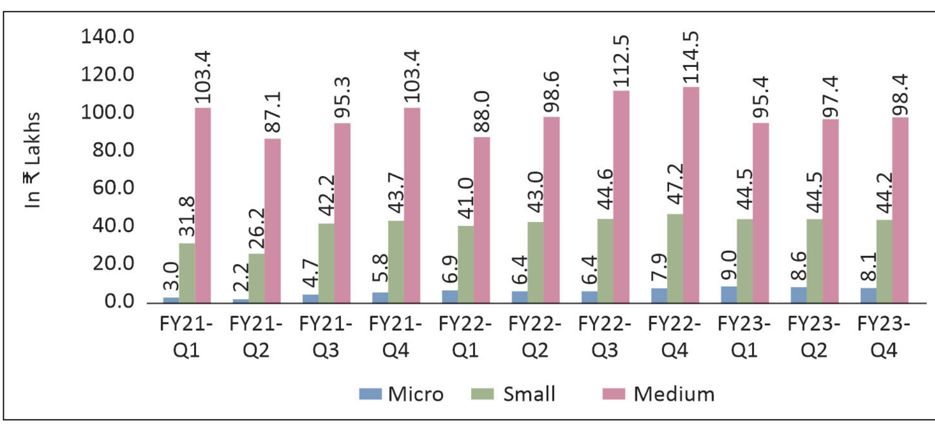


Note: All MSME fund-based (WC-TL) Originations considered excluding Renewals; Micro Exposure upto ₹ 1 crore; Small: Exposure between ₹ 1 crore and ₹ 10 crore; Medium Exposure between ₹ 10 crore and ₹ 50 crore

Source: SIDBI- TransUnion CIBIL Limited MSME Pulse; Exim Bank Research

It is noteworthy that there has been a decrease in average loan size for commercial loans availed by MSMEs since Q4-FY22, especially for small and medium enterprise borrowers. Analysis of data from SIDBI-TransUnion CIBIL report suggests that the average loan size for small enterprises has declined from ₹ 47.2 lakhs in Q4-FY22 to ₹ 44.2 lakhs in Q4-FY23, while that of medium enterprises has declined from ₹ 1.1 crore in Q4-FY22, to ₹ 98.4 lakh in Q4-FY23. It is noteworthy that the typical loan size for small and medium enterprises is greater than ₹ 1 crore. As per SIDBI-TransUnion CIBIL report, the decline in average loan size is attributable to the conservative approach by lenders, particularly banks, their low-risk appetite and the higher cost of collections for both public sector and private banks. It is noteworthy that while the loan ticket size of MSMEs by public sector banks and private banks reduced by nearly 21 percent and 7 percent y-o-y, respectively, during FY23-Q4, the average loan size by NBFCs increased by 9 percent y-o-y during the same period[13].

Exhibit 2.9: Average Loan Size of MSMEs in India



Source: SIDBI- TransUnion CIBIL Limited MSME Pulse; Exim Bank Research

State-wise Analysis of Credit Disbursement to MSMEs

Analysis of state-wise credit disbursed by SCBs to MSMEs in India reveals an interesting trend. A few states have a larger share in the credit disbursed to MSMEs as compared to their share in total number of registered MSMEs in

[13] SIDBI- TransUnion CIBIL Limited MSME Pulse, August 2023

the country. This includes states like Maharashtra, Gujarat, West Bengal, and Punjab, among others. However, in several other states such as Tamil Nadu, Uttar Pradesh, Rajasthan, Karnataka, Madhya Pradesh, Bihar, Andhra Pradesh, Odisha and several Northeastern and Himalayan States, the share of credit disbursed to MSMEs is below the share of the state in total registered MSMEs in the country (Table 2.1). It is noteworthy that, in several of these states, MSMEs contribute substantially to the State's total merchandise exports. For instance, as per DGCI&S data, nearly half of the exports from Uttar Pradesh and Rajasthan are from MSMEs exporters. However, the share of credit disbursed to MSMEs in states is much below the share of the states in total registered MSMEs in the country. Likewise, in states such as Mizoram and Arunachal Pradesh, where more than 4/5th of the exports come from MSME sector, the credit disbursement to MSMEs account for less than 0.1 percent of the overall credit disbursed to MSMEs in the country in FY23 (Table 2.1). This indicates that MSMEs in these states are underserved by SCBs, and there is a need for enhancing the credit flows to MSMEs in these states, so as to build capabilities for enhancing exports from these states.

Table 2.1: State-wise Comparison of Credit Flows to MSME by SCBs

State / UT	Total Udyam Registered MSMEs (in '000s)	% Share in Total Udyam Registered MSMEs	% Share of MSME Exports in the State's Total Merchandise Exports in FY24	Amount Disbursed to MSMEs in FY23 (In ₹ Crore)	% Share in total Amount Disbursed to MSMEs
Maharashtra	4437.3	16.6%	36.4%	326353.9	19.2%
Tamil Nadu	2638.1	9.9%	28.9%	165244.2	9.7%
Uttar Pradesh	2540.9	9.5%	49.8%	103656.9	6.1%
Rajasthan	1915.7	7.2%	50.5%	90593.9	5.3%
Gujarat	1900.0	7.1%	19.9%	161626.9	9.5%
Karnataka	1509.4	5.6%	24.5%	91371.9	5.4%
Madhya Pradesh	1269.4	4.8%	25.7%	59122.1	3.5%
West Bengal	1089.3	4.1%	53.5%	80244.7	4.7%
Bihar	1080.8	4.0%	18.0%	24481.5	1.4%
Punjab	1015.0	3.8%	52.4%	72400.8	4.3%
Telangana	928.4	3.5%	24.7%	64006.6	3.8%

State / UT	Total Udyam Registered MSMEs (in '000s)	% Share in Total Udyam Registered MSMEs	% Share of MSME Exports in the State's Total Merchandise Exports in FY24	Amount Disbursed to MSMEs in FY23 (In ₹ Crore)	% Share in total Amount Disbursed to MSMEs
Haryana	873.5	3.3%	54.5%	87551.0	5.2%
Andhra Pradesh	855.9	3.2%	28.1%	42022.8	2.5%
Odisha	835.1	3.1%	9.3%	25182.6	1.5%
Delhi	654.0	2.4%	34.1%	149947.9	8.8%
Kerala	624.7	2.3%	30.9%	43015.8	2.5%
Assam	489.7	1.8%	43.4%	14483.4	0.9%
Jharkhand	454.5	1.7%	10.9%	16820.4	1.0%
Jammu & Kashmir	418.9	1.6%	23.9%	8411.0	0.5%
Chhattisgarh	377.0	1.4%	43.4%	23164.5	1.4%
Uttarakhand	261.5	1.0%	33.3%	15246.7	0.9%
Himachal Pradesh	162.0	0.6%	21.1%	9894.0	0.6%
Manipur	69.3	0.3%	16.9%	754.0	0.04%
Tripura	58.1	0.2%	34.2%	1504.6	0.1%
Goa	53.5	0.2%	15.6%	3888.6	0.2%
Chandigarh	41.2	0.2%	53.5%	8435.6	0.5%
Puducherry	38.8	0.1%	19.0%	2561.3	0.2%
Nagaland	24.4	0.1%	44.7%	593.6	0.03%
Mizoram	23.2	0.1%	90.6%	414.3	0.02%
Meghalaya	21.5	0.1%	32.8%	715.6	0.04%
Dadra & Nagar Haveli And Daman & Diu	19.4	0.1%	22.9%	1708.9	0.1%
Arunachal Pradesh	13.2	0.05%	81.8%	580.0	0.03%
Andaman & Nicobar	12.6	0.05%	1.5%	265.3	0.02%
Sikkim	10.7	0.04%	20.0%	444.4	0.03%
Lakshadweep	0.9	0.003%	63.0%	29.1	0.002%
Total	**26717.7**	**100%**	**29.2%**	**1696738.3**	**100%**

Note: Cells highlighted in Orange indicate states whose share in registered MSMEs is higher than the share in credit disbursements to MSMEs.

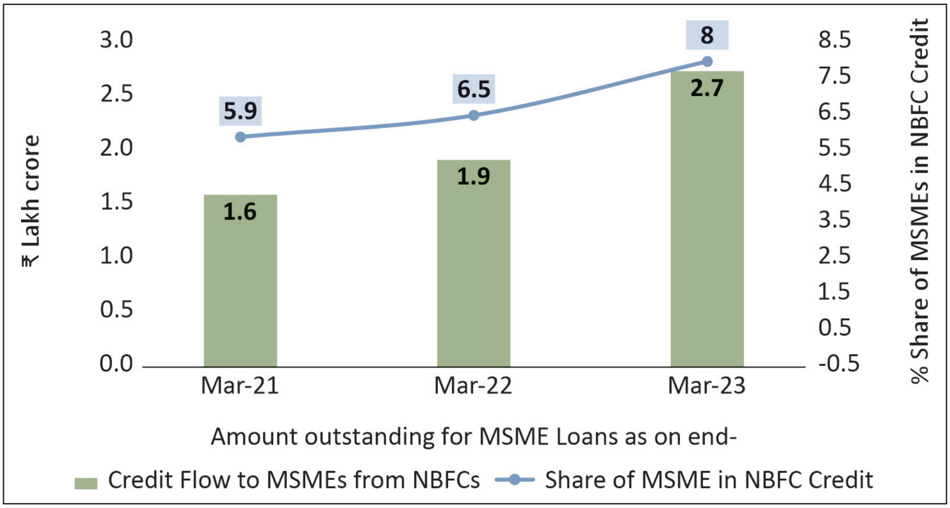
Udyam Registered MSMEs, as on July 2024 has been considered for this analysis.

Source: RBI; Rajya Sabha Unstarred Question No. 1232 Dated July 2023; Ministry of MSMEs; DGCI&S; Exim Bank Research

CREDIT FLOWS TO MSMEs THROUGH NBFCs

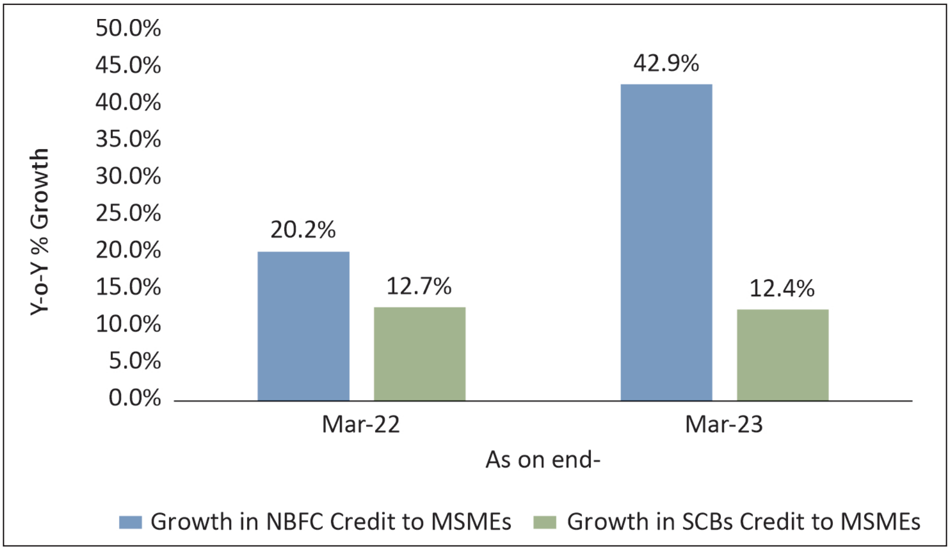
Apart from SCBs, NBFCs also play a crucial role in meeting the credit needs of MSMEs. NBFCs have steadily expanded their MSMEs portfolio, thereby contributing to overall financial inclusion and economic growth. Between end-March 2021 and end-March 2023, NBFC's outstanding credit to MSMEs recorded a robust CAGR of 31 percent to reach ₹ 2.7 lakh crore as on end-March 2023, up from ₹ 1.6 lakh crore as on end-March 2021 (Exhibit 2.10). The pace of expansion in NBFCs loans to MSMEs has been particularly robust in 2022-23, at a y-o-y growth rate of 42.9 percent, which is more than three times the growth in lending by SCBs to MSMEs (Exhibit 2.11).

Exhibit 2.10: NBFCs' Credit to MSME Sector



Source: RBI; Exim Bank Research

Exhibit 2.11: Comparison of Growth in Credit to MSME Sector – NBFCs vs Banks



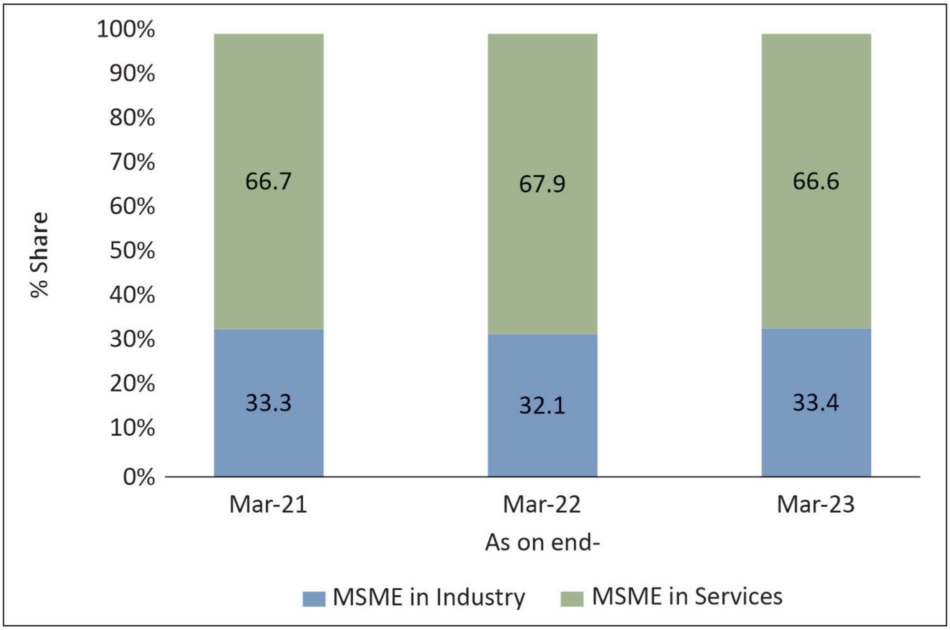
Source: RBI; Exim Bank Research

The co-lending framework for priority sector lending has also facilitated flow of credit by NBFCs to the MSME sector, leveraging on the low cost of funds of banks and greater reach of NBFCs[14]. In order to better leverage the respective comparative advantages of banks and NBFCs, the RBI introduced Co-Lending Model to provide greater operational flexibility to lending institutions, while requiring them to conform to the regulatory guidelines on outsourcing, KYC, etc. Under the framework, banks are permitted to co-lend with all registered NBFCs (including HFCs) based on a prior agreement. The co-lending banks take their share of the individual loans on a back-to-back basis in their books, while NBFCs are required to retain a minimum of 20 percent share of the individual loans on their books. The primary focus of the framework is to improve the flow of credit to the unserved and underserved sectors of the economy and make available funds to the ultimate beneficiary at an affordable cost, considering the lower cost of funds from banks and greater reach of the NBFCs.

[14] Ibid.

It is noteworthy that MSMEs engaged in services accounted for a substantial share of NBFC credit to the MSME sector. During 2022-23, NBFC credit to MSMEs engaged in services accounted for nearly two-third of the total NBFC credit to the MSME sector, while the share of NBFC credit to MSMEs engaged in industries stood at 33.4 percent. The share of MSMEs engaged in services in NBFC credit to the MSME sector as a whole has remained largely unchanged over the recent years.

Exhibit 2.12: NBFCs' Credit to MSMEs by Sector



Source: RBI; Exim Bank Research

NBFC's outstanding credit to MSMEs in the industry sector as on end-March 2023 has recorded a remarkable y-o-y growth rate of 48.5 percent, primarily driven by the credit to micro and small enterprises segment. Within industries sector, the share of NBFC credit to MSMEs is concentrated in the micro and small enterprises segment, which jointly accounted for a share of 78.1 percent in total NBFC's outstanding credit to MSMEs in the industries sector as on end-March 2023, followed by medium enterprises, with a share of 21.9 percent (Table 2.2).

Table 2.2: Credit Flow to MSMEs in Industry Sector in India by NBFCs

Type of Enterprise	Items	As on end-March 2021	As on end-March 2022	As on end-March 2023	% Share
Micro and Small Enterprises	Credit outstanding (₹ Crore)	38,051	44,329	71,638	78.1%
	% y-o-y Change	-	16.5	61.6	-
Medium Enterprises	Credit outstanding (₹ Crore)	14,919	17,411	20,068	21.9%
	% y-o-y Change		16.7	15.3	-
Total MSMEs in Industry sector	Credit outstanding (₹ Crore)	52,970	61,740	91,706	100%
	% y-o-y Change		16.6	48.5	-

Source: RBI; Exim Bank Research

CREDIT FLOWS TO MSMEs THROUGH OTHER FINANCIAL INSTITUTIONS

In addition to SCBs and NBFCs, there are several other financial institutions that also cater to the MSME sector. This includes institutions like Urban Co-operative Banks (UCBs), Regional Rural Banks (RRBs), and Small Finance Banks (SFBs)[15]. Apart from these, Small Industries Development Bank of India (SIDBI), which is the principal financial institution for promotion, financing and developing the MSME sector, also engages in lending to MSMEs, through both direct lending as well as refinancing to Banks and Financial Institutions (FIs). As on end-March 2023, outstanding credit to MSMEs by these institutions[16] jointly amounted to ₹ 2.45 lakh crore, accounting for a share of nearly 8.8 percent in total outstanding credit to MSMEs (Table 2.3). Total credit flows to the MSME sector by all financial institutions is estimated at ₹ 27.8 lakh crore, as on end-March 2023.

[15] SFBs were set up in 2016 to meet the financial needs of under-banked segments and ensure effective credit delivery credit to such segments. SFBs are differentiated or niche banks with minimum net worth of ₹ 200 crore, which is lower than other SCBs.

[16] Comprising UCBs, RRBs, SFB and SIDBI. For SIDBI, only direct lending to MSMEs has been considered in this analysis.

Table 2.3: Recent Trends in Credit Flows to MSMEs by Other Financial Institutions

Type of Institution	Amount Outstanding as on year ended (₹ Crore)			% Share in Total Outstanding Credit to MSMEs (As on Mar-23)
	Mar-21	Mar-22	Mar-23	
Urban Co-operative Banks	1,01,340.0	1,08,958.0	1,34,320.0	4.8%
Regional Rural Banks	39,977.0	41,644.0	49,407.0	1.8%
Small Finance Banks	29,434.1	39,111.0	43,226.5	1.6%
SIDBI's Direct Finance to MSMEs	11,581.0	14,187.0	18,409.0	0.7%
Total of Other Financial Institutions (A)	1,82,332.1	2,03,900.0	2,45,362.5	8.8%
Scheduled Commercial Banks (B)	17,83,924.8	20,11,057.0	22,60,135.3	81.3%
NBFCs (C)	1,59,811.1	1,91,908.7	2,74,157.6	9.9%
Total of All Financial Institutions (A+B+C)	21,26,068.0	24,06,866.7	27,79,655.4	100%

Source: RBI; SIDBI; Rajya Sabha Unstarred Question No. 443 Dated July 2023; Exim Bank Research

After SCBs and NBFCs, UCBs accounted for the highest share of 4.8 percent in total outstanding credit to MSMEs as on end-March 2023, followed by RRBs and SFBs, with shares of 1.8 percent and 1.6 percent, respectively, in the total outstanding credit to MSMEs, as on end-March 2023.

