



Implications of new MSMEs definition on investment and employment in India

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Abstract

India is expected to emerge as one of the world's leading economies on earth for the next ten years in good light political and economic situation. Micro, Small & Part of Medium Enterprises (MSME) is expected to play an important role in the economic development of India. In the development of this phase is very important to meet national investment and production obligations of important levels of activity in all cities, towns and rural areas across the country. In addition, it can expand supporting the development of four young entrepreneurs the power to create competitive businesses around the world comes from India.

MSME can be the backbone of current and future heights to grow businesses with domestic and foreign companies investing in the 'Make in India' program and doing the essential impact in the area of indigenization. 'Do in India by zero feature and zero effect', is an important opportunity. New the MSME wave should enable business development an eco program that empowers and sustains business continuously preparing to deliver the right product, the right quality, the right solution and the right service at a competitive price, both in domestic and international markets.

Key words: Micro, Small, Medium Enterprises, Enterprises, Market and Domestic market.

Introduction

The Indian revolution also offers a great opportunity to promote MSME Participation in Information, Communication and Telecommunication (ICT) sector, in line with government vision. It is equally important that the MSME segment develops in it all sectors of agriculture, manufacturing and services because each of

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these fields will continue to be large coupled with overall GDP growth and employment generation. The MSME sector will act as a catalyst to deliver about this socio-economic transformation.

India's GDP is expected to reach 8.5 percent, with a country that is likely to be worth USD 5 trillion by 2025. Part of the MSME has the potential to emerge as a backbone in this economy and act as the engine of growth, given a proper set of support and a permissive framework. MSME business development opportunity and support growth driven by innovation over the next decade by:

- Significantly increase the share of MSME donations to GDP from 8 percent to 15 percent by 2020;
- Generating employment rates of up to 50%. the work is total, in addition to doubling the current function 106 million MSME employees across agriculture, manufacturing and services sector³ ; and
- Increase the MSME contribution share across the key the public and private sectors are complementing the growth domestic demand, exports, indigenization and replacement.

Until recently, Micro, Small and Medium Enterprises (MSMEs), registered with the relevant government agencies, have been described in terms of investment in industry and machinery, as set out in Table A of Table 1. Registration is the eligibility for government advertising acquisitions. assistance, as set out in Table 2.

Table 1 MSME definitions

Source: Reviewing MSME Definition: Who Can Benefit From It?

	Panel A		Panel B	
	Old definition (Inv.)		New definition (mfg & ser.)	
	Mfg.	Services	Investment	Turnover
Micro	25 L	10 L	1 cr.	5 cr.
Small	5 cr.	2 cr.	10 cr.	50 cr.
Medium	10 cr.	5 cr.	50 cr.	250 cr.

According to the new definition, an entity qualifies as an MSME only if it satisfies both criteria

Table 2 Benefits of MSME registration

Source: Reviewing MSME Definition: Who Can Benefit From It?

Collateral free loans from banks	Ease of getting licenses, approvals and registrations
Reservation policies to manufacturing 1 production sector	Special consideration on international trade fairs
Octroi benefits	Waiver of stamp duty and registration fees

Exemption under Direct Tax Laws	Bar code registration subsidy
Subsidy on NSIC Performance and Credit ratings	Eligibility for IPS subsidy
Counter Guarantee from Government of India through CGSTI	Protection against delay in payment
Reduction in rate of interest from banks	15% CLCSS subsidy to purchase fully
Waiver in security deposit in government	Concession in electricity bills
Reimbursement of ISO Certification	Excise Exemption Scheme
Preference in procuring from government	P15% weightage in price preference
1% exemption on interest rate on OD	50% subsidy for patent registration

On March 25, an economic ban was imposed to address COVID-19. Understandably, this decision has severely damaged jobs and livelihoods, especially in the informal sector. To alleviate the hardship, the Prime Minister has proposed Rs. 20 lakh crore Atma Nirbhar Bharat stimuli and help package. On May 13, FM³ announced plans for the MSME sector. A highlight was the highly anticipated review of the enrollment process as an MSME, such as:

1. Eliminate the difference between the production business and services.
2. To increase the maximum investment in industry and machinery to qualify as an MSME.
3. We present “profit” as additional terms.

