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PAPER

Whitepaper

MSME revival and recovery:
The why and the how?

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TECHNOLOGY
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WHITE PAPER -- REVIVAL AND RECOVERY OF MSMEs

Background

The impact of COVID-19 on the economy is far from fully understood and perhaps the ravage that the pandemic is causing is not over yet. It has impacted both the supply side and the demand side of the value chain, worldwide. As a result, GDP growth rates have declined for a number of countries worldwide - not only for the developing ones, but also the developed economies. For India, given the large share of the Micro, Small and Medium Enterprises (MSMEs), in both GDP and employment, and the vast informality in the sector, the situation is perhaps graver. Why? Perhaps, because our understanding of this sector, in the absence of systematic data availability is limited.

Business, as we know, it (the pandemic) has changed, perhaps irrevocably, and the biggest impact is on people and livelihoods. According to the ILO, about 400 million people (76.2% of the total workforce) working in the informal economy in India were said to be at risk of poverty, with the coronavirus impacting their cash cycles. MSMEs, who are the backbone of India's inclusive growth story, have felt a significant impact and faced severe disruptions. As an important part of the domestic and global value chains, the plight of MSMEs is of deep concern.¹

Despite all the negative aspects, COVID-19 has also given us opportunities to not only redefine and rethink about the existing framework in not only social sectors like Education and Health, but also those pertaining to enterprises, especially the micro, small and medium ones. A key question to ask then is not only how we can ensure the revival and recovery of MSMEs, but also whether we want to go back to the world before the outbreak of this pandemic?

Introduction

The COVID-19 crisis and the lockdown were a phase of evolution for various MSME sectors. Digitalisation opened the gates for many local businesses to strengthen their operations and cope up with these stressful times.

The increasing affordability of smartphones, rising internet usage, and growing digital media use are shaping the future of MSMEs and start-ups in India. India is amongst the biggest and fastest developing markets for digital users. As [Digital India](#) emerges, one can see a paradigm shift in the conventional ways of business. The small and medium scale enterprises understand the value of digital transformation for business expansion. They believe digital proficiency is vital to set foot in the online market successfully. Needless to say, digitalization has become a critical factor for all enterprises to survive.²

While digitalisation holds a lot of promise, there are challenges aplenty in adoption of technology. This paper however focusses on a specific benefit of digitalisation – the

¹<https://www.livemint.com/opinion/online-views/opinion-covid-and-its-impact-on-economy-and-msmes-11603604611652.html>

²<https://www.financialexpress.com/industry/sme/cape-sme/msme-tech-many-msmes-are-still-unaware-of-digital-impact-they-fail-to-build-customer-loyalty-retention/2135175/>

availability of high frequency data that, when combined with other forms of data, can improve our understanding and perhaps our policy making with respect to the MSME sector.

The Centre for The Digital Future at the India Development Foundation, in collaboration with other researchers and institutions, aims to explore the use of real-time and other novel datasets to address important questions raised by experts. This project is supported by Facebook's Data for Good initiative. Under the aegis of this initiative, a number of Round Tables have been and are being organized. This paper is based on one of them: [“Revival and Recovery of MSME Sector”](#)

The focus of the discussion was on planning the revival and recovery of the MSME sector. It focused on the use of data, especially High Frequency Data, along with other traditional datasets, to understand and devise a meaningful recovery plan for the MSMEs in India.

Structure of the MSME sector and the associated issues

The number of MSMEs are around 54 times more than organized corporates. They see an almost equal distribution in rural and urban areas, with the states of U.P. and West Bengal witnessing the maximum numbers. ‘Rate of births and deaths’ of MSMEs, on an average, are approximately 3 and 2 million respectively. A lot of these distressed firms are owner proprietorships (approximately 95%). Though the Government has introduced several supporting measures like Udhyaam Registration portal which allows MSMEs to register free of cost, registration is something that eludes most MSMEs, a decision more strategic in nature; most of these firms are created by people, who cannot find a suitable job in the job market; post productive employment, the enterprise ‘dies’.

Though the employment generated by MSMEs is significant, their contribution to the country’s GDP is not in the same proportion. MSMEs are largely in the informal sector and tend to have a long-tailed distribution: large number of small enterprises which account for a very little output. They comprise, largely, of under skilled work force, and are, in addition, under audited. This also brings down the credibility of the sector. Apart from this a lot of the MSMEs tend to be stuck in a growth trap despite their potential. They are not willing to expand either because of lack of funds or strategic decisions like avoiding the labour laws, income tax, etc.³

While the former can be addressed by increasing the instruments and scope of financing made available to the businesses, the latter is complicated. With regards to financing, 30-40% of lending is in the hands of the money lender. Most MSMEs are not structured enough to easily procure a loan, leading to often collateral being required for the procurement of a loan and this leads to credit rationing. The Government of India has taken initiatives like Mudra to ensure that the MSMEs receive funding at lower rates. However, these schemes have not been as successful as was thought and there is a need to revamp them.

So even before COVID-19, the outlook of the MSME sector was bleak. The pandemic further added salt to the wounds present in the sector. The number of registrations for new enterprises was lower in April-May 2020 as compared to April-May 2019. The

³India- Country Report (2014) Labour Laws and Growth of Micro and Small Enterprises, International Labour Organisation.

number of entrepreneurial and skill building programs by the Government were lower as compared to last year.

But at the same time, this pandemic provided an opportunity to resolve these structural issues in the sector as part of revival and restructuring measures.