UCBs, RRBs, and SFBs are required to lend a substantial portion of their credit to priority sectors, which includes MSMEs. As per the RBI, UCBs are required to meet the target of 60 percent, 65 percent and 75 percent or higher of their adjusted net bank credit (ANBC) or credit equivalent of off balance-sheet exposure (CEOBE) for priority sectors by end-March 2023, 2025, and 2026, respectively. Likewise, RRBs and SFBs are required to lend at least 75 percent of their ANBC to priority sector. This is substantially higher when compared with 40 percent target in the case of SCBs.

It is interesting to note that UCBs, RRBs and SFBs have not only exceeded their priority sector lending targets in the recent years[17], but have also developed a niche in priority sector lending areas, particularly MSME. For instance, priority sector lending by UCBs, as at end-March 2023, comprised 66.9 percent of the total advances of UCBs and nearly 40.7 percent of the total advances of UCBs were to MSMEs alone. Likewise, 61.3 percent of the total advances of SFBs, as on end-March 2023, comprised priority sector lending and 24.3 percent of advances by SFBs were to MSMEs alone. The better delivery of credit to MSMEs by these institutions could be due to factors such as better outreach of RRBs and UCBs and increasing implementation of digital lending models by SFBs.

In its role as a development finance institution, SIDBI supports flow of credit to MSMEs primarily through refinancing support to banks, NBFCs and micro finance institutions (MFIs), thereby augmenting the capacity of banks/FIs to meet the needs of MSME sector. Direct lending to MSMEs comprised only 5.1 percent of SIDBI's total outstanding credit as on end-March 2023. Accordingly, the share of SIDBI's direct lending to MSMEs in total outstanding credit to MSMEs stood at a relatively lower 0.7 percent, as on end-March 2023.

Besides these institutions, Exim Bank, in its role a development finance institution, has been bridging the financing gaps for exports, including for MSMEs. Since inception, Exim Bank has played an instrumental role in providing medium to long term export financing to exporters. Exim Bank's wide array of financing programmes has been bolstering export capacities across various sectors, and also facilitating execution of export/deemed export contracts. Over the recent years, Exim Bank has launched several new initiatives to bridge the financing gaps for exports, particularly for MSMEs. The Bank is also catalysing innovation through its support to emerging MSME innovators, under the Ubharte Sitaare Programme (Box 1).

[17] RBI (2023), Trends and Progress of Banking in India 2022-23

Box 1: Exim Bank's Financing Support for MSMEs

Ubharte Sitaare Programme

The Ubharte Sitaare Programme (USP) was announced by the Hon'ble Finance Minister in the Budget Speech on February 01, 2020. The programme is aimed at identifying small and medium Indian enterprises with differentiated technologies, products, or processes, that have the potential to emerge as future export champions. The Programme diagnoses obstacles in their growth journey, and provides assistance through a mix of structured support, both financial and advisory services, including (a) debt (funded and non-funded facilities) at competitive rates and elongated tenors; (b) investments in equity / equity like instruments; and (c) technical assistance (including advisory services, grants and soft loans). The companies supported under USP are engaged in diversified sectors such as smart and energy-efficient home appliances, auto components, defence & aerospace, pharmaceuticals, electronics, engineering goods, healthcare services, agro and food processing, printing & publishing, sustainable waste management, among other.

Trade Assistance Programme

Exim Bank has developed a new, first-of-its-kind trade facilitation initiative, the 'Trade Assistance Programme' (TAP) to address the trade finance gap, particularly in the MSME sector. Under TAP, the Bank provides credit enhancement to trade instruments, thereby enhancing the capacity of commercial banks to support cross-border trade transactions. The Bank is leveraging its partnerships across the globe in identifying and supporting trade transactions involving untapped markets where trade lines are constrained or where the potential has not been harnessed. The various credit mechanisms under TAP are (i) Support to Trade Finance Instruments; (ii) Irrevocable Reimbursement Undertaking; (iii) Fronting of Guarantees; (iv) Risk Participation; (v) Trade Loans; (vi) Credit Lines; and (vii) Refinance.

Exim Finserve- Subsidiary at GIFT City

To further bridge the financing gaps, Exim Bank has set up its subsidiary in GIFT City, Exim Finserve. Announced in the Union Budget 2023, the subsidiary is offering a range of trade finance products to exporters, with a focus on factoring. With the launch of Exim Finserve, Exim Bank is now covering the entire canvas of trade with bank-intermediated trade finance along with open account trade, thereby providing a stronger pillar of support for Indian companies, particularly MSMEs, as they navigate an increasingly competitive and uncertain global economic environment. Factoring presents a viable receivables management and financing mechanism suited to the needs of MSMEs. It provides a combination of three essential services to exporters: receivables financing, coverage of the risk of non-payment, and management of accounts receivable. It is particularly beneficial for MSME exporters as it is primarily based on the quality of accounts receivable rather than collateral. It also has the potential to improve export competitiveness as it enables exporters to offer competitive credit terms to their buyers.

Grassroots Initiatives and Development (GRID)

Exim Bank, through its Grassroots Initiatives and Development (GRID) programme, supports enterprises based largely out of rural areas of the country or micro and small enterprises sourcing a majority of their products from grassroots organisations/artisans. The GRID programme addresses the needs of relatively disadvantaged sections of the society while creating expanded opportunities for traditional crafts persons and artisans. Under the programme, the Bank's assistance has enabled financial empowerment, employment generation and promotion of entrepreneurship among individual artisans primarily engaged in producing traditional handicraft and handloom products, while at the same time helped in preservation and revival of traditional heritage of Indian crafts.

Under the Programme, the Bank is also supporting interventions at the district level, in alignment with the 'Districts as Export Hubs (DEH)' initiative of the Government of India, to boost export capacity creation. The Bank has identified 64 products for interventions, including 5 districts from the Northeastern States of India. As part of this initiative, Exim Bank is supporting purchase of equipment, technology upgradation, development of common infrastructure facilities, etc. to boost export capacity creation at the district-level.

MSME FINANCING THROUGH TRADE RECEIVABLES DISCOUNTING SYSTEM (TReDS)

In additional to traditional credit, Trade Receivables Discounting System (TReDS), introduced by the Reserve Bank in 2014, also plays a crucial role in helping MSMEs to effectively meet their short-term financing needs. TReDS is an electronic platform that helps MSMEs manage their working capital needs by facilitating the financing / discounting of trade receivables through multiple financiers. TReDS platform enables MSME suppliers to discount their invoices and receive payments before their due date by ensuring the conversion of their trade receivables into liquid funds in a short period. These receivables can be due from corporates and other buyers, including government departments and public sector undertakings.

During 2018-19 to 2022-23, the number of invoices financed under TReDS recorded a remarkable CAGR of 82.2 percent, while the amount financed under TReDS has witnessed an even greater CAGR of 90.2 percent, to reach ₹ 76.6 thousand crore in 2022-23. The success rate of financing through TReDS has also been remarkably high since 2018-19, and stood at around 93.9 percent in 2022-23, indicating the significance of the platform as a reliable source for MSMEs in meeting their working capital needs.

Table 2.4: Trends in MSME Financing through TReDS

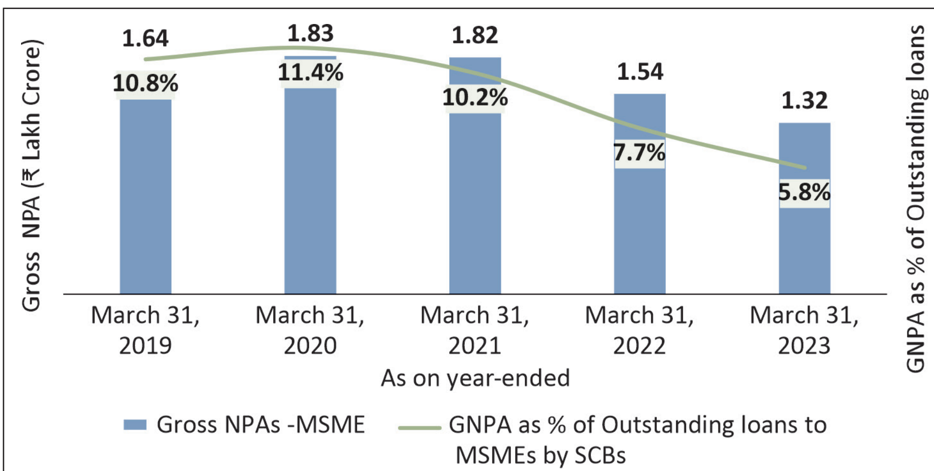
Financial Year	Invoices Uploaded		Invoices Financed		Success Rate in Financing
	Number of Invoices Uploaded	Amount (₹ Crore)	Number of Invoices Financed	Amount (₹ Crore)	Share of Number of Invoice Financed in Total Number of Invoice Uploaded
2018-19	2,51,695	6,699	2,32,098	5,854	92.2%
2019-20	5,30,077	13,088	4,77,969	11,165	90.2%
2020-21	8,61,560	19,669	7,86,555	17,080	91.3%
2021-22	17,33,553	44,111	16,40,824	40,308	94.7%
2022-23	27,24,872	83,955	25,58,531	76,645	93.9%
CAGR % (FY19-FY23)	81.4%	88.2%	82.2%	90.2%	-

Source: RBI

DELINQUENCIES IN MSME LOANS

Trends in delinquencies in MSME loans by SCBs indicate a steady decline in both the value and share of gross NPAs in MSME loans over the recent year. In absolute terms, the Gross NPAs in MSME loans by SCBs have declined from ₹ 1.64 lakh crore as on end-March 2019, to ₹ 1.32 lakh crore as on end-March 2023. The share of GNPAs in total MSME loan outstanding has also declined from 10.8 percent as on end-March 2019, to 5.8 percent as on end-March 2023 (Exhibit 2.13). This is indicative of the steady improvement in asset quality in MSME lending portfolio of SCBs, partially attributable to better end-to-end tracking due to increasing use of digital tools by SCBs.

Exhibit 2.13: Trends in NPAs in MSME Loans by SCBs



Source: RBI; Rajya Sabha Unstarred Question No. 443 Dated July 2023; Exim Bank Research

CONCLUSION

Analysis in the chapter highlights the landscape of MSME financing in India. Credit flows to MSMEs have shown a steady growth, driven by factors including ECLGS, and lower GNPAs on MSME loans. Notably, private sector banks have demonstrated robust growth in MSME loans, outpacing public sector banks and foreign banks in terms of credit growth rates. Private sector banks are witnessing enhanced credit disbursements, particularly to micro and small enterprises. The trends also highlight a notable decline in the number of MSME loan accounts across all categories of SCBs since 2020-21, with MSMEs transitioning to larger business entities. NBFCs and other financial institutions, alongside platforms like the TReDS, are providing diversified sources for meeting the financial needs of MSMEs. However, the regional analysis underscores the disparities in credit disbursement across states, signalling a need for targeted efforts to ensure equitable access to credit for MSMEs nationwide.

3. Government Schemes for MSMEs in India

Recognising the importance of MSME sector for employment generation, industrial output and exports, the Government of India has implemented several schemes aimed at bolstering the growth and sustainability of MSMEs. These initiatives encompass various facets such as finance, market access, infrastructure support, and ease of doing business, ensuring a holistic development framework for MSMEs. This chapter aims to highlight some of the key schemes put in place by the Government of India, particularly from the point of view of enhancing MSME's access to finance, market access and competitiveness.

GOI SCHEMES FOR IMPROVING ACCESS TO FINANCE FOR MSMEs

Access to finance is a critical driver for the growth of MSMEs. Over the recent years, several schemes have been introduced by the Government of India to enhance credit flows to MSMEs and address cost related issues in financing.

The Credit Guarantee Scheme for Micro and Small Enterprises (CGTMSE) is particularly significant, as it addresses the critical challenge of collateral requirements that often hinder small businesses from accessing credit. By offering substantial guarantee coverage, this scheme encourages banks to lend more freely to micro and small enterprises, thereby stimulating business activities and job creation.

Besides, to address the cost burden on export credit and enhance the global competitiveness of MSMEs, the GOI also has in place the Interest Equalisation Scheme for Pre- and Post-shipment Rupee Export Credit. This measure is crucial in ensuring that MSME exporters can maintain export competitiveness in the wake of rising cost of credit amid tight monetary conditions.

Moreover, the Credit-Linked Subsidy Support under the Prime Minister's Employment Generation Programme aims to incentivise the creation of new micro-enterprises in the non-farm sector. The scheme promotes entrepreneurship and inclusive economic development in the non-farm sector. This focus on diversification towards non-farm activities can reduce rural dependency on agriculture, thereby enhancing overall economic resilience.

Table 3.1: GOI Schemes for Enhancing Credit Flow for MSMEs

Scheme Name	Details
Credit Guarantee Fund Trust for Micro and Small Enterprises (CGTMSE) Scheme	• The scheme facilitates credit guarantee support for collateral free / third-party guarantee-free loans to the Micro and Small enterprises (MSEs). • Credit guarantee is provided for loans up to ₹5 crores, with Guarantee coverage ranging from 85 percent (for Micro Enterprise for credit up to ₹ 5 lakhs) to 75 percent (others). • For MSEs engaged in trade and retail activity, guarantee coverage is available up to 50 percent of the sanctioned amount subject to a limit of ₹50 lakh per MSE borrower for credit up to ₹1 crore.
Interest Equalisation Support for Pre- and Post-shipment Rupee Export Credit	• Under the Scheme, the Government of India extends interest equalisation of 2 percent for Manufacturers and Merchant Exporters exporting under specified 410 HS lines and 3 percent to the MSME manufacturers exporting under all HS lines. • The Interest Equalisation Scheme for Pre and Post Shipment Rupee Export Credit has been extended several times. The current scheme, which was earlier available till June 30, 2024, has been further extended till December 31, 2024. This extension is only available for MSME exporters, and the interest equalisation support has been capped at ₹ 50 lakh per IEC (import-export code).

Scheme Name	Details
Credit-Linked Subsidy Support Under the Prime Minister's Employment Generation Programme (PMEGP)	• This is a bank-financed subsidy programme for setting up new micro-enterprises in non-farm sector. • The objective of the schemes is to encourage new entrepreneurs to set up micro-enterprises through credit-linked subsidy support • Margin Money subsidy on Bank Loan ranges from 15 percent to 35 percent for projects up to ₹25 lakhs in manufacturing and ₹10 lakhs in service sector • For beneficiaries belonging to special categories such as SC/ST/Women/Physically handicapped/Minorities/Ex-Servicemen/North Eastern Region (NER), the margin money subsidy is 35 percent in rural areas and 25 percent in urban areas. The maximum cost of projects is ₹25 lakh in the manufacturing sector and ₹10 lakh in the service sector.
ECGC's Enhanced Risk Cover	• ECGC Ltd. has introduced a new scheme to provide enhanced export credit risk insurance cover to the extent of 90 percent to support small exporters under the Export Credit Insurance for Banks Whole Turnover Packaging Credit and Post Shipment (ECIB- WTPC & PS). • The scheme is expected to benefit a number of small-scale exporters availing export credit from banks which hold the ECGC WT-ECIB cover.

Source: Ministry of MSMEs, GOI; Exim Bank Research

GOI SCHEMES FOR MARKET ACCESS AND CAPACITY BUILDING OF MSMEs

Besides financing, there are several initiatives by the GOI for enhancing market access for MSMEs, with a strong focus on international cooperation, market development, and capacity building for adoption of sustainable practices. These schemes collectively aim to enhance the global competitiveness, operational efficiency, and sustainability of Indian MSMEs, fostering economic growth and innovation in the sector.

The Market Development Assistance (MDA) under the International Cooperation Scheme of the Ministry of MSME, for instance, focusses on building export capabilities of MSMEs by facilitating their participation in international trade events and providing market intelligence. This scheme covers costs such as space/stall charges, advertisement, registration fees, airfare, and freight, significantly lowering the financial barriers for MSMEs to enter global markets. Additionally, it supports the organisation of international conferences and seminars, further integrating MSMEs into global trade networks.

Likewise, another important component of the International Cooperation Scheme viz. the Capacity Building of First-Time MSE Exporters (CBFTE) sub-scheme, provides crucial support for first-time exporters by reimbursing costs associated with registration with export promotion councils, export insurance premiums, and quality certification. This reduces the initial financial burden on new exporters, enabling more MSMEs to venture into international markets. The collaboration with Export Promotion Councils and other organisations ensures efficient implementation and widespread reach of this support.

The Procurement and Marketing Support (PMS) Scheme focuses on enhancing market access and capacity building for MSMEs. It supports participation in trade fairs and exhibitions, adoption of modern packaging techniques, barcodes, e-commerce, and organising knowledge-sharing events. Additionally, it promotes the development of retail outlets for Geographical Indication (GI) products, supporting local artisans and traditional products.

The MSME Sustainable (ZED) Certification scheme promotes the adoption of zero defect and zero effect manufacturing practices. Financial assistance is provided for ZED certification, with additional subsidies for women, SC/ST-owned MSMEs, and those in special regions. The scheme also covers testing, quality/product certification, consultancy charges, and technology upgrades, encouraging sustainable and efficient manufacturing practices among MSMEs.

Table 3.2: GOI Schemes for Enhancing Market Access and Capacity Building of MSMEs

Scheme Name	Details
International Cooperation - Market Development Assistance of MSMEs (MDA) Scheme	• The scheme aims to build capacity of MSMEs for entering export market by facilitating their participation in international exhibitions/ fairs/ conferences/ seminar/ buyer-seller meets abroad as well as providing them with actionable market-intelligence and reimbursement of various costs involved in export of goods and services. • The scheme provides reimbursement to MSMEs for participation/visit in international exhibitions/fairs (both physical and virtual mode). Assistance includes reimbursement of space/stall charges, advertisement and publicity charges, registration fee, and air fare, duty allowance and freight charges (for physical mode only). • The scheme also provides reimbursement for holding international conferences and seminars by industry associations/Govt. organisations. Assistance includes reimbursement of charges for organising the seminar/ conferences (both physical and virtual mode), and air fare for foreign speakers/experts/resource persons (for physical mode only), among other
International Cooperation - Capacity Building of First-Time MSE Exporters (CBFTE)	• Under this component of the international cooperation scheme, costs associated with Registration cum Membership certification (RCMC), export insurance premium, and quality certification are reimbursed to first-time Micro and Small Exporter • The Ministry of MSME has signed MoUs with 18 Export Promotion Councils (EPCs), ECGC Ltd. and National Small Industries Corporation Ltd (NSIC) to act as implementing agencies for reimbursement of fees paid for eligible activities under the scheme.

