

**Impact of MSMED Act, 2006 on the growth of Small  
Industries in India**

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## ***ABSTRACT***

Globally, the micro small and medium enterprises (MSMEs) are contributing a major share in their respective economies and are responsible for the growth of the economy to a certain extent. Their role in economy cannot be overlooked. The main advantage of this sector is that it provides a large employment at a low capital cost. *MSME is a dynamic and highly contributing sector that nurtures entrepreneurial talent besides meeting social objectives including that of providing employment to millions of people across the country. The researcher tries to analyze the impact of MSMMED Act, 2006 on the growth of small industries in India. It has been observed that in promotion and growth of MSMEs, the role of MSMED Act is crucial and cannot be ignored. Thus, the present paper primarily focuses on analyzing the growth of MSME sector after the implementation of this Act. The paper has been prepared on the basis of extensive review of available literatures on the MSMED Act, 2006. The present research paper reveals that MSMED Act, 2006 has had a positive effect on the growth of MSME sector in India.*

**Keywords:** *MSME, MSMED Act, Economy, Growth, Enterprises*

## **INTRODUCTION**

Micro, Small and Medium Enterprises (MSMEs) have been globally acknowledged as instruments for achieving economic growth and development as well as employment creation (Rebecca, 2009). Globally, the micro small and medium enterprises (MSMEs) are contributing a major share in their respective economies and are responsible for the growth of the economy to a certain extent. Their role in economy cannot be overlooked. The main advantage of this sector is that it provides a large employment at a low capital cost.

The importance of MSME sector can be judged by the fact that around 50% of MSMEs in India are owned by underprivileged groups. MSMEs have played a commendable role in transition of India's economy from agrarian economy to an industrialized one. The MSME sector in India is the second largest employment generator just after agriculture. It generated employment for 73.2 million people in FY11 and the figures are expected to increase to 85 million by 2014.

Micro, Small and Medium Enterprises (MSMEs) in India have evolved considerably since independence. From being referred to merely as the Small Scale Industries (SSI) sector in the 60s and 70s, the MSME sector has progressed in scale and in the scope of business activities over the years. Today, MSMEs are present across sectors (manufacturing, trade and services) in India, thereby constituting a formidable component of the country's outstanding economic growth. While a key achievement of MSMEs over time has been their talent in utilising available domestic resources to deliver quality products and services, these firms have made their presence felt across India's key sectors as well as in prominent export markets. MSMEs have made an impact on a range of issues, from industrial progress to entrepreneurship and from job creation to economic empowerment.

During the 2<sup>nd</sup> and 3<sup>rd</sup> five year plan, India's main focus was on quick industrialization. The industrialization was capital intensive and overlooked the problem of unemployment in our country. Due to rapid industrialization in certain parts, there was a regional disparity. In the year 1955, Karve Committee Report suggested to have an environment for the small industries, which facilitates their growth and which is conducive for development. In the year 1951, Industries Development and Regulation Act was implemented, which clearly stated the reservation of certain items exclusively for manufacturing by the SSI sector.

For the development of Small industries and to have a clear demarcation between the manufacturing sector and service sector, MSMED Act, 2006 came into effect from 2<sup>nd</sup> October, 2006. The main motive behind implementing the act was to make the MSMEs competitive in this era of globalization. With the same objective in view, National Manufacturing Competitiveness Programme (NMCP) was announced in 2006. The major objectives of NMCP is to ensure conducive environment for the growth of MSME sector, implementation of quality management systems, building awareness on intellectual property rights, through support for entrepreneurs and providing marketing assistance to MSMEs to market their products through proper intermediaries. Till 2005, the term SSIs and SMEs were used interchangeably. MSMED Act was enacted to increase the competitiveness of MSMEs. Table-1 reflects the segregation of enterprises according to MSME Act 2006.

