Financial Resources of Rural Entrepreneurs – A Study

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Abstract

This study focuses on the financial sources of rural entrepreneurs. Most of the rural nonfarm enterprises are tiny enterprises and they fall under the category of unorganized or informal sector activities. These unorganized tiny enterprises do not run as per the rules and regulations of the state on finance, human and other functional areas of management. It means they depend on informal sources of finance, they do not keep books of accounts, they depend on family members to run the business and they practice rudimentary methods of marketing and advertisement. Mobilizing funds for an enterprise is the most important function of rural entrepreneur. Surveys of current and potential entrepreneurs suggest that obtaining adequate access to capital is one of the biggest challenges to starting and growing a new business. In this article we are going to understand and compare various sources of finance raised by the rural entrepreneurs. This was an empirical study based on data collected from nonfarm tiny enterprises located in three taluks of Karnataka. As there is data paucity, nonfarm enterprises were selected based on convenient and snowball sampling methods. Data was collected from both primary and secondary sources. Combination of questionnaire and interview methods were used to collect data. Collected data was processed and tabulated by using the Statistical Package for Social Sciences (SPSS). Processed data was analyzed through univariate data analysis. This article found that very less rural entrepreneurs were able to get finance from the organized sources of finance such as banks and cooperative societies. The role of self-help groups and cooperative societies as sources of finance was less. Even today more number of rural entrepreneurs depends on money lenders to finance their ventures.

KEYWORDS: Entrepreneurs, Finance, Financial Resources, Non-farm Sectors, Rural Entrepreneurs.

Introduction

This study focuses on the financial sources of rural entrepreneurs. Finance is essential for all kinds of economic activities. Role of finance in rural entrepreneurship is all the more important because it is the lifeblood of an enterprise. In fact it is the finance which pools together other resources such as men, machine and material to start and run the enterprise. Importance of finance in business can be compared to lubricant in the process of production. Mobilizing funds for an enterprise is the most important function of an entrepreneur. Surveys of current and potential entrepreneurs suggest that obtaining adequate access to capital is one of the biggest challenges to starting and growing a new business. Banks, financial institutions, money lenders are the main sources for financial aspects. Various schemes are by commercial banks and governments to motivate individuals to take up business activities. Particularly for rural entrepreneurs special schemes are introduced by government. But there are conflicting views on the sources of finance and availability of finance from different sources to rural enterprises. Some scholars and studies look at the positive side of financial factors others point out the problems and challenges face by the entrepreneurs in general and rural entrepreneurs in particular. In this article we are going to understand and compare various sources of finance raised by the rural entrepreneurs.

Problematization

Studies have identified the difficulties faced by start-ups in raising capital even in the developed economies. This section does not give detailed picture of the sources of finance of rural and urban entrepreneurs. On the other hand attention is paid on the challenges the entrepreneurs of rural areas face in the financial areas of management. Brijesh Patel and Kirit Chavda explained the problems of Indian rural entrepreneurs in getting finance as, most of the rural entrepreneurs fail to get external funds due to absence of tangible security and credit in the market. The procedure to avail the loan facility is too time-consuming that its delay often disappoints the rural entrepreneurs.[1]Comin and Nanda identified the difficulties faced by start-ups in raising capital might adversely impact the commercialization of new technologies. The lack of financial market liquidity has been traced to several related factors. At the most basic level, the willingness of financial intermediaries to lend to entrepreneurs depends on financial and securities laws in a country.[2]

Levine says that the level of competition between financial intermediaries can impact the terms of credit to start-ups as well as the degree to which capital is allocated to the highest-quality projects.[3] The scenario of financial aspect in India varies from other countries particularly in rural areas. Microfinance is the main source of finance to the entrepreneurs in India. India Rural Development Report 2012-13 has given information on microfinance. According to the report microfinance is an important source of finance without bank accounts in mainstream banks, has made inroads in lending to the poor. In India two models of microfinance are there- the Self Help Groups (SHG) and Bank Linkage programme and Micro Finance Institutions (MFIs). The SHG-Bank Linkage programme links SHGs to banks and provides savings and credit facilities. SHGs pool the savings of their members and use them and bank loans to them. Sixty-eight percent of microfinance customers or more than half the rural households are members of SHG.[4]

It is clear from the above discussion that financial aspects of rural entrepreneurship are not unproblematic. Though majority of the rural enterprises fall under the category of unorganized or informal sector activities, raising finance is the big challenge. Therefore existing researches force us to raise a number of questions on the existing body of knowledge on financial management practices of rural entrepreneurship. What are the methods of raising finance by rural entrepreneurs? What are the sources of finance of finance for them? In order to answer all these questions an extensive and in depth study is needed. This study is an attempt in that direction and attempts to examine the financial management practices of rural entrepreneurs.

