India's economic recovery after the COVID-19 lockdown needs policy, financial, technological and behavioural interventions to solve urgent problems as well as build the foundation to square the trinity of jobs, growth and sustainability.

Image: iStock

3. Economy-wide measures

A crisis of the scale of the COVID-19 pandemic presents infinite problems across geographies, communities, industries, administrative agencies, and support services in a country as vast, diverse and densely populated as India. We have curated a set of economy-wide issues that need policy and structural interventions to solve urgent problems and/or create an informed, integrated, and self-reliant yet globally agile economic system that can withstand future shocks.

In this section, we look at interventions to:

- Plan India's fiscal and monetary policy response to the COVID-19 pandemic
  - Assess the economic impact in the face of data limitations
  - Manage the unprecedented migration
  - Chart a strategic road to recovery
- Support small businesses
  - Identify micro, small and medium enterprises and their workers
  - Develop a vulnerability assessment framework of MSME sectors
  - Increase capacity of the *SAMADHAAN* system to expeditiously clear government dues
  - Improve creditworthiness of small businesses
- Increase capacity of the National Company Law Tribunal (NCLT) to efficiently manage cases
- Evaluate the impact on Indian trade

3.1 Plan India's fiscal and monetary policy response to the COVID-19 pandemic

Image: iStock

India's fiscal and monetary policy response to the COVID-19 pandemic has many dimensions, and depends largely on the planning horizon:

- **Immediate**, to address relief measures to cushion the nationwide lockdown, and
- **Medium to long-term**, to deal with the socioeconomic aftereffects of the pandemic in terms of public healthcare, priorities for state expenditure, and regulations to operate businesses and establishments in the near future.

The road to recovery is critically dependent on the exit strategies from the lockdown, which is rightly aimed at containing the outbreak and saving lives but has major consequences on livelihoods. The emerging situation for public finance post-lockdown has two main areas:

- A fiscal stimulus to cushion the adverse impact on firms, self-owned enterprises, and migrant workers, and
- Economic recovery in the medium term with stability of financial institutions, market prices and output growth.

India's three major challenges are to:

- Assess the economic impact in the face of data limitations
- Manage the unprecedented migration
- Chart the strategic road to recovery

3.1.1 Assess the economic impact in the face of data limitations

PROBLEM

It is challenging to conduct an impact assessment in India because most national aggregates such as gross domestic product (GDP) / gross value added (GVA) estimates by sectors, consumption expenditure, etc. come with a considerable time lag. Two high-frequency indicators — monthly industrial production and quarterly estimates of urban employment — can, at most, provide a snapshot of the economic situation.

The story of the large unorganised sector is much more complex. Surveys of informal manufacturing and service sector enterprises are available with a time lag of 3-4 years and, thus, do not provide updated information during periods of crisis. The other limitation of national aggregates is that they offer only a two-point comparability (or change) and have limited ability to capture economic shocks in real time or with a higher frequency. In the current situation of limited and scattered information, policy response would require good diagnostics before any remedial action is taken.

SOLUTION

As the first step, quick (thin sample) surveys must concentrate in three areas:

- **Rural Labour Enquiry[27]:** The Labour Bureau provides estimates of rural employment, wages, and occupations, but regular surveys are not being conducted for a variety of reasons, which hinders assessments of socioeconomic conditions of rural and agricultural households. A quick survey can provide leads into the emerging scenario on daily employment, wages, and in-migration.
- **Consumption expenditure:** Household consumption expenditure is a prime macro-indicator to assess the demand side of the economy, the underlying growth trends, and the overall economic well-being. In the absence of recent data, a thin sample quarterly survey would best serve to understand the current and future demand trends of households.
- **Factory/establishment survey:** This is critical to assess employment conditions in organised as well as unorganised sectors. A quick survey of registered factories and informal self-owned enterprises could estimate the extent of job loss and likelihood of closure.

FISCAL

Conducting surveys is both an administrative and an economic decision. Nationwide surveys involve significant costs and personnel, and are conducted by the Ministry of Statistics and Programme Implementation (MoSPI) with substantial state funding.

TIMELINE

These surveys are an immediate requirement. However, given the nationwide lockdown and exodus of migrant workers to their home states, the survey results should be aimed for in the first or second quarter of 2021. This would provide policymakers a clearer picture of the state of household consumption, rural distress, and industrial units.

IMPLEMENTERS

The consumption expenditure and establishment surveys can be conducted by the National Statistical Office (NSO). A quick round of Annual Survey of Industries can also be convened. Surveys on wages and rural workers can be done by the Labour Bureau.

JOBS

This initiative to gather information has no direct impact on jobs.

GROWTH

A clear understanding of the socioeconomic impact of the lockdown will allow more cogent policymaking, and help plan and deploy effective relief and recovery measures.

SUSTAINABILITY

This initiative has no direct impact on sustainability.

