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CII
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Growth of MSMEs: Opportunities and Challenges

Theme Paper

Role of technology in Indian MSMEs

Introduction

As a sector employing 70 million people across 26 million enterprises, the Micro, Small and Medium Enterprises (MSMEs) have demonstrated tremendous potential for development in the last decade. The Indian MSMEs have registered close to a 13% annual growth and are under the constant vigil of the government, policy makers, and economists, who are looking to them as key catalysts for India's exponential economic growth. Because of the game-changing nature of this sector, there is a lot of research undertaken to study MSMEs in detail, their operating conditions, untapped opportunities and the key challenges they face today

MSMEs	IN 2000	IN 2012
Currently employing	238 lakh	700 lakh
Number of enterprises	101 lakh	260 lakh
Annual growth rate	5-6 %	12 – 13 %

Source:
Report_working_group_5yearplan-2012-17.pdf from http://www.msme.gov.in/msme_aboutus.htm,

A mere glance into some representative material on MSMEs would reveal that 'Technology' is topic that does not miss to be mentioned in any noteworthy reports or articles. Working committees, policy makers, market research organizations – all of them – unanimously agree that technology is a panacea to several hurdles faced by this sector and identifying the right technology solution is going to be key in fostering growth in this sector. In the most recent five-year plan (2012-2017), a recommendation has been made for an allocation of Rs.9500 crores for various schemes under Technology.

The challenges facing Indian MSMEs today are discussed much at length in several studies and reports. Therefore, in this brief, I'm going to restrict focus on two key topics that will sustain readers' attention

1.The Manufacturing sector that forms the core of MSMEs and role of technology in this sector

2.Various Technology options available for the Indian MSMEs in general and how MSMEs can tap into these opportunities

Vertical Focus – Manufacturing and Technology benefits

MSMEs constitute 45% of India's manufacturing output. The sector is expected to contribute 25% to GDP in the next decade and create an additional 100 million jobs. That manufacturing is the core of MSMEs is evident from the fact that more than 50% of the budget proposed under the various technology schemes for MSMEs in the twelfth five year plan is earmarked for National Manufacturing Competitiveness Programme. Manufacturing companies in the MSME sector come in all sizes and shapes – right from the ones that make small electronic components to large leather or garment manufacturers; this sector offers the highest potential for employment and an opportunity to correct huge regional imbalances. As much as the manufacturing sector is having enormous growth potential, with globalization changing the way the world economies operate, this sector is at a turning point where competition is rife and innovation is a 'must-have' than a nice-to-have'.

GROWTH PARAMETERS	EXPECTED GROWTH POTENTIAL
Increased GDP contribution	25% in 10 years
Increased employment	100 million jobs in 10 years

Source:
An Intuit study from http://www.intuit.in/msmestudy.html

Technology infusion appears to be surefooted solution for the issues facing the manufacturing MSMEs. Technology needs to be infused both through indigenous development as well as external acquisition. Specialized and competitive manufacturing technologies can create significant impact in areas of Lean Manufacturing, Quality Management, Design Expertise, Intellectual Property Rights (IPRs), and even Marketing and Communications. The emerging manufacturing sectors like aerospace, defence, nano and bio technologies also have opportunities for growth out of innovative technologies. It is important to recognize that while there are several tools and technologies available for each of these manufacturing areas, it is important to use such tools to address the specific needs of an MSME unit – a one-size-fits-all approach will not help since the need of one MSME is likely to be hugely different from that of another. Technology infusion initiative can meet with success by collaborating with premier R&D, Technical Institutes in the country and carrying out studies and tests in the vicinity of and jointly with such premier institutions. A robust technology solution, customized to the specific needs of the MSME, will achieve manifold benefits of enhanced productivity, reduced wastage and optimum use of energy in the manufacturing sector.