**Table-1**

**Classification of Industries in MSME Act 2006**

Particulars	Investment in Plant & Machineries (For Manufacturing Enterprises)	Investment in Equipment (For Service Enterprises)
Micro Enterprises	Less than Rs. 25 lakhs	Less than Rs.10 lakhs

Small Enterprises	More than Rs. 25 lakhs and Less than Rs.5 crore	More than Rs.10 lakhs and less than Rs.2 crore
Medium Enterprises	More than Rs.5 crore and less than Rs.10 crore	More than Rs.2 crore and less than Rs.5 crore

Source: Compiled from MSME Annual Report (2012)

## REVIEW OF LITERATURE

Bala Subrahmanya (2004) highlighted the impact of globalization and domestic reforms on small-scale industries sector. The study stated that small industry had suffered in terms of growth of units, employment, output and exports. The Researcher highlighted that the policy changes had also thrown open new opportunities and markets for the small-scale industries sector. He suggested that the focus must be turned to technology development and strengthening of financial infrastructure in order to make Indian small industry internationally competitive and contribute to national income and employment.

According to Batra and Mahmood (2003), MSMEs in developing countries in East Asia receive support from local governments in the form of micro finance, interventions to increase private sector training, technology development, and market information.

Dallago and McIntyre (2003) stated that MSMEs are not themselves sufficient for growth without the proper development of institutions and support structures.

Sonia and Kansai Rajeev (2009) analyzed how far the globalization has had an impact on the MSMEs. They considered the period of study from 1973-74 to 2008-09. They analyzed the scenario before the liberalization era and as well as after the liberalization era. They analyzed the MSMEs on the basis of growth in the number of units, total production, employment generated by this sector and total contribution in exports. Their study concluded that the MSME sector has shown a better growth rate in all these parameters in the pre liberalization era as compared to post liberalization era.

The heterogeneous nature and small size of MSMEs needs adequate support from organized intermediaries. These intermediaries exist in every country in different forms. SMEs development agencies such as Small Business Administration (SBA) of the US, Small Business Service (SBS) of United Kingdom and SIDO (Small Industries Development Organization) in India are the intermediaries set up by the Government (Chandra, 2004).

In the Five year plans, MSMEs, because of their major contribution towards economy have created a major place for themselves. MSMEs have shown a relatively higher growth rate as compared to the overall industrial growth rate in the last decade. As the Indian economy is opening gates for the foreign players, it has become imperative for the government to

increase the competitiveness of MSME sector by making the flow of credit easy towards this sector. For making the sector competitive, government has implemented several schemes and programmes especially designed for the MSME sector (Rai, 2009).

The government policy towards SMEs may either encourage or discourage further expansion. Government of India has offered various attractive incentives and schemes for MSME sector but these measures backfire beyond a specified level leading to loss in valued benefits (Little et al, 1987; Mitra and Pingali, 1999). SMEs lack export competitiveness due to product reservation, regulatory policies at the entry and exit stages, lack of sufficient finance at affordable interest rates, rigid labour markets and infrastructure issues like power tariff and lack of export infrastructure (Das et al, 2007).

Bhavani T.A. (2010) studied about the quality employment opportunities generated by the MSME sector. He stressed on the point of quality employment and not short term employment. The author highlighted that MSMEs may contribute a high percentage towards employment generation but that is more quantitative in nature, rather than being qualitative. He also stressed on the use of technology for the MSMEs and argued in favour of technology upgradation, which in turn would improve remuneration, create quality employment opportunities and improve skills. Use of technology may reduce the rate of growth of employment in short run but it would ensure sustainable employment opportunities in the long run for the MSME sector.

Singh et al. (2012) analyzed the performance of Small scale industry in India and focused on policy changes which have opened new opportunities for this sector. Their study concluded that SSI sector has made good progress in terms of number of SSI units, production & employment levels. The study recommended the emergence of technology development and strengthening of financial infrastructure to boost SSI and to achieve growth target.

## **OBJECTIVES**

- To highlight the promotional and developmental activities of MSMED Act, 2006.
- To analyze the impact of MSMED Act, 2006 on the development of small enterprises.

