



Role of Micro, Small and Medium Enterprises (MSMEs) in India's Economic Growth

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Abstract

Micro, Small and Medium Enterprises (MSMEs) constitute the backbone of India's economic architecture. This paper examines the multifaceted contributions of MSMEs to India's Gross Domestic Product (GDP), employment generation, export promotion, and inclusive development up to the financial year 2017–18. Drawing on data from the Ministry of MSME, Annual Survey of Industries (ASI), and the Fourth All India Census of MSMEs, the paper analyses sector-wise growth patterns, policy interventions, and the structural challenges constraining the potential of this vital segment. Findings reveal that MSMEs account for approximately 29% of India's GDP, employ over 111 million workers, and contribute nearly 48% of total exports. The paper concludes with policy recommendations to strengthen the MSME ecosystem.

Keywords: Micro, Small and Medium Enterprises (MSMEs), India, Gross Domestic Product (GDP), employment generation, export promotion

Introduction

India's economic landscape is characterised by a dual structure: a relatively small organised sector and a vast unorganised sector dominated by micro, small and medium enterprises. MSMEs are not merely economic units; they are engines of entrepreneurship, innovation, and inclusive growth. Spread across both urban and rural geographies, they serve as the connective tissue between agriculture and large industry, ensuring that economic growth is broad-based rather than concentrated.

The MSME sector has been formally defined and recognised through the Micro, Small and Medium Enterprises Development (MSMED) Act of 2006, which provided a statutory basis for classification based on investment in plant and machinery (for manufacturing) and investment in equipment (for service enterprises). Under this framework, a micro enterprise in manufacturing is one with investment up to ₹25 lakh; a small enterprise up to ₹5 crore; and a medium enterprise up to ₹10 crore. For service enterprises, the respective thresholds are ₹10 lakh, ₹2 crore, and ₹5 crore.

Since liberalisation in 1991, and more so after the enactment of the MSMED Act, 2006, India's MSME sector has witnessed considerable growth. Government schemes such as the Prime Minister's Employment Generation Programme (PMEGP), Credit Guarantee Fund Trust for Micro and Small Enterprises (CGTMSE), and the Micro Units Development and Refinance Agency (MUDRA) have sought to address capital constraints, while initiatives like Make in India (2014) and Start-up India (2016) have fostered an entrepreneurial ecosystem. This paper traces the sector's trajectory and evaluates its macroeconomic significance up to 2017–18.

Review of Literature

A substantial body of research has examined the MSME sector's role in development economics, both globally and in the Indian context.

Baumol (1990) [1] distinguished between productive and unproductive entrepreneurship and emphasised that

institutional incentives determine whether entrepreneurial talent flows toward economic value creation. MSMEs in developing economies, Baumol argued, often operate in environments where informal institutions may divert energy away from productivity-enhancing activities.

Beck and Demircuc-Kunt (2006) [2], in their cross-country empirical study, found a strong positive association between SME activity and GDP growth, poverty reduction, and employment, though they cautioned that the direction of causality remains debated. Their findings are particularly relevant to India, where SMEs have historically driven rural non-farm employment.

In the Indian context, Mohan (2002) [6] documented that small-scale industries contributed significantly to manufacturing output and employment, particularly in labour-intensive sectors. Kathuria, Raj and Sen (2010) [5] highlighted the heterogeneity within the Indian MSME sector, noting that productivity disparities between registered and unregistered enterprises are substantial. The Fourth All India Census of MSMEs (2006–07), published by the Ministry of MSME, provided the most comprehensive baseline dataset and estimated around 26 million enterprises providing employment to approximately 60 million persons.

More recently, Bala Subrahmanya (2015) [9] argued that technological upgrading and cluster-based development are key to improving MSME competitiveness in a globalising economy. The role of financial inclusion, particularly through priority sector lending norms and MUDRA Yojana, has also attracted scholarly attention (RBI, 2016; SIDBI, 2017) [8].

Objectives of the Study

The present study is guided by the following objectives:

1. To assess the contribution of MSMEs to India's GDP and Gross Value Added (GVA) up to 2017–18.
2. To examine the employment generation capacity of the MSME sector.
3. To analyse the export contribution of MSMEs and their integration into global value chains.

4. To evaluate the policy framework governing MSMEs and identify structural constraints.
5. To recommend policy measures for enhancing MSME competitiveness and growth.

Methodology and Data Sources

This study is based on secondary data and employs a descriptive and analytical research design. Primary data sources include Annual Reports of the Ministry of MSME (Government of India), Fourth All India Census of MSMEs, data from the Reserve Bank of India (RBI), Small Industries Development Bank of India (SIDBI), Annual Survey of Industries (ASI) published by the Ministry of Statistics and Programme Implementation (MoSPI), and DGFT export statistics.

