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Evolution of MSME Classifications in India: Institutional Transformation, Policy Dynamics and Economic Implications

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Abstract

India's Micro, Small and Medium Enterprises (MSME) sector plays a crucial role in employment generation, industrial production, exports and regional development. The Government of India has been making continuous changes in the classification of MSMEs over time in response to the evolving industrial landscape, evolving inflation pressures, globalisation, as well as technological transformation and competitiveness issues. Yet, little research has been done to analyse the institutional changes in the classification of MSMEs and their wider implications for their development. Significant changes that occurred in the classification of MSME from Small-Scale Industries (SSI) to the present investment and turnover classification under the new MSME umbrella are critically discussed. The study delves into the relationships between policy change and the restructuring of enterprise formalisation, competitiveness, financial access and industrial growth dynamics, based on Institutional Theory and Institutional Isomorphism and the Resource-Based View. The paper is based on secondary literature, government reports and institutional policy documents, thus taking a conceptual and policy-review approach. The results indicate that changing the classification of MSME is not just an administrative matter, but an institutional move to respond to globalisation, market integration, technological modernisation and economic restructuring. While the new classifications have facilitated greater scalability, fostered formalisation and expanded business opportunities for enterprises, challenges of implementation, access disparity, and policy awareness remain. The study makes its contribution in the field of MSME literature by providing an integrated institutional view on the evolution of enterprise classification systems in India and presents a conceptual framework for the linkage between MSME classification reforms and aspects of economic development outcomes. The paper also offers policy suggestions to boost sustainability, competitiveness and inclusive industrial development of MSMEs.

Keywords: *MSMEs, MSME Definition Institutional Theory***,** *Small-Scale Industries Enterprise Classification***,** *Industrial Policy***,** *India***,** *Economic Development Formalisation***,** *SME Competitiveness*

INTRODUCTION

Micro, Small and Medium Enterprises (MSMEs) are an integral part of the Indian economy and form one of the most dynamic segments of the economy. The sector plays an important role in employment generation, increase in industrial production, exports, entrepreneurship development and balanced regional growth. Also, MSMEs are receptive complementary units to the large industries in that they supply intermediate products, create employment opportunities, thereby stepping towards inclusive economic development. The MSME is an important contributor to India's manufacturing production and exports and plays a key role in the reduction of regional disparities, according to the Ministry of MSME. In India, the growth of small businesses has always been linked with major economic, political and institutional changes. Traditional artisan-based production systems were the origin of small-scale industrial development and were put in the spotlight during post-independent industrialisation in India. In the Industrial Policy Resolution, 1948, the importance of Cottage and Small-Scale Industry for

Employment Generation and Rural Industrialisation was highlighted. Later, several institutional supports like the introduction of the Industries (Development and Regulation) Act, 1951, the Small-Scale Industries Board and the Central Small Industries Organisation were created to provide technical assistance, financial support and infrastructure to promote the sector.

This classification of small enterprises in India has been constantly evolving over the decades. Firstly, the criterion of enterprise classification was mainly based on the employment size and the investment in plant and machinery. But the economic liberalisation of 1991, globalisation, technological progress and growing competition and industrial shifts highlighted the shortcomings of previous classifications. The need arose for a more flexible and growth-oriented classification that could account for enterprise growth and competitiveness. Micro, Small and Medium Enterprises Development (MSMED) Act, 2006 was a huge institutional shift as it formally introduced the MSME framework and thrust enterprise categorisation into the micro, small and medium category. As per the latest revisions made by the Government of India in 2020, the MSMEs are no longer being defined based on manufacturing or service-based enterprises and are now defined on the basis of investment and turnover. While it is established from the existing literature that MSMEs play a major role in economic growth and entrepreneurship, there has been little attention given to their access to finance, competitiveness and innovation, employment creation and export performance **(Beck & Levine, 2005) & (Wiklund & Shepherd, 2005). (Audretsch, 2001)** investigated to understand the institutional logic in the nature of the evolution of the classification of MSMEs and its wider implications for development.

This gap becomes significant because the categories of enterprise are not just administrative ones, but can impact credit access, tax relief and incentives, government procurement, subsidy and regulatory protection. The institutional view posits that legitimacy pressures, environmental shifts and socio-economic change drive the change of organisational structures and policy frameworks. These theoretical views help to understand the process of change in the classification of MSMEs in India as part of a wider institutional adaptation process. In this context, the present study throws critical light on the historical evolution of the classification of MSME in India and its institutional, economic and policy implications. The paper draws attention to three questions: (1) what are the changes in the MSME classifications at various policy stages in India, (2) what were the factors behind the changing classifications and (3) what were the ramifications of the changes on enterprise growth, competitiveness and industrial development? The study has a conceptual and policy-review approach that utilises secondary literature, government reports and institutional documents.

Research Methodology

In the present study, the qualitative conceptual review and policy-analysis approach have been taken for analysing the evolution of the classification of MSMEs in India with their institutional and economic implications. The research is mainly secondary data gathered from peer-reviewed journal articles, Government policy documents, institutional reports and legislative notifications/official publications related to the MSME sector. Conceptual review methodology has been chosen as it was mainly aimed at critically analysing the changes in classification of MSMEs and their developmental implications, and there was no aim to find out a causal relationship. The keywords like "MSME classifications", "small-scale industries", "enterprise classification", "MSMED Act", "MSME policy reforms", "enterprise formalisation" and "SME competitiveness" were used to gather relevant literature from the major Academic databases, namely: Scopus, Web of Science, Google Scholar, JSTOR. Peer-reviewed research articles, seminal theoretical studies and official policy documents from the Ministry of MSME, Reserve Bank of India (RBI) and NITI Aayog were given utmost preference. The study uses thematic and interpretive analysis in order to find the dimensions that are major to the subject of MSME classification reform, which are institutional transformation, financial inclusion, competitiveness and industrial development and globalisation. Theoretical

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approaches, including Institutional Theory, Institutional Isomorphism, Resource-Based View and Structural Transformation Theory, were used to explain the general institutional reasoning of policy changes.