## **MEDHODOLOGY**

The present study is majorly based on secondary data. The data has been mainly collected from various MSME Annual Reports, Statistical Abstracts of India, Annual Reports of MSMEs, Reports of Ministry of MSMEs, World Bank & IFC and Development Commissioner (MSME,GOI) etc. The study covers a period from 1990-91 to 2012-13. Extensive review of the literature provided useful insight about the impact of MSMED Act, 2006 on the Small enterprises.

## **Promotional and developmental activities of MSMED Act, 2006**

The MSMED Act, 2006 was established with an objective to promote and develop the competitiveness of micro, small and medium enterprises. The Act came into effect from 2<sup>nd</sup> October, 2006. This Act has benefited the MSME sector much more than the previous Acts that had been implemented for the MSME sector. After 65 years of independence, still a lot needs to be done for addressing the problems of MSME sector and MSMED Act is a giant step towards that objective.

MSMED Act clearly demarcates the manufacturing enterprises from the service enterprises based on the ceilings of investment. It takes service sector as well under its ambit.

The main objectives of MSMED Act are:-

- To enhance the competitiveness of MSME sector in this era of globalization
- To facilitate the overall development of MSME sector
- To Focus on all the issues related to MSME sector

### ***Building awareness on IPRs***

The objective is to create and enhance awareness about intellectual property rights (IPRs) among the units in the sector by conducting training programs/ workshop and under taking pilot studies for industries clusters. This enables them to protect their ideas and business strategies and avoid infringement of the intellectual property belonging to others.

### ***Bar Coding***

Bar coding has emerged as an important marketing tool having wide global acceptability. In order to encourage units in the sector to adopt bar coding, a provision for re imbusement of 75% of one – time registration fee is promulgated to the enterprises.

### ***Quality Management Standards (QMS)***

The scheme aims at improving the quality of the product in the MSME sector and inculcating quality consciousness among units of the sector as per global standards.

### ***Credit Guarantee Fund Scheme***

Bank extends loan facilities for the budding entrepreneurs. But usually one has to face the problems of Collateral or third party guarantee in order to avail credit from banks. Realizing this constraint, Government of India and SIDBI started with a trust known as Credit Guarantee Fund Trust in year 2000. This trust runs a scheme known as Credit Guarantee Fund Trust for Micro Small Enterprises. Under this scheme, loans are provided to the budding entrepreneurs without the hassles of collateral or third party guarantee. The purpose of this scheme is to strengthen the credit flow to the MSME sector and encourage the entrepreneurs to achieve their dreams. The main objective is that the lender should give importance to project viability and secure the credit facility purely on the primary security of the assets financed. The Credit Guarantee scheme assures the lender (Bank ) that, in case the MSE unit which has availed collateral free credit from the lender fails to pay back the amount, the trust will make up for the losses to the bank. The trust will compensate up to 75 % to 85% of the losses depending upon the gender of the entrepreneur who availed the credit and the region to which he/she belongs. A maximum credit cap of Rs 100 lakhs (Rupees Hundred lakhs only) are eligible to be covered under this scheme.

### ***Microfinance Programme***

Under the scheme, the government of India provides funds to SIDBI under a 'portfolio risk fund' (PRF), which is utilized for security deposit requirement of the loan amount the MFIs/NGOs.

### ***FDI Policy***

With the promulgation of the MSMED act 2006 the restrictive 24% ceiling prescribed for equity holding by industrial undertaking, whether domestic or foreign, in the MSME has been done away with and MSME are defined solely on the basis of investment in the plant and machinery and equipment. Thus, the present policy on FDI in MSME permit FDI subject only to the sectoral equity caps, entry routes and other relevant sectoral regulation.

