

Indian MSMEs: Forever Dwarfs?

The Economic Survey 2019 brings forward a very interesting concept pertaining to MSMEs – The Dwarfs. According to the authors of the survey there exists a class of entities in India that have continued to remain small despite their vintage. These firms are specifically those that employ less than 100 workers and try to take advantage of a system that has been favoring firms by size and not their quality.

Such firms, according to the survey have refused to grow up and have fallen short in almost every parameter used to measure advancement and contribution to the overall economic wellbeing. The parameters include a firm's ability to create employment, contribution to the Net Value Added (NVA) and share in overall number of existing firms. It was found that these Dwarfs by number are almost 50% amongst organized manufacturing firms yet they contribute to only 14.1% of employment and 7.6% of the NVA. On the other hand, it is revealed that larger firms employing over 100 workers that have been in existence for less than ten years contribute to 21.2% of the employment along with 37.2% of the NVA, despite making up for just 5.5% of all firms. In fact, it is discovered that it is not the older firms that create the most value and the most employment, rather it is by those that are infants in terms of age.

By statistics, the authors of the survey show that employment creation peaks at 6-10 years' vintage and then declines; even NVA contributions start to decline post the 20 years' vintage. Therefore, it is observed that newer firms are more successful in meeting objectives of an economy than do older firms, which in turn become job destroyers and ultimately compensate worker count with capital.

Dwarfs maybe exclusive to the manufacturing sector

Even though the notion presented by the survey can be refuted by the fact that Indian firms have survived over the years by taking advantage of arcane laws, their stunted growth has been nonetheless responsible for India's lower technological evolution and export-oriented value added.

Furthermore, given the current situation, one can figure easily that the very source of this dwarfism lies in manufacturing. Service sector, while being identified by survey authors as a potential source of higher employment is comparably more dynamic in a fast-changing environment. Manufacturing MSMEs are spread across the value chain and recipients of much of turmoil, given the fact that they are much more tied-up to the vagaries of the market and OEM pressures. In a scenario, where margins are consistently being constricted and capacity utilization levels still hovering at around 70-75% levels, chances for expansion are surely bleak. One look at the IIP and core sector number reveals that inventory pressures are real across the value chain and fresh orders come at a discount. The credit offtake is another perspective worth considering here as it provides a glimpse of the overall MSME landscape and sentiment.

We note that even in one of the fastest expansion cycles in credit - seen in recent times, manufacturing based Micro and Small enterprises were not major participants. As per data available from the RBI, it is noticed that while total credit to the micro and small enterprise sector (under priority sector lending) grew by 11.78% YoY (as of May 2019), that of manufacturing-based enterprises grew by just 1.1%. If we contrast this with service-based enterprises, then their demand for credit grew by 18.33% on a YoY basis as on May 2019. This disparity becomes even more stark while assessing the first half of the current calendar year. It is revealed that between January and May 2019, total credit demand by micro and small enterprises grew by 10.76%. In this timeframe, demand from manufacturing enterprises grew by just 0.5%, however. For services, this number came at a very healthy 17.32%.



These figures state that manufacturing enterprises indeed are stuck in quagmire of demand volatility and stringent regulations. The question is therefore how we inject the growth hormone into our MSME in order to unleash their potential to the fullest. Structured hand holding and the survey's recommended 'sun set clause' are a few options come to mind in the first instance. However, the conditions have contributed to the Dwarfism are inherent to the Indian economy and beliefs entrenched for generations. It is thus the psyche towards business that requires an overhaul and the problem's identification is just a start to the crusade.