Horizontal Focus – Technology offerings for MSMEs
Cloud Computing and Software as a Service (SaaS):

One of the major barriers identified in technology adoption by the MSMEs is the high cost of acquiring such technologies/ softwares. With the advent of cloud computing, this barrier of high-cost for acquiring technology is slowly eroding. Cloud computing or SaaS allows for technology adopters to pay only for as much technology as they use, thus doing away with the need to make large investments in technology installation and upgrades. The Cloud offers huge scalability and agility potential, the lack of which is the biggest nightmare for the MSMEs that have invested in technologies.

Gamut of cloud computing services for MSMEs

MANAGING CONTENT VIRTUALLY ALLOWING ANYTIME ANYWHERE ACCESS TO DATA	STREAMLINING COMMUNICATIONS THROUGH EASY CONNECTIVITY	PROVIDING SECURE ACCESS TO CRITICAL INFORMATION AND PROTECTION FROM VIRTUAL THREATS AND SPAMS

healthcare and pharmaceuticals, biotechnology, aerospace need to exploit such solutions to develop and showcase their products and services. There are burgeoning infrastructure issues facing the MSMEs in urban areas, like scarcity of land, and issues with maintenance of industrial areas (waste and effluent treatment issues, water supply & drainage, issues with roads etc). Therefore, MSMEs should tap into such technologies and set shops in Tier-II cities and rural/semi-rural areas, which will also help address the urban-rural divides and regional imbalances.

Other ICT offerings: Besides Cloud computing or SaaS, there are various new technologies and tools in the Information and Communication technologies space that are engines for the sustainable growth of the MSMEs.

Market Intelligence: Tools and technologies on market intelligence will have a direct bearing on the competitiveness of an MSME. Today, one of the biggest challenges faced by MSMEs is lack of timely market information and delay in responding to the needs of the customers on account of such accessibility issues. With technological advancements, there is ease of access to MI tools, portals and service providers. Thus, MSMEs will not any be any less advantaged in tapping into Data marts and Business Warehouses to access real time information or connect with their global clients.

Resource Quality: Technology services also include creation of virtual universities and training portals which will come very handy to MSMEs that often lack qualified resources to carry out specialized and managerial activities. While specialized skills are still easier to impart through focused tool trainings, soft skills enablement is a challenge. It is as important, or perhaps more important, for employees of MSMEs to have required soft skills in order to emerge strong in a globally competitive market. CEOs and owners also need to be adequately trained to assess current market conditions, upcoming trends and emerging technologies to lead agile organizations. There is also an emerging market for certified trainers to impart standardized and efficient to MSMEs and initiatives need to be taken for standardization of online training curriculum.

Marketing and Financial Management: With social media and networks taking the world over, MSMEs must soon adopt benefits offered by these new-age mantras in order for sustainable, competitive growth. Indian MSMEs are leaving global footprints and the need to embrace initiatives like electronic marketing (eMarketing), B2B portals, setting up information dissemination centers is key.

Financial prowess is also a must-have for MSMEs to survive, let alone thrive. Banks and NBFCs are increasingly skeptical of lending finance to entrepreneurs and start-ups. Therefore, it becomes all the more important for MSMEs with new and innovative products/services to determine new sources of finance, and demonstrate promised returns on investments to their stakeholders. MSMEs should therefore move beyond using computers for merely raising Pos and invoice receipts to using efficient technologies like ERP and CRM to intelligently manage their finances.

AREAS WHERE TECHNOLOGY CAN HELP MSMEs	EXAMPLES
Product and services development	CAD, CAM, Design tools, Testing rooms
Marketing and branding	eMarketing, Market Intelligence, Info kiosks, Online Exhibitions, CRM
Resource Utilization	Training centers, Virtual universities, Online training portals
Technology consulting	Software/tool/vendor evaluation services, project management services
Financial management	M&A consulting services, Financial models and softwares for financial planning and control

Source:
KPMG analysis

In this brief, we have been able to provide only a gist of areas where technology can positively impact the MSMEs. Certainly, there are more technology offerings available in the market, and more areas where technology can make significant value-add to the Indian MSMEs. With due sponsorship from the government, and support from public & private institutions, adoption of right technologies at the right time in MSMEs can yield lasting benefits and launch India on the path to becoming a global economic leader.