## **Different Programmes for MSMEs**

### ***Entrepreneurship Development Programme***

Entrepreneurship development programs are being organized regularly to nurture the talent of youth by enlightening them on various aspects of industrial activity required for setting up MSMEs. These programs are generally conducted in DICs where they are motivated towards self-employment. The course contents of such programs are designed to provide useful information on product process design, manufacturing practices involved, testing and quality control, selection and usage of appropriate machinery and equipments, project profile preparation, marketing and pricing techniques.

### ***Management Development Programme***

The objective of imparting training on management practice system is to improve the decision making capabilities of existing and potential entrepreneurs resulting in higher productivity and profitability.

### ***Technology Up gradation Programme***

In general, MSMEs lack access to technology due to poor consultancy support/service for technological information, non availability of skilled man power, lack of awareness among entrepreneurs about emphasis on production and production cost, lack of managerial skill and poor adoptability to change trade trends. For technology up gradation DIC provide capital subsidy and other assistance to strengthen MSME Sector.

### ***Cluster Development Programme***

The ministry of MSME, government of India has adopted the cluster development program for following purposes; **i.** To support the sustainability and growth of MSMEs by addressing common issues such as improvement of technology skill and quality, **ii.** To build capacity of MSMEs for common supportive action through formation of SHGs, **iii.** To establish or upgrade infrastructural facilities in the new and existing industrial clusters of MSMEs, **iv.** To setup common facility centres.

### ***Marketing Assistance Programme***

Marketing is a key strategy to the success of any enterprise and it is more relevant about MSMEs. The sector is characterized by absence of strong brand presence in the market and largely unorganized marketing networks, unlike large enterprises. The objective of the marketing assistance programs are following; **i.** To enhance export from MSME units, **ii.** To encourage MSMEs in their efforts at tapping and developing overseas markets, **iii.** To increase participation of representatives of small or micro manufacturing enterprises under MSME India stall at international trade fairs and exhibitions.

### ***Exhibitions for MSMEs***

It is the one of the program implemented by the government of India for the promotion of MSME units. It is very help to the MSMEs to expand the reach of their market. The government of India conducted this program through DICs.

## **Impact of MSMED Act, 2006 on the Development of Small Enterprises**

**Table-2**

**Impact of MSMED Act on Small Enterprises**

<b>Clause</b>	<b>Salient Features</b>	<b>Impact</b>
1. Establishment of National Small and Medium Enterprises Board.	Mandatory quarterly meeting.	Small size of board members will make sure that the problems related to MSMEs are addressed immediately and the required corrective



		actions can be taken.
2. Concept of Enterprises	There is a very clear demarcation between manufacturing and rendering services.	It will facilitate the MSMEs to go for service sector enterprises as well.
3. Definition of Enterprises	There is a specific ceiling limit on investment in plant & machinery and investment in equipments for the manufacturing sector and service sector respectively.	Under this Act, the already existing small units can upgrade into medium units and can make use of the various facilities.
4. Filing of memoranda is optional for micro & small enterprises but it is mandatory for medium sized manufacturing enterprises, though medium sized service enterprises don't come under this obligation.	Registration is not a compulsion and its place has been taken by memorandum.	MSMEs are able to avail the benefits of the act immediately after setting up of the unit as they are free from the hassles of registration.
5. Procurement Policies	The central or the state government notifies about the preference policies for the goods and services provided by MSMEs.	It provides an opportunity to MSMEs to supply their goods and services without any hassles and helps in smooth flow of the enterprise.
6. Delayed payment penalty and dispute resolution	Period of payment by the procuring organization has been made 45 days.	On the basis of payment period, MSMEs can make a balance between their Cash inflows and cash outflows in a better manner.
7. Dispute Resolution	MSME facilitation Councils are setup and they resolve the disputes within a time period of 90 days.	This does not cost much on the pockets of MSMEs and the follow up of the matter regularly becomes easy and simple.
8. Delayed Payments	Deduction disallowed under section 23 of MSMED Act of	This clause will encourage the various procurement

	Tax audit.	agencies to make timely payments to the MSMEs and it will ensure smooth functioning of MSME units.
9. Closure of Business	Just need a statutory notification regarding the scheme of closure.	It helps in quick liquidation of the enterprise.

