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IMPACT OF COVID-19 ON MSME'S AND WAY FORWARD

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ABSTRACT

COVID-19 has posed financial risks for MSME's, particularly affecting their cash flows. It has caused major disruptions in the economy and even though the government has provided relief packages and extended their loan moratoriums till March 2021, it might not be enough for MSME's facing liquidity crunch in view of the lowered demand. Although the government has taken steps for making credit available to these enterprises, compliance issues related to taxation and labour still remain. Further, Moody's ratings have shown improvement in loan collections but warned of performance risks, at least for the next 6 to 12 months. India's sentiment index for SME's, CriSidEx has shown an improvement but the score still remains weak. This is a unique opportunity for MSME's to build long-term resilience.

Keywords: MSME, COVID, growth

1. Introduction

The Covid-19 pandemic has had an adverse impact on all parts of the economy. It has disrupted worldwide supply chains and brought international trade to a virtual standstill. In this context, it is important to analyze the impact of the lockdown on one of the most important sectors of our economy: MSME's. MSME's form a large part of the country's exports. They generate employment in both the formal and informal sector. They support a large section of the lower and middle class. Their sale or closure is likely to widen the economic gap. This retrogression is likely to sow discontent among small businesses and lead to socio-political strife further weakening investor confidence.

According to a survey, MSME's faced many hurdles while trying to avail the benefits of government schemes (LocalCircles' annual survey, 2021). One of the main challenges was that these benefits were only available to MSME's showing existing debt on their books. The main problem was funding, followed by lack of growth and bureaucratic inefficiencies. Only 21 percent of the businesses said they had benefitted from the Centre's schemes. Cash flow is another major problem, with only 31 percent saying they have over 3 months of cash.

The MSME's have faced stagnation in terms of revenue growth. This is reflected in FICCI's recommendations for the government to provide payment support programs to help them retain workers and pay wages. The other recommendations also point towards a severe cash crunch in the sector. The body has recommended the release of all pending payment and tax refunds from ministries and agencies immediately. Other recommendations were interest free and collateral free loans to cover fixed costs and more government orders for the sector.

As a result of the pandemic, many of these businesses are in danger of being classified as NPA's. The conditions created by the lockdown were not conducive to the sustainability of many of these enterprises. The NPA problem is one of the worst problems threatening the stability of the banking sector. This is a crucial time for the MSME's because if they are unable to survive, they will add to the burden of bad loans and the banks will have to write them off. Thus, it becomes crucial for the government to support them during this time, by measures like increasing the moratorium on payments or by waiving interest on interest, steps the government has taken.

Due to migration, many businesses faced a manpower crunch. Some were unable to pay the wages and had to let their employees go or reduce hiring. Overall, this has led to an increase in unemployment. Although the government has taken steps for making credit available to these enterprises, compliance issues related to taxation and labour still remain. Further, Moody's ratings have shown improvement in loan collections but warned of performance risks, at least for the next 6 to 12 months. India's sentiment index for SME's, CriSidEx has shown an improvement but the score still

remains weak. This is a unique opportunity for MSME's to build long-term resilience. The upcoming budget for 2021-22 will be a key policy instrument in enabling medium-term growth of the MSME sector and the economy.

2. Impact of COVID - 19

The pandemic has lowered demand, disrupted supply chains and most importantly, restricted or completely banned public gatherings. Neither of these things have been conducive for the growth of business. The impact on small business has been four-fold: revenue growth has declined, difficulty in raising money in debt markets, manpower reduction and supply chain breakdown has led to decline in exports.

Firstly, the disruption in industrial activities has led to a severe revenue loss for most states. Odisha has reported a revenue loss of Rs 10,000 -15,000 crore and Punjab Rs 20,000 crore. 21 states collectively incurred a loss of Rs. 97,100 crore in just one month (Ind-Ra). The halt in production and disruption of demand has translated to zero cash flow with businesses. Their revenue generation went on hold because of the lockdown. As a result, businesses are finding it hard to clear employee salaries, taxes, rent and other expenses. Many are on the verge of shutting down.

The government launched a Rupees 3 lakh crore emergency credit facility under Emergency Credit Line Guarantee Scheme (ECLGS). This was aimed at helping borrowers like MSME's meet their working capital requirement. However, it was found that many MSME's faced hurdles in availing the benefits of this scheme. The main obstruction was that it was restricted to MSME's that are already under debt (LocalCircles' annual survey, 2021). The MSME's which were able to avail the loans were able to meet their liquidity problems without finding any solution for their long term concerns regarding business volume. Lower than average utilisation rate for smaller borrowers and inequitable distribution of funds are some other concerns.

Thirdly, there was an impact on jobs. Many businesses had to cut employment due to dismal business performance. 14.7 million jobs were lost because of the pandemic (CMIE). India's workforce is also ageing thus the workforce has declined qualitatively as well.