MSMEs: Opportunities for growth through innovation in Aerospace and Defence

Major shifts occurring in the global aerospace and defence industry

The global aerospace and defence (A&D) industry is witnessing a significant shift. Commercial aviation will see a huge boom, while defence will continue to flatten or decline. Whilst there are still opportunities abound, particularly in Asia-Pacific, shifting demands and price pressures will force companies to rethink their strategies and increase their competitive advantages. Continued macro challenges and increased regulatory pressures will also likely drive new efficiencies, enhanced controls, and greater consolidation.

India presents a significant opportunity for growth

With spending in A&D on the rise in India, it is estimated to become the third largest market by 2020, after the US and China. Increasing passenger traffic and military expenditures are expected to boost demand for new aircrafts. Investment opportunities of US$110 billion are anticipated with US$80 billion in new aircraft and US$30 billion in the development of airport infrastructure by 2020, according to the Investment Commission of India.

Moving up the value-chain

European and American companies are now increasingly looking to India due to the comparative advantages of advanced engineering, low-cost manufacturing and local skills and capabilities.

KPMG's 2012 *Global Manufacturing Outlook* identified India as the second most popular sourcing destination, after China. A quarter of the 241 senior manufacturing executives who participated in the survey, expected to increase their sourcing activity in India over the next 12-18 months. Research and development (R&D), product development and the production of goods involving high intellectual property (IP) were the key activities they planned to source. This trend has significantly increased over the last three years and is expected to continue to do so.

MSMEs play a vital role in driving India's A&D industry

Micro, small and medium enterprises (MSMEs) are increasingly considered as India's growth engine, contributing significantly to manufacturing output, employment and exports. MSMEs account for nearly 45% of manufacturing output and 40% of total exports from the country.

The Ministry of Defence's recently revised defence offset policy now offers greater incentives to OEMs when selecting MSMEs as their offset partner. The agility, dynamism and ability to grasp new technologies – in addition to the low overheads of MSMEs are all attractive factors to global A&D manufacturers who are looking for potential partners.

A highly regulated industry

The A&D industry is highly regulated and demanding. Safety and regulatory compliance requirements are complex with stringent process and procedures a mandatory responsibility. MSMEs who are able to balance cost competitiveness with robust quality and control systems will be best positioned to compete for business with global players.

Prerequisites for MSMEs looking to compete:

- Innovation in product and process capability to drive cost competitiveness
- Excellence in technical and manufacturing capabilities
- Robust quality and control systems
- Full transparency and traceability across all processes
- Proactive understanding and compliance of changing regulatory requirements
- Vigilance and security of Intellectual Property Rights
- Alignment with government, industry and academia to drive R&D and innovation

With India's manufacturing sector maturing and moving further up the global value chain, the challenge for domestic companies looking to compete in A&D lie in scaling up and developing more sophisticated capabilities to effectively meet demand and stringent industry standards.

The opportunity is there for those MSMEs who are prepared to invest in their assets and innovate in preparation for the future.

The Indian Defence sector – MSME's perspective

The growing defence sector

India is not only one of the world's top 10 defense markets by import, but also is the one that is growing at a healthy rate. At the same time, it is also heavily reliant on foreign suppliers, with only 30 percent of its defense needs met domestically. The defence market in India presents a USD 181 bn opportunity over 2012-20, with the Indian Ministry of Defence (MoD) estimating an annual budget of USD 64 bn in 2020. The signing of several major contracts including the USD 4.4 bn (Sukhoi) deal for upgraded SU30MKI, the USD 4.1 bn (Boeing) deal for transport aircraft, , the USD 2.4 bn (Dassault and Thales) transaction for upgradation of Mirage 2000, and the USD 1 bn (Boeing) deal for P8I aircrafts has had a domino effect of enhancing outsourcing operations by the global OEMs and increasing traction in the process of identification of Indian partners

