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Research paper

Financial Institutions and SME Growth in South India through Access, Innovation, and Policy Support

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Abstract

India has emerged as one of the fastest-growing economies globally, with Small and Medium Enterprises (SMEs) playing a critical role in this expansion. This study investigates the role of financial institutions in supporting entrepreneurship and business growth among SMEs in South India. It specifically examines the challenges faced by entrepreneurs in accessing finance and evaluates the effectiveness of financial institutions in mitigating these challenges. A sample of 247 SMEs from four South Indian states was selected to analyze the level of institutional support and the impact of financial interventions on business development. The findings reveal that limited access to timely and adequate credit remains a significant barrier to SME growth. However, the study also highlights the proactive role of financial institutions in offering tailored credit schemes, technical assistance, and capacity-building programs. Furthermore, government policies, public-private collaborations, and innovative financial products have been identified as key enablers of a supportive entrepreneurial ecosystem. The study underscores the importance of financial literacy programs and awareness initiatives in empowering entrepreneurs to make informed financial decisions. Overall, this research provides actionable insights for policymakers and financial institutions to strengthen SME development and promote inclusive economic growth in South India.

Keywords: *Economy, Growth, Government, Financial Institutions, Support, SMEs.*

1. Introduction

India is a developing nation, and the government has been introducing many schemes to develop the nation by eradicating the nation's unemployment problem. Numerous reasons have contributed to the expansion, including: i) the government's strong socioeconomic policies; ii) the influx of both domestic and international capital; iii) an increase in disposable income; iv) rising consumption, among many other favorable characteristics. The MSME sector is probably going to keep contributing significantly to the expansion of the Indian economy. The MSME sector has grown impressively during the past 10 years in terms of employment, output, exports, and the number of units. This industry may contribute far more and realize its enormous potential if the proper support networks and enabling structure are in place. Over the last 60 years, the MSME sector of the Indian economy has become one of its most active and vibrant sectors. It created more than 11 core employment opportunities and has the potential to create more at a lower capital cost as compared to large industries. It also helps in the industrialization of rural and backward areas. This may result in reducing regional imbalances and a more equitable distribution of national income and wealth. MSMEs are complementary to large industries as ancillary units. The MSME sector contributes enormously to the socio-economic development of the country. These initiatives provide a lot of opportunities to MSMEs to start new businesses and continue existing businesses efficiently. Entrepreneurship and economic growth play a significant role in the nation's overall development. Entrepreneurship involves initiating, developing, and managing a fresh business venture to reach a specific goal. Alternatively, economic growth refers to the increase in a country's production of goods and services. Financial institutions may promote economic development and the creation of new businesses as they share a connection. This paper will examine how financial institutions aid in the growth of entrepreneurship and the economy.

Despite its contributions, this study has certain limitations. Firstly, the research is based on cross-sectional data, which restricts the ability to observe changes over time or draw causal inferences about the relationship between financial access and SME performance. Secondly, the study focuses specifically on four states in South India, and therefore, the findings may not be generalizable to SMEs in other parts of the country with different economic and institutional conditions. Additionally, self-reported data from entrepreneurs may introduce subjective bias, and the lack of firm-level financial performance indicators limits the depth of accounting-based analysis. Future research can address these limitations by adopting longitudinal designs and incorporating multi-region comparative studies to offer a broader understanding of SME financing in India.

2. Literature Review

2.1 Financial Institutions

Financial institutions play a vital role in the economy as they enable individuals to save, invest, and borrow money. These organizations also aid businesses in handling risks, acquiring funding, and expanding their activities (Demirguc-Kunt&Klapper, 2018). For the most part, finance remains an indispensable growth engine. The growth process is both strengthened and facilitated by finance. Finance, however, is not a prerequisite for progress. Even while finance and development are closely related, they have different identities; thus, there isn't a direct causal link between them.

2.1.1 The Importance of Entrepreneurship and Economic Growth

An economy's ability to expand is largely dependent on the highly driven individuals known as "entrepreneurs," who are not afraid to take chances to achieve measurable progress. This is demonstrated by the high growth and success rates of entrepreneurs in industrialized economies. An examination of India's past reveals that the British colonial empire suppressed Indian businesses and entrepreneurial spirit. Progress was slowed down by the British government's utter devastation of Indian handicrafts and local industries. However, Indian planners have recently been interested in the necessity of encouraging entrepreneurship for the nation's economic development. Though the country is committed to giving equal opportunity for growth and for reducing regional imbalances, entrepreneurial growth has been limited to certain regions of the nation. (Al-Mahrizi and Al-Habsi, 2018).

2.1.2 Fostering Entrepreneurship Through Financial Support Systems

The function of banks in economic growth has been defined and interpreted differently over time, according to an investigation into the history of economic philosophy. The wide foundation of entrepreneurship is one of the functions of banks in attaining economic growth. Banks are financial organizations that offer financial infrastructure, which is crucial to the growth process. Banks are more than just organizations that disburse money; they also contribute to the complete overhaul of the economy. Banks have the advantage of economics in their administration and are more effective than other organizations at mobilizing resources (Demirguc-Kunt & Klapper, 2018). Banks, particularly NABARD, are crucial to the growth of small businesses, which significantly contribute to the expansion of the industrial sector. Credit is only one of several inputs in the development wheel, thus, if it is not used appropriately, it won't do anything on its own. The recycling of money will inevitably come to a grinding halt if the revenue from the assets supported by the banks does not increase. One important element in encouraging entrepreneurship is timely and sufficient finance (Al-Mahrizi and Al-Habsi, 2018).