Time-series data spanning 2006–07 to 2017–18 are analysed using trend analysis and percentage-share computations. Sector-wise and state-wise disaggregation is performed wherever available. Data limitations are acknowledged: owing to the large unregistered component of the MSME sector, comprehensive enterprise-level census data are

available only for 2006–07, and subsequent estimates rely on projected growth rates.

MSME Sector: Size and Structure

1. Number of Enterprises

Based on the Fourth All India Census of MSMEs (reference year 2006–07), there were approximately 26.1 million working MSMEs in India. Extrapolating at the projected growth rate of around 4.5% per annum, as adopted by the Ministry of MSME, the number of enterprises rose to an estimated 63.05 million by 2017–18. The dominance of micro enterprises is overwhelming: they constitute over 99% of all MSMEs.

The sector is characterised by its largely rural and semi-urban concentration. According to census data, about 55% of MSMEs are located in rural areas, underscoring their critical role in decentralised development. The manufacturing segment accounts for around 32% of all enterprises, while the remaining 68% are engaged in services, including trade, repair, hospitality, and transport.

Table 1: Estimated Number of MSMEs and Employment (Selected Years)

Year	Estimated No. of MSMEs (Million)	Employment (Million Persons)	Growth Rate (% YoY)
2006–07	26.10	59.70	—
2009–10	29.80	69.26	4.50%
2012–13	44.78	101.83	5.10%
2015–16	51.10	108.35	4.50%
2017–18	63.05	111.40	4.20%

Source: Ministry of MSME, Annual Reports; Projected estimates based on Fourth All India Census (2006–07)

2. Classification by Enterprise Type

Micro enterprises constitute 99.4% of all MSMEs, small enterprises 0.52%, and medium enterprises 0.04% (Ministry of MSME, 2017–18 Annual Report). This skewed distribution has important policy implications: schemes designed for small and medium enterprises in terms of credit thresholds and technology support must be recalibrated to effectively reach the micro segment, which often lacks documentation, formal registration, and banking access.

The MSME sector's contribution to India's Gross Value Added (GVA) at factor cost has been a subject of robust government tracking since the enactment of the MSMED Act, 2006. As per the Ministry of MSME's Annual Report 2017–18, the sector's share in total GVA at current prices was estimated at approximately 29.7%.

In absolute terms, MSME GVA grew from ₹13.88 lakh crore in 2011–12 to ₹19.64 lakh crore in 2014–15 and further to an estimated ₹24.63 lakh crore in 2016–17. The nominal GDP of India stood at approximately ₹167 lakh crore in 2017–18 (CSO estimate), placing the MSME share at around 29–30%.

Contribution to GDP and Gross Value Added

Table 2: MSME GVA and Share in India's GDP

Year	MSME GVA (₹ Lakh Crore)	India's GDP (₹ Lakh Crore)	MSME Share (%)
2011–12	13.88	87.36	29.0%
2013–14	17.73	112.34	29.3%
2015–16	22.46	135.76	29.8%
2017–18	~26.10	~167.00	~29.7%

Source: Ministry of MSME Annual Reports; CSO National Accounts

The manufacturing sub-segment within MSMEs — often referred to as the Small Scale Industries (SSI) or MSME-manufacturing sector — has contributed approximately 7–8% to total GDP. However, the services component, comprising trade, repair, health, and hospitality, accounts for the larger portion of MSME GVA, reflecting the structural transformation of the Indian economy toward services.

Employment Generation

Employment generation is arguably the most vital function of MSMEs in the Indian context. India's demographic

dividend — a working-age population expected to peak around 2040 — makes the creation of productive employment a paramount policy challenge. Large industries and the organised sector, bound by capital-intensity and labour laws, cannot alone absorb India's annual addition of approximately 12 million new labour market entrants.

MSMEs are inherently more labour-intensive than large enterprises. The labour-to-capital ratio in the MSME sector is significantly higher: estimates from the Annual Survey of Industries suggest that MSMEs generate approximately 4 times more employment per unit of capital invested compared to large industries.

As of 2017–18, the MSME sector employed an estimated 111.4 million workers, making it the second largest employer after agriculture. This represents a more than 86% increase from the 59.7 million workers employed in 2006–07, reflecting robust job creation over the decade. The share of women workers in the MSME sector has also grown, particularly in food processing, textiles, and handicrafts. State-wise, Maharashtra, Tamil Nadu, Uttar Pradesh, West Bengal, and Gujarat account for the largest concentration of MSME employment. However, growth has also been significant in hitherto less-industrialised states like Rajasthan, Madhya Pradesh, and Bihar, indicating a gradual geographic diffusion of MSME activity.

