



AN INCLUSIVE GROWTH OF NORTH EASTERN REGION: NEED FOR AN ENHANCED ROLE OF SMES

- **Background**

- *Overview of the development of the NER*
- *Challenges and Opportunities faced by NE states*
- *Increased government focus towards the development of NER*

- **Analysis**

- *Enhanced role of MSMEs in the development of the NER*

HIGHLIGHT

Constituting 8% of the total Indian geographical size and representing only 3% of the Indian population, the North Eastern Region (NER) houses over 220 ethnic groups and almost an equal number of dialects divided into 3 different language groups. The region abodes over 160 schedule tribes and 400 other tribal and sub tribal communities and groups. Culturally, the North East India is a blend of two traditions of Indic Asia and Mongloid Asia. People of different cultures and ethnicity are always engaged in self preservation and this has often led to internal tension and racial conflicts in the region.

Amongst the most prosperous regions at the time of its inclusion in Indian political map, the development of NER has lagged behind the other states. Insurgency, a difficult geographical terrain, and a regional landlock, which resulted in a political and trade isolation, have been the major reasons for the decline of the North East India economy. The decline got a fresh thrust in 1947 with Indian independence and partition, which exacerbated the trade isolation of the NER.

A development strategy based on the resources of the region will occur simultaneously with the emergence of a group of strong entrepreneurs, which in turn calls for an enhancement of skill levels. A self induced development strategy will help in not only achieving the goal of economic growth of the region, but will also instil a sense of pride and belonging to the budding entrepreneur. An enhanced role of MSMEs is envisaged in the socio-economic growth of the region, and external players such as a rating agency have a key role in identifying this class of entrepreneurs and can also potentially help in their capacity building. The rating agencies can also help to improve the flow of finance to the MSMEs in terms of both - the quality and quantity of credit.

Background

Overview of the Development of NER

Table 1: Economic and Social Indices for the North Eastern Region

| State | Area (Sq. KM) 2011 | Population (Lac Persons) 2011 | Rural Population (%) 2011 | Sex Ratio 2011 | Literacy Rate (%) 2011 | Literacy Rate (%) 2011 Males | Literacy Rate (%) 2011 Females | Infant Mortality Rate (per '000) 2010 | % of Population Below Poverty Line - 2011-12 | GSDP (Rs. crore) (Constant Base: 2004-05) 2012-13* | Per Capita Electricity Consumption (KWH) 2009-10 | Per Capita GSDP 2012-13 | Surface Road Length (KM) 2011 | Surface Road Length / Area (Sq. KM) 2011 |
|-------------------|--------------------|-------------------------------|---------------------------|----------------|------------------------|------------------------------|--------------------------------|---------------------------------------|--|--|--|-------------------------|-------------------------------|--|
| Arunachal Pradesh | 83743 | 13.83 | 77 | 920 | 66.95 | 73.69 | 59.57 | 31 | 34.67 | 5934 | 470.00 | 42065 | 14336 | 0.17 |
| Assam | 78438 | 311.69 | 86 | 954 | 73.18 | 78.81 | 67.27 | 58 | 31.98 | 85690 | 204.80 | 26953 | 37816 | 0.48 |
| Manipur | 22327 | 27.22 | 70 | 987 | 79.85 | 86.49 | 73.17 | 14 | 36.89 | 8073 | 240.22 | 29077 | 8140 | 0.36 |
| Meghalaya | 22429 | 29.64 | 80 | 986 | 75.48 | 77.17 | 73.78 | 55 | 11.87 | 12072 | 675.19 | 39930 | 7072 | 0.32 |
| Mizoram | 21081 | 10.91 | 48 | 975 | 91.58 | 93.72 | 89.40 | 37 | 20.40 | 5017# | 376.99 | 45084 | 7001 | 0.33 |
| Nagaland | 16579 | 19.81 | 71 | 931 | 80.11 | 83.29 | 76.69 | 23 | 18.88 | 9871 | 218.03 | 48851 | 15470 | 0.93 |
| Sikkim | 7096 | 6.08 | 75 | 889 | 82.20 | 87.29 | 76.43 | 30 | 8.19 | 5491 | 850.00 | 88542 | 4119 | 0.58 |
| Tripura | 10486 | 36.71 | 74 | 961 | 87.75 | 92.18 | 83.15 | 27 | 14.05 | 16993 | 335.47 | 45382 | 14203 | 1.35 |
| NER states | 262179 | 455.89 | 82 | 944 | 79.64 | 84.08 | 74.93 | 34 | 22.11 | 149141 | 257.98 | 32073 | 108157 | 0.41 |
| India | 3287263 | 12101.90 | 69 | 940 | 71.04 | 82.14 | 65.46 | 47 | 21.92 | 5505433 | 778.71 | 44600 | 2341479 | 0.71 |

