



**MICRO, SMALL AND MEDIUM ENTERPRISES IN INDIA: TRENDS AND CHALLENGES**

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**Abstract**

Despite new policy initiatives for the MSME sector in India a clear agenda and action of development for them have been found wanting. This paper is an attempt to capture the MSMEs scenario in India in terms of the recent trends in production, employment, exports and their contribution to the Indian economy. Besides analysing the critical significance of the MSMEs sector in the context of globalisation, the paper also examines the capacity of this sector to face the challenges imposed by rising competition and necessitated by new initiatives.

**Keywords:** MSME Sector, Production, Globalisation.

**Introduction**

The Micro Small and Medium Enterprises (MSMEs) sector constitutes an important segment of the Indian economy in terms of its contribution to the country’s industrial production, exports, employment and creation of a broad entrepreneurial base. So, it is rightly regarded as the backbone of the modern Indian Economy. With the advent of planned economy from 1951 and the subsequent industrial policy followed by Government of India, both planners and Government earmarked a special role for small-scale industries and medium scale industries in the Indian economy. Their significance has not waned in the wake of LPG and thereafter. They enjoy certain inherent strengths such as lower over-head costs, flexibility in production, informality in labour relations, exploitation of local and latent resources and skills, capacity to execute small orders and to offer customised services. Empirical evidence indicates that small-scale enterprises can be an important vehicle for meeting the growth and equity objectives of developing economies (Ali, Jayasheela & Hans, 2006), and also meet the requirements of hi-tech and environment-friendly global standards.

As per the Micro Small and Medium Enterprises Act, 2006, MSMEs are broadly classified into two categories (a) Manufacturing and; (b) those engaged in supplying services. Both categories of enterprises have been further classified into micro, small and medium and large enterprises based on their investment in plant and machinery for (manufacturing enterprises) or on equipments (in case of enterprises providing/rendering services). According to the MSMEs Act under service enterprises category, micro enterprises is an enterprise where the investment in equipment does not exceed Rs.10 lakh; a small enterprise is one where the investment in equipment is more than Rs.10 lakh but does not exceed Rs.2 crore; a medium enterprise is that where the investment in equipment is more than Rs.2 crore but does not exceed Rs.5 crore. While for enterprises engaged in the manufacture or production, processing or preservation of goods, a micro enterprise is one where investment in plant and machinery does not exceed Rs.25 lakh. Small enterprise is one where investment in plant and machinery can be more than Rs.25 lakh but does not exceed Rs.5 crore. In a medium enterprise, the investment in plant and machinery can be more than Rs.5 crore but does not exceed Rs.10 crore (Annual Report Micro, Small and Medium Enterprises, 2008) Before this Act Government defined only Small-Scale Industries (SSI), and accordingly “SSI is an industrial undertaking in which the investment in fixed assets in plant and machinery whether held in ownership terms or on lease or by hire purchase, does not exceed Rs.100 lakh”.

The MSMEs in view of their employment potential and other intrinsic advantages are found suitable for rural economy and have been promoted on priority. The developed countries have formulated programs for these industries to achieve prosperity. In Japan the growth of small enterprises has provided the base for new society and even today it exhibits industrial excellence, which has astonished the world. The Japanese economy, which was totally destroyed during the War, has regained its strength to an appreciable extent due largely to the efforts of small enterprises and highest labour productivity. Countries in Europe, Asia, Africa and Latin America have formed inspiring and protecting policy framework for promoting small enterprises. Italy, which was once called as the “Sick man of Europe”, has prospered in small industries, which resulted in the rapid growth of the economy and is now called as “Japan of Europe” (Hejamadi, 2000).

More recently, enhancing MSMEs productivity and profitability has been viewed as an effective way of fostering the private sector contribution to the growth and equity objectives of development. MSME play a key role in the industrialisation of a developing country. This is because they provide immediate large scale employment and have a comparatively higher labour-capital ratio; they need a shorter gestation period and relatively smaller markets to be economic; they need lower investments; offer a method of ensuring a more equitable of distribution of income and facilitate a effective mobilisation resources of capital and skill which might



otherwise remain unutilised; and they stimulate the growth of industrial entrepreneurship and promote a more egalitarian pattern of ownership and location.