Scheme Name	Details
Procurement and Marketing Support (PMS) Scheme	• The scheme has three sub-components viz. ❑ Market access support to MSEs for participation in trade fairs/exhibitions, and vender development programmes. ❑ Capacity building support to MSEs in the form of financial support for adoption of modern packaging techniques, adoption of bar codes, adoption e-commerce by micro enterprises, and financial support for organising national workshops / seminars for knowledge sharing. ❑ Development of retail outlets for promoting GI products through financial assistance for infrastructure development. • The scheme targets Manufacturing / Service sector MSEs having valid Udyam Registration Certificate.
MSME Sustainable (ZED) Certification	• The scheme envisages promotion of ZED manufacturing amongst MSMEs, with a view to promote adoption of quality tools/systems and energy efficient manufacturing. • Under the scheme, financial assistance is provided to MSMEs in obtaining a ZED certification, in form of reimbursement of certification fees on successful certification, subject to a prescribed upper limit. • The scheme also extends additional subsidy of 10 percent for Women/SC/ST owned MSMEs or MSMEs in NER/Himalayan/Island territories/Left-wing Extremism (LWE) affected districts/aspirational districts. • Additional subsidy of 5 percent is also extended for MSMEs that are beneficiaries under the Scheme of Fund for Regeneration of Traditional Industries (SFURTI) and MSE-Cluster Development Programme (MSE-CDP) of the Ministry of MSME. • Besides, the scheme also provides financial assistance for testing/quality/product certification, reimbursement of consultancy charges, and support for technology upgradation for zero effect solutions, among others.

Source: Ministry of MSMEs, GOI; Exim Bank Research

GOI SCHEMES FOR INFRASTRUCTURE STRENGTHENING FOR MSMEs

The government recognises that robust infrastructure is the backbone of industrial success. The Micro & Small Enterprises - Cluster Development Programme (MSE-CDP) scheme is an important scheme for enhancing the infrastructure and collective capabilities of MSE clusters. MSE-CDP is a demand driven Central Sector Scheme wherein, State Governments send proposals for establishment of Common Facility Centers (CFCs) and/or establishment / up-gradation of Infrastructure Development projects as per requirements in the clusters. The establishment of CFCs is vital for providing shared resources and services to clusters, with government grants covering 70 percent to 80 percent of project costs depending on the project's location and the composition of the cluster. Clusters in Aspirational Districts, North Eastern Regions, and areas with a high percentage of micro, women-owned, or SC/ST-owned units receive higher grant percentages. Meanwhile, the Infrastructure Development component of the scheme focuses on setting up new industrial estates and upgrading existing ones. Government grants cover 50 percent to 70 percent of the project costs, with higher support for disadvantaged regions. This aspect of the scheme addresses the critical need for modern industrial infrastructure, thereby providing a conducive environment for scalability of MSEs.

Another important scheme focussing on infrastructure is the Scheme of Fund for Regeneration of Traditional Industries (SFURTI), which aims to revitalise traditional industries by organising artisans into collectives, enhancing production and adding value to their products. This scheme is crucial for preserving and promoting traditional craftsmanship while making these industries more competitive. Financial support under SFURTI includes grants of up to ₹2.5 crores for projects involving up to 500 artisans and up to ₹5 crores for larger projects. Under the scheme, there are three types of interventions viz. soft interventions, hard interventions, and thematic interventions. Soft interventions include support for skill development, marketing, design and product development, while hard interventions include infrastructure support such as creation of common facilities centres, raw material banks, warehousing facilities etc. Thematic interventions include support for other cross-cutting areas such as brand building, R&D, support for adoption of e-commerce, among others.

Table 3.3: GOI Schemes for Infrastructure Strengthening for MSMEs

Scheme Name	Details
Micro & Small Enterprises - Cluster Development Programme (MSE-CDP)	• The scheme includes hard interventions, for setting up of CFCs in clusters, as well as for infrastructure development in new/ existing industrial estates/areas • The scheme comprises two components viz. 1. Common Facility Centers: GOI grant up to 70 percent is extended for projects with costs between ₹5 crore and ₹10 crore, and up to 60 percent for project with costs between ₹10 crore and ₹30 crore. ○ Aspirational Districts, NER, Hill States, Island territories, LWE affected districts, and clusters with more than 50 percent women- or SC/ST-owned units, micro/village-owned units, or units owned by women receive grant up to 80 percent for projects with costs between ₹5 crore to ₹10 crore and up to 70 percent for projects with costs between ₹10 crore to ₹ 30 crore. 2. Infrastructure Development: GOI grant up to 60 percent is extended for projects with costs between ₹5 crore to ₹15 crore for setting up of new Industrial Estate / Flatted Factory Complex. Meanwhile, GOI grant for upgradation of current Industrial Estate/ Flatted Factory Complex is 50 percent for projects with costs between ₹5 crore to ₹10 crore. ○ In case of Aspirational Districts, NER, Hill States, Island territories, LWE affected districts and clusters with more than 50 percent (a) micro/ village or (b) women owned or (c) SC/ST owned units, GOI grant is up to 70 percent for projects with costs between ₹5 crore to ₹15 crore for setting up of new Industrial Estate / Flatted Factory Complex and up to 60 percent for projects with costs between ₹5 crore to ₹10 crore for up-gradation of existing Industrial Estate / Flatted Factory Complex.

Scheme Name	Details
Scheme of Fund for Regeneration of Traditional Industries (SFURTI)	• The scheme aims to organise traditional industries and artisans into collectives by increasing production and value addition to make products competitive, as also to promote traditional sectors and increase income of artisans, thereby providing sustainable employment. • The scheme includes financial support from GOI upto ₹2.5 crore for upto 500 artisans, and upto ₹5 crore for more than 500 artisans. • The scheme covers three types of interventions: ❑ Soft interventions – Activities to build general awareness, counselling, skill development and capacity building, exposure visits, market development initiatives, design and product development, etc. ❑ Hard interventions – Creation of common facility centres, raw material banks, upgradation of production infrastructure, warehousing facility, tools and technological upgradation, etc. ❑ Thematic interventions – Interventions on a cross-cutting basis for brand building, new media marketing, e-commerce initiatives, research and development, etc. • The financial assistance provided for any specific project shall be subject to a maximum of ₹5 crore to support soft, hard and thematic interventions.

Source: Ministry of MSMEs, GOI; Exim Bank Research

In addition to the aforementioned support, the Union Budget 2024-25 has also proposed several schemes for MSMEs in India, particularly focussing on enhancing their access to finance through formal sources. A new Credit Guarantee Scheme has been proposed in the budget for manufacturing MSMEs, with a view to help them in securing term loans for the purchase of equipment and machinery without collateral or third-party guarantee. Besides, the budget also proposed to increase the Mudra loan limit to ₹20 lakh under the 'Tarun' category for borrowers who have borrowed and repaid earlier ‘Tarun’ category loans. Additionally, the Budget has also lowered the turnover threshold for buyers from ₹500 crore to ₹250 crore for onboarding on the TReDS platform. This is expected to add nearly 7000 more companies to the platform.

CONCLUSION

The Government of India has several schemes aimed at boosting the MSME sector and traditional industries in India. These initiatives are addressing finance related issues, supporting marketing and capacity building efforts, and strengthening the existing infrastructure. Collectively, these schemes enhance the competitiveness, sustainability, and economic impact of MSMEs, fostering inclusive and resilient growth of the sector. Going forward, it would be crucial to learn from the best practices across all facets of support—financing, market access, and infrastructure development—from successful global models, in order to further bolster the support provided to MSMEs.

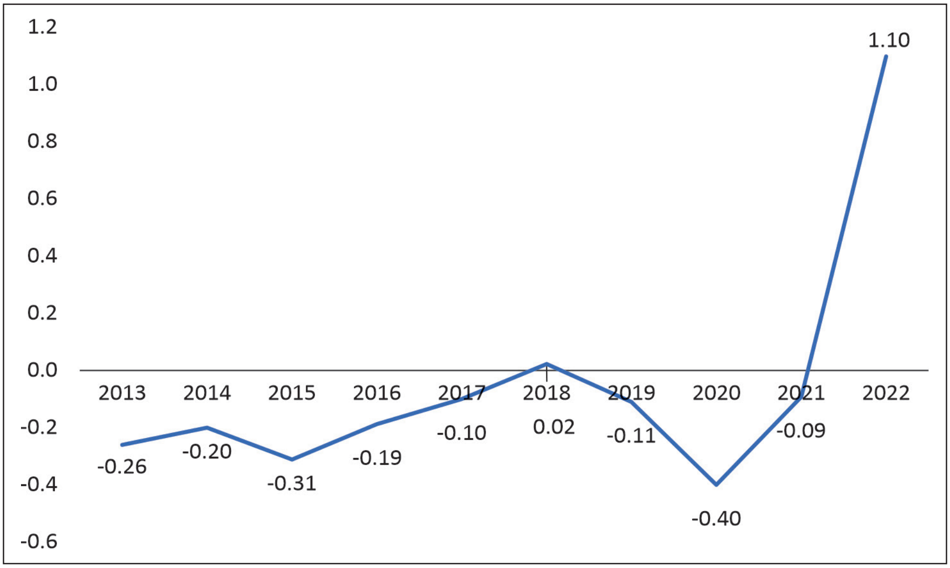
4. Global Benchmarking- Case Studies of Financing Programmes and Incentives

MSMEs are defined differently around the world. The categorisation can be based on a number of characteristics, including annual sales, number of employees, assets owned by the company, market capitalisation, or any combination of these aspects. While they may be defined differently, countries across the globe have a focus on schemes that support the growth and ensure sustainability of MSMEs. As access to finance is a major challenge for MSMEs across geographies, governments have a focus on programmes and incentives that address the financing gaps. This chapter delves into case studies and examples of government initiatives, particularly financing support across different countries for MSMEs.

Globally, since 2022, SMEs have been greatly impacted by persistent inflationary pressures and subsequent tightening of monetary policy. While inflation is on a downward trajectory, geopolitical tensions in the Middle East, their potential repercussions on energy markets, and rising price pressures due to disruptions in the Red Sea may contribute to rising inflation once again. Central banks continued to have a restrictive monetary policy for a significant period to ensure inflationary pressures are well-contained, and as a result, lending conditions have been tight.

As a result of the steep increase in policy interest rates in most countries around the world, the global cost of SME financing registered an increase in 2022. After years of low interest rates, rising inflationary pressures prompted a decisive response from central banks. The increase in policy interest rates was swiftly passed on to the real economy, resulting in higher corporate interest rates, including those for SME loans. As per an analysis by OECD covering nearly 50 countries, SME interest rate increased by 1.1 percentage points during 2022 (Exhibit 4.1). It is notable that even in 2008, during the global financial crisis, SME interest rates increased by only 0.38 percentage.

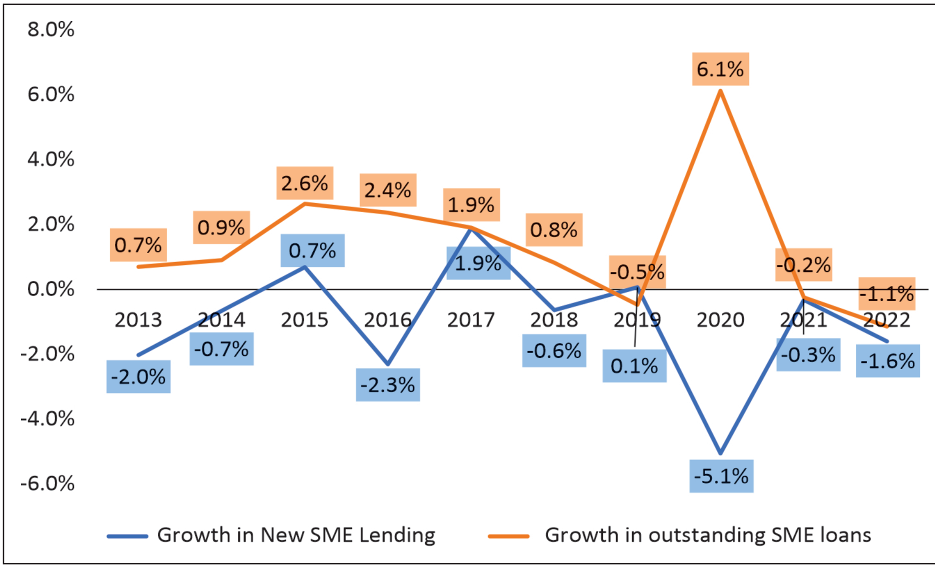
Exhibit 4.1: Changes in SME Interest Rates across 50 Countries (in Percentage Points)



Source: OECD, Exim Bank Research

Alongside the rise in interest rates, lending to MSMEs has been on a decline. As per OECD's analysis of financing conditions in nearly 50 countries, both new lending and outstanding loans to SMEs have declined, with some heterogeneity across countries. After declining in 2021 by 0.3 percent, the growth in new SME loans registered a further decline of 1.8 percent in 2022. The decline in new MSME lending can be partly explained by a reduced supply of credit. The stock of SME loans also declined, driven by a surge in repayment rates, as many SMEs tried to avoid higher borrowing costs, and by an increase in SME bankruptcies. The persistent stringent credit environment is likely to result in a continued downward trend in SME lending. In tandem with the decline in new lending in 2022, the growth the outstanding SME loans dropped by (-)1.1 percent. This decline followed negligible growth of 0.2 percent in 2021, following robust growth of 6.1 percent in 2020 (Exhibit 4.2).

Exhibit 4.2: Growth in New SME Lending and Outstanding SME Loans



Source: OECD, Exim Bank Research

Globally, governments have taken a variety of measures to help SMEs navigate the challenges posed by high inflation. These strategies are designed to ensure that SMEs have adequate access to financing amid rising costs. Immediate actions have included supporting SMEs in managing the increased expenses for energy and raw materials and enhancing lending conditions in a tight credit environment. Efforts to mitigate the impact of inflation on SMEs also include reducing late payments in both government-to-business and business-to-business transactions. Additionally, governments are facilitating access to a broad range of financial instruments to support SME investments, especially in areas like green and digital transitions. Further, there has also been a growing emphasis on promoting gender equality in access to capital.

Table 4.1: Government Policy Instruments to Foster SME Access to Finance, 2021-22

Country	Government Loan Guarantees	Direct Lending to SMEs	Subsidised Interest Rates	Special Guarantees and Loans for Startups	Venture Capital Funds (direct)	Funds of Funds	Business Angel Coinvestments	Nonfinancial Support for SMEs
Australia	X							X
Austria	X	X		X	X			X
Belgium	X	X						
Brazil								
Canada	X	X	X		X			X
Chile	X	X			X			
China		X	X	X				
Colombia				X		X	X	
Czech Republic	X	X	X		X	X		
Denmark					X	X	X	X
Estonia	X	X						
Finland	X				X	X	X	
France	X	X						
Georgia								X
Germany	X	X		X	X	X	X	X
Greece	X	X	X		X	X	X	X

Country	Government Loan Guarantees	Direct Lending to SMEs	Subsidised Interest Rates	Special Guarantees and Loans for Startups	Venture Capital Funds (direct)	Funds of Funds	Business Angel Coinvestments	Nonfinancial Support for SMEs
Hungary	X	X						X
India	X	X	X	X	X	X		X
Indonesia								
Ireland	X	X		X	X		X	X
Israel	X	X			X			X
Italy	X							X
Japan	X	X						
Kazakhstan	X	X	X					X
South Korea	X	X	X					
Latvia	X	X		X	X			X
Lithuania	X	X	X	X	X		X	X
Luxembourg	X					X		X
Malaysia								X
Mexico		X			X			X
Netherlands	X	X			X	X		X
New Zealand		X			X	X		X
Peru	X	X						

Country	Government Loan Guarantees	Direct Lending to SMEs	Subsidised Interest Rates	Special Guarantees and Loans for Startups	Venture Capital Funds (direct)	Funds of Funds	Business Angel Coinvestments	Nonfinancial Support for SMEs
Poland	X	X						X
Portugal	X							X
Serbia	X							
Slovak Republic	X	X	X	X	X			
Slovenia	X	X			X	X		X
South Africa								
Spain	X					X		
Sweden		X						X
Switzerland	X							
Thailand	X							
Turkey	X	X		X	X	X	X	X
Ukraine	X	X						
United Kingdom	X	X		X	X	X	X	X
United States	X	X				X		X

Source: OECD, Exim Bank Research

CHINA

China's MSME sector is a vital engine of economic growth, contributing significantly to employment and GDP in the country. SMEs contribute to approximately 50 percent of tax revenue, 60 percent of GDP, 70 percent of technological innovation, and 80 percent of urban employment in China. In 2022, there were about 52 million SMEs in China, and the number of newly registered enterprises reached an average of 23,800 per day[18].

Credit Scenario in China

As per the Financing SMEs and Entrepreneurs 2024 report by OECD, outstanding business loans for Micro and Small Enterprises in China increased to CNY 59.7 trillion (US$ 8,877.4 billion) in 2022, up by 19.4 percent from 2021. The share of outstanding business loans for MSEs in total outstanding business loans has been relatively stable, at 46.52 percent in 2021 and 49.12 percent in 2022, respectively. In recent years, China has improved and implemented the policy of reducing taxes and fees on debt finance. In 2022, SMEs were on average charged 1.42 percent of the total value of bank loans in the form of extra loan fees, slightly down by 0.39 percentage points as compared to the previous year.

Table 4.2: Credit Scenario of MSMEs in China

	2018	2019	2020	2021	2022
Outstanding Business Loans, Small and Medium Enterprises (RMB Billion)	33492	36900	42700	50000	59700
Share of Outstanding Loans to Small and Micro Enterprises in Total Outstanding Business Loans (%)	42.5	42.8	43.9	46.5	49.1
Interest Rate, SMEs (%)	5.17	4.9	4.8	4.5	4.5
% of Small and Micro Enterprises Needing Collateral to Obtain Bank Lending	52.5	53.2	50.9	–	–
Rejection Rate (%)	3.7	4.0	3.8	3.6	3.6
Non-performing Loans, Small and Micro Enterprises (% of all SME loans)	3.2	3.1	2.8	–	–

Source: OECD

[18] The Role of SMEs in China's Circular Economy Transition, European Union

Government Policies and Support

The Chinese government has implemented a range of policies and programmes to support MSMEs, focusing on financial support, innovation, and market access. One of the key initiatives is the establishment of SME Development Fund, which provides financing to small and medium-sized enterprises through equity investments and grants. The fund is aimed at encouraging innovation and technological advancement in the MSME sector. In 2022, this fund raised nearly CNY 90 billion (US$ 13.4 billion) and invested in more than 1,100 projects.

