

Make in India: Empowering the MSME Sector

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Abstract: Micro Small and Medium Enterprises (MSMEs) are considered as one of the most important growth engines for sustainable economic development in India. These are the units, specialised in specific products and services, who participate as ancillary industry/job worker/vendor, traders etc., to larger units. Consequently, they enable larger entities to complete the entire value chain in a cost effective manner. MSME sector has been recognized as significant contributor in inclusive growth and regionally balanced development. This sector has been undergoing a significant transition post liberalization era after opening up of the economy. Indian MSMEs suffer from issues like financial and human resource, infrastructure, legal and regulatory compliances, policy of de-reservation etc. This paper explores various opportunities and challenges for Indian MSMEs to be a part of the global value chain and gain a greater momentum to attain country's future growth expectation

I. Introduction

MSMEs are significant contributors to economy in terms of output and employment. MSMEs are units, specialised in specific products and services, who participate as ancillary industry/job worker/vendor, traders etc., to larger units. Consequently, they enable larger entities to complete the entire value chain in a cost effective manner. It has been observed in case of various countries that by creating infrastructure and supporting the MSMEs have enabled them to become more competitive and they have been able to contribute more towards economic development. In an increasingly globalized competitive environment, the MSMEs have to upgrade their skill, knowledge and have to adopt latest technologies and modern management practices to sustain and remain competitive. Government's role as a facilitator will help the sector to become more competitive and grow at a faster rate.

Definition of Micro Small and Medium Enterprise (MSME) in India:

The Micro Small and Medium Development Act (MSMED) 2006 was introduced in 2006. The MSMED act received assent of President of India on 16th June 2006 and the act came into force w.e.f. 2nd October 2006, vide notification dated 18th July 2006 issued by Ministry of Small Scale Industry. The Act had been introduced in order to provide for facilitating the promotion and development and enhancing the competitiveness of micro small and medium enterprises. The Act defines new concept viz. 'Enterprise' and also defines the 'Micro, Small & Medium' Enterprise. As per the act, "Enterprise means, an industrial undertaking or a business concern or any other establishment, by whatever name called, engaged in the manufacture or production of goods, in any manner, pertaining to any industry specified in the First Schedule to the Industries (Development and Regulation) Act, 1951 or engaged in providing or rendering of any service or services".

Definition of various segments of MSME as per MSMED Act, 2006, are as under			Priority Sector classification, as per RBI guidelines
Type of activity	Type of enterprise		
		Invest in plant & machinery *	
Manufacturing Enterprise	Micro	<=Rs.25 lakhs	Priority Sector
	Small	>Rs.25 lakhs & <=Rs.500 lakhs	Priority Sector
	Medium	>Rs.500 lakhs & <=Rs.1000 lakhs	Priority sector
Service Enterprise		Investment in Equipment \$	
	Micro	<=Rs.10 lakhs	Priority Sector for Exposure upto Rs.5 crores

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	Small	>Rs.10 lakhs & <=Rs.200 lakhs	Priority Sector for Exposure upto Rs.5 crores
	Medium	>Rs.200 lakhs & <=Rs.500lakhs	Priority Sector for Exposure upto Rs.10 crores

* Investment in terms of original cost excluding land and building and the items specified by the Ministry of Small Scale Industries vide its notification no. S.O. 1722 (E) dated October 5, 2006.

\$ Original cost excluding land and building and furniture, fittings and other items not directly related to the service rendered or as may be notified under the MSMED Act, 2006.

The following changes may be made to incentivize the sector and make the sector more efficient and competitive

Increase the upper limit of investment of MSME classification:

It may be noted that the above investment criteria is as per MSMED Act 2006 and the same is being continued till today, although since then due to inflation, prices for all segments have gone up substantially. As such time has come to revise the investment threshold, keeping in mind the inflation trend. It is necessary to invest in plant and machinery/equipment to improve productivity, quality and to remain competitive. The mechanization has further necessitated due to scarcity of skilled labour at affordable price. Many occasions, entrepreneurs are not willing to expand in same company, fearing loosing of various benefits reserved for them. As a result they open multiple business entities under the same management resulting in limited growth in terms of financials of as a single entity. This hampers further growth for these entities since investors require strong financials and robust growth prospects. The individual MSME unit is required to be equipped enough to supply large quantities of products to get economies of scale, which requires high investment in plant and machinery. To overcome the situation and to usher growth in MSME segment, upper limit of investment, should be upwardly revised linking to inflation and the revision should be done at an interval of may be every 3 years.

Inclusion of Traders under MSME and Priority sector: It may be observed that traders have been kept outside the purview of MSMED Act. Traders are one of the most important partners in the value chain since, products/services reaches to end user/consumer through traders only. Traders should also be included under MSMED act and advance granted to traders may be upto Rs.5 crores be included under priority sector lending, to support and increase the efficiency of the entire value chain.