THEORETICAL FOUNDATIONS

1. Institutional Theory

Institutional Theory explains how organisational structures, policies and practices evolve in response to broader socio-economic pressures, legitimacy requirements and environmental expectations. The theory argues that organisations often adopt structures and procedures not only for operational efficiency but also to gain legitimacy, stability and societal acceptance **(Meyer & Rowan, 1977).** Institutional environments shape organisational behaviour through regulatory systems, policy frameworks, social norms and professional expectations, thereby influencing the evolution of governance structures and economic institutions. In the context of MSMEs, enterprise classification systems can be understood as institutional mechanisms designed to regulate industrial activity, facilitate policy implementation and promote economic coordination. The evolution of MSME classifications in India reflects changing institutional priorities associated with industrialisation, globalisation, technological modernisation and economic liberalisation. The transition from traditional Small-Scale Industry (SSI) classifications toward investment- and turnover-based MSME classifications demonstrates how institutional reforms emerge as adaptive responses to evolving economic realities.

2. Institutional Isomorphism

The concept of Institutional Isomorphism, proposed by **(Dimaggio & Powell, 1983),** explains how organisations and institutional systems gradually become similar because of regulatory pressures, uncertainty and professional standardisation. The theory identifies three major forms of isomorphic change: coercive, mimetic and normative isomorphism. Coercive isomorphism emerges through formal regulations, state policies and legal requirements imposed by governments and regulatory institutions. In the Indian MSME sector, classificational reforms introduced through the MSMED Act, 2006 and the revised MSME criteria of 2020 illustrate coercive institutional adaptation designed to improve policy efficiency and regulatory coordination.

Mimetic isomorphism occurs when organisations or policy systems imitate successful models under conditions of uncertainty. The growing incorporation of turnover-based criteria and integrated enterprise classifications reflects India's attempt to align its MSME framework with international standards adopted in developed and emerging economies. Such reforms were influenced by increasing globalisation, international competition and changing industrial structures. Normative isomorphism originates from professionalisation, expert recommendations and institutional knowledge systems. Policy institutions, financial organisations, economic advisory bodies and international development agencies increasingly promoted more flexible and growth-oriented MSME classifications capable of supporting enterprise scalability and competitiveness. These processes contributed to the transformation of India's MSME classification framework from a protection-oriented model toward a competitiveness-driven institutional structure.

3. Resource-Based View (RBV)

The Resource-Based View (RBV), developed by **(Barney Jay, 1991),** argues that organisational competitiveness depends on the ability of firms to acquire, develop and utilise valuable, rare, inimitable and non-substitutable resources. Competitive advantage emerges when enterprises effectively combine financial, technological, managerial and human resources to improve productivity, innovation and market performance. Within the MSME sector, enterprise classification systems significantly influence access to strategic resources such as institutional finance, technological support, subsidies, market incentives and government procurement opportunities. MSME classification reforms, therefore, have important implications for enterprise competitiveness because classification determines eligibility for multiple developmental benefits and policy interventions.

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Earlier investment-based classifications often restricted enterprise expansion by discouraging firms from scaling production beyond prescribed thresholds. In contrast, revised MSME classifications introduced greater flexibility by incorporating turnover criteria and expanding investment ceilings. These reforms enabled enterprises to retain MSME benefits while pursuing growth and modernisation strategies. From the RBV perspective, the revised classification system strengthened the capacity of enterprises to mobilise financial and technological resources necessary for improving long-term competitiveness.

4. Structural Transformation Perspective

Structural Transformation Theory emphasises the gradual transition of economies from traditional, low-productivity activities toward more diversified, industrialised, and technology-intensive economic structures. The theory highlights the role of industrialisation, entrepreneurship and enterprise development in promoting employment generation, productivity growth and economic modernisation. The MSME sector occupies a central position within the structural transformation process because it acts as a bridge between informal economic activities and formal industrial production systems. In developing economies, MSMEs contribute to employment generation, regional industrialisation, export diversification and entrepreneurial development. Consequently, enterprise classification systems become important policy instruments for facilitating industrial transition and economic inclusion.

(Mathew, 2014) Investigating the evolution of MSME classifications in India reflects broader structural changes associated with liberalisation, globalisation and technological advancement. The inclusion of service enterprises under the MSMED Act, 2006 and the integration of turnover-based criteria in 2020 indicate the growing recognition of knowledge-intensive and service-oriented economic activities within India's industrial policy framework. These reforms demonstrate the shift from a narrow manufacturing-oriented perspective toward a more comprehensive understanding of enterprise development in a modern economy.

5. Theoretical Integration and Relevance to MSME Classification Reforms

The theoretical perspectives discussed above collectively provide a comprehensive framework for understanding the evolution of MSME classifications in India. Institutional Theory explains how policy reforms emerge in response to legitimacy pressures and changing socio-economic conditions, while Institutional Isomorphism highlights the influence of regulatory systems, globalisation and professional policy frameworks on institutional convergence. The Resource-Based View explains how classification systems affect enterprise access to strategic resources and competitiveness, whereas Structural Transformation Theory situates MSME reforms within the broader context of industrial modernisation and economic transition.