Further, as per the Ministry of Finance in China, the central government will allocate more than CNY 10 billion (US$ 1.55 billion) during 2021 to 2025 to support the growth of more than 1,000 “little giants”, or SMEs that focus on a market niche and master key technologies with strong innovation capacity.

In addition to financial support, China is also focusing on nurturing innovation through programmes such as the ‘Made in China 2025’ initiative. This initiative seeks to upgrade the manufacturing capabilities of Chinese MSMEs by promoting the adoption of advanced technologies and processes. The government provides subsidies and tax incentives to businesses that invest in research and development, helping them enhance their competitiveness in the global market.

China has developed a robust network of business incubators and technology parks to support start-ups and MSMEs. These facilities offer a range of services, including funding, mentorship, and access to research and development resources. By fostering a conducive environment for innovation, these incubators and technology parks have been instrumental in the success of numerous Chinese MSMEs.

The Export-Import Bank of China has developed a supply chain finance programme and linked its system to a number of third-party platforms to support the transfer of core corporate credit to micro and small enterprises upstream in the industrial value chain. The Bank has established a risk-sharing model for government-bank cooperation called Yuan Mao Dai, through which local government resources can be injected through the "local government capital pool + policy bank + on-lending bank" model to achieve better risk sharing. Focusing on cross-border logistics scenarios, the Bank developed a business plan for micro and small enterprises called "Wu Liu Dai (logistics loans)", which was successfully implemented in Shanghai and Jiangsu Province. The Bank also promoted integration of direct lending and on-lending and introduced the "Lian He Dai (joint lending)" business plan to explore new ways to develop policy based inclusive finance.

China's top economic planning authority, the National Development and Reform Commission (NDRC), along with several other government departments, has released a document, in February 2022, outlining measures to shore up support for MSMEs in the service industry. The NDRC outlines 43 policy measures to provide fiscal and logistical support for service industry businesses that have been particularly hard hit by the COVID-19 pandemic and related restrictions, in particular catering, retail, and travel. The policy list includes extension of tax reductions and exemptions, fiscal support measures, and support for implementing COVID prevention measures, among other incentives. The policy has been extended till December 31, 2024. The government has been keen to bolster support through such initiatives as uneven post-pandemic recovery continues to impact some of the most vulnerable industries and companies, particularly MSMEs.

THE USA

The US Small Business Administration (SBA) defines size standards for categorising businesses as "small business" in the USA. Size standards vary by industry and are generally based on the business' number of employees or average annual receipts. SBA issued the most recent size standards in January 2022. In addition to meeting these numerical standards, to be considered a small business by SBA, a business must be for-profit, independently owned and operated, be physically located in the USA, and may not be nationally dominant in its industry. However, generally, businesses in the USA with fewer than 500 employees are considered small businesses.

As of 2022, there are 33.2 million small businesses in the USA, which make up nearly 99.9 percent of all businesses in the USA and account for almost two-thirds of net new private sector jobs. Of those, 88 percent have fewer than 20 employees. Small businesses employ 61.7 million people, which is 46.4 percent of all employees in the USA. Of these, 56 million are employed in firms with fewer than 50 employees[19].

Credit Scenario in USA

As per the Financing SMEs and Entrepreneurs 2024 report by OECD, outstanding business loans for Micro and Small Enterprises in the USA increased to US$ 4.2 trillion 2022, from US$ 3.9 trillion in 2021. The share of outstanding business loans for MSEs in total outstanding business loans has marginally declined in 2021 to 20.34 percent as compared to 20.95 percent in 2020. The interest rate charged to SMEs also witnessed an increase from 3.13 percent in 2021 to 4.37 percent in 2022.

Table 4.3: Credit Scenario of MSMEs in the USA

	2018	2019	2020	2021	2022
Outstanding Business Loans, Small and Medium Enterprises (US$ Trillion)	3.5	3.7	4.2	3.9	4.0
Share of Outstanding Loans of Small and Micro Enterprises in the Total Outstanding Business Loans	17.9	17.3	21.0	20.3	–
Interest Rate, SMEs (%)	5.0	5.3	3.3	3.1	4.3
% of Small and Micro Enterprises Needing Collateral to Obtain Bank Lending	94.3	92.2	51.1	–	–
Rejection Rate	33.4	37.7	35.9	36.6	
Non-performing Loans, Small and Micro Enterprises (% of all SME Loans)	1.4	1.5	1.9	1.4	1.3

Source: OECD

[19] The White House, Council of Economic Advisers, 2023

Government Policies and Support

One of the primary pillars of support for MSMEs in the USA is the Small Business Administration, which was established in 1953 to aid, counsel, assist, and protect the interests of small business concerns. The SBA provides a wide range of programmes aimed at ensuring that SMEs have access to the necessary resources to thrive. A cornerstone of SBA's support is its loan programmes, particularly the 7(a) Loan Program, which is the agency's primary programme for providing financial assistance to small businesses. This programme offers loans to SMEs that might not qualify for traditional bank financing, ensuring they can secure the capital needed for expansion, operations, or startup costs. The SBA does not lend money directly but guarantees a portion of the loan, reducing the risk for lenders and making them more willing to offer loans to small businesses. The SBA's 504 Loan Program is another significant initiative, providing long-term, fixed-rate financing for major fixed assets such as land and buildings. This programme is particularly beneficial for small businesses looking to expand their physical presence or invest in major equipment.

Another notable programme of the SBA is the Paycheck Protection Program (PPP), introduced in response to the economic disruptions caused by the COVID-19 pandemic. The PPP provided forgivable loans to small businesses to cover payroll and other essential expenses, helping them to retain employees and stay afloat during the crisis. The PPP loans significantly mitigated the adverse impacts of the pandemic on the MSME sector.

Another important initiative of the SBA is the Small Business Innovation Research (SBIR) program. The SBIR programme aims to stimulate technological innovation by encouraging small businesses to engage in federal research and development projects. This programme not only provides funding but also facilitates partnerships between small businesses and federal agencies, leading to commercial successes and creation of high-tech jobs. Numerous successful companies, including Qualcomm and Symantec, have roots in the SBIR program, showcasing its effectiveness in fostering innovation and growth.

Another significant aspect of SBA support is the 8(a) Business Development Programme, which provides assistance to small businesses owned by socially and economically disadvantaged individuals. This programme helps these businesses compete in the marketplace by offering business development support and facilitating access to government contracting opportunities. The government's set-aside programmes mandate that a certain percentage of federal contracts be awarded to small businesses. The 8(a) program is instrumental in ensuring that disadvantaged SMEs benefit from these opportunities. The SBA also runs the Historically Underutilized Business Zones (HUBZone) programme, which encourages economic development in distressed areas by providing preferential access to federal procurement opportunities. The goal of the programme is to award at least 3 percent of federal contract dollars to HUBZone-certified companies each year. By helping SMEs in these areas, the HUBZone programme supports individual businesses, while also stimulating the local economies.

The Export-Import Bank of the United States (US Exim) provides various products and services for the small businesses to provide protection from commercial and political risk, access to cash flow, help with credit terms, etc. Programmes like Export Credit Insurance and Working Capital Loan Guarantee helps small businesses in safeguarding against risk, increasing sales, unlocking cash flow, and increasing global competitiveness.

There are several state and federal programmes and initiatives to support SMEs. Firstly, the R&D tax credit incentivises companies to undertake research activities. In order to take benefit of the R&D tax credit, the company must be pre-commercial, and there are a wide array of qualifying activities that allow tax claim such as prototyping, development of specific tooling, evaluation of process alternatives or improving qualities.

The Manufacturing Extension Partnerships (MEP) and the Manufacturing Innovation Institutes (Manufacturing USA) are the other programmes for helping SMEs. The MEP provides technical assistance and networking opportunities to SMEs. It has been created by the federal government and differs from the R&D tax credit as the activities that can be implemented include market research, marketing and sales, product design and development. The Manufacturing USA is a government initiative sponsored by R&D consortia focused on specific manufacturing technologies which includes SMEs but is not specifically dedicated to them. The programme rewards three main activities: R&D, technology transition and workshop development. The mission is to build an ecosystem of specialised experts and facilities.

The support provided by the US government to SMEs through the SBA and other initiatives is multifaceted and robust, addressing the diverse needs of small businesses. From financial assistance and business development services to innovation support and international trade facilitation, these programmes play a crucial role in fostering the growth and success of SMEs.

JAPAN

There are around 3.58 million SMEs in Japan[20]. SMEs in Japan accounted for 99.7 percent of all businesses and employed 33 million individuals, which is approximately 69.7 percent of the private sector labour force in 2021.

Credit Scenario in Japan

The Japanese Government offers financial support for SMEs in the form of credit guarantees and direct loans. In 2020, as a response to the COVID-19 crisis, government-affiliated and private financial institutions provided interest-free and unsecured loans[21]. As of March 2022, the total amount of outstanding SME loans was approximately JPY 314 trillion (US$ 2402 billion) provided by domestically licensed banks and credit associations; the outstanding amount of the credit guarantee programme was JPY 41.9 trillion (US$ 320.5 billion), covering 1.58 million SMEs; and the outstanding amount of direct loan programme was JPY 29.8 trillion (US$ 228.0 billion), covering 1.33 million of Japan's 3.58 million SMEs.

[20] SME Support Japan

[21] Financing SMEs and Entrepreneurs 2024, OECD

Table 4.4: Credit Scenario of MSMEs in Japan

	2018	2019	2020	2021	2022
Outstanding Business Loans, Small and Medium Enterprises (JPY Trillion)	415.0	424.7	459.3	460.0	480.1
Share of Outstanding Loans to Small and Micro Enterprises in the Total Outstanding Business Loans	67.8	67.5	68.6	70.3	70.0
% of Small and Micro Enterprises Needing Collateral to Obtain Bank Lending	29.4	28.2	26.8	26.0	
Non-performing Loans, % of All Business Loans	2.5	2.4	2.50	2.74	

Source: OECD, Exim Bank Research

Government Policies and Support

The Government of Japan has implemented several schemes and initiatives to bolster the MSME sector, focusing on financing, technological advancement, and export promotion. One of the key institutions in Japan's MSME support infrastructure is the Japan Finance Corporation (JFC). The JFC provides a variety of financial services tailored to the needs of MSMEs, including long-term loans, credit guarantees, and equity financing. The General Loans programme is particularly significant, offering low-interest loans to MSMEs for purposes such as business startup, expansion, and innovation.

In addition to direct loans, the JFC operates the Credit Guarantee Programme, which helps MSMEs secure loans from private financial institutions. Under this programme, the JFC guarantees a substantial portion of the loan, thereby reducing the risk for lenders and encouraging them to extend credit to smaller businesses. This scheme is essential for MSMEs that may lack the collateral or credit history typically required by traditional lender.

The Japan External Trade Organization (JETRO) also offers a wide range of services to help MSMEs expand their operations overseas. JETRO provides market intelligence, business matching services, and assistance with navigating foreign regulations, all of which are crucial for MSMEs looking to enter new markets.

One of the flagship initiatives of JETRO is the “Export Support Programme”, which offers comprehensive support to MSMEs aiming to increase their exports. This programme includes subsidies for participating in international trade fairs and exhibitions, which are valuable opportunities for MSMEs to showcase their products to a global audience and establish business connections. Additionally, JETRO organises business matching events and trade missions, facilitating direct interactions between Japanese MSMEs and potential foreign partners or buyer.

Japan also emphasises the importance of technological advancement and innovation in the MSME sector. The Small and Medium Enterprise Agency (SMEA) administers several programmes aimed at R&D promotion and adoption of cutting-edge technologies by MSMEs. One notable programme is the “Monozukuri Subsidy,” which provides grants to manufacturing MSMEs for investments in innovative production technologies and processes. This subsidy helps small manufacturers to improve their productivity, reduce costs, and enhance product quality, thereby boosting their competitiveness in both domestic and international markets.

Furthermore, Japan has established a network of local public technology centres across the country, which provide MSMEs with access to state-of-the-art research facilities, technical expertise, and consultancy services. These centres support small businesses in their innovation efforts, offering assistance with product development, testing, and quality assurance.

To support MSMEs in rural and economically disadvantaged areas, various regional development programmes have also been implemented by the Government of Japan. The regional revitalisation support programme provides financial assistance to MSMEs engaged in projects that contribute to the economic revitalisation of their regions. These grants support a wide range of activities, from tourism development and agricultural innovation to the revitalisation of traditional crafts and industries.

INDONESIA

As per Ministry for Economic Affairs of the Republic of Indonesia, there were 64.2 million MSMEs in Indonesia as of March 2022, that contribute 61 percent of Indonesia's GDP. In terms of workforce, MSMEs are also able to absorb 97 percent of total workforce in Indonesia, which is around 119.6 million people, thereby supporting economic inclusion and helping in poverty reduction.

Government Policies and Support

Bank Indonesia has initiated various programmes to provide affordable financing to MSMEs. The "People's Business Credit" (Kredit Usaha Rakyat, KUR) programme is a flagship initiative that offers subsidised loans to MSMEs. KUR loans are characterised by low interest rates and minimal collateral requirements, making them accessible to a broad range of small businesses. This programme aims to enhance the financial inclusion of MSMEs, enabling them to invest in business expansion, technology, and innovation.

Additionally, the Government of Indonesia has established a Micro and Small Business Credit Guarantee Program (Jamkrindo), which provides credit guarantees to financial institutions that lend to MSMEs. This programme mitigates the risk for lenders, encouraging them to offer more loans to small businesses. By reducing the risk associated with lending to MSMEs, Jamkrindo helps to increase the availability of credit and support the growth and development of these enterprises.

The Indonesian government has established several programmes to support the internationalisation of small and medium enterprises. The Ministry of Trade, through its Directorate General for National Export Development (DGNED), plays a pivotal role in this regard. DGNED offers a wide range of services to help MSMEs expand their operations overseas, including market research, export training, and participation in international trade fairs and exhibitions.

One of the notable initiatives of the DGNED is the Export Coaching Program (Program Pendampingan Ekspor), which provides comprehensive support to MSMEs with the objective of increasing their exports. This programme includes workshops on export procedures, standards compliance, and international marketing strategies. Additionally, it offers one-on-one coaching to help MSMEs develop export plans and connect with potential buyers and partners abroad. By equipping MSMEs with the knowledge and skills needed to succeed in international markets, this programme helps them to expand their reach and increase their export revenues.

Further, the Export-Import Bank of Indonesia (Indonesia Eximbank) provides financing and guarantees specifically aimed at supporting export-oriented MSMEs. Indonesia Eximbank offers various financial products, including pre-shipment and post-shipment financing, working capital loans, and export credit insurance. These financial services help MSMEs manage the risks associated with international trade, ensuring they have the necessary liquidity to fulfil export orders and expand their global presence.

To further support the internationalisation of MSMEs, the government has established the Indonesia Trade Promotion Center (ITPC) network, which operates in key global markets. ITPCs provide on-the-ground support to Indonesian MSMEs by facilitating market entry, conducting promotional activities, and offering business matching services. By providing local market intelligence and networking opportunities, ITPCs play a crucial role in helping MSMEs navigate foreign markets and establish successful international partnerships.

The Indonesian government also recognises the importance of supporting MSMEs in rural and economically disadvantaged areas. The One Village One Product (OVOP) programme is a key initiative aimed at promoting regional economic development through MSME support. OVOP encourages villages to develop and market unique local products, by providing financial assistance, training, and marketing support. By fostering local entrepreneurship and creating sustainable economic opportunities, OVOP helps to reduce regional disparities and promote inclusive economic growth. In this context, Indonesia Exim Bank’s “Go Export Village” programme supports the initiative through training, mentoring and assistance in production facilities.

BRAZIL

Micro and small enterprises form an essential part of the Brazilian economy, accounting for 93.7 percent of all legally constituted companies (20.3 million) according to the Enterprise Map, as of December 2023[22]. Registered MSMEs provide over 50 percent of all jobs in the formal sector in Brazil.

Credit Scenario in Brazil

Access to finance is a critical challenge for MSMEs in Brazil. The share of SMEs in total outstanding loans has reduced from 50.1 percent in 2007 to 44.7 percent in 2022. However, the outstanding business loan to SMEs has increased from BRL 497 billion (approx. US$ 136.2 billion) in 2018 to BRL 938 billion (approx. US$ 181.8 billion) in 2022.

Table 4.5: Credit Scenario of MSMEs in Brazil

	2018	2019	2020	2021	2022
Outstanding Business Loans, Small and Medium Enterprises (BRL Billion)	497	533	700	821	938
Share of Outstanding Loans, Small and Micro Enterprises % of total Outstanding Business Loans	34.5	37.3	39.9	42.67	44.7
Interest Rate, SMEs (%)	22.4	24.6	11.6	17.9	23.7
Non-performing Loans, Small and Micro Enterprises (% of SME Loans)	4.6	3.6	2.1	2.62	3.5

Source: OECD, Exim Bank Research

Government Policies and Support

The Brazilian government, through institutions like the Brazilian Development Bank (BNDES), provides several financial products tailored to the needs of MSMEs. The Special Agency for Industrial Financing (FINAME), a subsidiary of BNDES provides financing for acquisition of machinery and equipment produced domestically, thereby supporting MSMEs in their efforts to

[22] OECD

modernise their production capabilities. The programme offers long-term loans with favourable interest rates, enabling MSMEs to enhance their productivity and competitiveness.

BNDES is also improving access to credit for MSMEs through digitalisation of financial intermediation. Towards this, BNDES has developed a one-stop digital platform, Canal MPME to facilitate access to information for borrowers, automate procedures for loan applications and offer a range of online services.

Further, the BNDES Automático – Projetos de Investimento, supports investment projects of MSMEs in all sectors, mainly related to construction, expansion, or reform of facilities (store, warehouse, storage, factory, office, etc.), including acquisition of machinery, equipment, software, and related services accredited by BNDES.

The PROEX (Export Financing Program), managed by BNDES, is another crucial support mechanism for MSMEs. PROEX offers pre-shipment and post-shipment financing, ensuring that MSMEs have the liquidity needed to fulfil export orders and manage cash flow effectively. Additionally, PROEX provides export credit insurance, which protects MSMEs against the risks associated with international trade, such as buyer insolvency and political instability. This comprehensive support helps to reduce the financial risks of exporting and encourages more MSMEs to explore international markets.

The Brazilian Trade and Investment Promotion Agency (Apex-Brasil) also offers a range of services to help MSMEs enter and succeed in international markets, including market intelligence, business matchmaking, and support for participation in trade fairs and missions.

One notable initiative of Apex-Brasil is the PEIEX (Export Qualification Programme), which provides training and technical assistance to MSMEs aiming to begin their exports journey. This programme helps businesses understand international trade requirements, develop export strategies, and identify potential markets. By equipping MSMEs with the necessary skills and knowledge, PEIEX helps them navigate the complexities of international trade and increase their export revenues.

