



## MSMEs and Global Value Chains

This editorial is based on [“Integrating MSMEs into Global Value Chains”](#) which was published in The Hindu BusinessLine on 02/05/2022. It talks about the significance of integrating India’s MSMEs into Global Value Chains.

**For Prelims:** MSMEs, World Bank, Economic Survey, World Development Report, OECD METRO Model, MSME Samadhan, Industry 4.0

**For Mains:** MSMEs and Global Value Chains - Integration, Significance, Challenges

The **rapidly expanding [Global Value Chains \(GVCs\)](#) of multinational corporations (MNCs)** are increasingly dominating international trade, which **emerging economies like India can hardly afford to ignore.**

The limited presence of Indian **[micro, small and medium enterprises \(MSMEs\)](#)** in the GVCs is a consequence of the negligible share of internationalised MSMEs, which is primarily due to a **weak innovation base**, owing to **weak networks of MSMEs.**

The integration of Indian MSMEs with GVCs is the need of the hour for MSMEs. **India needs to create a hub for MSMEs** as a market with linkages to various countries by building and strengthening regional innovation systems and by establishing a multipurpose science and technology commission in the clusters of SMEs.

### What Role do the MSMEs Play in the Indian Economy?

- The MSMEs play a **fundamental role in India’s economic growth**, contributing **30% to its GDP** and nearly **50% to its exports**.
  - The sector **encompasses over 63 million enterprises** and provides a **livelihood to over 111 million workers.**
- The potential of MSMEs is well recognised by industry bodies, academics, and policymakers.
  - In a recently concluded MSME conclave, the **MSMEs’ potential in building a complete supply chain**, enhancing their global competitiveness was highlighted.

### What are the Global Value Chains?

- Global Value Chains (GVCs) refer to **international production sharing**, a phenomenon where production is broken into activities and tasks carried out in different countries.
- In recent decades, international trade is increasingly dominated by global value chains (GVCs) of multinational corporations (MNCs). **More than two-thirds of international trade now takes place within such GVCs.**
- Internationalisation led by the steadily expanding GVCs has been **rapidly reshaping the**

**competitive environment of business** in the global economy.

- It has **opened national markets to new competitors**, resulting in immense opportunities for both large and small firms.

## What is the Significance of Integration of MSMEs in the GVC?

- **Employment Generation:** As the [World Bank's World Development Report 2020 \(WDR 20\)](#) suggests, contingent upon deeper reforms in developing countries and policy continuity in industrial economies, **GVCs can help reduce poverty, and continue to augment growth and employment.**
  - The [Economic Survey of India](#) also highlighted that by participating in GVCs, India's manufacturing sector may witness an **addition of four million jobs by 2025** thus contributing **one-fourth of the total in value-added terms** towards the \$5 trillion economy.
- **Boost in Income:** Cross-country estimates suggest that a **1% increase in GVC participation can boost per-capita income by more than 1%**, particularly when countries engage in limited and advanced manufacturing.
- **Productivity Improvements:** GVC participation can precipitate significant firm-level productivity improvements.
  - WDR 2020 suggests that GVC firms engaged in manufacturing activities show **higher labour productivity than one-way traders or non-traders**, after controlling for firm-level capital intensity.
  - Innovation is one another component of competitiveness, and MSMEs can test advanced technologies in a pilot mode.
- **More Flexibility:** Integration into GVCs can not only support economic growth but might also be a crucial strategy in the post-pandemic recovery.
  - **GVCs enable firms to participate in international markets more flexibly**, as they might contribute only a small component of an overall supply chain rather than a product in its entirety.
- **Shockproofing:** The [OECD's METRO Model](#) shows that localised regimes are more vulnerable to shocks, and result in a significantly lower level of economic activity and fall in national incomes as compared to the interconnected regimes.
  - While interconnected regimes build resilience, stability and flexibility in the production networks, localised regimes offer fewer channels for adjustment to shocks.

## What are the Impediments to GVC Integration?

- **Access to Finance:** MSMEs' integration into GVCs depends crucially on access to finance, however, the **credit supply shortage to MSMEs** has been a concerning gap in India's MSME sector.
  - Despite its importance and potential, the **MSME sector is often plagued by a lack of working capital**, affecting its day-to-day operations.
  - Without improved access to finance, the goal of integrating MSMEs into supply chains will remain a challenge.
- **Informalisation:** Given that **95% of the MSMEs in India are in the informal sector**, access to formal finance remains a significant constraint.
  - Studies highlight that MSMEs as a whole **receive less than 6% of bank credit.**
- **Delayed Payments:** The number of applications filed by MSMEs on the delayed payment monitoring system [MSME Samadhan](#) has **crossed the 1-lakh mark, amounting to over ₹26,000 crore.**
- **Lesser Technological Understanding:** Moreover, **MSMEs are often hesitant in adopting digital solutions** due to **limited understanding** and **inadequate training.**
  - The emergence of new technologies of the [Fourth Industrial Revolution](#) (AI, Data Analytics, Robotics and related technologies) is a **bigger challenge for MSMEs than for organised large-scale manufacturing.**
- **Other Challenges:** The **lack of skilled workforce**, knowledge and **adequate physical infrastructure** are some other constraints that inhibit the efficiency of MSMEs and thus their integration into the Global Value Chains.

## What can be Done for a Smoother Integration of MSMEs into GVC?

- **Digitisation of MSME:** A recent MSME digital readiness survey by PayPal highlighted that **29% of the MSMEs witnessed an increase in online customers** and **32% experienced better payment solutions.**
  - The digital payment ecosystem holds immense potential for MSMEs by helping them **expand their online customer base** and **enabling faster flow of funds.**
  - The adoption of digitalisation by MSMEs certainly needs to be supported more and leveraged in **providing innovative financial solutions.**
- **Digital and FinTech Literacy:** It becomes essential to **provide training** and generate more **awareness among MSMEs about digitalisation** of banking systems and their operational dynamics to make the digital transformation smoother.
  - Moreover, a **strong impetus towards greater digitalisation in finance** is the need of the hour.
  - Doing so will reduce the dependence of MSMEs on informal sources of finance and reduce their operation cost given the latter's high lending rates.
- **Role of Banks:** Banks could also play other roles to help MSMEs in GVCs - they can **facilitate networking sessions with global companies.**
  - **Regular market updates can be provided** so that the MSMEs can take informed decisions on such markets. This can help them to mitigate risks.
  - **Global banks** also have a role to play here in terms of **connecting clients globally.**
- **Policy Reforms:** Participation in the GVCs necessitates **deeper reforms in labour markets, trade infrastructure,** and improvements in the overall business environment.
  - Policies directed towards **facilitating vertical GVC linkages** between domestic MSMEs and larger foreign and domestic firms can go a long way towards strengthening India's relative position in GVC trade.

### ***Drishti Mains Question***

Discuss the significance of integrating India's MSMEs into the Global Value Chains and suggest the measures that can be taken to pursue this objective.