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Institutional and Operational Barriers in CSR-Driven MSME Development: A Multidimensional Study of Sectoral and Regional Industrial Evolution in India

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Abstract: ***The evolution of Micro, Small and Medium Enterprises (MSMEs) in India reflects a complex interaction of regional industrial transitions, public sector institutional support, cluster-based development, and emerging regulatory frameworks such as Corporate Social Responsibility (CSR). This study examines the historical and structural transformation of Indian MSMEs from the 1960s to the contemporary period, with particular emphasis on the role of Public Sector Undertakings (PSUs), regional industrial ecosystems, and CSR-driven operational dynamics. Using a multidimensional analytical approach, the paper traces the shift of industrial activity from traditional hubs like Calcutta to growth-oriented regions such as Pune, Bangalore, Hyderabad, and Coimbatore, highlighting how political stability, infrastructure provisioning, and visionary leadership fostered MSME growth. Sectoral analyses of heavy engineering, aerospace, electronics, pharmaceuticals, agro-processing, and services reveal both upward value-chain movement and persistent vulnerabilities related to finance, technology, raw material dependency, and employment absorption. The study further investigates institutional and operational barriers to CSR adoption among MSMEs following the Companies Act, 2013, identifying regulatory burden, resource constraints, limited awareness, and inadequate impact measurement capabilities as key challenges. Drawing on cluster experiences and institutional interventions by organizations such as BHEL, HAL, BEL, ECIL, NSIC, CITD, and TiE, the paper argues that CSR can function as a strategic enabler rather than a compliance cost when aligned with core MSME competencies. The findings underscore the need for supportive policy frameworks, revitalized credit access, and sector-specific CSR models to strengthen MSME resilience and enhance their contribution to inclusive and sustainable industrial growth in India.***

Keywords*: In Corporate Social Responsibility, MSMEs, Public Sector Undertakings (PSUs), Regional Industrial Transformation, Institutional and Operational Barriers.***

I. INTRODUCTION

This study aims to examine the institutional, regional, and sectoral evolution of Micro, Small and Medium Enterprises (MSMEs) in India, with a specific focus on the role of Public Sector Undertakings (PSUs), industrial clusters, and the emerging challenges of Corporate Social Responsibility (CSR) integration under the Companies Act, 2013. The paper seeks to identify the key institutional and operational barriers that constrain sustainable MSME development and CSR adoption.

A. Regional and Sectoral Transformation of MSMEs in India

India's transition from a colonial-mercantile economy to a diversified industrial and service-oriented system has been shaped by regional industrial shifts, institutional support, and the expanding role of Micro, Small and Medium Enterprises (MSMEs). Since the 1960s, industrial activity has progressively migrated from traditional coastal centers such as Calcutta to inland growth hubs including Pune, Bangalore, and Hyderabad. This shift was driven largely by the establishment of Public Sector Undertakings (PSUs) such as BHEL, HAL, BEL, and ECIL, which functioned as industrial anchors by generating demand for ancillary MSMEs, facilitating technology diffusion, and developing skilled manpower.

The decline of Calcutta as India's industrial capital during the mid-1960s highlights the importance of political stability and policy alignment in sustaining industrial ecosystems. Socio-political unrest, militant trade unionism, and the freight equalization policy eroded the region's natural advantages, leading to capital flight and industrial stagnation.

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In contrast, Maharashtra—particularly Pune—benefited from a stable political environment, proactive infrastructure development by the Maharashtra Industrial Development Corporation (MIDC), and visionary industrial leadership. The growth of automobiles, pharmaceuticals, and heavy engineering in Pune laid the foundation for its later emergence as a technology and services hub.

