

ISED Discussion Paper

India's MSME Policy Architecture: A discussion

by
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Institute of Small Enterprises and Development

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Published by P.M. Mathew, for Institute of Small Enterprises and Development.

Series: ISED Discussion Paper

Price: 490.00 (India); US \$ 15.00 (Overseas)

About 'ISED Discussion Paper' Series

Brought out by the Institute's knowledge platform, the ISED Small Enterprise Observatory, titles under this Series are meant to stimulate a discussion on some of the latest developments in the economy and society. The contents of 'ISED Policy Briefs' emerge largely from the findings and experience of research work at the various Knowledge Centers of the Institute of Small Enterprises and Development. They are meant to be a backgrounder for policy debates and discussions at various levels.

Preface

The Pandemic COVID-19, which has triggered disruption in lives and livelihoods globally, obviously, re-shapes the present as also the future of economies and of humanity as a whole. However, it is a challenge and opportunity for humanity to outlive such constraints. Shaping new development strategies and promotion of enterprise and entrepreneurship alone can be the solution to this impasse. That means, we need to start speaking of the impacts at the “bottom of the pyramid”, and plan for broad basing the mass base of entrepreneurship.

Under the India MSME Communication Programme(IMCP), the ISED Small Enterprise Observatory, in co operation with the various Knowledge Centres of the Institute, makes a rigorous analysis of the latest currents in the MSME constituency, leading to a unique ‘Development Report’. This study is a spill-over of this exercise of Development Reporting on micro, small and medium enterprises (MSMEs) at the ISED.

While the team of the Observatory did a meticulous job under the guidance and support of the Project Leaders, individual members of the Team, including the editors and the Associates, have made their special contribution in specific thematic areas. While this title is significant in the present context of the Indian economy, and of the MSME developments in specific, I hope it will contribute to wider discussions in the subject area.

As this title comes out as a joint output of the Observatory and the ISED Centre for Enterprise Development, the Institute wishes to thank, without fail, the pains and efforts of the authors, and all who have supported it through inputs and suggestions. ISED has taken best efforts to ensure the quality and reliability of this paper. However, for the findings and views, the authors alone are responsible.

Cochin,
August 20, 2020

P.M.Mathew
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Abstract

The MSME policy architecture in a country involves the legal and institutional frame work, as also the policy response. India has a huge infrastructure of MSME policy institutions and programs. However these need to help enhancing the 'collective' and 'individual efficiency' strategies of enterprise development. However, there are several critical constraints which public policy seeks to address. Beyond the traditional strategies of cluster development, there is need for evolving new strategies of harnessing the potential of the entrepreneurs. Based on the more recent experience, issues such as climate change need to be factored seriously into MSME agenda of the country. This document provides a critical analysis of India's track of policy and programmes, and highlights some of the new and emerging issues.

KEY WORDS: *SME policy, individual efficiency, collective efficiency, clusters, climate change.*

1.0. Introduction

Policy institutions and the relative roles of stake holders are decisive in shaping the public policy landscape for MSMEs. Ever since Independence, India has initiated a significantly large institutional support system for these enterprises. While the role of an institutional support system is to meet the key objectives of public policy at a particular point of time, it is important that such institutions should adapt themselves to the changing times. This necessitates a built-in dynamism, both for the institutional structures, as also for the legal framework. The purpose of the following pages is to discuss their role and relevance in the emerging context of the country's larger agenda of enterprise development.

2.0. Legal and Institutional Setting

The legal and institutional framework relating to the MSME constituency has to be understood in relation to two aspects: 1) the stakeholder framework; and 2) the role of supporting institutions. The stake holder framework is guided by the basic legal framework, which defines the relative roles and responsibilities of each stakeholder.

The origin of the legal framework for MSMEs (the erstwhile 'small scale industries') has to be found in the Industries Development and Regulations Act of 1951. The Act defined and distinguished small scale and large enterprises on the basis of the investment in plant and machinery. This investment limit was administratively redefined from time to time, based on the inflation factor, as also an assessment of the changing needs of the times. Subsequently, many changes took place in these structures and policies as per changing needs. A formal legal structure came with the concept of a Basic Law. Thus arises a fundamental question:

How the institutional structure corresponds to the objective needs of the sector? Or, that the programmes are accommodated as per the needs of the institutions? While this problem arises in all countries, what is needed is mid-term corrections and restructuring. It is important that such rationale is discussed and deliberated, and new light thrown upon, on the basis of the changing realities.