Literature Review

The MSME sector has attracted significant scholarly attention because of its contribution to employment generation, industrial production, entrepreneurship development and economic growth. Existing literature broadly examines MSMEs from the perspectives of enterprise competitiveness, financial accessibility, industrial development, globalisation, and policy support mechanisms. However, relatively limited attention has been devoted to understanding the institutional evolution of MSME classifications and their broader implications for enterprise formalisation, policy accessibility and industrial transformation. The present review synthesises existing literature thematically to identify major scholarly trends, conceptual gaps and emerging research directions.

A. MSMEs and Economic Development

The literature has seen a significant recognition of the role of MSMEs in developing the economy and creating employment in developed and developing economies. Based on the support of labour-intensive production systems, **(Beck & Levine, 2005)** stated that small and medium enterprises play a significant role as drivers of poverty reduction, economic inclusion and employment expansion. **(Ayyagari et al., 2005)** pointed out that SMEs play a crucial role in industrial diversification, regional development and entrepreneurial expansion in emerging economies. All these studies point towards the significance of MSMEs as a tool to boost inclusive economic growth and structural transformation.

B. MSME Competitiveness and Resource Accessibility

A second key theme in the MSME literature is enterprise competitiveness and access to strategic commodities. The Resource Based View (RBV) of **(Barney Jay, 1991)** has suggested that competitiveness of the enterprise is related to its capacity to gain and exploit valuable financial, technological, and managerial resources. **(Singh et al., 2010)** added that in the current era of globalisation and competition, MSMEs need to strengthen and upgrade their technological capabilities, productivity and capacity for innovation to achieve long-term competitiveness. **(O'Regan et al., 2006)** also stated that innovation and technological modernisation are key to the enhancement of the competitive performance of manufacturing SMEs. In the same line, **(Tybout, 2000)** showed that export-oriented growth, technological adaptation and institutional support shall be essential to support the competitiveness of SMEs in the world market. Based on these studies, it is clear that enterprise performance and scalability are significantly influenced by access to institutional finance, technological infrastructure and policy incentives.

C. Institutional Reforms and Policy Transformation

The literature regarding MSMEs says that MSME reforms are based on the adaptation to the changing economic and industrial environment. **(Meyer & Rowan, 1977)** proposed that the structures of institutions have changed to ensure cohesion and continuation of the organization in a changing socio-economic environment. In a similar manner, **(Dimaggio & Powell, 1983)** proposed the idea of Institutional Isomorphism to account for the way that policy systems slowly change due to regulatory, professional and global pressures. These theoretical approaches are essential in understanding the development of the MSME classification in India **(Tambunan, 2008)** claimed that the role of the government and institutional changes are important in enhancing SME development in developing economies. Similarly, **(J. Storey, 2016)** stressed the need for a market-oriented policy framework that could facilitate enterprise development and competitiveness.

(Ashwin & Sapna, 2024) The shift from Small-Scale Industry (SSI) classification to MSME is indicative of the overall institutional change that has taken place due to globalisation, liberalisation, and technology modernisation in the Indian context. The current studies acknowledge the efforts of the MSMED Act, 2006 and the revised MSME classification, 2020, in making the policies more inclusive and scaling up the enterprises and their formalisation. Yet, a lot of literature is still descriptive and policy-oriented, with less focus on critically addressing the institutional logic underpinning classificational change.

D. MSME Formalisation and Financial Inclusion

Another significant field of study on MSMEs is financial inclusion and the formalisation of enterprises. One of the key constraints cited in various studies as affecting MSME growth and sustainability is the lack of access to institutional finance. It has been argued that if the enterprise registers formally, its access to credit, subsidies, governmental schemes and market opportunities is enhanced. Several recent reforms, like the Udyam registration, GST and digital financial systems, have promoted formalisation in the Indian MSME sector. However, the existing literature points towards the fact that formalisation enhances enterprise legitimation, transparency and institutional governance systems. But experts also report that barriers to digital literacy and procedural complexities, and a lack of awareness of formal registration mechanisms remain in the micro and rural enterprise sector.

E. Research Gaps and Critical Interpretation

The literature search paper shows that most of the research in MSME has been focused on enterprise financing, competitiveness, innovation, employment generation and industrial performance. While there are various studies on MSME policies and institutional supports, studies that critically

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discuss the historical evolution of the MSME classifications and the implications of the same have been limited. Most of the current studies take the classification of MSME as an administrative classification and not a dynamic institutional instrument that can influence enterprise behaviour, industrial structure and accessibility of industrial policies. Moreover, there is very little evidence of the impact of classificational changes on enterprise scalability, formalisation, competitiveness and structural changes in emerging economies like India. The other major gap is in terms of theory integration. The literature available so far usually investigates MSME development from a single point of view, like financial, competitiveness or entrepreneurship perspective, but fails to combine Institutional Theory, Institutional Isomorphism, Resource Based View and Structural Transformation Theory together in a single perspective. Hence, current scholarship on MSMEs reveals a fragmented institutional and developmental logic that underpins the MSME classification changes.