3.1.2 Manage the unprecedented migration

PROBLEM	One of the most unanticipated consequences of the nationwide lockdown is the mass migration of migrant daily or casual workers. This will emerge as one the central economic challenges as it has the potential to cascade into several other problems. The immediate consequence is loss of wage work for at least a quarter before any industrial activity can restart. Also, even after the lockdown is lifted, there could be a considerable delay in restarting industrial and construction activity as the labour movement back to work sites remains uncertain.
SOLUTION	Tackling the migration labour problem is partly economic and partly administrative. The respective states would have to scale up testing and medical facilities to contain the spread of the pandemic, and immediately provide a one-time financial relief that can partly offset the wage loss. However, providing such relief will require identification and a direct benefit scheme. Two policy options would be most effective in such a situation: - **A one-time cash transfer**, and - **Provision of basic food supplies per person**, from the Public Distribution System (PDS) for three months, before some industrial activity restarts.
FISCAL	Distributing money through DBT and food via the PDS will adversely impact the finances of state governments, especially in the states of Uttar Pradesh, Bihar, Jharkhand, and West Bengal as they are home to almost all migrant workers. However, this fiscal measure is an essential relief intervention to prevent millions of workers and their families from slipping into further distress.
TIMELINE	The measure must be deployed on priority as it involves the livelihood of workers.
IMPLEMENTERS	Central and state governments will have to coordinate to deliver comprehensive relief: each state government can provide a one-time DBT, while food and other financial assistance can be provided under centrally sponsored schemes.
JOBS	There is no estimate yet of the number of jobs lost due to the outward migration of the informal workforce from their places of work.
GROWTH	India's estimated 450 million informal workers comprise 90 per cent of its workforce, with 5-10 million workers added annually[28]. Lifting this despondent migrant workforce back on their feet is crucial to ensuring the country's economic stability.
SUSTAINABILITY	This initiative has no direct impact on sustainability.
TRADE-OFF	This measure will put a huge financial burden on central as well as state governments, more so since revenue income from economic activities and taxes are severely compromised due to the ongoing lockdown. However, this relief measure must be undertaken to ensure the survival and wellbeing of the country's economically weaker population who have lost all sources of livelihood.

3.1.3 Chart a strategic road to recovery

PROBLEM

Formulating a post-pandemic recovery map for India requires:

- assessing the immediate distress to daily / casual workers in sectors that have taken the maximum brunt of the lockdown,
- preventing the closure of firms and establishments in the near future, and
- revisiting the constraints on state finances.

Formulating the recovery roadmap will be an iterative process as the interventions are deployed and more data come to the fore, thus allowing a clearer understanding of the on-ground scenarios and, consequently, better targeting of the measures.

The Central government's much-needed, major economic package of INR 20 lakh crore (USD 263.5 billion) requires some more clarification:

- What measures will contribute to the recovery package?
- How will those contributions be funded?
- How will the resources be spent?

SOLUTION

The immediate policy concern is to offset the financial losses due to the lockdown and collapse of businesses (supply chains).

Post-lockdown, major production units – automobile, chemicals, garments, plastics, etc. may face manpower and demand shortages. The policy must ensure that these industrial units operate at their optimal capacity at the earliest.

Most of the supply chain vendors are service sector MSMEs (labour, technicians, managerial staff, warehouses and transport). While major industries will likely survive despite the financial hardship, the MSMEs are already severely affected due to a demand collapse of the final product.

Agriculture, food & beverage, textiles, and transport have the largest share of the household consumption basket, and at the same time have considerable linkages across all the three sectors of the economy: raw materials, manufacturing, and services. Similarly, hotels and restaurants would also face financial and manpower losses due to the displacement of workers. These supply chains must be prioritised.

FISCAL

The first round of fiscal incentives was announced at the start of the lockdown in March, 2020. Some of these, like relaxation in tax filings, etc. were regulatory, while targeted initiatives on provident fund contribution, welfare schemes, etc. were part of the fiscal stimulus package. This was followed by several smaller measures, and then the massive *Aatma Nirbhar Bharat Abhiyan* economic package in early-May.

These stimuluses and revenue expenditure across social sector schemes, DBT or other subsidy-based schemes will exert huge pressure on central and state government funds. However, a freeze in capital expenditure may hit sectors of construction, steel, cement, and labour engagement. Resuming construction activity would be a key policy decision.

TIMELINE

These measures have been announced with adequate urgency and must now be deployed on priority.

IMPLEMENTERS	Union and state governments, their various nodal agencies, and the RBI should collaborate to ease bottlenecks and remove red tape, and quickly reach relief to the beneficiaries.
JOBS	The implication for jobs would vary by sector and has been explored in detail in later sections.
GROWTH	These interventions are essential to restart the economy after the lockdown and mitigate its catastrophic impact on people, livelihoods, and businesses to revive India's growth trajectory.
SUSTAINABILITY	This initiative has no direct impact on sustainability.
TRADE-OFFS	Expenditure priorities may get largely confined to wages, salaries, medical, and establishment expenses. This in turn could curtail discretionary spending on travel, repairs, and maintenance, leading to a demand squeeze for durable goods.

India's economic recovery path from pandemic, however, has much larger trade-offs. As the full spectrum of the crisis unfolds, we have two important dimensions to tackle its consequences. First, the fact that the past is no guide to the future means that the traditional methodology of deductive assessment based on trend or time series economic analysis is no longer useful. Cross-sectional comparisons are also hampered by differential experiential trajectories.

