

# GREENING MSMES

Relevant for: Indian Economy | Topic: Issues relating to Growth & Development - Industry & Services Sector  
incl. MSMEs and PSUs

**Written by Shubham Gupta**

The micro, small and medium enterprises (MSME) sector is the backbone of the country's economy. Not only does the sector contribute nearly 30 per cent to the GDP, but the six crore MSMEs in the country also promote inclusive growth by providing employment to around 11 crore people. In next five to six years, MSMEs are envisaged to contribute 50 per cent to India's GDP and create 15 crore jobs.

These staggering numbers highlight our reliance on MSMEs. However, when it comes to meeting climate commitments and transitioning to low-carbon, sustainable development, expectations from MSMEs are low: They are limited to mere compliance with relevant environmental laws. There is no strategic roadmap to empower MSMEs to deal with transition risks, even as the global demand and supply chains swiftly shift to greener, environment-friendly processes and products while capitalising on newly generated business opportunities. For example, the transition from internal combustion engine (ICE) vehicles to electric vehicles (EVs) is expected to have a significant bearing on MSMEs in the auto-component industry as EVs have just 20 moving parts as compared to 2,000 parts in ICE vehicles. The competition is also expected to increase as new players such as tech companies and battery manufacturers, enter this industry.

Due to its unorganised nature and small size of individual firms (approximately 99 per cent of Indian MSMEs are micro-sized), the sector is among the most vulnerable in the Indian economy. The [COVID-19 pandemic](#) has highlighted this vulnerability as it is apprehended that millions of MSMEs are expected to shut down their operations owing to reduced demand caused by the lockdown. To combat this, the Rs 20-lakh-crore COVID-response package announced by the finance minister has several interventions targeting MSMEs including a much-needed revision in its definition. While these interventions should provide immediate relief to MSMEs, they miss out on the opportunity to provide a green stimulus.

As per an assessment report on financial packages announced by various countries, India's COVID-19 response stimulus is a brown package with no positive impact on the current trajectory of its manufacturing and energy industries. In comparison, countries such as South Korea, Germany, France, etc., have a net green fiscal stimulus.

For India, just achieving economic growth is not sufficient. We require job-led growth to provide employment to 400 million plus workforce. This makes the MSMEs' green transition extremely important as green sectors such as renewable energy (RE) and energy efficiency (EE) create more jobs than fossil fuel industries. A 2017 study by the University of Massachusetts estimates that a \$1-million (approximately Rs 7.34 crore) investment in RE or EE creates more than seven jobs vis-à-vis just 2.65 jobs in fossil fuel industries. A MSME-led green transition can create millions of additional jobs in the country at lower additional cost than large industries.

Catalysing the green transition of MSMEs requires recognition that downside risks of policy and demand uncertainties are more severe for them as compared to upsides. Most of them are technically and financially constrained to invest in new interventions, even if they recognise the business case for greening. However, certain government interventions can contribute in overcoming existing barriers.

Public procurement by the government, the largest purchaser of goods and services, constitutes nearly 20-22 per cent of GDP. Presently, 25 per cent of this procurement is mandated from MSMEs. However, there is no green focus in this procurement. Inclusion of a green procurement mandate in the public procurement can incentivise MSME suppliers to shift to greener products and processes. Green public procurement has been used by most OECD countries. India's own limited experience in procurement of LED lamps, star rating of appliances, etc., has been encouraging.

Access to finance is one of the biggest challenges among Indian MSMEs, with the overall financing gap estimated to be \$ 400 billion. While addressing this gap may take significantly longer time, tailored green financing programmes in key technologies and sectors such as waste management, electric vehicles, energy efficiency, renewables, will boost MSME growth in these sectors.

An increasing number of Indian MSMEs are getting integrated in global value chains, providing products and services to bigger players. A value chain driven approach of promoting greener processes and products will allow for more equitable distribution of the compliance cost. Global tech or corporate giants at the helm of these value chains should be nudged or regulated to co-share the onus of greening their respective sectoral value chains by providing necessary support to MSMEs at lower rungs. Based on global experiences, it is not an easy task but strengthening our policy framework on corporate sustainability should help us move in the right direction.

Incentives and penalties should work in tandem to promote good behaviour. Taxation of negative externalities and subsidisation or tax rebate on green investments can help nudge SMEs to go beyond just compliance. Environment regulations can also be upgraded based on risks posed by different sectors. However, these regulations need to be tested for their impact on MSMEs before large-scale enforcement.

Research and Development (R&D), skill development programmes, and strengthening of network linkages between research institutions, academia and MSMEs are required for enabling greater access to local innovations, knowledge and skill sets that are otherwise inaccessible. While this requirement is consistent across all sectors, sector-specific programmes for MSMEs would be beneficial. Similarly, training and capacity building on managerial aspects such as risk management and business development are crucial for encouraging MSMEs' participation in new markets for environment-friendly products.

Lastly, MSMEs cannot be responsive to India's green growth ambitions if their survival is consistently at stake either due to natural disasters or pandemics. To this end, there is a need to focus on adaptation strategies that can help Indian MSMEs withstand and quickly recover from such shocks. This is a multi-dimensional issue which requires continuous research, innovation in risk financing products, awareness and training, and inclusion of MSME considerations in national and state-level disaster and climate adaptation plans.

*The writer is Manager (Climate Finance), Climate Resilience Practice programme, World Resources Institute India. Vieware s personal*

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