

Effect of Demonetization on Employment Generation in Micro, Small and Medium Enterprises

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Abstract: In Indian economy small-scale and cottage industries occupy an important place, because of their employment potential and their contribution to total industrial output and exports. Small scale industries are largely dependent on cash in comparison to large scale industries where transactions can be made cashless. Demonetization has created a cash crunch that has sent the small scale units into disarray. Demonetization move has threatened large scale unemployment in small industries sector. The associated chambers of commerce in India (ASSOCHAM) president said that demonetization has negative impact as well because industries are suffering and people are losing jobs. The basic objective behind writing this paper is to elucidate the role of small scale industries in employment generation and effects of demonetization in creating unemployment in these industries. To achieve this objective we analyzed secondary data source and the same has been verified by the primary data analysis.

Key words: [Demonetization, Small Scale Industries, Cashless Economy, Employment]

1. Introduction

The importance of small-scale industries is very important to break the vicious circle of poverty, to generate employment for rural development and to provide balance in upliftment of developmental activities. The estimated contribution of this sector, to the country's GDP during 2012-13 was 37.54 per cent; while the total employment in the sector is 805.24 lakh; and the share of MSMEs in India's total export for the year 2014-15 was 44.70 per cent [1]. By less capital intensive and high labor absorption nature, SSI sector has emerged as an employment generating sector. SSI plays a key role development, has high potential for employment generation, diversification of the industrial base and dispersal of industries to rural and semi urban areas. In spite of having small scale industries which generates about 38% employment in the economy, the unemployment rate in India is 8.8% [2]. As per fifth annual employment-unemployment survey at all-India level, about 77 per cent of the households were having no regular wage/salaried person. Unemployment rate in India has shot up to a five-year high of 5 per cent in 2015-16, with the figure significantly higher at 8.7 per cent for women as compared to 4.3 per cent for men,

says a report by Labour Bureau [3]. Small scale industries mostly depend upon unskilled labour force. The Economic Survey 2014-15 stated that as per the Labour Bureau Report 2014, the present skilled workforce in India is only 2 %, which is much lower when compared to the developing nations [4]. A small scale unit located in a remote backward area may not have problem with respect to unskilled workers but this labour force is dependent upon the small cash amount for their daily bread and butter. Their wages are needed to be paid in cash. Therefore, due to demonetization such SSI units are facing acute shortage of cash amount for the payment of their unskilled labors. Government's move to demonetize currency will impact the SSI sector such as 'Secondary Steel Sector' as most of the business conducted by these mini mills and rolling factories is cash-based, which in turn would help the large producers, such as Tata Steel Ltd. Tata Steel said that demonetizing will also temporarily impact steel demand in rural India as the business there is mostly cash-based [5]. As the demonetization move completes one month on 8, December Thursday, the negative impacts are echoing louder now. The biggest threat being felt is an increase in unemployment, especially massive layoffs in small and medium scale industries sector [6]. The lopsided rural-urban spread of ATMs and bank branches has snuffed out economic activity in rural India, with micro, tiny and small enterprises finding it impossible to get cash in 100-rupee notes for their daily operations. This paper analyses the impact of demonetization and its tenure on small scale industries. There is a need in the economy to scrutinize the current situation of SSI in terms of employment generation.

2. Objective

The main objective of the study is to examine the effects of 'Demonetization- November 2016' on the employment generation capacity of the MSMEs during demonetization period. Besides this main objective, the paper also intends to study: (1) the importance of MSME sector in Indian Economy. (2) Employment generation in MSMEs.

3. Literature Review

Literature has been studied to understand the various key concepts for the purpose of this research paper. Literature review has the objective to lay down the

foundation for analyzing the effect of demonetization on employment generation in MSMEs. The research papers, news articles and various knowledge sources have been explored and explained in the following paragraphs.

