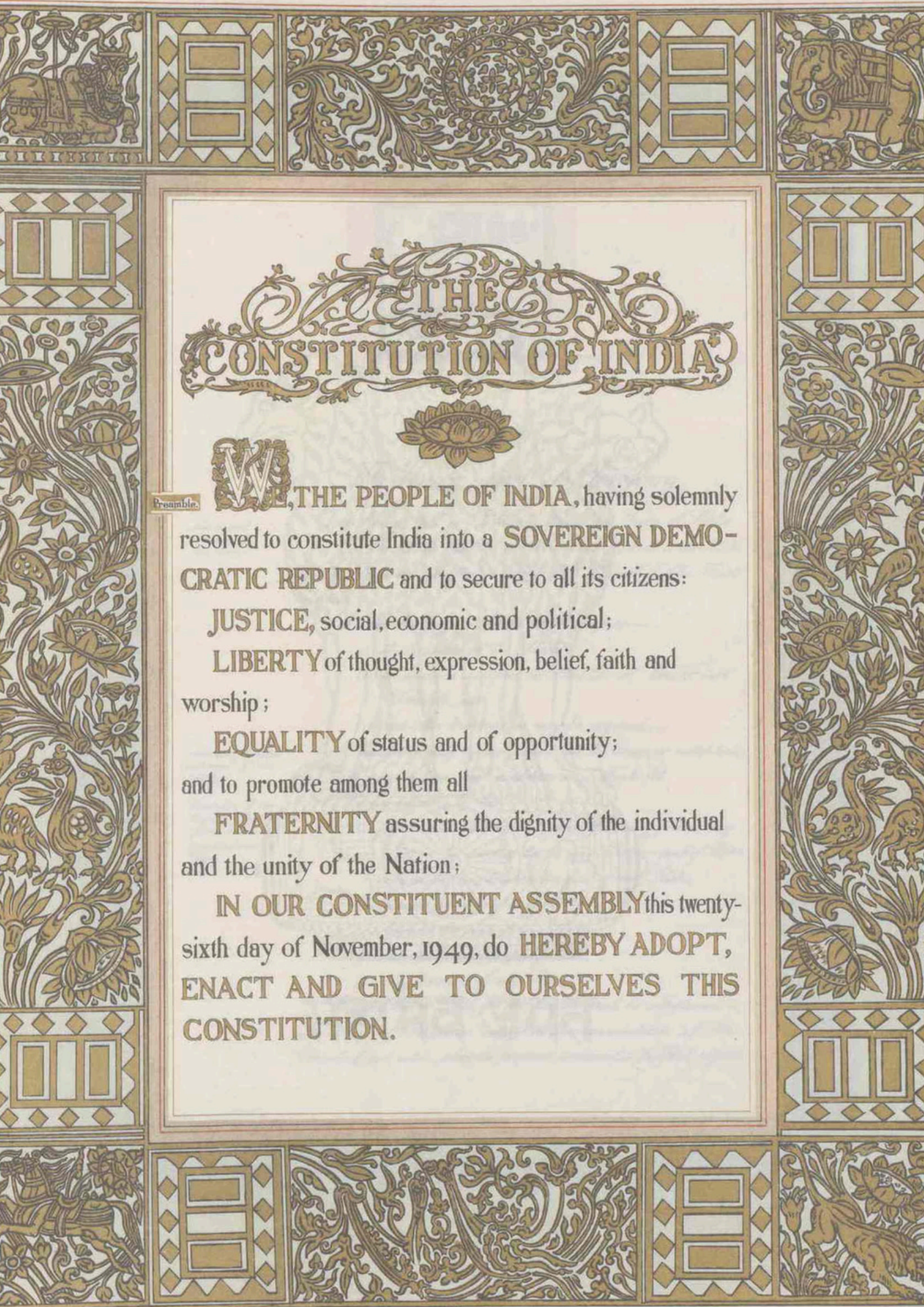


# BUILDING BLOCKS

A PRIMER ON THE GROWTH AND  
PERFORMANCE OF THE MSME  
SECTOR IN INDIA

Agrima Gupta  
Amrit Mahapatra

Office of Krishna Prasad Tenneti  
MP, Bapatla



# THE CONSTITUTION OF INDIA



Preamble.



**WE, THE PEOPLE OF INDIA**, having solemnly resolved to constitute India into a **SOVEREIGN DEMOCRATIC REPUBLIC** and to secure to all its citizens:

**JUSTICE**, social, economic and political;

**LIBERTY** of thought, expression, belief, faith and worship ;

**EQUALITY** of status and of opportunity;

and to promote among them all

**FRATERNITY** assuring the dignity of the individual and the unity of the Nation ;

**IN OUR CONSTITUENT ASSEMBLY** this twenty-sixth day of November, 1949, do **HEREBY ADOPT, ENACT AND GIVE TO OURSELVES THIS CONSTITUTION.**



*“The success of the young entrepreneur will be the key to India’s transformation in the new millennium.”*

**-- Mr. Dhirubhai Ambani**

Art. 43 of the Indian Constitution directs the government to endeavour to promote cottage industries, in line with Gandhian principles of inclusive development. The MSME sector has a key role to play in terms of employment generation, value-addition, and boosting incomes. This document is an attempt to review the present framework, the shortcomings and the best practices across the world on micro, small, and medium industries so as to implement them in India. We hope that this document provides an initiation point for fruitful discussions in the Parliament and beyond.

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## **FOREWORD**



After having spent over three decades in public service as an IPS officer, I am embarking on a new innings as a Member of Parliament. To that end, I aim at taking up issues of public welfare to drive inclusive growth. The Micro, Small and Medium Enterprises form the backbone of India's economy and are a major driver for inclusive growth. To that end, a comprehensive analysis of the functioning of the sector and highlighting the necessary reforms is essential.

