

SMALL IS SIGNIFICANT

TRAINING AND DEVELOPMENT NEEDS OF INDIAN MSMEs



Mathew James Manimala

Small is Significant: Training and Development Needs of Indian MSMEs

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PREFACE

Developing small and medium sized enterprises (SMEs) has become a priority for the governments of almost all countries. This is based on the recognition of the important contributions made by SMEs to the economy in terms of wealth creation, employment generation and innovations in products and processes. Obviously, such contributions have a tremendous impact on the development of the economy and the quality of people's life in general. It is well known that established organizations would have a vested interest in continuing with the existing technologies in which they have made heavy investments. They are also very conservative in increasing employment; in fact, it is the declared policy of many organizations to down-size (or right-size as they call the process) their employee strength. This is why much of the contributions towards innovation and employment generation comes from the new ventures, most of which are in the SME sector. It is no wonder, therefore, that governments and policymakers are interested in developing the SME sector.

Data on the mortality of SMEs suggest that they are highly vulnerable to the vagaries and vicissitudes of environmental forces. Their vulnerabilities are generally described as the 'liability of newness' or the 'liability of smallness'. An obvious inference from the situation is that SMEs need help, especially in the early stages of their development. The traditional method of providing help to SMEs

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is by facilitating the external environment for their operation. Of late, however, governments and policy makers have realized the need for building the internal capabilities of SMEs so that they could become strong primarily because of their own internal capabilities rather than the benevolence of the environment, which cannot be expected to continue forever. It is natural that training is perceived to be a major tool for the development of internal capabilities for SMEs. Accordingly, a large number of institutions and agencies were created both in the public as well as the private sector for providing training services to the SME sector.

One of the paradoxical observations about training in the SME sector is that while the training providers strongly feel that SMEs need training, their clientele hardly have any such feeling. It was against this background that we felt the need for assessing the training needs of SMEs as perceived by themselves. Coincidentally, we found that such a phenomenon is not restricted to the Indian context but is almost universal, as was found in the literature on SME training even in the context of developed nations. Obviously, the empirical studies on this subject were done primarily in the developed nations, with hardly any in the Indian context. Recognizing the need for conducting such a study in the Indian context, the International Finance Corporation (IFC) came forward to assist this research with financial support.

The idea of a study on SMEs was first mooted by Dr. Guy Pfeffermann, who was the Director of the Economics Department and the Chief Economist for the International Finance Corporation from 1988–2003, and later became the Founder-Director of the Global Business School Network (GBSN) initiative of IFC. It was in a GBSN meeting that we met him, when he suggested that IIMB/NSRCEL could undertake a study on Indian SMEs with the funding support of IFC. Subsequently, it was Dr. Michael Graglia, Project Officer of IFC, and Ms. Vasanti Muthukumar, Consultant appointed by IFC for this project, who monitored the progress of the work and guided us with their valuable suggestions. Professional and administrative support was provided by the NS Raghavan Centre for Entrepreneurial Learning (NSRCEL) at the Indian Institute of Management Bangalore (IIMB). As one of the missions of NSRCEL is to provide training to SMEs, we felt it was important for us to make an assessment of the training needs of SMEs, and hence it was chosen as the theme for the proposed research project.

While the findings of the study generally conformed to those of the Western studies, it has also generated a lot of insights about the special nature and concerns of Indian SMEs, especially in the new and high-tech segments. Analysis of the sub-segments based on size, nature of business, and level of technology used has also yielded a few interesting hypotheses. The theoretical and practical implications of these findings, especially for researchers and policy-makers, are discussed in the concluding chapter.

This book is divided into eight chapters. The first chapter presents the introduction and the review of the literature, which explains the context and relevance of the study. The second chapter discusses the methodology of the study and the

research tools used. The results and discussions are presented in the third, fourth, fifth, sixth and seventh chapters, each one except the third, being dedicated to the analysis based on a specific sub-classification of the sample. The third chapter presents the macro analysis of the total sample, while the seventh chapter has the analysis based on two dimensions, namely, the type of business activity and the level of technology used. The last chapter presents the conclusions and their theoretical and practical implications along with the recommendations for policy initiatives.