Objectives of the Study

The main objective of this study is to understand financialsources of rural entrepreneurs. The specific objectives of the study are –

1. To understand the theoretical background of financial sourcesof rural entrepreneurs.
2. To study the sources of finance of rural entrepreneurs.
3. To analyze on various sources for rural entrepreneurs.

Method of the study

This is an empirical study based on data collected from rural entrepreneurs located in two districts of Karnataka. Districts were selected based on their level of development. Two documents produced by the Government of Karnataka were used to decide the level of development. They are - one, High Power Committee for Redressal of Regional Imbalances Report, 2002, [5] and two, Human Development Report, 2014.[6]These reports have taluk-wise data on all the socio-economic indicators. Based on these data two taluks (Doddaballapura and Devanahally) were selected from the developed district (Bangalore Rural) and one taluk (Madhugiri) was selected from the backward district (Tumkur). In Devanahally taluk has 23 villages were randomly selected for data collection. In Doddaballapura taluk 18 villages were randomly selected for data collection. In Madhugiri taluk 19 villages were randomly selected for data collection.

In villages where more tiny units are operating 4 to 5 rural entrepreneurs were interviewed and in villages where less numbers of tiny units are operating only one entrepreneur was interviewed. All the entrepreneurs were selected based on convenient and snow ball sampling methods. In the selected villages the following tiny non-farm activities were considered for data collection. They are provision stores, stationery shops, bakery shops, flower sellers, vegetable sellers, medical shops, mutton shops, timber sellers, cloth sellers, brick makers, toy traders, beedi manufactures, garage centers, fruit sellers and street vendors.In order to collect data from the above primary sources schedule method, that is, combination of questionnaire and interview method was used. Questionnaire contained 145 questions and 90 rural entrepreneurs were chosen as samples for the purpose of research. 17 rural entrepreneurs who were engaged in manufacturing units and 73 rural entrepreneurs who were engaged in service units were interviewed to elicit information. In addition to the primary sources, data were also collected from secondary sources. The major secondary sources used were journals, articles, books, research papers, reports, and websites. Collected data were processed and tabulated by using the statistical package for social sciences. Frequencies were found and frequency tables were prepared. Data was analyzed through univariate analysis.

Conceptual Framework

Rural: The major conceptual hurdles one need to cross is connected with the meaning of rural, tiny non-farm activities and rural marketing. There are two pictures of rural in India. In the first picture rural is constructed in complete contrast to the urban and in the second picture boundaries between rural and urban is fluid and haggy. Census of

India presents rural and urban in poles apart mode. Census of India (2011) identifies urban areas with the following features (a) statutory towns,(b) Census towns with 5,000 and more population, majority (75 percent plus) engaged in non-agriculture works and population density of 400 per sq. km. According to the Census of India areas that do not meet the above criteria are rural[7]. Hence Census of India definition of rural is used in this study.

Rural Entrepreneurship (Non-farm):Tiny non-farm activates are identified using the definition given by the National Commission for Enterprises in the Unorganized Sector, 2007 (NCEUS). NCEUS considers the following as tiny and unorganized or informal activities - all unincorporated private enterprises owned by individual or households engaged in the sale and production of goods and services operated on a proprietary or partnership basis and with less than ten total workers. The above definition applies equally to all the sectors of the economy including agriculture. However, statistical operations in India so far have been covering only non-agricultural enterprises in the unorganized sector surveys[8]. Based on the above definition the concepts like non-farm sectors, non-agricultural sectors, rural self-employment and rural entrepreneurship are considered in the present study.