PSUs played a central role in shaping India's defense, aerospace, and electronics clusters. HAL and BEL in Bangalore and ECIL in Hyderabad catalyzed MSME ecosystems by outsourcing high-precision manufacturing, electronics fabrication, and component supply. These PSU-led networks enabled MSMEs to upgrade technologically and integrate into complex supply chains. However, PSU–MSME linkages also exposed operational vulnerabilities, as illustrated by the decline of ancillary units in the BHEL Trichy cluster due to market volatility, raw material cost disparities, and limited access to institutional finance. Cluster-based development further demonstrates the uneven nature of MSME growth. While Coimbatore and Salem successfully leveraged local skills, institutional coordination, and cooperative mechanisms to achieve global competitiveness, regions such as Ratnagiri remained industrially backward due to historical labor extraction, weak local value addition, and limited policy focus. Sectoral transitions, particularly in pharmaceuticals, reveal how regulatory regimes—from the Patents Act of 1970 to the post-TRIPS era—shaped MSME innovation, export orientation, and competitiveness, while also creating new compliance and cost pressures.

The post-1991 expansion of the services sector introduced digital technologies and e-commerce, enhancing market access and efficiency for MSMEs, but failed to generate adequate employment absorption. Overall, India's MSME evolution reflects a dynamic interaction of institutional support, regional policy environments, sectoral shifts, and emerging sustainability imperatives, underscoring the continued relevance of manufacturing-led and cluster-based MSME development.

1) Institutional Barriers

- Regulatory Compliance Burdens: The associate reporting and compliance obligations of the Companies Act, 2013, are often overwhelming for smaller businesses that lack the necessary administrative infrastructure.
- Lack of Government Pressure: Many Indian MSMEs do not perceive a strong need for CSR engagement because they experience lower community and governmental pressure compared to large corporations.
- Policy Misalignments: There is a notable absence of supportive policy frameworks, such as tax incentives specifically for MSME CSR spending, which limits the motivation for voluntary adoption.

2) Operational Barriers

- Resource Constraints: MSMEs are fundamentally limited by a lack of financial, human, and technical resources. Allocating a dedicated CSR budget or hiring specialized staff is often unfeasible.
- Knowledge and Expertise Gaps: A study using Interpretive Structural Modelling (ISM) identified 13 variables as barriers, highlighting that MSMEs focus on tactical rather than strategic needs due to limited information about CSR benefits.
- Measurement and Evaluation Difficulties: Due to a lack of technical expertise, MSMEs struggle to quantify the social impact of their initiatives, which is essential for building credibility with stakeholders and investors.

3) ISM Research: Identified Barriers to MSME CSR Engagement

Barrier Variable	Type	Impact on Engagement
Tactical Focus over Strategic	Operational	Prioritizes immediate survival over long-term social impact.
Limited Knowledge of CSR	Institutional	Prevents understanding of potential competitive advantages.
Financial Constraints	Operational	Leads to view of CSR as an expense rather than an opportunity.
Lack of Top Management Commitment	Operational	Prevents CSR from becoming part of the core business strategy.
Low Community Pressure	Social	Reduces the perceived urgency for social responsibility.
Inadequate Skills to Monitor Impact	Operational	Makes initiatives look uncoordinated and non-transparent.

B. Role of Leadership and Institutions in Navigating Barriers

To overcome these barriers, leadership and institutional support have been paramount. The Central Institute of Tool Design (CITD) in Hyderabad, Asia's first tool room established in 1968, has been a cornerstone for MSME upskilling. By offering programs in Mechatronics, Robotics, AI, and Tool Design, CITD provides the technical capacity that small businesses lack. It serves as a hub for consultancy and common facility services, allowing MSMEs to access advanced technology without the burden of high capital expenditure.

Similarly, Technocrats Industrial Estate,Balanagar, founded in early 1980's, has been instrumental in fostering an ecosystem of mentorship and investment. Through the "TiE Social Impact" program, successful entrepreneurs (Charter Members) mentor startups in areas like education, healthcare, and sustainability, emphasizing that "true entrepreneurship is not competition, but contribution". These platforms provide visibility and access to global networks, helping MSMEs bridge the knowledge gap and attract CSR-focused investments.