Hence the government must implement a survey-based rapid data collection and investigation strategy so that policy can be designed based on inductive analysis, learning from the impact of the crisis on the geographies of different socioeconomic conditions. This will also help repurpose public and private expenditure going forward.

The second dimension is the trade-off between economic optimisation and the alleviation of human distress. We have many difficult questions to address in this case as opposed to other types of crisis:

- Should the effort be to incentivise migrant labour to remain in their workplaces with attractive remuneration packages and a commitment to better working and living conditions (such as commitments to a slum free India, better quality public education and healthcare)?

  Or should the effort be to prevent a repeat of the unfolding tragedy by following a policy that leads to de-concentration of workers and dispersion of economic activity to areas of the country where the migrant laborers hail from?

- Should public resources be used to compensate those whose livelihoods will be substantially destroyed by the epidemic?

  Or should the focus be on supporting and growing resilient economic activities to maximise future output and welfare?

These questions may not have direct answers, but the solutions can only emerge with clear, defined objectives (drawn from a growing body of evidence) and the capacity to implement them through the administrative machinery.

3.2 Support small businesses

Image: iStock

India has an estimated 63.38 million unincorporated non-agricultural MSMEs. Of these, more than 63.05 million i.e. 99 per cent, are micro, 0.33 million are small, and approximately 5,000 are medium. Of all the MSMEs, 95.98 per cent are proprietary[29].

MSMEs represent 90 per cent of India's industrial units and contributes to 45 per cent of total industrial value addition. MSMEs also contributed almost half the country's exports—48.1 per cent—worth INR 11.1 lakh crore (USD 147.4 billion), in 2018-19[30].

India's estimated 450 million informal workers comprise 90 per cent of its total workforce, with 5-10 million workers added annually. About 40 per cent of these workers are employed with MSMEs[31].

The government has, over the years, taken steps to formalise the financing of MSMEs by setting up a nationwide network of regional rural banks (RRBs), small finance banks, NBFCs and MFIs; the specialised Small Industries Development Bank of India (SIDBI), and more recently, the Micro Units Development and Refinance Agency (MUDRA) under the *Pradhan Mantri MUDRA Yojana*.

The MSME sector, despite its rapid expansion in the past few years, was already in distress before the COVID-19 lockdown due to a perceived lack of creditworthiness. While short term relief measures are imperative to ease working capital constraints, the benefits of indiscriminate lending will be short-lived and only delay the inevitable non-performance of assets.

Sustained recovery and revival of this sector hinges on addressing the challenge of rampant informality, since most of these enterprises, especially in the voluminous micro segment, are not registered with the government. Creating a resilient MSME sector requires deep structural and regulatory reforms, starting with proper identification of the enterprises and establishing accountability of all stakeholders.

Proposed relief and recovery actions:

- Identify micro, small and medium enterprises and their workers
- Develop a vulnerability assessment framework of MSME sectors
- Increase capacity of the *SAMADHAAN* system to expeditiously clear government dues
- Improve creditworthiness of small businesses

3.2.1 Identify micro, small and medium enterprises and their workers

PROBLEM

The inability of the central and state governments to efficiently reach financial and in-kind relief to MSMEs and their workers during the COVID-19 lockdown, leading to the arduous mass migration of millions of workers from cities back to their native places, has illustrated the difficulties in rolling out targeted, large-scale support to such an informal sector without visibility on who they are, where they are, what they do, and their financial status.

The problem of accurate identification is two-fold:

- The sheer number of MSMEs, especially the informal one-person or micro enterprises, and
- The informal arrangements of employing workers, with little or no records.

On 13 May 2020, the government announced a collateral-free loan of INR 3 lakh crores (USD 39.8 billion) for MSMEs[32]. However, only a fraction of the total MSMEs are currently connected to any form of formal banking/NBFCs/MFIs or semi-formal systems such as the *Pradhan Mantri Jan Dhan Yojana* (PMJDY). Without these linkages, most of these enterprises will not have easy access to this loan.

A key challenge is the enrolment of these unknown MSMEs into an identification system that also provides visibility into the financial health of these enterprises.

SOLUTION

In the immediate term, the Ministry of Micro, Small and Medium Enterprises (MoMSME) should compile assorted existing national and state-level databases as best as possible to identify and secure information about these informal workers and business units.

In the **medium to longer term**, however, it must build an accurate, scalable, and real-time information system to identify and serve genuine beneficiaries of government schemes and aid. **This e-system could be named MISHRII (MSME Information System for Holistic and Real-time Identification, Incentives and Support)**.

MISHRII is a sugar substitute sweetener common in Indian households!

NON-FISCAL / STRATEGIC

There is a nominal cost to build the online information system. The major benefit will be the access to real-time, credible information about MSMEs and informal workers via a national, digital database, ensuring efficient, targeted delivery of aid and incentives.

TIMELINES

This initiative needs both, immediate and medium to long term measures.