SOUTH AFRICA

As per estimates, there are approximately 2.8 million MSMEs operating in South Africa. These enterprises are pivotal in driving economic growth, accounting for about 36 percent of the country's GDP, and approximately 60 percent of the total employment in the formal sector.

Government Policies and Support

The Government of South Africa has developed several financing schemes for the growth and sustainability of MSME sector. One of the key institutions in this effort is the Small Enterprise Finance Agency (SEFA). SEFA offers a range of financial products, including loans, credit guarantees, and equity financing, specifically tailored for MSMEs. The agency's mandate is to promote economic development by providing accessible and affordable financial services to small businesses that might not qualify for traditional bank financing.

A notable initiative under SEFA is the Direct Lending Programme, which provides loans to MSMEs for various purposes, such as working capital, asset acquisition, and business expansion. These loans are characterised by favourable interest rates and flexible repayment terms, designed to meet the unique needs of small businesses. SEFA also administers the Credit Guarantee Scheme, which helps MSMEs secure loans from private financial institutions by guaranteeing a portion of the loan amount. This reduces the risk for lenders and encourages them to extend credit to small businesses, thereby increasing the overall availability of financing for MSMEs.

In addition to SEFA, the Industrial Development Corporation (IDC) plays a significant role in financing MSMEs, particularly those in the industrial sector. The IDC provides a variety of financial products, including term loans, bridging finance, and equity investments, to support the growth and development of small enterprises. The Gro-E Youth Scheme is a targeted initiative by the IDC, offering financial support to young entrepreneurs aged 18-35. This scheme aims to encourage youth entrepreneurship and reduce unemployment by providing access to finance and business development services.

Further, the Department of Trade, Industry and Competition (DTIC), through its various programmes and agencies, provides extensive support for the internationalisation of MSMEs. One of the key initiatives is the Export Marketing and Investment Assistance (EMIA) Scheme, which offers financial support to MSMEs for their export promotion activities. The EMIA scheme covers costs related to participation in international trade fairs, exhibitions, and business missions, helping MSMEs to showcase their products and services to global markets.

Additionally, the South African Export Development and Promotion (SAEDP) Programme focuses on enhancing the export readiness of MSMEs. This programme provides training and technical assistance to help businesses understand international trade regulations, develop export strategies, and identify potential markets. By equipping MSMEs with the necessary skills and knowledge, the SAEDP programme facilitates their entry into global markets and increases their export revenues.

The Export Credit Insurance Corporation of South Africa (ECIC) offers export credit insurance to MSMEs, protecting them against the risks associated with international trade, such as non-payment by foreign buyers and political instability. This insurance coverage reduces the financial risks for exporters and encourages more MSMEs to explore international markets. ECIC also provides pre- and post-shipment financing, ensuring that MSMEs have the liquidity needed to fulfil export orders and manage cash flow effectively.

CONCLUSION

In conclusion, the support provided to SMEs across different markets exhibits some similarities, on account of the common challenges faced by the sector across countries. Globally, countries have implemented measures such as subsidised loans and credit guarantees, to alleviate the financing challenges for SMEs. Further, some countries have specific programmes for alleviating export marketing related challenges. There is also a focus on promoting entrepreneurship and innovation.

Apart from these commonalities, there are some differentiated programmes and initiatives that address specific local needs in countries. For instance, in Indonesia, the OVOP and Go Export Village programmes support regional economic development by promoting unique local products . Further, in Brazil, BNDES has developed a one-stop digital platform, Canal MPME to facilitate access to information for borrowers, automate procedures for loan applications and offer a range of online services.

5. Challenges and Strategies

The Government of India has set a target of US$ 2 trillion for exports by 2030. Achieving this target will critically hinge on enhancing the export orientation of MSMEs. As per the data from DGCIS, exports by MSMEs is provisionally estimated at US$ 127.5 billion during 2023-24, accounting for about 29.2 percent of India's merchandise exports during the year[23]. However, only 1 percent of Udyam-registered MSMEs are currently exporting. This highlights the substantial untapped export potential in the sector. MSMEs face myriad challenges that hinder their growth and sustainability. It is important to address these challenges to unleash the potential of this sector and enhance their participation in exports. This chapter focuses on identifying the challenges faced by MSMEs and recommending actionable strategies that can be adopted to overcome the challenges and strengthen the MSME sector.

RESULTS OF THE SURVEY OF MSMEs

With the objective of understanding the needs of the MSME sector and identifying the key obstacles faced by them, Exim Bank conducted a survey of MSMEs across various industries.

Of the survey respondents, 98.1 percent were already registered on the Udyam Portal. Nearly 56.1 percent of the survey respondents were small enterprises, 25.2 percent were medium enterprises, and 18.9 percent were micro enterprises.

As discussed in Chapter 1, there is dominance of males in ownership of MSMEs. In the survey as well, majority of the responses (83.2 percent) came from male-owned MSMEs. Majority of the respondents were engaged in

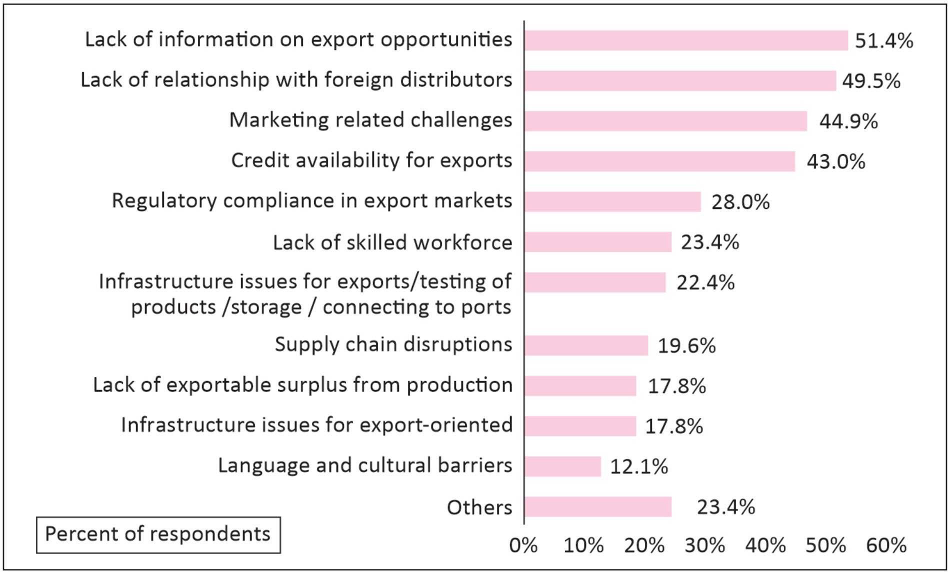
[23] This data is based on the active Udyam status of the MSMEs and valid IEC status.

manufacturing activity, accounting for 75.7 percent of the total respondents, while 4.7 percent of the respondents were engaged in only services, and 19.6 percent were engaged in both manufacturing and services. Nearly 72 percent of the respondents are also engaged in exports, which would help in better understanding of the challenges faced by MSMEs in exports.

As per the survey, lack of information on export opportunities is one of the major challenges faced by Indian MSMEs in exports, with 51.4 percent of the respondents considering this as a challenge. Lack of relationship with foreign distributors, agents and customers is another major challenge faced by Indian MSMEs in realising the export potential.

MSMEs also reported significant difficulties in marketing their products internationally, which is essential for gaining visibility and finding customers. A considerable percentage of respondents (43.0 percent) also faced challenges in obtaining the necessary financial support for exports. Navigating the complex regulatory frameworks of different export markets can also be daunting, with nearly 28.0 percent of the respondents reporting challenges in complying with regulations in export markets (Exhibit 5.1).

Exhibit 5.1: Key Challenges Faced by MSMEs in Exports



Note: Based on survey of 107 respondents.

Source: Exim Bank Research

FOCUS PRODUCTS AND MARKETS FOR DIVERSIFICATION OF MSME EXPORTS

Analysis of MSMEs' export patterns indicates a significant concentration in resource-intensive and low value-added products. For instance, only 3 out of the top 10 products (non-oil) exported by MSMEs in FY24 were high value-added/ high technology-intensive products, while the rest were either resource-intensive or low value-added goods. In contrast, 6 out of 10 top exported products in India's non-oil exports comprised high value-added/ high technology-intensive products during the same period. Enhancing production capacities in higher value-added products would be crucial for a substantive increase in exports from the MSME sector and imparting resilience to India's exports basket. An attempt has been made to identify focus products and destinations for diversification of MSME exports from India. An attempt has also been made to develop strategies for MSMEs to move up the value chain.

Table 5.1: Focus Products and Select Strategies for MSMEs to Move up the Value Chain

Sector	Existing Key Products Exported by MSMEs	Prospective High Value-Added Exports for MSMEs	Select Strategies for Enhancing MSME Exports
Gems and Jewellery	Gold and other precious metal jewellery; Pearls, precious and semi-precious stones	Lab-grown diamonds	Lab-grown diamonds are diamonds made in laboratories and factories, that are identical to natural diamonds in appearance and composition. The global lab-grown diamonds market was valued at US$ 24 billion in 2022, and is expected to reach US$ 59.2 billion by 2032, recording a CAGR of 9.6 percent[24]. Factors such as affordability, sustainability and similarity in characteristics with that of natural diamonds have been the key growth drivers for the surge in demand for lab-grown diamonds across the world.

[24] Allied Market Research

Sector	Existing Key Products Exported by MSMEs	Prospective High Value-Added Exports for MSMEs	Select Strategies for Enhancing MSME Exports
Gems and Jewellery	Gold and other precious metal jewellery; Pearls, precious and semi-precious stones (Contd...)	Lab-grown diamonds (Contd...)	With the rise in demand for lab-grown diamonds, India's export of polished lab grown diamonds are also growing, reaching an estimated US$ 1.4 billion during 2023-24. The USA is the largest consumer of lab-grown diamonds in the world, and is the topmost destination for India's exports of the product. Given that gems and jewellery sector is already an important export-oriented sector for MSMEs, exporters in this sector could focus on diversification towards lab-grown diamonds segment.
Agriculture and Allied Sector	Marine Products	Organic Aquaculture	Opportunities can be explored in the area of organic fish farming, also known as organic aquaculture, so as to obtain a premium pricing for fishery products in the overseas markets. Organic aquaculture is a developing sector wherein farmers produce a wide range of aquatic species – including fish, seaweeds and molluscs – in line with organic principles, thereby ensuring animal welfare, good water quality and human health. Environmentally conscious consumers around the world are willing to pay a higher price for such organic marine products.

Sector	Existing Key Products Exported by MSMEs	Prospective High Value-Added Exports for MSMEs	Select Strategies for Enhancing MSME Exports
Agriculture and Allied Sector	Basmati and Non-Basmati Rice	Gluten free products made of processed rice - snacks, ready to cook/ ready to eat products such as rice-based noodles, fermented rice flour, bakery products etc. Millet-based products	Diversification of exports towards high value-added cereal preparations like snacks, ready to cook/ ready to eat products including pasta and noodles made from rice and/or millets, fermented rice flour, puffed or flaked cereals items, can garner greater revenues for MSME exporters in the sector. Owing to the increasing incidences of lifestyle diseases due to gluten-resistance, as well as rising fitness consciousness across the world, the demand for gluten-free food products is increasing. These gluten-free food products are typically characterised by high fibre and low caloric content and have significant health benefits. According to recent research, the global market for gluten-free food products stood at an estimated US$ 6.5 billion in 2022 and is expected to register a robust CAGR of 9.8 percent during 2023 to 2030. Opportunities emerging in the gluten-free food industry can be tapped through encouragement for capacity expansion in processed cereal items, particularly those made from rice and millets. Developed countries from North America and Europe including the USA, Canada, Germany, and France are expected to be the top markets for gluten-free products, going forward[25]. These markets could be targeted for exports of gluten-free preparations.

[25] ISI Emerging Markets- Grand View Research

Sector	Existing Key Products Exported by MSMEs	Prospective High Value-Added Exports for MSMEs	Select Strategies for Enhancing MSME Exports
Agriculture and Allied Sector	Spices	Spice oleoresins	Oleoresins have high potency of active components that enable their usage in small dosages, while also leading to standardisation in taste and consistency. They find application in industries such as beverages, confectionery, meat canning, sauces, pharmaceuticals, seasonings etc. The global market for oleoresins is estimated to be valued at US$ 1.8 billion in 2023 and is expected to register strong CAGR of 6.9 percent during 2024 to 2030, to reach US$ 2.8 billion by 2030. Exporters could target European countries such as the UK, Germany, Belgium, France, Spain, and Austria, which are among the top markets for spice oleoresins in the world[26]. For building capacities in the segment, states which are among the top producers of spices in India could incentivise investments by developing spices park. Such spices park could be set up under a public private partnership mode, with facilities such as spices processing units as well as common processing and value addition facilities such as cleaning, sorting, grading, grinding, oil extraction, and packaging of spices for use by the local farmers, traders, exporters, and other stakeholders.

[26] Ibid.

Sector	Existing Key Products Exported by MSMEs	Prospective High Value-Added Exports for MSMEs	Select Strategies for Enhancing MSME Exports
Agriculture and Allied Sector (Contd...)	Spices (Contd...)	Spice oleoresins (Contd...)	The spices parks with specialised infrastructure and services would reduce investment needs by MSMEs in the segment and enable them to build capabilities to move up the value chain.
Pharmaceuticals	Drug formulations and biologicals	Focus on biosimilars	Globally, the demand for biologics is growing steadily as they can be used to treat and manage several chronic diseases including cancer, diabetes, infectious disorders, hormonal disorders, etc[27]. Biosimilars are highly similar biological products that are made using state-of-the-art technology to be comparable in characteristics to the reference biologics in terms of purity, bioactivity, and chemical identity. Significant opportunities exist for biosimilar exporters in markets such as Europe and the USA due to increasing acceptability of these drugs. Patents for 24 major blockbuster drugs with a combined sales value of US$ 149.5 billion in 2022 are going to expire during the period 2022-2030[28].

[27] Biologics are products derived from living organisms like bacteria, as well as from mammals, plants, and animals through genetic engineering. Some of the commonly known biologics include monoclonal antibodies (MABs), vaccines, recombinant proteins, antisense, RNAi, molecular therapy, among others

[28] Department of Pharmaceuticals, GOI (2023), Analysis on Leveraging the Patent Cliff

Sector	Existing Key Products Exported by MSMEs	Prospective High Value-Added Exports for MSMEs	Select Strategies for Enhancing MSME Exports
Pharmaceuticals (Contd...)	Drug formulations and biologicals (Contd...)	Focus on biosimilars (Contd...)	A blockbuster drug is an extremely popular drug that generates at least US$ 1 billion worth of annual sales revenue for the pharmaceutical company that produces them. This patent expiry is expected to create significant opportunity for biosimilar players, due to loss of exclusivity of these patented drugs. To tap the opportunities emerging in the segment, it would be crucial for MSMEs to enhance their R&D spendings. Drugs and pharmaceuticals industry is characterised by high requirement for R&D spending. As per Economic Survey 2023-24, the average R&D spending in the pharmaceuticals industry during FY19-FY21 was the highest among all industries. To incentivise R&D spending, particularly by MSMEs, the GOI could consider reinstating Income Tax deduction on expenditure incurred on R&D that was available earlier till 2016-17. Before 2016-17, the Central government provided a weighted tax deduction of 200 percent for any capital and revenue expenditure incurred on in-house R&D by a company, excluding expenditure on land and buildings. The Finance Act, 2016 restricted the availability of expenditure incurred on scientific research to 150 percent from April 1, 2017 and no weighted deduction from April 1, 2020. Reinstating this tax

Sector	Existing Key Products Exported by MSMEs	Prospective High Value-Added Exports for MSMEs	Select Strategies for Enhancing MSME Exports
Pharmaceuticals (Contd...)	Drug formulations and biologicals (Contd...)	Focus on biosimilars (Contd...)	incentive would be important to boost the R&D spending. Government could also consider providing dual tax credit allowances system that rewards both incremental expenses in R&D, as well as the level of spending in R&D, as provided by countries such as Canada.
Textile	Cotton readymade garments, fabrics, made-ups	Synthetic yarns, fabrics, made-ups and garments of man-made fibres; blended yarns, fabrics, made-ups and garments Technical textiles	The global technical textile market was valued at an estimated US$ 188.1 billion in 2022 and is expected to record a CAGR of 4.7 percent during 2023 to 2030, owing to greater awareness about the uses of technical textiles in various end-user industries. The global synthetic fibers market size was valued at US$ 66.1 billion in 2022 and is expected to register a CAGR of 7.4 percent from 2023 to 2030. Increasing consumer demand for cost-effective, durable, easy-to-wash, and maintainable fabrics is expected to drive the market in the forthcoming years. In addition, rising product applications in automobiles for seat covers, cushions, drive belts, airbags, and others are further adding to the market growth. The USA, EU, Central and South America could be targeted for exports of these products, as the demand in these regions are expected to grow significantly.

Sector	Existing Key Products Exported by MSMEs	Prospective High Value-Added Exports for MSMEs	Select Strategies for Enhancing MSME Exports
Automotive	Auto components/ Parts	Parts and Components for Electric Vehicles / hybrid vehicles	India currently relies on China for 60-70 percent of key EV components, including lithium-ion battery cells, e-motor magnets, and other electronics[29]. Localising production of EV components would help MSMEs to move up the automotive value chain. Once substantial capacities are built locally, expansion towards exports may also be targeted by MSMEs. In order to foster innovation in this segment, the government could consider introducing an innovation-linked incentive programme, particularly for next-generation technologies like fuel cells, hydrogen-fuelled internal combustion engines, and smart mobility etc., in addition to the current Production Linked Incentive scheme. Under this, manufacturing companies that drive breakthrough innovations in EV parts, smart mobility cars and related areas could be extended tax incentives on R&D spending and/ or other incentives, such as capex subsidies for R&D-related expenditures[30].

[29] Bain and Co (2023), India Electric Vehicles Report

[30] PWC(2024), VIKSIT: An approach for India to achieve USD 1 trillion exports

Sector	Existing Key Products Exported by MSMEs	Prospective High Value-Added Exports for MSMEs	Select Strategies for Enhancing MSME Exports
Electronics	Telecom Instruments; Electronic components	Strategic electronics such as drones and defence electronics	The global drone market size stood at nearly US$ 64.3 billion in 2023 and is expected to record a CAGR of 14.5 percent during 2024 to 2030. Markets such as the USA, EU, the UK, Saudi Arabia, South Africa, China are expected to drive the demand for drones in the forthcoming years. Strategic electronics, such drones and defence electronics, will also be essential considering India's rising domestic consumption and export focus. Rather than concentrating solely on the assembly of strategic electronic, MSMEs in the segment need to consider building capacities for backward integration for localising production and integrating in high-value operations like component manufacturing, design, and research.