In the cluster domain, the National Small Industries Corporation (NSIC) has been a significant facilitator for over five decades. NSIC provides integrated support services in marketing, finance, and technology, while also conducting its own CSR initiatives such as vocational training in computer skills, health camps, and the assembly of solar lanterns for rural areas. During the COVID-19 pandemic, the proactive pivot of PSUs like BHEL and SAIL to convert facilities into care centers and fund oxygen plants demonstrated the potential of corporate-led CSR to support the broader industrial and social ecosystem.

C. Synthesis of Sector-Wise and Region-Wise Progress

The evolution of India's MSMEs from simple ancillary providers in the 1960s to essential pillars of a globalized economy is a story of adaptation amidst friction.

1) Regional Transition: The shift from Calcutta to Pune was a transition from labor-hostile, policy-neutralized environments to pro-business, infrastructure-ready hubs.
2) Sectoral Progress: The transition from traditional clusters (Salem Sago) and heavy engineering (BHEL/HAL) to high-tech sectors like Electronics (ECIL) and Pharma illustrates a climb up the value chain, though often hampered by a lack of raw material self-sufficiency (APIs) and outdated technology.
3) Operational Shifts: The service sector boom forced a digital transformation but also highlighted a gap in employment generation that only a robust manufacturing MSME base can fill.
4) CSR Barriers: The primary obstacle remains the perception of CSR as a compliance cost rather than a tool for competitiveness. Strategic alignment with core business competencies, as seen in the Tata Swach water purifier or ITC's e-Choupal, remains the gold standard for sustainable impact.

As the Indian economy looks toward a 5 trillion dollar GDP target, the formalization of the MSME sector through the Udyam platform and the transition toward low-carbon manufacturing are the next frontiers. Institutions like CITD and TiE will continue to be vital in bridging the technical and mentorship gaps, while policy interventions must address the financial reluctance of banks and the logistical disparities between regional clusters.

D. Research Objectives

1) To analyze the regional and sectoral evolution of MSMEs in India.
2) To assess the role of PSUs and industrial clusters in MSME development.
3) To identify institutional and operational barriers to MSME growth and CSR adoption.
4) To suggest policy measures for sustainable and socially responsible MSME development

E. Research Methodology

This study is based on Secondary data. Secondary data are sourced from government reports, policy documents, industry publications, and peer-reviewed journals to support theoretical grounding and contextual analysis.

II. REVIEW OF LITERATURE

The evolution of India's industrial economy has been widely examined through the lenses of colonial legacy, regional political economy, and post-independence policy transformations. Studies on colonial governance and capital relocation highlight how Calcutta's early industrial dominance was rooted in its strategic position within the British mercantile system. However, literature documents that post-independence socio-political turbulence, militant trade unionism, and policy interventions such as freight equalization significantly undermined the region's industrial competitiveness, leading to capital flight and regional decline. These analyses underscore the critical role of political stability and policy alignment in sustaining industrial ecosystems.

Urban and regional industrial histories further reveal sharp spatial disparities in India's development trajectory. City-based studies of Pune and Coimbatore demonstrate how proactive institutional support, entrepreneurial leadership, and skill-based clustering facilitated industrial resilience and diversification.

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In contrast, regional analyses of districts such as Ratnagiri characterize them as zones of surplus labour and underdevelopment, where historical labour extraction, weak industrial policy focus, and limited local value addition constrained MSME growth. This body of literature establishes that regional outcomes are deeply shaped by institutional capacity and historical path dependence.

A substantial strand of research emphasizes the nation-building role of Public Sector Undertakings (PSUs) in India's industrialization process. Scholars and institutional reports consistently identify PSUs such as BHEL, HAL, BEL, and ECIL as anchor institutions that fostered technological capability, self-reliance, and large-scale employment generation. More importantly, these enterprises acted as industrial nurseries by nurturing extensive MSME ancillary networks, particularly in heavy engineering, aerospace, electronics, and defense manufacturing. However, recent studies caution that PSU–MSME linkages are increasingly strained due to demand volatility, procurement restructuring, and financial constraints faced by small suppliers.