2.1.3 SME Financing and Access to Credit

A comprehensive body of cross-country empirical research has consistently highlighted the critical role of financial access for small and medium-sized enterprises (SMEs) in fostering economic growth, reducing poverty, and enhancing productivity. It was observed that SMEs often faced more significant financing obstacles compared to large firms, primarily due to higher information asymmetries, limited collateral, and the lack of credit histories, which constrained their ability to secure external funding (Beck & Demirguc-Kunt, 2006). Across various countries, differences in lending practices, institutional quality, and regulatory environments influenced the extent to which banks provided financing to SMEs. In particular, the ownership structure of banks—whether state-owned, foreign-owned, or privately held—had a considerable impact on their willingness and capacity to lend to small businesses (Beck et al., 2011). Additionally, global analyses identified key drivers and impediments of SME lending, such as credit information systems, legal rights of borrowers and lenders, and the use of relationship-based versus transaction-based lending models (Beck et al., 2008). A significant constraint emerged from weak financial infrastructure and limited bank competition, which disproportionately affected SME access to credit in developing economies (Beck et al., 2004). Furthermore, the importance of SME financing was underscored in terms of its positive association with poverty alleviation and employment generation, with countries that promoted financial inclusion demonstrating more inclusive economic growth (Beck et al., 2005). Overall, the literature reinforced the conclusion that access to finance remains a substantial barrier to SME development and that tailored policy interventions and reforms in banking practices are essential to bridge the credit gap and stimulate inclusive economic performance.

2.1.4 Financial Institutions' Role in Supporting Economic Growth

The majority of developing nations are currently dominated by the primary sector, and India is no different. As a result, a rational foundation for acknowledging the contribution of the industrial sector to the nation’s overall economic growth emerges. The improvement of the standard of living for society’s members is the ultimate goal of all economic development. Creating an atmosphere that allows for the best possible use of resources such as capital, labor, or materials is the responsibility of the entrepreneur in this situation. India is not an exception to the rule that the majority of developing nations are currently dominated by the primary sector. As a result, a rational foundation for acknowledging the contribution of the industrial sector to the nation’s overall economic growth emerges. Improving the standard of living for society's members is the ultimate goal of all economic development (Al-Azri and Al-Habsi, 2019).
In this case, the entrepreneur’s job is to create an atmosphere that allows resources such as cash, labor, or materials to be used as efficiently as possible. in charge of creating over half of the new service innovations and producers. State and private entrepreneurs coexist in a nation like India. Private business owners oversee the small-scale industrial sector. Therefore, encouraging entrepreneurship in the small and medium-sized industrial sectors is crucial to accelerating development. In India, there is a need for a broad-based entrepreneurial class because the activation of the factors of production must be accelerated to increase economic growth, spread economic activity, develop tribal and backward areas, create jobs, raise the standard of living for the weaker segments of society, and involve all segments of society in the growth process. New people can only start their own business if a favorable environment is established. An entrepreneur acts as a catalyst, generating wealth, opening new opportunities, and promoting growth in other economic sectors.

2.1.5 Money used to start or grow a business

Credit can make a big difference in the lives of the poor through the enhancement of income and job opportunities. Many small and tiny sector industrial units in rural areas have suffered a setback, while many have gone sick beyond redemption, primarily because not much

care was taken first to formulate the credit plans (Demirguc-Kunt&Klapper, 2018). As regards the common credit-related problems faced by the SSI units, inadequacy of credit limits sanctioned was reported to be the most important one, followed by an increase in interest rate, banks' insistence on adequate security, including collateral, and delay in sanction/disbursement of credit facilities. Borrowers are not getting credit in time. This has led to misuse or inefficient use of the credit. It is said that even for a simple loan, bankers take more than a month to consider the application (Al-Azri and Al-Habsi, 2019).

Bank finance is not going to help the rural poor in a big way unless economically viable programmes are implemented at the micro level to generate productive employment. Finance is lacking in the small-scale sector (Demirguc-Kunt&Klapper, 2018). Even after a good amount of financial assistance and credit facilities, the small-scale sector suffers a lot. The very high rate of interest charged on loans, blockage of capital, dependence on unorganized sources, delay in payment of bills, and lengthy procedures of financial institutions create obstacles in the growth of small-scale units. A good magnitude of financial assistance and credit facilities is still more acute in the small-scale sector. Small entrepreneurs are compelled to meet their financial requirements from the unorganized sector at a very high rate of interest.

2.1.6 Money Movement

According to the recommendations of the Nayak Committee, the RBI has taken several steps to guarantee prompt and sufficient credit to the SSI sector (Al-Balushi and Al-Busaidi 2019). For example, SSI units' working capital requirements are now calculated using a simplified process. The working capital requirements of SSI units were to be calculated by banks in April 1993 using at least 20% of the anticipated yearly turnover (Lin et al. 2018). Banks have also been asked to make sure that out of the funds available to all SSI sector segments 40% are made available to units that have invested up to DIT 5 lakhs in plant and machinery 20% are available to units that have invested between DIT 5 and DIT 25 lakhs and the remaining 40% are available to the other SSI units (Fink and Steffen 2018). Local area banks and specialized commercial bank branches will be the best means of providing small business owners with bank credit. Information regarding the credit risk of investing in small business owners in their areas can be found in local area banks (Al-Harrasi and Al-Hinai, 2017).