Data and MSMEs

There stands a need for MSMEs to 'graduate' to the next rung on the ladder – from micro to small, from small to medium and so on.

India's small and medium businesses are in the spotlight now as the Modi Government has pushed out several initiatives to boost the sector, cue Atmanirbhar Bharat. Given the current scenario due to COVID-19, more and more consumers are looking online, e-commerce is booming and it provides the potential for SMBs to transform and build on digitisation of their businesses - a shift that has been underway and began post demonetisation in 2016.

According to the Cisco India SMB Digital Maturity Study 2020, digitalisation of small and medium businesses (SMBs) could add anywhere between \$158-216 billion to India's GDP by 2024 and contribute to the country's economic recovery post COVID-19.⁴ Besides this, an important point to note is that MSMEs can intelligently use data to decipher consumer journeys; the challenge, however, lies in procurement of relevant, high-quality data and its deciphering.

Parallel to this, weaving and implementation of policies that will, actually, benefit the MSMEs, requires a number of points to be addressed, as far as data procurement, and application of the sieved information it supplies, is concerned.

In order to ensure that we get better quality data, there is a need to identify a sample of MSME companies which have a decent likelihood of survival in the next five years and track them over time. The identification of these companies is something that can also depend on the likelihood of use of electronic instruments and/or banking systems. This sample can then be merged with other available datasets to for better insights.

Another problem with data is the difficulty in getting it at one point. Data is dispersed across ministries and is often of not very good quality. The officials, many times, don't upload data on the websites, despite legislation saying otherwise. Hence, there stands a need to think of ways to either automatically capture data through digitisation or to incentivize Government officials to ensure speedy availability of data.

When it comes to types of data we have four broad categories: firm to firm transactions data, worker mobility data, credit card or bank related data and other datasets like credit registry, nightlight, etc. All these datasets can then be combined and used for either real time analysis or ex-post analysis. Ex-post analysis can be used to answer more structured questions; real time analysis can be used for faster policy evaluation or in predictive models.

⁴ <https://www.businessinsider.in/business/news/digitisation-is-the-only-choice-for-small-businesses-in-india-and-it-may-add-up-to-200-billion-to-the-gdp/articleshow/77215217.cms>

Apart from traditional datasets, researchers and policymakers need to be open to more data sources and use innovative methods to link them with the MSME sector. These can be High Frequency data like the Facebook mobility datasets, data from aggregators like (Amazon, Flipkart, Swiggy, etc.) or data from Fintech firms working with the MSME sectors. While doing so, we need to keep in mind that these external, high frequency datasets will help us to infer about a specific subsample of the sample that we would have identified.

Analysing data is an essential component for extending varied assistance to MSMEs, as most of them are too small for customized support. Capturing data is also essential to offer primary and rescue capital (as is also working closely with Fintech companies). Data pertaining to MSMEs is disparate, needs continuous updating, and, in addition, information is not available at one place, at one time. The Government has at its disposal large amounts of data that should be placed in the public domain, but this has not been the case, also because of concerns pertaining to the authenticity of the data. Data pertaining to MSMEs may be extracted at the State level (for e.g. U.P. and West Bengal), in addition to the Central level. In order to ensure the quality of data, there stands a need to identify a sample of MSME companies which have a decent likelihood of survival in the next five years. This sample can then be merged with other available datasets for better insights.

Some pertinent questions for future work

- Do we want MSMEs to survive or thrive?
- Post COVID-19, do we want to start the process of reviving the MSME sector afresh, or 'spruce-up' the 'older' version?
- How can policies be revamped to ensure that the MSME sector becomes organised (including incentivisation)?
- Is there a way to expand the role of the MSME sector in upgrading quality and supply of goods and services? In other words, can MSMEs start to play a more significant role in being better organized supporters and suppliers?
- How do we identify the subset from the sample of MSME firms that have a reasonable chance of survival and/or are likely to use banking systems and electronic instruments?
- Using newer forms of data can we identify distress in the sector before it actually happens?

Conclusion

While trying to plan a revival of the MSME sector, it is important to focus on both the structural issues related to MSMEs, as well as issues related to availability and analysis of data. The questions mentioned above are in no way exhaustive, and along the course as we try and answer some of the questions, many more will arise, but for informed policy making it is vital that we know more about this sector. Here two points need to be noted:

1. Data from non-traditional sources, as mentioned above, can be instrumental in carrying out research on structural issues as well as for real time policy making on the small business sector.
2. Some data are already available with various levels of government (for example Udyog Aadhar and other registration data, the MCA 21 data etc.), but they exist in different departments, are not standardised and often not shared despite regulations to the contrary.

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About IDF: IDF is powered by the belief that rigorous research should inform debates, discussions and decisions on matters of public policy. Over the past 16 years of IDF’s journey, the organization has worked with over 80 partners including Governments, multilaterals, corporates and civil society organisations. IDF’s research is based along four pillars: fostering an innovation economy; using technology for developmental objectives; enhancing India’s human capital; and measuring the efficacy of development policies. More info on: www.idfresearch.org

About CDF: CDF was launched on 30th October, 2019, with a vision to conduct actionable research on the impact of digitization on the economy and society. The inquiries are analytical, without any pre-determined bias, multi-dimensional and evidence-based and provides policy and regulatory insights that enable the transition to an optimal digital economy and society. The Centre was established and incubated as an entity by the India Development Foundation (IDF), a private non-profit research organisation set up as a Trust in 2003. More info on: www.cdfresearch.org