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Role of Micro, Small and Medium Enterprises (MSMEs) in Indian Economy

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Abstract

In India role of micro, small and medium enterprises (MSMEs) in the economic and social development of the country is well recognised. MSME sector is a nursery of entrepreneurship, often driven by individual creativity and innovation. This sector contributes 37.54 per cent of the country's GDP, 37.33 per cent of the manufactured output and 40 per cent of total exports. The MSME sector has provided employment to about 117 million through 51 million enterprises. The study found that MSME sector has made significant role in overall development of the country.

Keywords: *MSMEs, Employment, Production, GDP*

JEL Classification: *L26, L32, L53*

Introduction

Small Business development as an issue has become more increasingly important in recent years in both developed and developing countries (Ray & Hutchinson, 1983). Substantial money and energy world-wide has been invested in support services for the small and mid-sized enterprises (SME) sector, as interest has grown in the development small enterprises (Bolton Committee, 1971; International Labour Organisation, 1992). The attention and significance of micro-enterprise development among economic architects and international assistance agencies stem from the need for more direct assistance to the reduction of poverty (Neck, 1977).

During the struggle for independence in India, Mahatma Gandhi-"Father of the Nation" has been keen on the protection and expansion of traditional, mainly rural, household enterprises. Another stand of thinking has been shaped by the report of the Ford Foundation team (Government of India, 1954) which emphasised the role of modern small-scale units as an industrial structure.

MSMEs provide immediate large scale employment; they approach a method of confirming a more equitable distribution of the national income and they facilitate an effective mobilization of resources and skill which might otherwise remain unutilized. Some of the problems that unexpected urbanization tends to create will be avoided by the establishment of small samples of industrial production all over the country (Planning Commission, Second Five-Year Plan,1956-61).

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Micro, Small and Medium Enterprises (MSME) sector has appeared as a highly promising and dynamic sector of the Indian economy over the last five decades. This sector plays very important role by offering large employment opportunities at relatively lower capital cost than large industries as well as helps in industrialization of rural & backward areas, to reducing regional disparities, promising more equitable distribution of national income and wealth. MSMEs serving to fill out large industries as ancillary units and this sector contribute immensely to the socioeconomic development of the country. This sector contributes 37.54 per cent of the country's GDP, 37.33 per cent of the manufactured output and 40 per cent of total exports. The MSME sector provides employment to about 117 million persons through 51 million enterprises. In the MSMEs labour to capital ratio and the overall growth is much higher than in the large industries. MSMEs are more evenly distributed in different geographic parts of the nation. Thus, MSMEs are important for the national growth objectives that are 'inclusive economic growth' (Annual Report 2015-16, Ministry of Micro Small and Medium Enterprises, Government of India).

By using comparatively low capital investment, higher employment opportunities and ample official support, the small-scale sector maintained its growth trend in the pre-reform period. Importance of MSMEs has not been undermined in the post-liberalization era and even in the Ninth Five-Year Plan (1997-2002) document, it has been agreed that: The small sector has become matured and is in a position to make a much larger contribution to the national economy as well as can face the challenges of large industry, including multinationals.

Ragunathan (1988) opined that the Industrial Policy Resolution of April 1948, rightly found the small scale industries as being "Particularly suitable for the better usage of local resources and for the accomplishment of local self-sufficiency in respect of certain types of necessary consumer goods like food, cloth and agricultural equipment".

Definition of MSMEs as per the MSME Development Act, 2006

Presently in India, micro, small and medium enterprises as per the MSME Development Act, 2006 has been defined based on their investment in plant and machinery (for manufacturing enterprise) and on equipment's for enterprises providing services. As per this act the Micro, Small and Medium Enterprises (MSME) are classified in two Classes these are as follows:

Manufacturing Enterprises: The enterprises engaged in the manufacture or production of goods relating to any industry specified in the first schedule to the industries (Development and Regulation Act, 1951). The Manufacturing Enterprise is defined in terms of investment in Plant & Machinery.

- A micro enterprise is an enterprise where investment in plant and machinery does not exceed Rs 25 lakhs.
- A small enterprise is an enterprise where the investment in plant and machinery is more than Rs 25 lakh but does not exceed Rs 5 crores.
- A medium enterprise is an enterprise where the investment in plant and machinery is more than Rs 5 crores but does not exceed Rs 10 crores.