Panel B of Table 1 contains the definitions. The most important review is an increase in the investment limit for medium-sized businesses, starting from Rs. 10 crores up to Rs.50 crore.

The following are some of the incentives included in the FM economic plan:⁴

1. Rs. 3 lakh crore business emergency workplace, including MSMEs,
2. Rs. Less than 20k crore loans for fixed MSMEs,
3. Rs. 50k crore equity infusion through the MSME Fund,
4. There are no international tenders for government tenders up to Rs. 200 million.

³ Minister of Finance

⁴ <https://pib.gov.in/PressReleaseDetailm.aspx?PRID=1623601>

There are two reasons for high-level revisions: one, accounting for inflation; and, secondly, empowering firms to protect the economy from high productivity and to avoid “dividing” businesses to remain “small”, so that they can continue to receive legal assistance.

Who might benefit from the top review? It will benefit businesses currently outside of investment limits, who can still register as MSMEs. We quantify the size and composition of companies that may benefit from redefine. The CMIE⁵ Prowess website is analyzed objectively, as the beneficiaries are likely to be large businesses and companies.

New definition of MSME in India: good or bad? Why?

Micro Small & Medium Enterprises (MSMEs) are defined in India under the MSMED Act 2006 on the basis of large-scale industrial and mechanical investment, excluding real estate and real estate investments.

[According to 2006 definition, Production units invested less than Rs 25 lakh (Rs 2.5 million) are Micro, those between Rs 25 lakh and Rs 5 crore (Rs 50 million) are Small and at Rs 5 crore to Rs 10 crore (Rs 100 mn) As average. Similarly, for Service units, the corresponding investment limits range from Rs 10 lakh (Rs 1 mn) Micro, between Rs 10 lakh to Rs 2 crore (Rs 20 mn) Small and between Rs 2 crore to Rs 5 crore (Rs 50 mn) Medium]

Over time, the MSME sector has been raising the need for revision / amendment of the MSME definition. Cabinet recently approved a draft proposal to change the definition of MSMEs. Highlights of the proposal are:

1. It eliminates the condition of investment and instead proposes to define MSMEs on the basis of annual sales profits.
2. There is no difference between the production unit and the service.
3. The proposed limits are: Costs up to Rs 5 crore (Rs 50 mn); Small- up to Rs 75 crore (Rs 750 mn) and Medium- up to Rs 250 crore (Rs 2.5 bn).

However, it is currently a proposal that the Government has approved. For it to be effective, the proposal will need to be amended by the MSMED⁶ Act and passed by Parliament.

The question asked in many parts is why a change in meaning was needed?

I give four reasons.

Firstly, the definition was freezed in 2006. After 12 years, with continued erosion of value of Rupee, the thresholds have become impractical. Adjusting for inflation would have required to enhance the limit by 2-3 times.

⁵Centre for Monitoring Indian Economy

⁶The Micro, Small and Medium Enterprises Development Act, 2006

Secondly, many sectors where MSMEs have substantial share such as Pharmaceuticals, Auto-component, Food processing among others have been demanding a many-fold increase in the investment limit needed to be compliant of the new mandatory and industrial standards. The de minimis investment exceeded at least five crore even if one had low turnover.

Thirdly, the investment based definition creates an uneven field for older enterprises vis a vis new enterprises. Setting up a unit to produce a product today would require several times more investment than the one set-up ten or twenty years ago to produce the same product with similar quantity. What could be a micro unit because of historical investment figures, would become medium or large if set up today. It becomes a barrier for new entrants.

Finally, to prove that a unit fell in a specific category, the MSMEs ran around CAs to certify the value of plant and machinery. It is alleged that many large enterprises also under-reported the investment, got CA certificate and partook in the Public Procurement ear-marked for MSEs.

Therefore, change in criterion of defining MSMEs has been considered using Turnover as the basis. **The advantages of having such a definition could be:**

The Turn-over based criterion resolves many of the ills of earlier regime. It is transparent, as authorities could always cross check the turnover through platforms such as GSTN. No CA certificate would be required.

Secondly, it also levels the field for new and old enterprises as the comparison is not between historical investments and current investments but between current turnovers.

