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THE IMPACT OF SUSTAINABLE FINANCE ON SMALL AND MEDIUM-SIZED ENTERPRISES (SMES): A COMPREHENSIVE STUDY

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Abstract

In recent years, the global business landscape has witnessed a paradigm shift towards sustainability and responsible business practices where Small and Medium-sized Enterprises (SMEs) are increasingly under scrutiny to align their financial practices with sustainable development goals. This research paper investigates the profound impact of sustainable finance on Small and Medium- sized Enterprises (SMEs). SMEs play a pivotal role in economies worldwide, and their ability to integrate sustainability into their financial strategies is of paramount importance. This study employs a mixed-methods approach, combining quantitative financial analysis with qualitative insights from SMEs, financial institutions, investors, and policymakers. The primary objective of this research is to create awareness and examine how sustainable finance practices influence the financial performance, risk management, and environmental and social outcomes of SMEs. It also investigates the accessibility and the impact of sustainable finance on SMEs and the regulatory environment shaping their adoption. Furthermore, the study explores the perception and the relationship between sustainable finance practices and SMEs embracing sustainability by their stakeholders and analyzes the factors that contribute to their success or present obstacles. The implications of this research extend to multiple stakeholders, including SME owners and managers seeking to balance profitability with sustainability, financial institutions seeking to offer tailored sustainable finance solutions, and policymakers aiming to promote sustainable practices in the SME sector. As sustainable finance gains momentum in the global financial landscape, this study contributes valuable insights into the intricate relationship between sustainable finance and SMEs, ultimately guiding efforts to drive economic growth, environmental responsibility, and social well- being in tandem.

Keywords: *Sustainable Finance, Small and Medium-sized Enterprises (SMEs), Financial Performance, Environmental Impact, Social Impact, Regulatory Environment.*

Introduction:

In our Indian Economy Small and Medium Enterprises have always been playing a significant rather vital role as they contribute minimum 40% to exports and at least 45% to Industrial production, with a small contribution to GDP approximately 12% by simultaneously providing employment to about 42 Million skilled and unskilled workers across our economy which represents nearly 26 million entreprises.This SME sector is more likely to create and generate one million jobs every year and also meanwhile shall play a very vital role in progressing

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the demographic dividends. The real unsung heroes of India are the millions of mom and pop enterprises, which are silently making goods and providing services at competitive rates, creating additional jobs for millions of skilled and unskilled workers and facing the challenges of globalization. The reason being the SME sector has always demonstrated true Indian entrepreneurship with some of the biggest names in India having their roots in the sector.

The meaning of sustainable means financing both areas where one is what is already environment-friendly today and the other area is what is transitioning to environment-friendly performance levels over time (transition finance). Transition finance refers to financing the private investments in order to reduce today's high greenhouse gas emissions or also other environmental impacts or side effects and transition to a climate neutral and a better sustainable economy. For example, these could be investments in green production methods or on the other hand reducing the environmental footprint as far as possible, where no green technologies are yet available. Transition finance on the other hand is urgently needed to reduce greenhouse gas emissions by 55% and our environmental impact by 2030. Rather it's often been needed or required by companies that want to become sustainable in the near future, but need to do so in steps over time - in other words, companies with different starting points that want to finance their journey towards a sustainable future. In order to boost investments into sustainability, every small and medium enterprises (SMEs) –shall play a crucial part of an economy. In the current scenario the sustainable finance framework focuses on capital markets. But the fact is SMEs normally get external finance from banks, and also assistance from bank-based financial systems work differently than market-based financial systems. Therefore, there need to be proper regulations to take the characteristics and advantages of bank-financed SMEs into account. Decentralization with individual financing of credible transition plans, rather than extensive disclosure of data, could lead to the necessary rise of investments. There is a high need to adapt to the changes being brought into due to the above. Revised Classification applicable w.e.f 1st July 2020