Table 3: MSME Export Contribution (₹ Crore)

Year	Total National Exports (₹ Crore)	MSME Exports (₹ Crore)	Share (%)
2012–13	19,05,011	8,68,133	45.6%
2013–14	19,26,024	8,77,534	45.6%
2015–16	17,18,856	7,96,688	46.3%
2016–17	18,51,048	8,71,070	47.1%
2017–18	~19,62,167	~9,54,011	~48.6%

Source: Ministry of MSME Annual Report 2017–18; DGFT Export Data

India's MSMEs participate significantly in global value chains (GVCs), particularly as ancillary suppliers to large domestic and multinational corporations. Clusters such as Tiruppur (knitwear), Moradabad (brassware), Agra (footwear), Surat (textiles and diamonds), and Ludhiana (cycle parts and hosiery) are internationally recognised export hubs.

Sectoral Distribution

The MSME sector in India spans manufacturing, trade, and services. The manufacturing segment includes agro-based industries, textiles and garments, leather products, metal products, chemicals, paper and printing, and engineering goods. The services segment includes retail trade, hospitality, repair services, construction, transport, and information technology.

According to the Fourth All India Census, food products (12.1%), textile (7.5%), non-metallic mineral products (6.3%), and metal products (5.8%) were among the top manufacturing subsectors by number of enterprises. In the services segment, repair and maintenance of motor vehicles and retail trade were dominant categories.

The integration of MSMEs with the formal financial system has improved over time. Priority sector lending (PSL) guidelines mandate that commercial banks lend at least 7.5% of their Adjusted Net Bank Credit (ANBC) to micro enterprises. The launch of MUDRA (Micro Units Development and Refinance Agency) in April 2015 specifically targeted the micro segment, with loan categories named Shishu (up to ₹50,000), Kishor (₹50,001–₹5 lakh), and Tarun (₹5 lakh–₹10 lakh). As of 2017–18, MUDRA had cumulatively sanctioned over ₹6 lakh crore across more than 12 crore loan accounts since inception.

Policy Framework and Government Initiatives

The MSME policy ecosystem in India has evolved considerably since the 1990s. The abolition of the reserved list for small-scale industries, which once protected specific product categories, was completed by 2007, exposing the sector to competitive market forces. Simultaneously, the government strengthened the support infrastructure through a range of promotional schemes.

Export Contribution

MSMEs play a critical role in India's export basket, contributing to both merchandise and service exports. Their products span a diverse range including readymade garments, leather goods, sports goods, processed food, auto components, engineering products, gems and jewellery, and software services.

As per DGFT and Ministry of MSME data, MSME-related exports as a proportion of total national exports averaged around 44–48% during the period 2012–13 to 2017–18. In 2017–18, India's total merchandise exports stood at approximately US\$ 303 billion, of which MSME exports accounted for an estimated US\$ 147 billion, representing a share of approximately 48.6%.

1. Credit Support

The Credit Guarantee Fund Trust for Micro and Small Enterprises (CGTMSE), established in 2000, provides collateral-free credit guarantees for loans up to ₹2 crore (raised to ₹1 crore in 2016 and again revised). As of March 2018, cumulative guarantees approved exceeded ₹1.5 lakh crore, benefiting over 3.5 million accounts.

2. Technology and Cluster Development

The Ministry of MSME's Cluster Development Programme (CDP) has supported over 600 clusters across the country, focusing on infrastructure, common facility centres (CFCs), and soft interventions such as skill development and design. The Technology Centre Systems Programme (TCSP), funded partially through the World Bank, has established Advanced Technology Centres to upgrade sectoral technology standards.

3. Skill Development

The National Skill Development Corporation (NSDC) and sector-specific Skill Development Councils work in conjunction with MSME clusters to train workers. The Pradhan Mantri Kaushal Vikas Yojana (PMKVY), launched in 2015, has progressively incorporated MSME sector skills into its training framework.

4. Digital and Financial Inclusion

Post-demonetisation (November 2016), the government accelerated the push toward digital payments within the MSME ecosystem. The GeM (Government e-Marketplace) portal, launched in August 2016, opened public procurement to registered MSMEs, providing a significant and assured demand channel. As of 2017–18, GeM had registered over 1 lakh sellers and processed transactions worth several thousand crore rupees.

Challenges Facing the MSME Sector

Despite impressive aggregate statistics, Indian MSMEs confront a range of structural and institutional challenges that constrain their growth trajectory.

Access to Finance: Despite PSL norms and MUDRA, a significant proportion of MSMEs remain underserved by formal credit. The RBI's Report of the Expert Committee on MSMEs (2019) estimated a credit gap of approximately ₹25 lakh crore between the demand for and supply of formal finance. High collateral requirements, documentation burdens, and information asymmetries deter formal lending.