The present study tries to fill these gaps by giving a thorough and comprehensive institutional analysis of the evolution of the MSME classification in India and looking at the implications of MSME on enterprise formalisation, competitiveness, financial inclusion and industrial development. The study combines various theories and approaches both in the process of analysis and in organising the research material, adding to the efforts to provide a more comprehensive understanding of the reform of MSME classification in the context of economic transformation and institutional modernisation.

Discussion

Table 1: Evolution of MSME classifications in India (1950-2025)

Period / Policy Phase	Enterprise Classification	Investment / Classification Criteria	Major Institutional Changes	Policy Orientation
1950 SSI Framework	Small Scale Industries (SSI)	Investment up to ₹0.5 million with employment ceiling (50 workers with power / 100 without power)	Initial formal recognition of small industries based on fixed assets and employment criteria	Employment generation and rural industrialization
1960 Revision	SSI	Investment up to ₹0.5 million	Employment condition removed from classification	Simplification of industrial classification
1966 Industrial Revision	SSI & Ancillary Units	SSI: ₹0.75 million; Ancillary: ₹1 million	Shift from fixed assets to plant and machinery basis; introduction of ancillary industries	Industrial specialization and supply-chain integration
1975 Expansion Policy	SSI & Ancillary Units	SSI: ₹1 million; Ancillary: ₹1.5 million	Expansion of investment thresholds	Industrial capacity enhancement
1977 Tiny Sector Policy	SSI, Ancillary & Tiny Units	Tiny units: ₹0.1 million	Tiny industries introduced for rural and semi-urban areas	Decentralized rural entrepreneurship
1980 Industrial Modernization	SSI, Ancillary & Tiny Units	SSI: ₹2 million; Tiny: ₹0.2 million	Increased investment ceilings due to inflation and modernization needs	Technology upgradation
1985 Service Sector Recognition	SSI, Ancillary, Tiny & SSSE	SSI: ₹3.5 million	Small Scale Service Establishments (SSSEs) formally recognized	Expansion toward service economy
1991 Liberalization Reforms	SSI, Tiny, EOU & SSSBE	SSI: ₹6 million	Export-Oriented Units (EOUs) and service-business enterprises	Global competitiveness

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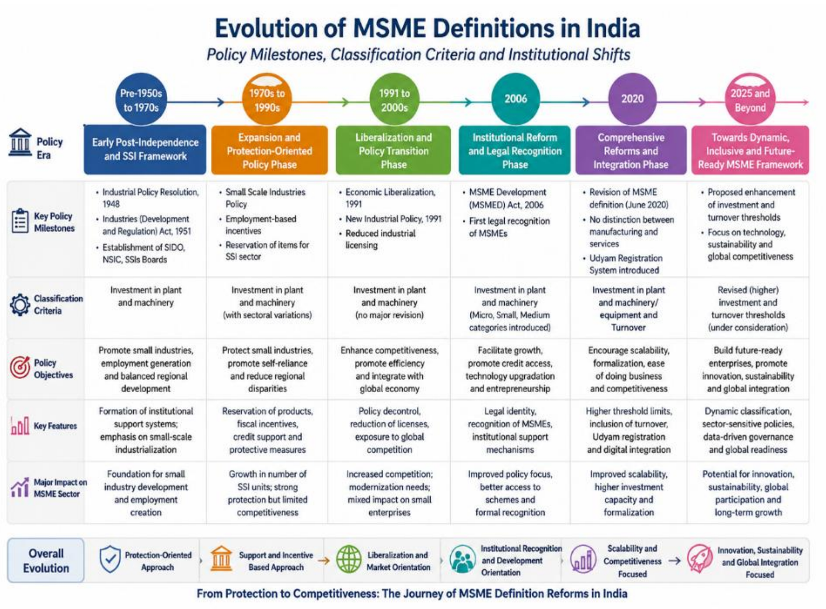
			introduced; location restrictions removed	and export orientation
1997 Post-Liberalization Expansion	SSI & Related Categories	Investment ceiling increased to ₹30 million	Significant expansion of thresholds after liberalization	Competitiveness and industrial scaling
1999 Rationalization Policy	SSI & Related Categories	Reduced to ₹10 million	Thresholds reduced to prevent misuse by larger firms	Targeted support for genuine small firms
2000 Adjustment Framework	SSI & Service Enterprises	SSI: ₹10 million	Service-sector enterprise support strengthened	Service-sector integration
MSMED Act 2006	Micro, Small & Medium Enterprises	Separate investment limits for manufacturing and services	Formal introduction of MSME framework; service enterprises institutionalized	Competitiveness, formalization and enterprise development
MSME Revision 2020	Unified MSME Classification	Investment + turnover criteria introduced	Manufacturing/service distinction removed; turnover-based classification adopted	Scalability, formalization and growth orientation
MSME Revision 2025	Expanded MSME Framework	Significantly revised investment and turnover ceilings	Large expansion in thresholds to accommodate inflation and enterprise growth	Industrial expansion and economic resilience

Source: Compiled and synthesised by the author from Government of India policy documents, MSMED Act notifications and MSME classification revisions.

Figure 1: Timeline of institutional evolution of MSME classifications in India



Source: Developed by the author based on Government of India MSME policy notifications and institutional reforms.

Table 1 and **Figure 1** provide a profile of institutional and policy shifts in the classification of MSMEs in India between 1950-2025 and the changing developmental priorities of the Indian economy. The original Small-Scale Industry (SSI) concept tended to focus on job creation, balanced regional development and rural industrialisation based on investment and employment criteria only. Gradually, the classification of the system changed towards investment in plant and machinery as the industrialisation and technological needs had grown over the years of the industry.

