KIRTANE & PANDIT

IMPORTANCE OF FUND MANAGEMENT FOR THE MSME

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Backdrop

The Micro, Small & Medium Enterprises sector, better known as the MSME sector is one of the fastest growing sectors in India.

The MSME sector has emerged as a highly vibrant and dynamic sector of the Indian economy over the last six decades. MSMEs not only play crucial role in providing large employment opportunities at comparatively lower capital cost than large industries but also help in industrialization of rural & backward areas, thereby, reducing regional imbalances, assuring more equitable distribution of national income and wealth.

As on 31st March 2022, there are approximately 80 lac registered enterprises that generated an employment of around 6.30 crores of employees. (Source: Statistics & Data Division, DCMSME)

Who are considered as MSME?

The Central Government has enacted the Micro, Small & Medium Enterprises Development (MSMED) Act, 2006 to give impetus to the growth of the industry. The Act provides mechanisms to structure the sector and to address any governance or operational issues faced by the MSMEs. Entities are required to register under MSME Act to avail various benefits.

Entities into manufacturing, services, wholesale trade and retail trade who satisfy following criteria are eligible to register -

Category → Criteria ↓	Micro	Small	Medium
Investment and Annual Turnover	invst. in P&M / Equipment < 1 crore and Turnover < 5 crores	1 crore < Invst.in P&M / Equipment < 10 crores and 5 crores < Turnover < 50 crores	10 crores < Invst. in P&M / Equipment < 50 crores and 50 crores < Turnover < 250 crores

Source : Notification in the Gazette published by The Ministry of Micro Small and Medium Enterprises

Applying these criteria for purpose of discussion around MSME, India has a vast majority of the MSMEs spread over various corners of the country that form a part of the unorganised sector. According to a report released by the India Brand Equity Foundation (IBEF) in July 2022, India has approximately 6.3 crores of active MSME units. Considering the 80 lacs registered MSMEs on the Udyam portal, the percentage of the registered MSMEs spans to just around 13%.

The peculiarities of unorganized sector include lack of many aspects like formation of legal entity, clarity of ownership of family businesses, records of businesses and hence clear revenue generating capacity, formal education of personnel running the business and so forth. These aspects clearly pose issues for such businesses to acquire funds from organized sector like Banks, NBFC, Government scheme, Micro Finance entities and only means left are money lenders who charge exorbitant interest and undertake unfair trade practices.

Hence, there is need to bring in awareness of importance of funds and its management in businesses. The Government is strongly taking and advocating such initiatives as it not only helps in growing the economy through right measures, but it also and more importantly helps MSME businesses to grow and avail greater benefits. We as professionals also need to lay heavy emphasis on making businessmen understand the benefits of formal fund management and help them with nuances that make them hesitant.

What is fund management?

Fund management is ensuring that the right amount of funds is made available to the business at right time from the right source for right period and these funds are put to use in most appropriate manner. The efficiency of any organisation depends upon the ease of access to funds and subsequently, the effective deployment of these funds for the desired purpose. Thus, Fund management is not only about access to funds and deployment of funds but also knowing the necessity, timing, source, cost, alternatives and such other aspects of it.

Let's look at these aspects in a detailed manner

Choosing the right source of funds

Tapping the right source of funds depends upon the purpose for which the funding is needed and the cost at which it shall be raised. Parameters like timing of fund deployment (single or in tranches), its end use, duration, nature of asset, collateral and such other factors need to be considered.

On ground it has been observed that MSMEs lack knowledge about various sources of funds available in the market today and they primarily stick to the traditional sources of private money lenders or bank finance.

MSMEs can look at various other avenues like equity funds, ECB funding / other foreign currency loans, bill discounting, government schemes that may be more appropriate depending upon the need of business.

To provide adequate impetus to this sector, numerous funding schemes have been initiated for registered MSMEs by the Ministry of MSME through financial institutions like Small Industries Development bank of India (SIDBI), National Bank for Agriculture & Rural Development (NABARD), National Small Industries Corporation (NSIC), Export Import Bank of India (EXIM), to name the major ones. There are dedicated collateral free credit guarantee schemes for the initial capital requirement as well as requirement for expansion, technical upgradation, modernisation of existing units.

The MSME Ministry is channelizing efforts to enable the registered MSMEs to have access to the right sources of finance for the right purpose, starting from seed funding, expansion financing to working capital financing.