100% EOU should be classified under Priority sector without any limit in terms of Exposure, investment in P&M/Equipment or turnover: Exporter plays crucial role in terms of foreign exchange earnings. For overall growth in exports and to boost foreign exchange earnings and reserves, export credit should be classified under priority sector, irrespective of any limits for investment in plant and machinery/equipment, exposure or turnover, since exporters have to abide by various rules and norms of the importing country, which necessitates higher investment in plant and machinery/equipment than their domestic counterparts.

II. MSMEs contribution to Indian Economy

For collecting and compiling the data for the MSMEs sector (including Khadi, Village and Coir Industries), the Fourth All India Census of MSMEs with reference year 2006-07, was launched during 2007-08 in the country. Fourth All India Census 2006-07 covered both registered and unregistered sectors. Final Report, on Fourth All India Census of Micro, Small & Medium Enterprises 2006-2007: for Registered Sector and Unregistered Sector, has been brought out by DC MSME, GOI. The MSME sector contributes nearly 8% of the country's Gross Domestic Product (GDP), 45% of the manufacturing output, and 40% of the country's total exports. It reflects the importance and growth prospects of MSMEs in Indian economy. Registered MSME sector provides employment to 93.09 lakhs people through 15.64 lakhs units pan India. It may be observed from the following data, average employment as well as gross output per unit was highest for medium enterprise among the MSME segment.

Sector	No of working enterprise (lakh)	No of employment (lakh)	Average number of employment per enterprise	Gross Output per unit (Rs.in lakh)
Micro	14.85	65.34	4.40	21.08
Small	0.76	23.43	30.62	416.57
Medium	0.03	4.32	160.87	2819.94

(source: from 4th census , only for registered MSMEs, reference year 2006-07)

Problem of access to Capital

The MSMEs mainly depend on bank finance for timely and adequate flow of credit to the sector.

Sources of Financing

Among the present sources of financing, the common trend is towards raising bank finance. Current Sources of Borrowings by MSMEs in India

- Banks
- Informal Lenders

Regarding access to finance following options could be viewed as some of the international best practices:-

Access to Fund

- Borrowing
- Equity Financing
- Venture Capital
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Government Support

- To encourage bank lending to MSMEs and form credit guarantee companies
- Central re-guaranty program as incentive
- Marketing and promotion
- Developing a uniform Credit Rating System
- Developing a secondary market for the guaranteed portion of loans
- Development of micro credit program.

Need for Venture Capital

Although MSMEs commonly use traditional debt, Venture capital is viewed as a more appropriate financing instrument for enterprises with high-growth-potential as well as at start-up stage. During the start-up phase, firms need finance for research and development of products and services and for marketing the same. It takes time to generate profit and start repayment of debt. They should look for venture capital to cater to their financial need to establish, expand and grow. Recent trend in this area are crowd funding, peer to peer lending, Micro lending etc. Hence, policy related to the accessibility of alternative sources of capital to MSMEs should be framed to encourage growth.

Access to Equity Capital

Another problem is the accessibility of Equity capital. There is negligible flow of equity capital into this sector at present, throwing challenges to MSMEs for their future growth. At startup phase either promoters use their own funds or raise funds from private equity funds and venture capitalists. Due to lack of market for private equity/venture capital in India, the Indian entrepreneurs prefer to rely on own funds and support from friends and relatives to meet their capital requirements. The cost of raising debt is not only higher but also difficult to raise at startup phase. Thus, to fund the next level of growth, access to equity funds via capital markets is preferable and hence there is a need for an exchange for SMEs. Due to the strong need felt for a dedicated Exchange for MSMEs, SEBI had permitted BSE and NSE to set up Exchange for MSMEs in terms of the recommendations of the PM's Task Force on MSMEs. Bombay Stock Exchange (BSE) had launched the 'BSE SME Exchange' and National Stock Exchange (NSE) started 'NSE Emerge'.

SME Exchanges have immense potential to offer various opportunities as far as SME listing is concerned. There are few advantages of using a dedicated SME exchange viz. listing norms are simplified and flexible. MSME Entrepreneurs mostly depend on funds from family and friends and on private equity in some handful cases. However, they are reluctant to allow outside investors viz. private equity and venture capitalist, may be due to fear of equity dilution, fear of becoming minority stake holder, or fear of losing control over business or their business secret and practices will be shared with competitor/general public. To solve these problems, education and training should be provided to the entrepreneurs. It may be concluded that in order to cater to the financing needs of MSMEs, following approaches may be adopted

- ✓ Govt. may allocate special funds to banks, with a specific mandate to fund MSMEs at start-up level.
- ✓ Encourage higher participation of Development banks and Community banks.