The study was conducted in Bangalore, the Silicon Valley of India, and hence it can be considered to be especially representative of the new-gen SMEs, although it was observed that the older types of industries were still predominant in our sample. As we have taken special care in developing a master list of all SMEs in and around Bangalore and to select 300 respondents using the process of random-number generation, we can legitimately claim that the sample is reasonably representative of SMEs in India and, to a large extent, of the emerging economies. It is with this confidence that we present the findings of this study to the community of SME entrepreneurs as well as the SME trainers, consultants, policy-makers and researchers.

—*Mathew J Manimala*

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It goes without saying that, in conducting this study and preparing this report, we have received a lot of support from a few national and international institutions and several individuals associated with these institutions. Financial support from the International Finance Corporation (IFC) was indeed the most critical resource support that made it possible for us to conduct this study. As we have mentioned in the Preface, it was Dr. Guy Pfeffermann, Director-GBSN, who mooted this idea during his discussions with us on the Global Business School Network (GBSN), a networking initiative of IFC. Subsequently, it was Dr. Michael Graglia, Project Officer of IFC, and Ms. Vasanti Muthukumar, Consultant appointed by IFC for this project, who monitored the progress of the work and guided us with their valuable suggestions. We thank them for their seminal contributions for the design and conduct of this study.

At IIMB, it was the N S Raghavan Centre for Entrepreneurial Learning (NSRCEL) that hosted this project, which was initiated when the author of this report was the Chairperson of NSRCEL. We gratefully acknowledge the support and encouragement provided by the founder of NSRCEL and the Chairman of its Advisory Council, Mr N. S. Raghavan, for all entrepreneurship-related projects, such as research, education & training, and incubation. Prof. S. Sundararajan, who succeeded this author as the Chairperson of NSRCEL, was also very supportive of

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this project and provided all administrative assistance required. In this context, we should specially mention the administrative support provided by Mr R. Nagaraj, Chief Operating Officer of NSRCEL and his team. The support from the larger institutional system was made available under the guidance of the Director of IIMB, Prof. P.G. Apte, and the then Dean (Academic), Prof. R. Srinivasan, which was continued under his successor as Dean (Academic), Prof. Shyamal Roy.

While the academic and administrative support for the project was provided by the concerned staff at IIMB, the specific individuals who helped us with various tasks of the project are: Mr Sudhir Kumar who handled the overall responsibility for administering the project as well as for collecting and analyzing the data; Mr Gloryson R. B. Chalil (doctoral scholar then) and Mr Rajeev C. M. (project associate), who helped with the data collection; and Mr P. Sridhar and Mrs. R. Gowri who provided the secretarial assistance. Last but most important, it is the contribution from the 300 SME owners/ directors, whose responses form the basis of the analysis presented in this book, that has made it a worthwhile effort both for the author as well as the potential readers.

While I thank the institutions and individuals who helped me in carrying out this research project, I take the responsibility for any inadequacies in the analysis and presentation. It is my fervent hope that the data-analyses, inferences and recommendations presented in this book will be useful for researchers, academics, consultants, trainers, entrepreneurs as well as policy makers.

—*Mathew J Manimala*

CHAPTER 1

INTRODUCTION

Characteristics, Concerns and Institutional Environment of Indian MSMEs, and the Rationale for the Study

There is a growing recognition of the fact across the globe that micro, small and medium enterprises (MSMEs) have a catalytic role in the economic development of nations. In fact, they are considered to be the driving force behind the growth and vibrancy of any economy. The contributions of MSMEs to employment generation, economic output, innovations in products and services, balanced regional development, and alleviation of poverty, are being appreciated by Governments and the civil societies alike. The MSME sector has been serving as a nursery for nurturing entrepreneurial talents of citizens so that they are enabled to create large and growing ventures over a period of time. Some units from the MSME sector grow over a period of time and ultimately graduate as large entities, although their numbers are relatively small (rather miniscule). According to the [Annual Report \(2020–21\)](#) of the Government of India Ministry of MSME, the total number of Micro enterprises in India is 630.52 lakh (which is more than 99% of the total estimated number of 633.88 lakh MSMEs), whereas the Small sector has about