Offsets – An emerging opportunity

The Indian MoD aims to achieve better defence preparedness, own sophisticated technology, develop robust manufacturing footprint and create highly skilled workforce that could be a part of this emerging growth story. The remarkable scale of imports in the procurement pipeline has provided the government an opportunity to leverage its buying powers to develop, strengthen and promote its domestic capabilities, with an objective to attain self reliance in the defence sector.

A significant step towards developing India's domestic defence capability was taken with the introduction of offset provisions in Defence Procurement Procedure (DPP) 2005. Such offset provisions are essentially mechanisms for ploughing back a minimum of 30 percent of the contract value into India, to allow the domestic defence companies to participate in production on order values exceeding INR 300 crore that have been placed on the vendors by the Indian Government.

MSME participation in the Indian Defence sector

The stated objective (as per Indian MoD) of the Defence Offset Policy is "*to leverage capital acquisitions to develop Indian defense industry by fostering development of internationally competitive enterprises; augmenting capacity for research, design and development related to defense products and services; and encouraging development of synergistic sectors like civil aerospace and internal security*"

The government realizes that Indian micro, small and medium scale organizations would play a pivotal role in India's quest for self reliance in developing defence manufacturing capability through effective offset policy implementation.

The Indian private industry consists of more than 5,000 micro, small and medium defence companies that have primarily come into existence due to outsourcing requirements of the government DPSUs. While, over a period of time, these organizations have acquired basic quality certifications and supply chain capabilities, their growth has been highly dependent on the order inflow from the government companies

Revision in defence offset guidelines (2012)

Since its introduction in 2005, the policy has seen many revisions to address issues faced by the various stakeholders in its effective implementation. The 2012 revised policy guidelines that came into effect from 1 August 2012 are an attempt to further broaden the prospects for international defence contractors to dispense their offset obligations and smoothen the process for offset absorption by the Indian industry.

One of the major changes brought about in the revised guidelines is the provision of incentivizing prime contractors to engage MSMEs by granting multipliers for calculating offsets.

Category	Export	FDI	TOT to Indian Enterprise	Transfer of equipment to Indian enterprise
Description of category	Executing export orders for eligible products/ services.	FDI in Indian enterprises, for manufacture and / or maintenance of eligible products / services.	TOT to Indian enterprises for manufacture and / or maintenance of eligible products / services	Investment in 'Kind' in Indian enterprises through the non-equity route for manufacture and / or maintenance of eligible products/ services
Valuation of offset credits	• Amount of exported products/ services subject to value addition in India • Value addition = export amount – (imported component + Fee/ Royalty)	Amount of FDI (equity investment)	10% of value of buyback of eligible products/ services to the extent of value addition in India.	-
Multiplier	1.5 if IOP is a MSME	1.5 if IOP is a MSME	1.5 if IOP is a MSME	1.5 if IOP is a MSME
Discharge	70% minimum			

defence offsets.

There is a strong need of for skill, process and infrastructure development to help the MSMEs upgrade their functioning if they have to become IOPs of the global defence companies. In addition, limited financial resources at the disposal of MSMEs restrict their growth potential.

Governmental support in the form of Cluster Development for SMEs and setting up of an Offset Fund, along with OEMs having offset obligations could go a long way in enhancing their capabilities.

