MSMEs in India: The Leading Issues of Today

ISED Discussion Paper

by
ISED Small Enterprise Observatory
jointly with
ISED Centre for Responsible Business

Institute of Small Enterprises and Development

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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 purpose of this Discretion 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 and strategies.

In every democracy, the developmental outcomes are decided by people's aspirations, to begin with. These aspirations need to be articulated through effective platforms. Institutions are the outcome of these platforms and their initiatives. People's mandate legitimizes the actions of institutions. Unless public policy, evolved a through democratic process, gives proper signals, one cannot expect India to realize its aspirations on the MSME front.

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Cochin
February 23, 2017

P.M.Mathew

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Abstract

In every democracy, the developmental outcomes are decided by people's aspirations, to begin with. These aspirations need to be articulated through effective platforms. Institutions are the outcome of these platforms and their initiatives. People's mandate legitimizes the actions of institutions. Unless public policy, evolved through democratic process, gives proper signals, one cannot expect India to realize its aspirations on the MSME front.

Key words: Leading issues, MSMEs, people's mandate, institutions, MSMEs

1.0. Introduction

Since 1990, the macroeconomic policy, and more specifically, the policies relating to micro small and medium enterprises in India, have followed a path of liberalization, with much less role for government, both regulatory and promotional. While the mixed perceptions on the MSME role continue to get reflected in public policy, the accelerated focus on growth and their possible implications on MSMEs need closer analysis. While the leading issues in the policy and practice of MSME development are least discussed and articulated in the country, the task of the following pages is to identify and discuss some of the major trends.

2.0. Indian Economy in 2016

The state of the Indian economy, as in 2015-16 and afterwards, explain the recent political transition and the developmental implications thereon. The major sources of information, on which one can draw some meaningful conclusions, are provided by the Ministry of Finance and the Reserve Bank of India.

2.1. GDP Growth Behaviour

India is set to become the fastest-growing big economy in the world, edging past China. It is set to clock a 7% rise in GDP in 2017, compared with 6.9% for China. Global growth is expected to rise moderately to 3.0% in 2015 from 2.6% in 2014 and further increase to 3.3% in 2017; there will be significant divergence in trends and that the "oil price collapse will result in winners and losers"(The World bank,2016).

According to the Economic Survey, the earlier perception about slow industrial growth during the last three years, is at variance with the latest gross domestic product estimates, based on a new methodology and with 2011- 12 as the base year. The latter indicates an industrial recovery led by mining and manufacturing. However, in the current year, credit growth, corporate performance, and the Index of Industrial Production continue to point towards slow industrial growth. Infrastructure growth in terms of eight core industries has been higher than industrial growth since 2011-12, and this trend is expected to continue. The Economic Survey also noted that, the number of macro level and sectoral initiatives undertaken to improve industrial growth are expected to yield positive results over time.

The corporate sector performance, of listed manufacturing companies in the private sector, in terms of growth of sales and net profit, appeared on y-o-y basis to turn around while there was a marginal decline in Q1 of 2016-17. There was no discernible improvement in capacity utilization in the first two quarter of 2016-17, as per the 34th round of the Reserve Bank of India's (RBI's) Order Books, Inventories and Capacity Utilisation Survey.

In infrastructure, the focus has been on resolving long-pending issues like pricing of gas, establishing processes and procedures for transparent auction of coal and minerals, and improving power generation and distribution.

A monthly index of eight core industries, viz. coal, fertilizer, electricity, crude oil, natural gas, refinery product, steel, and cement, comprising 38 per cent of the weight of items in the IIP, is released to gauge the impact on overall economic activity. A comparison between the annual average growth rate in the eight core industries and the IIP shows that, since 2011-12 the higher annual growth of the eight core industries than of the IIP, implies slowdown in the growth of consumer goods. The IIP as of March 2016 stood at 188, which was 6.4% higher than the index in March 2015. The overall growth in eight core industries during April-March 2014-15 has declined to 4.4 per cent compared to 2.7 per cent. Electricity (11.3per cent), coal (1.7 per cent), and cement (11.9 per cent) boosted the performance, while natural gas (10.5 per cent), fertilizers (22.9 per cent), crude oil (5.1 per cent), refinery products (10.8 per cent), and steel (3.4 per cent) accounted for moderation in growth.