In the light of these facts, this paper makes an attempt to (a) analyse the performance of MSMEs in India, (b) understand the problems and challenges faced by this sector, and (c) suggest some policy measures.

**Growth and Performance of MSMEs**

While historically, the small-scale industries were related to the small man and his own resources, after Independence there has been a rapid growth of the small enterprises sector due to a number of reasons (Jayasheela and Hans, 2006). Thus, over the years the small enterprises sector registered continuous growth in the number of units, production, employment and exports. According to the Ministry of MSMEs, the number of micro and small enterprises (MSEs) in India rose from 109.49 lakh in 2002-03 to 128.44 lakh in 2006-07 (see Table 1).

**Table – 1Number of Micro and Small Enterprises in India (in lakh)**

Year	No of Units		Total
	Registered	Unregistered	
2017-18	16.3	93.46	109.49(4.1)
2018-19	17.14	96.83	113.95(4.1)
2019-20	18.24	100.35	118.59(4.1)
2020-21	19.30	104.12	123.42(4.1)
2020-21*	20.32	108.12	128.44(4.1)

Source: Economic Survey of India 2007-08 & Office of the Development Commissioner (MSME) \* Estimates based on definitions prior to enactment of MSMED Act, 2006.

Note: Figures in parenthesis indicate percentage growth over previous year.

Medium Enterprises has been defined for the first time under the MSMED Act, 2006. Hence no firm statistics are available with respect to medium enterprises presently. However, informal sources suggest medium enterprises in India, to be between 10000-15000. Further it is estimated that they contribute about 2 per cent of GDP, over 10 percent to manufacturing output and around 10 percent to the national export (Annual Report Ministry of MSME, 2020).

**Employment Generation**

It has already been shown in our analysis that employment growth rate for small enterprises in the recent period are higher than that of the large-scale sector (Debroy; Laveesh, 2017). The employment opportunities provided by the Micro and Small Enterprises sector have a general increasing trend (see Table 2). The annual average growth rate of the employment opportunity provided by the MSMEs sector, in India is impressively at 4.04 per cent. The MSMEs provide employment to an estimated 31.2 million persons in the rural and urban areas of the country which is second only to agriculture in absolute terms. Thus, MSMEs sector in India has also played a vital role in employment generation for a labour-surplus economy.

**Table- 2Employment Generation (lakh persons)**

Year	Employment	Growth over previous years (%)
2017-2018	263.68	4.5
2018-2019	275.30	4.4
2019-2020	287.55	4.5
2020-2021	299.85	4.3
2020-2021*	312.52	4.2

Source: Economic Survey of India 2017-18 & Office of the Development Commissioner (MSME) \*Estimates based on definitions prior to enactment of MSMED Act, 2006.

**Growth Trend of Production**

There has also been a steady growth in the production front of the MSMEs. In the year 2018-19 the increase in the production over the previous year was registered 8.7 per cent at constant prices i.e.,2017-18 prices.



Table- 3Growth of Micro and Small Enterprises’ production

Year	Production (Rs. Crore)#	Growth over previous years (%)
2017-18	306771	8.7
2018-19	336344	9.6
2019-20	372938	10.9
2020-21	418884	12.3
2020-21*	471663	12.6

Source: Economic Survey of India 2007-08 & Office of the Development Commissioner (MSME), \*Estimates based on definitions prior to enactment of MSMED Act, 2006.

Export Performance

In addition to the employment generation, the role of MSMEs sector in the country’s exports is also commendable. Overall MSMEs exports contribute around 45-50 per cent of export basket while direct export account for nearly 35 per cent of total exports. The major MSMEs exports consists of low skilled labour-intensive goods like garments, leather products, gems and jewellery products, sport goods plastic products processed food etc. The exports of MSMEs sector continuously showed increasing trends (see Table 4). Exports from MSMEs Sector was Rs.386013 crore in 2018-19 with 20.7 per cent growth over the previous years, which increased to Rs.150242 crore in 2005-06 with a growth rate of 20.8 per cent growth over the previous years.