Source: Exim Bank Research

An attempt has been made to identify markets with potential for enhancing exports from MSMEs. For this purpose, the share of MSMEs in India's non-oil exports to various destinations is benchmarked against the share of MSMEs in India's overall non-oil exports in FY24. Based on this analysis, it is noted that several of India's key destinations for non-oil exports remain under-tapped by MSMEs. These include some of India's top export destinations such as the USA, Saudi Arabia, Hong Kong, the Netherlands, Italy, Singapore, Belgium, among others (Table 5.2). There is substantial scope for MSMEs to enhance their exports in these top markets that are currently under-tapped, given the considerable import demand in these countries.

Table 5.2: Target Countries for Expanding Export Footprint of MSMEs

Country	Share of MSME in India's Non-oil Exports to the Country in FY24	India's Non-Oil Exports to the Country in FY24 (US$ Bn)	Total Non-Oil Imports by the Country in 2023 (US$ Bn)
The USA	35.1%	71.7	2905.9
Saudi Arabia	31.5%	10.7	153.9
Hong Kong	34.9%	8.2	641.0
The Netherlands	34.1%	8.1	520.2
Italy	31.4%	8.0	546.3
Singapore	19.8%	7.5	335.2
Belgium	26.9%	6.7	460.9
Turkey	24.4%	5.7	292.7
Malaysia	28.1%	5.6	215.1
Mexico	21.4%	5.3	555.2
Brazil	19.6%	5.2	204.1
Japan	26.8%	5.0	591.2
Thailand	33.5%	5.0	236.9
South Korea	25.4%	5.0	471.2
Nepal	29.8%	5.0	7.8
Indonesia	26.0%	5.0	181.6
South Africa	22.2%	4.4	84.8
Sri Lanka	33.5%	3.4	12.3
Philippines	29.0%	2.0	112.6
Taiwan	28.6%	1.6	301.8
World	36.1%	352.8	20213.9

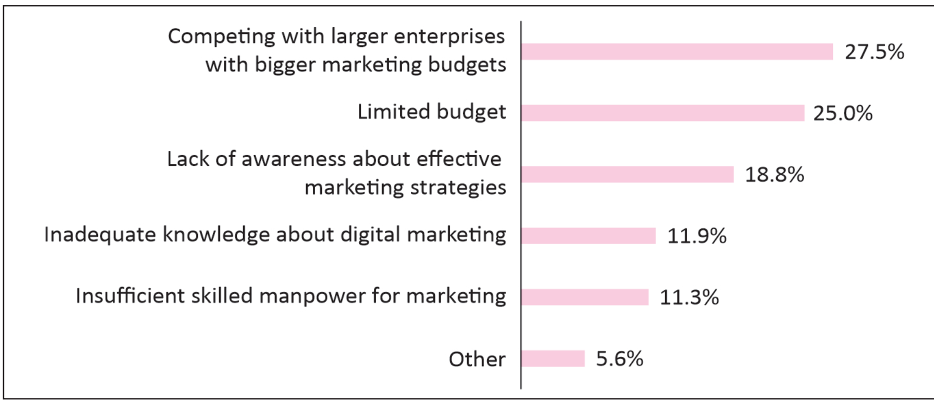
Source: ITC Trademap; DGCI&S; Ministry of MSMEs; Exim Bank Research

STRENGTHENING MARKETING AND BRANDING EFFORTS

As per the survey, one of the most pressing concerns for MSMEs is marketing. MSMEs face marketing-related problems due to their limited size and scale of operation. The marketing issues can be characterised as internal marketing issues and external marketing issues.

Internal marketing issues are due to lack of awareness about recent market demands and marketing strategies, limited budget and lack of skilled manpower. These are also external marketing issues such as competition from larger enterprises with bigger marketing budgets.

Exhibit 5.2: Challenges in Marketing



Source: Exim Bank Research

Intense competition from established brands is a key challenge cited by MSMEs in Exim Bank's survey. Large corporations with well-established brands can afford to invest heavily in export marketing and branding activities, creating significant barriers for MSMEs trying to compete in the sector. In the survey conducted by Exim Bank, 27.5 percent of the respondents considered competing with larger enterprises with bigger marketing budgets as a major problem.

Another significant challenge faced by MSMEs in India is the lack of resources. Unlike large enterprises that can allocate substantial budgets to marketing and branding activities, MSMEs often operate on tight financial margins. This lack of financial resources limits their ability to invest in comprehensive marketing campaigns, high-quality advertising, and brand development activities. The high costs associated with traditional advertising mediums such as television, radio, and print can be prohibitive for MSMEs, preventing them from reaching a broader audience. As a result, these enterprises struggle to build brand awareness and recognition, which are critical for attracting and retaining customers. In the survey conducted by Exim Bank, 25.0 percent of the respondents considered limited budget as a major problem for the marketing related issues.

Digital marketing is a low-cost alternative, but 11.9 percent of MSMEs in the survey indicated inadequate knowledge about this. Clearly, several MSMEs in India are unable to keep pace with the technological advancements that can ease their marketing efforts. This technological gap also puts MSMEs at a disadvantage compared to larger competitors who can effectively utilise these tools to reach and engage their target audience.

Furthermore, inadequate marketing knowledge and expertise pose a significant challenge for MSMEs. Many small business owners lack training in marketing strategies. This lack of training and expertise results in missed opportunities for market penetration and growth, as MSMEs fail to effectively communicate their value propositions to potential customers.

Another critical issue is the difficulty in establishing a strong brand identity. A unique and compelling brand identity is essential for differentiating a business from its competitors. However, MSMEs often lack the resources and expertise needed to create and maintain a distinct brand image.

The marketing efforts of MSMEs are frequently localised, focusing on their immediate geographical area and lacking the scale to expand beyond these boundaries. This limited reach restricts their customer base and hampers growth opportunities. In an increasingly globalised market, the ability to reach and engage with customers beyond local boundaries is critical for business expansion and competitiveness. However, without the necessary resources and infrastructure, MSMEs find it challenging to tap into new markets and grow their business.

To overcome these challenges, MSMEs need to adopt effective strategies that leverage available resources, embrace cost-effective marketing techniques and enhance their marketing knowledge and capabilities.

One of the most promising approaches is leveraging digital marketing, which offers a cost-effective way for MSMEs to reach a broad audience and compete with larger enterprises. By utilising social media platforms, MSMEs can engage with their target audience, build brand awareness, and drive sales. Creating and sharing valuable content, running targeted ad campaigns, and engaging with customers through social media can significantly enhance an MSME's marketing efforts. Adopting innovative branding techniques can help MSMEs differentiate themselves in the market. Storytelling, creating a unique brand voice, and emphasising brand values can help build a connection with customers. Consistent branding across all touchpoints, including packaging, advertising, and customer interactions, can reinforce brand identity and recognition.

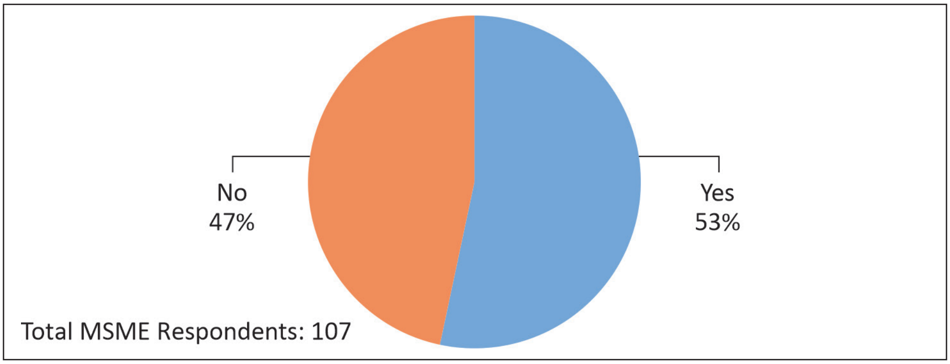
The Government of India offers support to assist exporters in their marketing efforts through schemes such as the MDA and the MAI, with the objective of enhancing market access for exporters in both new and existing markets. To effectively support the growth and international competitiveness of MSMEs, the GOI could consider consolidating and streamlining the schemes and pooling the funds from these programmes. A unified, streamlined programme would be easier for MSMEs to navigate and access. The consolidated scheme could be made exclusively available to MSMEs. By doing so, the government can create a more targeted and impactful support system for MSMEs, ensuring that their limited resources are focused on those businesses that need them the most.

Moreover, the scope of consolidated scheme could be extended beyond just participation in events and conducting market studies, to include funding support for critical areas such as brand building, preparation of marketing materials, etc. This would better position MSMEs to enter and compete in global markets.

ALLEVIATING FINANCING RELATED CHALLENGES FOR MSMEs

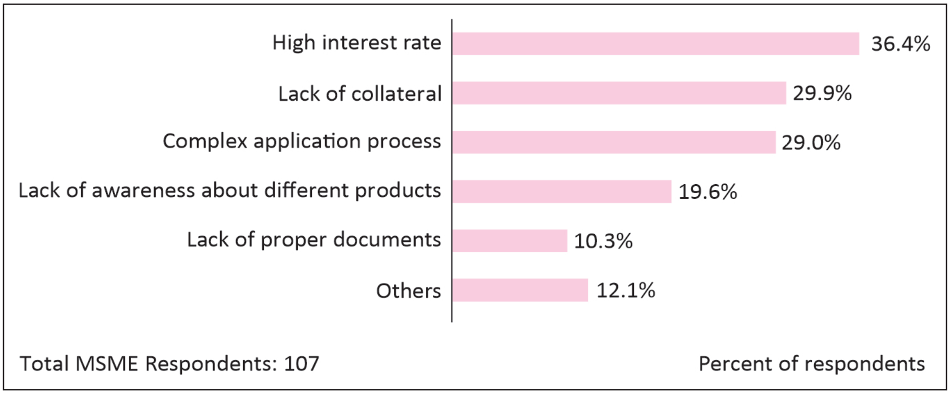
Analysis of the survey responses indicate that nearly 53 percent of the respondent MSMEs found it challenging to obtain financing for their businesses from the banking sector (Exhibit 5.3). Majority of the respondent MSMEs found high interest rates as the topmost challenge in securing financing, particularly for export business. Besides high interest rates, some of the other key challenges faced by MSMEs in securing financing included lack of collateral, complex application process, lack of awareness about different products and lack of proper documents (Exhibit 5.4).

Exhibit 5.3: Share of MSME Respondents Facing Challenges in Obtaining Financing from Banking Sector



Source: Exim Bank's Survey of MSMEs

Exhibit 5.4: Key Challenges in Securing Financing for MSME Exporters



Source: Exim Bank's Survey of MSMEs

Data from the RBI corroborates some of these findings. Comparison of the Weighted Average Lending Rate (WALR) of SCBs on fresh rupee loans and outstanding loans for MSMEs is notably higher than that of the loans for large industries and infrastructure sectors. As on end-March 2024, the WALR of SCBs on fresh rupee loans to MSMEs stood at 9.99 percent, while the WALR on fresh rupee loans to large industries and infrastructure stood lower at 8.39 percent and 8.74 percent, respectively. Likewise, WALR on outstanding rupee loans of SCBs to MSMEs stood at 10.31 percent as on end-March 2024, as compared to 8.69 percent for large industries and 9.11 percent for infrastructure sector (Table 5.3).

Table 5.3: Comparison of WALR of SCBs on Loans to MSMEs vis-à-vis Select Industry Categories

As on End	Industry (Large)	MSMEs	Infrastructure Sector	Trade Sector
WALR on Fresh Rupee Loans by SCBs (Percent)				
Mar-22	6.5	8.7	7.1	7.4
Mar-23	8.3	9.8	8.6	8.9
Jun-23	8.2	9.8	8.5	8.7
Sep-23	8.1	9.8	8.5	8.9
Dec-23	8.1	9.9	8.4	8.9
Mar-24	8.4	10.0	8.7	8.5
WALR on Outstanding Rupee Loans by SCBs (Percent)				
Mar-22	7.8	9.3	8.3	8.1
Mar-23	8.8	10.3	9.0	9.5
Jun-23	8.8	10.3	9.1	9.5
Sep-23	8.8	10.5	9.1	9.5
Dec-23	8.7	10.5	9.1	9.6
Mar-24	8.7	10.3	9.1	9.5

Source: RBI

With the monetary tightening in the economy since May 2022, the WALR across different industry categories, for both fresh rupee loans and outstanding loans, have increased steadily. In the case of MSMEs, the WALR on fresh rupee loans by SCBs increased by about 133 basis points, from 8.66 percent as on end-March 2022 to 9.99 percent as on end-March

2024, while the WALR on outstanding rupee loans by SCBs to MSMEs rose by about 103 basis points during the same period.

Besides interest rates on MSME loans, the interest rates on short term rupee export credit have also increased steadily since 2022. As on end-March 2022, the maximum median interest rate on outstanding pre-shipment rupee export credit (up to 180 days) from public sector banks stood at 10.7 percent and has increased by 220 basis points over a two-year period to reach 12.9 percent as on end-March 2024. Likewise, the maximum median interest rates on post-shipment export credit like demand bills has grown by a substantial 697 basis points, while that of usance bills (91-180 days) has grown by 118 basis points during the same period. This is indicative of the significant hike in cost of credit for export sector, which may further exacerbate the already constrained access to finance for MSMEs (Table 5.4).

Table 5.4: Median Range of Interest Rates on Outstanding Rupee Export Credit by SCBs

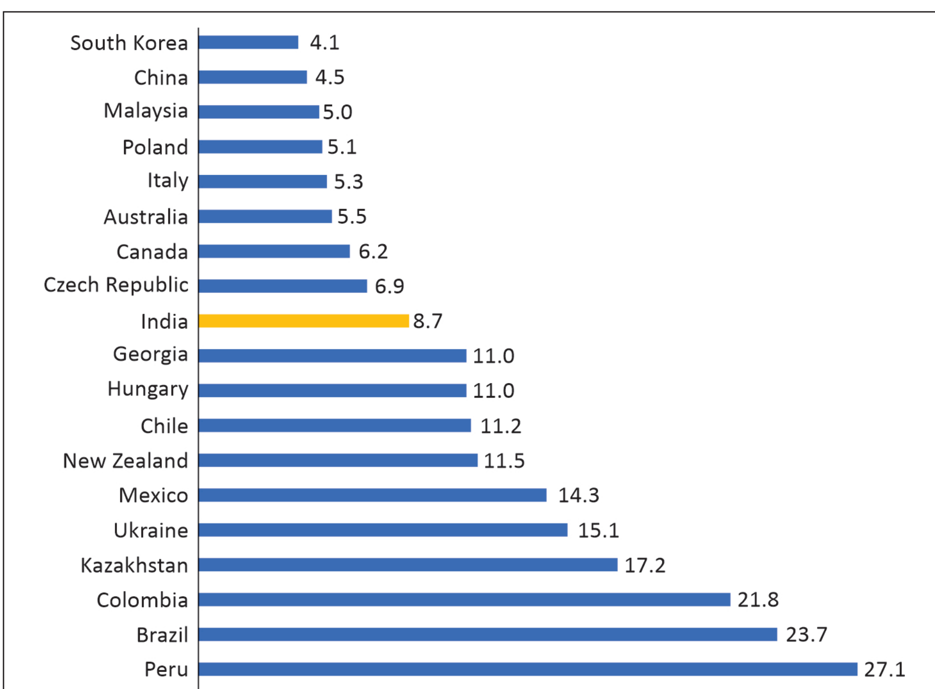
Bank Group	Pre-shipment Credit		Post-shipment Credit					
			Demand Bills		Usance Bills			
	Upto 180 days				Upto 90 days		91 to 180 days	
	Min	Max	Min	Max	Min	Max	Min	Max
(Percent per annum)								
For Quarter ended-March 2022								
Public Sector Banks	7.0	10.7	4.9	9.1	5.6	10.7	7.2	10.2
Pvt. Sec. Banks	5.4	12.7	7.5	10.7	5.9	11.7	5.3	12.0
Foreign Banks	4.1	8.0	9.4	16.0	4.4	7.7	5.1	7.5
For Quarter ended-March 2023								
Public Sector Banks	6.0	10.9	6.9	12.0	7.4	11.5	8.2	10.9
Pvt. Sec. Banks	6.4	13.8	6.4	12.8	6.2	13.4	6.2	12.5
Foreign Banks	7.0	9.2	10.0	12.0	7.1	8.8	6.9	8.8
For Quarter ended-March 2024								
Public Sector Banks	6.5	12.9	7.5	16.1	7.2	14.0	8.6	11.4
Pvt. Sec. Banks	6.6	14.1	8.2	10.6	7.5	12.5	7.5	11.9
Foreign Banks	7.4	10.0	10.4	12.4	8.1	9.2	7.2	9.3

Source: RBI; Exim Bank Research

The rising financing costs in India align with a global trend of increasing interest rates for business loans. Since 2022, the global financing costs have surged, as governments around the world are tightening monetary policy to combat rising inflation. Central banks' responses, characterised by significant hikes in policy interest rates, have been transmitted to the real economy, markedly affecting corporate interest rates, particularly for MSMEs. According to the OECD Financing SMEs and Entrepreneurs 2024 report, all countries registered an increase in SME interest rates during 2022.

The interest rates on fresh rupee loans to MSMEs in India as of March 2022 were compared with the interest rates for MSMEs in select countries in 2022. The results indicate that India's interest rates for MSME loans were lower than in Brazil, Mexico, and New Zealand, but higher than in South Korea, China, Malaysia, and Australia (Exhibit 5.5).

Exhibit 5.5: Interest Rates for MSME Loans in Percentage (2022)



Source: OECD Financing SMEs and Entrepreneurs 2024 Report, RBI, Exim Bank Research

Rationalising Interest Rates for MSMEs

Reinstating the Interest Subvention Scheme for MSMEs

An important way for easing the cost of credit for MSMEs in the current high interest rate environment could be the reinstatement of the interest subvention scheme that was available for MSMEs till March 31, 2021. The Government of India had introduced the Interest Subvention Scheme for MSMEs in November 2018. Under the scheme, interest subvention support of 2 percent was extended for all GST registered MSMEs, on fresh or incremental loans, for both working capital and term loan up to ₹ 100 lakh. SIDBI acted as a Nodal Agency for the purpose of channelising of the interest subvention to various lending institutions. However, the scheme has been defunct since March 31, 2021. Reinstating the scheme could provide the much-needed relief to MSMEs in easing their cost of finance. Lowering the cost of finance would be useful for MSMEs to enhance capital expenditure for production capacities and lead to generation of exportable surplus. As noted earlier, nearly 17.8 percent of the MSME exporters surveyed by Exim Bank cited lack of exportable surplus as challenge for exporting.