* GSDP: Gross State Domestic Product

#: 2010-11 data

Source: http://mospi.nic.in/mospi_new/upload/SYB2013/ch2.html

<http://dbie.rbi.org.in/DBIE/dbie.rbi?site=statistics>

http://planningcommission.nic.in/news/pre_pov2307.pdf

The table above depicts that the social indicators for the NER are still higher than the national average. However, the growth indicators measured by Per capita GSDP and population below poverty line and the state of infrastructure measured by per capita electricity consumption and surface road per area (sq. km.) are the cause of worry for the development of the NER. With the introduction of market based economic reforms, differences in the growth rates of the rest of India and NER have steadily diverged. During the period 1990-91 to 2004-05 and then from 2004-05 to 2012-13, the average GSDP of all states in constant prices increased at 6% and 8% respectively per year corresponding to 4.4% and 7% in NER. In 1990-91, the region's per capita income at current prices was lower than the national average by 20%, the gap widened to 31% in 2004-05 and 40% in 2011-12. This is despite the fact that states such as Arunachal Pradesh and Mizoram pull up the NER per capita averages due to low base. The highly populous states such as Assam score poorly on per capita indicators. The per capita GSDP of Assam is 40.58% lower than the national average in 2011.

A deeper understanding of the income generation mechanism indicates that even in states where the per capita income is higher than the national average, much of the income is generated in the public administration department. This underlines the overwhelming dependence on the government machinery and the lack of private entrepreneurship in the NER. A higher literacy rate has not been converted into productive economic activities. Slow pace of industrialization has led to a high rate of unemployment and underemployment.

A structural transformation is required to ensure the development and prosperity of the NER. It calls for significant changes in policies and institutions promoting an inclusive growth of the entrepreneurship at the grass-root levels.

Challenges and Opportunities in the NER

The NER has been richly endowed with natural resources and its human resource is an asset to the economic development given the sense of gender equality and the higher levels of literacy that already exists. However, the social environment is yet not conducive to the economic growth of the region. The region poses some special challenges to the State that must be overcome before the gap between the financial situation of the NER and the rest of India is bridged. These challenges can be broadly classified as follows:

1. Diplomatic and economic initiatives with foreign neighbours
2. Law and Order, especially internal security
3. Inclusive Governance

Diplomatic and Economic Initiatives with Foreign Neighbours

With almost 96% of NER borders comprising of international boundaries, the region has been landlocked with minimal trade opportunities that have resulted in a deprivation of the North East economy.

Furthermore, the region has suffered from cross border migration, insurgency, terrorism, drugs and arms and non conventional security threats for the local ethnic groups.

The Ministry of External Affairs has prioritized to establish connectivity and communication links cross border to promote trade and commerce with our international neighbours through its Look East Policy. This aims to provide the infrastructural support to promote industrialization, given the rich heritage, which offers vast opportunities to khadi and village industries and MSMEs operating in the business of handicraft products, sericulture, tea etc. Further initiatives are required to promote cross border investment in and by the NE states which will include setting up of dialogue between international trade partners.

Even though stringent law and order measures are mandated by the Look East Policy in wake of increased security threat, it offers huge potential to the NE states to earn significant foreign exchange for the Indian economy.

Law and Order, Especially Internal Security

Hosting hundreds of ethnic groups within it, the North Eastern states have always faced internal conflicts and racial tensions amongst its own populace. With limited resources available for growth and a quest to establish its own regional and ethnic identity, every group is engaged in self preservation. This has created an environment of insurgency, social insecurity and has hampered any initiative towards self development within people.

Government's efforts towards controlling the security situation have only made the region a militant rule and vested interests have annihilated any private entrepreneurship from the states.

Inclusive Governance

An inclusive growth calls for inclusive governance comprising building institutions for strengthening state departments and agencies to promote fruitful partnership between civil society and state administrations. A top-down approach would enable the institutions to support the development of capacity in the people of the North East.