2.2 Microfinance efficacy

Microfinance has emerged as a pivotal tool in addressing poverty and financial exclusion, particularly in rural and underserved communities. It was found that microfinance initiatives significantly contributed to poverty alleviation by enhancing household income, improving energy access, and fostering entrepreneurial activity; however, their effectiveness varied depending on institutional frameworks and socio-economic contexts (Masselus, 2024). Systematic reviews of microfinance-led outcomes revealed that while access to small loans and financial services empowered rural communities, especially women, the long-term sustainability of such interventions required strong community participation, financial literacy, and infrastructural support (Parwez, 2025). Moreover, microfinance played a crucial role in empowering vulnerable women through entrepreneurship by offering opportunities for income generation and economic independence. Yet, several challenges such as limited market access, patriarchal constraints, and insufficient policy support persisted, thereby necessitating a holistic approach that included skill development, mentorship, and inclusive governance (Ranabahu & Tanima, 2022). On the theoretical front, the possibility of credit rationing within the context of the Stiglitz-Weiss model was re-examined, reaffirming that asymmetric information between lenders and borrowers could lead to rationing even in the presence of creditworthy applicants. This occurred because higher interest rates might attract riskier borrowers, prompting financial institutions to limit loan supply to minimize default risks (Arnold & Riley, 2009). Collectively, the literature emphasized that while microfinance can be a transformative instrument for social and economic empowerment, its integration with broader structural reforms and targeted policies is essential to overcome systemic limitations and ensure equitable access to credit.

2.3 Exploring Financing Channels for SMEs: The Role of Financial Institutions

The finest financial performance is the result of a variety of talents that are developed through financial management strategies. According to Lin et al. (2018), an organization's behavior and use of financial planning knowledge define its financial management practices. SME financial performance problems are often caused by a lack of knowledge about financial management and the unpredictable nature of the company environment. Whether the manager is an owner or a hired manager, the company’s profitability will suffer if financial decisions are made incorrectly. As a result, ineffective financial management may affect SME profitability. Insufficient understanding of effective financial management has frequently led to the failure of SMEs (Ongena et al., 2019).

2.4Support Services

Financial planning entails establishing financial goals, creating financial policies, and creating financial processes. According to Al-Balushi and Al-Busaidi (2019), this kind of planning is crucial to the accomplishment of any business endeavor and its seamless operation. The failure of numerous technically sound and mechanically feasible industrial projects can be attributed to inadequate financial planning. For both large and small businesses, financial planning is crucial both during the startup phase and for continuing businesses. This is because in the ever-evolving business world of today, financial planning must be an ongoing process for business endeavors to survive and expand (Ongena et al., 2019).

2.5 Risk Management

Financial institutions face numerous challenges in managing risks (Ongena et al., 2019). Some of the challenges include credit risk, market risk, operational risk, and reputational risk. Credit risk is the chance that a borrower may fail to make payments. Credit or another monetary responsibility. Market risk refers to the possibility of suffering financial losses as a result of shifts in market circumstances.

2.6 Role of Financial Institutions in Providing Financial Inclusion

The mobilization of people’s savings through inclusive financing contributes to the nation’s economic development and expansion. In addition, it educates the public about moneylenders and other unofficial sources of financial services, which are expensive and unreliable. If our rural economy is strengthened, it can be a useful ally during monetary and economic crises. In essence, financial inclusion is

predicated on three key ideas, namely. financial services affordability uses and admission. Recent developments in global markets have shown how urgently financial inclusion is needed in the rural and economically disadvantaged areas of the nation. Extending banking facilities to all parts is important as it helps in achieving not only comprehensive growth and development.

2.7 Credit Rationing and Information Asymmetry

Credit rationing has remained a persistent issue in financial markets, particularly affecting small and medium enterprises (SMEs), firms in emerging economies, and low-carbon investment initiatives. Research indicated that information asymmetry plays a pivotal role in limiting access to credit, often resulting in inefficient resource allocation and hindered economic growth. It was observed that when lenders lacked adequate information about borrowers, they tended to ration credit rather than raise interest rates to mitigate the risk of adverse selection and moral hazard (Flatnes, 2021). Firm-specific characteristics such as size, age, and ownership structure were found to significantly influence credit access, and the impact of asymmetric information was notably pronounced along gender lines, with women-led enterprises facing higher barriers (Sackey et al., 2023). The introduction of loan guarantee schemes proved beneficial in alleviating credit constraints and contributed to improved economic welfare by enhancing borrower-lender trust and reducing perceived risk (Wang et al., 2020). Despite these mechanisms, persistent supply-side and demand-side issues continued to hinder SME financing, with banks exercising caution even when viable demand for credit existed (Andretta, 2021). In the context of sustainable development, it was revealed that credit rationing obstructed investment in low-carbon projects due to perceived uncertainty and long-term return horizons, thereby undermining green transition efforts (Haas & Kempa, 2023). Additionally, credit risk and pricing were found to be significantly influenced by both economic factors and the degree of information asymmetry, which served as moderating variables in financial decisions (Marjohan & Andriani, 2024). Moreover, discouraged borrowing emerged as a critical phenomenon among SMEs, where firms refrained from applying for credit due to expectations of rejection, further reinforcing the cycle of underinvestment and limited growth (Kishore Kunal, 2025; Nguyen, 2021). This collective body of research underscored the critical need for enhanced transparency, better credit assessment tools, and targeted financial policies to reduce credit rationing and support inclusive economic development.

2.7.1 Importance of Financial Inclusion

The concept of inclusive financing thus refers to providing economic enlargement with equal opportunities to society. It is creating opportunities for growth and making it accessible to society. Inclusive financing occurs when members of society, despite of their individual position, take part in the process and contribute to the process without any prejudice. Therefore, it highlights that economic prospects shaped in the growth process are accessible to all, primarily to the poor, to the utmost extent possible.