The Parliament is not merely an expression of people's faith in democracy but also an extension of it. The importance of the same lies not just in the fact that it is a few hundred members debating proposed legislations or issues of national importance. Rather, it is in that 130 crore citizens are symbolically engaged in a process of deliberation, deciding what is in their mutual and collective interest. As certain roadblocks stand in our way in achieving the full potential of the micro, small and medium enterprises sector, I, like many other citizens, turn toward the Parliament.

This report, published by my office, intends to throw light on the state of MSME sector in India. It is a primer, based on questions asked in the Houses of Parliament, reports of its committees, and other compendiums of national and global publications that are relevant to the same. It is my earnest desire that this primer leads to spirited deliberations in the Parliament so as to drive growth for all and leverage the potential of India's MSME sector for achieving the goal of making India a \$5 trillion economy.

**Krishna Prasad Tenneti**

**(MP, Bapatla, Andhra Pradesh)**

## **Building Blocks: A Primer on the Growth and Performance of the MSME Sector in India**

In 2008, before the idea of electric vehicles had gained prominence as an alternative to traditional fossil fuel-based vehicles, Ampere Vehicles was founded in Tamil Nadu. Led by a woman entrepreneur Ms. Hemalatha Annamalai, Ampere became the first company in India to indigenously manufacture key components of an electric vehicle. Medium, small and micro enterprises (“**MSMEs**”) have formed the backbone of innovation and manufacturing in India.

MSMEs form an important pillar of India’s socio-economic development. The 2023-24 Economic Survey highlighted that India needs to create nearly 7.85 million jobs annually in the non-farm sector to cater to the growing workforce. MSME sector is the country’s second largest employer after agriculture.<sup>1</sup> It is therefore evident that MSMEs would be the driving force behind job creation in the years to come.

The share of the manufacturing sector in the total gross value added at current prices was 14.3% in 2023-24.<sup>2</sup> To adequately diversify the economy and shift the burden of driving growth from the service sector, the vision has been to increase the share of the manufacturing sector to 25% by 2025.<sup>3</sup> In 2022-23, MSMEs contributed 35.4% to the all-India manufacturing output.<sup>4</sup> 32% of all jobs created by MSMEs in 2023-24 were in the manufacturing sector.<sup>5</sup> Therefore, MSMEs have the potential to form the bedrock for further development of the manufacturing sector.

### **HIGHLIGHTS**

**Manufacturing Sector:** Share in Gross Value Added stood at 14.3% in 2023-24.

**MSMEs and manufacturing:** MSMEs contributed 35.4% to all-India manufacturing output.

**MSMEs and employment generation:** MSME sector is the second-largest employer after agriculture.

Realising the promise that this sector holds, this primer aims to undertake a critical analysis of the growth and development of MSMEs. The Micro, Small and Medium Enterprises Development Act, 2006 (“**MSMED Act**”) provided a fillip to the MSME sector. Initiatives have been taken thereafter, to address specific issues such as digitisation, credit availability to and formalisation of MSMEs. However, gaps still remain that have inhibited the sector from reaching its full potential.

## I. Evolution of policies related to the MSME Sector

The sector developed in three distinct phases marked by the introduction of various policies to recognise, encourage and incentivise MSMEs.<sup>6</sup>

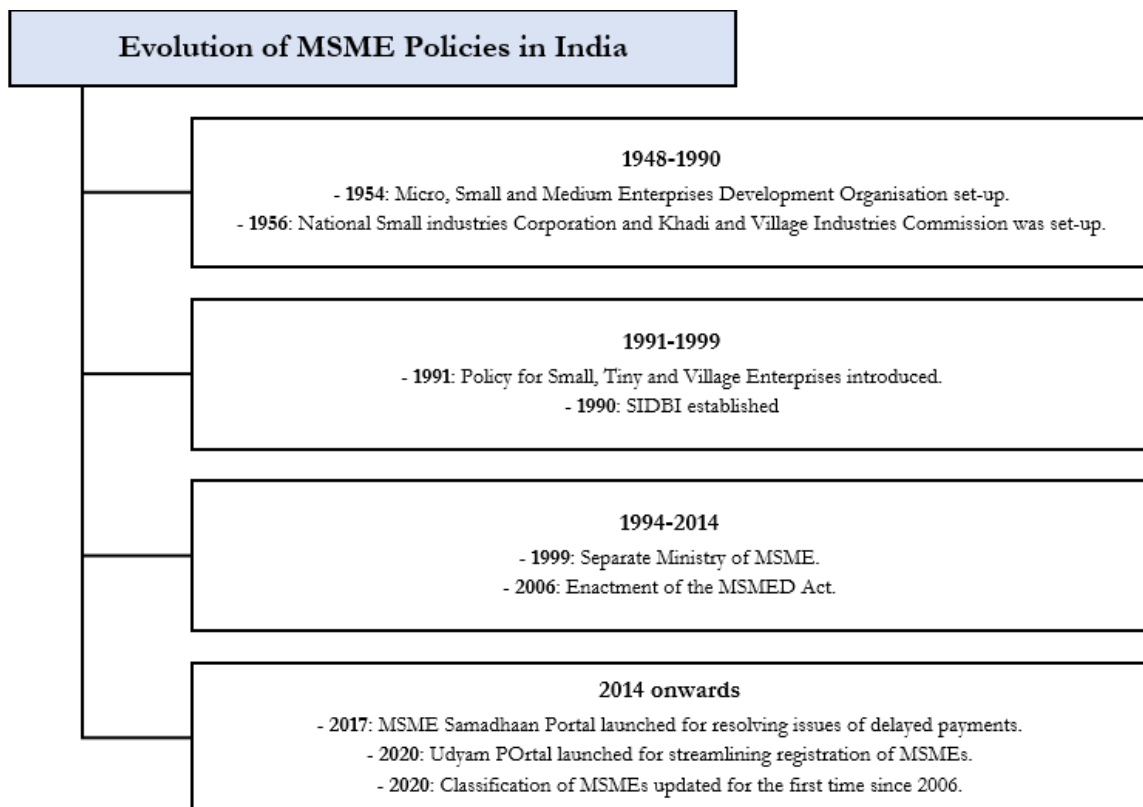
### a. 1948-1990

Various policy resolutions during this period provided recognition to micro and small enterprises and acknowledged them as an effective tool in expanding employment opportunities. The Small Industries Development Organisation (now renamed as Micro, Small and Medium Enterprises Development Organisation) was set-up in 1954.

