

MSMEs in India: Sectoral and Subsectoral Strategies

ISED Discussion Paper

by
ISED Small Enterprise Observatory
jointly with
ISED Centre for Enterprise Development



Institute of Small Enterprises and Development

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Institute of Small Enterprises and Development
ISED House, ISED Enclave, ISED Road,
Cochin-682 028, India
URL: www.isedonline.org
Email: info@isedonline.org



ISED Small Enterprise Observatory
ISED House, ISED Enclave,
ISED Road, Cochin - 682 028
URL: www.isedonline.org
Email: seo@isedonline.org

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About 'ISED Discussion Paper' Series

This monograph forms part of the '*ISED Discussion Paper*' series of the Institute. Brought out by ISED Small Enterprise Observatory (ISED-SEO), the Institute's knowledge platform, titles under this Series are meant to offer a platform for discussion on some of the latest developments in the economy and society. The contents of this document may be used for debates and discussions, as also for preparation of course materials, but with due acknowledgement only.

Preface

The economic reforms era in India is also marked by a development strategy for the MSME sector. The focus, progressively has been on value chains and inter sectoral linkages. However, there is no doubt that, in order to remain sustainable,, innovation is the only way forward. In this context, public policy need to show the way of having the right mix of individual efficiency and collective efficiency strategies. Seeing both the woods and the trees, in their respective roles, is the need of the times. A subsector approach is a useful analytical and operational approach that can guide both policy and practice.

The purpose of this Discussion Paper is to bring to light some of the least known aspects of the subject. It is also meant to initiate a wider discussion on the subject so that it may contribute to public policy dialogue and strategies.

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Cochin

February 23, 2017

P.M.Mathew

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Abstract

A proper understanding of business demography is a sine qua non for development of meaningful enterprise development. The industrial and enterprise development strategies during the economic reforms era has been marked by a progressive focus on value chains and inter-sectoral linkages. However, there is no doubt that, in order to remain sustainable, innovation is the way forward. In this context, public policy need to show the way of having the right mix of individual efficiency and collective efficiency strategies. A subsector approach is a useful analytical and operational approach that can guide both policy and practice. Based on their broad features, one can distinguish four subsector categories among MSMEs in India: legacy subsectors, manufacturing subsectors, New Economy subsectors, and triple bottom line subsectors. These subsectors have their specific role and relevance in the national and regional economy. The task of public policy and strategy is to identify their specificities, and to develop action programmes accordingly.

Key words: subsector approach, legacy subsectors, manufacturing subsectors, New Economy subsectors, 'triple bottom line' subsectors

1.0. Introduction

Size-based categorisation of enterprises is often considered as a convenient method of understanding and analysis, and thereby to target public programmes and to measure their impact. While, from the point of view of programme implementation, this offers some convenience, for analytical purposes, the results often get blurred, or become mechanical. For meaningful policy making, there need to be an understanding of SMEs as part of a 'total system', rather than as stand alone entities. The purpose of our discussion here is to offer 'subsector' as an alternative analytical approach for understanding and analysing the MSME space in the Indian context. The discussion also specifically looks into the relevance of this approach in the context of the emerging paradigm of globalisation, where MSMEs show an enhanced tendency of getting vertically and horizontally integrated. Global value chains are decisive in shaping their destinies. Where are these enterprises placed in the global value chain? How are they impacted by the changes in tastes and preferences of consumers globally? Beyond stand-alone concepts and entities, a subsectoral understanding and analysis of enterprises can offer meaningful answers to these questions.

2.0. Conceptual Framework

The term 'subsector', in India, is both a system as well as an analytical approach. A "subsector" does not refer to a component of an individual sector of the economy. It includes a set of economic activities that cuts across several sectors, traditionally agricultural, industrial and commercial sectors, and now electronics and I.T. The term 'subsector' can be approached as: 1) a set of activities; 2) related set of rules governing those activities; 3) a conceptual way of viewing problems of economic organisation; and 4) a way

