



## Challenges and Opportunities for Micro, Small and Medium Enterprises

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### Abstract

Micro, small, and medium enterprises (MS-MEs) are vital to the economy, representing over 90% of firms and contributing 50-80% of employment. They play a key role in fostering diversity, innovation, and growth, especially in developing nations, where they account for 18-27% of GDP and 80-98% of informal sector jobs. Strengthening their productivity and resilience is crucial for job creation and social cohesion, particularly during global shocks. Despite extensive research, many MS-MEs face obstacles that hinder sustainable performance and entry into higher-value chains, often due to regulatory frameworks that restrict growth. Addressing these challenges can help them thrive within business ecosystems and enhance national development. This analysis explores the interconnected issues MS-MEs encounter in emerging economies, highlighting the importance of the political economy and institutional factors. Individual case studies illustrate specific challenges, revealing systemic effects that impede growth and resilience. The narrative emphasizes the need for Australia to adapt support mechanisms and balance between universal and customized capital solutions. MS-MEs are increasingly recognized for their contributions to economic development and service diversity. The informal sector holds significant growth potential, aiding nations in achieving policies for broader and more productive economic activities. Thus, countries should assess trade-offs between formal sector expansion and the social benefits of the informal economy, prompting a reevaluation of success metrics in this inclusive sector.

**Keywords:** Micro, small, and medium enterprises (MS-MEs), ecosystems.

**1. Introduction** Micro, small and medium enterprises (MS-MEs) feature prominently in the economic structure of every country. The prevailing state of global economy nevertheless leads varying measures being taken to boost their contribution further. Micro and Small Enterprises (MSEs) also known as Very Small Enterprises, are established within a national economy as important vehicle for job creation, generating income, bolstering import substitution, widening



the export base, promoting balanced regional development and consequently effecting overall economic growth and development. MSEs are everywhere, producing everything and contributing enormously to the socio-economic development of rural and urban areas as well as to the national economy in general. It is encouraging to witness that, there are more focus on the role of MSEs and Mega companies. Small and medium enterprises are often viewed as a catalyst for achieving industrial and economic growth.

Micro, Small and Medium Enterprises are among the most dynamic contributors to economic development. They participate significantly in income generation, employment creation particularly in rural areas, balanced economic and regional development, creation of entrepreneurship opportunities, improvement of women economic participation, provision of raw materials and products to large and mega enterprises. Despite their crucial role in the national economic development, MSEs face number of challenges (Fekadu, 2019). Small businesses, especially micro enterprises, often have limited scope for growth and face various external and internal challenges that hamper their development. In order to boost the contribution of MSEs to the economy and enhance their competitiveness, an array of opportunities is available that enables them to minimize challenges and realize their full potential.

## **2. Conceptual Foundations of Micro, Small and Medium Enterprises**

Micro, small, and medium enterprises (MS-MEs) play a vital role in social and economic development throughout the world. While their specific definitions vary between developed and developing countries, the essence of MS-MEs is universally applicable. These enterprises are essential for job creation and fostering entrepreneurship. Moreover, MS-MEs are considered strategic vehicles for achieving the Sustainable Development Goals because they are closely involved with the social economy, are typically labour-intensive, are more adaptative to the economic and physical environment, and allow population groups with few opportunities to achieve a better life. They often serve as incubators for new ideas and innovation, thus opening new paths for rapid economic development. MS-MEs also contribute to the economy by improving cascading value chains, stimulating business growth and innovation, reducing rural-urban migration, and maintaining social fabric (KOSHY, 2019).

In addition to these broad contributions, MS-MEs create many specific economic and social benefits. They account for a high share of employment and value added in many countries. Their total share in gross domestic product (GDP) can vary between 20 and 50 per cent depending on the type of country, but their resilience is undoubted. In emergencies, MS-MEs react rapidly and reconfigure to create adapted products and services, helping the ongoing provision of goods and services (Fekadu, 2019). The investment by companies in the formal economy in addition to job creation is equally important. When these investments are widely diffused and they engage with institutional support systems, the sustained cohesion of the economy improves on average. Formally registered companies are hesitant to innovate if pervasive informal enterprises operate alongside them, thus reducing the attractiveness of investment project options.