Immediate

- One option to identify workers is through the *Jan Dhan* - *Aadhaar* - Mobile (JAM) trinity, a major database of the Indian citizenry. However, this system is rife with errors, duplications, and authenticity issues, and not reliable unless cross-verification parameters are instituted.
- MSME-related information is presently scattered across datasets such as the *Udyog Aadhaar Memorandum* (UAM) which has 13 million self-registrations, the MSME Databank, and the Goods and Services Tax Network (GSTN)[33]. The first two datasets have self-certified, voluntary information provided by businesses / individuals and

are hence not reliable, while the GSTN is a statutory requirement only for businesses with turnovers exceeding INR 40 lakhs (USD 0.05 million) per year.

- The MUDRA and SIDBI also have partial records of MSMEs. Approximately 10 million enterprises have availed MUDRA loans annually since its launch in 2015, mostly in the '*Shishu*' category (up to INR 50,000 (about USD 664)), directed at proprietary micro units identified via this dataset[34]. SIDBI's vast network and portfolio will yield information on entities it has financed and refinanced.

Medium to long term

- The fourth (and the last) census on MSMEs was conducted in 2006-07. It is thus imperative to take a fresh census of MSMEs and issue them a **Unique Business Identification Number (UBIN)** so that they can be recognised and referenced[35]. MSMEs can be segregated at national, state, or sectoral levels.
- The MoMSME should develop one nationwide, centralised online platform to identify and track MSMEs (through their UBINs) and informal workers. This platform should collect data on the size, distribution, and economic contribution of these workers to the national output, and seed details such as occupation, days of employment and monthly income into their *Aadhaar*-linked profiles. This platform should be linked with the goods and services tax (GST), value added tax (VAT), income tax, and other tax databases, and the banking network for DBT.
- Informal workers who wish to benefit from government support systems, will have to provide visibility into their financial health. This will enable the authorities to:
  - Identify beneficiaries of minimum wages under the *Wage Code, 2019*, and
  - Maintain an authentic database to better target policies and welfare schemes on matters such as life and disability cover; health and maternity benefits; old-age protection; education, housing, etc.
- The MSME e-platform **MISHRII** may be developed over time, but its architecture should be formalised by the first quarter of 2021. The Unique Identification Authority of India (UIDAI) can then import data from various individual and enterprise identity systems to populate it.
- The UIDAI has the skill sets, resources, experience, and reach to rapidly expand the *Aadhaar* database to capture employment details, cross-linked with bank account information, of individuals interested in availing government aid or incentive schemes. This can be piloted on a voluntary basis to check for efficacy before mass-scale deployment. Now is an opportune moment, given the powerful impetus of aid, for the MSMEs and their employees to register. The UIDAI can use the mobile short message service (SMS) to collect and authenticate information. This method is commonly used by power distribution companies and city gas distribution networks for metering.

IMPLEMENTERS	The MoMSME, SIDBI and UIDAI should take the lead in developing the MISHRII, with the MoMSME being the nodal agency.
JOBS	This initiative has no direct impact on jobs.
GROWTH	This visibility of the MSMEs and their workers will allow the government to develop targeted and effective policy measures and interventions, thus making them more productive and resilient in the longer term.

SUSTAINABILITY	This initiative has no immediate direct impact on sustainability. However, the potential to get incentives and support during trying times could lower the temptation to dilute sustainability standards further to save costs. Further, an advanced database could help to track and enforce compliance with environmental standards by the MSMEs in return for government aid.
TRADE-OFF	The J–A–M trinity, especially *Aadhaar*, has come under scrutiny for privacy issues. To offset such concerns, the registrations on MISHRII should be kept voluntary for those interested in availing government incentives and aid.

3.2.2 Develop a vulnerability assessment framework of MSME sectors

PROBLEM

The MSME sector is often considered as a homogenous group. But there are major differences in their exposure to risk, profitability and ability to quickly recover from setbacks. The recovery of MSMEs from the COVID-19 crisis depends on several vulnerability factors:

- Financial health, including cash flow and debt,
- Product and services markets with different demand revival trajectories,
- Availability of a migrant workforce from other states, and
- Exposure to the export market.

The high baseline risks in this sector makes the failure of many firms, especially in the micro segment, inevitable. Thus, it is imperative that enterprises that demonstrate the willingness and propensity to survive, be saved through proactive action.

The government's generous INR 3.7 lakh crores (USD 49.1 billion) package for the MSMEs can provide them much needed liquidity[36]. However, it does not prioritise the beneficiaries based on their economic importance and vulnerability of sectors. Also, the package is a short-term intervention and does not address the long term systemic and external challenges that impact each MSME sector.