Bodies like the North Eastern Council and the Ministry of Development of North Eastern Region (MDoNER) have been instituted at the regional and the national level respectively to focus on and fund the development of North Eastern states specifically. It is no more the crunch in the financial resources that threaten the economic growth of the NER, but the limits that the people of North East have imposed on themselves in terms of their capacity and entrepreneurship.

INCREASED GOVERNMENT FOCUS TOWARDS THE DEVELOPMENT IN THE NER

It has already been established that the development of NER is constrained by the limited participation of the local people. The strategy to be followed has to revolve around the encouragement of capacity and entrepreneurship of the local population that would generate fresh employment opportunities in the region. A holistic approach for the successful transformation of the investment into developmental outcomes encompasses the development of the MSMEs in the region. This will empower the people through participatory development starting from the grass root level. A few key areas of focus for greenfield MSMEs would be:

- Rural development with a focus of non-farm avocations such as milling units, expansion of horticulture, creation of cold storage facilities, etc.
- Khadi industries such as pottery, beekeeping, food processing, carpentry and black smithy, khadi and poly-vastra, etc.
- Development of manufacturing units based on locally available resources such as sericulture, tea industry in Assam and cement industry in Meghalaya
- Harnessing hydro-electric power generation potential which will give rise to units in power and energy sector such as transformer manufacturing units
- Developing services such as tourism
- Augmenting infrastructure including rail, road, inland water and air to facilitate two way movement of people and goods will create opportunities for construction and engineering units
- Improving communication networks including broadband and wireless network that shall hold the potential for the telecom units

| State | Key MSME Industry |
|--------------------------|--|
| Arunachal Pradesh | Arts and Craft; Weaving; Cane and Bambo |
| Assam | Tea; Tourism; Traditional Cottage Industry |
| Manipur | Handloom Handicrafts; Sericulture; Food Processing |
| Meghalaya | Food Processing; Horticulture; Mining |
| Nagaland | Bamboo; Food Processing; Horticulture |
| Mizoram | Bamboo; Energy; Sericulture |
| Tripura | Food Processing; Bamboo; Handloom Handicrafts |

* Source: Ministry of MSME Annual Report 2013

These sectors succor for the most advantageous employment generating avenues of the NER. Cluster development of the identified sectors will boost the growth rate of MSMEs in the NER.

As per an International Finance Corporation report, the NER accounts for less than 2% of the number of MSME units in India. Required way forth is creating an enabling environment for the flow of investment to the right class of entrepreneurs and capacity development that would need imparting skills to the people to enhance their productivity.

Analysis

Inclusive Growth of MSMEs and the Role of Rating Agencies

The strategy of inclusive growth empowers the smallest of the units and enables them to overcome their problems and attain growth. Bringing individuals together to form small enterprises, enhancing their skills to promote capacity development and creating an enabling environment for the development of the enterprises is an arduous task. Devolution of adequate funds to the right set of entrepreneurs and capacity building requires a larger financial outlay, which has been historically denied to the NER. North East India remains the least evolved financial market. It has one of the highest average population per bank branch as is depicted by the Table 3 below. The levels of financial inclusion are also the lowest in the NER as depicted by Table 4.

| State/Union Territory | Total Bank Branches | Average Population Per Bank Branch (In Thousands) - 2009 |
|-----------------------|---------------------|--|
| Arunachal Pradesh | 77 | 16 |
| Assam | 1420 | 21 |
| Manipur | 81 | 33 |
| Meghalaya | 206 | 12 |
| Mizoram | 95 | 10 |
| Nagaland | 87 | 25 |
| Sikkim | 71 | 8 |
| Tripura | 219 | 16 |
| NER | 2256 | 18 |
| All-India | 82485 | 14 |

* Source:

