A Study Of Credit Rating Potential And Awareness Among SMEs In Baddi Region Of Himachal Pradesh

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ABSTRACT

Purpose: This research paper aims to find out the awareness level of credit-rating agencies among SMEs and to find out the factors which enhance the growth of credit rating products.

Design/Methodology/Approach: Data was collected through self administered survey of around 150 SMEs in Baddi, Una and Panchkula region, and exploratory factor analysis was conducted to analyze the data with the help of SPSS 16.0.

Findings: The findings reported that most of the SMEs lacked awareness about Credit rating products. The three factors which can enhance the effectiveness of credit rating companies are managerial effectiveness, credibility and creative marketing efforts.

Originality/value: This paper provides an empirical evidence of SMEs awareness about credit rating products. This paper also suggests why SMEs are lacking opportunities of getting benefits of Credit rating products.

Keywords: Entrepreneurship, SMEs, Credit Rating

JEL Classification: M00, M10

INTRODUCTION

Small and medium-scale industries are one of the key drivers of economic growth in India. The major responsibility of the development of these industries lies with the State government. However, the Central government also assists them through various schemes and programmes. The major initiatives taken by the Central government for the development of the SME sector are:

1) To provide financial assistance in the form of funds from financial institutions and banks.

2) To enhance their infrastructure.

3) To help them in upgrading their technology.

4) To provide them with quality testing procedure.

After the liberalization in 1991, most of the SMEs were struggling to find a growth path due to competition from global brands. In India, a majority of the people are living in the rural areas are earning their livelihood from agriculture. If the SME sector grows, then the pressure on the agricultural sector (to provide livelihood) will ease considerably. As defined by the Ministry of Small Scale Industries, " A SME is an Industrial undertaking in which investment in fixed assets like land, plant and machinery does not exceed ₹ 1 crore, subject to the condition that these industries are not owned, controlled and are not the subsidiary of any Industrial undertaking." (Refer To Table 2). Generally, SSIs are categorized in three categories :

1) Cottage based Industries

2) Agro based Industries

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Table 1: Growth of Employment and Production In SME's		
Year	Employment (lakh persons)	Production (₹ Crore)
2008-09	659.35	880805
2009-2010	695.38	982919
2010-2011	732.17	1095758
Source: Annual Report of MSMEs (2011-12)		

Table 2: Definition of MSMEs		
Category	Investment (Plant and Machinery)	Service (Turnover)
Micro Enterprises	Less than ₹ 25 lakh	Less the ₹ 10 lakh
Small Enterprises	Less than ₹ 5 crore	Less than ₹ 2 crore
Medium Enterprises	Less than ₹ 10 crore	Less than ₹ 5 crore
Source: Annual Report 2011-12 on MSME's		

3) Small Industries

Although the small scale industries are suffering from a lot of problems like - financial problems, marketing problems, power and water related problems and export difficulties, but still, they offer large scale employment in our country. SSIs also offer a more equitable distribution of national income. As per the annual report of small scale industries (2011-2012), there has been a consistent growth in employment and production in the small scale industries (Table 1).

AN OVERVIEW OF CREDIT RATING

Credit rating is an evaluation tool developed by rating agencies for the measurement of small-scale industries. It is not based on mathematical calculation, but it is based on the judgement and experience of the rating agencies. There are certain benefits of awarding credit ratings to SMEs in India. An SME with a credit rating will receive the following benefits :

1) Faster and easy availability of loan.

2) Increased credibility with bankers, customers and business associates.

3) Support of export initiatives.

4) The Rating acts as a self improvement tool (the SME will improve its functioning and processes to better its rating for future evaluation).

OBJECTIVES OF THE STUDY

1) To find out the awareness level of credit rating among the small scale industries in Baddi region of Himachal Pradesh.

2) To find out the market potential of credit rating among small and medium scale industries in Baddi region.

3) To find out the underlying factors that can enhance the growth of credit rating products for SMEs.

LITERATURE REVIEW

Cantor and Packer (1997) revealed that different companies used different rating scales for credit rating, due to which, some agencies gave higher rating than others; however, it was mainly due to selection of sample biasness.

Kraussl (2005) analyzed that credit rating has a smaller impact on financial market and growth of SMEs in emerging economies. Carey et al. (2005) tried to examine the implications of new banking regulations (Basel II) for the Irish SME sector. The results showed a high degree of Irish SME dependence on banks as a source of funding.

Ongori (2008) revealed that SMEs are not strategically positioned to compete with large enterprises due to lack of ICT's adoption and the author further found that a major barrier to ICT's adoption in SMEs was lack of infrastructure;

as managers were not aware of ICT benefits and lack of security in ICT tools usage.

Kumar and Singh (2009) stated that in this liberalized economy, the SSI sector is facing challenges from the domestic as well as foreign players, hence for survival and growth, the government should provide incentives to these industries. Laxmi and Murugan (2009) highlighted that one of the biggest challenges for any SME in India is availing the credit facilities from banks. So, in order to solve this issue, the researchers suggested that banks should simplify the documentation process, lower interest rate and increase the period of repayment and service.

