

Barriers To Microfinance Access For MSMEs: A Study Of Bengaluru's Challenges

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Abstract

MSMEs are becoming essential for accelerating the expansion of Indian economy, primarily in metropolitan region like Bengaluru. Despite being a large industry, they somehow encounter considerable obstacles when trying to obtain microfinance for survival and expansion. This article illustrates the difficulties MSMEs in Bengaluru face in obtaining microfinance, based on data collected from 120 micro small and medium business units, it emphasises the importance on variables including education levels, type of business, and the size of the firm to predict microfinance access. By combining ANOVA and Chi-square tests in the analysis, the results show that the level of education of entrepreneurs have a significant impact on their understanding of modern financial services available in the market, including micro financial services. While the business units according to their nature are affected by the interest rates at which the microfinance is available and the recent developments in terms of policy reforms have made microfinance more accessible to family run business houses and sole proprietary firms. This Study shows that gaps in financial literacy and regulatory authorities' support still exist, in spite of constant policy reforms. The most appropriate course of action is to customise microfinance services to the diverse needs of MSMEs and to educate entrepreneurs about financial products.

Key Words: Microfinance institutions, MSME units, Funding, Financial access

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I. Introduction:

The economy benefits from the advancements in entrepreneurship, innovation and the job creation by micro, small and medium-sized businesses. MSMEs make up to 30% of India's GDP, producing half of the exports and employing over 110 million people. Microfinance and MSME units serve as vital drivers of economic growth and development for developing economies.

For micro, small and medium sized business units, obtaining financial services –including microfinance remains a formidable obstacle. A wide range of financial services, including credit, savings account and insurance are covered in microfinance and are geared toward helping individuals and companies that lack access to traditional bank services. As a result it makes it possible for MSMEs to obtain the capital needed for business expansion and sustainability.

Microfinance is a beacon of hope for the majority of micro small and medium enterprises as it supports in the working capital requirements for start-ups with less complications compared to the traditional sources of funds.

Bengaluru, renowned as the silicon valley of India, has a vibrant micro, small and medium dominated economy and the sector represent a range of businesses, including manufacturing, biotechnology and information technology and more, each contributing significantly to the local economy's potentials to expand at its current rate, while the region's rapid urbanisation and prominence as a major economic hub indicates microfinance services will grow to be more vital. Despite the fact microfinance being crucial to these firms' success, their biggest challenge is access to the range of services provided by microfinance institutions. The below table explores the number of micro small and medium units registered through Udyam portal-Government of India's single window system and the employment generated through these units. 32.13% of micro units and 28.85% of employment generated through micro units in Karnataka are based in Bengaluru region, while 47.77% of small units and 64.34% of employment generated through small enterprises and 32.61% of medium enterprises 34.40% of employment created through medium enterprises in Karnataka are based in Bengaluru region, indicating the significance of MSMEs in employment generation and innovation.

Table-1: Bengaluru Districts (Rural and Urban) MSME Units registered and employment generated

District	Micro		Small		Medium		Total Units	Total Employment
	Units	Employment	Units	Employment	Units	Employment		
Bengaluru (Rural)	58,564	5,62,446	1,468	65,632	169	30,668	60,201	6,58,746
Bengaluru (Urban)	3,08,500	21,39,178	13,408	5,98,800	1,575	3,33,266	3,23,483	30,71,244
Karnataka	11,42,379	93,62,213	31,139	10,32,613	2,713	4,45,950	11,76,231	1,08,40,776

Source: Karnataka state Economic Survey and Udyam Registration Portal, GOI

II. Literature Review

While there are numerous research works discussing about the challenges faced by MSME units, some of them are briefly discussed below pertaining to the challenges faced in accessing microfinance services.

According to (Poornima, 2016a), MSMEs are highly on the unstructured form of sources for financing their firms that includes personal financing/family wealth and money lenders and lack of collateral and financial awareness is seen as a major reason for non-dependency on the formal financing. (Shankar, 2016) analysed the challenges of small enterprises in south Asia that are not met by microfinance institutions, (Rajamani et al., 2022), MSME's life cycle stage plays a vital role in the access to finance, as different sources of finance being more accessible during different stages of their life cycle. (Biswas, 2014) MSMEs facing considerable constraints in financing is a major barrier for the sector. (Esubalew & Raghurama, 2021), MSMEs prioritise commercial banks lower in the list of financing sources as they observe commercial banks are intended for larger business units.