This was followed by the setting-up of the National Small Industries Corporation and the Khadi and Village Industries Commission in 1956. These policies were aimed at supporting and augmenting the growth of MSMEs.

### b. 1990-1999

In 1991, the Policy for Small, Tiny and Village Enterprises was introduced in the wake of liberalisation. It aimed to replace protection with competitiveness to enable MSMEs to face foreign competition. The importance of providing finance to the sector was realised through the Small Development Bank of India (“**SIDBI**”) and Technology Development and Modernisation Fund.



### c. 1999-2014

The Ministry of MSME came into being from 1999 to make concerted efforts towards the development and promotion of the sector. In 2000, a new policy package was announced to address the persisting problems relating to credit, infrastructure, technology and marketing.

In 2006, these multiple policy efforts culminated in the enactment of the MSMED Act. At its inception, the MSMED Act defined micro, small and medium enterprises in terms of investment in plant and machinery. The concept of “enterprise” was recognised as comprising both manufacturing and service entities.

### d. 2014 onwards

Since 2014, focus has been on digitalisation. In 2017, the MSME Samadhaan Portal was launched to address issues related to delayed payments, allowing MSMEs to file complaints and seek resolutions thereby improving cash flow and financial stability. MSME Sampark is a dedicated job portal that connects job seekers with MSME employers, it aims at bridging the gap between talent and industry needs.

The Udyam Portal has facilitated ease of access for registration of MSMEs. It offers benefits such as simpler access to loans, subsidies and other government schemes. It enhances financial support and operational ease for small and medium enterprises. In wake of the COVID-19 pandemic, the Emergency Credit Line Guarantee Scheme was launched to provide collateral-free loans to MSMEs affected by the same to ensure continuity.

The classification of MSMEs was updated in 2020 in view of changing market dynamics.<sup>7</sup> It is now based on the composite criteria of investment in plant and machinery along with annual turnover.

|                           | 2006 Definition   |  | 2020 Definition  |
|---------------------------|---|--|--|
|                           | Manufacturing   | Service  |  |
| <b>Micro Enterprises</b>  | Investment not more than Rs. 25 lakhs                             | Investment not more than Rs. 10 lakhs                            | Investment not more than Rs. 1 crore<br>Annual turnover not more than Rs. 5 crores     |
| <b>Small Enterprises</b>  | Investment more than Rs. 25 lakhs but not more than Rs. 5 crores  | Investment more than Rs. 10 lakhs but not more than Rs. 2 crores | Investment not more than Rs. 10 crores<br>Annual turnover not more than Rs. 50 crores  |
| <b>Medium Enterprises</b> | Investment more than Rs. 5 crores but not more than Rs. 10 crores | Investment more than Rs. 2 crores but not more than Rs. 5 crores | Investment not more than Rs. 50 crores<br>Annual turnover not more than Rs. 250 crores |

**[Table 1] Source: Ministry of MSME**

The government’s focus on the MSME sector is evident from its forward-looking policies. These policies have aided in development of the sector as an important pillar of the Indian economy.



## II. Growth and Development of the MSME Sector

The concept of cottage industries has been intrinsic to the Indian economy. The importance accorded to promotion of cottage and small industries is evident from the fact that the same has been enshrined as a Directive Principle of State Policy.<sup>8</sup> In the past decades, impetus has been on the formalisation of small-scale industries which has led to the growth of the sector.

### a. Financial performance of MSMEs

MSMEs form the backbone of the Indian economy. They contribute approximately 30% to India's GDP and have created close to 11 crore jobs.<sup>9</sup> Launch of the Udyam Assist Platform has enabled formalisation of MSMEs thereby increasing their access to priority sector lending.

As per the 73<sup>rd</sup> round of the National Sample Survey, there were 633.88 lakh non-agricultural enterprises engaged in various economic activities.<sup>10</sup> The micro sector accounts for more than 99% of the total MSMEs with the small and medium sector having a 0.52% and 0.01% share.

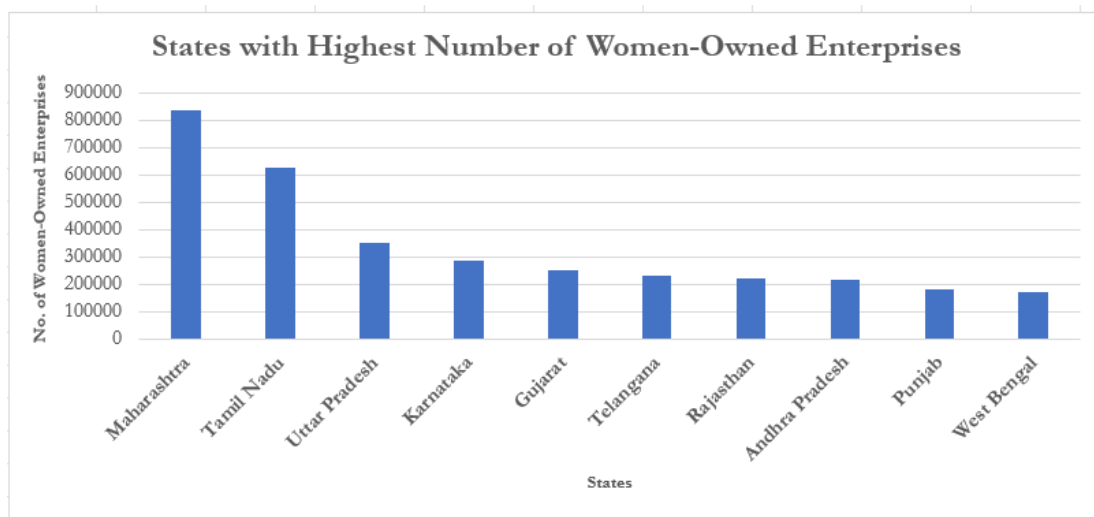
|                | Estimated Number of Enterprises (in lakhs) |        |        | Total % |
|----------------|--|--------|--------|---------|
|                | Rural                                      | Urban  | Total  |         |
| Manufacturing  | 114.14                                     | 82.5   | 196.65 | 31      |
| Trade          | 108.71                                     | 121.64 | 230.35 | 36      |
| Other Services | 102  | 104.85 | 206.85 | 33      |