Discussion

Studies have identified the difficulties faced by start-ups in raising capital even in the developed economies. These difficulties might adversely impact the commercialization of new technologies. At the most basic level the willingness of financial intermediaries to lend to entrepreneurs depends on financial and securities laws in a country.[9]The development of financial market in India is drastically different from other countries. This difference is more pronounced in rural areas of the country. Compared to bank networks in the urban regions rural India has less number of bank branches. So in rural India microfinance is the main source of finance to the entrepreneurs. India Rural Development Report gives a detailed picture of this lopsided development of financial market in rural India. According to the report microfinance is an important tool in providing finance to people without bank accounts and access to mainstream finance and it has made inroads in lending to the poor. Report further explains that in India two models of microfinance are working - the Self Help Group (SHG) and Micro Finance Institutions (MFIs). National Bank for Agriculture and Rural Development (NABARD) links SHGs to banks and provides them savings and credit facilities. SHG pool the savings of their members and deposits the same savings in banks and gets loans from these banks (India Rural Development Report 2012-13).[10] Sixty-eight percent of microfinance customers or more than half the rural households are members of SHGs.[11]

Micro Finance Institutions(MFIs)are not wide spread like the SHGs'. They are relatively narrower in reach and provided loans through joint liability groups to almost 32 million customers. Initially MFIs were popular among the rural people. But later MFIlost credibility due to the micro finance crisis in Andhra Pradesh. A number of factors such as credit given without proper creditworthiness assessments, high interest rates and coercive loan recovery practices led to the crisis.[12]In the midst of all these ups and downs both central and state government felt that critical issue for income generation and enhancing the non-farm sector is that microfinance credit.[13] The same point is highlighted by National Commission for Enterprises in Unorganised Sectors, (NCEUS) and the Commission suggested catering credits through different agencies to the needs of some selected segments to the unorganised sector. As a result of all these efforts a number of schemes such as Laghu Udyami credit Card, Swarojgar Credit Card, Artisans Credit Card are introduced. These cards do not cover the entire unorganised sectors.[14]

Micro finance is the suitable financial source to rural people in India. It is considered as a grassroots instrument to alleviate poverty.[15]Micro enterprises require small loans or microcredit which is the term used for extending of small loans to very poor people, especially women, for generating income through self-employment activities. Lack of capitals as a major constraint to the development of women owned enterprises in rural areas which was mainly due to lack of identity and assets as collateral security.[16] Recent studies on family business show that entrepreneur's financing decisions are crucially influenced by owner's attitudes towards the utility of debt as a form of funding. Small family business and owners who do not have formal planning processes in place tend to rely on family loans as a source of support. Family business owners are averse to debt and this aversion is based on the possibility of large losses in case of loan failure. Small family firms' reliance on family loans and debt might be related to owners' interest in retaining control and choosing to establish limits on gearing because of risk factors and belief that stock exchange might be disadvantageous.[17]

As a result of the above problems rural entrepreneurs in India are facing severe problem in mobilizing capital for their start-ups. Most of the rural entrepreneurs fail to get external funds due to absence of tangible security and credit in the market. The procedure to avail the loan facility is too time-consuming and expensive. Delay in getting finance often disappoints the rural entrepreneurs. With global recession everywhere economic activities moving in slow phase. Large and medium enterprises who have taken large amount of loans from the banks are not paying and non performing assets of banks are mounting. All these developments have slowed the flow of finance. All are affected by these developments but the rural entrepreneurs are more affected. Because even during normal condition they were facing credit crunch now in the credit crisis they are not getting even the little they used to get in the normal condition. Major difficulties faced by rural entrepreneurs include low level of purchasing power of rural consumer so sales volume is insufficient, lack of finance to start business, reduced profits due to competition, pricing of goods and services, Financial statements are difficult to be maintained by rural entrepreneur, stringent tax laws, lack of guarantees for raising up of loans, difficulty in raising capital through equity, dependence on small money lenders for loans for which they charge discriminating interest rates and huge rent and property cost. These all problems create a difficulty in raising money through loans.

