

EGROW Essay Competition 2020-Challenges of COVID-19
COVID-19 AND MSMEs

MSMEs (Micro, Small and Medium Enterprises) and their role in Indian Economy

When it comes to the developing countries, MSMEs are said to be the backbone of the economy as it provides huge employment and promotes economic development through its wider reach and innovative ideas for product development. MSMEs contribute around 30% of India's GDP and contribute 42.38% of total exports (*PIB, for year 2012-13*). MSMEs have provided plenty of employment opportunities in urban and rural areas, covering over a range of skill sets. It has helped in improving the livelihood of semi-skilled labourers, women, marginalized sections of society and differently abled people. This sector requires very less capital, which means many businesses can get registered and take advantage of special government policies. Government has always prioritized infrastructural development, dispersion of financial resources and technological advancement to support the employment provided by MSMEs. Some of the policy initiatives by government are (*from the website of ministry of Micro, Small and Medium Enterprises*):

- **Micro and Small Enterprises Cluster Development**
The scheme targets for enhancing productivity, competitiveness and capacity building of MSMEs. It provides financial assistance for establishment of Common Facility Centers (CFCs) for testing, training centers, R&D, Effluent treatment, upgrade infrastructure facilities, etc.
- **Financial Support to MSMEs in ZED (Zero Defect & Zero Effect)**
The purpose of this scheme is to inculcate ZED practices in manufacturing processes, ensure continuous improvement and support the Make in India initiative. After ZED assessment, MSMEs can reduce wastages, increase productivity, expand their market IPOs, develop new products and processes, etc.
- **International Cooperation Scheme**
This scheme covers visits of MSME delegations to other countries in international exhibitions/trade fairs, conferences/summits/workshops. It also includes participation of MSME delegation in international exhibitions and holding/organizing mega international exhibitions or fair and international Joint Committee Meetings/Joint Working Group Meetings/Government to Government bilateral meetings with other countries in India by the ministry of MSME or organizations under it.

MSME sector provides the stability of employment and growth. They are supplying their goods and services to the Multinational corporations that mean they are competitive and desirable in the markets. They are playing an important role of promoting inclusive growth by employing people from various backgrounds and regions with different capabilities. MSMEs are instrumental in carrying out government initiatives like Make in India and it is actively contributing to the share of Indian goods in international markets.

COVID-19 (Coronavirus Disease 2019) and Economic Crisis

With the virus spreading across the globe, we are witnessing multifaceted crises glooming over the nations. We can see the situation of health emergency and occurrence of financial crisis is intensifying as the disease spread is broadening. The virus can be contained only through practicing social distancing, maintenance of

hygiene and conducting testing nationwide for its earlier detection. As long as no vaccine is available we have to follow the above rules for containment of virus strictly.

Due to the lockdown in many countries for an indefinite period of time, economies are suffering badly. The employees are working from home and those who have to go out for work are also sitting at their homes, schools and colleges are closed, countries have closed their borders, hotels and restaurants are shut and production of goods and services is halted or delayed. If the situation continues for a longer period of time we can expect global recession coming anytime soon. In fact the United States of America has reported 16.8 million Americans filing for unemployment and it is likely to hit 14.7%, the highest level since 1940. Currently every nation around the world is dealing in its own capacity and the priority is to save lives and restore normalcy. From the prevailing scenario we can see that there is a tradeoff between saving lives and letting economic activities run as usual. There is a high degree of uncertain scenario, resulting in improper planning and inappropriate cost and benefit analysis to make future predictions. The virus is affecting every country around the world but differently because of varying resources, technological advancement, degree of reliance on international trade and economic stability. Governments and international organizations are working rigorously on measures to be taken before it does permanent damage to lives and livelihoods.