The changes brought in the 1970's and 1980's emphasised decentralised entrepreneurship and the significance of the service businesses. But the liberalisation reforms of 1991 constituted an important institutional change, with the liberalisation of investment limits, export-led orientation of the products and an opening up of MSMEs to the competitive global markets. The MSME framework was formalised with the MSMED Act, 2006 and with the revised classification of 2020, investment and turnover-based criteria were also incorporated, while the distinction between manufacturing and service enterprises was eliminated.

Institutional and Economic Implications of MSME Classification Reforms

The changing classifications of MSMEs in India have had institutional and economic implications in the fields of enterprise development and competitiveness of industry and policy implementation. Eligibility to avail credit facilities, subsidies, tax benefits, government procurement preferences, infrastructure support and technological assistance is dictated by the enterprise classification systems. Hence, a change in the classification of MSMEs will impact not only their policy administration but also show its impact on enterprise behaviour, enterprise growth strategies and enterprise sustainability. Increased investment and turnover-based classification of MSMEs is the broader structural change phenomenon in the era of globalisation, liberalisation, and institutional modernisation.

I. Enterprise Formalization

One of the key impacts of the classification changes of MSMEs has been the rise in the degree of formalisation of MSMEs in the Indian economy. Previous schemes of SSI were mostly in the context of disjointed administration systems where a significant percentage of businesses were informal or semi-formal. The new MSME framework that came into effect after the reforms in 2020 put greater emphasis on enterprise formalisation, which has been interwoven with digital registrations, the Goods and Services Tax (GST) framework, and the Udyam registration platforms. Turnover-related parameters facilitated the adoption of good bookkeeping and reporting practices and integration into formal regulatory processes. Formalisation, from an institutional perspective, enhances enterprise legitimacy, visibility and accessibility in financial and governance systems. According to Institutional Theory, organisations form a formal structure in order to gain legitimacy and to survive in fluctuating economic landscapes. In the Indian context, formalisation has facilitated access of enterprises to institutional finance, government schemes and digital markets. Yet, there is still a long journey to go, as many micro and rural businesses still struggle with issues of digital literacy, bureaucratic processes, and awareness of formal registration processes.

II. Credit Accessibility and Financial Inclusion

MSME classification reforms have also contributed significantly to improving financial inclusion and institutional credit access. Historically, the barriers to finance for MSMEs in India were one of the biggest restraints on the growth and competitiveness of MSMEs. Measures to promote investment were used as criteria to define an enterprise, leading to the problem of cutting off its expansion, as the firm that overstepped the limits became ineligible for subsidised credit and institutional facilities. The changes to the classification of MSMEs greatly raised the limits on investment and added a turnover criterion, facilitating enterprises to grow without defaulting on getting policy benefits automatically. The changes improved access to bank credit, government-backed financial schemes and institutional lending programs. The financial institution credibility of enterprises was further enhanced by an increasing formal registration system.

If viewed through the lens of the Resource-Based View (RBV), access to institutional finance is a strategic resource that is required to grow enterprises, foster innovation and technological modernisation. Accessibility of credit facilities helps MSMEs to invest in infrastructure, implement modern technologies and grow their market operations. However, despite the policy measures taken, there is still a big funding gap, especially in rural and informal areas, for microenterprises. Despite the fact that a wide proportion of MSMEs is not effectively included in the financial system, the factors of collateral, procedural delays and information asymmetry continue to plague effective financial inclusion.

III. MSME Competitiveness and Scalability

The redefined MSME framework has introduced a new paradigm in terms of enterprise competitiveness and scalability in the industrial ecosystem of India. Previous SSI policies tended to be protectionist and were often found to induce a "threshold effect" of intentionally limiting enterprise growth for the purpose of maintaining eligibility for policy benefits. These restrictions put off technological upgrading, productivity improvement and industrial modernisation. The 2020 reforms tried to address this structural problem by significantly raising the limits of investments and turnover and eliminating the difference between manufacturing and services companies. These reforms fostered enterprise growth and diminished growth disincentives. The enterprises were granted growing freedom to take up new technologies and enhance their productivity and value chain linkages with fearless institutional support. This is further understood as adaptive reactions to globalisation and competitive market pressures through the theoretical lenses of Institutional Isomorphism. The MSME path in India slowly progressed towards global classification, which focuses on competitiveness, efficiency and integration into the market. Thus, MSMEs are no longer only production units to be protected, but dynamic economic units with the potential to innovate and grow exports and diversify industries.

IV. Employment Generation and Industrial Development

MSMEs have been playing a crucial role in employment creation and decentralisation of industrialisation in India traditionally. Previous policy regimes centred on the need to increase labour intensity in production and industrialise the countryside as a way of narrowing down geographic inequalities and achieving inclusive economic growth. With its spread and reach in manufacturing, services and rural industries, MSME has played a major role in job creation, specifically amongst the semi-skilled and low-income group. Changes in MSME classifications have also impacted employment through enterprise growth and diversification into new economic activities. The classification of a service enterprise as an MSME under the MSMED Act, 2006 and the elimination of the distinction between manufacturing and services in 2020 indicated the shift of the Indian economy towards the service industry and knowledge-intensive activities. From a structural transformation point of view, MSMEs serve as a link between the activities of the informal economy and the formal industrial system. They not only help develop entrepreneurship but also help in the utilisation of local resources and industrialisation of the region and also help in economic diversification and the country's manufacturing production. Despite this, the employment quality, wage gap, labour informality and productivity limitations are key issues that impact the long-term developmental effect of MSMEs.