(Maiti, 2018), favourable policies and legal framework creates larger opportunities for banks and other alternative financial supports systems to fund MSMEs in India. (Choudhury & Goswami, 2017), reviewed MSME financing gaps from 1995 to 2017, analysing micro, small and medium units play a vital role in the development of an economy and formal lending sources are essential for the development of the sector. (Doris Wambui & Nairobi, n.d.) examined the effects of microfinance services on the performance of small and medium enterprises in Kenya and analysed saving schemes and loan grace period as statistically significant influences in the performance of MSMEs.

(Snehal & Hingu, n.d.), the main challenge faced by MSMEs in financial access is the deficiency of collateral assets and financial awareness among the businesspersons. (Banks & Njeru Njue, 2017) dearth of credit worthiness and low net value of small and medium entrepreneurs confines the SMEs access to formal finance (Marwa, 2014), the discrepancy between MSME characteristics and conventional funding requirements has resulted in failure of financing MSMEs in Tanzania. (Choudhury & Goswami, 2017) examined the factors that hinder SMEs in Bangladesh from obtaining finance from FIs and found unfavourable credit terms, high rates of interest, education and skills of business owners as the obstacles for SMEs in accessing finance. (Gayathridevi MA, 2014), evaluated the barriers faced by women entrepreneurs in Bengaluru and identified financial barrier as the most significant among the numerous barriers. (Rajamani et al., 2022) proposed a conceptual framework to measure financial difficulties of MSMEs for financial access in different stages of its life cycle. (A.R et al., 2015) highlighted the financial needs and challenges faced by street vendors in Tirunelveli and Nagerkovil towns in Tamil Nadu, and recommended increased awareness programs to benefit street vendors' access to finance and endure their micro entrepreneurial efforts. (Chan & Lin, 2013) explored the financing challenges of micro and small enterprises in China, and analysed MSE owners in China need lesser credit costs, extended loan repayment periods and instalment payments for repaying loans to reduce the barriers in financial access. (Asst & Scholar, 2020) overviewed the microfinance and its role in women empowerment in Karnataka and analysed microfinance sector in India needs a further capital of more than Rs. 5,000 crores to withstand its 25-30% annual growth target for the next three years.

Objective of the Study

To study:

1. Barriers faced by MSMEs while accessing microfinance services
2. Impact of regulatory and policy frameworks on MSMEs' access to microfinance services
3. Role of financial institutions on their outreach strategies, loan application processes, and customer support systems, its impact on MSMEs

III. Methodology

The current research objects at studying the microfinance access in the region of Bengaluru with special attention to MSMEs. Primary quantitative research was conducted using a structured questionnaire and statistical methods including ANOVA and Chi-Square were used to comprehend the aspects, issues, and prospects of

microfinance access to MSMEs in the region. The study applies an empirical research design focusing on entrepreneurs with operational businesses that are either micro, small or medium. In terms of sampling technique, the study adopted convenience sampling which is non-probability approach. Convenience sampling was limited only to the regions of Bengaluru due to the geographical location of the target population. Size of the Sample for this study is considered to be 120 entrepreneurs. The latter groups were chosen taking into account the operational magnitudes like micro, small and medium enterprises.

A structured questionnaire was developed exclusively for this research as instrument to collect data. The questionnaire covered a range of topics related to the entrepreneurial experience, including demographic details; basic characteristics of the business

Data analysis was done involving the use of descriptive as well as inferential statistical techniques. Descriptive statistics summarizes demographic characteristics of the respondents, and gives overview about their business.

Two important statistical techniques involved to derive deeper analytical insights:

1. ANOVA: In this context, the question provided was analyzed through ANOVA, which is popularly known as Analysis of Variance. Whether there are significant differences in facing challenges while accessing microfinance among micro, small, and medium enterprises were considered by performing the ANOVA test.

2. Chi-Square Test: The Chi-Square test was applied to determine any association between categorical variables such as business size, problems faced, and assistance obtained through channels. For instance, it revealed whether more cases of particular problems are in a certain

Table-2 Showing the ANOVA Results

Hypothesis	Source of Variation	Sum of Squares	Degrees of Freedom	Mean Square	F-value	P-value	F critical
H₀ Level of Education has no influence on the lack of information financial products	Between Groups	476.8	5	95.36	4.260313	0.006488	2.620654
	Within Groups	537.2	24	22.38333			
	Total	1014	29				
H₀ Nature of Business has no influence on interest rates of microfinance loans being satisfactory	Between Groups	698.5714286	6	116.4285714	4.289473684	0.003457	2.445259395
	Within Groups	760	28	27.14285714			
	Total	1458.571429	34				
H₀ Nature of Business has no influence on the type of microfinance service applied for	Between Groups	388.2857143	4	97.07142857	3.465657939	0.019247007	2.689627574
	Within Groups	840.2857143	30	28.00952381			
	Total	1228.571429	34				