2.7.2 Services Offered by Financial Institutions to Promote Financial Inclusion

Financial institutions assist in offering a range of financial services for individuals and organizations to manage their finances effectively. Financial institutions provide various services to encourage financial inclusion.

1. Savings Accounts

An important financial instrument that allows people to save money and earn interest is a savings account. Financial institutions provide a range of savings accounts with different benefits, such as low fees and no minimum balance requirements, to ensure that they are accessible to a wide range of people.

2. Loans

Most of the banks require mortgage or collateral security for their loans. When compared with the formalities to be completed to secure a loan, securing a loan from a moneylender becomes easier than from banks for meeting their daily requirements. Basically, it is seen that banks are interested in meeting their annual or financial targets, which is why they are paying more attention to accounts that are larger. Banks show less interest in accounts requiring small loans, as they are not profitable to them

3. Insurance

Admittance to finance by the household is done for several reasons, but the most vital are contingency planning and risk mitigation. For the insurable contingencies, people go for savings for retirement, get insurance, and some risk hedging products. Once such basic wants are met, and then households require access to credit for the creation of a livelihood. Along with these, they also require credit for day-to-day consumption and emergencies. Finally, individuals require savings and investment for wealth creation. (Tabak et al., 2016).

4. Banking on mobile devices

People may easily and conveniently obtain financial services through mobile banking. With the use of bank-provided mobile banking apps, people may move money, pay their bills, and check their account balances.

2.7.3 Statement of the Problem

The presence of women entrepreneurs in SME sectors is crucial for achieving rapid economic growth through industrialization, as it fosters a congenial entrepreneurial climate, enabling them to pursue careers in developing countries like India. Consequently, the governmental policy directions and performance of commercial banks, financial Institutions, and training institutions engaged in promoting and developing women entrepreneurs become very crucial for the country. Today, banks and financial institutions are playing an important role in extending financial help to women entrepreneurs. The government is giving various incentives and support to women entrepreneurs. Despite these incentives and support, they lack adequate finances. The efficiency of current financial services, including grants, loans, and venture capital, in promoting the expansion of SMEs is unclear. Furthermore, little is known about the obstacles to financial inclusion, such as strict lending regulations and low financial literacy. This study aims to determine how these financial services affect SMEs' sustainability and success, as well as how financial institutions may better assist regional entrepreneurs.

2.7.4 Objectives of the study

1. To present the opportunities for small and medium-scale enterprises in India.
2. To present the socio-economic profile of the sample respondents.
3. To trace out the influencing variable through the Structural Equation Model.
4. To offer suggestions to the small and medium-scale entrepreneurs.

2.7.5 Sampling Design

The present study conducted in South India, Andhra Pradesh, Karnataka, Kerala and Tamil Nadu states come under South India. There are lots of different cultures in the state; the people's behaviour, income level, attitude, and business style are different in the above 4 states. The central Government has taken many steps to promote entrepreneurs, which help our country's economy. The present study was conducted in South India, a structured questionnaire was framed and distributed for data collection, and Google Forms were used to collect data from other states. The clear instructions were given in the questionnaire to the respondents; if they were eligible, they could continue to fill out the questionnaire. 40 printed questionnaires were distributed in Tamil Nadu, remaining were collected online.
The following table 1 shows the data collection from different states.

Table 1: Data collection details

Sl. No.	State	Number of data collected
1	Andhra Pradesh	61
2	Karnataka	62
3	Kerala	59
4	Tamil Nadu	65
	Total	247

The above table shows the data collection details from 4 states in South India; 61 respondents filled the questionnaire from Andhra Pradesh. 61 respondents filled the questionnaire from Karnataka, 59 respondents filled out the questionnaire from Kerala, and 65 questionnaires were filled out from Tamil Nadu. All put together, 247 samples were taken for this study.

2.8 Tools and Techniques

The respondents' socioeconomic status was displayed using a straightforward % evaluation. Coefficient correlation was used to determine the relationship between the various dimensions, and the Structural Equation Model was utilized to identify the variables that fit the various dimensions used for this study.

2.9 Analysis and Interpretation – Percentage analysis

Table 2 highlights the gender distribution of the respondents. Out of the 247 individuals surveyed, a majority of 166 respondents, accounting for 67.21%, were male, while 81 respondents, representing 32.79%, were female. These values indicated that male respondents significantly outnumbered their female counterparts in the study, suggesting a gender disparity among the participants. This gender imbalance warrants a discussion on gender-specific barriers in entrepreneurship, particularly challenges faced by women, such as stricter collateral requirements and limited access to credit, which may contribute to their underrepresentation.

Table 2: Gender of the respondents

Gender	Male	Female	Total
Number of respondents	166	81	247
Percentage	67.21	32.79	90

Source: Primary data

Table 3 outlined the age group distribution of the respondents. Out of the total 247 individuals surveyed, the highest number—86 respondents, representing 34.82%—belonged to the 41 to 50 years age group. This was followed by 68 respondents (27.53%) aged between 31 and 40 years, and 48 respondents (19.43%) who were under 30 years of age. Additionally, 45 respondents, accounting for 18.22%, were above 50 years old. These values indicated that most respondents were middle-aged, with a notable representation across all age groups.