**[Table 2] Source: 73<sup>rd</sup> round of the National Sample Survey (2015-16)**

The highest proportion of MSMEs were involved in trade related activities followed by other services and manufacturing. An urban-rural distribution is also evident with rural areas accounting for more MSME units than urban areas.

### b. Participation of women in MSMEs

Level of participation of women is essential in determining the success of any economy. In a reply to an Unstarred Question in the Rajya Sabha, it was stated that as on 31 January 2024, women-owned MSMEs constituted 20.5% of the total number of MSMEs registered on the Udyam Portal since its inception in 2020.<sup>11</sup>



**[Graph 1] Source: Rajya Sabha Unstarred Question No. 263 by Shri Masthan Rao Yadav**

These women-owned MSMEs contribute 18.73% to employment generation by MSMEs and involve 11.15% of the total investment. The contribution to the total turnover stands at 10.22%. The Udyam Assist Portal collates information on Informal Micro Enterprises (“IMEs”). According to this, women-owned IMEs constituted 70.49% of the total and their contribution to employment was 70.84%.<sup>12</sup> Thus, it is evident that women-led enterprises continue to operate largely in the informal and unorganised sector.

There is also variation in the participation of women across states. Maharashtra, Tamil Nadu, Uttar Pradesh and Karnataka are the top states with the highest number of women-owned MSMEs. As is evident from the data, women-owned MSMEs constitute less than a quarter of the total registered MSMEs. This indicates the existence of certain barriers to entry for women entrepreneurs in the MSME sector. Lack of formalisation is also evident from the fact that women-entrepreneurs dominate the IME sector.

### **c. Participation of SC/ST/OBC communities in MSMEs**

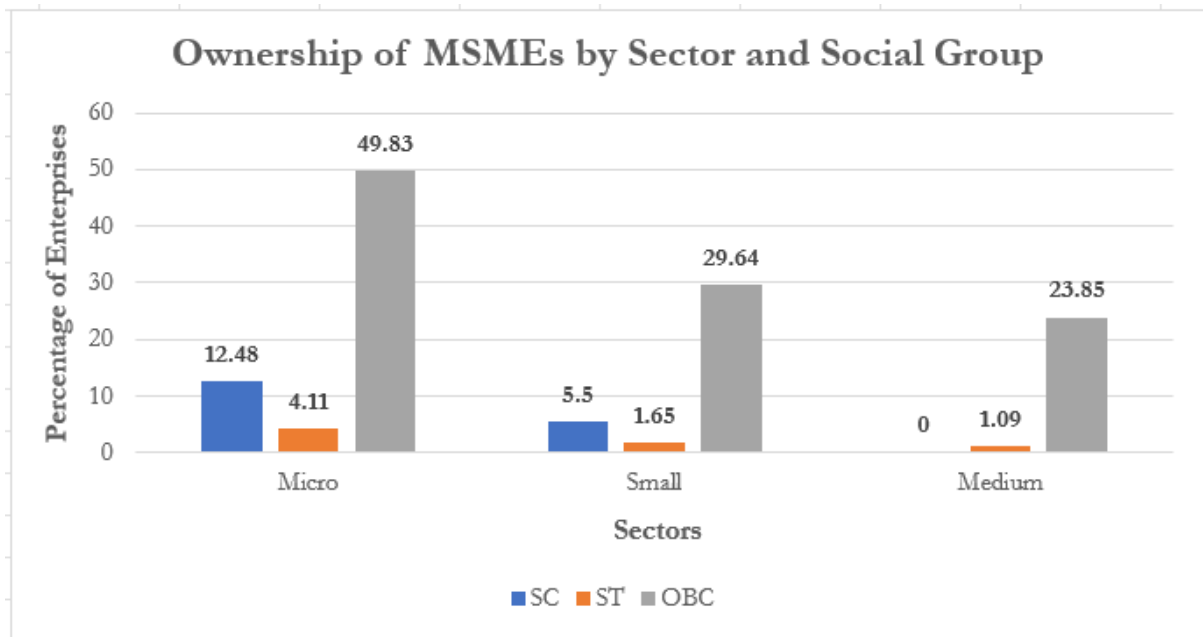
Socially backward groups accounted for ownership of approximately 66.27% of MSMEs. The larger proportion of this is owned by the OBC community which constitutes 49.72% of the ownership. The SC and ST communities are underrepresented with SC and ST owners at 12.45% and 4.10% respectively.<sup>13</sup>

There also exists a rural-urban divide in the number of MSMEs owned by socially backward groups. In rural areas almost 73.67% of MSMEs are owned by SC/ST/OBCs, whereas in urban areas they own about 58.68% of MSMEs.

| Sector | SC    | ST   | OBC   | Others | Not Known |
|--------|-------|------|-------|--------|-----------|
| Rural  | 15.37 | 6.70 | 51.59 | 25.62  | 0.72      |
| Urban  | 9.45  | 1.43 | 47.80 | 40.46  | 0.86      |

**[Table 3] Source: Ministry of MSME Annual Report 2023-24**

A sector-wise analysis shows that the highest ownership was in the micro-sector, with 66.42%. This was followed by the small and medium sectors at 36.8% and 24.94% respectively.