An annexure of various schemes is attached for reference at end of the article. MSMEs should also look at newer avenues like Neo banks, micro finance, angel investors, venture capital, venture debts and the likes to ensure knowledgeable decisions are made.

Apportioning of funds within the asset classes

Funds raised for capital purposes intended for purchase and installation of capital assets typically in the form of property, plant or equipment should not be allocated for working capital needs or trade credit purposes and vice versa. This is because the nature of every type of capital has an inherent gestation for deployment & the subsequent recovery, which, if tampered with, can lead to a never-ending spiralling cash flow crunch.

There are numerous cases where MSMEs have raised funds for business purposes but have been unknowingly diverted to procuring of expensive personal assets under the misconception of asset creation. Businesses can suffer due to lack of liquidity while exhausting the funding ability at the cost of business growth.

Receivables management

The MSME Act, 2006 specifies a 45-day credit period for the recipient of any goods or services to pay the MSME supplier. The law requires the buyer to pay to the micro and small enterprises compound interest at monthly rests at three times the rate notified by the RBI if the payment to the supplier is delayed beyond 45 days or the date agreed through contract, whichever is earlier. However, MSMEs usually don't take recourse to this clause due to the risk of losing business from large corporates.

An institutional mechanism in the form of TReDS is also set up by Government in order to facilitate the discounting of invoices for MSMEs from corporate buyers through multiple financers. This platform ensures that MSMEs can realise their invoicing proceeds before the due date & the funds can be recirculated in the business.

Guidance on bill discounting facility, non-recourse factoring has helped enterprises to improve their cash flow position substantially. Putting control mechanisms in place to harp upon receivable ageing and recover the dues on or before the due dates will help maintain a steady cash inflow.

Payables management

Analysing the end-to-end gestation period from procurement of raw material to sales realisation and eventually back working the credit period to be offered to the suppliers is what the MSMEs need to work upon. Back-to-back payment terms with suppliers vis-à-vis customer terms need to be built in. The working capital cycle needs to be a self-sustaining one and resorting to working capital bank limits should only be a stop-gap arrangement.

The MSMEs are also assisted in procuring of raw materials at subsidised rates by Government, facilitating for participating in Government tenders with exemptions in EMD, supporting in marketing of the finished goods in the open market to face competition.

Inventory management

Some businesses require heavy investment in inventory while some have inventory that are more in number. Accurately managing inventory with respect to quantity and timing can help MSMEs save a lot of working capital in terms of locked capital, storage costs, possibility of damages or items becoming absolute, etc. Approaches like just in time, six sigma, minimum movement of goods, ABC analysis and management, etc can help in achieving optimum inventory size further leading to efficient working capital management.

Investment management

Generating an investible surplus is a sign of a healthy business. Apportioning of the excess funds generated in business or recirculating the same, depends on the future capital needs of the company in the short-term / long-term including expansion plans for technology upgradation / capital investments in property, plant, equipment. Parking of excess funds in short term instruments, whether debt or equity would depend upon the liquidity requirements of the company. Redeployment of investible surplus therefore needs to be an outcome of an active cash flow management strategy devised by professionals' / domain experts with a focus on the risk-return-liquidity profile of the individual business and the industry in which it operates. Periodic review mechanism needs to be set up through formation of investment committees having adequate management representation to ensure transparency & ownership in decision making.

Budgeting & Controlling

Financial planning forms an integral part of the fund management process. Budgets encompass the projected business plan of the enterprise over the short / mid / long term, which helps to ascertain, map and plan for gaps, if any. Finally, all kinds of business budgets culminate into a cash impact and hence the budgeting needs to be done in all the stages of a business cycle.

Majority of MSMEs do not prepare budgets and hence most business decisions are taken on an ad-hoc basis, rather than relying on a business plan.

Implementing budgetary controls primarily include sales budgets, production budget, capacity planning, capex budget, sourcing budget, headcount budget, EBIT budget and cash flow budget. The periodic tracking of the actuals vis-à-vis the budgets allows to review, remap and thereby control the funding allocation & apportionment.