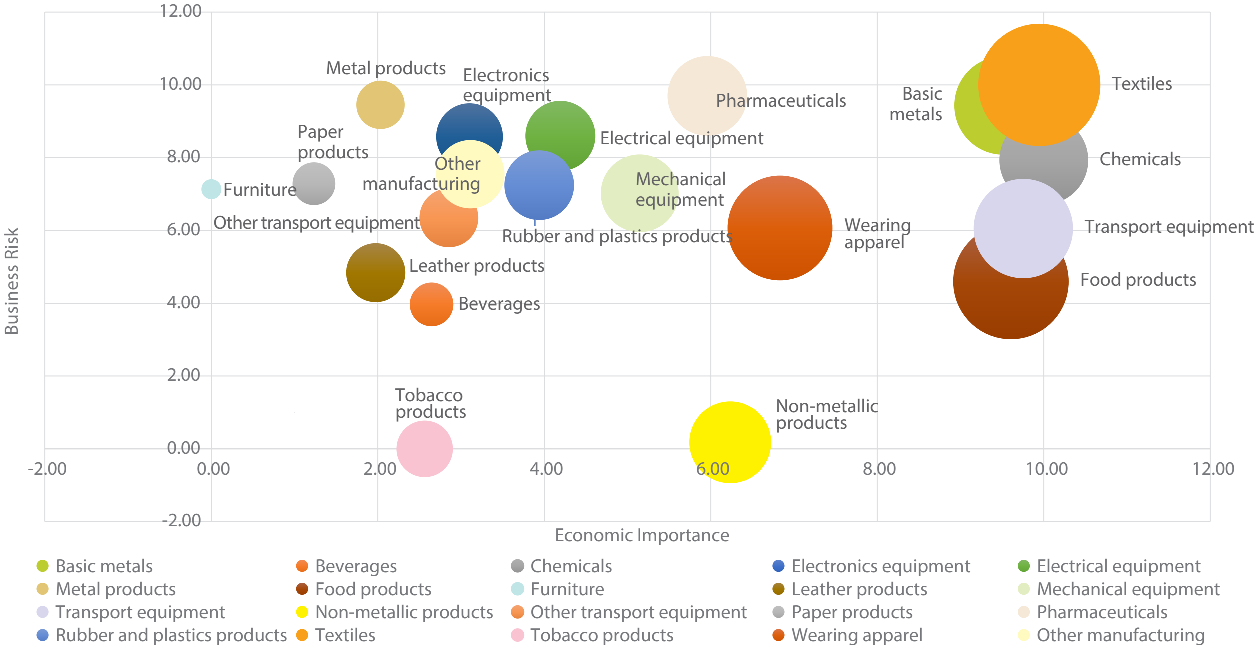
SOLUTION

We recommend that the MoMSME develop a **vulnerability assessment framework** of MSME sectors to efficiently target support measures by accounting for varying levels of vulnerabilities and sectoral nuances, resulting in effective use of government resources.

As a case study we have developed a two-dimensional matrix to compare the relative vulnerability of MSME sectors across two parameters:

- **Economic importance**: This indicator represents the relative contribution of an MSME sector to economic value addition (represented by GVA and employment). Higher the economic value addition and employment, higher the economic importance.
- **Business risk**: This indicator represents the liquidity of the MSMEs, which in turn is represented by a fraction of working capital supported by available cash resources (represented by cash in hand and at bank), and their cash conversion cycle (CCC) i.e. the time taken for the enterprise to recover its receivables. A lower value of cash to working capital ratio, coupled with a high CCC, presents a high business risk as the enterprises reopen after the COVID-19 crisis. Figure 1 illustrates the vulnerability matrix.

Figure 1 Assessing the vulnerabilities of India's MSME sectors



Source: CEEW analysis

The **three most vulnerable sectors** as per the matrix are:

- Textile manufacturing
- Chemical products
- Metal products

The sector-wise vulnerability assessment framework would help:

- **Revive the tail-end of the value chain:** Support measures should be driven by demand side economics, which means revival of MSMEs at the tail-end of the value chain. Enterprises in critical supply chains and markets, especially those that are export-oriented or have high employment elasticity (rubber and plastic products, electrical and optical equipment, transport equipment, and textiles), need special attention.
- **Synergise interventions with existing support measures:** The COVID-19 recovery measures should factor in existing support schemes such as cash transfers, especially to micro industries, as they constitute more than 99 per cent of all MSMEs.

FISCAL

This solution proposes a framework to target fiscal and non-fiscal support measures for MSMEs. Developing such a matrix will incur nominal cost. Cost of actual support depends on the nature and extent of measures adopted by the government.

TIMELINE

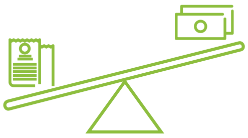
This vulnerability matrix should be developed at the earliest to prioritise financial assistance for the MSMEs.

IMPLEMENTERS

The MoMSME and its designated regional Development Institutes (MSME-DI) should implement this with support from independent think tanks.

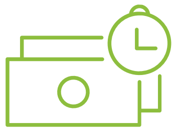
JOBS	The MSME sector is India's largest employer after agriculture, representing 40 per cent of the national workforce. These livelihoods depend directly on the viability of the sector, and targeted interventions will preserve most of these despite the COVID-19 crisis while creating new opportunities.
GROWTH	The MSME sector represents 90 per cent of India's industrial units and contributes to 45 per cent of total industrial value addition. MSMEs also contributed 48.1 per cent of the country's exports, worth INR 11.1 lakh crore (USD 147.4 billion), in 2018-19[38]. Further, textile, the largest commodity in India's merchandise export basket, is predominantly manufactured by MSMEs[39]. This sector contributed 12.2 per cent of total exports in 2018-19 and is crucial for India's forex earnings[40]. Ensuring the vast and rapidly growing MSME sector's revival after the lockdown will prevent a structural collapse of the economy, and set India back on its growth trajectory.
SUSTAINABILITY	This initiative has no direct impact on sustainability.