Results: The above table discuss the relationship between demographic variables of MSME entrepreneurs and the microfinance lending firms, through the ANOVA Test it is observed that the level of education impacts the awareness of information about financial products, as F Calculated value- 4.260313 is greater than F critical value- 2.620654, therefore H₀ is rejected. It is also observed that Nature of Business has an influence on interest rates of microfinance loans being satisfactory to the MSME units, as F Calculated value- 4.289473684 is greater than F critical value- 2.445259395, therefore H₀ is rejected and Nature of business has an influence over the type of microfinance service applied for as the F Calculated value- 3.465657939 is greater than F Critical value- 2.689627574, therefore H₀ is rejected. Indicating that the awareness level about the availability of financial services, interest rates and type of microfinance service are vital for the MSMEs to access the microfinance services.

Table-3: Chi-Square Analysis on Relationship between Microfinance Services and MSMEs

Sl. No	Hypothesis	Probability (Value)	Chi-square (Value)	Remarks	Degree of Freedom
1	<u>H₀ Years</u> of Business operation has no influence on current regulations are supportive of MSMEs seeking microfinance services	0.841717624	10.45666825	Accepted	16
2	<u>H₀ Nature</u> of Business has no influence on policy changes improving MSMEs' access to microfinance services in recent years	0.003375176	46.97318842	Rejected	24
3	<u>H₀ Annual</u> Turnover of the firm has no influence on outreach strategies of microfinance institutions	0.964622416	7.405869813	Accepted	16
4	<u>H₀ Primary</u> Industry Sector has no influence on loan application process at financial institutions is user-friendly for MSMEs	0.984667129	11.53391442	Accepted	24

Results: The above table discusses the relationship between microfinance services and MSMEs, through the Chi Square Test, it is observed that the relationship between Years of Business operation is not Significant with the Current regulations being supportive to MSMEs seeking microfinance services, as the Chi square value 10.45666825 is lesser than the distribution table value 26.296 at 16 degree of freedom with 5% level of significance. This indicates the fact that micro, small and medium scale entrepreneurs irrespective of their business experience, expect the regulations to be more supportive in order to avail microfinance services. While the nature of business particularly the sole proprietary units, partnership units and family managed business units opine that the policy changes in the recent years have influenced the access to microfinance services as the H₀ is rejected with the Chi square value 46.97318842 being more than the distribution table value 36.415 at 24 degree of freedom with 5% level of significance.

MSME units with different annual turnover have no significance with the outreach strategies of microfinance institutions, as the Chi square value 7.405869813 being less than the distribution table value 26.296 at 16 degree of freedom with 5% level of significance, H₀ is accepted; indicating that the microfinance institutions are reaching out well to the MSME units, irrespective of their income level. Primary sector to which the MSME units belong has no influence over the loan application process at microfinance institutions being user friendly, as the Chi square value 11.53391442 being lesser than the distribution table value 36.415 at 24 degree of freedom with 5% level of significance, H₀ is accepted, indicating that the loan application process to be more effective and user friendly for the sectors that are of paramount importance, as micro small and medium units act as an important indicator in the in the economic development.

IV. Conclusion:

Microfinance services accessed by MSMEs in Bengaluru were analyzed based on barriers of accessing the services, whereby ANOVA and Chi-Square tests are applied for the statistical analysis. From the findings of the ANOVA, huge differences exist in ways in which micro, small, and medium enterprises experience challenges when accessing the microfinance services. For instance, the results regarding ANOVA show that the difference in the level of education of the entrepreneurs determines the awareness of the range of financial products, while the nature of the business determines the satisfaction of the entrepreneurs with interest rates and the type of microfinance service applied for. While the Chi-Square test explores the relationship between various characteristics of firms and the availability of microfinance and the recent policy changes made easier access to microfinance, especially for sole proprietorship and family-managed business. Outreach strategies of microfinance institutions are found effective in all different business turn over levels, and the loan application is also friendly irrespective of the primary industrial sector. The improvement of policy and outreach by the financial institutions have made the microfinance available services to MSMEs of Bengaluru. However, awareness and alignment of the regulatory framework that is set to improve such enterprises in a growing urban economy is seen lacking.

Future Scope

Future research will explore the question of whether digital microfinance platforms present an avenue for improved access to financial services by MSMEs in the larger urban centers, such as Bengaluru or State and National level.

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