The literature on industrial clusters and MSME ecosystems highlights clustering as a key mechanism for enhancing competitiveness, innovation, and resilience. Empirical studies of clusters such as Coimbatore's engineering hub and Salem's sago and starch industry illustrate how local skill specialization, cooperative institutions, and collective infrastructure enable MSMEs to integrate into national and global value chains. At the same time, evidence from clusters like BHEL Trichy reveals structural vulnerabilities related to raw material cost disparities, limited access to institutional finance, and dependence on single large buyers.

Sector-specific studies further enrich the understanding of MSME dynamics. Research on aerospace and electronics clusters in Bangalore and Hyderabad links their growth to PSU-driven technology transfer and human capital formation, which later supported the rise of IT and knowledge-based industries. Similarly, the pharmaceutical literature traces the industry's evolution through distinct regulatory regimes, demonstrating how policy shifts—from the Patents Act of 1970 to the post-TRIPS era—reshaped MSME innovation, export orientation, and competitiveness, while simultaneously increasing compliance and cost pressures.

The structural transformation literature documents India's post-1991 shift toward services-led growth, noting its high productivity gains but limited employment absorption. Scholars argue that while digitalization and e-commerce have expanded market access for MSMEs, traditional service-sector enterprises remain characterized by informality and low earnings, reinforcing the need for a strong manufacturing base.

More recent studies focus on MSME financing, sustainability, and resilience, highlighting persistent credit constraints, technological gaps, and challenges in transitioning toward low-carbon production models. Within this context, CSR-related literature identifies significant institutional and operational barriers to CSR adoption among MSMEs, including regulatory complexity, resource limitations, limited awareness, and difficulties in impact measurement. The consensus across studies suggests that CSR remains largely compliance-driven rather than strategically integrated within MSME operations.

Finally, literature on entrepreneurship and ecosystem builders underscores the importance of institutional intermediaries such as tool rooms, universities, industry associations, and entrepreneurial networks. Organizations like CITD, TiE, and university-based entrepreneurship cells are identified as critical enablers of skill development, mentoring, innovation diffusion, and startup formation, helping bridge gaps left by markets and formal policy frameworks.

Overall, the literature reveals that MSME development in India is shaped by a complex interplay of regional political economy, institutional support, sectoral dynamics, and evolving regulatory expectations. While PSUs and clusters have historically driven MSME growth, contemporary challenges related to finance, sustainability, and CSR integration necessitate more coordinated, context-sensitive policy and institutional interventions.

III.FINDINGS

All The study shows that the development of MSMEs in India depends far more on regional institutional conditions than on market forces alone. Regions such as Pune, Bangalore, and Hyderabad, which have benefited from political stability, supportive industrial policies, and strong public institutions, have been able to build resilient and dynamic MSME ecosystems. In contrast, regions marked by socio-political instability and policy distortions—most notably the industrial decline of Kolkata—have experienced stagnation, business closures, and declining entrepreneurial activity. These contrasts clearly underline the importance of governance quality and institutional continuity in shaping MSME performance.

Public Sector Undertakings (PSUs) have played a foundational role in nurturing MSMEs by creating stable demand, transferring technology, and setting production and quality benchmarks. Organizations such as HAL, BEL, BHEL, and ECIL enabled the emergence of extensive networks of ancillary units in sectors like defence, heavy engineering, and electronics. At the same time, the findings suggest that overdependence on PSUs can make MSMEs vulnerable to fluctuations in public procurement. This risk is evident in the BHEL–Trichy cluster, where changes in demand patterns led to a sharp decline in ancillary units.

The study further highlights the significance of cluster-based development in strengthening MSME competitiveness. Well-established clusters—such as Coimbatore's engineering cluster, Salem's sago and starch industry, and pharmaceutical clusters in Maharashtra and Gujarat—demonstrate higher productivity, innovation, and export capacity. These advantages stem from shared infrastructure, collective learning, and strong institutional support. In contrast, regions like Ratnagiri, despite being rich in natural resources, continue to face under-industrialization and large-scale labour migration due to weak institutional support and ineffective cluster governance.