3.1 MSMEs: - MSMEs are transcendent for the overall development of Indian Economy. This enterprise acts as an alternative for large scale industries which occupy an influential place in any developing country like India. Although the primary responsibility lies with the state Governments for the development and promotion of MSMEs, the culminate body for the inception and enforcement of decree and supervision to MSMEs in India is Ministry of Micro, Small and Medium Enterprises. Micro, Small and Medium Enterprises Development (MSMED) Act, was notified in 2006, to speed up the development of MSMEs. In accordance with the provision of Micro, Small & Medium Enterprises Development (MSMED) Act, 2006 the Micro, Small and Medium Enterprises (MSME) are classified in two Classes:

(a) Manufacturing Enterprises- The Manufacturing Enterprises are defined in terms of investment in Plant & Machinery.

Table 1: Classification of Manufacturing Sector MSME

Enterprises	Investment in Plant & Machinery
Micro Enterprises	Does not exceed twenty five lakh rupees
Small Enterprises	More than twenty five lakh rupees but does not exceed five Crore rupees
Medium Enterprises	More than five Crore rupees but does not exceed ten Crore rupees

Source: Development Commissioner (MSME), Ministry of Micro, Small & Medium Enterprises, Govt. of India. http://www.dcmsme.gov.in/ssiindia/defination_msme.htm

Table 2: Classification of Service Sector MSME

Enterprises	Investment in Plant & Machinery
Micro Enterprises	Does not exceed ten lakh rupees
Small Enterprises	More than ten lakh rupees but does not exceed two crore rupees
Medium Enterprises	More than two crore rupees but does not exceed five core rupees

(b) Service Enterprises: The limit for investment in plant and machinery / equipment for manufacturing /

service enterprises, as notified vide S.O. 1642(E) dtd.29-09-2006 are as under:

Source: Development Commissioner (MSME), Ministry of Micro, Small & Medium Enterprises, Govt. of India. http://www.dcmsme.gov.in/ssiindia/defination_msme.htm.

Fourth All India Census of Micro, Small & Medium Enterprises 2006-2007 classified the MSMEs into Registered and Unregistered Sectors. It defined the registered and unregistered sectors as:

3.2 Role of MSMEs in Indian Economy

MSMEs constitute a large part of Indian Economy. It also has a very important contribution towards development of the Economy. “During the past decade this sector has recorded higher growth rate as compared to overall Industrial Average. The total number of MSMEs operating in India significantly increased 207 per cent between 2000-01 and 2009-10 and the sector registered a sterling 21.52 per cent compounded annual growth in terms of production [7].”

Role of MSMEs in Employment Generation and Socio-economic Development: As per final report of fourth all India census of MSME “60.22% of enterprises are operating in Rural Sector” [8]. This report also says that “9.09% units were reported to be women enterprises where as 62.43% enterprises were found to be owned by socially backward groups, viz., SCs, STs and OBCs.” [9] So a significant role of this sector can be seen in the changed society. “It is estimated that in terms of value, the sector accounts for 45% of the manufacturing output and employs over 6 crore people [10].” The labour to capital ratio in MSMEs and the overall growth in the sector is much higher than in the large industries. Thus the existence of MSMEs in India provides a platform to achieve the goal of prosperity with fairness and involvement of all.

Table 3: Contribution of MSME Sector in GDP and Output (At 2004-05 prices)

Year	Share of MSME Sector In Total GDP (%)			Share of MSME Manufacturing output in total Manufacturing Output (%)
	Manufacturing Sector MSME	Services Sector MSME	Total	
2010-11	7.39	29.30	36.69	38.50
2011-12	7.27	30.70	37.97	37.47
2012-13	7.04	30.50	37.54	37.33

Source: Annual Report MSME 2015-16, Ministry of MSME, GOI. Table 2.3 [12].

Contribution in GDP and Output: MSME sector in India has significant contribution in GDP and manufacturing output. “The estimated contribution of manufacturing sector Micro, Small and Medium Enterprises (MSME) to GDP, during 2012-13, is 7.04%. However, taking into

account the contribution of services sector MSME, which is estimated at 30.50% during 2012-13, the share of MSME sector in GDP of the country, during 2012-13, is 37.54% [11].