Table 3: Age group of the respondents

Sl. No.	Age group	Number of respondents	Percentage
1	Less than 30 years	48	19.43
2	31 years to 40 years	68	27.53
3	41 years to 50 years	86	34.82
4	Above 50 years	45	18.22
	Total	247	100

Source: Primary data

Table 4 shows the educational qualifications of the respondents. Out of 247 sample respondents, thirty-nine (15.79%) respondents had completed schooling. Fifty-six (22.67%) respondents are diploma / ITI holders. One hundred and four (42.11%) respondents are undergraduates, and the remaining forty-eight (19.43%) respondents are postgraduates. The majority (42.11%) of the respondents are undergraduates.

Table 4: Qualification

Educational Qualification	Schooling	Diploma / ITI / others	Under Graduate	Post Graduate	Total
Number of respondents	39	56	104	48	247
Percentage	15.79	22.67	42.11	19.43	100

Source: Primary data

Table 5 illustrates the marital status of the respondents. Out of the total 247 individuals surveyed, a significant majority of 211 respondents, accounting for 85.43%, were married. In contrast, only 36 respondents, making up 14.57%, were unmarried. These values indicated that most of the respondents were married, suggesting a prevalence of familial responsibilities among the surveyed group.

Table 5: Marital Demographics of the Survey Population

Marital Status	Married	Unmarried	Total
Number of respondents	211	36	247
Percentage	85.43	14.57	100

Source: Primary data

Table 6 shows the firm size of the respondents. Out of 247 respondents, ninety-seven (39.27%) have small-scale industries, and the remaining one hundred and fifty (60.73%) have medium-scale industries. The majority (60.73%) of the respondents have medium-scale industries.

Table 6: Size of the firm

Firm Size	Small	Medium	Total
Number of respondents	97	150	247
Percentage	39.27	60.73	100

Source: Primary data

Table 7 presents the distribution of respondents based on the location of their enterprises. Among the 247 respondents surveyed, the highest proportion—95 individuals, accounting for 38.46%—operated their enterprises in urban areas. This was followed closely by 86 respondents (34.82%) who had their businesses located in semi-urban regions. Meanwhile, 66 respondents, representing 26.72% of the total, operated in rural areas. These figures indicated that urban and semi-urban locations collectively hosted most of the enterprises, highlighting a concentration of business activity outside rural zones.

Table 7 : Location of the enterprise of the respondents

Location of the enterprise	Urban	Semi urban	Rural	Total
Number of respondents	95	86	66	247
Percentage	38.46	34.82	26.72	100

Source: Primary data

Table 8 shows the business ownership of the respondents; ninety-six (38.87%) respondents are sole proprietors. Seventy-four (29.96%) respondents are in partnership. Forty-four (17.81%) respondents are in a private limited and the remaining thirty-three (13.36%) respondents are in a co-operative society. The majority (38.87%) of the respondents are sole proprietors.

Table 8: Type of ownership of the respondents

Type of ownership	Sole proprietorship	Partnership	Private limited	Co-operative society	Total
Number of respondents	96	74	44	33	247
Percentage	38.87	29.96	17.81	13.36	100

Source: Primary data

Table 9 shows the capital invested in the business; forty-four (17.81%) respondents have invested below 10 lakhs in the business. Sixty-eight (27.53%) respondents have invested 11 lakhs to 50 lakhs. Ninety-eight (39.68%) respondents have invested 51 lakhs to 90 lakhs in the business, and the remaining thirty-seven (14.98%) respondents have invested above 90 lakhs in the business. The majority (39.68%) of the respondents have invested 51 lakhs to 90 lakhs in the business.

Table 9: Capital invested in enterprise

Capital invested in the enterprise	Below 10 lakhs	11 lakhs to 50 lakhs	51 lakhs to 90 lakhs	Above 90 lakhs	Total
Number of respondents	44	68	98	37	247
Percentage	17.81	27.53	39.68	14.98	100

Source: Primary data

The influence of FI in encouraging entrepreneurship in SME businesses in the study region has been determined by the researcher using four dimensions. The dimensions are (i) Choose financial institutions as a source of finance, (ii) Give your opinion about financial institution lending norms, (iii) The statement below relates to the rate of your opinion about accessibility of financial institutions, and (iv) The statement below is appropriate to rate your opinion about financial support of financial institutions. The variables under each dimension are listed hereunder.

3. Structural Equation Model

3.1 The level of impact of financial institutions as a source of finance

The researcher has taken the dimension Financial institutions as a source of finance, this dimension has ten variables, i.e. (i) Trouble free accessibility of financial institutions, (ii) Easy lending procedures of financial institutions, (iii) Flexible lending norms of financial institutions, (iv) Less collateral requirements, (v) Low transaction cost, (vi) Flexible repayment terms, (vii) Low interest rate, (viii) Subsisized credit, (ix) Transparency in lending and (x) Regular availability of loanable funds. The expected score for good fitness was presented in the table, and the calculated values are also presented in the following table.

Table 10: SEM - Model Fit Summary – The level of impact of Financial institutions as a source of finance

Test Factor	TLI (Tucker-Lewis index)	NFI (Normed fit index)	GFI (Goodness-of-fit index)	Chi-Square	CFI (Comparative fit index)	RMSEA (Root mean square error of approximation)	AGFI (Adjusted goodness-of-fit index)
Value	0.911	0.962	0.983	52.899	0.973	0.031	0.961
Range	>0.90	>0.95	>0.95	p>0.05	>0.95	<0.06	>0.95
Result	Good Fit	Good Fit	Good Fit	1% level	Good Fit	Good Fit	Good Fit

Source: Computed data

The above table shows that the values are above the minimum requirement range. This dimension has eleven variables, the output of the SEM presented in the above table. The values of chi-square, GFI, AGFI, CFI, NFI, TLI, and RMSEA are above the required range. The analysis concluded that all the variables are fit, and all eleven variables may be taken for further studies.