Source: Compiled from Annual Reports of MSMEs (2012)

MSMED Act, 2006 has had a favourable effect on the growth of MSME Sector in India. Table-3 highlights the growth of this sector in terms of Number of units, Employment, Market Value of Fixed assets and Gross Output from the period 2006-07 to 2011-12.

**Table-3**

**Growth of MSMEs after the implementation of MSMED Act, 2006**

Sl. No.	Year	Total Working Enterprise (In Lakh)	Employment (In Lakh)	Market Value of Fixed Assets (In Crore)	Gross Output (In Crore)
1	2006-07	361.76	805.23	868543.79	1351383.45
2	2007-08	377.37	842.23	917437.46	1435179.26
3	2008-09	393.70	881.14	971407.49	1524234.83
4	2009-10	410.82	922.19	1029331.46	1619355.53
5	2010-11	428.77	965.69	1094893.42	1721553.42
6	2011-12	447.73	1012.59	1176939.36	1834332.05

Source: Annual Reports of MSMEs (2012)

Table-3 clearly shows that since 2006, there has been an immense growth in the MSME sector. The number of units increased from 361.76 lakhs in year 2006-07 to 447.73 lakhs in the year 2011-12, reflecting an increase of 23.76% over the last 6 years.

Similarly, employment under this sector increased from 805.23 lakhs in year 2006-07 to 1012.59 lakhs in the year 2011-12, reflecting an increase of 25.75% over the last 6 years.

Market Value of Fixed Assets under this sector increased from 868543.79 crore in year 2006-07 to 1176939.36 crore in the year 2011-12, reflecting an increase of 35.51% over the last 6 years.

Gross Output of this sector increased from 1351383.45 crore in year 2006-07 to 1834332.05 crore in the year 2011-12, reflecting an increase of 35.73% over the last 6 years.

## CONCLUSION

Micro, Small and Medium Enterprises contribute a major portion in our economy. Though, this sector is responsible for large volume of exports, it had to face a lot of problems in smooth flow of its operation in the past. In the past, government came up with various acts for the upliftment of this sector but not much was done at the grass root level. Financial constrain still remains the biggest bottleneck for MSMEs.

Realizing the key position that MSME sector holds in our economy, MSMED Act, 2006 came into effect from 2<sup>nd</sup> October, 2006. It made a clear demarcation between the manufacturing enterprises and service enterprises. A mandatory quarterly meeting by the established board members was made a regular exercise under this Act. It facilitated the addressing of issues related to MSMEs and quick actions on the issues. Since, this Act considered Service sector also as a part of MSMEs, it encouraged various budding entrepreneurs to go for service sector enterprises like Restaurants, Tours & Travels, and Hotels etc.

This Act gave liberty to already existing small industries to upgrade themselves to medium units according to the ceilings in investment and take benefit of the various facilities. Registration of MSMEs under this Act was not made an obligation and the registration part was replaced by memorandum. Now MSMEs can avail the benefits of the Act as soon as they are setup. This Act also provides the hassle free movement of goods and services produced by MSMEs from one place to another. Another major benefit that the MSMEs get under this Act is quick dispute resolution. MSME facilitation Councils are setup and they help in quick settlement of disputes of this sector. The section 23 under the MSMED Act encourages the various procurement agencies to make timely payments to MSMEs. Even if an MSME unit wants to go for liquidation, it can do it easily under this Act.

Analyzing the data from the year 2006-07 to 2011-12, clearly indicated that how the MSME sector has grown since this Act came into effect. The total number of units has shown a growth rate of 23% over the last 6 years. Employment under this sector has also shown growth rate of 25%. Similarly, Market value of fixed assets has reflected a growth rate of 35% and Gross output of this sector has shown a growth rate of 36%.

To sum it up, it is quite evident that MSMED Act, 2006 has had a positive impact on the growth of small industries and has benefited this sector with various facilities under the Act.

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