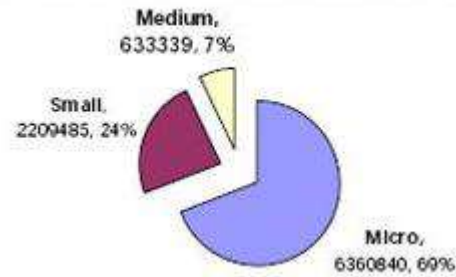
Contribution in Exports: Union Minister of Micro, Small & Medium Enterprises, Mr. Kalraj Mishra in a written reply to a question in Lok Sabha on 27 July 2015 informed that “the share of MSMEs in India’s total export, for the year 2012-13, 2013-14 and 2014-15, has been estimated as 43.00 per cent, 42.38 per cent and 44.70 per cent respectively[13].

3.3 Employment Generation

With enactment of MSME Act 2006, MSME-Development Organization works with wide mandate of promotion and development of MSME sector [14]. Under MSME-DO there are 60 offices and 21 autonomous bodies which include Tool Rooms, Training Institutions and Project -cum-Process Development centers [15]. All these not only help in increasing the MSME sector units across the country but also making the human resource trained with better employability skills. The MSME sector which includes registered and unregistered units is the second largest sector in India in terms of employment generation after agriculture sector. Ministry of MSME has implemented number of schemes and programs such as Prime Minister’s Employment Generation Programme and Micro and Small Enterprises - Cluster Development Programmed (MSE-CDP) that is designed to help and promote the MSME units and employment generation is this sector. As per information by Govt. of India “the number of working enterprises (activities excluded include mainly major service activities e.g. wholesale/retail trade, legal, educational & social services, hotel & restaurants, transports and storage & warehousing (except cold storage) in MSME sector was 361.76 lakhs in the year 2006-07 and was 467.56 lakhs in the year 2012-13 projected in Annual Report 2013-14, showing Compound Annual Growth Rate (CAGR) of 4.37% for last 6 years. The employment in MSME sector was 805.24 lakhs in the year 2006-07 and was 1061.52 lakhs (projected) in the year 2012-13 showing Compound Annual Growth Rate (CAGR) of 4.71% for last 6 years [16].

Distribution of Working Enterprises by Area: - Ural area with 200.19 lakh of working enterprises accounted for 55.34% of the total working enterprises in MSME sector whereas urban area located 161.57 lakh working enterprises accounted for 44.66% of the working enterprises in MSME sector [17].

Number of Employment generation by MSME IN 2009-10



Employment by type of MSME enterprises



Exhibit 1: Employment type and Employment Generation by MSME Sector, Source: Annual reports, ministry of MSME, Government of India [18].

3.4 Demonetization in India

On 8th Nov 2016 Government of India put forward a policy which refrain Rs. 500 and Rs. 1000 notes as a legal tender. This is not the first time when India is facing the demonetization effect, but surely this time the effect is much difficult to adjust with. India’s economy is heavily dependent in liquid form i.e. cash.

3.5. Effect of Demonetization on MSME

Currency status: before 08th Nov – 17.5 Lack Crore (14.5 500 & 1000) before 8 November 2016 the total banknotes in circulation in India was 17.5 lakh crore which was nearly 86% of the total money supply. Currently 14.5 lakh crores rupee have been released by the government in the economy, it means the economy is lacking behind with Rs 3 lakh crore. MSME sector in India comprises registered and unregistered units. The unregistered units which comprises a large proportion in MSME, mainly depends on cash to complete their operating cycle. The effect of crush crunch on the employability and productivity of the MSME units can be studied under the following points: **Effect on Wage Payments:** Due to largely dependence on cash they are finding difficult to pay their laborers. **Effect on Payments to Suppliers:** Not able to pay to suppliers for small items. **Effect on Demand:** Since the customers are also taking time to change with the modern economic system, MSMEs are facing the problem in this front. **Effect on Level of Production:** Production has also been cut down due to cash crunch.

4. Research Methodology

4.1 Type of Research: The research can be classified into two types, based on the nature of problem: One exploratory, which is conducted when the problem is complex and its dimensions are not clear to the researcher. Another classification is as Conclusive which can be further divided into two types as Descriptive and Causal. Since the present study is intended to enquire into the effects of the demonetization on employment generation of the MSME sector, it can be classified as Descriptive research.