Classes and types of Micros, Small and Medium Enterprise (MSME) sector			
Composition Criteria Allocation of investment in assets like Plant & Machinery/equipment and Average / Annual Turnover			
Classification	Micro	Small	Medium
Manufacturing and Service Sector Enterprises	Allocation of investments in assets like Plant and Machinery or Equipment upto Rs.1 crore and Annual Turnover does not exceed Rs. 5 crore	Allocation of investments in assets like Plant and Machinery or Equipment upto Rs.10 crore and Annual Turnover does not exceed Rs. 50 crore	Allocation of Investment in assets like Plant and Machinery or Equipment upto Rs.50 crore and Annual Turnover does not exceed Rs. 250 crore

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The Ministry of Micro, Small & Medium Enterprises considers the MSME sector to contribute to the excellent growth potential and also play a pivotal role in India's overall economic development, in this SME Finance plays a crucial part. As we are aware that SMEs are just capable of generating incomes, assets, and enhance employment opportunities for its owners or employees but all things are done at a very small scale. Every country has defined SMEs in its different manner and also has introduced its owns rules and regulations about what constitutes an SME. On the other hand the overall size is usually considered to be the best indicator to assess which part of a sector a company belongs to. The most important market function is the financing of small and mediumsized enterprises. It can be referred to as a way capital can be provided, acquired, or cost for different types of companies made available on the market.The ever increasing number of small and medium enterprises in India reflects a highly valued and better rated dividend. As defined by Section 7 of the Micro, Small and Medium Enterprises Development Act, 2006.

Classification of Msmes in India:

Type of enterprise	Investment	Turnover
Micro	Rs 1 crore	Rs 5 crore
Small	Rs 10 crore	Rs 50 crore
Medium	Rs 50 crore	Rs 250 crore

The above criteria makes it very difficult for all the small and medium enterprises (SMEs) to make available the access credit from banks, especially in the earlier years.

Keeping in mind their flexibility, the SMEs can take many different forms. There can be different varieties such as proprietorships, corporations, cooperatives, and HUFs (Hindu Undivided Families). One of the very important elements of these provisions in our economy is that the enterprises are not classified as small or medium size based on factors like no or employees , space used and many other things.

The Present Scenario of the SME Sector in India:

India's Small and Medium Enterprises contribute nearly half of India's artificial affair, 40 of the country's import and produce one million jobs annually. In addition, these enterprises produce over 8,000 quality products that are exported to overseas requests. Small and Medium Enterprises (SMEs) have grown to over 48 million in recent times, with a4.5 growth rate. On the other hand, raising finances for similar businesses can be veritably delicate due to limited coffers available to small companies. As a result, the government continues to ignore the significance of this sector in boosting GDP, though it provides an motivation for overall profitable growth.

Despite a cut- throat competition from the United States and China, India's frugality is anticipated to cross the border of those of Italy and Brazil within 15 times and be more prominent than Russia's by 2050.

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The SME sector is essential to achieving lesser import numbers in India. Out of total exports from the country(43), 43 come from small and medium- sized businesses, further than eight times that contributed by large companies.

Importance of SMES in India:

Some authors have argued that SMEs play an essential part in a nation's profitable development due to their inflexibility in the face of profitable query and technological change. Producing goods and services in a way that employs further people than larger enterprises, therefore creating fresh jobs and helping to spread income more unevenly. SMEs produce further openings for employment and business in an agrarian frugality than any other enterprise by furnishing a range of simple to complex services. Support entrepreneurship Small and medium- sized enterprises (SMEs) contribute to entrepreneurial development. SMEs can work the strengths of large and small enterprises to produce a productive capacity that contributes to strong profitable systems. Sustainable finance involves making investment opinions that consider not only fiscal returns but also environmental, social and governance factors. Also appertained to as "green finance" it's a broad term with multiple delineations depending on environment. Sustainable Finance is investment planning that integrates environmental, social, and governance (ESG) factors. Up until now, businesses were profit- driven and the focus of their attention was their shareholders. But now the precedence's have changed. While taking backing opinions the finance director keeps in mind the following factors. The cost of raising finance from colorful sources is different and finance directors always prefer the source with minimal cost. threat.

- Cash Flow Position.
- Control Considerations
- Advanced hand development and retention
- Stronger stakeholder connections.
- Bettered effectiveness and Cost savings across the business as a whole.
- Advanced character.
- More access to, and retention of, staff.