India accounts for 1.8 per cent of the world's manufacturing output. For manufacturing companies in the private sector, although growth in sales has been stagnant for the last two years, net profit has started rising from the last quarter of 2015-16, showing improved efficiency of the companies, which is a positive sign for growth of the manufacturing sector in India. Capacity utilization, as measured by the 34th round of the Order Books, Inventories and Capacity Utilisation Survey (OBICUS) of the RBI, registered an increase in Q4 of 2015-16 over the previous quarter although it was marginally lower than its level in the previous year. The (Y-o-Y) growth in new orders decelerated from 12.0 per cent in Q2 of 2015-16 to -1.8 per cent in Q1 of 2016-17 (PIB, 2016)

As per the latest data available on national income, consumption expenditure, and capital formation at constant 2011-12 prices, the rate of growth of GCF has declined by 1.5% from Dec 2015 to Mar 2016. At 26.9% of GDP in Jan to March quarter capital formation is the lowest year.

During April-November 2014-15, total FDI inflows (including equity inflows, reinvested earnings, and other capital) were US$ 27.4 billion, while FDI equity inflows were US$ 18.9 billion. Cumulative FDI inflows from April 2000 to November 2014 were US$ 350.9 billion. Services, construction, telecommunications, computer software and hardware, drugs and pharmaceuticals, the automobile industry, chemicals, and power have attracted a proportionately high share of total inflows.

The RBI comes out with an exhaustive analysis. Despite the immense efforts in recent years of both the Government and RBI to restore macroeconomic stability to the economy, three areas are still "work in progress" from RBI's perspective. First, economic growth is still below levels that the country is capable of. Second, inflation projections for January 2016 (as of early August 2015) are still at the upper limits of RBI's inflation objective. Third, the willingness of banks to cut base rates whereby they forego income on existing borrowers in order to attract more new business is muted; not only does weak corporate investment reduce the volume of new profitable loans, some bank capital positions, weakened by NPAs, may prevent them from lending freely.

The short term macroeconomic priorities of the Reserve Bank focus on bringing down inflation in line with the proposed glide path; work with the Government and banks on speeding up the resolution of distressed projects and cleaning up bank balance sheets; ensure banks have the capital to make provisions, support new lending, and thus pass on future possible rate cuts.

2.2. Employment

The latest estimates, as in October shows that, in January-March this year, 64,000 jobs were created in eight crucial sectors of the economy. Manufacturing job growth remains under stress. Sequentially, employment generation in most labour-intensive sectors slowed in 2015-16, showed the 28th Quarterly Report on Changes in Employment, released by the Labour Bureau. Every quarter, the Chandigarh-based Labour Bureau conducts quarterly job surveys to gauge the impact of government policies on employment generation in the textiles, leather, metal, automobiles, gems and jewellery, transport, information technology (IT) and handloom sectors. Though the number of new jobs was the lowest in four quarters, it rose sharply compared to the year-ago period, primarily driven by the IT sector. In the December quarter of 2015-16, 135,000 new jobs were generated, while in the same quarter the previous year 158,000 jobs had been created. However, 185,000 jobs were created in the IT/BPO (76,000), Textiles & apparel (72,000) and Metal working (37,000) while other sectors lost a total of 50,000 jobs. Data for the last eight year's corresponding quarters also reflect that all sectors experienced decline in employment on many occasions except for Textiles, including Apparels sector while trend of employment in IT/BPO sector was independent from seasonality. Most jobs created in the twelve months ended December 2015 were direct labour (167,000), while contract labour diminished by 36,000. 122,000 jobs created during the same period belonged to export-oriented industries, Textiles including apparel (95,000), ITO/BP (46,000) and Metal working (25,000) making a total of 166,000 while the other sectors lost 44,000 jobs. the largest looser being the automobile sector. However, the pace of employment generation is yet to recover to its pre-2010 level. Information technology business process outsourcing (IT-BPO) and textiles continue to be the key export oriented sectors generating large employment from 2009 to 2015. Over this twelve month period all the non-exporting entities suffered loss of jobs in different in percentages, barring a marginal increase of less than 1% in the June-September 2015 quarter.

2.3. Financial Sector

In the financial sector, RBI envisages the need to increase efficiency through greater entry and competition. The most appropriate institutions will prevail when the competitive arena is level, so we have to remove regulatory privileges as well as impediments wherever possible, especially those that are biased towards some form of ownership or some particular institutional form. We need