- **COVID-19 and India's MSME sector**

- *The COVID-19 Pandemic is the "greatest emergency since Indian Independence," according to the former Reserve Bank of India Governor and economist Raghuram Rajan.*
It is rightly mentioned by economist *Raghuram Rajan* that India is witnessing the greatest emergency since its Independence. Indian government is taking strict actions to deal with the economic crises brought in by the pandemic caused due to COVID-19. The country is under lockdown and is ordered to maintain social distancing till 14th April 2019 and is expected to extend for a longer period. The biggest concern is India's population residing in '*Bottom of the pyramid*' (*CK Prahalad, 2004*). Among them are the people who work as daily wagers and belong to low income groups, some of them are part of the low skill workforce working in MSMEs. This sector needs an urgent financial stimulus to help the businesses and the workers.
- Also, MSMEs contribute significantly in the total exports but, due to the pandemic world demand has contracted. USA and Europe, the major importers of Indian goods are severely hit by the virus and that adds to the tension in the MSME sector by reduction in their overseas demand. Countries around the world are dispersing their funds to the priority sector goods and services which will help in coping up with the virus. It's not clear when we can expect the demand from the rest of the world, so this issue will remain a big concern for small and medium businesses in India.
- Over 97% of MSMEs can be classified as micro firms (with an investment in plant and machinery less than ₹25 lakh), and 94% are unregistered with the government. Socially vulnerable groups operate two thirds of the MSMEs and 20% of them are operated by women. MSMEs are the source of livelihood for the weakest sections of the society. Due to financial instability, social insecurities, workers from unorganized sectors depend on the government assistance for sustaining their lives. It calls for the government to track these small workers and help them survive through direct cash transfers and free *Ration* distribution.
- MSMEs are highly dependent on cash flows and due to the pandemic there is non-availability of raw materials, restricted movement of workers and non-accessibility to the infrastructure and transport.

This lack of accessibility of essential resources will disrupt the operations of various businesses. The cash outflow is resulted due to expenditure on salaries, rent payments, insurance and loan repayments. The policymakers are dealing with the tough task of containment of the present health emergency and framing policies to minimizing the adverse effects of the pandemic on the economy. MSMEs are the most vulnerable section of the Indian economy and need the support so that the stakeholders like entrepreneurs, their employees and their suppliers can survive. Shortage or nonexistence of demand and supply is one of the major issues MSMEs are going to witness due to deepening of economic crises on the verge of COVID-19.

- Human lives are more important than anything else, and everyone has the right to access health facilities without any discrimination especially in the time of global health crisis. This takes us to the point of safety of the workers. The workers working in the MSMEs should be given proper equipment and sanitary facilities to make them feel safe. Taking care of workers is the moral responsibility of the employer and it's his/her duty to make proper arrangements for any medical emergency. Apart from these measures, financial support should be provided, so that they can take care of their families and can help in containment of the pandemic.

Policy response for supporting MSMEs around the world (IMF)

There are various Fiscal and Monetary measures taken by the countries around the world to keep the MSME sector sustainable. These policies will support MSMEs financially and economically so that even if the production activities are halted, the businesses don't go bankrupt. MSMEs are said to be the catalyst for socio economic transformation of the country. By employing people from urban and rural areas, the sector is critical for providing employment and discouraging rural-urban migration in developing countries by providing better job opportunities. In such difficult times special support has to be provided by the governments so that those employed in the sector can be retained. Some of the policies taken by countries around the globe are:

Fiscal Policies

(1) Liquidity support:

In order to provide adequate cash flows to MSMEs and businesses, the most widely implemented policy is deferment of tax payments and accelerated refund of tax credit. It will help in the availability of working capital with enterprises and they can make necessary expenditures on operational activities.

(2) Direct financial support:

For affected microenterprises, liberal professions, and independent workers direct assistance from the government can be very beneficial. It includes reimbursements or direct payments for the eligible expenditures incurred by MSMEs and other businesses.

(3) Postponement of rent and utility payments:

The priority in the current scenario is to keep the businesses, specifically MSMEs operational so that employment and output can be maintained after things get back to normalcy. As there are restrictions on the production activities, supply has been disrupted. In that case there is no way or it is very restrictive for a business to operate. So, the postponement of rent and utility payments comes as a big relief and reduces the pressure on already distressed microenterprises and SMEs.