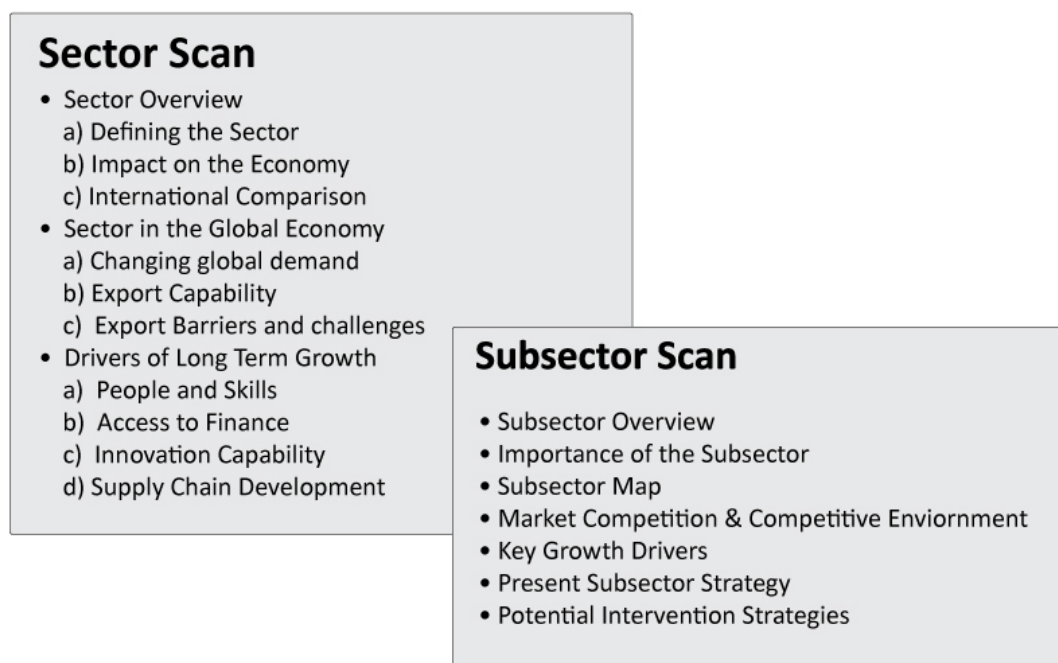
of organising research. The 'subsector approach' is a "systems" approach to the study of economic activity, where, the emphasis is on the interdependence of economic units, particularly those involved in the process of production and distribution. Interdependence plays a central role in understanding the dynamics of change and evolution. It can also be used as a tool for comparative static analysis, examining the implications of alternative development patterns, policy changes, or project interventions. In short, it enables a particular enterprise activity to be seen and analysed in terms of its totality, and thereby, making policy and strategies easier.

There are five key concepts behind any subsectoral analysis: 1) verticality; 2) effective demand; 3) coordination with channels; 4) competition between channels; and 5) leverage. Subsector performance has various dimensions: 1) approach to efficiency, equality, and progressiveness; 2) synchronisation of exchange efficiency and transaction cost; 3) adaptation dynamism; 4) progressiveness; and 5) access to market and to information.

3.0. Sub-sector in the MSME Context

MSMEs have the increasing compulsion of being part of the global value chains. As manufacturing is increasingly becoming global, MSMEs need to equip themselves well with particular subsectors, as part of the corresponding value chain. Manufacturing today requires a logic built around a subsector for its sustainability and growth. The various functions of manufacturing, on the other hand, should meet the associated supply chain requirements.

Manufacturing, today, is increasingly driven by knowledge. An understanding of the knowledge economy, as it emerges, is crucial in this context. While the subsector approach does not provide a universal answer to all the

Figure 1: Sector Scan & Subsector Scan

Source: ISED Small Enterprise Observatory

problems of MSME research, it offers by stratification, a better explanation for the complexities of the global value chains as they emerge, and their relevance to the context of MSMEs.

The Economist, London, in its March 3, 2012 issue kick-started a debate on the relevance of SMEs in the context of the present global economic crisis. The Journal hypothesises that “small firms are a big problem” in Europe today. In the Euro zone, SME-dominant countries like Greece and Spain have failed to grow because of high regulations. Italy’s small-firm bias derives in part from a reverence for family firms. Only 19 per cent of Portuguese manufacturers have 250 or more workers, compared with 55 per cent of industrial firms in Germany. Thus, unless

one spotlights on the country’s geo-political background against the larger global background, one cannot fully understand the country experience. For example UK and GCC countries depend on their mineral resources, while countries in Africa are biased towards agriculture and USA, Switzerland, China and Singapore depend on technology as the backbone for their economy. The eastern European countries and Mexico, for example have welfare oriented economies with less emphasis on capital centric activities. Similarly, without having an understanding of the meso and macro-global picture of an industry, it is difficult to understand SME activity in any particular country. In India, this leads us to the finding that growth and employment generation are becoming increasingly size neutral. What matters here is the subsectoral position

What is a subsector?

Subsector is a set of economic activities that cuts across several sectors, traditionally agricultural, industrial and commercial sectors, and now electronics and I.T. There are five key concepts behind any subsectoral analysis: 1) verticality; 2) effective demand; 3) coordination with channels; 4) competition between channels; and 5) leverage. Subsector performance has various dimensions: 1) approach to efficiency, equality, and progressiveness; 2) synchronisation of exchange efficiency and transaction cost; 3) adaptation dynamism; 4) progressiveness; and 5) access to market and to information.