Fourthly, the partial lockdown in certain areas and states, has made it difficult to maintain supply chain levels. Even if MSME's are allowed to open, their business depends on a variety of other ancillary industries that are integral to the entire operation. As of August 1, only 1 in 4 MSME's, were using even half of their installed capacity (Kishore, 2020).

3. Government's Response

3.1 Change in Definition

In accordance with the provision of Micro, Small & Medium Enterprises Development (MSMED) Act, 2006 the Micro, Small and Medium Enterprises (MSME) are classified as below:

- i. a micro enterprise, where the investment in plant and machinery or equipment does not exceed one crore rupees and turnover does not exceed five crore rupees;
- ii. a small enterprise, where the investment in plant and machinery or equipment does not exceed ten crore rupees and turnover does not exceed fifty crore rupees; and
- iii. a medium enterprise, where the investment in plant and machinery or equipment does not exceed fifty crore rupees and turnover does not exceed two hundred and fifty crore rupees.

The new classification has come into effect from 1st July, 2020. The earlier criterion of classification of MSMEs under MSMED Act, 2006 was based on investment in plant and machinery / equipment. It was different for manufacturing and services units. It was also very low in terms of financial limits. Since then, the economy has undergone significant changes. a revision in MSME criteria of classification was announced in the Aatmnirbhar Bharat package on 13th May, 2020. This has been done in order to be realistic with time and to establish an objective system of classification and to provide ease of doing business (Ministry of Micro, Small and Medium Enterprises, 2021, p. 2).

The artificial difference between manufacturing and services sector has been removed. The government also decided to exclude the export turnover in the limits of turnover for any category of MSME units. All of these steps are expected to help the MSME's grow, provide ease of doing business, encourage investment and create more jobs in the sector.

3.2 Financial Support

The government announced a 3 Lakh Crore Emergency Credit Line Guarantee Scheme to provide emergency credit to MSME's. Under this scheme, 2.46 Lakh crore has already been sanctioned. However, the MSME sector is so large that this is unlikely to make a significant impact on the availability of finance to the sector. These initiative are more useful as moral support. According to a survey by SME Chamber of India, " only 45 percent of the labour is back at their jobs, the rest are still in their villages even one year after the lockdown was announced – most of those are in sectors such as infrastructure, real estate, and logistics."

With the arrival of the severe second wave of the Coronavirus, MFI's have seen their asset quality deteriorate. Smaller MFI's have faced difficulty in raising credit. The central bank has taken a positive step to ease liquidity pressures by allowing

Priority sector lending (PSL) classification for loans extended by Small Finance Banks (SFBs) to Microfinance Institutions (MFIs) for onward lending. As per existing guidelines, these loans did not qualify under PSL norms. The above dispensation is valid till March 31, 2022 for fresh credit extended to eligible MFIs (gross loan portfolio upto Rs.500 crore) and will be permitted upto 10% of the bank PSL portfolio as on March 31, 2021. (CARE Ratings, 2021)

3.3 Hand-holding Schemes by Government

Directions have been issued at the Secretary level to ensure timely release of MSME payments. No global procurement for orders up to 200 crores will be carried out. RBI has extended the moratorium on loans by three months. An ICT based online portal called CHAMPIONS has been launched by the ministry of MSME.

UdyogAadhar Memorandum Scheme simplified procedure for registration of MSME's by reducing the number of forms to be filled to two and making the process completely free and online. This has removed the hassle of paperwork and allowed entrepreneurs to register through their Aadhar card.

The government also provides incentive to new and innovative ideas by providing financial support to Host Institutions exploring and implementing them. 75-85 per cent of the project cost can be borne by the government, upto INR 8 Lakh. An MSME company can be eligible if it comes up with an innovative product or service

Prime Minister's Employment Generation Programme (PMEGP) Scheme has encouraged women entrepreneurs to set up projects. Under this, women are considered under Special Category and are entitled to 25 per cent to 35 per cent subsidy depending on the location.

The Ministry of MSME website also has a grievance monitoring system for people to lodge their complaints, suggestions and queries relating to the sector. The status of one's complaint can be checked online as it keeps updating the status.

4. Challenges Ahead

Loan portfolios of lending institutions like non-banking financial institutions (NBFC) and micro-finance institutions (MFI) might see significantly higher loan delinquencies as the Coronavirus second and third waves hit the country. According to CARES rating, "The outstanding credit to medium enterprises has witnessed a sharp growth of almost 29% in FY21 and has driven the overall growth in credit to the MSME segment." The impact would be visible "in the urban and semi-urban portfolios before spreading to the rural portfolios," the credit rating agency said.

The US federal reserve's Chairman has warned of extended economic weakness in the US which has led to weakness in global markets as well. Although the Finance Minister doled out measures worth Rs. 5.94 trillion for a slew of sectors, the sentiment remains weak. The future of the sector depends crucially on the way the epidemic is contained in the following year.

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