

## MSMEs: Engines to Achieve Sustainable Development Goals



### Key Message

- India's aim to achieve the Sustainable Development Goals and the targets of Nationally Determined Contributions (NDC) may not be possible if it doesn't amend the trends of jobless growth and serious concerns of environmental degradation.
- It is estimated that, in order to streamline the current alarming job situation, India will need to add 15 million new jobs annually, for the next 15 years. (Bhattacharya, A. and Bijapurkar, A., 2017) India also has a long way to go before it achieves basic living standards for all. In 2011, its poverty-stricken population constituted 20.6 per cent of the world's poorest. (Donnan, 2014) India stands low on the Human Development Index, with a rank of 135 among 187 countries, and with 58% of its population lacking the means to meet essential needs. A growing population and increasing urbanisation have led to a huge increase in consumption demands. This poses a serious threat to the sustainability of the impressive economic growth.
- MSMEs are seen as an important opportunity in the times when policies like Make in India and Startup India are promoting manufacturing and young entrepreneurship in India. It is critical to focus on medium and small enterprises, especially rural social enterprises, as an agent for local economic development. Opportunities lie in exploring how India's policies like Make in India are incentivising local green enterprises.

## Context

India has experienced a steady growth path in the last few years. The recent government estimates indicate that the real Gross Domestic Product (GDP) grew at a rate of 7.1% in 2016-17 (MOSPI, 2017). Much of this growth is attributed to the progress of industrial sectors, such as manufacturing, construction, transportation, communication, utility services, etc., that have been growing at a steady rate. Although rapid economic growth has brought huge benefits to India, it has had a detrimental effect on the country's environment and social frames, exposing urban centres to serious pollution related concerns and rising inequalities emerging from the jobless scenario.

The growing sectors, mainly secondary and tertiary, failed to provide employment to the relatively larger share of workforce, unlike the agricultural sector. Moreover, the GHG emissions accompanying India's fast paced growth pose a significant threat to India's climate change mitigation target of reducing emission intensity of GDP by 33-35% by 2030, as compared to 2005 levels. In addition, because of increased resource and energy consumption, there is also a burden on India's natural resource base and energy requirements. The situation, thus, warrants the need for adopting greener and fairer practices for development.

## MSMEs in India: Scope in the Economy

According to FICCI's estimates, within the manufacturing sector, the Micro, Small and Medium Enterprises (MSME) sector accounts for about 45% of the manufacturing output, 95% of the industrial units, and 40% of the exports. Besides, the sector provides employment to almost 60 million people, mostly in the rural areas of the country, making it the largest source of employment after the agricultural sector. The development of this sector, thus, holds key to inclusive growth, and plays a critical role in India's future. All these parameters contribute towards the potential of this sector to be an alternative source of livelihood for the masses, thereby contributing to the country's GDP.

## Trends: Indian Economy & Sustainability

- According to the 27th Quarterly Employment Survey by the Ministry of Labour, there were 43,000 job losses in the first quarter of FY 2015-2016. **"The economy is generating fewer jobs per unit of GDP"**, says D.K. Joshi, chief economist at Crisil, a ratings and research firm. Illustratively, in manufacturing, if a decade ago, 11 people were needed to execute a piece of work that generated INR 1 million worth of industrial GDP, today only six are needed. He adds, "The economy has become less labour-absorbent."
- A large part of India's growth can be attributed to the **growth of ICT sector**. The sector was predominantly driven by software services; however, most upcoming Indian start-ups in the ICT sector are product-based companies. Although an emerging concept, in this new era, smart devices assume major control over manufacturing and distribution functions in the economy. This has distorted various traditional economic sectors – agriculture, tourism, transport and services.
- **Goods and Services Tax (GST)** is the new unified tax regime introduced in the country. Local stakeholders have voiced against the implementation of GST, calling it as an act that will put rural enterprise in further distress. Lokavidya Jan Andolan, a civil society platform, says - "Industrial (large scale) producers and service-providers will obviously benefit from this 'no-boundaries' market system, where buying and selling has been freed from the 'limitations and vagaries of localities and geographies'. Small producers/service-providers have been forced to participate in this market system, most often on very adverse terms of trade. We demand for no-tax/zero-tax on handmade produce and services (which permits for inclusion in the all-India market system)."