3.1 The level of impact of financial institutions as a source of finance

To determine the degree of influence of financial institutions as a source of funding, the researchers looked at 10 different factors. The fitness is displayed in the following table based on the 10 variables that were used to determine it. Table 11 below displays the mean and standard deviation of the financial institutions' influence as a source of funding.

Table 11: The level of impact of Financial institutions as a source of finance

The level of impact of financial institutions as a source of finance	Medium	Low	High	Total
Number of respondents	97	113	37	247
Percentage	39.27	45.75	14.98	100

Source: Computed data

Table 11 shows the level of impact of Financial institutions as a source of finance for the respondents. One hundred and thirteen (45.75%) of the respondents said the level of impact of financial institutions as a source of finance is low. Ninety-seven (39.27%) respondents said the level of impact of financial institutions as a source of finance is medium, and the remaining thirty-seven (14.98%) respondents said the level of impact of financial institutions as a source of finance is high. Majority (45.75%) of the respondents said the level of impact of financial institutions as a source of finance is low.

3.2 The level of impact on opinions about financial institutions' lending norms

The researcher has taken the dimension, The level of impact on opinions about financial institutions' lending norms, has seven variables, i.e. (i)have experienced many difficulties to provide collateral, (ii) have been experienced difficulty to provide documents, (iii) have been experiencing difficulty to prepare a business plan, (iv) have experienced difficulty to bare accruing cost, (v) Interest rate is reasonable, (vi) Delay in the processing of application and (vii) Inadequacy of quantum of loan amount. The expected score for good fitness was presented in the table, and the calculated values are also presented in the following table.

Table 12: SEM - Model Fit Summary – The level of impact on opinions about financial institutions' lending norms

Test Factor	TLI (Tucker-Lewis index)	NFI (Normed fit index)	GFI (Goodness-of-fit index)	RMSEA (Root mean square error of approximation)	Chi-Square	CFI (Comparative fit index)	AGFI (Adjusted goodness-of-fit index)
Value	0.927	0.959	0.968	0.038	47.473	0.972	0.974
Range	>0.90	>0.95	>0.95	<0.06	p>0.05	>0.95	>0.95
Result	Good Fit	Good Fit	Good Fit	Good Fit	1% level	Good Fit	Good Fit

Source: Computed data

The above table shows that the values are above the minimum requirement range. This dimension has eleven variables, the output of the SEM presented in the above table. The values of chi-square, GFI, AGFI, CFI, NFI, TLI, and RMSEA are above the required range. The analysis concluded that all the variables are fit; all eleven variables may be taken for further studies.

3.3 The level of impact on opinions about financial institutions' lending norms

Table 13 shows the level of impact on opinions about financial institutions' lending norms of the respondents. Ninety-one (36.84%) of the respondents said the level of impact on opinions about financial institutions' lending norms is low. One hundred and sixteen (46.96%) respondents said the level of impact on opinions about financial institutions' lending norms is medium, and forty (16.19%) respondents said the level of impact on opinions about financial institutions' lending norms is high. Majority (46.96%) of the respondents said the level of impact on opinions about financial institutions' lending norms is low.

Table 13: Impact on opinion about financial institutions' lending norms

Impact on opinion about financial institutions' lending norms	Number of respondents	Percentage
High	40	16.19
Low	91	36.84
Medium	116	46.96
Total	247	100

Source: Computed data

3.4 The level of impact on the accessibility of Financial Institutions

The researcher has taken the dimension "the level of impact on the accessibility of financial institutions", there are five variables, i.e. (i) awareness about financing institutions, (ii) awareness about schemes of financing, (iii) awareness about lending procedures and financial institution terms and conditions of lending, (iv) accessibility of Financial services offered by the Financial institutions and (v) accessibility of Person in-charge of financial institutions. The expected score for good fitness was presented in the table, and the calculated values are also presented in the following table.
Table 14 shows that the values are above the minimum requirement range. This dimension has eleven variables, the output of the SEM presented in the above table. The values of chi-square, GFI, AGFI, CFI, NFI, TLI, and RMSEA are above the required range. The analysis concluded that all the variables are fit; all eleven variables may be taken for further studies.

Table 14: SEM - Model Fit Summary – The level of impact on the accessibility of Financial Institutions

Test Factor	AGFI (Adjusted goodness-of-fit index)	CFI (Comparative fit index)	Chi-Square	GFI (Goodness-of-fit index)	NFI (Normed fit index)	RMSEA (Root mean square error of approximation)	TLI (Tucker-Lewis index)
Value	0.9762	0.958	50.818	0.977	0.963	0.039	0.912
Range	>0.95	>0.95	p>0.05	>0.95	>0.95	<0.06	>0.90
Result	Good Fit	Good Fit	1% level	Good Fit	Good Fit	Good Fit	Good Fit

Source: Computed data

3.5 The level of impact on the accessibility of Financial Institutions

The above table shows the level of impact on the accessibility of Financial Institutions of the respondents. One hundred and twenty-three (49.80%) of the respondents said the level of impact on the accessibility of Financial Institutions is low. Eighty-nine (36.03%) respondents said the level of impact on the accessibility of Financial Institutions is medium, and the remaining thirty-five (14.17%) respondents said the level of impact on the accessibility of Financial Institutions is high. Majority (49.80%) of the respondents said the level of impact on the accessibility of Financial Institutions is low.