The MSMEs sector has thus, acquired a prominent place in the socio-economic development of the country during the past five decades, contributing to the overall growth of the gross domestic product (GDP) towards employment generation and exports. According to new definition the MSMEs contribute nearly 8-9 per cent of Gross Domestic Product of our country (Based on Third All India Census of Micro and Small Enterprises 2018-19, Ministry of MSMEs, 2007). Having emerged as the engine of growth for Indian Industry, the performance of MSMEs sector has had a direct impact on the growth of the national economy. The micro and small enterprises sector, which accounts for 37 per cent of the country’s manufacturing output, can achieve sustained higher growth by enhancing its technological capabilities and improving product and service quality, noted the Economic Survey 2018-19. The sector with a total size of US\$140 billion, contributing over 45 per cent of the country’s industrial production and around 40 per cent of the total exports and employing over 31 million people can source improved manufacturing techniques and management processes with greater ease, said the Survey (CII, 2018; The Hindu Business Line, 2018).

Problems and Challenges

With increasing competition on account of globalisation of the Indian economy, size of the enterprises and the level of technology employed by them have assumed critical significance in the context of the small enterprises becoming globally competitive. Several policy initiatives have been taken during the years to address the problems faced by the sector, which mainly relate to access to timely and adequate credit, technological obsolescence, infrastructure bottlenecks, marketing constraints and a plethora of rule and regulations. Despite numerous policy measures during the past four decades, Indian small-scale units have remained mostly tiny, technologically backward and lacking in competitive strength, vis-à-vis the large units. Following is the some of the reasons for their failure.

Problem of Credit Lack of adequate and timely institutional credit is a frequent complaint of the Micro, Small and Medium Enterprises. The capital base of majority of MSMEs is very weak. Banks insist on collaterals, which the small entrepreneurs, with limited resources, are unable to furnish. Bank officials frequently point out to the high level of Non-Performing Assets and the poor culture of repayments to justify their cautious lending policies. The problem is that there is no trust and understanding between bank officials and industrialists in India. During recession, the bankers often cut back on lending, impose heavy penalties for defaults and try to recover as many advances as possible. This makes it nearly impossible for the industry, and especially the small-scale industry, to survive through a recession (Bhide, 2000)

A Study by the Federation of India Chambers of Commerce and Industry (FICCI), March 2004 pointed out that the share of small industry sector in bank credit outstanding which was 14.2 per cent earlier, has come down to 11.1 per cent in March 2003. The shortage of finance and credit creates a whole group of problems relating to size of the unit, the quality of labour, market coverage, purchase of raw materials, machinery and equipment; all these problems in turn lead to low and poor quality of production (Ramappa & Basavaraja, 2006).



Cover Page

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### **Problem of Marketing**

Marketing is another major stumbling block for MSMEs as they lack marketing wherewithal to sell their products effectively. Financial difficulties don't permit them to offer attractive credit terms etc to the marketing intermediaries. Another problem being faced by them in the field of marketing is from competitive (dis) advantage vis-à-vis large-scale units, because of shortage of capital and financial resources etc. Many MSMEs supplying the same product creates a situation of competition among them. Large-scale industries finding themselves in a strong bargaining position, a purchase product from MSMEs at competitive rates the result they ultimately lose in the bargain.

### **Problem of Power**

There is inadequate supply of power for the MSMEs of the country. The supply of power is uncertain and breakdown is frequent which results in damage to the plant and causes suspension of work for long hours. The shortage of power was 9.4 per cent in the year 1986-87, and 10.8 percent in 2017-18, but it increased to 17 per cent in 2001 (Third SSI Census Report 2017-18; Ramappa & Basavaraja, op cit).