Service Enterprises: The enterprises involved in providing or execution of services and are defined in terms of investment in equipment.

- A micro enterprise is an enterprise where investment in equipment does not exceed Rs 10 lakh.
- A small enterprise is an enterprise where the investment in equipment will be more than Rs 10 lakh but does not exceed Rs 2crores.
- A medium enterprise is an enterprise where the investment in equipment will be more than Rs 2crore but does not exceed Rs 5 crores.

Objective of the study

To analyse the performance of Micro, Small and Medium enterprises (MSMEs) in India with respect to growth of total working MSMEs; employment generation; investment in fixed assets; gross output; contribution to country's GDP and contribution to manufacturing output.

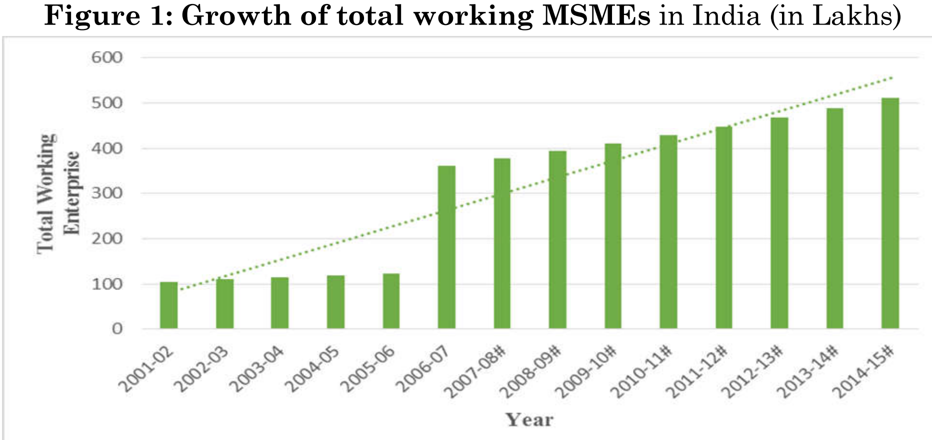
Methodology of the study

The study is based on secondary information, which has been collected from various annual reports of MSMEs and SSI. Further, information has also been collected from different issues of Economic Survey, Government of India and Handbook of Statistics on the Indian Economy, RBI. In the present study data from 2001-02 to 2014-15 have been considered. The collected data has been presented in tabular form and for lucid presentation, graphs have been used.

Analysis and Interpretation

Number of working MSMEs: The small-scale industrial sector has been playing a crucial role for the Indian economy in terms of employment and growth. MSME has recorded a high rate of growth since independence irrespective of difficult competition from the large sector and not so-encouraging support from the government.

Figure 1: Growth of total working MSMEs in India (in Lakhs)



Source: Annual Report, 2013-14, 2014-15 & 2015-16.
Ministry of Micro, Small and Medium Enterprises, www.msme.gov.in

It can be deciphered from the above figure 1 that the number of MSMEs has increased steadily in India from 105.21 lakhs units in 2001-02 to 510.57 lakhs units in

2014-15. This could be possible due to the conducive policy environment during post liberalization era of 1991. Number of MSMEs increases significantly from the year 2006-07 onwards due to changes in definition of MSMEs as per MSMEs Development Act, 2006, which has widen the scope of definition given earlier. Increase in number of MSMEs leads to increase in investment which leads to capital formation of India. Not only investment, increase in number of MSMEs also pushed up employment of India where unemployment is one of the severe problem.

