MSMEs in Focus: How Budget 2025-26 Fuels Sustainable and Inclusive Development

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Abstract

Micro, Small, and Medium Enterprises (MSMEs) form the backbone of India's economy, contributing significantly to GDP, exports and employment generation. Despite their critical role, MSMEs continue to face persistent challenges including inadequate access to credit, barriers to digital transformation, regulatory bottlenecks and increasing global competition. The Union Budget 2025-26 introduces a series of reforms and initiatives aimed at addressing these constraints while fostering innovation, inclusivity and competitiveness. Key measures include revised MSME classification norms, enhanced credit guarantees, the introduction of MSME Credit Cards, targeted funds for startups and first-time entrepreneurs and export promotion missions. The study is based on a qualitative and descriptive research design using secondary data sourced from government budget documents, policy reports, institutional publications and relevant academic literature. A thematic analysis approach is employed to evaluate the policy measures introduced in Union Budget 2025-26 and their implications for the MSME sector. Additionally, the budget emphasizes support for labor-intensive sectors, digital integration and alternative financing mechanisms. This paper analyzes these initiatives within the broader policy framework and highlights their potential to strengthen MSMEs as engines of economic transformation. It argues that while the budget provides a strong foundation for sustainable and inclusive growth, effective implementation, institutional coordination and entrepreneur awareness will be crucial to unlocking the sector's full potential and advancing India's goal of becoming a $5 trillion economy.

Keywords: MSMEs, union budget 2025-26, economic growth, credit support.

Introduction

Micro, Small and Medium Enterprises (MSMEs) are companies that are relatively small in a comparison with large companies but are an important part of the economic development. These businesses are categorized according to their level of investing in plant, machinery or equipments and the turnover per year. The classification assists in giving specific policy guidance, financial aid and incentives to various business sizes. MSMEs are contributing close to 30 to the GDP and they also employ more than 11 Crore individuals (AMBIT Finvest, 2025). They are critical towards promoting entrepreneurship, regional development and economic inclusivity. These are not only economic entities, but the pillars of societies and they provide jobs and enhance inclusive growth especially to the working poor, women, youths and marginalized communities. The industry promotes entrepreneurship since someone can easily set up their own businesses with low capital. The MSMEs are encouraging the industrialization in the less developed regions and in this process contribute to the alleviation of the regional economic development inequalities.

The MSMEs are largely concentrated in rural India, with 32 million of the total 63 million MSMEs located in rural India. These small companies are very important in the economic growth of the rural areas as they bring about ripple effect of prosperity and growth. The MSME sector in India has been a silent social worker in improving rural India, economic growth, employment and low capital entrepreneurship. The Agra footwear industry is a bright illustration of how the MSME sector has transformed the face of rural India since 28% of footwear exported globally comes out of the MSME sector in India. These small and medium enterprises are very important in increasing the total exports of India with the contribution of about 45 percent to the export earnings of the country (Agnivesh Kumar, 2024). According to government reports, women have more than 20 percent MSMEs (13.5 million businesses). These types of enterprises, which are oriented towards traditional crafts and food processing, as well as modern technological start-ups are MSME run by women and are also an indicator of the flexibility and strength of the Indian woman. (IIFL Finance, 2024).

What is MSMEs

MSMEs are businesses that are characterized with their boundaries of investment in equipment and the yearly turnover. They are employed in manufacturing, service and trade. Concerns MSMEs are significant to the Indian economic system, because they generate employment, encourage entrepreneurship and improve innovation. The classification criteria have over the years been modified depending on the existing business reality based on the team of originally established classification criteria in the MSMED Act of 2006. (India Filings, 2025).

MSMEs New Definition

MSMEs are very significant in economic growth in India as they contribute a lot to the GDP, exports and people created. The government has realised their importance and, at regular intervals, updated the MSME classification criteria to be more relevant to the dynamic business environment and enable entrepreneurs to get the necessary benefits like loans, subsidies and tax incentives. Finance Minister Nirmala Sitharaman in the Union Budget 2025 made significant changes to the New MSME classification, raising the investment threshold by 2.5 times and doubling the turnover threshold. The new MSME requirements can be implemented since April 1, 2025. The rationale behind this move is to create momentum of growth, spur innovation and provide a more facilitating environment in which MSMEs can thrive. In this article, we shall consider the MSME New Definition. The new definition of MSME, which was announced in the Union budget 2025, could take effect on April 1, 2025. After the application, the new investment and turnover threshold will be applied to categories businesses into Micro, Small and Medium Enterprises (IndiaFilings, 2025).