## Trends in MSMEs Sector

- Most of the MSMEs still prefer to undertake renovation and modernisations from either fund generated internally, or borrow from informal financing channels. As per the statistics compiled in the fourth census of MSME sector for registered units (April 2011), only about 11.7 per cent of MSMEs availed finance from institutional sources, and about 1 per cent had taken finance from non-institutional sources.
- A recent report by the National Skill Development Council of India forecasts that there could be an incremental shortfall of 240-250 million people by 2022, in 20 high growth sectors of the Indian economy, and in the unorganised segment. Over 13 million people are required every year in 90 skill categories. So, while 12.8 million youth enter the job market every year, the annual current capacity for vocational training in India is just around 4.3 million. A mere 2% of Indian workers are formally skilled. In the current situation, as MSMEs are the biggest generators of employment in the country, it is necessary to reduce skill gaps amongst MSMEs to promote the concept of inclusive growth. (CII, 2011) This gap in skills is corroborated by the ADB study. More than 85% of innovative small and medium firms see the unavailability of skilled workers as a barrier to innovation, making it one of the foremost challenges in SME innovation. (Pachouri & Sharma, 2016)
- Timely access to valuable information is critical for SMEs to gain strategic advantage in pursuing innovation. The information barriers are with respect to access to information on technology and markets. More than 75% of the innovative small firms, and 86% of the medium firms, face barriers pertaining to technology information and information on markets in India. (Pachouri & Sharma, 2016)

## State of MSMEs – Macro Perspective

India is still ranked 130th globally in the World Bank's ease of doing business index for 2015, which reflects the burdensome regulatory environment in which SMEs operate. The high costs involved in meeting a large number of regulatory requirements tend to negatively affect the innovation capacity of the firms. The Government of India looks at small and medium enterprises (SMEs) under the Micro, Small and Medium Enterprises Development Act 2006, which seeks to develop and enhance the competitiveness of MSMEs as a whole. In the act, for the first time, the concept of "enterprise" has been made to include both manufacturing and services firms. Also described in the act, for

the first time, is the concept of "medium" enterprises. The MSME ecosystem is administered through the Ministry of Micro, Small and Medium Enterprises, which has, broadly speaking, two major divisions. These include the Small and Medium Enterprises division, and the Agro and Rural Industries division.

Available data from the Fourth All India Census of MSME in 2006-07 indicates that around 60% of these enterprises are based in rural areas of the country, and 45% of the total manufacturing output is contributed by the MSME sector. The share of MSME sector in the total exports of India is about 40%. (Das, 2017)

## MSMEs in India: What's in the definition?

The recent announcement by the Ministry of MSMEs revised the definition of MSMEs in India. It now classifies MSMEs on the basis of their annual turnover, as against the earlier classification based on investment in plant and machinery for goods companies, and in equipment for services firms. It is of great importance that MSMEs are distinguished from other firms, so that the economy can accurately target policy interventions to address the special needs or disadvantages or a special contribution to the economy of such MSMEs.

Keeping this in mind, let us compare the recent definition of MSMEs by the Government of India, with the standard definition used by International Finance Corporation (IFC)<sup>1</sup> (IEG: World Bank, IFC and MIGA, 2012) and European Commission (EC)<sup>1</sup>. (Berisha & Pula, 2015) (Refer Table 1)

TABLE 1: Definition of MSMEs – A Comparison			
MSMEs	Micro	Small	Medium
Annual Turnover (new definition)	Less/equal to INR 50 million	INR 50 million – INR 750 million	INR 750 million – INR 2.5 billion
Annual Turnover* (IFC definition)	Less/equal to INR 6.5 million	INR 6.5 million – INR 195 million	INR 195 million – INR 975 million
Annual Turnover# (EC Definition)	Less/equal to INR 160 million	INR 160 million – INR 800 million	INR 800 million – INR 4 billion