MSMEs, on their part, need to move up the learning curve quickly and develop the required long term mindset to have a sustained play in this sector

Micro, Small and Medium Enterprises- Procurement

Introduction

MSMEs play a significant role in the Indian economy in terms of output, employment generation, exports etc. MSMEs not only play crucial role in providing large employment opportunities at comparatively lower capital cost than large industries but also help in industrialization of rural & backward areas, thereby, reducing regional imbalances, assuring more equitable distribution of national income and wealth. MSMEs are complementary to large industries as ancillary units and this sector contributes enormously to the socio-economic development of the country. However, they are faced with a number of challenges in areas of credit availability and cost, raw material procurement, marketing, infrastructure availability, technology, manpower and labour laws.

In India, given the large employment generation by SMEs, specially in the disadvantaged/informal sector, the preference to SMEs is important for achieving the stated national objectives of growth with equity and inclusion. Several steps are being taken in order to facilitate the MSMEs in procurement of raw materials and marketing of finished products. Sharp fluctuations in market prices of critical items and their unavailability may be avoided by allocation of such raw material items by PSUs for distribution to MSEs. The recently government approved' Public Procurement Policy' is another step towards promoting MSEs by enhancing their competitiveness through increased participation in Government purchases, encouraging linkages between MSEs and large enterprises and increased share of supplies to Government, Ministries/Departments, their aided institutions and PSUs.

Salient features of the Public Procurement Policy:

•Procurement goal of minimum 20 per cent of the total annual purchases of the products or services produced or rendered by MSEs for every Central Ministry/Department/PSU

•Sub-target of 4% to be earmarked for procurement from MSEs owned by SC/ST entrepreneurs

•Overall target of 20% proposed to be made mandatory at the end of 3 years

•Organisation of special Vendor Development Programmes, Buyer-Seller Meets etc by central Government Ministry/Department/PSUs

•Reporting of goals set with respect to procurement to be met from MSEs and the achievement made thereto in Annual Reports

•MSEs participating in a tender quoting price within the band of L1+15% may also be allowed to supply at L1 price where L1 price is from someone other than an MSE

•Continued procurement of 358 items from MSEs, reserved for exclusive purchase

•Defence armament imports not to be included in computing the 20% goal for M/o Defence

•Review Committee and Grievance cell to be set up

MSMEs are expected to reap certain benefits with the implementation of the policy. With assured public procurement, the MSE sector has only itself as a competitor among its vast variety of products. It is expected to not only encourage better marketing strategies but also provide an incentive for new designs and technologies so that their produce can compete even in international markets. This might have a stabilizing effect on market fluctuations of demand and supply and liquidity crisis. With MSEs great employment generation potential, the new procurement policy is expected to be a boost to keep generating new products with mostly locally available resources both in material and manpower. Thus with a substantial section of national economy in good spirits, government would have its hands strengthened to chalked out policies to deal with the impact of global economic crisis.

Best Practices for assisting MSME's Procurement in Select Countries:

USA: 23% of prime contracts as statutory annual goal for small business procurement by federal agencies

Malaysia: 30% of procurement activity reserved for SMEs involved in the vendor development program

Brazil: New law in force since January 2007 establishes criteria that are meant to increase participation of smaller businesses in public procurement. Other examples of regulations that require a set percentage of contracts in particular industries must go to SMEs are prevalent in Australia, Thailand and China

Canada: In contracts for which aboriginal populations are the primary recipients, procurement is to be restricted to qualified aboriginal suppliers.

United Kingdom: Special Contract Arrangements require contracting authorities to give special consideration to buying goods and services from suppliers which employ severely disabled people.

South Africa: The 2000 Preferential Procurement Policy Framework Act provides that a preference point system must be followed in awarding public contracts

Europe: Current package of directives on public procurement designed to reduce administrative burden and costs related to tendering, make procurement systems more transparent and easier for SMEs (in particular) to access, and to encourage the use of information technology systems (e-procurement) to simplify the process

Realizing the potential of Food Processing in India: Role of MSMEs

Background

A lot has been discussed about India's abysmally low processing levels across food categories, compared to other developed countries. The Ministry of Food Processing in it's vision statement has also stipulated a target for the share of processed and value added foods for the country by 2015. It has been generally believed that higher processing levels result in higher farmer incomes, employment, improved supply chain infrastructure, improved nutritional intake by consumers. Hence various quarters of industry and Government have endorsed the need to increase processing levels in food.