**[Graph 2] Source: Ministry of MSME Annual Report 2023-24**

### III. Challenges faced by the MSME Sector

The government has been taking steps in the right direction for growth of the MSME sector. Despite this however, certain bottlenecks remain that have inhibited MSMEs from reaching their full potential or even exiting business. 50,919 MSMEs shut down their business in the last five years.<sup>14</sup> A closer look at these will be helpful in pinpointing problem areas and look for relevant solutions. The Economic Survey 2023-24 highlights factors such as limited access to finance, markets, technology, digitisation and infrastructural bottlenecks as restricting factors.

#### a. Lack of access to credit

A major issue faced by the MSME sector has been the cumbersome processes in place for accessing credit. This leaves out a large chunk of enterprises from accessing formal sources of credit. The overall credit gap in the MSME sector has been estimated to be approximately Rs. 20-

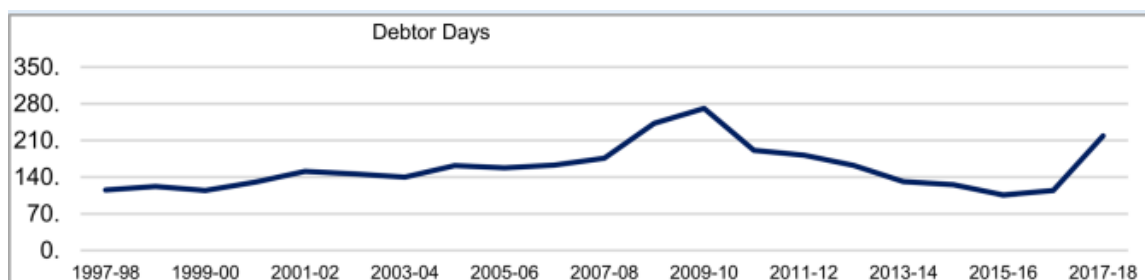
25 lakh crores.<sup>15</sup> MSMEs are also unable to borrow at globally competitive rates due to insufficient affordable financing institutions that focus on MSMEs.<sup>16</sup>

Due to the perceived higher risks associated with the sector, it encounters prohibitive interest rates. The government has focussed on providing collateral-free loans to MSMEs through schemes such as the Prime Minister’s Employment Generation Programme and Credit Guarantee Fund Trust for Micro and Small Enterprises (“CGTMSE”). Despite this, the majority of MSMEs have had to provide collaterals even after being eligible for collateral-free loans. Since 99% of enterprises belong to the micro sector, they typically do not have collateral to offer to banks and are therefore left out of the formal credit sector.<sup>17</sup>

These substantive problems coupled with logistical issues of complex loan processes act as a double whammy. The procedures for applying and securing loans are often intricate and time-consuming. This deters many MSMEs from pursuing formal lines of credit and incentivises resorting to more informal, often expensive, lending sources.

#### **b. Issue of delayed payments**

Delay in payments by buyers is one of the major issues faced by the MSME sector.<sup>18</sup> This has a severe adverse impact on their financial stability and growth. Delayed payments from large enterprises and public sector units create extended payment cycles, leading to cash flow disruptions. As of December 2023, 9589 applications on delayed payments were pending as per the Samadhaan Portal, involving Rs. 8069.7 crores.<sup>19</sup>



**[Graph 3] Source: UK Sinha Committee Report, 2019**

The government brought in the forty-five days rule to tackle this issue under the MSMED Act.<sup>20</sup> This requires all buyers receiving goods from MSMEs to settle their payments within a period of forty-five days. However, enforcement remains an issue and payments still extend beyond the prescribed timeline. MSMEs also do not possess adequate bargaining power to enforce the legal provisions under the MSMED Act.<sup>21</sup> An assessment of the general trend shows that debtor days usually exceed ninety days.

The government has sought to address this by penalising the non-adherence to the forty-five days rule. The Finance Act, 2023 amended the Income-tax Act, 1961 to provide that companies that are late in making payments to MSMEs cannot claim it as an expenditure. They will have to pay tax on it and may claim a refund later.<sup>22</sup>

This rule however, has also had an unintended consequence – buyers have started finding alternatives to MSMEs for supply of goods and services in order to legally circumvent the forty-five days rule. This is because the general industry standard is to complete payments within sixty days. This has led to a loss of business for MSMEs and is the reason that this policy has also faced hesitation from within the MSME sector.<sup>23</sup>

#### HIGHLIGHTS

**Lack of Access to Credit:** UK Sinha Committee estimated the overall credit gap in the MSME sector to be Rs. 20-25 lakh crores.

**Issue of Delayed Payments:** As of December 2023, 9589 applications involving Rs. 8069.7 crores were pending on the Samadhaan Portal.

**High Regulatory Burden:** Typical MSME required to deal with around 364 compliances every year.

**Lack of Adequate Skilling and Job Opportunities:** Only 0.06% of those trained at Tool Rooms and Technical Institutions found jobs.

#### c. High regulatory burden

MSMEs in India face a labyrinth of regulatory requirements, which are often complex and time-consuming. The compliance process involves multiple filings and adherence to various laws and regulations, such as labour laws, tax laws, and environmental regulations. This complexity diverts valuable resources away from core business activities, hindering growth and innovation.

A typical MSME is required to deal with approximately 364 compliances in a year – almost one compliance a day. Out of these, 194 are labour related.<sup>24</sup> The financial burden of compliance is significant for MSMEs. The cost of hiring legal and accounting experts to navigate regulatory requirements can be prohibitive, especially for small enterprises. Additionally, the cost of non-compliance, including fines and penalties, can further strain financial resources.