Proposition of raising funds through equity is out of question for the rural entrepreneurs. So loans are the primary source of finance for them which proved to be a great challenge for the rural entrepreneurship. Various policies of RBI regarding priority sector lending failed to achieve its objectives. To some extent micro financing movements started in India worked well. Self-help groups are the basic constituent unit of micro finance movement in India. Self-help groups are a group of a few individuals who pool their savings into a fund from which they can borrow as and when they need. Self-help groups are linked to banks and these banks lend two to three times of the deposits at cheaper rate of interest. But joining an existing SHG is often a costly affair for an aspiring villager. It is because in order to maintain parity among the members groups made it mandatory that a new member has to join by depositing the total accumulated amount of savings and interest of groups. So starting new SHG is an easy as compared to join existing one. NGO's also played important role in rural development. These NGO's are usually registered as societies and trust. They have less capital resources as they cannot raise equity capital.India Rural Development Report says that micro and small enterprises are eligible for credit at reduced rates under priority sector lending activities for non-farm activities, along with agriculture. The RBI also introduced a General Credit Card schemes in 2006 to provide access to credit to non-agricultural clients in rural and semi-urban along the lines of Kishan Credit Card scheme.[18]According to National Commission for Enterprises in the Unorganised Sector, institutional financial assistance to non-farm unorganised enterprises consists of 1) direct credit 2) indirect credit 3) micro credit 4) subsidy under government schemes.[19]

In the light of these financial problems of rural entrepreneurs at macro we shall examine the financial sources of rural entrepreneurs of Devanahally, Doddaballapura and Madhugiri taluks. In order to understand the finance sources of the rural entrepreneurs the following indicators are used. They are – external sources of finance, internal sources of finance and other sources of finance by rural entrepreneurs. The following table represent different sources of finance by rural entrepreneurs.

Table 1.External and Internal Sources of Finance to Rural Entrepreneurship (in percentage)

Sources of Finance	Devanahally	Doddaballapura	Madhugiri	Total
External Sources				
Bank	50	00	33	26
Cooperative Society	12	00	00	05
SHG	00	00	33	09
Money Lender	25	67	17	39
Others	00	11	00	04
Bank and SHG	13	00	17	09
Society and SHG	00	11	00	04
SHG and ML	00	11	00	04
Total	100	100	100	100
Internal Sources				
Own Savings	70	60	50	60
Parents	20	30	42	31
Relatives	10	10	08	09
Total	100	100	100	100
Internal and External Sources				
Own Savings	17	30	20	23
Parents	17	24	30	23
Banks	25	00	20	14

Money Lenders	33	46	10	31
Society	08	00	00	03
SHG	00	00	20	06
Total	100	100	100	100

Note – SHG = Self-Help Group, ML = Money Lender
Source: Data Collected from Field Work.

The above table has data on the external and internal sources of finance of rural entrepreneurs. Banks, self-help groups, cooperative societies and money lenders are the main external sources of finance. Among these external sources of finance banks, self-help groups and cooperative societies are the organized sources of finance. Money lenders and other sources are the main unorganized sources of finance. Loan from organized source has low or reasonable rate of interest, flexible terms and conditions and less stringent actions if borrower defaults. Compared to organized sources loan from unorganized sources has exorbitant rate of interest, rigid terms and conditions and if borrower defaults to repay he or she would loss the properties pledge to get the loan. That is why all the borrowers are very eager to get loan from the organized sources. In this study out of 90 rural entrepreneurs studied only 23 (21 percent) entrepreneurs borrowed from outside sources for business purpose. Of these 23 entrepreneurs only 26 percent of the rural entrepreneurs could get finance from banks. When compared to the total entrepreneurs of three taluks definitely banks were not significant sources of finance. But if we add other sources of finance such as self-help groups and cooperative societies to the source of bank the overall percentage of finance obtained from banks increases to 53 percent. It means fifty percent of rural entrepreneurs got finance directly or indirectly (through self-help groups and cooperative societies) from the banks.