Literature Review:

Alex Nicholls - The market for sustainable finance is growing globally. Sustainable finance can be deployed as negative/exclusionary investments that aim to "do no harm" or positive/integrated investments that can be deployed to create additional social or environmental impact typically aligned with the SDGs. Most importantly, the regulatory and disclosure infrastructure remains incomplete and inconsistent across countries. As a result, robust and comparable impact performance data, which is necessary for the effective allocation of sustainable finance, is absent. In this context, local, national, regional, and transnational governance bodies have an opportunity to use policy to correct the market failures in the current sustainable finance market. The need for further dramatic growth in the supply of sustainable finance, already evidenced by the shortfall in SDG funding, has been further amplified in the post-COVID19 world and the acceleration of the climate crisis. To achieve this, investors, investors, intermediaries, and policy makers will need to find ways to work effectively together with an increased sense of urgency.

Satish Kumar, Dipasha Sharma,Sandeep Rao,Weng Marc Lim & Sachin Kumar Mangla(Nov 2021)- This study follows a literature review approach using analysis to exfoliate light on the performance and wisdom of sustainable finance exploration. This approach, which exemplifies the use of big data analytics through machine literacy of scholarly exploration, is especially noteworthy given the astonishing absence of the operation and discussion of new- age technologies in sustainable finance exploration. In doing so, this study contributes in a new way by using on the power of big data analytics through machine literacy — and furnishing lesser visibility to it in the process — to uncover the most influential papers and top contributing journals, authors, institutions, and countries, as well as the methodological choices and exploration surrounds, and by revealing the temporal elaboration of motifs and the major themes bolstering the intellectual structure for sustainable finance exploration.

Bharati1 , Dr. Govind Patra(2022)-The study's findings indicated that the regulatory standards for the environment are sufficiently complex and that the regulatory regime is not helpful. Clear government regulations on green financing for small businesses are lacking. The cost of adopting the green financing initiative is quite high, and there are additional costs for certification and due diligence. This places a financial strain on SMEs owing to the environmental burden. Adoption of the green finance project required qualified workers, but skilled labor was more expensive for these SMEs since it costs more to train and skill people. Regulative policies, proper support and encouragement to achieve its full potential is important for the expansion of any business. Therefore, policymakers ought to offer the incentive support to make the path to achieve green finance initiatives by SMEs for their long term sustainability and for the overall benefit of the economy.

KD Raju- Small industry in India has found itself in an intensely competitive environment since 1991, thanks to globalization, domestic economic liberalization and dilution of sector- specific protective measures. The international and national policy changes have thrown open new opportunities and markets for the Indian small industry. Concerted effort is needed from the government and small industry to imbibe technological dynamism.Financial infrastructure needs to be broadened and adequate inflow of credit to the sector be ensured taking into consideration the growing investment demand, including the requirements of technological transformation. Small industry should be allowed to come up only in designated industrial areas for better monitoring and periodic surveys. A technologically vibrant, internationally competitive small and medium industry should be encouraged to emerge, to make a sustainable contribution to national income, employment and exports. It is essential to take care of the sector to enable it to take care of the Indian economy.

Objectives of the Study:

1. To create an awareness on sustainable finance.
2. To Study the impact of sustainable finance on SMEs
3. To investigate the relationship between sustainable finance practices and SMEs
4. To understand the regulatory and policy environment impacting sustainable finance for SMEs.

Scope of study:

The Researcher focuses majorly on sustainable finance on SMEs and can encompass various aspects where it investigates different sustainable finance practices, such as green loans, sustainable bonds, impact investing, or ESG integration, and their impact on SMEs. Small and medium-sized businesses (SMEs), an important segment of the economy, must play a share in boosting investments in sustainability. Capital markets are the focus of the present framework for sustainable finance. Bank-based financial systems operate differently from market-based financial systems, yet SMEs typically obtain external financing from banks. Therefore, the advantages and features of SMEs with bank financing must be considered in the regulation. Instead of comprehensive data disclosure, decentralized and individual financing of realistic transition plans could spur the necessary increase in investments.

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Methodology:

Sources of data collection: Our research is based on purely secondary research .

Secondary data:

It majorly consists of the information collected from various sources like books, websites, journals etc.