Extending Higher Rates to MSMEs under IES for Rupee Export Credit

Besides this, in the wake of rising cost of export credit, the Government of India could also consider extending a suitable higher rate of interest equalisation support under the Interest Equalisation Scheme (IES) for Pre-Shipment/ Post-Shipment Rupee Export Credit, in consultation with relevant stakeholders such as the RBI. It may be noted that, till March 2022, the interest equalisation support under the scheme was 5 percent for all MSME exporters. However, as per the current guideline of the scheme, support extended to MSME exporters is lower at 3 percent. The same may be increased to the previous higher rate of 5 percent. Besides, there is also need to ensure timely extension of the IES. As per the latest notice by the DGFT, the scheme is only valid till December 31, 2024, with no clarity on future extension or scope. Moreover, retrospective extensions also lead to operational issues for banks. As per Exim Bank's discussion with banks, after the scheme had previously ended on September 30, 2021, the extension of the scheme was intimated to banks in March 2022 on a retrospective basis from October 1, 2021, which resulted in substantial rework and operational hassles, as the banks had discontinued providing the benefits to the eligible loans under the scheme after it ended in September, 2021.

Enhancing Availability of Working Capital for MSMEs

As per CRISIL Research estimates, nearly 70 percent of the total debt requirement of MSMEs partain to working capital. However, only one-fourth of the debt requirement is sourced formally[31]. This could be another plausible reason for the high cost of capital for MSMEs. Access to finance i.e. timely and adequate credit, particularly working capital, would be critical for MSMEs to improve their export competitiveness and tap export opportunities.

With a view to bridge the large unmet need for working capital from formal sources by MSMEs, Exim Bank has launched a Working Capital Guarantee Programme (WCGP). Several export credit agencies (ECAs) have similar Working Capital Guarantee Programmes that complement the financial services provided by the banks in their respective countries. The US Exim, Export Development Canada, UK Export Finance and the African Export–Import Bank are some ECAs extending working capital guarantee programmes. All these working capital guarantee programmes are made scalable through the commercial banking networks in the respective countries.

Exim Bank is currently awaiting approval from the RBI for the programme. Once approved, the support will act as a catalyst to enhance credit flow to MSMEs and have a multiplier effect in terms of fostering MSME growth, boosting exports, and generating employment opportunities. The initial support would enable MSMEs to establish themselves as reliable exporters. Gradually, the improved track record of MSMEs will enhance their creditworthiness, allowing banks/NBFCs/FIs to extend credit to these businesses without relying on the guarantee support. This virtuous cycle—guarantee leading to business growth and improved creditworthiness—would amplify the impact of the programme.The Government of India can consider providing a backstop facility for the programme to enable Exim Bank to consider higher guarantee amount and scale up the support under

[31] CRISIL (2023), One out of five MSMEs to see stretch in working capital days

the programme. Such a backstop corpus can be leveraged by Exim Bank for higher exposure under the programme, thereby catalysing enhanced credit flow to the MSME sector and leading to incremental exports.

Strengthening the CGTMSE Scheme

Besides high rate of interest, lack of collateral is the second most pressing challenge for MSMEs, as per Exim Bank's survey. In this context, the CGTMSE acts as an important scheme for providing collateral free loans for micro and small enterprises. However, recent data suggests that the number of guarantees issued under the CGTMSE is substantially low when compared to the number of MSEs in the country. As per latest available data, the number of guarantees approved under CGTMSE as of December 31, 2023 stood at only 11.02 lakh, amounting to ₹ 1.36 lakh crore[32]. Given that there are nearly 2.46 crore registered MSEs in the country[33], there is clearly scope for expanding the number of beneficiaries under the scheme through targeted awareness programmes for MSEs.

Moreover, the scheme is only available for micro and small enterprises and does not cover the medium enterprises. The GOI could consider expanding the scheme to include medium enterprises for enhancing the coverage of the scheme. Enhancing credit access would be critical for MSMEs to scale up their operations and build exportable surplus.

Support for Scaling up Exim Bank's Trade Assistance Programme to Bridge the Financing Gaps

The global trade finance gap has widened to US$ 2.5 trillion in 2022. Recognising the challenges, Exim Bank has developed a new, first-of-its-kind trade facilitation initiative in India, the 'Trade Assistance Programme' (TAP) to address the trade finance gap, particularly in the MSME sector. The Bank has so far supported over 640 export transactions under TAP across 43 countries, leading to nearly US$ 2.4 billion worth of incremental exports from India.

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[32] Rajya Sabha Unstarred Question No. 239 to be Answered on 05.02.2024, on credit for MSMEs

[33] As of April 2024

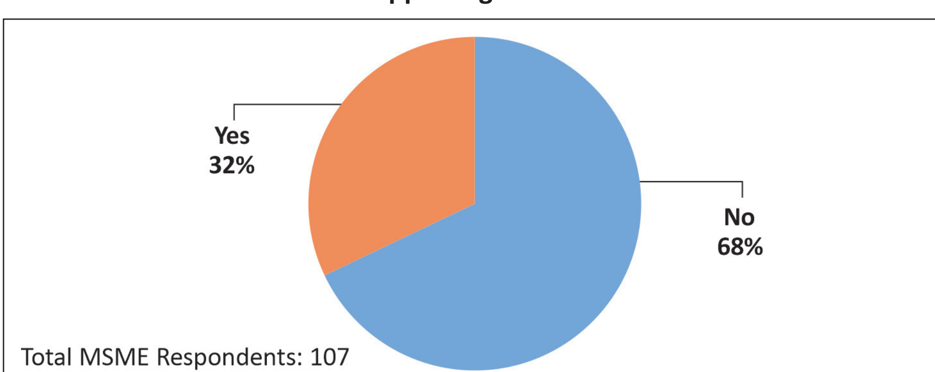
With the slowing demand in advanced economies, support under TAP will gain further salience for diversification of exports across non-traditional markets. TAP is increasingly receiving enquiries for supporting exports to high-risk countries. Given that Exim Bank's risk appetite is constrained due to the possibility of high default risk and challenging forex situation in select countries, the Government of India may consider risk sharing under TAP through a designated fund.

Further, assistance from Indian embassies abroad could be instrumental in facilitating introductions, providing market insights and fostering collaborations with potential overseas banking partners, to enhance the reach and effectiveness of the programme. Moreover, to amplify the reach and impact of the programme, the GOI could encourage scheduled commercial banks in India to partner with Exim Bank under TAP.

CREATING AWARENESS FOR LEVERAGING EXISTING CREDIT SUPPORT SCHEMES

Lack of awareness about different products and the support schemes of the Government of India also emerged as key challenges for MSME exporters surveyed by Exim Bank. Analysis of the survey responses indicates that more than two-third of the MSME respondents were unaware of the existing support schemes for MSMEs (Exhibit 5.6).

Exhibit 5.6: Share of MSME Respondents Aware of Government Schemes for Supporting MSMEs



Source: Exim Bank's Survey of MSMEs

There is need for creating awareness about existing schemes that support financing for exports and export capability creation. Awareness of schemes such as the CGTMSE, which provide collateral free loans to micro and small enterprises, for loans up to ₹ 5 crores, will be crucial. As per Exim Bank's discussion with banks and exporters, MSMEs lack awareness about the CGTMSE. Besides CGTMSE, there is also a need for raising awareness about initiatives such as the portal for 59-minute loans from PSB for MSMEs. The portal was launched in 2019 to enable easy access to credit for MSMEs. Through this portal, in-principal approval for loans in the range of ₹ 1 lakh up to ₹ 5 crore are extended, including collateral-free loans with CGTMSE coverage, as the portal is linked directly with CGTMSE. MSMEs can also check their eligibility of the CGTMSE coverage in real time through this portal. However, as per latest data as on May 2, 2024, only 2.49 lakh loans have been extended through the 59-minute loans portal, with sanctioned amount of ₹ 86,635 crore[34]. This is substantially low considering that there are 2.5 crore Udyam registered MSMEs[35], with significant credit needs.

In addition, there is also a need for enhancing awareness about fintech-enabled innovative financing solutions for MSMEs such as the GST Sahay portal. The GST Sahay App has been developed for providing cashflow based financing for MSMEs, in line with the recommendations made by the U.K. Sinha Committee of the RBI on MSME Sector for creating a second TReDS window for reverse factoring to enable MSMEs to obtain cash-flow based lending for their invoices. This initiative is aimed at eliminating the need for a buyer on the TReDS platform, thereby reducing the number of steps and lowering the operational costs. Accordingly, SIDBI, in association with Indian Software Products Industry Round Table (iSPIRT) and Online PSB Loans Ltd. (OPL) has built the GST Sahay App, an On-Tap Invoice Based Financing (IBF) Application, to enable the provision of completely paperless, presence less, collateral free, cashflow based and straight through financing to MSMEs for small ticket loans for their purchase invoices and sales invoices. Through GST Sahay, MSMEs can access collateral free, invoice-based loans of up to ₹ 1 crore. This initiative needs to be popularised through outreach activities and awareness campaigns, in order to enable greater number of MSMEs to benefit from the portal.

[34] Ministry of MSME Dashboard, Accessed on June 26, 2024

[35] As of April 2024

STRENGTHENING RECEIVABLES FINANCING FOR TRADE FINANCE

Fostering a Robust Operating Environment for International Trade Financing Services (ITFS) Platform

As noted earlier in the Study, flow of receivables financing to MSMEs through the TReDS platform recorded a robust CAGR of 90.2 percent during 2018-19 to 2022-23, with a remarkable success rate in invoiced financed at 93.9 percent during 2022-23. Recognising that financiers are generally not inclined to bid for payables of low-rated buyers, the RBI permitted insurance facility for TReDS transactions in June 2023. The permission for insurance companies to enter the ecosystem consisting of MSME sellers, buyers and financiers would aid financiers to hedge default risk. The RBI has also taken measures to expand the pool of financiers and to enable a secondary market for factoring units. These are expected to further enhance the availability of finance for MSMEs through the platform, in the forthcoming years. In the Union Budget 2024-25, the government has also reduced the turnover threshold for MSME buyers' mandatory onboarding on the TReDS platform from ₹ 500 crore to ₹ 250 crore, which is expected to bring approximately 22 Central Public Sector Enterprises (CPSEs) and around 7,000 additional companies onto the platform, thereby broadening the scope of suppliers. While such regulatory easing are steps in the right direction, there is also a need for strengthening the receivables financing for cross-border transactions. To that end, in 2021, the International Financial Services Centres Authority (IFSCA) had set up the 'International Trade Financing Services Platform (ITFS)' for providing trade finance services at IFSC. The ITFS is an initiative of the Government of India to build an electronic platform for facilitating trade financing for exporters and importers by providing access to multiple financiers. The trade financing services include import factoring, export factoring, reverse factoring, forfaiting, insurance/credit guarantee among others. At present, there are four registered ITFS platform entities that are operational at the IFSC. The first-ever export finance transaction by an Indian bank through the ITFS platform was undertaken in February 2024. There is substantial scope for enhancing the scale and quantum of export finance from ITFS.

In order to tap into the potential of ITFS for enhancing export finance, it would be important to foster a robust operating environment. To that end, simplified processes along with transparent and predictable regulatory frameworks may help attract greater participation from financial service providers and banks to conduct export financing through ITFS while maintaining robust risk management practices. The success of the platform depends a lot on being able to attract large numbers of buyers, sellers and lenders from across the globe. Businesses are traditionally cautious in adopting new technologies, often favouring a 'wait and watch' strategy. Consequently, it is imperative for the four license holders to effectively market their propositions to ensure robust participation. Sustaining momentum will also require a strong emphasis on education. Given that not all MSMEs possess a high level of technological proficiency and many operate with limited resources, it is essential to establish mechanisms for continuous support and guidance. These measures will be critical in ensuring the success of the platform.

Regulatory Easing for Fostering Factoring Services from IFSC

Exim Bank has set up its subsidiary in GIFT City, Exim Finserve, with a view to bridge financing gaps for exporters through a range of trade finance products, with a focus on factoring. Factoring presents a viable receivables management and financing mechanism suited to the needs of MSMEs. It provides a combination of three essential services to exporters: receivables financing, coverage of the risk of non-payment, and management of accounts receivable. It is particularly beneficial for MSME exporters as it is primarily based on the quality of accounts receivable rather than collateral. It also has the potential to improve export competitiveness as it enables exporters to offer competitive credit terms to their buyers.

China has been able to leverage international factoring for catalysing exports. International factoring volumes for China were nearly US$ 123 billion in 2023, as compared to US$ 1.1 billion in case of India. Improving the regulatory and operational framework for factoring services in GIFT City could boost the growth of international factoring services in India.

A factoring company requires credit insurance to cover its exposure from the export bills financed, especially when the export factoring is on non-recourse basis. IFSCA factoring guidelines do not allow factoring service providers in the IFSC to avail credit insurance from entities outside the IFSC. Further, it is observed that at present, while three insurance agencies are offering their services from GIFT City, the same could not be efficiently and effectively used by Exim Finserve, largely because of the existing rules and regulations. This renders availability of insurance in GIFT City inadequate and expensive.

To have the GIFT City at par or above the leading global financials hubs, it is important to provide a conducive business eco-system. In this context, IFSCA could explore the possibility of allowing overseas insurance cover for the export factoring entities that have set up their base in the GIFT City or at least, for the time being, allow insurance companies registered with the Insurance Regulatory and Development Authority of India and operating from India to cover factoring transactions originating from IFSC and registered with IFSCA. Suitable measures towards providing insurance cover for export factors can enable growth of factoring business in GIFT City and also incentivise other entities to establish presence in the GIFT City.

Interest Subvention for Factoring

Globally, several governments provide interest equalisation support to enable competitive credit for exporters and bolster export competitiveness. In India as well, under the Interest Equalisation Scheme for Pre and Post Shipment Rupee Export Credit, interest equalisation of 3 percent is available for MSME manufacturer exporters exporting under any HS lines, and 2 percent for manufacturer exporters and merchant exporters exporting under 410 HS lines. This reduces the cost of borrowing for exporters. Similar interest subvention support can be extended for export factoring, at least till the time substantial revenues are generated by the factoring business in India and economies of scales are achieved. This would help reduce the cost of international factoring for exporters and enable more MSMEs to benefit from export factoring.

Promoting FinTech for Supply Chain Finance

Fin-techs and alternative finance providers can play an instrumental role in bridging the trade finance gaps through collaborations in areas such as supply chain financing (SCF). Fintechs can supplement conventional sources of trade financing, mostly banks, by using digital interfaces and electronic invoice systems. SCF solutions provided by fintechs can be an alternative to bank-intermediated financing. They are built on inter-firm open account trading and allow suppliers to raise money based on the creditworthiness of the business at the top of the supply chain while a third party bridges the gap for early payment. Fintechs can also be beneficial for bridging the financing gap for MSMEs, as they can utilise the technology platforms of fintechs to sell their trade receivables. However, scaling up SCF volumes through fintechs would require technological capability, resources, and awareness. As an international financial centre, GIFT City offers a regulatory framework that allows multiple technology and innovations to develop under the IFSCA FinTech Sandbox. Some tech giants are already developing and testing blockchain-based supply chain solutions under the IFSCA FinTech Sandbox. The IFSCA FinTech Framework also allows tech companies developing supply chain finance solutions and platforms for global financial institutions to operate from the IFSC. In addition to the framework, IFSCA could consider introducing a FinTech incentive schemes with a specific focus on supply chain finance in GIFT City[36]. Besides, IFSCA could also consider developing a multi-funder platform to incentivise the participation in SCF by lenders who may otherwise be unable or unwilling to develop their own SCF platforms, including commercial banks. IFSCA could develop an enabling regulatory framework for SCF and advise and support commercial banks in developing new products.

CAPACITY BUILDING OF MSME EXPORTERS

To enhance the exports of Indian MSMEs, facilitating their integration into global value chains is imperative. However, one of the major hurdles faced by these enterprises is the difficulty in meeting international product quality

[36] PWC (2024), Export credit and role of the IFSC

standards. Exporters need to have in-depth knowledge of the latest global developments pertaining to packaging / eco-labelling, quality standards, regulatory norms and mandatory certification requirements, among others, to be able to expand their footprint into highly regulated markets of developed countries. Exporters also need to acquaint themselves with the rules and procedures of importing countries. It is therefore imperative to create an eco-system which supports exporters in adhering to the requirements in the export markets. This could be done through creating awareness about the rules, procedures and required standards, as well as through easing the financial burden associated with obtaining related certifications.

Reimbursement of Certification Costs

Adhering to standards and obtaining the requisite certifications entail considerable cost to the exporters, due to which many small players may be unable to access the international market. As discussed in Chapter 3, with a view to facilitate the internationalisation efforts of Indian MSEs and encourage them to produce and offer products and services of international standards in the export markets, the GOI has launched the 'Capacity Building of First Time MSE Exporters' scheme. There is a need for efforts to create awareness among aspiring and first-time MSE exporters about this initiative and encourage them to avail the benefits under this scheme. Moreover, the CBFTE is available only for first time exporters and could be expanded to include all MSEs.

Besides, to improve market access for existing exporters, state governments in India could also consider introducing a scheme for providing a refund of expenses incurred on obtaining standards and certifications. Under CBFTE, there is a limit of 75 percent of the testing and quality certification cost with a ceiling of ₹ 1 Lakh per MSE, which may not be sufficient for some of the testing and certification requirements. For instance, as per industry estimates, Conformite Europeene (CE) certification testing cost ranges between US$ 4000-US$ 12,000, depending on the CE testing required by the manufacturer and product under consideration[37]. While obtaining such certification is important

[37] Integrated Assessment Services-India, CE Certification Cost

to access the European markets in certain high value-added products, obtaining the certification could be cost prohibitive for MSMEs. In such cases, support from state governments could be useful for further reducing the financial burden and improving competitiveness of MSME exporters in the state. State governments could consider reimbursement of expenses incurred for obtaining statutory certifications like CE, China Compulsory Certificate (CCC), Good Manufacturing Practices (GMP) certification, etc., to the extent of 50 - 100 percent, subject to a ceiling per MSME exporting unit. This would help promote exports from MSME's in high technology sectors. Besides, to incentivise exports of pharmaceuticals, state governments could consider reimbursement of expenditure incurred on obtaining certificate of WHO-GMP or US-FDA certificate, to the extent of 50 percent, subject to a suitable ceiling per company. A similar support is being provided by the Government of Madhya Pradesh as part of its MSME Policy 2021, for supporting exports from MSMEs in the pharmaceutical sector. Likewise, similar sector-specific reimbursements of certification cost could also be considered for MSMEs in products that face significant SPS/ TBT measures and are important export items for MSMEs.

Decentralisation of Product Testing and Quality Management for MSMEs

The Ministry of MSME currently operates four accredited testing centers in Delhi, Mumbai, Kolkata, and Chennai. These testing centers are equipped with indigenous and imported state of art equipment in the disciplines of chemical, mechanical, metallurgical and electrical to undertake performance test, type test and acceptance test of semi-finished, finished products etc. These centers also undertake calibration works for measuring instruments and equipment conforming to national and International standards. Centers are accredited by National Accreditation Board of Testing & Calibration laboratories (NABL) certification as per ISO (17025), Bureau of Indian Standards, Railways (RDSO), Defense (CSD & DGQA) etc. In addition, there are 7 MSME testing stations that operate in Hyderabad, Bengaluru, Changacherry, Bhopal, Kolhapur, Jaipur and Puducherry. However, it is important to note that testing and certification requirements vary across different sectors. Therefore, there is a need for developing sector-specific facilities at MSME clusters to decentralise testing and quality management and provide specialised product testing and certification services to meet export standards.