(4) Corona Response Investment Initiative in the EU budget :

Out of 0.3% of its 2019 GDP, European Union (27) has planned to make public investment for hospitals, SMEs, labor markets and stressed regions. This fiscal stimulus can be used to meet the liquidity requirements, direct financial support, tax exemptions, investment in public health and other policies which can revive the growth of the economy.

Apart from the above mentioned fiscal policy measures; there are many other steps that are taken to help in overcoming the pandemic. A direct measure is the expansion of the coverage of unemployment benefits until the lockdown. It will help those who became unemployed due to the practice of social distancing, like daily wagers. Higher Infrastructure investment along with improvements of the public health management system will accelerate the process of dealing with the crises.

Monetary Policies

(1) Delay of loan payments and extension of loan tenors:

For MSMEs, it is right to say that “Cash is the king”. In line with the objective of fiscal policy, through monetary policy also, the government is trying to provide the sector as much liquidity as possible. Delay of loan payment will ensure that the funds are used in a productive manner and can be used for meeting the urgent expenses by the MSMEs.

(2) Credit support measures for eligible SMEs:

It includes support in the form of assurance of guarantee, extension of the credit for the benefit of the SMEs. This measure will make funds easily available for the eligible enterprises to maintain its financial stability.

(3) Tolerance for higher NPLs (non-performing loans):

China and many other countries have made provision for tolerance of higher NPLs or NPAs (non-performing assets) for loans by epidemic-hit sectors and SMEs. Presently, we are experiencing a supply side shock, where the production activities has come to a halt, businesses will not be in a position to repay their loans and that will result in increasing NPLs in the Balance sheet of the banks. For the epidemic-hit sectors, this provision will bring a sigh of relief.

(4) Low interest loans with 100 percent government guarantee:

This is the most widely used policy to encourage the availability of funds with the MSMEs. The cash then can be put to use for making the payments of salary, which is of a primary need. These measures can help the government to reach the person standing at the end of the line, as through these payments the labourers working in the MSMEs can enjoy financial security.

(5) Principal moratoriums for affected SMEs:

Principal moratorium implies the suspension of principal loan amounts. The enterprises can take the benefit of the policy to defer their principal loan amount payment. As per this policy only the principal amount will be postponed and the interest will be charged in that deferred period. MSMEs can do the cost-benefit analysis for the implication of the policy. They can opt for the policy if it's urgent and there is a shortage of cash to carry on the operational activities.

(6) Lowering bank's reserve requirements:

By lowering the reserve requirements by the banks, more loanable funds will be available in the economy. These funds will be used by various sectors of the economy and will help in reviving the economy by improving the aggregate demand and supply.

Other monetary policy includes, “ECB (European Central Bank) Banking Supervision”-that asked the banks to not pay the dividends for the financial years 2019 and 2020 or buy back shares during COVID-19 pandemic. So that the conserved capital is used to support households, small businesses and corporate borrowers and/or to absorb losses on existing exposures to such borrowers.

Policy measures taken by India:

MSMEs are among the worst hit sectors of the economy due to the emergency like situation caused due to Coronavirus. Micro, Small and Medium Enterprises (MSMEs) employs around 50% of industrial workers. The high concentration of employment in MSMEs calls for an urgent fiscal stimulus to safeguard the backbone of Indian economy. Not every business and individual can afford this lockdown; sectors like MSMEs are unable to carry their operations anymore because they don't have accessibility to raw materials, transportation facilities and enough finance. Key policy measures taken up by the government, RBI and other regulatory institutions are given below:

- Reserve Bank of India (RBI) has taken several steps to increase the availability of loanable funds with the banking and non-banking sector. The purpose is to facilitate economic activities so that there won't be deficiency of liquidity in goods and financial markets. The repo and reverse repo rates have been reduced by 75 and 90 basis points to 4.4 and 4.0 percent, respectively, Cash Reserve Ratio (CRR) has been reduced by 100 basis points, deferred interest payment on working capital facilities without an asset classification downgrade and three-month moratorium on loan repayments. RBI has also provided regulatory forbearance on asset classification of loans to MSMEs; this will restrain banks from taking any actions against MSMEs for noncompliance in repayment of loan amounts. These regulatory measures will promote credit flows to the retail and Micro, Small and Medium Enterprises (MSMEs) and will ensure easy accessibility to working capital. Working capital works as blood for any organization, it is essential for making payments to the workers, suppliers and other necessary expenses.
- Small Industries Development Bank of India (SIDBI) is supporting MSMEs manufacturing products or providing services related to fighting the pandemic caused due to Coronavirus with two schemes:
 - SAFE Scheme: The SIDBI Assistance to facilitate emergency response against COVID-19.
 - SAFE Plus Scheme: Special scheme to provide emergency working capital under government order.
- Under these schemes loans are extended to MSMEs at a low rate of interest of 5% within 48 hours.

What are the other measures that can shield MSMEs from the crises?

According to the Economic Census data, over 95% of firms employed less than five workers and 94% were not registered with the government. Additionally, more than 81% of MSMEs are self-financed with only around 7% borrowing from formal institutions and government sources (Economics census, 2013).

[Taken from the source:

<https://www.hindustantimes.com/analysis/msmes-is-critical-in-times-of-covid-19/story-6Juiu9zs4jKUdkHLobT6WJ.html>]

As the data shows that most of the MSMEs employing fewer than five workers are not registered with the government. This will restrict them from taking benefits of government policies like reduced rate of interest, moratorium on loan repayments, relaxation for non-payment of loans, etc. This implies that the policies won't rescue the hardest hit sector and its stakeholders. Additional measures India can take:

- Most of the monetary policies implemented by India will push the demand, whereas the pandemic has worsened mostly on the supply side of the economy. It will do very less for increasing production activities and will not do enough for a much needed push to the aggregate supply. The policies should be helping the production units with the special care given to the unorganized sector. Historically whenever an economy experienced an unforeseen event like demonetization and GST, small businesses are the one to feel the heat instantly because they don't have the capacity to mitigate the losses caused due to uncertainty. MSMEs have a major contribution in total output that means keeping that sector stable in hard times is very important for sustaining the economy.
 - Subsidies should be given to small production units and MSMEs. It can be done by subsidizing intermediate goods, so that the cost burden is minimized. The price will be shared by the government and in a way this will result in direct financial help at a time when MSMEs are running out of cash.
 - Tax benefits in the form of tax waiver for production of essential goods and services should be given. This will incentivize the producers and slowly and gradually they can carry on with the production.
- China has started balanced reopening of the businesses. India should also make some mechanism where some of the businesses can start operating so that supply of goods and services is revived. In case of non-operability for a long time, we can face severe consequences like rise in inflation and unemployment rates. This can be devastating for Indian economy because our major chunk of population is poor and they cannot sustain if the crises escalate further. For carrying on with the production some policies which can be implemented are:
 - E- Marketplace should be made accessible to MSMEs, where they can connect with their buyers and sellers. For that, the government should have the records of MSMEs set up in a particular region. This might not help all the businesses because of the dominance of unorganized sectors in India, but the government can initiate and incentivize the businesses for making them registered. Also, the policies and incentives should be communicated to the smallest enterprise so that the purpose of benefiting the marginal workers is fulfilled. In the whole process political willingness is must where the project is carried to the business in a Mission mode.
 - To expand the reach of MSMEs, the government can help with online marketing. This will expand the reach of the goods and services produced by them. It will also help MSMEs in the long run for their growth and development. In fact MSMEs carry on their activities in a traditional way and broad market reach through promotions can help MSMEs to modernize their way of doing business.
- Government should also come to the rescue of workers working in unorganized sectors. MSMEs have a huge number of unregistered businesses, some are operating in rural areas as well. Organized MSMEs are receiving different types of policy support from the government but unfortunately these policies are unable to improve the lives and livelihoods of people working in unorganized sectors. This issue can be addressed through direct benefit transfer of aids in their Jan-Dhan accounts by

identifying them. This responsibility can be given to the local administrators, who are aware of the ground realities and will ensure effective implementation of such initiatives.