Ma and Lin (2010) revealed that SMEs are facing difficulties like downturn in trade that leads to reduction in cash flows and turnover. Bheemanagouda and Madegowda (2010) stated that ratings provided by credit rating agencies are not authentic and credit rating agencies have not been able to accomplish the goal of investor interest protection. Ali and Sristy (2010) revealed that SSIs offer a higher productivity of capital than the capital intensive sector due to low investment per worker. Pinto and Raghurama (2010) found that the small-scale sector had been considered as one of the major contributors to economic development of India, and the basic reason for this is that the quantum of capital and employment potential offered by SSIs is more than two or three times than what is provided by the large scale sector.

Sharma (2011) recommended eight strategic decisions for small businesses to be successful in exports.

Iyengar (2012) analyzed that reliability of rating assigned by two major credit rating agencies i.e. Moody's and Standard and Poor (S&P), and the findings suggested that both of these rating agencies are non- responsive to each other's ratings. Kar and Kalyani (2012) revealed that execution of strategy with a prudent use of the state's natural, social and financial resources made Gujarat small scale enterprises more viable for high economic growth, which was not the case with Odisha's SMEs.

RESEARCH METHODOLOGY

❖ **Research Design :** This research is mainly descriptive in nature as the data was collected through a self administered questionnaire on a sample size of 150 SMEs during the period from May to July 2012 in Baddi region of Himachal Pradesh. The responses were collected on the basis of convenience sampling. The Questionnaire consisted of two parts in which Part A contained questions related to the awareness of Credit Rating and Part B consisted of 9 statements related to the impact of growth of credit rating products.

It was very necessary to understand the faults of the research instrument. Hence, the questionnaire was pilot tested on 30 SMEs and the errors were corrected.

Table 3 : Analysis of Interest and Awareness of SME's Regarding Credit Rating		
	No of Respondents	**Percentage**
Did you ever hear about SME's Credit Rating?		
Yes	44	29.3
No	106	70.7
Did any Credit Rating organization approach you for Credit Rating?		
Yes	24	16.0
No	126	84.0
Did you ever go through the Credit Rating exercise ?		
Yes	16	10.7
No	134	89.3
Are you planning to go through the process of Credit Rating?		
Yes	109	72.7
No	25	16.7
Source : Primary Data		

Table 4 : Factor Analysis			
Sr no of Factors	Name of the factor	Statements	Factor loading
Factor 1	Management Effectiveness	Credit Rating companies provide consultancy for the improvement of business practices.	-.813
		Credit rating helps in organizing the MSMEs &SMEs.	.864
		Credit rating helps in relaxation w.r.t providing collaterals.	.739
Factor 2	Credibility	Credit rating serves as a good source of publicity for the rated entity.	-.904
		Credit rating helps in getting adequate quantum and timely loan from the bank	.844
Factor 3	Reputation enhancement	Credit rating will help in lowering the rate of interest and relax the bank's conditions.	.921
		Reputed third party opinion	.920
Factor 4	Marketing efficiency	Credit rating helps in marketing through publication and online channels	-.846
Source : Primary Data			

ANALYSIS AND DISCUSSION

From the Table 3, it is quite evident there was a lack of awareness about Credit Rating in SMEs of Baddi region. Only 30% of these industries had heard about credit rating. Most importantly, even the credit rating organizations were not focusing on these SMEs. Only 16% of such enterprises had been approached by these rating agencies. Almost 90% of the small and medium scale industries in this area had not been rated ever. However, 72% of the SMEs were interested in getting themselves rated by any credit rating agency.

❖ **Factor Analysis :** By conducting factor analysis, this research paper made an attempt to identify the underlying factors which can enhance the growth of the credit rating products in Baddi region. Factor analysis is mainly used for data reduction to identify a small number of factors that explain most of the variance observed in a much larger number of variables. To apply factor analysis, it was important to understand whether the data was adequate for this test or not. KMO test was applied and the value came out to be 0.74, which is above the value of .5. This means that the sample was adequate for undergoing factor analysis. Further, the value of Barlett's test was significant, which suggested that correlation matrix is not an identity matrix.

Principle component factor analysis was used to extract the factors and the number of factors to be retained was on the basis of screeplot and total variance explained. The solution gave four factors which accounted for 84.72% of the total data, which is quite good. The details of the factors, statements and factor loadings are given in the Table 4.

FINDINGS

1) Most of the SMEs were not aware about the credit rating products and the benefits such a rating offered for their enterprises.

2) Most of the small and medium scale industries were interested to know about the credit rating products.

3) Credit rating agencies need to improve their credibility, as most of the SMEs felt that these ratings were useless.

4) Credit rating agencies were not pitching in these areas, where there is so much potential for such ratings.

5) On the other hand, the SMEs who had already gone through the process of securing a credit rating for their enterprise suggested that the rating helps them in increasing credibility, marketing efficiency and management efficiency.

CONCLUSION

This research reveals that credit rating companies have not been able to penetrate in Baddi region of Himachal Pradesh as the awareness is very low. Most of the SMEs are interested in credit rating, but they were unaware of the benefits of these products.

Credit rating companies like CRISIL, ICRA, and FITCH etc. should increase their sales force and ask them to make these small and medium scale industries aware about the benefits of Credit Ratings. The SME's which had gone through the rating process believed that the rating helped them in increasing credibility, managerial effectiveness, marketing efforts and building reputation for raising funds from venture capitalist and banks. One of the key findings of this study is that the SMEs believed that credit rating agencies were not providing accurate and authentic ratings. Hence, Credit Rating agencies need to improve their credibility so that they can attract more small scale industries for the rating process. Small scale industries must look forward to get themselves rated as it will help them in raising funds and in export activities.

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