\*1 Dollar = 65 INR #1 Euro = 80 INR

The new definition is definitely a step forward towards using the criteria that is more commonly used at a global level to define MSMEs – Annual Turnover. However, diving deeper, two observations can be made. **First**, the definition of each category (micro, small and medium enterprises), as per the new Indian definition, is too broad as compared to the IFC global definition. This is especially true for the case of micro enterprise. Policy and market support systems for micro enterprises are particularly different, and it is critical that the category of micro enterprises is not shadowed by 'bigger' enterprises. **Second**, most of the countries and international bodies, like IFC, EC and World Bank, use the number of employees as one of the core criteria to define MSMEs. A third of the 132 economies studied by World Bank and IFC in 2010, defines MSMEs as ones having up to 250 employees. (Kushnir, Mirmulstein, & Ramalho, 2010) It is of critical importance for India to consider these concerns in the new definition of MSMEs, for ensuring better targeting of enterprises at the bottom of the pyramid.

## MSMEs: Engines to Achieve Sustainable Development Goals – How?

Bold new approaches are needed to meet the global challenge of overcoming poverty and achieving the Sustainable Development Goals in the face of growing threats from ecosystem decline and climate change. There are many cases from across India that corroborate the role of MSMEs in providing poverty and environment solutions while building a resilient economy.

### *Local economic development results in more jobs being created, particularly benefiting the poor*

MSMEs in India provide employment to almost 60 million people, mostly in the rural areas of the country, making it the largest source of employment after the agricultural sector. As a contribution to economy and development, MSMEs **develop economies at the local level** – especially providing jobs and livelihood opportunities to the lower economic strata of the society. In this way, these play a major role in including the poor and the marginalised in the mainstream development model. MSMEs also bring **value addition** at the local level, unlike big businesses where most of the value addition is at the end of the value chain, thus building the value of shared prosperity in practice, and addressing inequities. In this way, MSMEs directly contribute to various socio economic SDGs, like SDG 1 (No poverty), SDG 8 (Jobs and growth) and SDG 10 (Reduce inequalities). By developing basic needs service delivery models in rural areas, MSMEs have the potential to contribute to SDG 6 (Water for all) and SDG 7 (Energy for all), among others.

[Dharani Farmers Producer Company](#) and [Sittilingi Organic Farmers Association](#), through local value addition of organic agriculture produce, are able to provide direct income benefits to the small holder farmers and marginalised communities in southern India.

### *MSMEs bring diversity of business and risks, and thus strengthen resilience of the economy*

The Micro, Small and Medium Enterprises (MSME) sector accounts for about 45% of the

manufacturing output, 95% of the industrial units, and 40% of the exports. What is more important is that micro, small and medium enterprises (MSMEs) have demonstrated considerable strength and resilience in maintaining a consistent rate of growth and employment generation during the global recession and economic slowdown. **Clusters of small businesses** build more diverse economic models in comparison to big businesses. This is critical in building resilience of the system.

With the advent of industrialisation, the crafts and handicraft sector has suffered losses in its economy. Traditional crafts have largely been marginalised by mass-produced machine-made consumer goods, which tend to be cheaper due to the economies of scale associated with mechanisation. In such a time, entrepreneurial initiatives, like [Dastkar](#), [Saathi Samaj Sevi Sanstha](#) and [Mithan Handicraft Development Private Limited](#), are playing a critical role in sustaining the sector and the livelihoods of people, mostly the poor and marginalised, associated with the handicrafts sector.

### *Environmentally conscious MSMEs ensure green and inclusive economic development*

MSMEs are usually dependent on the **locally endowed natural resources**, and are therefore environmentally conscious. The ownership of natural resources is high in local green enterprises, as the communities are dependent on the resources for their sustenance and livelihood. So, the design of the MSMEs impacts various ecological SDGs – SDG 13 (Combat climate change), SDG 14 (Water ecosystems) and SDG 15 (Terrestrial ecosystems). Various innovations in MSMEs can show the path towards achieving SDG 12 (Sustainable Consumption and Production).

Increasing generation of waste is one of the major environmental and social concerns. Some MSMEs have seen this as an economic opportunity. [Daily Dump](#) has innovated a business model for composting of solid waste at the household level, while [Green the Gap](#) is using waste to make marketable products.