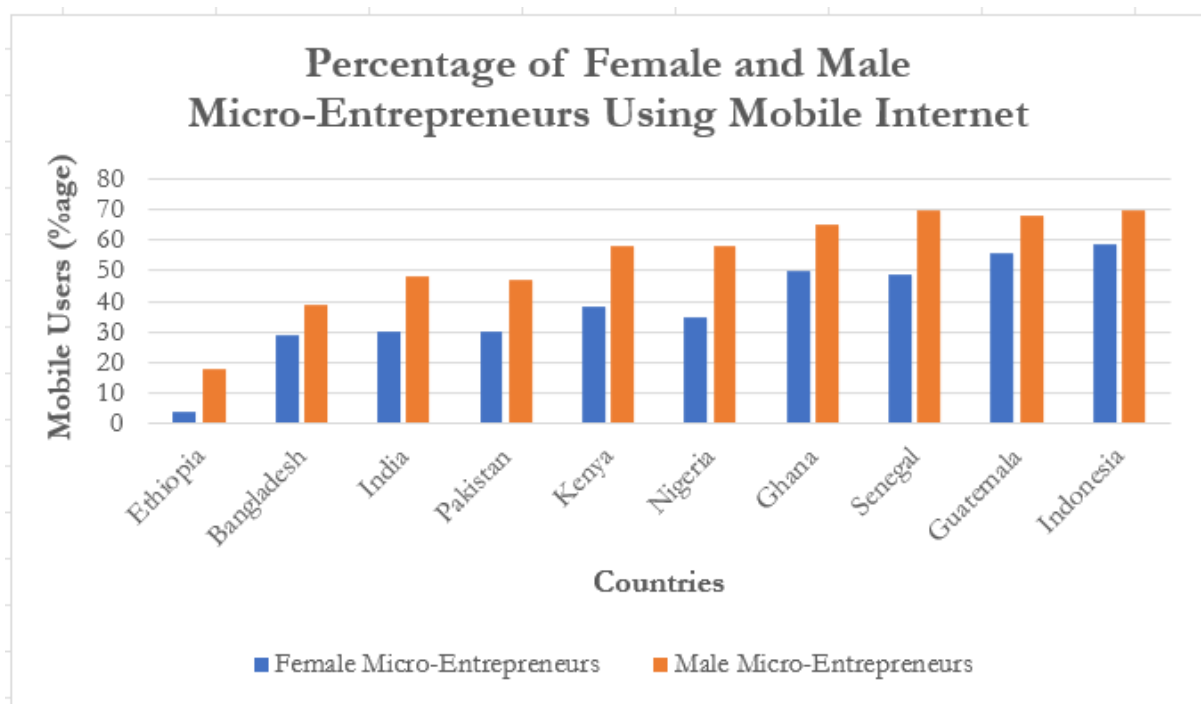
Further, the fragmentation of the regulatory framework across states also contributes to the cumbersome processes. The uneven implementation of regulations across different states and

limited awareness of support mechanisms exacerbates the regulatory burden. This fragmentation creates inconsistencies and uncertainties for MSMEs, making it challenging to operate smoothly.

#### d. Low adoption of technology

Many MSMEs in India struggle with inadequate access to modern technologies and the expertise to implement them. Despite the push for digitalization, a significant portion of MSMEs remain reliant on outdated machinery and manual processes. This lack of technological integration limits their operational efficiency and ability to innovate.

Only about 30% women micro-entrepreneurs and 48% of male micro-entrepreneurs in India use mobile internet.<sup>25</sup> A study by the Broadband Commission Working Group on Connectivity for MSMEs concluded that 85% of enterprises using digital technologies said that they increased sales as a result, and 81% reported that digitisation helped them cut costs.<sup>26</sup> This highlights the importance of access to internet for growth in business of MSMEs.



**[Graph 4] Source: GSMA Report on Understanding Women Micro-Entrepreneurs' Use of Mobile Phones for Business**

The financial burden of investing in new technologies is a significant barrier for MSMEs. The initial costs associated with technological upgrades can be prohibitive, especially for smaller enterprises with limited capital. This financial strain hampers their ability to adopt advanced technological solutions, affecting their competitiveness and growth potential.

#### e. Infrastructural deficiency

The lack of robust physical and digital infrastructure severely impacts the efficiency and productivity of MSMEs in India. Poor quality roads, unreliable power supply, and inadequate telecommunications networks hinder operational capabilities, limiting the ability of MSMEs to compete effectively in both domestic and international markets.

MSMEs face high logistics and supply chain management costs due to inefficient infrastructure. The lack of streamlined transportation networks and warehousing facilities increases operational expenses, making it challenging for MSMEs to maintain competitive pricing and timely delivery of goods and services.

The Economic Survey 2023-24 noted that existing building regulations limit factory usage, reduce land utility and result in unquantified costs. Land remains unutilised while complying with the four building regulations relating to ground coverage, setbacks, parking and floor area ratio.<sup>27</sup>

#### f. Inadequate skilling of MSME workers

MSMEs in India face a severe shortage of skilled labour. The overall skilling level in India is abysmal. According to the Periodic Labour Force Survey 2022-23, 4.4% of the youth in the age bracket of 15-29 years has received formal vocational training while another 16.6% has received informal training. This means that only 21% of the youth of the country is skilled.

Although the MSME sector is a major employer, the retentions in the sector are low. This is because, with a small pool of skilled labour, the competition among different enterprises for the same human resources is high.<sup>28</sup> The institutions such as District Industries Centres which had the potential of playing a capacity building role, have failed to transform themselves from regulatory bodies to facilitating agencies.<sup>29</sup>

| Year    | Trainees trained | Units assisted | Trainees who opted for placement | Total trainees placed (wage and self-employment) |
|---------|------------------|----------------|----------------------------------|--|
| 2023-24 | 2,03,569         | 41,446         | 17,173                           | 11,705   |

**[Table 4] Source: Ministry of MSME Annual Report 2023-24**

The Ministry of MSME has set up Tool Rooms and Technical Institutions (“**TR & TI**”) to provide practical skill development training to unemployed youth and industry workforce. Currently, 18 TR & TI exist throughout the country. The government is running a programme to add another 20 TR & TI at a cost Rs. 3500 crores.<sup>30</sup> However, focus should also be on the output produced by these TR & TI. In 2023-24, over 2 lakh trainees underwent training; out of those only 17,173