4.2 Population and Sampling Decisions: Population: The population for this research covers all the MSME units in five districts of Uttar Pradesh: Allahabad, Pratapgarh, Jaunpur, Mirzapur and Varanasi. **Sample Size:** Total hundred samples have been collected ten from each district. **Sampling Method:** Quota sampling (non-probability) has used for the purpose of data collection. Ten MSME units have been selected in each district on the basis of judgment for the purpose of data collection. **Data Collection Tool:** Structured questionnaire for enquiring on different aspects of the problem have been used for data collection.

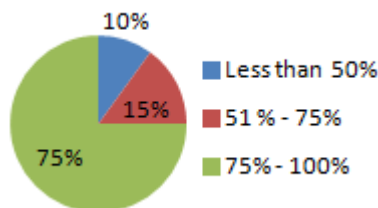
4.3 Data Presentation and Analysis Tools: MS Excel table and charts have been used for the purpose of presentation and analysis of data.

4.4 Hypothesis Testing: The research is aimed at enquiring into the effect of demonetization on employment generation capacity of MSME sector. The employability has been examined through the extent of production capacity utilization and meeting sales targets. Since the data collected is of non-parametric in nature, the Chi Square test has been used to test the hypothesis.

5. Data Analysis & Interpretation

(1) Percentage utilization of production capacity before Demonetization

Scale	Responses
Less than 50%	4
51 % - 75%	6
75% - 100%	30
Total	40

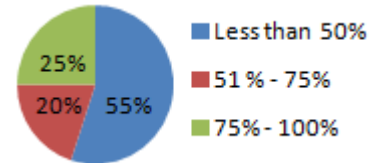


Data collected on the production capacity and utilization of production capacity before demonetization (i.e. before 08 Nov 2016) reveals that 75% of respondent companies

have been able to operate on 75% to 100% of their capacity before the demonetization.

(2) Percentage utilization of production capacity during Demonetization (up to first week of January 2017)

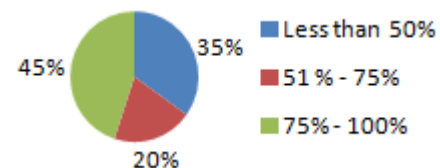
Scale	Responses
Less than 50%	22
51 % - 75%	8
75% - 100%	10
Total	40



Data collected on utilization of production capacity after demonetization reveals that 55% of respondent companies were able to utilize the production capacity less than 50% which implies that larger proportion of companies were finding it difficult to utilize the production capacity due to demonetization.

(3) Percentage of monthly sales during demonetization

Scale	Responses
Less than 50%	14
51 % - 75%	8
75% - 100%	18
Total	40



The above table and chart figure out that only 45% respondents were able to manage 75-100% sales during demonetization.

6. Hypothesis Testing

The data collected is non-parametric in nature and therefore Chi Square Test is used for the purpose of hypothesis testing. The formula for the Chi Square: $\chi^2 = \sum ((O - E)^2 / E)$.

Decision rule: If the calculated value is less than the table value, the null hypothesis will be accepted and alternate is rejected.

Hypothesis for the Research:

Ho: There is no significant effect of demonetization on the utilization of production capacity in MSME sector.

H₁: There is significant effect of demonetization on the utilization of production capacity in MSME sector.

Scale	< 50%	51% - 75%	75% - 100%	Total
Before Demonetization	4	6	30	40
During Demonetization	22	8	10	40
Total	26	14	40	80

Scale	< 50%	51% - 75%	75% - 100%	Total
Before Demonetization	13	7	20	40
During Demonetization	13	7	20	40
Total	26	14	40	80

O	E	(O-E)	(O-E) ²	(O-E) ² /E
4	13	-9	81	6.230769
22	13	9	81	6.230769
6	7	-1	1	0.142857
8	7	1	1	0.142857
30	20	10	100	5
10	20	-10	100	5
				22.74725

Degrees of freedom = (r-1)*(c-1) = 2*1=2. Significance level for this test = 5%. The table value of Chi Square distribution at 2 degrees of freedom and 5% significant level: 5.991. Since the table value is less than the calculated value the Null hypothesis is rejected and alternate is accepted. The result of hypothesis testing proves that the demonetization has significant effect on utilization of production capacity in MSME sector. Therefore, it can be understood that demonetization has significant effect on the employment generation capacity of MSME sector.

