ORF ISSUE BRIEF

AUGUST 2015 ISSUE BRIEF # 101

Pushing India's Small-Scale Industries to the Economic Forefront

Shruti Gupta

Introduction

India currently stands on the brink of being reckoned as the fastest growing economy in the world: In 2016, its projected growth rate is 7.6 percent. Prime Minister Narendra Modi's flagship 'Make in India' programme is expected to herald India into its era of growth. This lion of a campaign—which aims to boost the manufacturing sector—has roared defiantly in both the domestic and international arena and promises economic development.

India's demographic dividend is considered to be its biggest asset. It also is, however, a potential liability: With more than 65 percent of the population below the age of 35, the looming danger of unmanageable unemployment hangs heavy. Over the last few years, the services sector has carried the burden of economic growth; however, with its 64.8-percent share in the GDP, the services sector accounts for only 26.8 percent of employment.[1] What is thus crucial for the 'Make in India' initiative is employment generation for the 12 million individuals entering the workforce every year. Further, the hourly labour wage in India is estimated at $1.46 as against the $1.74 wage rate in China.[2] This opens a huge window of opportunity for India to attract investments which will in turn spur on domestic manufacturing.

It has become an imperative, given how manufacturing growth has stagnated in the last few years. The sector's current contribution to GDP is 16 percent. Its share in export is abysmal, with exports being dominated by skill-intensive industries such as automobiles and engineering goods. Such performance in manufacturing is in stark contrast to those of countries like China, Japan, and

Germany. China, for example, contributes 13.7 percent to world manufacturing; India contributes less than 2 percent. The need of the hour is to push the manufacturing sector on the path of competitiveness and competency.

While 'Make in India' is a laudable initiative, there is a more specific task for policy-makers: The field of vision needs to be narrowed to small domestic players who define the nation's manufacturing landscape. The micro, small and medium enterprises (MSMEs) currently employ 12 crore individuals and contribute 15 percent to GDP.[3] With its growth rate outpacing that of the Indian economy, small-scale businesses yield the power to transform the socio-economic architecture of the country. However, these small-scale industries have been long ignored in spite of their contribution to the Indian economy. Such situation is uninformed, given that small-scale industries have the potential to be the backbone of economic growth through appropriate institutional and statutory mechanisms which may be accorded them.

Since the Modi government came to power in May 2014, efforts have been made to bring MSMEs to the forefront of the economy. The focus has been on addressing problems that weaken the foundation and hamper the growth of these industries, primarily, credit, marketing and inefficiency. This paper focuses on the initiatives launched to help small-scale industries achieve the projected growth rate of 25 percent by 2022, along with areas in which policy interventions are necessary.

Funding the Unfunded

The growth and development of MSMEs across the country has been stunted due to the lack of available financial facilities. The two formal sources of credit for small business are corporate banks and micro finance institutions (MFIs). But small-scale enterprises face a quandary: they are considered too small and thus risky by corporate lenders, yet they are too large for most MFIs. Only four percent of small businesses end up falling within the purview of the Indian banking system. The remaining enterprises are established on the brink of the formal banking system, giving them no alternative but to avail financing from moneylenders who charge exorbitant interest rates.

In an attempt to achieve the national imperative of financial inclusion, the Modi-led NDA government announced the creation of the Micro Units Development Refinance Agency (MUDRA) Bank in March 2015. The role of the Bank centres on refinancing as well regulating MFIs. It will have an initial corpus of INR 20,000 crore and a credit guarantee corpus of INR 3,000 crore. As announced at the launch of the MUDRA, it will provide finance to banks and other financial institutions at 7 percent. While the interest charged to the end borrower will depend on the risk margin of the institute, it will certainly push down the interest rate charged currently which averages at 23 percent.[4] The Bank also aims to mould its financing as per the growth stage of the MSME. Previously, all financial assistance revolved around either promoting an industry, product or developing a specific capability. The three stages of development of a business have been identified, namely: *shishu; kishor;* and *tarun*. As the needs of small-scale entrepreneurs vary significantly from one stage to another, this financing model is expected to enable a more sustainable and holistic growth.