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3.31 lakh units (0.52%) and the Medium sector has only 0.05 lakh units (0.01%). The unduly skewed proportions in favor of micro units among MSMEs in India (compared to other emerging economy nations, as reported in the next paragraph below) may be due to the fact that the definition of MSMEs in India is based on investments, which are periodically revised upwards to adjust for inflation, and hence would include more units in the lower categories. On the contrary, if the definitions are based on the number of employees, as is done in many other countries, there is no need for periodic revision of the norms, except when the technological developments would cause drastic reductions in labour-requirements. However, as the financial resources available with MSMEs are limited and their operations are of a very small scale, they are generally slow in adopting new technologies. (Issues related to the definition of MSMEs will be discussed in a subsequent section of this chapter).

Following the enactment of the Micro, Small and Medium Enterprises Development (MSMED) Act in the year 2006, the Government of India integrated two of its ministries, namely: the Ministry of Small Scale Industries (M/o SSI) and the Ministry of Agro and Rural Industries (M/o ARI), to form the Ministry of Micro, Small and Medium Enterprises (M/o MSME, 2023). Until that time, there were no separate definitions of Micro and Medium industries in India, wherein both these categories were covered under the broad umbrella of Small Scale Industries (SSI). In other countries, however, there was special focus on medium scale industries. Accordingly, the sector was designated as ‘Small and Medium Enterprises (SMEs)’, where the micro industries were included under the ‘Small’ category. For the purpose of the present research, we would follow the ‘SME’ categorization, mainly for two reasons. One is that micro-enterprises are mostly ‘self-managed’ by the entrepreneurs with very few employees, if any. Even when they employ someone, they will be their family members or relatives. Hence it is unlikely that they would feel the need for training their so-called employees. If at all some training is needed, the number of people to be trained will be too few that it will not be viable to organize any formal training sessions for them. The most common practice in such situations is for the proprietor to provide the required training to his/her employees on the job. The second reason is that the sponsors of this research project, the International Finance Corporation (IFC), which provided funding support for this project, had the specific objective of assessing the training needs of SMEs. For the above reasons, the present study will follow the SME categorization, and structure the subsequent discussions and research on the ‘Training Needs of SMEs’.

The World Bank report on SME finance (World Bank, 2017) estimates that about 90% of all business units worldwide are SMEs, and that they generate more than 50% of employment. Their contribution to GDP in emerging economies is about 40%, which will be much more if the contributions of informal (unregistered) SMEs are also taken into account. Thus, the role of SMEs in the economic development is especially important for the developing countries. Ac-

According to a United Nations report (UN-DESA, 2020), there are about 365–445 million MSMEs in emerging economies, out of which only about 25–30 million are formal SMEs, about 55–70 million are formal (registered) micro-enterprises, and about 285–345 million are informal (unregistered) micro-enterprises. It is obvious that among MSMEs only a small percentage (about 7%) are SMEs, and the remaining 93% are micro enterprises, of which only about 15% are formal (registered) units, with a large majority of MSMEs (about 78%) being informal/unregistered micro units.

According to a survey on start-ups in the US (Mansfield, 2019), a large majority of start-ups have very small beginning, with almost 70% starting at home, and about 50% of them failing by the 5th year (which is an indication of their vulnerabilities). Data on the Indian economy too show a similar picture as may be seen from the tables given later in this chapter. The literature also suggests that the SME sector is characterized by a lot of flexibilities as well as vulnerabilities. They are also in a paradoxical situation of being in need for training and other kinds of assistance and not being able to recognize this need and/or pay for such services.