7. Findings of the Research

On the basis of analysis of primary data and hypothesis testing, the research has concluded with following interesting findings:

- 1. Demonetization has Negative Effect on Utilization of Production Capacity:** The study reveals that there is negative effect of demonetization on utilization of production capacity. The hypothesis testing has proved that cash crunch due to demonetization has badly affected the MSMEs in maintaining their production levels. Only 25% respondents were able to manage the capacity to its fullest.
- 2. Demonetization has Negative Effect on Employment Generation Capacity of MSME Sector:** Since the production capacity could not be utilized fully due to cash crunch in most of the MSMEs, the daily wage and unorganized labor force had to lose their jobs during the period of demonetization.

Therefore, it can be stated that demonetization had negative effect on Employment Generation capacity of MSME sector.

- 3. Demonetization has negative effect on the achieving the sales target:** The study shows that sales target has also not been achieved during demonetization Along with the examination of effect of demonetization on employment generation of the MSMEs, the study has also explored intensive literature review on the topic. On this basis two points needs to be highlighted:
- 4. Significant role of MSME sector in Indian Economy:** The MSME sector has very important role to play in terms of overall development especially in rural area. The study reveals that this sector is contributing more to export, provides employment and hence uplifts the living being of people.
- 5. Role of MSMEs in Employment Generation and Socio-economic Development:** The employment generation by this sector has increased from 805.24 lakhs in the year 2006-07 to 1061.52 lakhs (projected) in the year 2012-13 with Compound Annual Growth Rate (CAGR) of 4.71% for last 6 years.

The findings of the research are similar to other reports on the topic. A study conducted by All India Manufacturers' Organization (AIMO) has reported a drop in employment and loss in revenue in MSMEs. "Medium and large scale industries engaged in infrastructure projects, such as big-ticket road construction, reported a 35 per cent cut in employment and 45 per cent revenue loss. The number of jobs and revenue are expected to dip by 40 per cent by March."²⁰ Another study by the India Development Foundation (IDF) assessed the impact negative as it says "the SME sector seems to have suffered a negative impact of demonetisation"²¹

8. Conclusion

The Demonetization -2016 had been aimed at curbing the corruption, tax erosion and fighting against the duplicate currency in circulation. This action of Indian government has effects on all sectors of economy; some of them had positive and others faced negative effects on their respective businesses. This study had the objective to understand the effect of demonetization on employment generation capability of MSME sector. There may be long term and short term effect of Demonetization. This study has covered only short term effect of Demonetization.

Suggestion: There are many sectors of the economy such as MSME sector that depend on the Cash flow. The result of the study discloses the fact that this sector has suffered a lot; may be for a short period of time. The unorganized labors have to lose their jobs and this figure cannot be estimated easily. Therefore, it is suggested that the Government should plan for such sectors of economy before going for Demonetization. This will help the

unorganized labors to continue in their jobs. It is also suggested that all the sectors that have negative effects of the Demonetization must be identified and action may be taken to protect them before the demonetization is executed.

Limitation of the Study: The limitations of the study are: Sampling Limitations: The sample is comparatively low and non-random sampling technique has been used. This study has covered only the five districts of UP. Only Short term Effect: The research has limited its scope in examining only the short term effect of Demonetization. Result only on the basis of Production Level: This study has examined the Demonetization effect on employment generation through one variable only i.e. utilization of production capacity. The employment generation capability of the MSME sector can be studied with the help of other variables too such as Sales target and Demand analysis.

Future Scope of the Study: The new research can be undertaken by covering bigger geographical area that will give the picture for whole country. The Effect of Demonetization may be different in Medium, Small and Micro Enterprises of this sector. Therefore, different such studies can be undertaken which will provide focused result. The current study has highlighted fact that before the Demonetization need to care small sectors of the economy. This study has not covered any other effects of Demonetization which may be positive in different areas such as controlling corruption. The MSME sector which provides large number of jobs for the unskilled and unorganized manpower especially in rural areas could not bear with the cash crunch though only for a short time as long term effect are out of the scope of this research work.

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