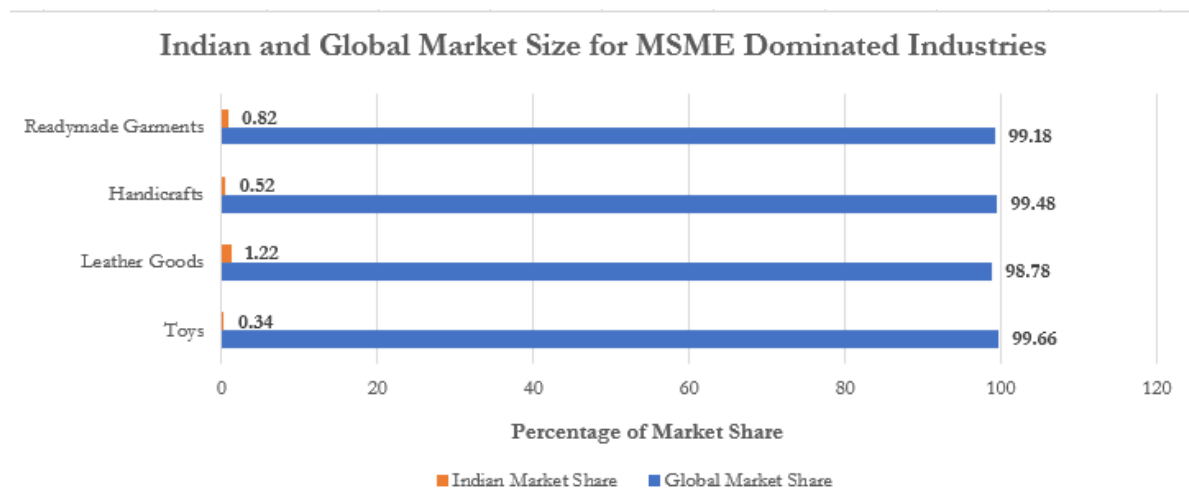
sought placement and 11,705 got placed. This means that less than 0.06% of all those who received training actually became a part of the workforce.

Therefore, the problem exists and needs to be solved at two levels – provision of adequate and quality opportunities for skilling and up-skilling, as well as securing jobs after such training.

**g. Challenges faced by MSMEs in exports**

MSMEs in India face significant challenges when attempting to penetrate international markets. These challenges hinder their ability to grow and contribute to the economy. MSMEs often struggle to access international markets due to limited resources and lack of knowledge about global trade practices.<sup>31</sup> This restricts their ability to expand and compete globally. Despite contributing approximately 45.56% of India's total exports during April-September 2023, MSMEs face barriers that impede their potential for growth.<sup>32</sup>

Tariff and non-tariff barriers significantly increase the cost of doing business internationally for MSMEs. These include high tariffs, stringent quality standards, and complex customs procedures, which can be prohibitive for smaller firms with limited negotiating power and resources.<sup>33</sup> While India has a large population, a large proportion is still economically disadvantaged. This leads to a situation where the effective size of the Indian market is smaller despite its large population.<sup>34</sup>



**[Graph 5] Source: NITI Aayog Report on Boosting Exports for MSMEs**

Inefficient logistics and supply chain management further add to the operational costs for MSMEs. Poor infrastructure and high logistics costs make it challenging for MSMEs to deliver products efficiently and compete with larger firms. The Economic Survey 2023-24 underscores the need for improved infrastructure and reduced logistical costs to support MSME exports.



#### IV. Best Practices and Policy Recommendations

As detailed above, the government policies related to MSMEs have led to enhancement in the growth of the sector but despite sincere efforts, gaps still remain. In this regard, it would be prudent to look at international and national best practices followed to give impetus to the MSME sector.

##### a. Improving access to credit

The problem of access to credit exists on two levels – lack of affordable financing institutions and difficulty in furnishing collateral. On the first, the **United Kingdom** has the British Business Bank which supports small businesses in accessing finance through various programs including guarantees, equity investments and debt funds.<sup>35</sup> In India, SIDBI acts as the apex regulatory body for MSMEs. There is a need to streamline its functions to ensure its effectiveness as an entity that focusses on promoting and financing the development of MSMEs.

On the issue of collateral, the first step should be effective implementation of the CGTMSE and enhancing its coverage to include more sectors and business types. In addition, the **UK Sinha Committee** recommended replacing physical collateral with high trust information on an MSMEs future cash flow-based lending.<sup>36</sup> Thus, adopting a combination of both these approaches would ensure regular credit flow to MSMEs and consequent smooth functioning.



##### b. Resolving the issue of delayed payments

There is a need to review the forty-five days settlement rule in light of industry standards. Thus, proper stakeholder consultations need to be had to ensure that it actually serves the purpose of resolving the issue of delayed payments instead of just hindering business. There needs to be some level of flexibility in the payment cycle to accommodate needs of the buyer and seller. In the

current scheme of things, even in the presence of a written agreement, the payment timeline cannot extend beyond 45 days.<sup>37</sup>

As opposed to this rigid approach, the **European Union's** Late Payment Directive takes the flexible route.<sup>38</sup> A timeline of thirty business days is prescribed for all business-to-business transactions. However, derogations from this timeline are permissible. In commercial transactions between undertakings, parties may agree to a payment term of up to sixty calendar days and in the retail sector, transactions involving the purchase of slow-moving goods may have payment cycles of up to one hundred and twenty calendar days.<sup>39</sup>

The Australian Government's Payment Times Reporting Scheme requires large businesses to report their payment practices to ensure timely payments to suppliers.<sup>40</sup> India too should introduce mandatory reporting of payment practices by large corporations, akin to the Australian Payment Times Reporting Scheme, to enhance transparency and ensure timely payments to MSMEs.