### **Problem of Raw Material**

In view of rising tempo of industrial activity, the shortage of right type of raw material at standard price has affected the entire industrial sector. Because of their smallness and weak financial position, MSMEs are in a vulnerable position. Often, they have to utilise the services of middlemen to get raw materials on credit. Such an arrangement has serious repercussions on costs and revenues. The situation is particularly disadvantageous when raw materials are imported, as the profit margins of middlemen are rather high. Their meagre resources induce small industrialists to use cheap and inferior materials, which naturally affects the quality of their finished products. Moreover, irregular supply of certain raw materials adversely affects their production programs (Desai, 2019).

### **Policy for the strengthening of MSMEs**

Following are the some of the policy prescriptions that can improve the environment, potential and performance of micro, small and medium enterprises.

The protection (provided by an external agency like the government) can never be a viable alternative to the inherent competitive strength of any economic organization as it is neither possible nor feasible in the long run. All industrial units, small or large, have to sustain themselves on their own competitive strength by successfully facing competition in market economies. Even to provide employment in a sustainable way and at higher wages, industrial units have to be competitive and commercially viable (Bhavani, 2020). Therefore, the policy of protection to the MSMEs sector should give way to a more proactive policy of helping them to enhance their competitiveness in a market-driven economy through improved product quality, increased productivity and innovation. It should aim at long-term sustainable growth of the MSMEs sector rather than at short-term subsistence (Bhide, op. cit.). In the era of liberalisation and deregulation, de-reservation also has become a feature of present industrial policy.<sup>1</sup> micro and small enterprise managers can taste success not just by survival but also by competing in the market.

### **Public Private Partnership (PPP)**

There is a need for innovative strategies to tackle the problems of MSMEs. Public-private partnership (PPP) between public institutions and private businesses could be one such strategy. This would require contribution of resources by both as also participation in the planning and decision-making processes and leveraging the competencies of each for collaborative, promotional efforts (Bhide, op. cit)

### **Easy Access to Finance**

Various expert committees appointed by the GOI and RBI emphasise that the lack of adequate and timely financing on competitive terms is the single most important constraint to the growth and development of the MSMEs. The demand for finance, implicit as well as explicit, from small industry will be substantial considering its size, structure, growth pattern, need for restructuring and technology development (Bala Subrahmanya, Mathirajan, Balachandra, 2020).

The low-cost funds should be provided to small enterprises to enable them to contain their cost of output thereby making their products more competitive, for this government should remove interest rate caps on small loans. In addition, the government should create a trading corporations and e-commerce portal for the small enterprises. In order to augment the growth and momentum of MSMEs in the present age of Information Technology, there is a need to reconstruct and reorient the present strategy dealing with this segment of the Indian industrial sector with close association between government and industrial association. At present SSI sector needs big incentives, not piecemeal (Kumar & Bala, 2017). The void left by big banks has to be filled up by the micro-finance institutions, urgently.



Cover Page



### Promoting Entrepreneurship

The problems of entrepreneurs are multi-dimensional. These can be solved by the coordinated efforts of entrepreneurs, coordinated functioning of promotional agencies and governmental assistance without red tapism or bureaucratic delays. The entrepreneurs have to be educated and they should have proper training in acquiring the necessary skill and expertise in running an enterprise. More important is the ability and venturesomeness to assume risks and succeed in overrunning it (Narayanaswamy, Manivel & Baskar, 2019).

### Technology up gradation

In the present competitive environment without significant technological progress, it is hardly conducive for small enterprises to secure for themselves the business opportunities in the high-end spectrum of manufactured goods. So, the MSMEs in India need to upgrade technologies on a continuous basis to remain competitive. Up gradation of manufacturing processes and management practices through the induction of appropriate technology and up gradation of international quality standards are essential prerequisites for taking advantage of the emerging opportunities in post WTO regime (Kumar & Bala, 2017). The government can provide the infrastructure and train the managers in the use of the software which can eliminate waste, compress production cycles, and improve the quality of the products (Bhide, op. cit).