Other incentives

Registered MSMEs are also provided with various incentives under other laws. Knowledge of same can help MSMEs avail these benefits that can further help in fund management, like MSME can get registered under Startup India initiative. Under this initiative, eligible companies can get recognised as start-ups by DPIIT, in order to access a host of tax benefits, easier compliance, IPR fast-tracking and more. Launched on 16th January 2016, the Startup India initiative, has rolled out several programs with the objective of supporting entrepreneurs, building a robust start-up ecosystem and transforming India into a country of job creators instead of job seekers. Below are few of the benefits of this scheme –

- Compliance regime based on self-Certification
- Legal Support and Fast-tracking Patent Examination at Lower Costs
- Relaxed norms of public procurement
- Credit guarantee fund
- Tax exemptions for eligible start-ups w.r.t. long term capital gain, business profits, investments above fair market value, etc.
- Faster exit

Risks and Corporate Governance

The business cannot work in silo and is always affected by changes in various environment around it including legal, market, political, financial, etc. And these changes can have effects on fund management plans. Taking advise of experts for understanding the intricacies of such changes and its impact on funds from immediate as well as future perspective is of utmost essence. Having a disciplined approached through well thought of corporate structure towards fund management in such and regular business scenario can add value to the fund management effort. Effective controls, detailed operating procedures, financial transparency, timely reporting are few of the aspects that can be put in place which will help in having effective fund management.

The aspect of fund deployment to the desired use in the optimum manner is equally significant for getting the results and returns in the estimated timelines. Most of the times, either due to lack of awareness or due to the high cost of professionals, MSMEs miss out on the financial expertise required to manage their finances. MSMEs need to understand the stage of business they are at and accordingly seek appropriate help of professionals. Right from being a start-up to getting ready for an IPO, each stage of business requires different expertise with respect to fund management. Given below is a short summary of what peculiarities one can look at during different stages of business growth –

Stage of Business	Fund requirement for	Challenges in fund procurement	Funding options	Key fund management aspects
Inception	Setting up, plant & machinery, team building, establishing product market fit, etc.	Lack of past records, collaterals, competition, focus required on business creation, cost	Equity – Own / Angel / Venture, Debt – Venture / Government scheme	Lack of plan for fund utilization, funds getting locked in non-urgent requirements
Early growth	Working capital, team building, marketing	Lack of past records, collaterals, competition, focus required on business creation, cost	Equity – Own / Angel / Venture, Debt – Venture / Government scheme / Banks / NBFC	Getting funds, unmonitored fund utilization, unawareness of fund management methods
Growth	Marketing, working capital	Projections mapped to business, Well thought out business plan, valuations	Equity – Venture / Private Equity Debt – Banks / NBFC	Lack of control, spend on personal avenues, locking capital avenues not in line with business plan
Expansion	Business growth, diversification, acquisitions	Timing and quantum management, valuations	Equity – Private equity / IPO	Preparing for expansion funding, presence of transparent monitoring and reporting systems, control mechanism and appropriate corporate structure

MSMEs need to be more proactive in their approach when it comes to managing their business and then and then only shall the support extended to them by the regulators can fructify. They need to understand the importance of knowledge-based services that professionals can provide and should take full advantage of such services for the betterment of their business. Choice of right consulting partner at every stage of business can bring in required expertise in most cost efficient manner. MSMEs need to understand the value of opportunity loss and time value of money in the right perspective and engage consultants or enhance their involvement as business progresses.

Professional advice can help to address majority of the above issues which can provide a stable platform for the MSMEs to concentrate on their business growth. This will not only help resolve and improve on current challenges, but also shall create a solid foundation for the upcoming business that will help MSMEs set-up themselves, sustain and grow further exponentially.

Annexure of MSME schemes

Sr. No.	Name of the Scheme	Who is eligible	Scheme Details	How to Apply
1.	CREDIT GUARANTEE FUND TRUST FOR MICRO AND SMALL ENTERPRISES (CGTMSE)	Existing and New Micro and Small enterprises engaged in Manufacturing or Service activity excluding agriculture, Self-Help Groups (SHG), etc.	Credit guarantee for loans up to Rs. 2 crores, without collateral and third-party guarantee. Guarantee coverage ranges from 85% (Micro Enterprise up to Rs 5 lakhs) to 75% (others). 50% coverage is for retail activity	Through member lending institutions i.e. Banks and NBFC
2.	Prime Minister's Employment Generation Programme(PMEGP)	Any individual, above 18 years of age can apply	Credit linked subsidy program for setting up new micro-enterprise in non-farm sector. Margin Money subsidy ranges from 15% to 35% of project cost for projects up to Rs. 50 Lakh in Manufacturing sector and Rs. 20 Lakh in the Service sector For beneficiaries belonging to Special categories such as SC/ST/ Women/ Minorities/ Ex-Servicemen/ Transgenders/ Aspirational districts/NER, the margin money subsidy is 35% in rural areas and 25% in urban areas	Through PMEGP Portal.