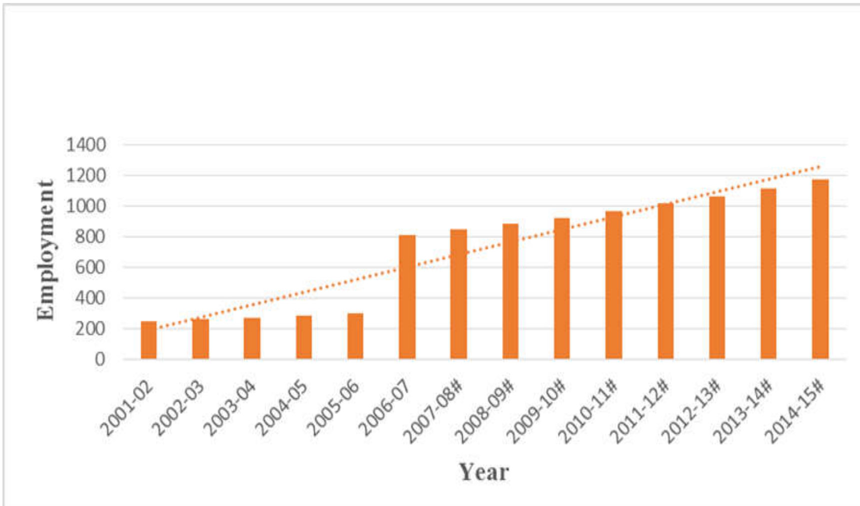
Table 1: Performance of SSI / MSME Units, Employment, Investments and Gross Output

Year	Total Working Enterprise (In Lakh)	Employment (In Lakh)	Investment in Fixed Assets (In Rs Crores)	Gross Output (In Rs Crores)
2001-02	105.21	249.33	154349	282270
2002-03	109.49	260.21	162317	314850
2003-04	113.95	271.42	170219	364547
2004-05	118.59	282.57	178699	429796
2005-06	123.42	294.91	188113	497842
2006-07	361.76	805.23	868543.79	1351383.45
2007-08	377.37	842.23	917437.46	1435179.26
2008-09	393.7	881.14	971407.49	1524234.83
2009-10	410.82	922.19	1029331.46	1619355.53
2010-11	428.77	965.69	1094893.42	1721553.42
2011-12	447.73	1012.59	1176939.36	1834332.05
2012-13	467.54	1,061.40	1,268,763.67	NA
2013-14	488.46	1,114.29	1,363,700.54	NA
2014-15	510.57	1,171.32	1,471,912.94	NA

Source: Annual Report, 2013-14, 2014-15 & 2015-16. Ministry of Micro, Small and Medium Enterprises, www.msme.gov.in

Employment generated by MSMEs: Rapid economic growth requires the generation of a large economic surplus in all fields of productive activity. The advantage of large industries is that they are generally capital intensive and accordingly per capita productivity and economic surplus is greater in them. Against this, the small scale industries are generally labour intensive. Accordingly, they have a substantially higher employment potential as compared to the large scale industries. P. C. Mahalanobis had this to say on the employment potential of small scale and cottage industries: "In view of the meagreness of capital resources there is no possibility in the short run, for creating much employment through the factory industries. Now consider the household or cottage industries. They require very little capital. About six or seven hundred rupees would get an artisan family started. With any given investment, employment possibilities would be ten or fifteen or even twenty times greater in comparison with corresponding factory industries".

Figure 2: Trends in Employment Generated by MSMEs in India (in Lakhs)

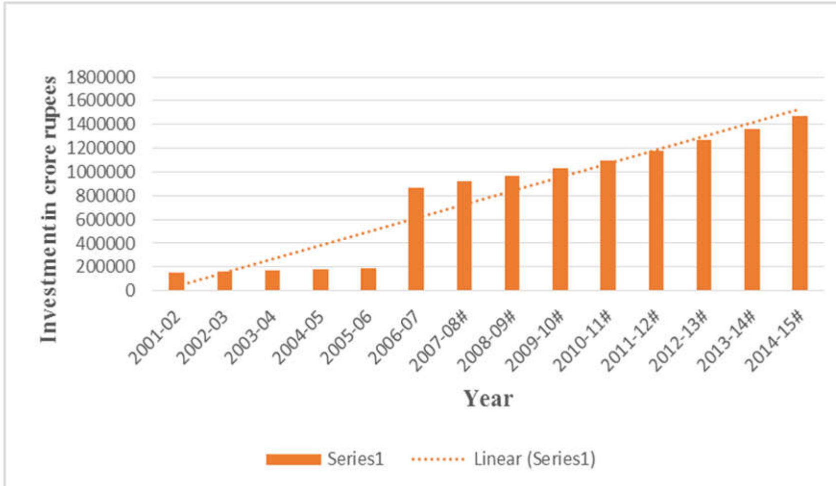


Source: Annual Report, 2013-14, 2014-15 & 2015-16.
Ministry of Micro, Small and Medium Enterprises, www.msme.gov.in