By surveying existing literature on MB-MEs and backbone services, it appears that significant and complex opportunities and challenges stem from their growth and survival.

### **3. Policy and Institutional Context**

Most government policies targeting micro, small and medium enterprises (MS-MEs) focus on stimulating demand rather than addressing key restrictions on their supply of financial and value-added growth. While various degrees of supportive MS-ME policies have been implemented, significant challenges persist. Yet the numerous efforts to develop these policies provide good examples and lessons that may be valuable to other countries. Describing the policy and institutional framework for MS-ME assistance is relevant for several reasons. Policy initiatives react to the issues of highest importance, often based on well-documented surveys. They highlight sector characteristics, shedding light on the economic and social significance of MS-MEs. Finally, constraints to MS-ME operations, growth, and branching into the formal sector can limit the effectiveness of assistance efforts.

Surveying existing policies in a variety of countries can pinpoint common measures that improve the institutional framework for MS-ME assistance. Evaluating coherence and effectiveness of these measures is sensitive to context, yet this examination still yields useful insights. A Classical category of policy support aims to expand MS-ME access to finance. This type of aid may increase some countries' growth potential and employment more than throughout the rest of the economy (Dismas Moyi, 2014). Hence both supply and demand need to adapt to maximise return on MS-ME finance. A prevalent focus on enhancing access to funds may neglect the intermediation of financial structures and institutions, while emphasis on facilitating transactions often overlooks financing arrangements.

### **4. Financial Constraints and Access to Capital**

Access to sufficient capital represents a major obstacle for Micro, Small and Medium Enterprises (MS-MEs). Various types of financing assist firms during different stages of development but are often unavailable due to stringent collateral, income, and solvency requirements. CEPII (2020) connects small firm size to high risk for financiers, while (KAMAU KUNG'U, 2011) points to perceived high risk, high transaction costs, and low returns. Empirical evidence identifies access to finance as the most significant barrier to growth in numerous developing economies (Alemu, 2017). For Ethiopian MS-MEs, major sources of financing include personal savings, family and friends, and microfinance; less than 10% of firms report government support. In Kenya, a 2010 survey indicated high dissatisfaction among micro and small enterprises with access to funding from major financial institutions.

### **5. Business Environment: Regulatory and Taxation Considerations**

Micro and small enterprises, as the backbone of many economies, face numerous challenges across the globe. Serbia is no exception as these enterprises have trouble with demand, financing, property rights, and tax issues. McKinsey analyses of the sector have shown that applying smart regulation and easing tax burdens can protect jobs and encourage growth without compromising





government revenue and public welfare (Aanu Ojeka, 2011). Further investment can also improve knowledge and access to technology that could bolster growth in advance of future demand surges.

## **6. Innovation, Technology Adoption, and Productivity**

Micro, small, and medium enterprises (MS-MEs) are recognized as an important engine for production growth and job creation; accounting for over 60% of employment and around 40% of gross value added in low- and middle-income countries, firms in this sector have been found to be less productive, more constrained in accessing finance and technology, and face higher regulatory barriers than their large counterparts. Innovation and technology adoption play an important role in productivity growth. However, for developing countries, the availability of technological innovation strategies does not suit MS-ME contexts and leaves tech adoption ineffective. In Pakistan, MS-MEs struggle with four key issues of innovation: evaluation of current behind-the-curve; understanding of technological change on the go; development of productive & affordable research and experimentation to lead adaptation; matching upstream and downstream of tech for productivity upgrade. Given these facts, it is hard to imagine that MS-ME could purposefully follow current engineering & tech without thinking of its practical implication to their operation (Ayu Kusumawardhany, 2018).

## **7. Market Access and Value Chains**

The contributions of micro, small and medium enterprises (MS-MEs) to the economy are substantial. They provide key economic functions such as creating job opportunities, generating income for the population, promoting entrepreneurial spirit, producing goods and services, contributing to gross domestic product (GDP), and enhancing local, regional and national development. In Indonesia, 99.99 per cent of business units and 97 per cent of the workforce belong to the MSM-E category, while MSM-Es also contribute 61.5 per cent of Indonesia's gross value added and 57 per cent of GDP (., 2017).