### **c. Reducing regulatory burden on MSMEs**

**Singapore's** regulatory framework includes a single-window system for businesses' registration and compliance, significantly reducing the time and effort required for regulatory processes.<sup>41</sup> India does have initiatives like Udyam Registration, MSME Samadhaan, Startup India Hub, Digital MSME Scheme, and E-Samiksha to streamline MSME registration and compliance. However, these do not yet constitute a fully integrated single-window system like Singapore's framework.

**New Zealand** offers an online business portal that provides comprehensive information and services to simplify compliance and regulatory requirements. India could adopt specific practices like a centralised dashboard, detailed walkthroughs of compliance processes, integrated access to government services and a user-friendly design.

#### **HIGHLIGHTS**

**Improving Access to Credit:** UK Sinha Committee recommended replacing physical assets as collateral with cash-flow based lending.

**Resolving Delayed Payments:** European Union provides some scope of flexibility with its thirty-days payment rule.

**Skill Development for MSMEs:** Germany has dual education system with combines vocational training with apprenticeships.

#### d. Encouraging technology adoption by MSMEs

The **South Korean** government provides substantial grants and subsidies for technology upgrades and innovation in MSMEs through programmes like the Korea Technology and Information Promotion Agency for MSMEs (“**TIPA**”).<sup>42</sup> South Korea’s TIPA is more effective due to its substantial and targeted grants and subsidies, which are specifically designed to support technology upgrades and innovation in MSMEs, making it easier for businesses to adopt cutting-edge technologies.

India could benefit from adopting a similar comprehensive approach by increasing the scale and scope of its existing schemes, like the Technology Development Fund and Digital MSME Scheme, to provide more substantial financial support and tailored assistance for technology adoption and innovation in MSMEs.



#### e. Addressing infrastructural deficiencies

**China** has benefitted immensely from developing numerous industrial parks and special economic zones with state-of-the-art infrastructure to support MSMEs.<sup>43</sup> India can look to develop advanced infrastructure within industrial parks and special economic zones, including high-quality roads, utilities, and digital connectivity.

To attract and incentive MSMEs, there is a requirement to design and allocate specific areas within industrial parks for MSMEs with customised facilities and support services. For MSMEs operating in these zones, substantial incentives and subsidies should be provided. Along with this, comprehensive support services should be established within the zones, such as technical assistance, training, and business development support.

#### f. Skill development with a focus on MSMEs

**Germany** presents a stellar example of vocational training. Its dual education system combines apprenticeships in companies with vocational education in schools, ensuring a skilled workforce for MSMEs.<sup>44</sup> India should also look to foster strong partnerships between educational institutions and MSMEs to ensure that training programs meet industry needs and provide relevant skills.

In addition to this, there is a need to develop structured pathways where students can seamlessly transition from vocational education to apprenticeships within companies. Further, Incentives should be offered to companies for participating in apprenticeship programs, such as tax benefits or subsidies.



#### g. Incentivising and subsidising exports

**United Kingdom** has facilitated trade missions and international exhibitions tailored to MSMEs, providing platforms for them to showcase products and network with global buyers.<sup>45</sup> **South Korea** has established and strengthened export promotion councils that offer targeted support, market insights and trade facilitation specifically for MSMEs.<sup>46</sup>

**Singapore** has streamlined digital export procedures to reduce paperwork and expedite the export processes for MSMEs.<sup>47</sup> **Germany** has enhanced comprehensive export credit insurance to safeguard MSMEs against non-payment risks and encourage international trade.<sup>48</sup>

Some of these processes already exist in India but need to be streamlined and strengthened; such as the One District One Product initiative that looks to market Indian goods internationally. A National Trade Network could be established to minimise transaction costs and address informational asymmetry.<sup>49</sup>

## V. Conclusion

India's economy is driven by MSMEs that continue to drive innovation, generate employment and foster a sense of community. The sector is dominated by micro-enterprises and within that section, nano-enterprises form a major proportion. Nano-enterprises are often defined as those that have an annual turnover between Rs. 10 lakhs and Rs. 1 crore with hyperlocal roots and focus.<sup>50</sup>

The MSMED Act does not recognise the nano-enterprises as a distinct category within MSMEs. However, in reality their needs differ from the micro-sector and this presents a necessity to revisit the taxonomy of MSMEs under the MSMED Act. The focus should be on empowering nano-enterprises through adequate credit and capacity building. In this manner, well-functioning **one million nano-enterprises of one million each** would act as the bedrock for economic growth.

The present report deep-dives into the evolution and development of the MSME sector. It focusses on changing policies and the consequent shifting landscape in which MSMEs have operated since independence. Emphasis is also on the problems currently faced by the MSME sector and the government's initiatives in this regard. An attempt has been made to peruse policies related to MSMEs throughout the world and collate best practices that are well-suited to be adopted in the context of India.

Relaxing collateral requirements for MSMEs, providing flexibility on the forty-five days payment rule and establishing MSMEs within special economic zones are some measures that could provide the required impetus to MSMEs. It is a flourishing sector with immense potential that can be realised with well-timed and well thought out policies that aim at capacity building and ease of doing business. This would enable MSMEs to not only compete with larger businesses but also see themselves transforming into large-scale businesses; thereby boosting the economy and aiding in employment generation.

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## **VII. Acknowledgements**

After spending over three decades in public service, I have embarked on a new journey as a Parliamentarian wherein I intend to drive the discussions on public policy in a positive direction through debates, discussions, and reports on issues of national importance. This primer on the MSME sector is a step in that direction.

None of this would have been possible without the enthusiastic support of the people of Bapatla who elected me to represent them in the Lok Sabha. I am grateful for the faith that they have reposed in me. I am thankful to the members of the august House, both past and present, for asking pertinent questions that have turned out to be a rich source of information in compiling this primer.

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I hope that this primer furthers the important work being done for the promotion and capacity-building of micro, small and medium enterprises in India so that our country becomes a shining beacon for the rest of the world.

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