Significance of Sustainable Finance on small and Medium- sized Enterprises (SMEs) :

Sustainable finance has significant implications for small and medium-sized enterprises (SMEs) for several reasons. SMEs play a crucial role in economic development and employment generation in many countries, and integrating sustainability into their financial practices can have far-reaching benefits.

Access to Capital: Embracing sustainable finance practices can help SMEs access a broader range of capital sources.This expanded pool of funding can be particularly important for SMEs looking to grow and expand their operations.

Competitive Advantage: SMEs that incorporate sustainability into their business models can gain a competitive advantage in the market. Consumers, especially younger generations, are increasingly conscious of sustainability issues and are more likely to support businesses that align with their values.

Regulatory Compliance: As governments worldwide introduce stricter regulations and reporting requirements related to ESG factors, SMEs need to adapt to remain compliant. Sustainable finance practices can help SMEs navigate these evolving regulatory landscapes more effectively, reducing the risk of fines or penalties for non-compliance.

Innovation and Efficiency:

Long-Term Resilience: Sustainability is about thinking long-term. By integrating sustainable finance principles, SMEs can build a foundation for long-term resilience and adaptability in an evolving business landscape characterized by climate change, shifting consumer preferences, and changing regulations.

Access to International Markets: Many international markets require compliance with sustainability standards and certifications.

Applications of Sustainable Finance on small and Medium- sized Enterprises (SMEs) :

Sustainable finance, also known as responsible or green finance, plays a crucial role in promoting environmental and social sustainability within the business world. When applied to small and medium-sized enterprises (SMEs), it can have several positive impacts:

Access to Capital: SMEs often struggle to access financing due to their size and risk profile. Sustainable finance options, such as green bonds or impact investments, can provide SMEs with alternative sources of capital, helping them grow and develop in a sustainable manner.

Reduced Operational Costs: Sustainable finance can be used to fund projects that improve energy efficiency, reduce waste, or promote sustainable supply chain practices. This can lead to lower operational costs, making SMEs more competitive in the long run.

Market Differentiation: Adopting sustainable finance principles and practices can set SMEs apart from competitors. Many consumers and investors today prefer to support businesses that prioritize environmental and social responsibility, potentially leading to increased market share and customer loyalty.

Risk Management: Integrating sustainability into financial strategies can help SMEs identify and mitigate risks related to environmental, social, and governance (ESG) factors. This can prevent costly legal issues, reputation damage, and operational disruptions.

Access to New Markets: Sustainable finance can enable SMEs to enter new markets that have sustainability criteria

or regulations in place. For example, exporting green products or services can open doors to countries with strict environmental standards.

Innovation and R&D: Funding from sustainable finance sources can support SMEs in developing innovative, environmentally friendly products and services. This can lead to patentable technologies and a competitive advantage.

Supplier Engagement: SMEs can use sustainable finance to encourage their suppliers to adopt more sustainable practices. This not only benefits the SME but also contributes to a more sustainable supply chain ecosystem.

Stakeholder Engagement: Engaging with stakeholders, including employees, customers, and investors, on sustainability initiatives funded by sustainable finance can foster a sense of pride and purpose among SME employees and attract socially responsible investors.

Compliance with Regulations: As governments worldwide introduce stricter regulations related to sustainability, SMEs can use sustainable finance to ensure compliance and avoid fines or legal issues.

Long-Term Viability: Sustainable finance encourages SMEs to think about their long-term viability by considering the environmental and social impacts of their operations. This can lead to more resilient businesses in the face of global challenges.

Impact of sustainable finance on SMEs

By controlling emissions, encouraging the development of renewable energy sources, and supporting sustainable development towards ESG—Environmental, Social, and Governance— Sustainable Finance is one financial tool used to combat climate change and its effects. Three key components make up the connected effort to create a future for people and the world that is inclusive, sustainable, and resilient. Economic expansion, social inclusion, and environmental preservation are the core elements. The impact of sustainable finance on Small and Medium-sized Enterprises (SMEs) can be profound and multifaceted. Sustainable finance practices can influence various aspects of SMEs' operations and financial performance.