It is clear from the figures given in the above table that large number of rural entrepreneurs, almost 39 percent of the rural entrepreneurs; depend on money lenders to finance their business ventures. Rural entrepreneurs also borrowed 4 percent each from other sources and from money lenders and cooperative societies. If we add these figures to the percentages of money lenders total borrowings from the unorganized sector increases to 47 percent. There are some rural entrepreneurs who either did not go for or could not get finance from external sources. In other words they depended on internal sources of finance. Own savings, contribution from the parents and money borrowed from friends and relatives with or without interest are the main internal sources of finance. Of the total 90 entrepreneurs, 32 (29 percent) rural entrepreneurs mobilized finance for their business internally. Among the internal sources of finance own savings financed almost 60 percent of the rural ventures. After own savings 31 percent of the rural entrepreneurs got finance to start business from their parents. Among the taluks we cannot find much variation so far as internal sources of finance is concerned. However when we look into the external sources of finance in Doddaballapura most of the rural entrepreneurs (89 percent) could not get finance from organized sources. They had to depend heavily on money lenders and other unorganized sources of finance.

In addition to the above entrepreneurs who borrowed from internal and external sources there were around 35 (32 percent) rural entrepreneurs who borrowed both from internal and external sources. Here also percentages of rural entrepreneurs borrowing from money lenders (31 percent) were more than any other sources. Own savings and contribution from parents were the important sources of finance under both category. The empirical evidences we have discussed in the above paragraphs brings two factors to forefront. One, some of the rural entrepreneurs could get finance from organized sector. Two, even now the role of money lenders and other sources of unorganized sectors have not diminished significantly. Indeed commercial banks are making some efforts to reach out to the rural people. In spite of the presence of commercial banks and self-help groups' money lenders have occupied major part.

Another source of finance to rural entrepreneurs isSelf Help Groups (SHGs). Self-help groups form the basic constituent unit of micro finance movement in India. Self-help groups are a group of a few individuals who pool their savings into a fund from which they can borrow as and when necessary. Such a group is linked with banks but joining an existing SHG is often a costly affair for an aspiring villager as in order to maintain parity among the members a new member has to join by depositing the total accumulated individual savings and interest of groups. NABARD reports thatsixty-eight percent of microfinance customers or more than half the rural households are members of self-help groups.[20]The present data has found that 09 percent of the rural entrepreneurs have benefited from SHGs in Madhugiritaluk. However role of SHGs in financing rural entrepreneurs in Devanahally and Doddaballapura taluks is very insignificant. In both the taluks rural entrepreneurs raised funds from money lenders, banks and co-operative banks along with SHGs. But still the micro credit programme is yet to take deep roots in the state. Given the limited outreach of Non-Government Organizations (NGOs), despite their large number, there is a case for the state Governments to intervene proactively by promoting and supporting the SHGs. Micro financing through SHGs and NGOs consists of small loans in the range of Rs. 2000 to 3000 is not sufficient to finance entrepreneurial ventures. Given the demonstrated enthusiasm and capacity of the SHGs there is a case for increasing the loan amount so as to help them to set up and sustain micro enterprises which could in turn provide regular employment and income to poorer households.[21]

Commercial banks have a role to finance the initial capital and also working capital requirement of small enterprises. But the present study shows that only a small number of rural entrepreneurs could obtain finance from the commercial banks. Compared to private money lenders commercial banks role in financing the rural entrepreneurs is less not significant. National Commission for Enterprises in the Unorganised Sector (NCEUS) has pointed out that rural entrepreneurs' inability to meet all the documentation requirements of the commercial banks is the main reason for not availing bank loan. We have already seen in the social background of entrepreneur who becomes rural entrepreneurs. Most of the time those who face distress conditions shift towards non-farm activities. These entrepreneurs face several problems such as weak financial base, difficulty in establishing right property over joint property, difficulty in finding guarantors and last but not the least difficulty in understanding the exact requirements. The last problem arises due to their low educational levels and lack of guidance. Banks find it difficult to advance loans in the absence of proper documents. Increased involvement of commercial banks in micro financing is absolutely essential for a sustainable micro financing programme.[22]

Conclusion

In this paper we have discussed the sources of finance of rural entrepreneurs. It is found that very less rural entrepreneurs were able to get finance from the organized sources of finance such as banks and cooperative societies. If we consider the self-help groups and cooperative societies under organized sources of finance number of rural entrepreneurs who got finance from organized sources increases a little. Even today more number of rural entrepreneurs depends on money lenders to finance their ventures. It is easier get finance from the money lenders but the exorbitant rate of interest money lenders charge eats up the large part of entrepreneurs' profit.

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