Operational challenges remain a persistent constraint on MSME growth. Even where technical skills are available, MSMEs often struggle with limited access to formal finance, conservative lending practices, and regional disparities in raw material costs. These constraints restrict investments in technology upgradation, modernization, and compliance with international quality and sustainability standards, limiting MSMEs' ability to integrate into high-value supply chains.

The findings also reveal that CSR adoption among MSMEs is largely driven by compliance requirements and pressure from large corporate buyers rather than by strategic intent. Low awareness levels, limited managerial capacity, absence of simple impact-measurement tools, and a lack of MSME-specific incentives prevent CSR from becoming an integral part of business strategy. As a result, many MSMEs continue to view CSR as a regulatory obligation rather than as an opportunity to enhance competitiveness and long-term sustainability.

Finally, the study points to a structural imbalance in India's growth pattern. While the rapid expansion of the service sector after liberalization has significantly contributed to GDP growth, it has created relatively limited employment opportunities. Manufacturing MSMEs, on the other hand, remain crucial for inclusive and broad-based employment generation. However, their potential continues to be underutilized due to policy neglect, technological gaps, and weak coordination among supporting institutions.

IV. SUGGESTIONS

1) Encourage MSMEs to reduce overdependence on PSUs by expanding linkages with private markets, export channels, and digital platforms.
2) Formulate MSME-specific CSR guidelines with simplified compliance requirements and incentive-based adoption mechanisms.
3) Integrate CSR activities with MSMEs' core business functions to enhance sustainability and long-term competitiveness.
4) Strengthen cluster-level institutions to facilitate shared infrastructure, collective procurement, and coordinated compliance support.
5) Introduce cluster-based and guarantee-backed financing models to improve MSME access to formal credit.
6) Support technology upgradation through long-term, affordable financing with adequate moratorium periods.
7) Address regional disparities in input costs and logistics through targeted infrastructure development and policy support.
8) Promote domestic production of critical inputs in strategic sectors by integrating MSMEs into upstream supply chains.
9) Expand institutional support systems such as tool rooms, incubators, and mentoring networks to enhance MSME capability building.

V. CONCLUSIONS

The study of institutional and operational barriers in MSME development reveals that regional success is fundamentally tied to the synergy between political stability, proactive infrastructure development, and visionary leadership. The stagnation of the Calcutta industrial belt serves as a cautionary tale of how socio-political unrest and policy neutralization (freight equalization) can derail a thriving economic center. Conversely, the rise of Pune and Bangalore demonstrates the "nursery effect" of strategic PSUs, where HAL, BEL, and BHEL provided the early demand and technical standards that allowed a sophisticated layer of private MSMEs to emerge.

Operational barriers, particularly in the realm of finance and technology, remain persistent. The Trichy BHEL cluster's decline due to procurement shifts and raw material price disparities highlights the vulnerability of MSMEs to external market forces. In the pharmaceutical sector, the dependency on Chinese APIs represents a strategic risk that can only be mitigated through large-scale domestic investment and regulatory streamlining.

Finally, the integration of CSR into MSME operations is currently in a formative stage. While the 2013 mandate has formalized social expenditure for large firms, MSMEs require a more supportive framework that includes:

1) Simplified Impact Measurement Tools: Allowing small units to demonstrate their social value to stakeholders without excessive administrative costs.
2) Demand Aggregation: To help MSMEs negotiate better commercial terms for raw materials and equipment, as seen in the pharma cluster recommendations.