Despite their significant roles in stimulating economic growth, the market access of MSM-Es remains a big question. In rural areas, many MSM-Es rely on backward production techniques, raw materials are not readily available which causes MSM-Es to be unable to meet standards and certification required by buyers. In urban areas, buyers of raw materials or components tend to exploit MSM-Es pricewise and deliver supplies late. The global market requires entrepreneurship based skills. Therefore, to compete from micro and small scale onwards, all of these problems in the chain must be overcome (Ear & Sok, 2015).

## **8. Human Capital and Skills Development**

Human capital and skills development are critical for micro, small and medium-sized enterprises (MS-MEs). Training and upskilling are essential to increase labour productivity and earnings, notably in the context of corporate skills shortages and labour market frictions. Yet when survey-based assessments of skills needs are compared with macroeconomic estimates of the returns to training, a gap emerges (O & Jian Bing, 2019). The type and intensity of training often fail to



address upgrading requirements, a situation exacerbated by relatively lower-quality training supply and mismatched corporate perceptions of the knowledge and skills imparted (Mulyono, 2014). A particular risk associated with the high rate of employee turnover in MS-MEs, which remains above pre-COVID-19 levels, is that trained workers tend to leave immediately after enjoying the training investment made. The lack of an efficient, meritocratic promotion system, borrowing additional career enhancement opportunities from formal training participation, and salary compensation structures that do not attach to training intensity intensify the risk and reinforce the existing training gap.

## **9. resilience and Risk Management**

Micro, small, and medium enterprises (MS-MEs) are especially vulnerable to disruptions from various sources, including climate-related disasters, pandemics, and macroeconomic shocks. The importance of enhancing their resilience lies not only in safeguarding local businesses in a challenging environment, but also in maintaining jobs, boosting customer and supplier confidence, and facilitating longer-term recovery. MS-ME vulnerability increases when they have limited access to finance, operate in low-margin sectors, or lack diversified supply and customer bases, while measures such as business continuity planning, diversification of activities and suppliers, and maintaining cash reserves strengthen resilience (Burch et al., 2022).

Resilience refers to the capacity to absorb external shocks while still functioning at some level. Creating a resilient organisation requires consideration of six factors: leadership, systems and processes, external linkages, people, business models and strategies, and organisation size and structure. Certainly, MS-MEs can and do exhibit resilience. Compared to larger firms, they demonstrate different types of resilience to shocks because of their unique characteristics.

Micro-sized firms (with fewer than 10 employees, often classified as 'very small' by international standards) differ from small and medium-sized enterprises both in the services they provide and in their management. Whether they engage in tending neighbourhood stock markets, offering beauty treatments in the home, or selling surplus agricultural products, they also reflect the limited disposable income of the urban poor.

## **10. Sustainability and Social Responsibility**

In recent years, micro, small, and medium enterprises (MS-MEs) have increasingly prioritized environmental sustainability and various aspects of social responsibility. Such commitments are often formalized in corporate social responsibility policies that address environmental, social, and governance considerations. The motivation is to enhance long-term viability and competitiveness through contributions to the equitable and sustainable development of economies and societies. Even though MS-MEs may have limited capacity to implement sustainability and social responsibility strategies, they have the potential to play a significant role in these areas.

All enterprises, regardless of size, are confronted by the challenges and opportunities presented by climate change. Environmental sustainability encompasses (i) resource efficiency, (ii) waste reduction, (iii) greenhouse gas emissions abatement, and (iv) environmentally friendly products,



processes, and services. The MS-ME sector can contribute substantially to reducing energy and material inputs, lowering waste and emissions, and assisting companies in adopting eco-innovation through second-hand goods, product-as-a-service models, remanufacturing, and repair (Mamingi, 2011).

Support for women's and youth entrepreneurship also figures prominently in a large number of policy initiatives. The specific types of support requested by entrepreneurs in these groups differ from those sought by other MSME owners. MS-MEs directed by women and youth often require additional assistance to enhance the effectiveness of existing measures (Ayalu et al., 2022).