This session would dwell upon taking stock of where we have reached in terms of processing levels over the last decade. Various processed and packaged food categories such as dairy products, poultry, instant foods, bakery and confectionary have been witnessing double digit volume growth over the last five years. The market is also graduating towards higher value added products such as probiotics, fortified foods, better for your foods, which in turn have a direct positive impact on gross margins.

MSMEs have a key role in taking rural and ethnic Indian products to customers in India and in Global markets. Many small enterprises have been performing this role very well in categories such as milk, processed fruits and vegetables, spices, pulp, rice and flour processing, instant foods, sea foods to name a few. However, given the enormous growth being witnessed in various food categories

It may be fair to say that the role of the MSME sector needs to be further expanded from being back-end processors with an opportunistic approach to serious value chain players with a strategic role.

This would require MSMEs to start approaching the market differently and create niches for themselves on a growth and profitability platform. This would entail MSMEs to work with single minded focus on the following 4 pillars:

- Customer centricity
- Product differentiation
- Technology as an enabler
- Capability shifts

These are the underlying drivers which could help MSMEs tread the path to strong growth, profitability and value to shareholders.

Customer centricity:

Multiple consumer trends are shaping consumption in the country. Some of these are:

- Unpackaged to packaged
- Unbranded to branded
- Increased consumption of protein oriented foods
- Convenience and on the go consumption
- Health and wellness
- Cuisine diversity

A large part of the product innovations have been coming from the larger Indian and multinational players. This is very different in some of the developed countries where smaller companies often are the pioneers of responding to consumer needs through product and process innovation. In food, like any consumer product, there is a strong need for MSMEs to be customer and market centric, and create products catering to the needs of the evolving consumers. T his, no doubt, requires investment and bandwidth, but is the only slow and painful way to create positions of strength

Product differentiation

A large section of Indian home grown entrepreneurs have traditionally been topline focused and taken the route of commodity trading, rather than serious investment in value addition and hence product differentiation. This is so evident in the fact that a very small part of our Indian palate actually has been successfully replicated in packaged formats. In developed countries, food industry players have successfully created mindspace and palate-space for packaged foods. Going ahead, the curve is steep and the competition is strong. MSMEs have to continuously innovate and create products that could help transform the consumer towards packaged, healthy and tasty alternatives as compared to the un-organized channel. The concern for supply chain challenges in India are omni-present. However these challenges could pave the way for newer shelf life enhancement formats such as microwave technology, packaging formats such as tetra brik, targeted products for specific customer groups, thrust on branding and efficient go-to-market programs. The key here would entail being pioneers, not followers.

Technology as an enabler

Technology is changing the world around us, consumers and businesses. Early bird adoption of technologies related to shelf life, cold chain, fortification, packaging could lead to competitive advantage. MSMEs have traditionally been tied down by their investment capabilities and have been largely late adopters. The new age of packaged food requires companies to look at technology as an enabler for value and differentiation.

Capability shifts

At an overall level, the critical success factors of the food business are transforming from being sourcing and manufacturing oriented to innovation and marketing & distribution oriented. This is a very drastic shift in the overall skills sets that small scale firms have traditionally invested in. The risk that MSMEs need to hedge against is to be overpowered into becoming subcontractors by market leaders or competing against the unorganized channel. To counter this the MSME segment needs to bolster its capabilities towards the emerging critical success factors of the processed foods business.

Conclusion

The role of MSMEs is crucial to the growth of the processed food sector. Firms in this segment need to move from being mere incubators of small ideas towards become vehicles for effective scale up and value creation. Many firms have started taking small steps in acknowledgement of these changes and it may be time that the entire MSME community starts looking at the processed foods space in a different light.

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