Institutional Mechanism for Supporting MSME Exporters

As part of the Districts as Exports Hubs (DEH) initiative, the GOI has already established State and District-level Export Promotion Councils in all states/ districts[38], which are playing a crucial role in supporting export activities. To further strengthen the institutional mechanism for strengthening participation of MSMEs in global trade, MSME internationalisation centres could be set up across key export clusters[39]. Such centres may provide end-to-end support to MSME firms for conducting exports. These centres may also provide support services including hands-on support to MSME exporters such as logistics support, guidance for trade compliance, order and lead management services, finance and insurance related consultancy etc[40].

Capacity Building/Awareness Programmes for MSME Exporters

Creating awareness among exporters about export procedures, regulations and standards related to various products is a crucial aspect of enhancing exports for MSMEs. Awareness programmes/ workshops for creating awareness about the procedures to obtain clearances and certifications would help expand MSMEs' exports to the more regulated markets. To that end, the GOI, in collaboration with state governments, could conduct regular district-level workshops/ seminars/ conferences on different aspects of international trade and across different sectors. Industry associations and agencies, in coordination with State-level Export Promotion Councils and the proposed MSME international centres can help in organising such programmes. Training and awareness drives could also be conducted in major production hubs for dissemination of information pertaining to the certifications required

[38] DGFT(2024), Note - Districts as Export Hubs Initiative

[39] PWC (2024), VIKSIT: An approach for India to achieve USD 1 trillion exports

[40] ibid.

for exports, including process of application and support provided by the Government of India.

Creation of a Single-Window Trade Information Portal for Exporters

As per Exim Bank's survey, lack of information on export opportunities is the biggest concern for MSMEs, with nearly 51.4 percent of respondents highlighting it as a key challenge for exports. Aspiring MSME exporters in India often face challenges in obtaining information on export procedures, documentation needs, market trends, and different government export assistance programmes. To counter this issue, it would be important to create a single, trustworthy, user-friendly platform that offers in-depth knowledge of the export sector as a whole. The Ministry of Commerce and Industry's Niryat Portal and the India Trade Portal are examples of current platforms that offer insights into India's export trends, tariffs, export procedures and documentation etc.

Exim Bank's Exim Mitra Platform also offers diverse range of information, advisory and support services to bridge the information gaps for exporters. The Exim Mitra portal has a trade finance section wherein details of products for exporters and location of select banks have been provided along with broad terms and conditions for availing the facilities from these banks. Exporters can also submit preliminary information for availing trade finance on the website, which is shared with partner banks and financial institutions. However, multiplicity of portals can create confusion among MSMEs regarding reliable sources of information. Hence, there is a need for a one-stop portal to enhance ease of access to trade related information for MSMEs.To that end, the Government of India has recently launched the Trade Connect ePlatform, which has been jointly developed by the Ministry of Commerce and Industry, the Ministry of MSME, Exim Bank, the Department of Financial Services (DFS), Ministry of Finance, and the Ministry of External Affairs (MEA). The trade portal aims to provide a host of information related to exports and imports with a view to bridge the information gap for aspiring as well as existing exporters. This portal could be further enhanced on similar lines as the USA's International Trade Administration (ITA) portal, which not only provides information on trade trends, tariffs, export procedures, documentation, and trade agreement related information, but also provides comprehensive market research, and information on financing options for exports. In addition, the ITA portal also provides compliance and risk management support, access to networking events and support for grievance redressal. These could be used as a learning template for creating a single unified portal for providing information and advisory support for MSME exporters.

LEVERAGING E-COMMERCE FOR ENHANCING MSME EXPORTS

e-Commerce is a low-cost method for businesses for building market presence. It entails lower operational costs, as there is no need for a physical point of sale. This particularly helps MSMEs that have limited capital. e-Commerce presents an opportunity to such enterprises to enter newer markets and high-value sectors that are usually associated with higher entry costs.

Promoting Exports of GI Products through e-Commerce

India has comparative advantage in certain products and focusing on these products for e-commerce exports would enable the sellers to garner greater revenues and establish their brand identity. The DGFT's e-Commerce Exports Handbook for MSMEs identifies a list of such products where India has comparative advantage, that may be targeted by MSMEs aspiring to export through e-commerce mode. These include products such as handloom textiles and apparel; leather and leather goods; handicrafts and home décor; beauty and personal care products; semi-precious jewellery and accessories; automotive parts; ayush and herbal products; spices, tea and coffee; engineering goods.; and religious artifacts.

In addition to these products, the Government of India could also consider promoting Indian products with Geographical Indications (GI) through e-commerce by collaborating with leading e-commerce platforms. This would be useful for MSMEs as several GI tagged products fall under the categories of handicrafts, agricultural products, handloom products and foodstuff, which are crucial sectors for MSMEs. A similar approach is being adopted by the Government of Italy, which has signed a memorandum of understanding with the e-commerce platform Amazon, to promote Italian products that have a protected designation of origin (PDO) or protected geographical indication (PGI). In addition to promotion of such products, the collaboration aims to strengthen the protection of such products sold on the e-commerce platform, through identification and reporting of violations of intellectual property rights of products with PDO or PGI, as well as through checking unfair practices related to sharing of incorrect product information. The agreement also allows Amazon to promptly remove counterfeit products. Similar collaboration could be considered by the Government of India as well, which would help improve consumer confidence on quality and authenticity, and enhance sales and exports of GI tagged products through e-commerce mode.

Expanding the ITPS to Cover more Countries

The International Tracked Packet Service (ITPS) is a competitive service for transmission and delivery of packets. The ITPS has been designed by India Post to meet the cross-border shipping requirements of e-commerce exporters including MSMEs, small businesses and merchants, and promote exports using local post offices. India Post already provides the service for 41 destinations. However, several of India's top export destinations are currently not covered under the ITPS. India has been proactively expanding the number of ITPS partners over the recent years. In fact, in June 2023 alone, India added 23 new partner countries under the ITPS framework. Going forward, key export destinations like Bangladesh, Saudi Arabia, the UK, could also be considered for collaboration under the ITPS.

Besides, there is also a need to consider rationalising the postage fee charged under the ITPS. Currently, the ITPS provides shipping solution to exporters for packages weighing up to 2 kgs, along with pick-up and volume-based discount to contractual customers. The postage fee for such packages varies depending on the destination country, and stands at an average of nearly ₹ 341 for the first 50 gms and an average of ₹ 32.8 for every additional 50 gms[41], exclusive of GST. This could be cost prohibitive for small value exporters. As per estimates, nearly 2 lakh e-commerce export transactions were undertaken through the postal route, with an average consignment value of nearly ₹ 2,600. As postal e-commerce routes are used predominantly for small value exports by MSMEs, the government could consider rationalising/ waiving the postage fee for MSME exporters.

Promoting ONDC for International Trade

The Open Network for Digital Commerce (ONDC) is an initiative of the Department for Promotion of Industry and Internal Trade (DPIIT), Ministry of Commerce and Industry. The ONDC offers a network to enable local digital commerce stores across industries to be discovered and engaged by any network-enabled applications. ONDC is neither an aggregator application nor a hosting platform, and all existing digital commerce applications and platforms can voluntarily choose to adopt and be a part of the ONDC network.

Presently, e-commerce buyers and sellers have to be on the same app for a transaction which happens through the same platform. Under the ONDC framework, a buyer registered on one participating e-commerce site may purchase goods from a seller on another participating e-commerce site. Moreover, the ONDC architecture does not only include buyers and sellers, but also includes logistic providers for the delivery of goods. In essence, the ONDC enables the digitisation of the entire value chain. The platform creates new opportunities and limits e-commerce monopolies by supporting MSMEs and small traders to get on online platforms across various segments.

The ONDC network protocol operates without geographical restrictions, allowing any seller the freedom to offer products and services to buyers across any location, even internationally. Notably, the network has successfully conducted its first cross-border transaction in January 2024, with Singapore and is progressing towards scaling up this initiative.

[41] Exim Bank Calculation based on country-wise tariff data; Source: India Post

However, in order to scale up ONDC beyond the borders of India, there are a few key enablers that would be crucial to put in place. These include:

I. **Seamless cross-border payment settlements:** This would entail clear information on country-level regulations and rules for cross-border payments.

II. **Robust grievance redressal systems:** Different countries have different laws pertaining to consumer protection, therefore protections in one nation might not be the same as those in the nation where the firm is registered. A robust, comprehensive and clear redressal system would help provide prompt, satisfactory grievance resolution, fostering user confidence for cross-border transactions.

III. **Awareness about country-specific guidelines:** It would be important to ensure that buyer and seller apps know about country-specific guidelines for the sale of products. For example, the USA prohibits import of several wildlife-based products[42]. Designing and implementing standardised guidelines for e-commerce exporters listed on the ONDC could help ensure a seamless experience for consumers.

IV. **Collaboration with international e-commerce platforms:** ONDC could also collaborate with international e-commerce platforms to participate on the network. This would help build an ecosystem that would also give Indian consumers access to local digital commerce experiences in other partner countries.

Addressing Regulatory Complexities in e-Commerce

Currently, there are host of regulations in India for e-commerce, involving multiple government agencies and departments governing different aspects of e-commerce operations. For instance, the Consumer Protection Act, 2019 and the Consumer Protection (e-Commerce) Rules, 2020, which deal with the responsibilities and liabilities of the sellers and e-commerce

[42] "Bringing animal products into the United States," Centers for Disease Control and Prevention

platforms to protect the consumers is governed by the Ministry of Consumer Affairs, Food and Public Distribution. In June 2021, the Ministry proposed additional amendments to the Rules, including alteration of the definition of an e-commerce entity; mandatory registration of e-commerce entities; establishment of a grievance redressal mechanism; a ban on manipulation of e-commerce search results; and a ban on flash sales. Apart from this, the Competition Act, 2000 keeps in check anti-competitive practices and abuse of dominant position, which also covers certain areas under e-commerce operations. Besides these, the Sale of Goods Act, 1930, related to sales and shipping policies, the Legal Metrology Act, 2009 for the packaging and labelling of products, the Foreign Exchange Management Act, 2000 for realisation of export proceeds, and the Payments and Settlement Systems Act, 2007, among others, also govern various aspects of e-commerce[43].

Such multiplicity of regulations and regulatory bodies increases compliance burden and may affect the ease of doing business, particularly from the perspective of MSME e-commerce players. Multiplicity of regulatory bodies and complex regulatory approaches could also impede investments and expansion in overseas markets. A single, comprehensive e-commerce policy is therefore important for supporting growth of e-commerce exports.

While the DPIIT released the draft e-Commerce Policy in 2018-19, with a view to strengthen the e-Commerce regulatory landscape in India, the policy is still in its draft stage and yet to be adopted. There is a need to expedite the finalisation of the national e-Commerce policy. The policy should include short-term and long-term strategies to promote the growth and development of the sector, in line with domestic priorities and international best practices. Regulations related to e-commerce must also be aligned with the national policy to avoid ambiguity and conflicting regulations. Policies related to e-commerce exports could also be aligned with the national e-commerce policy.

[43] ADB (2023), Benchmarking Adoption of e-Commerce across the G20 Members

Enhancing Access to Export Credit for e-Commerce Exporters

In a recent representation made to the Government of India, firms had highlighted the non-availability of pre-shipment and post-shipment export credit for e-commerce exporters. As per Exim Bank's discussion with select commercial banks, the main challenge with export credit to e-commerce players is the unavailability of confirmed orders/Letters of Credit. Besides, it was also noted that the banks found it challenging to conduct due diligence of buyers as also to ascertain the nature of sales (domestic/overseas), as the transactions are done online. Further, banks also found it challenging to track the realisation of export proceeds in e-commerce, as it may not be routed through traditional banking channel.

In order to address the issues of e-commerce exporters in availing export credit, it would first be important to distinguish between the traditional modes of trade and e-commerce, and their distinct financing requirements. Unlike the traditional mode of transaction, where payment is usually made after the receipt of goods by the buyer, e-commerce exports typically allow upfront payments to sellers through payment gateways at the time of placing the order. Moreover, the frequency of shipments is higher in e-commerce exports as compared to offline exports. Additionally, a seller may forward deploy inventory to an overseas warehouse, and a single shipment may get sold over a period of months, with the seller receiving multiple remittances against one shipping bill. These complexities increase the documentation burden on e-commerce exporters and also lead to reconciliation problems.

Therefore, a thorough assessment of the financing requirement of e-commerce exporters, perhaps through a Working Group approach, would be crucial to highlight specific challenges faced by e-commerce exporters in obtaining export credit and design tailored financing programmes for e-commerce exporters.

It is noteworthy that, the Export-Import Bank of Thailand (Exim Thailand) has introduced a separate financing programme for e-commerce viz. e-Commerce Financing Loan. Under the programme, Exim Thailand extends short term revolving credit (including pre and post-shipment) for a period of up to 10 months for business operators who trade through e-commerce platforms viz. Alibaba, Thai Trade and Amazon[44]. On similar lines, a specific programme could also be designed to support e-commerce exporters in India by scheduled commercial banks.

CONCLUSION

Micro, Small, and Medium Enterprises are crucial to India's exports, accounting for about 29.2 percent of India's merchandise exports in 2023-24. The study notes that despite the significance of MSMEs for India's exports, several challenges affect their participation in exports, including lack of information on export opportunities, lack of relationship with foreign distributors, agents and customers, marketing related challenges, challenges in obtaining the necessary financial support for exports and challenges in complying with regulations in export markets, among others.

Addressing the challenges faced by MSMEs requires a holistic approach with interventions targeted at supporting marketing efforts, bridging financing gaps, bolstering export capacity, strengthening of support programmes and institutions, and promoting innovative modes such as e-commerce. For strengthening marketing and branding efforts, the study suggests consolidation of the MAI and MDA scheme, making it exclusive for MSMEs and expanding the scope of the consolidated scheme to include areas such as brand building, creation of marketing materials etc. On the financing front, some of the challenges noted from Exim Bank's survey include high-interest rates, lack of collateral, complex application processes, and insufficient awareness of financial products. To counter these, the study suggests reinstating the Interest Subvention Scheme for MSMEs, increasing interest equalisation support for rupee export credit, and strengthening the CGTMSE scheme for improving credit access. Raising awareness about credit support options like CGTMSE and popularising the GST Sahay App for collateral-free invoice-based loans are also crucial steps in this direction. Enhancing receivables financing through platforms like TReDS and ITFS, can

[44] EXIM e-Commerce Financing Loan, Exim Thailand Website

also help enhance access to collateral free financing, including for exports. For leveraging e-commerce, the study proposes strategies such as promotion of GI products through e-commerce platforms, expanding the ITPS to cover more countries, promoting ONDC, addressing regulatory complexities, and tailored financing solutions for e-commerce exporters. Additionally, capacity building initiatives for creating awareness and reimbursement of certification costs etc., could also help enhance the participation of MSMEs in international trade.

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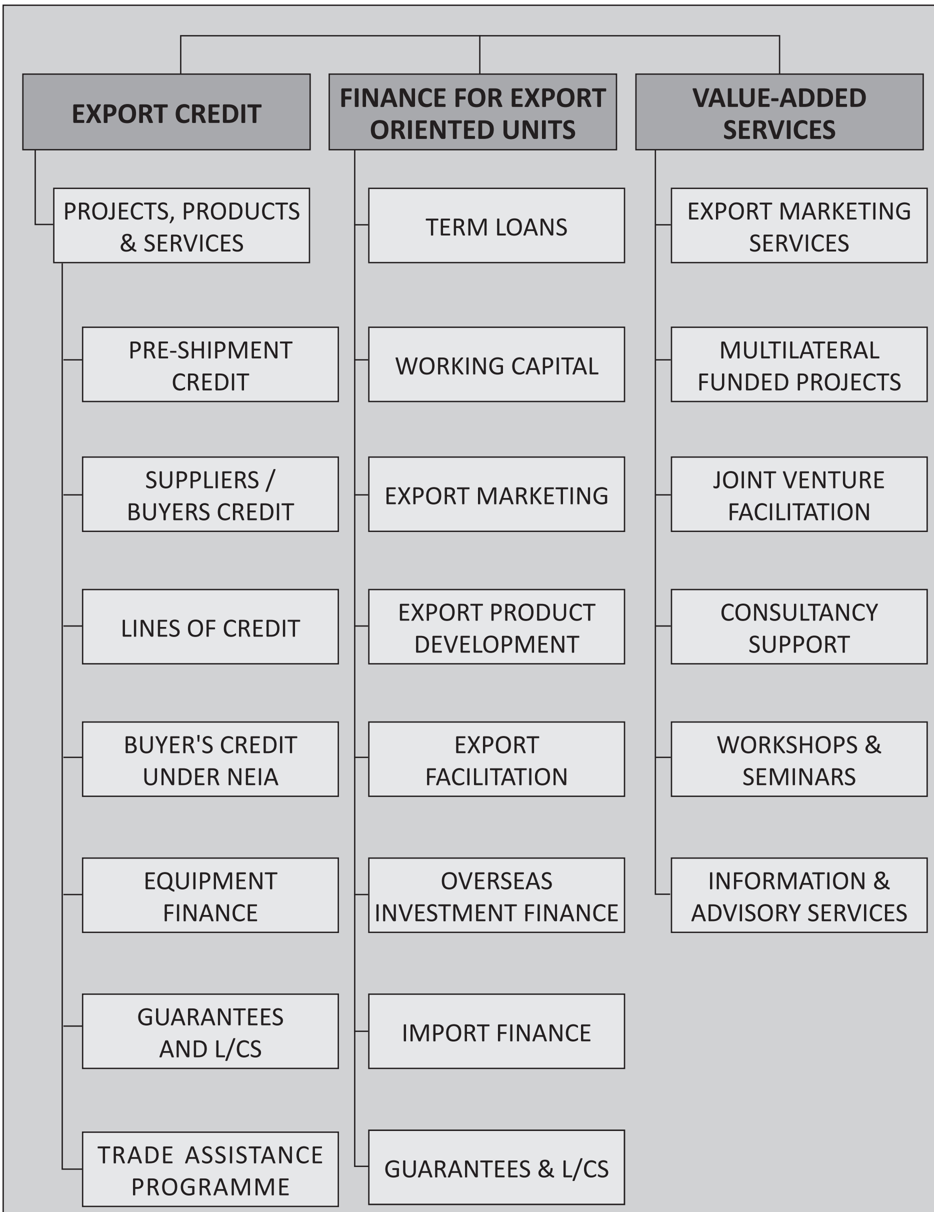

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