It can be observed from the above figure 2 that number of persons employed in MSMEs has risen from 249.33 lakhs in 2001-02 to 1,171.32 lakhs in 2014-15. The huge increase in employment has been observed from the year 2006-07 onwards. Trend line also shows a steady increase of employment over the years. The increasing trend may be due to the changes in MSME definition as per MSMEs Development Act, 2006 which has widen the scope as well as coverage of MSME sector which leads to mass labour absorption has taken place in the unorganized/ informal enterprises.

Investment in fixed assets by MSMEs: The MSMED Act, 2006 gives us tools for classification of enterprises based on their investment size and the nature of the activity undertaken by that enterprise. Enterprises are classified into two categories as per MSMED Act. These are manufacturing enterprises and service enterprises. For each of these categories, a definition is given to describe what comprises a micro enterprise or a small enterprise or a medium enterprise. Enterprises not coming under the above three categories would be treated as a large scale enterprise in India. It can be interpreted from the figure 3 that investment made by the MSMEs has increased steadily from ₹ 154349 crores in 2001-02 to ₹ 1471912.94 crores in 2014-15. The huge increase in fixed investment in MSME sector has been observed from the year 2006-07. The increasing trend gives a clear indication of the fact that investment in MSMEs has been showing a significant growth, which helps in increasing the total capital formation of the country.

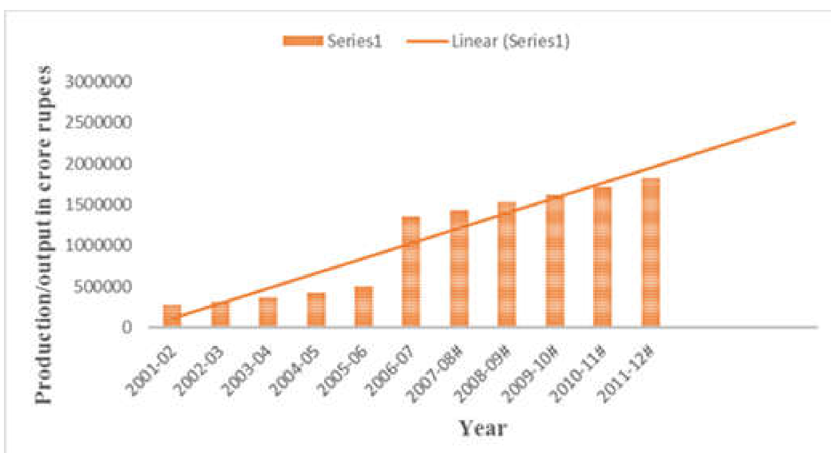
Figure 3: Trends of Fixed Investment in MSMEs (Rs. in Crore)



Source: Annual Report, 2013-14, 2014-15 & 2015-16.
Ministry of Micro, Small and Medium Enterprises, www.msme.gov.in

Production made by MSMEs: In India, MSMEs are manufacturing over 6,000 products. Some of the major products produced by subsectors of MSMEs in terms of manufacturing output are food products (18.97%), textiles and readymade garments (14.05%), basic metal (8.81%), chemical and products with chemical content (7.55%), metallic products (7.52%), machinery and equipments (6.35%), transport equipments (4.5%), rubber and plastic products (3.9%), furniture (2.62%), paper and paper products (2.03%) and leather and leather products (1.98%).

Figure 4: Trends in Output of MSMEs in India (in Crore)



Source: Annual Report, 2013-14, 2014-15 & 2015-16.
Ministry of Micro, Small and Medium Enterprises, www.msme.gov.in

It can be observed from the figure 4 that production made by MSMEs has risen from Rs 2,82,270 crores in 2001-02 to Rs 18,34,332.05 crores in 2011-12. Output (production) data are not available for the years 2012-13, 2013-14 and 2014-15. The huge increase in production has been observed from the year 2006-07 onwards.