<http://www.rbi.org.in/scripts/PublicationView.aspx?id=12661>

| Item | All-India | | | NER | | |
|--|-----------|------|------|------|------|------|
| | 2001 | 2011 | 2012 | 2001 | 2011 | 2012 |
| Households availing banking services (in %) | 35.2 | 58.7 | - | 28.8 | 47.3 | - |
| Population per bank branch ('000) | 15.6 | 13.3 | 12.5 | 19.5 | 18.1 | 17.3 |
| No. of accounts per 1000 Population (credit) | 51 | 100 | 106 | 37 | 54 | 54 |
| No. of accounts per 1000 population (all deposits) | 416 | 669 | 734 | 321 | 476 | 540 |
| No. of accounts per 1000 population (savings deposits) | 272 | 516 | 571 | 202 | 367 | 423 |
| Per capita credit outstanding (Rs. '000) | 5.2 | 33.7 | 39.1 | 2 | 12.1 | 13.9 |
| Per capita total deposits (Rs. '000) | 9.2 | 44.5 | 49.4 | 5.5 | 22.8 | 26.5 |

* Source: RBI (for number of deposits accounts, credit accounts, credit outstanding, and deposits outstanding); Office of the Registrar General and Census Commissioner of India for population and households' data.

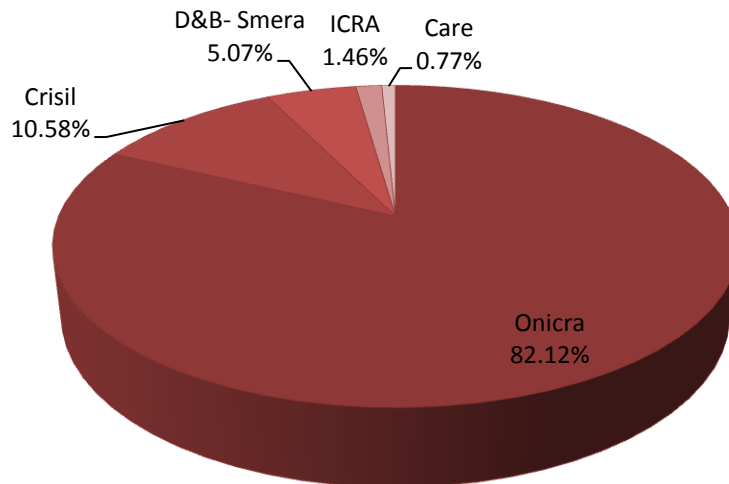
The North Eastern states reel behind the national average in all the indices for measuring access to bank as well as finance. The financial exclusion of the NER, the lack of economic growth and the need to build the entrepreneurship and capacities in the region carve out a clear role for players like rating agencies, private and social equity investors, etc. These agencies, specializing in understanding the dynamics of new and small set ups, need to be engaged to cultivate the small scale entrepreneurship in the region.

The role of rating agency assumes significance as it can guide the financial institutions to identify the right class of entrepreneurs to fund, can help the entrepreneurs to zero on the right economic activity to engage in through their reports and help identify the gaps in skills and encourage capacity building for creating an environment conducive for economic growth of the region.

There are about 29.8 mn MSMEs in the organized sector all across India as per the Census Survey 2010 of Ministry of MSME. Of these, approximately 1.0 mn are situated in the NER, constituting 3.36% of the total MSMEs in India. Of these 1.0 mn units, only 1163 units have been rated under the Performance and Credit Rating Scheme of NSIC by 25th Feb 2014. This translates to 0.12% of the MSME units in NER being rated. On the whole, the MSME units in NER formed 1.45% of the total units being rated across all India.

A total of 80339 units have been rated under the NSIC Performance and Credit Rating Scheme since inception of the scheme in 2005 till 25th February 2014. Of these, only 1163 units belong to NER. Onicra has led the baton in the NER to encourage the investment climate there.

Share of Rating Agencies in Total NER Based Rated Units



The penetration of the rating agencies in the NER is very low. There is a clear lack of awareness among the MSMEs in the region regarding the benefits of a performance and credit rating. From the perspective of a rating agency, this is a result of the difficult geographical terrain, high cost of developing a relationship and then maintaining the same with regard to the compensation received by the rating agency for these units. The challenges faced by the MSMEs in the region impede the efforts of the rating agencies to develop a high network there. The government has already initiated some preferential treatment to the units in the region, however, more needs to be done keeping in view the challenges discussed above.

The government, both central and state, has twin responsibilities of encouraging more units to set up and educate them about the benefits of rating. The penetration of the rating agencies can be encouraged and leveraged to support the government policies and schemes on various entrepreneurship, technology up-gradation and capacity building. Rating agencies such as Onicra can play an important role in the financial inclusion of the MSMEs, improve the self regulation and create a participative environment for both the public and private investors, in turn setting up the road for social and economic growth of the NER.

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