The second task of the MUDRA is regulating MFIs operating across the nation. This topic has been the centre of debate following the Andhra Pradesh crisis of 2010. The lack of regulation of MFIs in the state led to high interest rates and the coercion of borrowers, leaving them in deep desperation; over 50 borrowers were reported to have committed suicide in the aftermath of the crisis. This spurred the government to enact the Andhra Pradesh Micro finance Institutions (Regulation of Money lending) Act. While the intention of the government was to protect the interests of entrepreneurs, recovery rates in the state plummeted, resulting in extensive downsizing and closure of MFIs. It is therefore imperative that the MUDRA draws the fine line between under-regulation and over-regulation to safeguard the ambitions of both small-scale businesses as well as MFIs.

The MUDRA is still in its infancy and its objectives remain unclear. What is known is that currently, the MUDRA Bank's objectives overlap with those of the Small Industries Development Bank of India's (SIDBI), leading to doubts about the need for a new bank. Questions are being asked whether instead, restructuring of the SIDBI, a higher budget allocation and introducing more relevant schemes, could help solve the inherent problems faced by the country's MSMEs. Further, the Bank as a regulator and a refinancer of MFIs has attracted criticism from various fronts. If the Bank's roles are not clearly defined, it might not only prove inutile but can, potentially, do harm by replicating the Andhra Pradesh crisis on a national level. During the launch of the bank, the Finance Ministry talked about the government's aim to introduce it as an Act of Parliament. By emphasising that the Bank will have legal basis, it wished to instil confidence in the concept of the MUDRA Bank.

Increasing Efficiency in Registration

Since India slipped in ranking from 140 in 2014 to 142 in 2015 in the 'Ease of Doing Business' study, removing impediments in setting up and running a business has been high on the agenda of the Modi government. As things stand, it takes 30 days to start a business with nearly 13 procedures and clearances to be obtained.[5] The procedure is time consuming and involves extensive red tape and therefore, deters entrepreneurs from registering their units. Further, for example, the registration of MSMEs requires the entrepreneur to obtain the ownership/tenancy rights of the premises of operations. In the case of Delhi, for example, many MSMEs are located in Lal Dora districts, making it highly difficult to obtain the requisite clearances from the Municipal Corporation.

The registration procedures for small-scale industries is under the purview of the State Directorate, Commissioner of Industries and District Industries Centres. The registration of these businesses is on the basis of product as well as region. The business is required to register once before commencement, and another time thereafter through filing of the Entrepreneurs Memorandum.

In order to boost the setting up of MSMEs, the policy of registration of these enterprises has been centred on the themes of 'easy', 'speedy', and 'encouraging'. The introduction of the Entrepreneurs Memorandum as part of the Micro, Small and Medium Enterprises Development (MSMED) Act, 2006, liberated the entrepreneurs from the hurdles of registration of enterprises required under previous policy regime.[6] Unfortunately, the approach adopted by policy-makers was not on increasing efficiency of the registration agencies or cutting down on redundant approvals sought. The registration of small-scale industries was made voluntary, leaving existing and proposed small businesses with no statutory basis.

While in principle, the voluntary registration procedure encourages budding entrepreneurs, it deprives them of one fundamental right: that of availing benefits and policy measures introduced by the government for their benefit. Thus, the INR24,124-crore allocation to MSMEs in the 12th Five-year Plan is expected to benefit only the registered MSMEs, which account for only five percent of the total.

Moreover, limited information is available regarding the unorganised sector of MSMEs. Available information date back to 31 March 2007 and a sample survey methodology was adopted for enumeration purposes. In addition, activities under seven sectors such as wholesale/retail trade, legal, educational, and social services, are not included. Therefore, policy-makers do not have sufficient information regarding the operations and problems faced by the unorganised sectors. To counter the issue, INR100 crore have been allocated in the 12th Five Year Plan for promoting online filing of the Entrepreneurs Memorandum.[7] While it aims to slowly bring the informal sector under the umbrella of the formal sector, progress has been excruciatingly slow.

Upgrading Infrastructure

The physical and knowledge infrastructure of micro, small and medium enterprises is crumbling due to obsolesce and global competition. These enterprises are established as part of industrial corridors or on the periphery of urban settlements. Due to the poor planning of industrial corridors, small-scale enterprises do not have the option to expand their operations. In the case of urban establishments, there is inadequate electricity, water and transport facilities. This increases the cost of production, making it impossible for MSMEs to compete in international markets or become an integral part of the global value chains.