3.0. Macro Policy Framework

The macro policy framework of MSMEs have evolved over a period of time. Initially, it was guided by administrative decisions. A consultative process was introduced with the introduction of the MSME Development Act. The macro level policy regime includes, the National Board of MSMEs, which provides the overall policy guidelines to the Ministry. At the legislative level, the legislative committees on MSME, in the Parliament and the State Legislative Assemblies, come out with their reports and recommendations. The banking related policies get shape through the Department of Financial Services in the Ministry of Finance, as also through the Reserve Bank of India. Regarding regional policies relating to enterprise development, the Panchayati Raj Act empowers the Panchayati Raj institutions to take care of matters relating to village and small scale industries. However, Panchayati Raj, in practice, is weak in many States.

'Policy visibility' is an important aspect determining the strength of public policy, as also the benefits accrued to the society. 'Policy visibility' means the clarity involved in policy among the people at large, and thereby, its impact on the society as a whole. But, on the other side, visibility is also conditioned by the strength of policy institutions. In a country where public policy institutions are weak, one cannot expect substantial impact of policy

Public Policy and Economic Governance

A policy statement by the government, by itself, cannot lead to concrete action at the ground level. It can be a tool, but its effect depends upon the kind of governance system. For example, 'women entrepreneurship development' is a policy priority meant for women empowerment. But the term, 'entrepreneurship' is abstract; the domain of action is rather unclear. On the other hand, 'enterprise development', more visible, has its logic and instrumentality, but the aspect of 'empowerment' may not fit in. Similarly, in a 'Backward Area Development' programme, enterprise development can be the focus; but, in practice, it need not lead to enterprise development *per se*, but may lead to area development. Economic governance is altogether different from the word 'governance', as it is popularly used.

on the lives of people.

3.1. Policy Institutions

Policy visibility in India, is constrained by the allocation of Business Rules of the Govt of India. The MSME constituency is divided among several ministries. For example, the Ministry of Textiles has more coverage than that of the Ministry of MSME, in relation to the number of enterprises it deals with.. Similarly, the Ministry of Electronics and Information Technology, has a vast coverage area. The growth of the so called 'new economy' essentially means a significant growth of smaller units as players in this subsector.

An overall policy statement for the MSME sector, by itself, cannot lead to concrete action, unless the priorities of public policy are clearly spelled out in relation to the respective roles of the policy institutions. Therefore, the impact of policy on MSMEs is dependent on how this is spelled out. A new policy can be a tool, but its effect depends upon how it is prioritized in the overall business of governance in the country. For example, 'women enterprise development' is a policy priority. But it is one among the priorities relating to women empowerment. Here, the domain of action is rather unclear, and naturally, the performance of even the best of programmes is likely to fall apart from their objectives. On the other hand, enterprise development has its logic and instrumentality, where the aspect of 'empowerment' may not fit in. Similarly, in a 'Backward Area Development' programme, enterprise development can be the focus; but, in practice, it need not lead to enterprise development *per se*.

The inconsistency, as we note above, is a question of irregularities relating to the policy process. It has now been universally accepted that public policy need to

be evidence-based. What is the process through which a new policy is announced? Is it based on a simple announcement? Or is it the outcome of a parliamentary process by which the theme of the subject is discussed in the legislative bodies? Or, are the policy institutions themselves too weak to support such a consultative process, so that it takes place without adequate background information? While seeking answers to such questions, there is a consensus that, evidence-base need to come up. A closer examination of the working of policy institutions may provide significant inputs for such an understanding. We, therefore, attempt to have a brief digression on the subject.

3.1.1. Prime Minister's Office

It is common practice in many countries, today, that the Office of the Prime Minister takes policy directions on to SME development, either directly or through a high level apex body (e.g.: SBA in USA, Japan, UK). Soon after Independence, the Prime Minister's Office was instrumental in appointing the Ford Foundation Team, which laid the basic policy relating to MSMEs in the country. The basic building blocks of this policy of the 1950s got radically changed, with the appointment of the Abid Husain Committee, which came as part of a larger policy of liberalization in the country. In 2010, the Prime Minister Dr. Manmohan Singh appointed a Task Force on MSMEs, the recommendations of which formed the main thrust of policy of the then government. Though development of MSMEs is one among the businesses of the Govt of India, the complexity of the subject and its strategic nature often demands some lead role by the PMO. The national flagship programs, such as 'Make in India' maintain their visibility essentially because of their "flagship" nature and national importance.