### **11. Comparative Perspectives: Lessons from Regional Experiences**

It is important to examine regional experiences in MSME policies. A comparative perspective sheds light on challenges and opportunities encountered by MSMEs, bringing to the fore transferable lessons and best practices. Different regions tackled similar challenges through diverse policies, yielding varying outcomes. Establishing a vision of policies likely to foster resilience and competitiveness in fragile contexts—a pressing issue—requires analyzing their implementation elsewhere.

Many studies have investigated the growth of MSMEs across Africa, Asia and the Pacific, the Commonwealth of Independent States (CIS), Latin America and the Caribbean, and the Middle East and North Africa. The policy challenges faced, the practices adopted and the evidence gathered in each region frequently overlap (Fekadu, 2019). Even though the geographic coverage of existing evidence is broad, it varies substantially across economies, with the focus often resting on larger firms and sectors (Ear & Sok, 2015). Nevertheless, the available insights are useful to link similar themes, determine patterns at the national and global levels, and highlight the relevance of different regional experiences.

### **12. Policy Implications and Strategic Recommendations**

Access to finance is the most serious challenge confronting MS-MEs across the globe. They perceive severe obstacles in accessing debt finance and other funding sources compared to larger enterprises, and such obstacles limit their ability to acquire fixed assets and invest in productivity-enhancing measures. Empirical estimates suggest that around half of MS-MEs in developing economies engage in only partially satisfactory financing, that around one-fourth lack access to financing or find it prohibitive, and that one-fifth of MS-MEs resort to informal financing (Fekadu Etefa, 2019).

Out of 162 countries where data is available, a broad ranking of the overall condition of financing access assigns 118th position to the Philippines, 133rd to Indonesia, and 162nd (out of 165) to Timor Leste. In the same countries, the microenterprise financing-access situation occupies 78th place, the small-enterprise situation ranks 101st, and the medium-enterprise situation comes in at 158th. The availability of financing and collateral, together with the cost of financing, are key variables influencing financial-access ratings for enterprises. Credit-reference-system coverage for microenterprises stands at only 2.2%, while small enterprises score 14.3% and medium-sized





enterprises attain a coverage of just under 50%, underlining the importance of borrowing in planning investment and conducting business.

### 13. Conclusion

Although micro, small, and medium enterprises (MS-MEs) are classified in diverse ways, gaps remain in the availability of solid definitions from either national or international frameworks. Countries typically introduce their own apertures to demarcate micro, small, and medium enterprises, focusing on parameters like the number of employees, total sales, or total assets. The classification also connects to local contexts: one country's medium-sized firm may mesh, broadly speaking, with another country's small-sized framework. At the United Nations level, the most familiar estimate indicates that MSEs represent 90% of businesses and account for 60–70% of employment worldwide, making them cornerstone actors for achieving productive and inclusive economic growth in many regions (Fekadu Etefa, 2019). Their affordability and minimal-entry costs offer opportunities alike for creating businesses from scratch.

Especially in developing countries, opportunities for entrepreneurship arise directly from the government. Such aspects include but are hardly limited to reduced operational licenses, registration fees, taxes, public-private partnerships (PPPs), tax holidays, and micro credits granted to students to start their own businesses while at schools, colleges, or universities. Need for entrepreneurship also comes from globalization, growing at an exceedingly rapid pace. Therefore, the significance of enhancing capabilities of existing businesses or launching new ones agitates in all corners across the globe. Unemployment that sees a positive correlation upward along with increased population in many regions further demands the fortification of entrepreneurship across the manufacturing and service sectors alike, from food to beautician and amenities.

Constraints inhibiting the growth of MSEs remain commonplace. The most severe side affects accessibility to financial resources, blocking growth at the national and worldwide levels. Stakeholders distinguished at the governmental level include banks, cooperatives, NGOs, and other regulators whose role remains prominent. Certain factors, often beyond one's control, also surround MSEs, such as inflation. Nevertheless, myriad of efforts not only alleviate the financial burden but also solidify growing capabilities across the manufacturing and service sectors.

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