3.	Scheme of Fund for Regeneration of Traditional Industries(SFURTI)	Existing artisans from traditional industries in sectors such as Handicraft, Textile, Agro-Processing, Bamboo, Honey, Coir, Khadi, etc.	Artisans are constituted into Special Purpose Vehicles (SPVs) by Implementing Agencies (State/Central Govt. organizations, NGOs) who need to provide land and 10% (5% in NER, J&K and Hill Areas) of Hard Intervention Financial assistance of up to 90% (95% in NER, J&K and Hill Areas) of Hard Intervention cost, entire cost of Soft Intervention, Technical Agency fee and Implementing Agency fee is given by GoI	Through SFURTI Portal.
4.	2nd Loan for up-gradation of the existing PMEGP/REGP/ MUDRA units	Existing well performing PMEGP/REGP/MU DR A units	Maximum subsidy would be 15% of the project cost (20% for NER and Hill States). The balance amount of the total project cost is provided by Banks as term loan.	Through PMEGP Portal.
5.	National SC-ST Hub Scheme	Aspiring and Existing SC/ST Entrepreneurs.	25% subsidy on purchase of plant & machinery /equipments or Rs. 25 lakh whichever is less. Reimbursement of fees charged for bank loan processing, testing services, membership of Export Promotion Council, membership in Govt. promoted eCommerce Portals, Single Point Registration Scheme of NSI. Free skill trainings and distribution of trade specific tool kits to trained candidates under the Skill Development programmes.	Through SC ST HUB Portal

6.	A Scheme for Promotion of Innovation, Rural Industries and Entrepreneurship (ASPIRE)	Any agency/institution of Government of India/ State government or existing training centres under Ministries/Departments of Government of India/State Government, Industry Associations, Academic Institutions. Any not-for-profit private institutions with experience in successfully executing incubation and/or skill development programs may be eligible to set up an LBI.	Maximum of INR 1 crore. to Government agencies & INR 75 lakh to Private agencies for procuring plant and machinery. Maximum of INR 1 crore. to Government and Private agencies as operational expenditure support towards manpower cost, running incubation and skill development programmers, etc.	Through Ministry of MSME Portal
7.	Credit Guarantee Scheme for Subordinate Debt (CGSSD) for Stressed MSMEs	This Scheme seeks to extend support to the promoter(s) of the operational MSMEs which are stressed and have become NPA as on 30th April, 2020 and standard as on 01th November, 2016.	Promoter(s) of the MSMEs are given credit equal to 50% of their stake (equity plus debt) or Rs. 75 lakh whichever is lower	MSMEs meeting the eligibility criteria may approach eligible Banks.
8.	Credit Linked Capital Subsidy Scheme (CLCSS)	Any MSME unit is eligible under this scheme. But the units replacing existing equipment or technology with the same equipment or technology will not qualify for a subsidy under this scheme. Similarly, the units upgrading with used machinery would not be eligible under this scheme	This scheme provides an upfront subsidy of 15% on institutional credit up to Rs.1 crore (i.e. a subsidy cap of Rs.15 lakh) for identified sectors/subsectors/ technologies.	Through 12 Nodal Banks or agencies
9.	SIDBI Make In India Loan For Enterprises (SMILE)	New enterprises in the manufacturing and the services sector and existing enterprises undertaking expansion	The minimum loan size is Rs.10 lakh for equipment and finance. The minimum loan size for others is Rs.25 lakh. The repayment period is up to 10 years, including moratorium of up to 36 months	Through SIDBI.

Overview of Kirtane & Pandit LLP

Kirtane & Pandit LLP, Chartered Accountants (KPCA) is an Accounting, Auditing & Consulting firm with a widespread established network of financial experts across India. With the "Step ahead, Always" motto, we partner your growth journey with the delivery of sound financial solutions & value added approach.

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