Infrastructure Deficits: Erratic power supply, poor road connectivity, and inadequate logistics infrastructure impose significant costs on MSMEs, particularly those located in rural and semi-urban areas. The cost of business for small enterprises in India remains higher than in comparator economies due to these infrastructural gaps.

Technology Adoption: Indian MSMEs lag significantly behind their counterparts in China, Taiwan, and Germany in technology adoption, research and development expenditure, and productivity. The average value added per worker in Indian MSMEs is a fraction of that in large enterprises.

Delayed Payments: The MSME Act, 2006 mandates that buyers pay MSME suppliers within 45 days. However, non-compliance is widespread, leading to working capital crises. The Ministry of MSME's Samadhaan portal for delayed payment complaints was launched in October 2017 to address this issue.

Regulatory Burden: Despite simplification efforts, MSMEs continue to face multiple inspections, registrations, and compliances under various labour, environmental, and commercial laws. The compliance burden is disproportionately heavy for small enterprises with limited managerial capacity.

GST Implementation: The introduction of the Goods and Services Tax (GST) in July 2017 had a disruptive short-term impact on many MSMEs, particularly in the informal sector. Issues related to input tax credit, frequent return filing, and the compliance burden adversely affected cash flows in 2017–18.

State-wise Performance

The MSME sector exhibits significant inter-state variation in terms of enterprise density, output, and employment. Industrially advanced states like Tamil Nadu, Maharashtra, Gujarat, and Karnataka host a disproportionately large share of registered MSMEs and account for a higher share of MSME GVA. Tamil Nadu alone accounted for approximately 8% of all registered manufacturing MSMEs. However, states like Uttar Pradesh, West Bengal, and Rajasthan account for a large share of unregistered and household-level enterprises, particularly in handloom, handicrafts, and agro-processing. Government schemes such as the One District One Product (ODOP) initiative (launched by Uttar Pradesh in 2018) reflect an attempt to leverage local specialisation and scale up MSME clusters in lagging regions.

MSMEs and Financial Inclusion

The MSME sector serves as an important vehicle for financial inclusion. As millions of micro-entrepreneurs — many of them first-generation businesspersons from

scheduled castes, scheduled tribes, and other backward communities — access institutional credit for the first time through MUDRA Yojana and self-help group linkages, financial inclusion deepens.

Women-owned enterprises represent a growing segment. As per census estimates, women-owned enterprises constitute approximately 13.7% of all MSMEs, with high concentrations in food processing, tailoring, handicrafts, and beauty services. Government schemes have increasingly incorporated gender-specific support, including preferential access to credit, training, and market linkages.

Conclusion and Policy Recommendations

The MSME sector is not merely a statistical category — it represents the entrepreneurial spirit, resilience, and productive energy of millions of Indians operating with limited resources in challenging environments. Its contributions to GDP (approximately 29.7%), employment (111 million workers), and exports (approximately 48.6% of total) as of 2017–18 affirm its indispensable role in India's economic architecture.

Yet the sector's full potential remains unrealised due to persistent credit gaps, infrastructural deficits, technological backwardness, and regulatory complexity. To unlock this potential, the following policy recommendations are advanced:

- 1. Formalisation Incentives:** The registration process for MSMEs under Udyog Aadhaar should be further simplified and linked to a unified compliance platform that reduces duplication. Incentives for formalisation, including tax benefits and preferential credit terms, should be strengthened.
- 2. Credit Architecture Reform:** The CGTMSE coverage limit should be progressively enhanced. Receivables-based financing (invoice discounting and factoring) should be mainstreamed through the TReDS (Trade Receivables Discounting System) platform to address working capital constraints without collateral.
- 3. Technology Upgradation:** The Technology Upgrade Fund Scheme (TUFS) and sector-specific technology missions should be scaled up. The establishment of sector-specific technology parks and incubators in MSME clusters can catalyse productivity improvements.
- 4. Market Access:** Public procurement mandates for MSMEs should be strictly enforced and extended. The GeM portal should be deepened with buyer capacity-building and dispute resolution mechanisms. Export promotion councils should develop MSME-specific internationalisation programmes.
- 5. Skilling and Human Capital:** Investment in vocational education and apprenticeship programmes linked to MSME clusters will improve both the productivity of existing workers and the employability of new entrants. Entrepreneurship education at the school and college level can generate a future pipeline of MSME entrepreneurs.

With sustained policy attention and structural reforms, the MSME sector has the potential to drive India toward the twin goals of a \$5 trillion economy and broad-based inclusive development.=

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