Why budget 2025 has presented the new MSMEs definition criteria

- **Fostering Innovation and Growth:** Through the provision of the opportunity to invest more in plant and machinery or equipment, but without going beyond the MSME boundaries, the government promotes modernization and the use of technologies as well as infrastructure development.

- **Global Competitiveness:** The recent thresholds of the MSME classification allow the medium-sized businesses to compete on the international arena. Having increased turnover limit (₹500 crore), they can magnify the production and explore the international markets without sacrificing the benefits of being an MSME.

- **Employment Generation**: MSMEs are the best job generators particularly in semi-urban and rural locations. Increased thresholds will allow bigger businesses to employ additional employees which would lead to a stronger domestic work force.

- **Streamlined Compliance & Governance:** One, revised framework within the new MSME category reduces the amount of paperwork and promotes ease of doing business which is one of the main goals of recent economic reforms in India.

Methodology

This study adopts a qualitative descriptive research design based on secondary data. Data are collected from Union Budget 2025–26 documents, Government of India reports, policy briefs and existing academic literature related to MSMEs. A thematic and content analysis is used to qualitatively describe and interpret how Budget 2025–26 supports sustainable and inclusive development of MSMEs.

Addressing Challenges Faced by MSMEs

- **Limited Access to Finance:** According to recent reports, formal credit is only available to 14% of India's 63 million small businesses. The estimated $530 billion credit gap in the MSME sector is highlighted by this figure. Strict collateral requirements and inadequate credit histories for many MSMEs, especially those in rural and underserved areas are the obstacles causing this restricted access (The Economic Times, 2025).

- **International Threat:** International players, who frequently enjoy economies of scale, cutting-edge technologies, and improved access to capital, are becoming more and more competitive with Indian MSMEs. Domestic MSMEs may struggle to maintain their market share both domestically and internationally due to this increased competition. Due to factors such as new markets, shifting consumer preferences, and technological breakthroughs, the global market is constantly evolving. For MSMEs to stay competitive and relevant, they must quickly adjust to these changes.

- **Barriers to Digital Transformation:** Many MSME owners and employees lack the necessary skills to utilize digital tools effectively. This gap in digital literacy can prevent businesses from adopting e-commerce platforms or digital payment systems. Inadequate internet connectivity and technological infrastructure in many rural areas hinder the ability of MSMEs to adopt digital solutions.

- **Regulatory Cholesterol:** Policies may not be uniformly implemented across different regions or sectors, leading to disparities in support received by MSMEs. Frequent changes in policies can create uncertainty and increase compliance costs for MSMEs. Many entrepreneurs are unaware of the various schemes available for financial assistance or capacity building. This lack of awareness prevents them from taking advantage of government support.

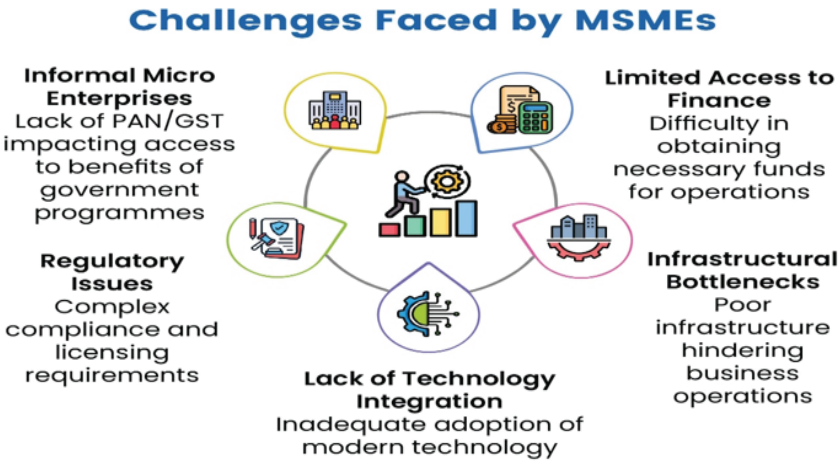

Fig 1: Challenges of MSMEs

Source: *(Vision IAS, 2025)*

The MSMEs Budget 2025-26 Initiatives

Finance Minister Nirmala Sitharaman introduced several initiatives that focus on supporting the MSME sector in the Union Budget 2025-26 on February 1, 2025. These policies will aim to improve access to credit, facilitate innovation and boost growth in this essential sector of the economy. The following are the key highlights:

a) **Revised MSME Classification:** Another change of high importance in the budget is revision of the limit on investment and turnover of MSMEs. The new classification criteria include the following:

ENTERPRISE CATEGORY	CURRENT INVESTMENT LIMIT	REVISED INVESTMENT LIMIT	CURRENT TURNOVER LIMIT	REVISED TURNOVER LIMIT
MICRO ENTERPRISE	₹1 crore	₹2.5 crore	₹5 crore	₹10 crore
SMALL ENTERPRISE	₹10 crore	₹25 crore	₹50 crore	₹100 crore
MEDIUM ENTERPRISE	₹50 crore	₹125 crore	₹250 crore	₹500 crore

Fig 2: New MSME Classification Criteria as per Union Budget 2025

Source: *(Press Information Bureau, 2025)*

- **Micro Enterprises:** Micro units are now allowed to invest up to 2.5 crore and make an annual turnover of up to 10 crores (previously micro was restricted to 1 crore of investment). This growth encourages them to grow without the risk of being reclassified now.

- **Small Enterprise:** The gap between 10 crore and 25 crores in investment and 50 to 100 crores in turnover gives room to the micro-enterprise to easily migrate to the small category.

- **Medium Enterprises:** Since medium-sized businesses are permitted to operate with up to 125 crores in investments and 500 crores in revenue, they may enter the export market and draw in larger domestic and foreign investors.

b) **Enhanced Credit Availability:** Micro and small businesses' credit guarantee coverage was increased from 5 crores to 10 crores, allowing for an additional 1.5 lakh crore in credit over the course of five years. By increasing it to 20 crores with a 1 percent fee on loans in 27 priority sectors, Startups Guarantee Coverage was doubled. International trade is promoted by the Rs 20 crore term loans with higher guarantee coverage available to all exporter MSMEs (Drishti IAS, 2025).

c) **Introduction to MSME Credit Cards:** A new Micro Enterprise Card (ME-Card) is introduced in the budget to improve credit availability for microbusinesses that have registered on the Udyam portal. To issue 10 lakh cards in the first year, each card will have a ₹5 lakh credit limit. It is anticipated that this initiative will lower administrative barriers and expedite small business loan access. (India Filings, 2025).

d) **Funds for Startups & Scheme for First-Time Entrepreneurs:** To give start-ups in a variety of industries financial support, a fund of ₹10,000 crore has been established. By improving access to capital, these funds hope to help startups grow and spur innovation. In the 2025 budget, the Indian government unveiled a new program to assist new business owners, with a special emphasis on women and members of scheduled castes (SC) and scheduled tribes (ST). Over the next five years, the program hopes to help 5 lakh women, SC, and ST first-time business owners. Term loans up to ₹2 crore are available to qualified business owners to launch and expand their enterprises (TCS iON BizHub, 2025).

e) **Focus on Labour - Intensive Sectors:** The production of non-leather footwear, component manufacturing, and design innovation will all be supported by a dedicated Focus Product Scheme for the footwear and leather sector. It is anticipated that this initiative will contribute to a turnover of ₹4 lakh crore and create 22 lakh jobs. Furthermore, a new initiative for the toy sector seeks to strengthen skill development and cluster-based growth, establishing India as a major global center for toy production. A National Institute of Food Technology, Entrepreneurship and Management will be founded in Bihar to support the food processing industry in the eastern region by encouraging innovation, entrepreneurship, and industrial expansion.

f) **Export Promotion Mission & Bharat Trade Net:** The ministries of finance, MSME, and commerce will work together to create an export promotion mission with sectoral and ministerial goals. The objective of this mission is to integrate MSMEs into international supply chains and improve India's export capabilities. A centralized platform for trade documentation and financing solutions will be established with the launch of Bharat Trade Net (BTN). By lowering non-tariff trade barriers that prevent MSME participation in international markets, this initiative seeks to increase the effectiveness of international trade procedures.