3.2.3 Increase capacity of the *SAMADHAAN* system to expeditiously clear government dues



INR 10,582 crore
Amount owed by central and state government departments and PSEs to MSEs (April 2020)

40,000
Delayed payment applications filed by MSEs in the SAMADHAAN portal since 2017



18,000
Delayed payment cases taken up for resolution by MSEFCs

Data points: CEEW compilation

PROBLEM

As per the MoMSME's *SAMADHAAN* Delayed Payment Monitoring System, various central and state government departments and public sector enterprises (PSEs) collectively owe approximately INR 10,582 crore (USD 1.4 billion) to micro and small enterprises (MSEs). Of these, applications worth only INR 599 crore (USD 79.5 million) have been disposed of by the Micro and Small Enterprises Facilitation Council (MSEFC). This includes INR 91 crore (USD 12 million) of INR 1,978 crore (USD 262.5 million) outstanding with central ministries, departments and central public sector enterprises (CPSEs)[41] .

Since the launch of the *SAMADHAAN* portal in 2017, over 40,000 applications have been filed, of which only 18,000 have been taken up by the MSEFCs as active cases for resolution. Further, the MSEFCs have to clear these applications within 90 days as per the *MSME Development Act 2006*, but that has not been the trend, with unresolved applications pending since 2017[42]. The *SAMADHAAN* system also has a high rejection rate of approximately 55 per cent, which has led to over 9,000 cases being arbitrated in the MSEFC courts.

These delayed and contested payments pose a huge challenge for the MSEs, which are already constrained by high fixed costs, revenue streams disrupted by the COVID-19 lockdown, and a major liquidity crisis perpetuated by the reluctance of banks, MFIs and NBFCs to lend to them.

In a major relief, on 13 May 2020, the Finance Minister announced the clearing of all MSME receivables from the government and CPSEs within 45 days[43]. However, it is unclear how the process will be accelerated given the limitations on travel and availability of MSE and MSEFC representatives due to the crisis.

SOLUTION

The government should prioritise clearing the receivables of all MSEs who are long term suppliers with a good track record on a provisional basis. This will reduce the number of cases that need to be addressed within the 45-day timeline.

Further, the government needs to immediately issue a directive to the states to expand the capacity of the MSEFCs so that the resolution of the cases can be expedited.

FISCAL	Clearing outstanding dues to MSEs involves pay-out of funds but does not create any additional burden as these funds should have been provisioned by the procuring agencies. However, in case these agencies are themselves cash-strapped and unable to pay the dues, the central government would have to step in with additional liquidity. This particularly applies to pending dues from state governments that are currently in financial distress and may not prioritise MSE payments.
TIMELINE	This capacity should be increased immediately to support the government's directive to clear MSE dues within 45 days as part of urgent relief efforts.
IMPLEMENTER	The MoMSME, their state nodal agencies, central and state government departments and public sector enterprises should pay their outstanding dues to MSEs.
JOBS	Recovering these long-outstanding dues will infuse liquidity into MSEs and allow them to pay wages to their employees, preventing further job losses and erosion of workforce.
GROWTH	Ending lengthy arbitration with government departments and PSEs for outstanding payment will provide relief to MSEs and allow them to focus on their businesses. This will contribute to India's economic recovery, and in turn, add to government taxes as well as household income and spending.
SUSTAINABILITY	The Ministry should establish a strong framework to conduct business between government departments and MSEs. This will help to prevent the accumulation of such dues in the future, build trust, ensure smooth flow of capital, and increase the resilience of these small businesses withstand such emergencies.

3.2.4 Improve creditworthiness of small businesses

In order to cushion the impact of the COVID-19 pandemic on the MSME sector, on 23 April 2020, the RBI tried to inject liquidity into the market through the targeted long-term repo operation 2.0 (TLTRO 2.0)[44]. To avoid a repeat of TLTRO 1.0, where the offered INR 1 lakh crore (USD 13.27 billion) had been channelled primarily to large corporates with high credit ratings, TLTRO 2.0 preconditioned that banks must lend half of the offered INR 25,000 crore (USD 3.32 billion) to small and medium NBFCs and MFIs so that the intended support reaches the MSMEs. However, RBI received bids for only INR 12,850 crore (USD 1.70 billion) as banks showed little interest in increasing exposure to a sector already plagued with NPAs and delinquencies, which are expected to increase manifold in the wake of the crisis.

The RBI has also provided special refinance facilities for INR 25,000 crore (USD 3.32 billion) to the National Bank for Agriculture and Rural Development (NABARD) for refinancing of RRBs, cooperative banks and MFIs, and INR 15,000 crore (USD 1.99 billion) to SIDBI for on-lending / refinancing. But these, too, have found few takers. This risk aversion of banks to lend to MSMEs reflects the reality that organised finance remains elusive for these enterprises.