V. Export Competitiveness and Global Integration

The defining process of MSMEs has also made Indian businesses more export-oriented and globalised. Liberalisation reforms after 1991 brought Indian MSMEs within the ambit of international competition and at the same time gave them opportunities to export. The policy reform efforts increasingly focused on enhancing competitiveness, quality standards and technological modernisation, and market participation in the international market. The recognition of Export-Oriented Units (EOUs) and service-sector enterprises was a testament to the increasing policy focus on connecting MSMEs with the global value chains. The new investment and turnover limits allowed companies to further scale up production capacity and boost their operational efficiency for export readiness. Digitalisation, formalisation, and technological upgrading supporting institutional reforms also helped MSMEs to integrate into international markets. But, Indian MSMEs still have to encounter problems of quality certification, international standard compliance, logistics cost and limited global market information. Many enterprises face a number of these barriers, which limit their full exploitation of the benefits of globalisation and export opportunities.

VI. Institutional and Policy Challenges

MSME classification frameworks in India still face a few institutional and policy challenges, despite the reforms. The lack of classification systems that are dynamic and inflation-indexed is one major issue. Policy revision happens episodically (reactive) after long time periods and temporary policy distortions or classification inefficiencies occur. One other key difficulty is the disparities in terms of policy accessibility among regions and enterprise classes. Despite administrative hurdles, many microenterprises, especially those in rural and informal areas, are still outside the umbrella of institutional financing and digital platforms, as well as government support. The expansion of the investment thresholds might also be creating an imbalance between the size of the targeted businesses and the support being offered to the more vulnerable micro companies. Additionally, bureaucratic coordination and the lack of data and infrastructure remain issues with the implementation of policies. The adoption of digital governance systems has enhanced transparency and efficiency, but digital exclusion and technological constraints still impact smaller businesses.

Future Policy Directions and Strategic Recommendations

The constant changing of classifications of MSMEs in India is an epitome of the shifting focus of Industrial policy, modernisation, and enterprise development. While recent initiatives have led to a tremendous improvement in enterprise scalability, formalisation, and competitiveness, the fast-changing global markets, digital economies and technological transformation call for a more adaptive and future-oriented MSME policy framework. It is therefore essential that future policy reform goes beyond static classification and is flexible, innovation-centric, and institution-responsive, thereby able to cater to the ever-changing and diverse needs of the MSME sector.

Table 2: Comparative MSME/SME Classification Frameworks Across Major Economies

Country/Region	Classification Basis	Enterprise Criteria	Key Institutional Features	Policy Orientation
India	Investment + Annual Turnover	Micro: Investment ≤ ₹2.5 crore & Turnover ≤ ₹10 crore; Small: Investment ≤ ₹25 crore & Turnover ≤ ₹100 crore; Medium: Investment ≤ ₹125 crore & Turnover ≤ ₹500 crore	Unified framework for manufacturing and services under revised MSME classification	Formalization, scalability, competitiveness and digital integration
European Union (EU)	Employees + Turnover + Balance Sheet	Medium: <250 employees and turnover ≤ €50 million or balance sheet ≤ €43 million; Small: <50 employees and turnover ≤ €10 million; Micro: <10 employees and turnover ≤ €2 million	Multi-dimensional classification integrating employment and financial indicators	Innovation, SME sustainability and regional competitiveness
United States	Industry-Specific Employee or Revenue Thresholds	SBA standards vary across industries; generally based on employee size or annual receipts/revenue	Sector-specific and NAICS-based flexible classification framework	Business competitiveness, procurement participation and entrepreneurial expansion
China	Employees + Revenue +	Criteria differ across sectors; manufacturing SMEs classified using	Highly sector-sensitive classification	Industrial modernization, export

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	Assets (Sector-Specific)	employee strength, annual revenue and total assets	linked with industrial policy priorities	competitiveness and manufacturing expansion
United Kingdom	Employees + Turnover + Balance Sheet	Small firms: <50 employees and turnover ≤ £10 million; Medium firms: <250 employees and turnover ≤ £50 million	Closely aligned with EU SME framework	Innovation support and SME-led economic growth
Japan	Capital Investment + Employees	Manufacturing: Capital ≤ ¥300 million and ≤300 employees; Services and retail have lower thresholds	Industry-specific classification based on enterprise size and capital structure	SME protection, productivity enhancement and technological upgrading

Source: Compiled and synthesised by the author from official policy frameworks of the Government of India, European Commission, U.S. Small Business Administration (SBA), and SME regulatory frameworks of China, the United Kingdom and Japan.

As shown in **Table 2**, these compare frameworks of the classification of MSME/SME in key global economies and there is also a difference in how enterprises are classified from an institutional perspective. However, while China appears to be following a hybrid model of investment and turnover-based, India mainly focuses on formalisation and scalability and the European Union and the United Kingdom mainly rely on employment and turnover-based to foster innovation and regional competitiveness. The United States have a flexible system, with thresholds of revenue and the number of employees, and China and Japan have thresholds based on sector-sensitive criteria that are connected to industrial modernisation and productivity. The table overall shows that there is no single classification of MSMEs around the world, and that classifications of MSMEs everywhere serve as a strategic policy tool aiming at competitiveness, innovation, globalisation, and economic transformation.