Policy Recommendations for MSMEs

a) **MSME: the Past and the Prospect:** In the manufacturing environment in India, a marked change in sector composition has occurred over the last ten years, which has experienced high growth in MSMEs. The consumption-based goods such as automobiles, wood products, furniture, pharmaceuticals have experienced a lot of growth and the production-based ones such as machinery, chemicals, non-metallic minerals, rubber and plastic products have had a balance. Enhancement of efficiency, skills and flexibility of MSMEs is essential in order to support the industrial growth. They can also be more developed by encouraging research and development investments, formalizing smaller manufacturing, solving supply chain problems, improving access of markets and reducing compliance costs. Industrial growth of 9.5 in FY24 provided 8.2% economic growth. Better productivity and use of resources also showed improvement in the form of 5.9% growth in the number of unincorporated enterprises in India between October 2022 and September 2023. The introduction of the Udyam Registration portal in July 2020 has played a key role in formalizing MSMEs, by offering an easy online self-declaration-based and free registration procedure.

b) **Credit Guarantee Schemes (CGSs) :** Credit Guarantee Schemes (CGSs) are a popular policy instrument to deal with the financing issues of MSMEs, which tend to have difficulties in accessing formal credit because of the absence of collateral or the inclusion of high risk by the bank. In these schemes, a government-sponsored entity or a government agency guarantees in part, 50-80 percent of the loan amount, of the loan granted to MSMEs. This system lowers the credit risk of the lenders and allows them to reduce their collateral demands and finance otherwise underserved firms. The effects are enormous, since they open more opportunities to borrowing and promote entrepreneurship and business. Some of the most notable cases of this are the Credit Guarantee Fund Trust of the Micro and Small Enterprise (CGTMSE) in India and the Credit Guarantee Fund (KODIT) in Korea that have contributed to the growth of MSME financing. Nevertheless, the CGSs need to be properly designed: they should be able to support the long-term viability, provide mechanisms to mitigate the moral hazard and have sufficient monitoring and evaluation to track the performance. CGSs when well-designed offer a compromise between financial inclusion and financial system stability (Beck et al., 2010a).

c) **Alternative Finance:** Alternative finance presents MSMEs with a wider range of capital options that is not limited to traditional bank loans, which is more flexible and inclusive in the access to capital. Venture capital and private equity are more appropriate in growth-oriented businesses, particularly in technology-based industries since they provide financial capital, but also strategic advice and managerial skills. Peer-to-peer (P2P) and digital lending are additional fintech lending platforms that have lowered bureaucratic barriers by cutting down on unnecessary paperwork and hastening the process of disbursement, which is particularly helpful with small companies in urgent liquidity requirements. Instead, crowdfunding enables MSMEs to raise financial capital directly through communities or investors, without using intermediaries and extending the participation and democratizing finance. Governments are known to play a key role in making these innovative mechanisms sustainable and reliable, by setting fair rules on fintech, providing tax breaks to entice them and building investor protection frameworks. All these efforts contribute to robust financial systems and more chances of MSMEs operating successfully in competitive markets (Bruton et al., 2015a).

d) **Interest Subsidies:** Interest subsidies are a significant policy tool that aims at alleviating the financial burden on MSMEs to reduce the effective borrowing costs. In this mechanism, the government will be absorbing part of the interest charged on loans enabling MSMEs to obtain credit at cheaper rates. This method is of particular importance when economic stress (the COVID-19 pandemic, inflationary shocks or natural disasters) makes liquidity supplies scarce, and reducing revenues severely limit the capacity of MSMEs to repay loans. To remain efficient and financially viable, however, interest subsidies should be sharply targeted, i.e. targeted to particular industries, company sizes, or less prosperous regions, to ensure that as much impact is achieved as possible with minimum burden on the budgetary books. As an example, the Targeted Longer-Term Refinancing Operations (TLTROs) by the European Central Bank served as a proxy stimulus to MSME lending by encouraging the banks to give credit during the COVID-19 crisis. These specific interventions underscore the value of interest subsidies as a transitional relief program and an analytical instrument to ensure financial sustainability and growth in the inclusive MSME to remain sustainable (Juergensen et al., 2020a)