Importance of MSME sector in Indian Economy

Contribution to GDP: As per the revised method recommended by the Central Statistics Office (CSO), Ministry of Statistics and Programme Implementation (MoSPI), on the basis of the data on Gross Domestic Product (GDP) published by CSO, MoSPI and final results of the up-to-date Census (Fourth Census), accompanied (with base reference year 2006-07), in which the data was collected till 2009 and results put out in 2011-12, the projected contribution of MSME sector (including service segment) to GDP during 2010-11, 2011-12 & 2012-13 are 36.69 per cent, 37.97 & 37.54 per cent respectively. Further, the contribution of manufacturing sector of MSME to Gross Domestic Product (GDP) has declined marginally from 7.73% in 2006-2007 to 7.04% in 2012-13. The contribution of the MSME service sector to the Gross Domestic Product (GDP) has increased from 27.42% in 2006-2007 to 30.5% in 2012-13. Total contribution made by MSME sector has increased from 35.13% in 2006-2007 to 37.54% in 2012-2013. This happen due to the better performance made by service sector of MSMEs in the context of Indian economy.

Share in manufacturing output: The total number of SSI units has increased from 79.6 lakhs in 1994-95 to 133.68 lakhs in 2007-08, indicating annual growth rate of 4.1 percent, but their production (at 1993-94 prices) increased from Rs 1,09,116 crores in 1994-95 to Rs 532979 crores in 2007-08 i.e. an annual average growth of 13 percent. The contribution of the MSME sector to overall industrial production has declined marginally from 42.02% in 2006-2007 to 37.33% in 2012-13. Decline in share of manufacturing output over the years by the MSME sector may be due to better performance made by the other segment of industrial production.

Contribution to export: With the establishment of a huge number of contemporary small-scale industries in the post-independence period, the involvement of the small-scale sector in export earnings has increased by leaps and bounds. It is encouraging to observe that majority of the exports of small-scale industries output consists of non-traditional items like readymade garments, sports goods, leather sandals and chappals, other leather products, canned and processed fish, woollen garments and knitwear, processed foods, chemicals and allied products and a large number of engineering goods. The volume of export made by the MSMEs has increased steadily from Rs 96.64 billion in 1990-91 to Rs 6301.05 billion in 2011-12. The huge increase in export made by MSME sector has been observed from the year 1990-91 onwards. This may be due to the adoption of liberal economic policy of the government which leads to earn more foreign currency as well as create more employment opportunity.

Mobilisation of Capital and Entrepreneurial Skill: The small-scale industries are at a divergent advantage as far as the utilisation of capital and entrepreneurial skill is concerned. A number of entrepreneurs are spread over small towns and villages of the country. Obviously, large scale industries cannot make use of them as effectively as the small-scale and village industries scattered over every parts of the country. Similarly, large-scale industries cannot utilise the savings made by people in areas far flung from the urban centres. But this task can be successfully done by setting up a network of small scale and cottage industries. In addition, a great number of other resources scattered over the country can be put to a decisive use by the small scale and cottage industries.

Regional Dispersal of Industries: Large enterprises are usually concentrated in metropolitan cities. The smaller towns and the rural areas in order to benefit from modern industrialism must inspire small enterprises. Industrialisation of the country can become complete only if it go through into the distant corners of the country. It may not be feasible to start small enterprises in every village, but it is fairly possible to select a group of villages and start small enterprises to satisfy to the needs of the small area from the local centre. Decentralisation of industrial enterprises also helps to tap local resources such as raw materials, idle savings local talents and also improves the standard of living in backward regions. In addition, decentralisation helps to solve the problems of bottle neck in the few industrial towns by widening the area of employment. It is pertinent to note that, out of total, 51.77% of MSMEs are located in rural areas whereas 48.23% of total units are established in urban areas of the country. The establishment of more enterprises in rural areas helps to remove regional disparity of income and unemployment problem and ensures proper utilisation of local resources.

Conclusion

Based on the findings of previous studies, MSMEs are struggling with certain problems, namely, financial assistance, lack of marketing assistance, lack of technical assistance, allocation of raw materials, imported component and equipment, absence of MSME friendly legislation, limited capital and knowledge, lack of access to global markets etc. However, MSME sector has made significant contribution towards employment generation, investment and GDP. Further, in order to increase the performance of MSME sector government need to simplify the existing policy on urgent basis.

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