1) Dynamic and Inflation-Indexed MSME Classification

A major challenge for the MSME framework in India has been the tendency to periodically revise the classification of enterprises. Extended periods for policy adjustments can result in classification distortions as thresholds are not always useful in practice due to the effects of inflation and technological and production cost modifications over time. Such automatic adjustment of investment and turnover thresholds based on changes in the economy should therefore be adopted in future MSME policy. This will make it easier to maintain policy continuity, cut through administrative red tape and ensure enterprise classifications continue to reflect the current industrial environment. This should be complemented by sector-specific classification mechanisms, as well, since the sector varies a great deal in terms of capital intensity and operational structures between manufacturing, services and technology and digital companies. There may be a lack of fit between the uniform classification systems and the diversity of enterprise activities in a modern economy.

2) Digitalisation and Data-Driven Governance

The increased incorporation of a digital governance system offers great opportunities to boost MSME policy implementation and institutional efficiency. In future, the policy changes in favour of MSMEs should include digital governance systems that connect various data and platforms such as the Udyam register, GST portal, and digital bank and enterprise accounts. This integration may help to enhance transparency, lighten up the burden of bureaucracy, and boost real-time policy monitoring. AI, big data analysis and digital finance technologies can also enhance evidence-based policy making by enabling the identification of enterprise needs and monitoring financial inclusion, as well as strengthening policy targeting procedures. Access to institutional finance, subsidies, export support and government procurement can also be made easier with digital governance for small enterprises.

3) Innovation and Technology-Oriented MSME Policies

In a global economy that is becoming increasingly competitive, enterprise sustainability is largely based on the ability to innovate, modernise, and improve productivity. Future MSME policies should thus move away from subsidy-based policies towards policies that enable MSMEs to innovate for development. The government should focus on providing support for research and development, incentives for digital transformation, integration of Industry 4.0, and technology incubators for MSMEs. Focusing on the technology-based start-up enterprises, digital companies and knowledge-intensive MSMEs that can help in the modernisation of industry and making it competitive in the global market should be given special focus. Technological adaptation and entrepreneurial innovation can be greatly boosted through building collaborative innovation ecosystems between universities, research institutions, industry associations and MSMEs.

4) Green and Sustainable MSME Development

Sustainable policy and the responsible contribution of industry to the environment have become key areas of industrial policy in the world. Hence, future reforms in MSMEs should include the principles of green industrial development in the enterprise policy framework in India. There is certainly a strong advocacy for the sustainable use of the environment, adoption of renewable energy, waste minimisation, and climate-resilient industrial development through the active role of environmentally sustainable MSMEs. With a focus on institutional support, the promotion of green financing mechanisms, carbon reduction incentives and environmentally sustainable production technologies shall be encouraged. In addition, MSMEs should be encouraged to implement the circular economy and sustainable supply-chain systems that can enhance their long-term competitiveness in international markets that increasingly demand conformance with environmental requirements.

5) Inclusive and Region-Sensitive Policy Frameworks

Despite considerable reforms, there are some regional differences that affect the development of MSMEs in India. Businesses in rural and less developed areas frequently suffer from a lack of infrastructure and a lower level of institutional accessibility and technological capabilities as compared to urban industrial centres. Thus, future MSME policies should have a region-sensitive and inclusive approach and be able to respond to the problems of structural inequality in the enterprise ecosystem. Women entrepreneurs, rural enterprises, marginalised population and micro enterprises should be given special policy support, which operate in informal sectors. Decentralised support facilities, regional enterprise facilitation centres or specially designed capacity development programmes can enhance institutional accessibility.

6) Global Competitiveness and International Integration

This operational environment of MSMEs is still undergoing a transformation because of globalisation and international market integration. Further MSME policies should thus aim at enhancing export competitiveness, international certificate standards, participation and integration in international value chains, and digital trade. Export financing support mechanism, logistics infrastructure and quality certification bodies should be strengthened and international market intelligence should be improved to enhance the global participation of Indian MSMEs. Digital commerce platforms and cross-border e-commerce systems can continue to provide a new opportunity for international expansion, especially for small and medium enterprises.

7) Strategic Policy Outlook

The future of MSME development in India hinges on the formulation of adaptive, innovation-oriented, and institutionally responsive policy frameworks that can strike a balance between enterprise growth and inclusive economic development. MSME classifications should not be considered as administrative but rather tools capable of impacting competitiveness, formalisation, technological