- ✓ MSME trade association should impart proper guidance and training to the entrepreneurs to encourage using the stock market as a source of financing.
- ✓ Formulate broad based guidelines and encourage various financing options viz. Venture Capital, Private Equity etc.

De-reservation of sectors earlier reserved for SSIs

Since 1991 onwards, general economic policy moved towards openness of the economy both for investment and imports, the very rationale for continuation of reservation of items to be produced exclusive by the SSI was brought under scrutiny. Consequently, process of de-reservation of items reserved exclusively for SSI segment began in 1997. It is observed that, total of 844 items have been de reserved since 1997, the year wise breakup of the same is given below.

Sr.no.	Year	No of items de reserved
1	From 1997 2001	39
2	2002	51
3	2003	75
4	2004	85
5	2005	108
6	2006	180
7	2007	212
8	2008	93
9	2010	1
	Total	844

(source:www.dcmsme.gov.in)

As per Govt of India, as on 30th July 2010, only 20 items have been reserved for exclusive manufacture of Micro and Small Enterprise. However, this policy of reservation for exclusive manufacture by MSE sector has been dispensed with the dereservation of these remaining 20 items vide notification no.S.O.998(E) dated 10th April 2015.

As such Post liberalization, market has thus become quite competitive for both existing and new MSMEs and MSMEs have to gear up fully in all aspect to remain competitive and sustainable. Liberalization and Globalization have opened up foreign markets to Indian entrepreneurs also. Indian MSMEs should encash this opportunity by taking part in value chain as vendor/subcontractor/job worker/ancillary industry/service provider etc. Further FDI has been allowed in various sectors in Indian economy which has also opened up opportunities for outsourcing of various activities within India, which should be beneficial for Indian MSMEs.

III. Conclusion

It is observed that, as per constitution, MSMEs are Proprietorship, Partnership and closely held Private Ltd Companies. The entrepreneurs in this segment are 1st, 2nd or 3rd generation entrepreneurs who are involved in family oriented business. Many a times these enterprises face challenges due to lack of leadership qualities, dispute among promoters and lack of succession. It has been observed that many a time the younger generations after completion of their higher studies are not keen to participate in family business rather want to join corporate world, which throws challenges to the units even to continue, keep aside growth prospects. Sometimes entrepreneurs themselves do not encourage their children to participate in the business considering hardship and challenges being faced by them in the segment. Conversely it has also been observed, next generation have joined large corporate/MNCs after completion of higher studies and have joined backed their family business after gathering 5- 6 years of experience in corporate world. They bring knowledge and expertise of large corporate in their family business and these units may show better growth prospects.

MSMEs mostly run the business traditionally and slow in upgrading their skill set, which makes them vulnerable to competition. They should upgrade their skill set and knowledge, in tandem with various changes in industry and economy, to remain competitive. Smaller units mostly depend upon the skill set of the entrepreneurs only. People are the key resources of any enterprise who drive the business and make success happen even in difficult situation. However due to various constraints, MSMEs employ limited people and sometimes engage semi-skilled resources who are expected to accomplish multi-task and play various roles as

and when situation demands, which sometimes not only hampers quality of products and services offered by the enterprise but also creates bottlenecks for growth. Entrepreneur should also focus on this vital area to keep an enterprise sustainable and successful.

It is important to promote entrepreneurship for encouraging innovation and competition. Growing credit portfolio without growth in creditworthy borrowers creates the burden as NPAs for lenders. Growth of creditworthy borrowers is important for enhancing the quality of credit. Government should encourage IITs, IIMs, ITIs, Govt. and private engineering colleges and management institutes to have more linkage with MSMEs, to develop various techniques to reduce cost and improve efficiencies and to innovate new products and services. These will not only help students of these institutes to gather firsthand knowledge about business but also develop entrepreneurship skill and encourage them to become entrepreneur. Thus industry will see a new era of entrepreneurs who are well qualified and visionary and ready to take the segments to much higher heights.

All government notification/guidelines/scheme regarding MSMEs should be directly sent to all Banks/F.I.s dealing with MSMEs, to have firsthand information about government policies and guidelines which will in turn help Banks/F.I.s to formulate and customise products and services for its customers in a time bound manner. India is a vast country where natural resources for alternative energy viz. solar energy, wind energy, ocean energy, natural gas are available in abundant. Government should harness these energies for industrial use at affordable rate. This will create new industries in these segments as well as reduce overall cost of production. This will also reduce substantial forex outgo by reducing cost of import of fossil fuel, thereby improving country's balance of payment.

Government should set up industry specific industrial parks in various MSME clusters along with infrastructure facilities viz. easy power & water connection, waste management system, single window clearance for various government processes etc. Government should also take initiative in cluster development by connecting these clusters with railways, roadways and ports to reduce transportation cost and time, which will in turn increase productivity and will usher growth in economy.

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