SMEs: SPECIAL FEATURES AND CHARACTERISTICS

While most businesses start as small enterprises, it is only a miniscule proportion of them that launch themselves on a growth path (Manimala, 2022). The latter group is different in some of the general characteristics of SMEs, especially in terms of their greater market-orientation (rather than production-orientation), willingness to delegate routine tasks (rather than personally supervise and control them), and focus on long-term strategies (rather than short-term operational issues), as was also observed by Smallbone et al. (1995). However, the present sub-section proposes to briefly describe the characteristics attributed to the businesses that would remain as SMEs for a fairly long period of time without achieving any significant growth. Many are the features identified by researchers (e.g.: Gélinas and Bigras, 2004) as distinguishing characteristics of SMEs, such as: limited number of owners (mostly one or two); need for autonomy and independence; high involvement of owners in the business and their low propensity to delegate; focus on producing for the existing market (which is often a single large customer) rather than exploring new markets; priority to effectiveness over efficiency; flexibility in operations as well as in the organizational structure to facilitate internal and/or external interactions; less precise division of responsibilities, which promotes greater interaction among different levels; simplicity of decision-making processes; greater use of labour and relatively low utilization of technology (especially IT and ITES); focus on the immediate and urgent actions and incremental planning rather than on long-term strategies; limited access to financial resources; greater emphasis on stability rather than on growth; more of informal rather than formal communications; and so on. Some of the special characteristics of SMEs and their implications are briefly described below.

(a) Entrepreneurial Initiatives of Individuals or Small Teams

SME startups tend to evolve around a single entrepreneur or a small team of entrepreneurs, often leveraging on a skill-set specifically available in the team. There are some SMEs that are being set up purely as a means of earning livelihood for their proprietors. These include many trading and retail establishments. While in most countries the definition of SMEs continues to include only manufacturing and services, there are other countries that adopt a broader definition and include retailing as well. According to a report on small businesses in the US (Main & Bottorff, 2023), about 99.9% of the startups are small, and about 80% of these are having single owners and are managed without any employees. Although the individual or small group initiatives help in focusing the action, it also becomes a serious limitation when actions beyond the interests and competencies of the promoters are required by the exigencies of business growth.

(b) Operational Flexibility

The direct involvement of the owner(s), coupled with flat structures and the involvement of a small number of people ensures that there is greater operational flexibility. While it is generally believed that SMEs have greater operational flexibilities, some researchers have found that their flexibilities are restricted to certain aspects of business such as strategic planning and HR management, whereas the large firms are more flexible in respect of technological capability, sourcing practices, integration practices, etc. (Mishra, 2016). On the other hand, decision-making on such important issues as changes in product-mix or price-mix in response to market conditions would be faster in SMEs. The trouble is that the speed in decision-making can also lead to arbitrariness and lack of proper analysis.

(c) Relatively Lower Cost of Production

There are different claims about the cost structures of large organizations and SMEs. It is often argued that the large organizations can derive cost advantages through economies of scale and smooth cash-flows from different sources. While SMEs do not have such advantages, they have the benefits of lower overheads and wage structures, whereas large organizations have the burden of heavy fixed investments and high rates of wages, salaries and employee-benefits. Besides, SMEs can often create flexibility even in the 'fixed' type of costs by hiring such services as and when required, which is being done by many SMEs for their digital infrastructure needs (Varughese, 2021). Such measures for reducing wages and overheads translate into lower cost of production, at least up to limited volumes. Lower costs offer great initial advantages especially in attracting and retaining price-conscious customers but can also act as a deterrent against the firm in taking up value-added services for the higher-end markets. With the low rates of compensation in SMEs, they would find it difficult to attract specialists and experts required for upgrading their products and services.

(d) Positive Inclination to New Technologies

There are two apparently contradictory perspectives about the technological inclinations of SMEs. One is that they have a greater propensity to adopt and internalize the new technologies, which is facilitated by their flexibility, informality and adaptability (Renuka & Venkateshwara, 2006; Dean et al., 1998). The opposite perspective is that they are low on the utilization of technological developments (Gélinas and Bigras, 2004), as this would require heavy investments, including in R&D. Such contradictory perspectives can be explained by the fact that they are probably referring to two different stages in the life of SMEs. When new technologies emerge, some individuals in the community may be quick to perceive the entrepreneurial opportunities offered by them and create new ventures based on them. Thus, there are many ventures that start with new technologies, as the entrepreneurs would perceive very little competition for them in the market. On the other hand, if a venture is already started with conventional technologies, any further developments happening in the field are unlikely to be adopted by SMEs, for fear of the investments required in people and infrastructure. The two apparently contradictory perspectives can thus be reconciled. Although the startups based on new technologies have very little competition, they may also have a high propensity to fail because of low market-acceptance. The so-called ‘first-mover advantage’ may turn out to be a ‘first-mover disadvantage’ for some startups. Their successors may learn from the failures of the first movers and make it a success later.