### Training for Manpower

The non-availability of skilled manpower is an important constraint, especially for hi-tech industries. Government training institutes are often ill equipped, follow outdated curricula and are theoretical in approach. Specialised training institutes can be started on the PPP concept wherein infrastructure can be provided by the government while the management can be left to either an NGO or an industry association. Government should establish Training Centres so that it will help to effectively train manpower in MSMEs. It has as to rationalise the labour laws, which are rigid (Chandawakar & Kulkarni, 2019).

### Testing and Certification Facilities

A network of testing and certification facilities need to be put in place for the use of MSMEs, especially for those who wish to enter the export market. Specialised facilities often require expensive and sophisticated instruments.

### Marketing Assistance

Difficulties in marketing their products have always been a major problem for the small manufacturers. Government agencies have often failed in providing assistance since officials have little understanding of market intricacies. Instead of competing severely against each other through undercutting in prices, the small manufacturers could try a collaborative approach by setting up marketing consortia (Bhide, op. cit).The government should adopt a policy of stable price and quantity preference in purchases of the products from MSMEs. The government should promote establishment of marketing companies for the products of MSMEs. Special efforts are, required to, be made, in all exporting areas to develop consciousness towards quality, diversification and technology improvement (Chandawakar & Kulkarni, op. cit).

### Basic infrastructure

Providing basic infrastructure to MSMEs clusters through industrial estates has been the traditional strategy of most governments for promoting these industries. However, increasingly small units, especially in hi-tech areas, are in need of specialised infrastructure and services of international standards. Government is not in a position to provide and maintain such facilities in bulk. Specialised facilities can be jointly funded by government and the user-industries and thereafter, handed over to expert private agencies for maintenance.

Industrial estates set up by the government can be handed over to associations of local industries for maintenance along with the tax revenues. Infrastructure projects can be structured to make them attractive to private investors by offering them as ‘packages’ combining commercially viable projects with the not-so viable ones or by offering subsidies and tax concessions for the unviable segments (Bhide, 2020).

### In-house Research and Development

There should be encouragement to the research and development (R&D) in the MSMEs. To promote R and D in small industry it may be essential to reorient public policy from support through ‘technology transfer’ to support to ‘in house and in-depth R and D and technological innovations. Further, it is imperative to strengthen the existing financial and technological infrastructure for R and D and innovations and make it easily accessible to small firms and to prepare technopreneurs for tomorrow. This has to be done particularly at the district level to be more effective. This will lend greater stability to small industry development in the country(Bala



Subrahmanya, Mathirajan & Balachandra, 2002). From the human angle it is required that MSMEs become a ground for developing human resources of non-farm sector and lend credibility to the phenomenon of inclusive growth in yet another way.

### Conclusion

MSME contribute significantly to social and economic development objectives such as labour absorption, income distribution, rural development, poverty eradication, regional balance and promotion of entrepreneurship. In the sixty years of India's Independence the small-scale sector has acquired a prominent place in the socio-economic development of the country. Its performance in creditable, yet proper and innovative approach alludes. The sector needs many corrective steps to succeed in the 21st century. The key to success for MSMEs would lie in looking at the globe as a market and succeed out there. As a result of globalisation and liberalisation, coupled with WTO regime, Indian MSMEs have been passing through a transitional period. With the slowing down of economies of US and European Union on the one hand, and the ever-increasing competition from Chinese economy, Indian economy is in a situation where it has to take more measured steps. According to Mr. Jawahar Sircar, Additional Secretary and Development Commissioner, Ministry of Micro, Small and Medium Enterprises (MSMEs), the government has identified three thrust areas for increasing competitiveness in this respect: technology (including quality), skills development and finance. The National Manufacturing Competitiveness Programme has therefore, been implemented (CII, op. cit).

A technologically vibrant and internationally competitive small industry should be encouraged to emerge, to make a sustainable contribution to national income, employment and exports. All the external support including policy assistance has a meaning only when individual units are motivated. Industry and government agencies can play a significant role in educating small units about the changes in the business environment and the necessity of going in for technological up gradation. To play a meaningful role, it is essential for both industry associations and government agencies to change their attitudes and to instil trust and confidence in the 'small' units. And some of them can even plan to graduate to 'medium' units.

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Cover Page



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