It would be realistic also: after inflation adjustment the definition of small enterprise on the basis of investment would have been Rs 15 crore today. Keeping turnover five times the investment, a very conservative figure, we have Rs 75 crore as a threshold which is what is proposed in the new definition.

But there is flip side too. There are few sectors where investment is low but turnover is high for example gems and jewellery units, units producing Aluminium conductor steel-reinforced cable (ACSR) among others. Many of the units have been under small category owing to investment criteria but having high turnover ranging from Rs 100 to 30 crore. They enjoyed benefits under Public Procurement Policy for MSEs which mandates 20% set-aside for Micro and Small Units in all central government purchases. Suddenly, the reserved pie of the cake is out of their reach. The PPP for MSE would not be available for units having more than Rs 75 crore annual turnover.

Keeping in view that in the proposed thresholds, there would be hardly any Micro and Small unit that could participate in high volume government tenders, it has been proposed by FISME that where smaller units have not bid, the reserved category benefits could be passed on to Medium enterprises.

One criticism about the new definition is that India still does not take into account the number of people employed. Globally, the two most important elements used to define MSMEs remain turnover and employment. I think the decision for not including the employment criterion may be because of inability of the system to cross check employment figures in a transparent manner. The practice of underreporting number of people employed is widespread especially in smaller units to remain below the threshold of 10 employees to save on very high social security and compliance costs. Lack of labour reforms has exacerbated the situation. Adding such a criteria would have led to more paper work and corruption.

Overall, the new definition is a vast improvement over the earlier definition and should help MSMEs to face new challenges in a better frame.

Importance and role of MSMEs in the Indian Economy

1. To generate large scale employment

In India, capital is scarce and labour abundant. MSMEs are thought to have lower capital-output and capital-labour ratios than large-scale industries, and therefore, better serve growth and employment objectives. The MSME sector in India has grown significantly since 1960 – with an average annual growth rate of 4.4% in the number of units and 4.62% in employment (currently employing 30 million). Not only do MSMEs generate the highest employment per capita investment, but they also go a long way in checking rural-urban migration by providing people living in isolated areas with a sustainable source of employment.

2. To sustain economic growth and increase exports

Non-traditional products account for more than 95% of the MSME exports (dominating in the export of sports goods, readymade garments, plastic products etc.). Since these products are mostly handcrafted and hence eco-friendly, there exists a tremendous potential to expand the quantum of MSME led exports. Also, MSMEs act as ancillary industries for Large Scale Industries providing them with raw materials, vital components and backward linkages e.g. large scale cycle manufacturers of Ludhiana rely heavily on the MSMEs of Malerkotla which produce cycle parts.

3. Making Growth Inclusive

MSMEs are instruments of inclusive growth which touch upon the lives of the most vulnerable and marginalized. For many families, it is the only source of livelihood. Thus, instead of taking a welfare approach, this sector seeks to empower people to break the cycle of poverty and deprivation. It focuses on people's skills and agency. However, different segments of the MSME sector are dominated by different social groups.

Size and Structure of MSMEs

Before answering the question posed above, it will be helpful to understand the size and structure of the MSME registered sector. It will help us to see that while MSMEs are being distributed, potential beneficiaries are likely to fall.

What covers the MSME sector is confusing. Includes all illegal non-agricultural sector. It consists of 634 lakh unregulated businesses, employing 1110 lakh people, contributing 29% of GDP and more than 40% of India exports in 2015-16 (Report⁷). Government sources often use these figures to illustrate the importance of the sector in the national economy. The characters of the "small industry" often persuade them to argue that MSMEs form the basis of India's production and business base — in contrast to the popular view of corporations⁸ that are the engine of the economy.

⁷ Department of Service Report, 2018-19; RBI 2019

⁸ Includes large corporations and commercial houses

The above account compares the entire non-agricultural sector with MSME. However, units registered with statutory bodies (particularly the Development Commissioner, MSME) form a small portion of the above-mentioned scale. In addition, major units within the MSME registered sector are part of the legal or regulated sector as they fall under Industrial Law or Companies Act (some are listed on the stock exchange). Although most (if not all) of the unregistered institutions or businesses, by law, are eligible to register as MSMEs, they usually do not register.