To give credit where it is due, the government over recent years has undertaken several measures to improve the infrastructure for small-scale enterprises. The primary focus has been on cluster development undertaken through initiatives such as the Industrial Infrastructure Upgradation Scheme (IIUS) and Integrated Infrastructural Development (IID) Scheme. While the IIUS focuses on upgrading existing identified clusters, the IID aims to establish as well as upgrade micro enterprises in rural and urban areas.[8] The government did live up to its promise of creating and upgrading enterprises with the requisite physical amenities. There have been several issues, however, with regards to implementing the schemes. First, majority of these clusters suffer erratic power supply, resulting in many idle and unproductive hours in the workplace. Second, inadequate water supply leaves them reliant on water tankers, which substantially increase the cost of production. Third, the progress of upgradation has been slow due to which only a small percentage of small-scale enterprises have benefited from these schemes.

To address the problem of electrification, the Prime Minister has launched the Deen Dayal Upadhayaya Gram Jyoti Yojana (DDUGJY), an ambitious scheme that aims to provide 24x7 power to small-scale businesses located in rural areas. The scheme draws inspiration from the Gujarat electrification model. The proposal to segregate the feeder for agricultural and non-agricultural undertakings and strengthening the sub-transmission, and distribution infrastructure through metering will reduce the peak load enabling uninterrupted power supply.

The need for knowledge infrastructure has become more pronounced in recent years with the emergence of global and domestic value chains. Due to the reduction of tariff barriers leading to increased competition, the requirement to develop a niche market or product has gained prominence. Through their expertise, knowledge clusters are leaders in innovation and invention. India has several knowledge clusters in operation under the patronage of the Indian government as well as international agencies. However, for Indian MSMEs to infuse themselves into the global value chain they have to develop a more comprehensive network of domestic value chains along with expanding and upgrading their knowledge clusters continuously.

As illustrated earlier, the government has recognised the need to develop and upgrade MSME infrastructure. However, schemes introduced over the years have been fragmented and tend to address problems in isolation. The DDUGJY is a significant move to recognise and address the fundamental problems facing small-scale industries. But no effort has been made to solve other issues like water, logistics, and waste management. It is time that the Ministry of Micro, Small and Medium Enterprises undertakes cluster mapping to approach the problems of small-scale enterprises holistically so as to ensure sustainable growth and development of these enterprises.

Way Forward

The Modi-led NDA government's social and economic rhetoric has so far been defined by catchphrases which have gained unprecedented public support. These were initiated through *'acche din aane wale hai'* and propelled by the *'sabka saath sabka vikas'* campaign. Subsequently, numerous schemes were launched which focus of the lower strata of the economic pyramid. While each campaign focuses on a fundamental socioeconomic issue, they have all been launched independent of each other.

In order for the 'Make in India' campaign to achieve its objectives, other campaigns, primarily 'Skill India', 'Digital India' and 'Smart Cities', need to be brought under its umbrella. A majority of MSMEs are run by first-generation entrepreneurs who lack technical and managerial competencies. Through skilling initiatives, these small-scale businesses can be the face of the Indian manufacturing unit on the global stage. The 'Digital India' scheme, for example, can have a profound impact on the functioning and productivity of small-scale industries. The visionary objective of the programme will digitally empower every individual to gain easy access to government services. By easing the process of registration, setting up and running businesses, it will act as an incentive for budding entrepreneurs to in fact *make in India*. Further, urban planning which will be done under the banner of the 'Smart Cities' programme should be mindful of the needs of small-scale businesses and their integration into these settlements.

Further, India witnessed the highest surge in the agricultural population in the world between 1980 and 2011.With nearly 80 percent of farmers being small and marginal, and agriculture growing at 1.1 percent (2014-15), the onus of robust economic growth falls on the shoulders of the manufacturing sector.[9] The urgency to generate alternative employment opportunities in non-agricultural avenues can be met by appropriately incentivising micro, small and medium enterprises. This in turn will further strengthen the potential of the country's demographic dividend.

India's small-scale industries have in recent years been starved of policy reforms and initiatives. It is said that the lion runs fastest when it is hungry: If tweaked, the 'Make in India' campaign can feed the growth potential of India.

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Endnotes:

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ABOUT THE AUTHOR

Shruti Gupta is a former Research Intern at ORF.

Observer Research Foundation,
20, Rouse Avenue, New Delhi-110 002
Phone: +91-11-43520020 Fax: +91-11-43520003
www.orfonline.org email: orf@orfonline.org