## Union Budget 2018 and the Gain-Pain Points for Green MSMEs

The Union Budget 2018 extended sops to MSMEs, with the cut of corporate tax rate of 25% for companies with an annual turnover of up to INR 2.5 billion, as one of the major highlights. Some other key announcements include:

### Credit and incubation support

- INR 3 trillion (2018-19) under *Pradhan Mantri Mudra Yojana* or Mudra scheme.<sup>1</sup> (Bhaskar, 2018)
- Allocation under Prime Minister Employment Generation Programme has gone up from INR 10.24 billion (2017-18) to INR 18 billion (2018-19) for generating *self-employment* opportunities through the establishment of about 88,000 micro enterprises in the non-farm sector.

### Technology upgradation

- Allocation for *National Manufacturing Competitiveness Programme* has gone up from INR 5.06 billion (2017-18) to INR 10.06 billion (2018-19).

### Sectoral incentives: (Press Information Bureau, 2018)

- Allocation under *Khadi Grant* has been enhanced significantly from INR 2.65 billion (2017-18) to INR 4.15 billion (2018-19).
- Under *Scheme for Fund for Regeneration of Traditional Industries (SFURTI)*, the budgetary allocation has increased from INR 100 million (2017-18) to INR 1.25 billion (2018-19). This will give an unprecedented boost to employment generation in the traditional and rural industries.
- The allocation under *ASPIRE (A Scheme for Promotion of Innovation, Rural Industry and Entrepreneurship)* has been raised from INR 500 million (2017-18) to INR 2.32 billion (2018-19), with an aim to set up 100

livelihood business incubators and 20 technology business incubators.

- Textile, bamboo and fisheries are some of the other sectors that have received special allocations.

## Take Aways

The Union Budget 2018 is surely a big leap towards creating an enabling ecosystem for MSMEs in India, especially the tax cut and credit support initiatives of the government. However, for these MSMEs to contribute effectively in building a greener and inclusive economy, and to support India in achieving SDGs, some points need to be considered:

**Rural entrepreneurship** in the country provides triple benefits of poverty eradication, economic and livelihood resilience, and provision of (basic) goods and services to the rural population of the country. It is, therefore, very critical for the Government of India to incentivise the set up and sustenance of such local enterprises in rural India. Currently, it holds a portfolio of INR 2.32 billion (ASPIRE) of the total INR 65 billion budget for MSMEs.

There is limited attention to **greening the MSMEs** in the Union Budget 2018. MSMEs are one of the core engines of the Indian economy, and are projected to grow further in the coming decade. MSMEs, especially manufacturing sector enterprises, are particularly resource intensive and emit high quantum of pollution and carbon emissions. For India to fulfil her international commitments (Nationally Determined Contributions and Sustainable Development Goals), it is of high importance to invest in greening the current MSMEs and promoting green MSMEs in future. For this, India needs to focus on technology and market innovations, on one hand. On the other hand, India needs to identify economic sectors where there is a huge need and a high potential for setting up MSMEs. Some such upcoming sectors are waste, eco-tourism, decentralised renewable energy and organic agriculture based enterprises.

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<sup>1</sup> The MUDRA scheme was founded with the motto of “funding the unfunded” by extending financial support, including refinancing, to the micro segment of the economy.

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### About Development Alternatives Group [www.devalt.org](http://www.devalt.org)

Development Alternatives (DA) is a premier social enterprise with a global presence in the fields of green economic development, social equity and environmental management. It is credited with numerous technology and delivery system innovations that help create sustainable livelihoods in the developing world. DA focuses on empowering communities through strengthening people's institutions and facilitating their access to basic needs; enabling economic opportunities through skill development for green jobs and enterprise creation; and promoting low carbon pathways for development through natural resource management models and clean technology solutions.

### About Green Economy Coalition

The Green Economy Coalition (GEC) is the world's largest movement for green and fair economies. An alliance of more than 50 civil society organisations, trade unions, businesses and campaigners, the GEC takes a holistic systems approach to tackling some of the biggest challenges of today: extreme poverty, climate change, biodiversity loss, rising inequality, and weak governance. The GEC believes that these issues cannot be tackled alone. They are symptoms of an economic system that is ill-equipped to respond to today's global challenges, and require systemic economic reform to address.

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