There is no official register of operating businesses or reliable estimates of their role in outgoing and regular employment. Departmental estimates are often the result of the last MSME census conducted in 2006-07. Utilizes online registration of new extrapolation businesses (RBI 2019).⁹

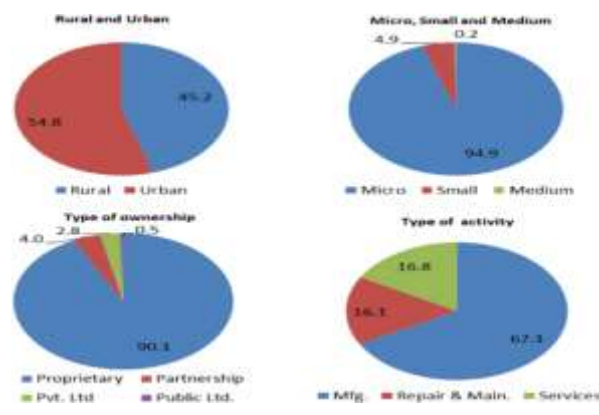
In the absence of the latest reliable data, we define the size and structure of MSME registrants according to the fourth census. In 2006-07, there were 15.64 lakh registered units; 95% of them were small units (i.e., invested less than Rs. 25 lakhs in industry and machinery in real value). 45% of the registered units were rural firms, 90% of which had an average of six employees per unit. More than two-thirds of the units were produced; the total output per unit was Rs. 46 lakhs (Table 3). However, only 70% of active units are registered units. Some are closed or traceable.

Table 3 Establishment of MSME registered sector: abridged statistics as census 4, 2006–07.

In other words, most registered MSMEs make up a small portion of the MSME sector as defined by the Department, previously reported. However, the most prominent among them are outside the informal sector and are part of the formal or legal sector. Mapping the boundaries of the MSME sector is almost impossible for the following reason: registered MSMEs are defined by investment in industry and services, while other legal data sets follow the terms of employment.

Although they make up a small portion of MSMEs, the registered units are not the same at all. For example, 95% of them are small units and 90% have ownership concerns. In contrast, although accounting for 0.2% of total units, approximately half of units are medium-sized businesses (Fig. 1). The medium business employs 27 times more employees, has 73 times a fixed asset and produces 62 times more than the standard unit in the registered MSME sector (Fig. 2).

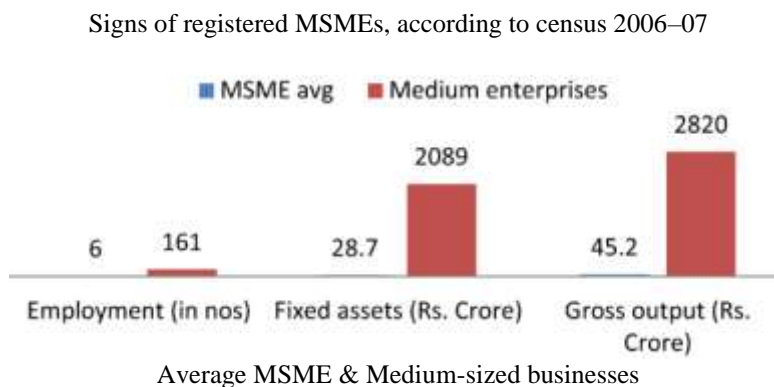
Fig. 1



⁹ The report said: “After the fourth MSME Census in 2006-07, there has been no census. Much of the extrapolation has relied upon data on new registration”

(<https://www.rbi.org.in/Scripts/PublicationReportDetails.aspx?UriPage=&ID=924>).

Fig. 2



Data and operating system

The structure of the size of Indian private companies is also greatly distorted. Of the approximately one million registered companies (and company registrar, DCA¹⁰), only about 60,000 are listed on the stock exchange, accounting for most of the payments and product (or sales). The CMIE Prowess website has about 50,000 large companies compared to those listed. However, most of the balance sheets on the website are incomplete. Therefore, our analysis is based on the data of 20,440 FY2016 companies and 17,450 companies for the year FY2018¹¹, in which complete information on

- (1) fixed investment in industry and machinery and
- (2) profits - to identify potential beneficiaries under the new youth. Definition of MSME. More than half of the companies are still in services, while the rest are in industry.