(e) Capacity to Innovate, With a Focus on Niche Markets

SMEs have shown a high degree of skill in innovation, improvisation and reverse engineering. This is because such decisions need not be approved by several levels in the organization as required in large established organizations. SMEs are adept at meeting niche-market requirements and capturing export markets where volumes are not huge. Focusing too narrowly on niche markets has its dangers too, especially when the niche is prone to frequent and turbulent changes.

(f) Employment Generation

SMEs are usually the prime drivers of job creation in any economy. Data from some developed countries show that the SME sector is responsible for up to 80% of the new jobs created in those countries. This is to be expected, as larger corporations generally operate with a ‘right sizing’ orientation and are constantly trying to reduce employment. So, the new jobs come primarily in the growth-oriented new/small ventures. There is also a tendency for SMEs to use labor-intensive technologies as it helps them avoid high initial investments as well as create flexibilities in operations. Though labor-intensive technologies would save costs in the short run, it can be costlier in the long run especially when the numbers grow large and competitors come up with cheaper production-technologies.

Data on employment generated by Indian MSMEs are as follows ([Annual Report, 2021–22](#)): 630.52 lakh Micro-units employed about 1076.19 people (with an average of 1.70 employees per unit); 3.31 lakh Small-units employed about 31.95 lakh people (with an average of 9.65 employees per unit); and 0.05 lakh Medium-units employed about 1.75 lakh people (with an average of 35 employees per unit). It is obvious that the contribution of Micro-units to employment-generation is rather limited. An average of 1.7 employees per unit would imply that there could be many units with one or no employee. The real contribution to employment generation within MSMEs is from the Medium-sector, but they constitute only a minuscule segment of 0.16% of MSMEs. The largest segment among MSMEs is the Micro-units, which constitute about 97%, and their contribution to employment generation is practically nil. In general, one can say that MSMEs are employment-minimizers (rather than generators), except for a very small percentage of growth-oriented ventures among them. Most MSMEs would like to minimize investments in all aspects of their business, including labor.

(g) Utilizing Locally Available Human and Material Resources

SMEs provide jobs locally and hence utilize the manpower available locally. Since it is unviable for them to transport materials over long distances, they often improvise with materials that are available locally. The same is the case with human resources. SMEs do not have the resources or the capability to do national or global search for experts or to attract and retain them, if found. Hence, they develop a tendency to manage with what they have rather than what they need. While this orientation helps in the initial years to reduce costs substantially and get things going, it can become a major hurdle to quality improvement and enterprise growth at a later stage.

(h) Reducing Regional Imbalances

Unlike large industrial units where divisibility of operations is more difficult, SMEs enjoy the flexibility of location. In developed countries, SMEs can be found to be spread virtually everywhere, even though some specific locations emerge as ‘clusters’ for units of a similar kind. Nevertheless, the spread of SMEs is a fact, which enhances their attraction from a national or regional policy of balanced development. The localization of SMEs and the consequent spreading to different localities and regions are due to their inability to make large investments and service customers in multiple locations. Hence, different SMEs are created in different locations to cater to the local needs, leading to the spreading of SME units. Although the individual contribution of each SME may not be perceived as significant, their large numbers spread out in different regions of the country will prove to be a boon to the overall development of the nation by reducing regional imbalances ([Durante, 2004](#)). The impact of the SMEs on a particular region will,

however, depend on the social capital available and the social embeddedness of the firm (Cooke et al., 2005).

SMALL AND MEDIUM ENTERPRISES (SMEs): DEFINITIONAL ISSUES

Though ‘SME’ is a widely used acronym to collectively designate the small and medium enterprises as a group, the Government of India definition was initially restricted only to the Small Scale Industries (SSI) sector. This was probably because such definitions were used primarily for determining the small units’ eligibility for certain concessions and preferential treatments, for which the medium and large units were not considered. SSIs in India were defined in terms of their investment in plant and machinery, which was Rs. 10 million for the general category and Rs. 50 million for some specific product categories. Later, after the enactment of the MSMED (Micro, Small and Medium Enterprises Development) Act in 2006, bringing the Micro and Medium industries into the fold of ‘SSI’ with separate definitions for them, the norms got revised further upwards. As per the latest norms implemented with effect from 1st July 2020, MSMEs are defined using the Composite Criteria of Investment in Plant & Machinery/Equipment and Annual Turnover (Ministry of MSME, 2023). Accordingly, there are three categories of what was defined earlier as Small Scale Industries, which are as follows:

- Micro Units are defined as those with Investment in Plant and Machinery or Equipment not more than Rs.1 crore (10 million) and Annual Turnover not more than Rs. 5 crore (50 million);
- Small Units are defined as those with Investment in Plant and Machinery or Equipment not more than Rs.10 crore (100 million) and Annual Turnover not more than Rs. 50 crore (500 million); and
- Medium Units are defined as those with Investment in Plant and Machinery or Equipment not more than Rs.50 crore (500 million) and Annual Turnover not more than Rs. 250 crore (2500 million).

Most other countries use the number of employees as the criterion for defining SMEs, the general norm being less than 10 for Tiny/Micro units, 10–49 for Small units, and 50–249 for Medium units.

Small firms are a heterogeneous group, including sole proprietorships and partnerships to limited companies, with a range of businesses such as trading, manufacturing and services, which may be in various stages of development, such as start-ups, expanding businesses, stable and steady ones, and the so-called ‘lifestyle’ businesses seeking profitable growth (Dunsby, 1996). According to Gibb (1996), small business is a way of life; it is about personal risk; it means managing interdependencies, where ‘know-who’ and ‘know-how’ are more important than ‘know-what’; it means standing alone, where the buck really stops with you; it

means learning by doing (see also UNCTAD, 2001: 133), which manifests in a variety of ways and hence defies classification.

According to the earlier definition of the Ministry of SSI, Government of India, SSIs are industrial undertakings in which the investment in fixed assets in plant and machinery whether held on ownership terms, on lease or on hire-purchase, does not exceed Rs.10 million. The Small Scale Service & Business Enterprises (SSSBEs) are industry-related service and business enterprises with investment in fixed assets, excluding land and building, up to Rs. 1 million, irrespective of the location of the units (Ministry of SSI, 2004). There is also a definition for micro-enterprises, which were then popularly known as “Tiny Units”. A tiny unit is one where investment in plant & machinery does not exceed Rs. 2.5 million”. (Ministry of SSI, 2004)

One of the well-accepted definitions of SMEs in the international context is by the Commission of European Communities which states that: “The category of micro, small and medium-sized enterprises (SMEs) is made up of enterprises which employ fewer than 250 persons and which have an annual turnover not exceeding EUR 50 million, and/or an annual balance-sheet-total not exceeding EUR 43 million. Within the SME category, a small enterprise is defined as an enterprise, which employs fewer than 50 persons and whose annual turnover and/or annual balance-sheet-total, does not exceed EUR 10 million. And within the SME category, a micro enterprise is defined as an enterprise, which employs fewer than 10 persons and whose annual turnover and/or annual balance-sheet-total, does not exceed EUR 2 million” (European Commission, 2003).

For the purpose of the present study, we thought it is more appropriate to choose a definition based on employment rather than turnover or investment. This is not only because this study is aimed at assessing the training needs of SMEs, which would naturally be linked to the number and types of employees with the unit, but also because entrepreneurs may be guarded against revealing their financial data, and even in cases where the accurate data are obtained, the value of the same amounts invested in different years may not be comparable. Accordingly, our definition of SMEs for the present study is as follows: Micro/Tiny enterprises are defined as those firms with less than 10 employees, small enterprises with 10–49 employees, and medium as those with 50–249 employees. While this is an operational definition, which helps the researchers to identify the population and select the sample, the practitioners and policy makers look at it in a different perspective, as may be seen from the following statement: “Definitions become particularly important where they are used to set thresholds for eligibility for grants or regulations” (Confederation of British Industries, 1996).

THE INDIAN SME SECTOR—AN OVERVIEW

The data given in this section are about the period when India had an exclusive definition of Small Scale Industries (SSIs), which did not include the micro- and medium industries. Accordingly, India then had more than 3 million SSIs, which