Limitations of the Study

Despite providing a comprehensive policy-oriented analysis, this study has certain limitations. First, the research relies exclusively on secondary data, which restricts the ability to capture real-time responses and ground-level experiences of MSME owners and stakeholders. Second, as the Union Budget 2025–26 is a recent policy intervention, the study cannot empirically evaluate the actual outcomes or long-term impact of the announced measures. Third, variations in implementation across states and sectors are not empirically examined, which may influence the effectiveness of budgetary provisions. Future research may address these limitations by incorporating primary data, such as surveys or interviews with MSME entrepreneurs, financial institutions, and policymakers, and by conducting longitudinal studies to assess the real-world impact of budgetary reforms on MSME performance and growth.

Conclusion

The Union Budget 2025-26 underscores the government's recognition of MSMEs as the engines of economic dynamism and inclusive growth. By revising classification norms, enhancing credit access through innovative measures such as MSME credit cards, creating targeted funds for startups and first-time entrepreneurs and introducing export-oriented missions, the budget lays down a robust framework for strengthening the competitiveness and resilience of the sector. These measures represent a significant step toward addressing long-standing challenges of credit scarcity, limited scale, and inadequate integration into global value chains.

The conclusions drawn in this study are firmly grounded in existing literature on MSME development and public policy effectiveness. Prior studies have consistently emphasized that access to affordable finance, regulatory simplification and integration into global value chains are decisive factors influencing MSME sustainability and growth (Beck et al., 2010b; Bruton et al., 2015b). The Union Budget 2025-26 reinforces these empirically supported pathways by expanding credit guarantee mechanisms, promoting alternative financing models and introducing export facilitation platforms such as Bharat TradeNet. Unlike earlier policy interventions that largely focused on short-term relief, the present budget reflects a strategic evolution toward long-term structural empowerment, aligning closely with scholarly findings on inclusive industrial growth and financial resilience among MSMEs (Juergensen et al., 2020b).

The findings of this study are consistent with prior empirical and policy-oriented research that highlights access to finance, regulatory simplification and market integration as critical drivers of MSME growth. Earlier studies emphasize the role of credit guarantee schemes and alternative financing mechanisms in reducing credit constraints for small enterprises. The Union Budget 2025-26 builds upon these insights by expanding credit guarantees, introducing MSME credit cards, and promoting fintech-enabled financing, thereby reinforcing established policy recommendations with stronger fiscal backing.

Similarly, previous empirical evidence suggests that MSMEs integrated into global value chains exhibit higher productivity and resilience. The export promotion mission and Bharat TradeNet initiative align with these findings by facilitating international trade participation and reducing non-tariff barriers. Compared to earlier budgets, which largely focused on short-term liquidity support, Budget 2025-26 demonstrates a more structural and forward-looking approach, emphasizing scalability, innovation and global competitiveness. This progression marks a significant advancement in MSME policy design and strengthens the scholarly contribution of the present study by situating it within the continuum of existing empirical research.

From a policy standpoint, the budget reflects a strategic shift from short-term relief to long-term structural empowerment. The emphasis on alternative finance, credit guarantee schemes and interest subsidies demonstrates a clear intent to diversify financial channels while lowering the risks associated with MSME lending. Likewise, initiatives focused on digital adoption, skill-building and cluster-based development in labor-intensive sectors illustrate a holistic approach that goes beyond financial incentives, aiming to create sustainable ecosystems for entrepreneurship.

However, the success of these initiatives will depend on effective implementation, simplified compliance mechanisms and improved awareness among entrepreneurs, particularly in rural and underserved regions. Strengthening institutional capacity, ensuring equitable access to schemes and aligning state-level policies with central reforms will be critical for maximizing impact.

In essence, the budget positions MSMEs not merely as recipients of support but as active contributors to India's transition into a $5 trillion economy. Their empowerment will be vital for achieving broader policy goals such as employment generation, regional balance and global competitiveness. By combining financial inclusion with structural reforms, the Union Budget 2025-26 provides a blueprint for transforming MSMEs into powerful agents of economic transformation and social progress.

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