Results

Table 4 shows the distribution of potential companies with smaller, smaller, medium and large companies (i.e., residues) in size, according to MSME definitions old and new for FY2016 and FY2018. The table also shows changes in distribution due to redefine. In FY2016, qualified companies such as MSME increased by 3380; or, 30% of sample companies. Most of them are medium-sized businesses. The number of small businesses eligible under the new definition has dropped by 496, or 9%. The same pattern can be seen in FY2018 again.

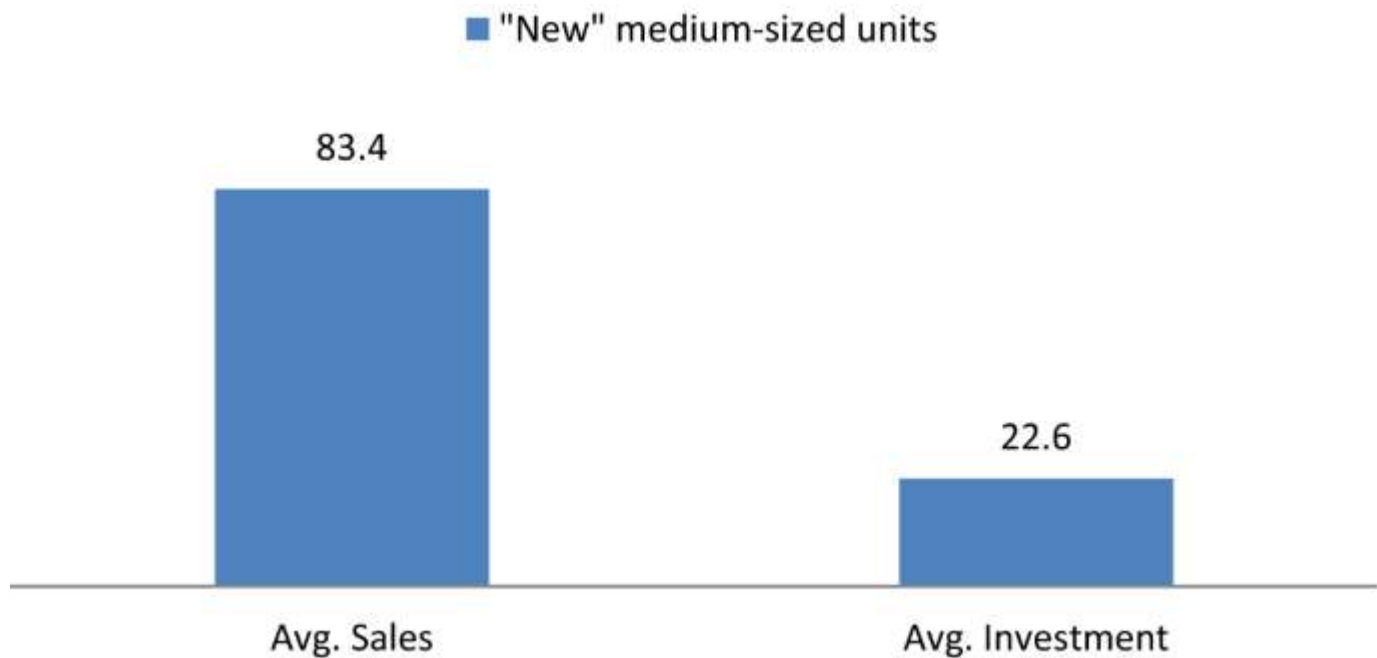
Table 4 Total number of companies based on two definitions.

By FY2016, 3743 companies that were outside the MSME sector have now been included in the new definition, data analysis shows. About 60% of them work in the industry and the rest are in services. As Figure 3 shows, the average selling price of these companies is Rs. 83.4 crores, with an investment of between Rs. 22.6 million.

¹⁰ Department of Corporate Affairs

¹¹ Fiscal Year 2018

Fig. 3



Medium sales and investment of “new” medium-sized units (Rs. Crore) by FY2016

It is instructive to compare the size of the potential beneficiaries with the MSME sector as a whole. On average, the sales revenue of potential beneficiaries is 191 times greater than the maximum effect of registered MSME. Although the two figures are not one year old, therefore, they are not comparable, the magnitude of the difference between them is so great that they appear to belong to a different “world”.