Table 15 : The level of impact on the accessibility of Financial Institutions

The level of impact on the accessibility of Financial Institutions	Number of respondents	Percentage
High	35	14.17
Low	123	49.80
Medium	89	36.03
Total	247	100

Source : Computed data

4. The level of Impact of financial support from financial institutions

The researcher has taken the dimension, there are five variables, i.e. (i) Financial institutions assist to Small and medium enterprise to fulfil start-up finance requirements, (ii) Financial support to fulfil working capital requirements, (iii) Financial institutions assistance to fulfil long term finance requirements, (iv) Financial institutions assist to fulfil modernization and expansion finance requirements, (v) Support to overcome business difficulties, (vi) Formal sources of finance in stimulating the firms growth and (vii) Apprise the formal sources of finance in stimulating the operational efficiency.
The following table presents the GFI (Goodness-of-fit index), AGFI (Adjusted goodness-of-fit index), CFI (Comparative fit index), NFI (Normed fit index), TLI (Tucker-Lewis index), and RMSEA (Root mean square error of approximation). The expected score for good fitness was presented in the table, and the calculated values are also presented in the following table.

Table 16: SEM - Model Fit Summary –The level of Impact of financial support from financial institutions

Test Factor	AGFI (Adjusted goodness-of-fit index)	CFI (Comparative fit index)	Chi-Square	GFI (Goodness-of-fit index)	NFI (Normed fit index)	RMSEA (Root mean square error of approximation)	TLI (Tucker-Lewis index)
Value	0.991	0.968	49.904	0.961	0.972	0.041	0.933
Range	>0.95	>0.95	p>0.05	>0.95	>0.95	<0.06	>0.90
Result	Good Fit	Good Fit	1% level	Good Fit	Good Fit	Good Fit	Good Fit

Source: Computed data

The above table shows that the values are above the minimum requirement range. This dimension has eleven variables, the output of the SEM presented in the above table. The values of chi-square, GFI, AGFI, CFI, NFI, TLI, and RMSEA are above the required range. The analysis concluded that all the variables are fit, all eleven variables may be taken for further studies.

4.1 The level of impact of Financial Support from Financial Institutions

The researchers have taken seven variables to find the level of impact on the accessibility of financial institutions. The five variables taken to find the fitness, the above table shows the fitness. The following table shows the level of impact on accessibility of financial institutions.

Table 17: Accessibility of Financial Institutions

Sl. No.	Accessibility of Financial Institutions	Number of respondents	Percentage
1	Low	123	49.80
2	Medium	89	36.03
3	High	35	14.17
	Total	247	100

Source: Computed data

The above table shows the Level of Accessibility of Financial Institutions of the respondents. One hundred and twenty-three (49.80%) of the respondents said the Accessibility of Financial Institutions is low. Eighty-nine (36.03%) respondents said the Accessibility of Financial Institutions is medium, and the remaining thirty-five (14.17%) respondents said the Accessibility of Financial Institutions is high. The majority (49.80%) of the respondents said the Accessibility of Financial Institutions is low.

Pearson's correlation coefficient

D1- The level of impact of Financial institutions as a source of finance

D2-The level of impact on opinions about financial institutions' lending norms

D3-The level of impact on the accessibility of Financial Institutions

D4-The level of Impact of financial support from financial institutions

D5-Impact in Small and Medium Enterprises

Table 18: Pearson's correlation coefficient

		D1	D2	D3	D4	D5
D1	Pearson Correlation	1				
	Sig. (2-tailed)					
	N	247				
D2	Pearson Correlation	.410*	1			
	Sig. (2-tailed)	.009				
	N	247	247			
D3	Pearson Correlation	.784	.059	1		
	Sig. (2-tailed)	.001	.185			
	N	247	247	247		
D4	Pearson Correlation	.511	-.384	-.140	1	
	Sig. (2-tailed)	.001	.000	.002		
	N	247	247	247	247	
D5	Pearson Correlation	.419*	.514	.526	-.007	1
	Sig. (2-tailed)	.017	.012	.005	.873	
	N	247	247	247	247	247

*. Correlation is significant at the 0.05 level (2-tailed)

. Correlation is significant at the 0.01 level (2-tailed)

The above table shows the relationship between the various dimensions that impact the small and medium-scale enterprise development in South India. The four dimensions taken to find the impact on Small and Medium Enterprises. The correlation tools are used to find the relationship.

The level of impact of financial institutions as a source of finance (0.419) has a positive and significant relationship with the performance of small and medium enterprises at 5% significance level.

The level of impact on opinions about financial institutions' lending norms (0.514) and the level of impact on the accessibility of financial institutions (0.526) have a positive and significant relationship with the performance of small and medium enterprises at 5% significance level.

5. Findings

The researcher presented findings from percentage analysis, structural equation model, and correlation.

5.1 Structural Equation Model

The researcher had taken four dimensions to find the variables which to find the level of impact of financial institutions on the small and medium enterprise development.

1. The level of impact of Financial institutions as a source of finance – the researcher took eleven variables to find the fitness. The analysis concluded that all the variables are fit; all eleven variables may be taken for further studies.
2. The level of impact on opinions about financial institutions' lending norms – the researcher took seven variables to find the fitness. The analysis concluded that all the variables are fit; all eleven variables may be taken for further studies.
3. The level of impact on the accessibility of Financial Institutions – the researcher took eleven variables to find the fitness. The analysis concluded that all the variables are fit; all eleven variables may be taken for further studies.
4. The level of Impact of financial support from financial institutions - the researcher took five variables to find the fitness. The analysis concluded that all the variables are fit; all eleven variables may be taken for further studies.

5.2 Pearson's correlation coefficient

The level of impact of financial institutions as a source of finance (0.419) has a positive and significant relationship with the performance of small and medium enterprises at 5% significance level.