PROBLEM

The MSME sector is marred by low creditworthiness. Credit growth of MSMEs has been steadily declining for several months now due to widespread NPAs and payment defaults, and the risk appetite to lend to these units has taken a severe hit in the current economic crisis. It is now clear that liquidity injections will not ensure last mile credit delivery.

On 13 May 2020, the government introduced a collateral- and guarantee-free loan of INR 3 lakh crore (USD 39.81 billion), with a one-year moratorium on interest payment, to MSMEs as immediate financial relief[45]. To encourage lenders, the government has provided full credit guarantee on this amount. While this will infuse liquidity in the short term, it is a tremendous strain on government funds and does not address the creditworthiness of MSMEs.

SOLUTION

There is a high risk of a significant proportion of these loans turning into NPAs, which would reiterate the lack of creditworthiness of MSMEs. The government should **mandate the lenders to introduce a mechanism to track the fund utilisation and financial health of the borrowers on a monthly basis, and intervene at the first signs of distress**.

NON-FISCAL / STRATEGIC

This tracking mechanism will provide visibility into gradual NPA build-up and allow the lenders and the government to take timely corrective action. Moreover, this is an opportune moment to institute formal tracking of MSME financing as a business practice and bring them into the ambit of core banking.

TIMELINE

This tracking mechanism should be instituted immediately, to coincide with the disbursal of these loans.

IMPLEMENTERS

The MoMSME and Ministry of Finance (MoF) should constitute a joint task force to evaluate this mechanism as a pilot, and eventually institutionalise it for the MSME sector.

JOBS

This is a compliance measure and has no direct impact on jobs. However, improving the creditworthiness of MSMEs will benefit millions of workers employed in this sector.

GROWTH	This mechanism will introduce fiscal discipline in the lenders as well as the enterprises, and over time, will improve the creditworthiness of MSMEs and integrate them into mainstream banking. It will also alert the government to NPA build-up, which can freeze up capital and impede growth. This will enhance the overall economic prism of the country.
SUSTAINABILITY	This initiative has no direct impact on sustainability. However, since lack of access to capital has been a major hindrance for MSMEs to adopt cleaner technologies, improved creditworthiness would eventually help them install energy efficient equipment and technologies[46].

3.3 Increase capacity of the National Company Law Tribunal to efficiently manage cases


Image: iStock

PROBLEM

Since its inception on 1 June 2016, the National Company Law Tribunal (NCLT) has received about 62,000 cases, of which over 40,000 cases were disposed of, and 21,500 cases were pending as of March 2020[47]. The number of cases referred to the NCLT is estimated to be rising at a rate of 10 per cent annually due to the introduction of the *Insolvency and Bankruptcy Code* (IBC).

In April 2020, the Cabinet suspended sections of the IBC that trigger insolvency proceedings against defaulters for a period of six months, extendable to one year[48]. While this will ease the pressure on stressed businesses in the near term, we can expect an exponential increase in the number of cases referred to the NCLT after the sections are resumed and the RBI lifts COVID-19 related moratorium on recognition of NPAs.

The NCLT was already struggling to manage its caseload before the pandemic. It took an average of 350 days to resolve cases as opposed to the mandated maximum of 270 days for companies and 135 days for start-ups and small companies. The NCLT's judgments are frequently litigated in courts, further delaying the final resolution of these cases.

SOLUTION

There is an urgent need to increase the bench strength of the NCLT. There are currently 15 open positions for judges that should be filled immediately; however, it would **need a much higher bench strength to address the peak in bankruptcies. We recommend that the NCLT consider adding temporary benches to handle this surge.** These branches should also geographically cover major business centres countrywide to ease access for MSMEs.

STRATEGIC	This intervention relates to the business as usual functioning of the NCLT and does not require a separate financial outlay, although a modest increase might be needed to set up the temporary benches.
TIMELINE	The capacity should be increased within the next 8 to 12 months. The recruitments should start immediately to ensure that the benches are in place in that time frame.
IMPLEMENTER	The Ministry of Corporate Affairs (MoCA) must initiate the process to fill the open positions for judges and the temporary expansion of bench strength.
JOBS	This measure can create over 1500 direct jobs once approved capacity is recruited. It also indirectly impacts employment across all companies referred to NCLT for resolution.
GROWTH	This measure will expedite clearance of bad assets and allow for better liquidity in banks and, consequently, recovery of industrial ecosystems. Not initiating these steps, on the other hand, will result in increased NPAs on the bank balance sheets, resulting in increased provisioning, and overall freezing of credit lines that will be detrimental to the entire economy.
SUSTAINABILITY	This initiative has no direct impact on sustainability.