Table 5 reports the number of listed companies — that is, those listed on the stock exchange — on the CMIE¹² Prowess website. As stock listings require the most important disclosures and regulations, they are always the most prominent companies. Does the definition of MSMEs bring the maximum number of companies listed in the MSME sector? The answer is yes. By FY2016, according to the old definition, the listed MSMEs were 1753. The number rises to 2492, or 42%, according to a new definition.

Table 5 Shares of listed and unregistered companies, for MSMEs.

From: Reviewing the MSME Definition: Who Is the Most Beneficial?

	Old definition				New definition			
	Total	Unlisted	Listed	% listed	Total	Unlisted	Listed	% listed
2016								
Micro	2873	2288	585	20.4	3006	2385	621	20.7
Small	5751	4947	804	14.0	5255	4388	867	16.5
Medium	2129	1765	364	17.1	5872	4868	1004	17.1

¹² Centre for Monitoring Indian Economy

	Old definition				New definition			
	Total	Unlisted	Listed	% listed	Total	Unlisted	Listed	% listed
Large	9687	7153	2534	26.2	6307	4512	1795	28.5
MSMEs	10,753	9000	1753	16.3	14,133	11,641	2492	17.6
Total	20,440	16,153	4287	21.0	20,440	16,153	4287	21.0
2018								
Micro	2343	1760	583	24.9	2381	1821	560	23.5
Small	4617	3814	803	17.4	4146	3305	841	20.3
Medium	1785	1417	368	20.6	4815	3856	959	19.9
Large	8705	6419	2286	26.3	6108	4428	1680	27.5
MSMEs	8745	6991	1754	20.1	11,342	8982	2360	20.8
Total	17,450	13,410	4040	23.2	17,450	13,410	4040	23.2

In other words, in the companies listed in our sample, those eligible as MSMEs increase from 41% in the old definition to 58% under the new definition. The same holds for FY2018 again. These results indicate that the redesign of MSMEs has resulted in a large number of listed companies, which is why large businesses are relatively small, under MSMEs. The redesign has expanded the scope of medium-sized businesses.

Discussion of findings

If our estimates are correct and the comprehensive comparisons made work, the redesign only helped large corporations enter the MSME registered sector. Therefore, the redefinition appears to be nothing other than a combination of MSMEs. The millions of businesses that are excluded from the informal sector, which are economically vulnerable, in need of public assistance do not seem to benefit from redefinition.

One could argue that the government does not prevent a large number of unincorporated businesses from registering for legal gain. Here's a rub. Registration costs and barriers associated with small businesses appear to be so high that subscribers, or fail to register. Thus the proverb "small businessman" who is reported to be a victim of government subsidies, fails to benefit from the extended legal definition. If the government is serious about helping smaller units, it should develop "Easy Registration" for really small businesses.

Conclusions

Registered MSMEs form a subset of the MSME sector (as defined by the service). The latter includes all illegal non-agricultural sector in terms of policy, which is eligible for legal assistance. Registered MSMEs, which

create an investment base for small businesses, must produce goods and services that require a large number of employees. Most of those units are in the informal or informal sector and most of them are located in an urban, manufacturing area, employing an average of about six people. However, the effect of the registered sector appears to be largely due to larger units registered as industries and companies listed in the stock market. Dualism shows significant differences or inequalities within the MSME registered sector.

Recently, the definition of registered MSME has been revised upwards, increasing its ambit in the understanding of major units. Its purpose is to remedy inflation and to promote a productive economy by avoiding the fragmentation of units in order to maintain government benefits.

To find out who can benefit from the definition, we reviewed the CMIE Strategic website. The result shows that they can only benefit medium-sized businesses with an average profit of Rs. 87 crores, as well as a fixed industrial and mechanical investment of Rs. 22.6 million. The sales revenue of potential beneficiaries is 191 times greater than the total registered MSME product in the middle.

The transformation of MSMEs under the Atma Nirbhar Bharat package aimed at addressing the pressures of informal sector businesses (and their employees) will likely benefit some 3700 companies and listed companies. Therefore, the policy appears to be a cover-up for private companies.