Small and medium-sized industries can have access to more sources of cash because of sustainable finance solutions which include green loans and sustainable bonds. This might assist them in funding initiatives, boosting operations, or investing in sustainability programmes that would have been financially difficult in the past. Studies have indicated that SMEs who adopt sustainable finance practices typically perform more favorably financially. They might see enhanced cash flow management, decreased operational costs, and increased profitability due to which sustainable enterprises are frequently viewed as less risky and more desirable by lenders and investors hence it improves the financial performance.

Sustainable financing encourages SMEs to take social and environmental risks into account when developing their business plans. The possibility for expensive disruptions and liabilities can be decreased for SMEs by addressing these risks, improving their long-term financial stability due to which risk can be reduced. SMEs can obtain a competitive edge in the market by embracing sustainability. Customers and investors increasingly favor companies that show a dedication to social and environmental responsibility. Sustainable business practices can help SMEs draw in more clients and investors. It gives access to new markets where Environmental activities may provide access to fresh clientele and market niches. For instance, goods or services with eco- friendly certifications may appeal to customers who care about the environment or to companies looking for sustainable suppliers.

Sustainable financial services frequently complies with laws relating to social and environmental responsibility. SMEs may assure compliance with changing legislation by using these practices, avoiding potential fines and legal troubles. Healthy financial practices and ethical company conduct can improve SMEs' good name and brand recognition. A favorable public image can result in more devoted and trustworthy customers. Sustainable development frequently serves as a catalyst for both innovation and process efficiency. Sustainability initiatives may inspire SMEs to develop new goods, services, or operational enhancements that lower expenses and boost earnings.

Engagement of Employees: SMEs that prioritize sustainability may do a better job of attracting and retaining talent. Strong environmental and social values are frequently preferred by employees, which engages the employees and increases productivity and lowers turnover. Green finance practices enable SMEs to see their firm from a long-term perspective. This may result in more adaptable tactics that take into account the changing social, economic, and environmental conditions. Investors that are looking for companies that produce both financial returns and beneficial social or environmental effects may be drawn to sustainable SMEs. Small and medium- sized enterprises (SMEs) who participate in sustainable finance are frequently better positioned to support the accomplishment of the Sustainable Development Goals of the United Nations, further strengthening their social and environmental impact.

It's important to note that the impact of sustainable finance on SMEs may vary depending on factors such as the industry, location, and the specific sustainability practices adopted. However, as the global focus on sustainability continues to grow, SMEs are increasingly recognizing the benefits of integrating sustainable finance into their business strategies.

Relationship between sustainable finance practices and SME:

Sustainable finance is a process of the integration of different environmental, social, and governance (ESG) criterias into the financial decision-making processes. SMEs, on the other hand, represent a significant portion of the global economy and often face unique challenges and opportunities when it comes to sustainability.

Regulatory and policy environment impacting sustainable finance for SMEs

ESG Disclosure Requirements - ESG disclosure should be transparent about a company's efforts (or lack thereof) to transition to a net-zero economy. Disclosure also compel management teams to take responsibility for operations that have negative effects on the environment, social issues, or both. Many nations have passed laws requiring businesses, especially SMEs, to declare their ESG performance, or they are considering doing so. Investors and others can evaluate a company's sustainability practises using these disclosures.

Green Bond and Green Loan Frameworks: The Green Finance Framework (the "Framework") has been established by REC as part of its sustainable financing initiative. It serves as the foundation for the issuance of green bonds, loans, and other financial instruments (collectively, "Green Financing Instruments") that are used to finance and/or refinance Eligible Green Projects that adhere to the green finance principles outlined below.

The goal of this Framework is to establish a uniform process for all future green financing instruments, guaranteeing that the objectives of this Framework are adhered to for each instrument issued and that the proceeds are invested in renewable energy and energy efficiency. Guidelines for green bonds and green loans, which are financial instruments intended to finance sustainable initiatives, may be established by governments and regulatory authorities. These frameworks facilitate SMEs' access to funding for environmental projects.