The level of impact on opinions about financial institutions' lending norms (0.514) and the level of impact on the accessibility of financial institutions (0.526) have a positive and significant relationship with the performance of small and medium enterprises at 5% significance level.

5.3 Suggestions

The following points can be given as suggestions for the financial institutions in supporting the SMEs for the development of individuals and the nation. The points mentioned could be considered for further development and growth are discussed below:

1. Flexible Terms and Conditions:

The financial institutions should offer more flexible terms in providing loans and lower interest rates for Small and Medium Entrepreneurs to overcome the financial barriers in start-ups in South India.

2. Altering the Financial Products:
Financial institutions should be able to alter their financial products, such as microloans and working capital loans, to meet the special needs of small and medium enterprises in different sectors.

3. Government Association:

The government should join hands with the financial institutions to make more efficient access to subsidies, grants, and schemes aimed at SME growth in South India.

4. Financial Literacy Programs and Campaigns:

Financial education programs have to be made more powerful to allow entrepreneurs to have the knowledge to manage their finances well and understand available funding options in the market.

5. Venture Capital:

The financial institutions must be encouraged to provide venture capital for the SMEs with innovative ideas and those who are in need of start-ups with the need for capital to start their operations.

6. Access to Digital Financing:

SMEs should be encouraged to adopt the digital platforms for application of loans, payments, and receiving funds, financial management, and making financial services easily available and accessible to SMEs in remote areas.

7. Mitigation of Credit Risk Tools:

The development of alternative credit scoring models would help financial institutions measure the capability of SMEs with limited credit history, and would help improve the chances of the SMEs in securing loans.

8. Skill Development Programs:

Financial institutions can mentor, provide workshops, and skill-development programs to the SMEs, which would help SMEs in the betterment in managing finances better, plan for growth and development in various environments.

9. Funding Specific Sectors:

Specific sectors such as agriculture, manufacturing, and technological aspects should be concentrated more by the financial institutions to meet the distinct needs of industries in South India.

10. Pre and post loan monitoring and Support:

The financial institutions should support the SMEs in acquiring new loans and monitor post-loan payments and services to ensure achieving long-term sustainability and growth of the organisations.

6. Policy Review and Regulatory Gaps:

Although financial institutions offer several support mechanisms for SMEs, a more in-depth assessment of existing policies, such as the Reserve Bank of India's Priority Sector Lending (PSL) guidelines, is warranted. While PSL mandates banks to allocate a portion of their credit to sectors including SMEs, the actual disbursal process is often hindered by procedural delays, stringent documentation norms, and a lack of tailored financial products. Many SMEs, especially first-generation entrepreneurs or those in informal sectors, struggle to meet the eligibility criteria despite being covered under PSL. This suggests a disconnect between policy design and ground-level execution. Moreover, while PSL aims to reduce credit rationing, the implementation has not fully addressed the information asymmetry and risk aversion among lenders. Therefore, the study recommends that financial institutions collaborate with regulatory bodies to bridge these gaps by simplifying access to PSL credit, increasing transparency, and designing monitoring frameworks that ensure equitable distribution of loans across regions and genders.

7. Conclusion

The findings of this study underscore the pivotal role of financial institutions in shaping the entrepreneurial landscape and fostering the growth of small and medium-sized enterprises (SMEs) in South India. While tailored financial products such as venture capital, microloans,

and working capital loans contribute significantly to SME development, systemic barriers—including rigid lending norms, low financial literacy, and limited outreach—persist and disproportionately affect first-time and rural entrepreneurs. These findings complement the insights of Chakraborty and Jain (2020), who emphasized the role of both banks and non-banking financial institutions (NBFIs) in providing nuanced financial support. However, this study extends their work by offering empirical evidence from a regional context and highlighting how procedural inefficiencies and institutional inaccessibility still hamper financial inclusion at the grassroots level. Importantly, the analysis reveals that enhanced financial access not only strengthens individual business performance but also contributes to broader macroeconomic outcomes such as employment generation, regional industrialization, and GDP growth. By facilitating SME expansion, financial institutions contribute directly to Sustainable Development Goal 8, which advocates for inclusive economic growth and decent work opportunities.

Moreover, the study reveals that regional policy interventions should account for state-level variations in institutional reach, digital infrastructure, and socioeconomic conditions. Tailored policy responses that address these contextual disparities can help reduce inter-state economic imbalances and support equitable national growth. Future policy frameworks should therefore promote dynamic collaborations between state governments, financial institutions, and development agencies to ensure region-specific strategies. In terms of practical and theoretical implications, this research recommends expanding financial literacy programs, integrating digital financing platforms, and redesigning credit scoring models to account for informal sector realities. Furthermore, the study recommends longitudinal research designs in future studies to evaluate the long-term effectiveness of financial interventions on SME performance, sustainability, and resilience across economic cycles. An adaptive, inclusive, and transparent financial ecosystem—supported by robust policy and institutional commitment—is essential for catalyzing entrepreneurship and driving South India's socio-economic transformation.

From an accounting perspective, the findings reveal that access to formal finance plays a critical role in shaping SME financial management practices, particularly in financial reporting, budgeting, and loan documentation. The study suggests that limited access to credit often correlates with poor record-keeping and informal accounting methods, which in turn affect SMEs' eligibility for institutional credit. This has implications for accounting standard adoption, tax compliance, and internal audit systems among SMEs. This study underscores the need for capacity-building in financial documentation, which could bridge the gap between SMEs and formal financial institutions, fostering greater transparency and accountability in financial reporting.

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