- Confederation of Indian Industry (CII) has suggested deferment of Equated Monthly Installments and interest rate on working capital to maintain the liquidity in MSME sector. It recommended creation of a corpus by the government to help out MSMEs by providing them with cash to pay wages and salaries. Period of non-performing assets can be extended to 150 days from the present 90 days, if required banks can help on SOS basis to overcome liquidity crunch.

What can we learn?

There will always be these “Black Swan” (Nassim Nicholas Taleb, 2007) events which we can never know about. We will know about them fully once they get over. Such an event is COVID-19.

In the course of time, when we actually encounter such events, we never know what we will gain or lose at the end of it. Uncertainty is a part of life and it can come in many forms. The best we can do is to keep a 360 degree view of what’s happening around us and try not to repeat the mistakes made in the past. Like many other events happened in our history, this too shall pass. But the question is what we will learn?

Lessons MSMEs can learn:

- As discussed above, the major issue with MSMEs during uncertain times is the deficiency of cash. Due to the small size and weak financial position of MSMEs, they are highly dependent on cash. It can be improved if financial inclusion of its forward and backward linkages is achieved. Then MSMEs can diversify their mode of doing business by using E-Banking more often and that will inspire related businesses to follow the same path, so it will work as a tool of financial advancement of the whole sector. They should innovate the ways of doing business in accordance with changing technologies. The major requirement is providing financial literacy to their employees and workers. Government should focus more on training and organizing workshops to enhance skills so that MSMEs can be competitive enough to survive in domestic as well as international markets.
- MSMEs struggle to get capital, mostly working capital due to the high cost of capital. Working capital is a very essential part of financing day to day transactions and it can make a huge difference in costing of a business. If working capital is managed by the funds received from retailers and traders with whom the business deals, then the cost of capital required to borrow funds can be saved. Special funds with low interest rates are needed to be allocated for the purpose of fulfilling working capital requirements in selected MSMEs. Because of non-availability of funds, MSMEs are dependent on the informal sector with higher cost. By making the funds easily available, MSMEs can concentrate on their production processes and can plan to expand their operations.
- MSMEs are not working at their full potential; they lack well trained staff and management skills. Even if you have access to all the resources but management skills help you to get things done effectively and efficiently. This crisis like situation can be handled in a better way if things are planned. But planning requires analytical skills, proper coordination, maintenance of records, technical knowhow and leader’s guidance. MSMEs don’t have a good record for their management and that reflects in its unpreparedness for any dealing with some non-conventional situations. MSMEs can now assess where they are lacking and make proper planning systems to shield their businesses in uncertain times.

Conclusion:

The importance of MSMEs in India can be assessed through its contributions in employment generation, inclusive growth and share in exports. Still MSMEs don't have access to easy credit, robust infrastructure and technical skills. These factors contribute most when the economy experiences a negative shock or any unforeseen event. We can shield our economy's major employment generating sector by not only making policies but ensuring their proper implementation.

The biggest challenge the sector is facing is inefficient management practices. MSMEs can become cost effective and profitable by working as per management principles. Management is not considered an important activity and as a result lacks managerial skills.

Another area of improvement is training and skills development programmes. The ways of training should be highly localized, that is depending on where they live, what their cultural, traditional and social values are and what their educational orientation is. This can be done by the respective state governments with the support from local bodies and targeted businesses.

We have to be hopeful yet realistic for what the future brings and remember that *there are opportunities out there, even in miseries*. We all have to stand together to fight the health crises and economic battle. We will learn and grow with time, either good or bad.

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I hereby declare that the ideas are original and not plagiarized.

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