Tax Incentives and Subsidies: In order to motivate SMEs adopting sustainable practices or make investments in environmentally friendly technologies, several governments offer tax breaks, grants, or

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subsidies. These incentives may increase the appeal of SMEs using sustainable business methods. Governments provide grants or cash payments to businesses as a means of fostering economic growth. Tax incentives are always intended to lower a company's overall tax burden and boost profitability. They can take a number of shapes: -Tax exemptions completely exempt

businesses from fulfilling certain obligations.

Tax reductions may offset some of the taxes that a company must pay.

- Taxes paid in advance are partially repaid through tax refunds and rebates.
- Tax credits are more flexible since they may frequently be carried forward to upcoming tax years or sold on the secondary market, allowing a business to offset a portion of its tax liability.

ESG Reporting Standards: ESG reporting focuses on revealing data about a company's operations and risks in three categories: corporate governance, social responsibility, and environmental stewardship. Consumers use ESG reports to determine whether their purchases are supporting a business that shares their values.

Environmental and Social Impact Assessment: Projects having potentially significant environmental and social implications are given an environmental (and social) impact assessment (EIA). Before the Bank conducts its Analysis Mission, the Borrower makes EIAs available to the affected residents and local nonprofit organizations.

Green Procurement: The term "green procurement" describes the practice of buying products and services that have little or no negative environmental impact. The adoption of environmentally conscious corporate practices is being driven by the demand for recyclable goods, energy-efficient systems, and clean technology and fuels. In green procurement, an organization is more concerned with the effects of its purchasing choice on the environment than it is with the price of the goods and service.

Findings were as follows:

According to research, the effectiveness of sustainable finance or Climate finance required for MSME and Companies for greener production infrastructure and government of India missions on climate Change, Regular to boost the ESG to promote sustainable development and Economic growth.This study empirically examines the influence of credit to SMEs as a factor of their sustainability and also on banks' risk. If we talk about the credit to this as a significant factor for SME to grow and sustain , the results indicate that enhancing credit to SMEs would decrease the value of non-performing loans in banks. These loans refer to SMEs that can invest in their growth and sustainability. When SMEs are able to access sources of financing and enhance their negotiating ability, they are able to improve their business-development activities and production technologies. On the other hand, SMEs make a significant contribution to the economy, which also supports their growth and sustainability which should be an important component of economic policy. All ESG funds are Sustainable finance are a lucrative opportunity for both investors and corporations and have a positive impact on environmental and Economic growth. It is not seen as consistent in terms of growth; the government has to initiate the policy measures to adopt green or sustainable finance in the ESG global wave. We may also conclude that, the future of sustainable finance involves going at the grass root level with banks of all sectors who are launching new products that might support the sustainability concept in a better manner. On the other hand the Customers at a grassroots level will be given an opportunity to select, or opt out of, products that would offer personalized suggestions regarding different purchases made alongwith their environmental impact. We hope that these features will also encourage all consumers to select more sustainable market alternatives. These purchases will be linked to data collected on individuals irrespective of different judgements and arguments made on the same.

Conclusion:

In conclusion, sustainable finance is not just a trend but a fundamental shift in the business landscape. SMEs that embrace sustainability can reap various benefits, including improved access to capital, competitive advantages, risk mitigation, regulatory compliance, innovation, and enhanced reputation. By integrating sustainability into their financial strategies, SMEs can position themselves for long-term success and contribute positively to society and the environment.More foreign direct investment to be encouraged in waste management, Ecotourism, renewable energy, organic agriculture and development of new-age technology in MSME. Collaboration with global partners plays a vital role in adopting climate change and large companies are shifting to green energy to minimize the negative environmental impact of its activity and regulation to be focused on the green economy.

Scope for Further Research:

The researchers in study have justified that In this context, local, national, regional, and transnational governance bodies have an opportunity to use policy to correct the market failures in the current sustainable finance market. But there is a need for further dramatic growth in the supply of sustainable finance, already evidenced by the shortfall in SDG funding, which has been further amplified in the post-COVID19 world and the acceleration of the climate crisis. Further research can be done To achieve this and also all types of investors, investees, intermediaries, and policy makers will need to find ways to work effectively together with an increased sense of urgency.

Limitations:

The study has been conducted by using only secondary data sources which comprises books, research papers, journals etc. On The findings developed through the study might reveal variations due the different regulatory and policy impacting sustainable finance on SMEs

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