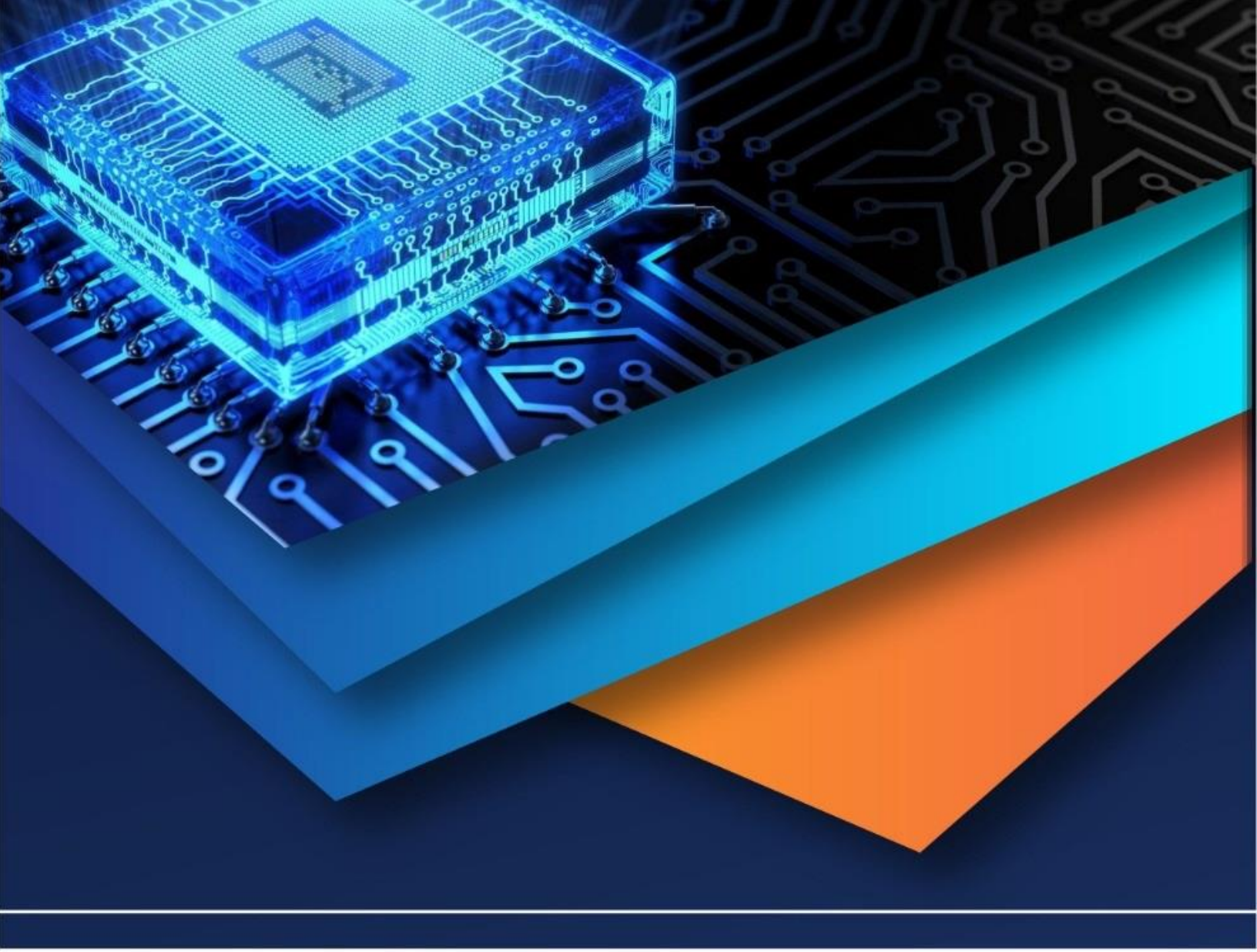
3) Sector-Specific CSR Strategies: Tailoring initiatives to a unit's core competencies to ensure sustainability and scalability.
4) Revitalized Banking Support: Facilitating credit access for modernization, acknowledging that technically sound MSMEs are the bedrock of India's export ambitions.

Through a combination of collaborative partnerships, innovative solutions, and a transition toward a low-carbon, formalized economy, India's MSMEs can move from being passive beneficiaries of regional growth to proactive drivers of global industrial and social excellence.

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