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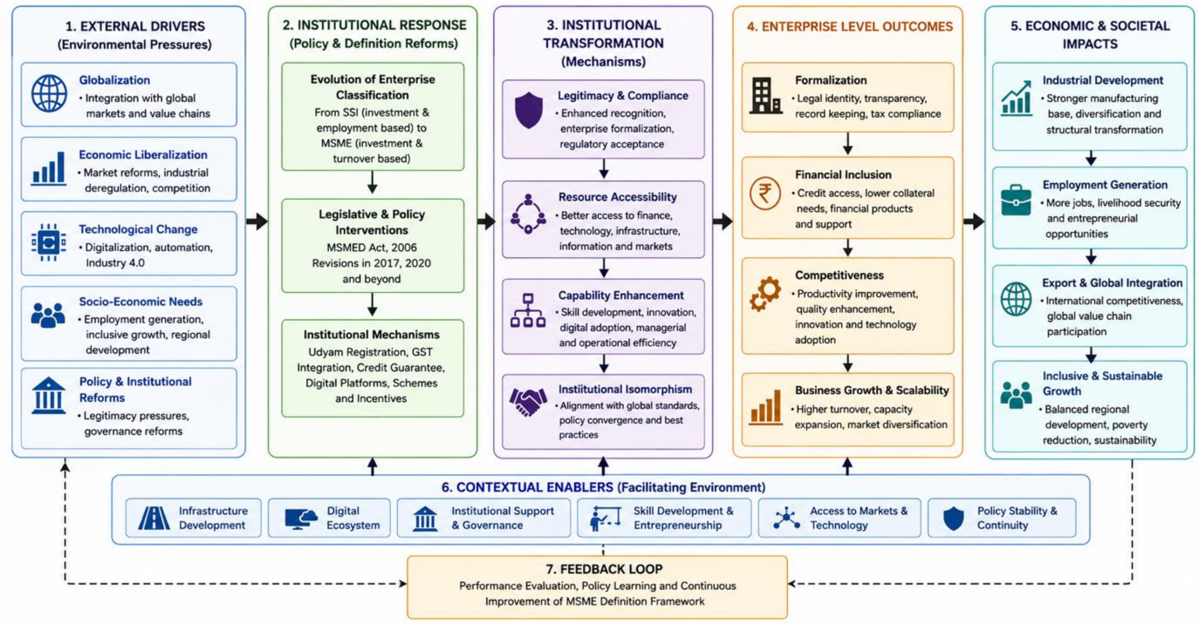
modernisation, and industrial transformation of the institutionalisation.

Proposed Conceptual Framework

Figure 2: Conceptual framework of institutional transformation through the evolution of MSME classifications in India



Source: Developed by the author based on Government of India MSME policy notifications.

Figure 2 shows an institutional transformation conceptual framework for the evolutionary transformation in the MSMEs classification in India. It outlines the effect external economic and institutional factors, such as globalisation, economic liberalisation, technological development, and socio-economic development demands, have had on policy reforms and the classification of enterprises. These external drivers triggered institutional reactions by way of legislative measures like the MSMED Act, 2006, revised MSME classifications and digital governance measures like Udyam registration and integration with GST. The framework also outlines how these institutional changes played a role in enterprise-level transformations through formalisation, financial inclusion, competitiveness and business scalability. Better access to finance and technology, and digital infrastructure and support services, improves enterprise productivity and market integration. As a result, these changes brought a wider effect on the economy and society, such as industrial growth, job creation, export competitiveness and inclusive economic growth.

The introduction of contextual enablers and feedback mechanisms emphasises the evolution of MSME policy as a dynamic and adaptive process. In sum, the overall message of the framework is that MSME classification transformation is not an administrative but strategic institutional tools that enable MSME economic modernisation, enterprise development and structural change in the Indian economy.

Conclusion

The MSME classification in India evolved as part of the institutional transformation of the Indian economy as a whole, which was driven by both economic liberalisation and globalisation, along with technological modernisation and shifting industrial focus. This paper shows that the classification systems of MSMEs are not simply administrative tools, but strategic policy tools which affect formalisation, financial access, competitiveness and industrial development. The shift from the protection-oriented industrial policy approach under the Small-Scale Industry (SSI) classification to a more growth-focused MSME under the integrated framework of investment and turnover reflects the transition from protection to growth and global competitiveness. The results show that successive reforms, especially the MSMED Act, 2006 and the revised classification of MSMEs in 2020, have led to a significant increase in enterprise scalability as well as formalisation and integration into institutional finance and digital governance. These reforms also signified India's integration into the world economy and the changing dynamics of the markets. Despite the considerable progress made, however, the effectiveness of the implementation of the policy on MSMEs is hampered by challenges associated with policy accessibility, geographical disparities, digital exclusion, infrastructural constraints, and financial exclusion.

The present study is an attempt to bring mutual learning by taking an institutional lens through combining the three perspectives of Institutional Theory, Institutional Isomorphism and Resource-Based View and Structural Transformation which provides a comprehensive understanding of the Reforming of the classification of MSMEs in India. In the end, it makes the point that the future MSME policies need to take adaptive, innovation-centric and inclusive forms that can harmonise enterprise growth, sustainability and the long-term transformation of industries in an increasingly competitive global economy.

Limitations and Future Research Directions

The current study aims at conceptual and institutional analysis in detail of the evolution of MSME classification in India, along with its overall economic impact. But there are some limitations to the study. Firstly, the study relies mostly on secondary sources such as journal articles, policy papers and government reports, and may be somewhat restricted with regard to empirical validation of findings. Second, the study is conceptual and a review and therefore it does not statistically analyse the effect of the MSME classification changes on enterprise performance, employment creation, productivity or financial inclusion results. Third, the analysis primarily draws on the Indian context, and thus does not necessarily enable a more general cross-country comparison of enterprise classification systems and institutional policy frameworks.

These limitations notwithstanding, several important directions for future research are opened by the study. Future research can be conducted using a quantitative and an econometric approach and study the long-term effects of change in MSME classification on enterprise growth, export performance, innovation capacity and industrial productivity. Firm-level surveys and case study approaches can also help to dissect classificational changes and implications for enterprise behaviour and formalization and access to institutional finance in different sectors and regions. More in-depth insights for the convergence and adaptation of policies between developed and developing countries as well as between MSMEs and other enterprises could also be gained by comparative international studies on the classification frameworks of MSMEs across developed and emerging economies. Moreover, future studies could investigate the role of digital governance and Artificial Intelligence in MSMEs in the context of the changing ecosystem of enterprises and the transformation towards Industry 4.0 and sustainability-focused policies.

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