3.4 Evaluate the impact on Indian trade

Image: iStock

PROBLEM

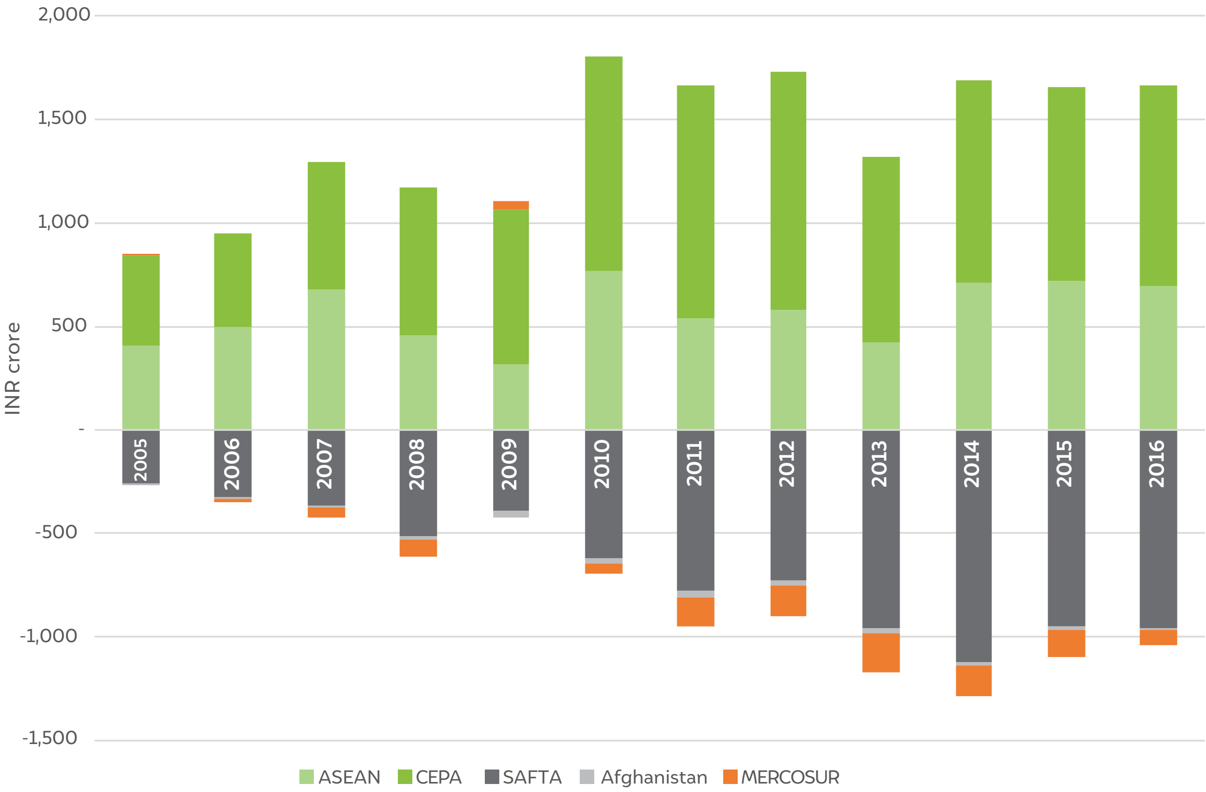
The global lockdown and trade restrictions have led to a precipitous fall in consumer demand, leading to a massive inventory build-up. The post-lockdown period will globally see companies liquidating their inventories and flooding the markets with cheaper products when faced with tepid demand rebound.

An analysis of the merchandise trade balance across India's Free Trade Agreements (FTAs) reveals that the Association of Southeast Asian Nations (ASEAN) and Comprehensive Economic Partnership Agreement (CEPA) countries have been reaping the benefits of India's positive trade balance (Figure 2). In 2017, India imported electrical machinery worth INR 7.94 lakh crore (USD 100.544 billion) from ASEAN countries, with about 42 per cent coming from Singapore[49]. Further, the imports saw a big jump from 2018 to 2019: electrical machinery and parts grew by 158 per cent and capital goods by 142 per cent[50].

This matter warrants scrutiny, because while Singapore has a thriving electronics industry that mainly produces semiconductors, there is no evidence of a large manufacturing base of electrical machinery[52] and capital goods like power and mechanical equipment[53]. This indicates a possible re-exporting of goods in violation of the FTA's 'country of origin' clause which mandates a minimum 35 per cent value addition by the exporting country to avail concessions.

Given China's dependence on exports to maintain its manufacturing industry, it may undercut product prices and route low-cost exports through the ASEAN countries under the cover of FTAs. This could pose a serious threat to Indian industries, especially in the post-pandemic recovery period since ASEAN trade constitutes a major share of India's positive trade balance.

Figure 2 India's merchandise trade balance across existing FTAs



Note: ASEAN – The Association of Southeast Asian Nations Free Trade Agreement
CEPA – Comprehensive Economic Partnership Agreement with Japan and South Korea
SAFTA – The South Asian Free Trade Area
MERCOSUR – India MERCOSUR Preferential Trade Agreement with Brazil, Argentina, Uruguay, and Paraguay

Source: CEEW analysis

India must take appropriate protection measures against such practices to prevent a collapse of its own industries, especially strategic ones such as ferrous and non-ferrous metals, textiles, pharmaceuticals, solar cells and modules, and heavy machinery.

SOLUTION

We recommend that the government immediately initiate two measures:

- **Identify goods categories with an unusual trade balance:** The immediate requirement is to identify the goods categories which lie in the suspicious category of violating the rules of origin country as per Article 7 of the trade agreement between India and ASEAN countries. For this, the *Customs Tariff Act*, 1975 can be modified, on the similar line of changes proposed in the budget 2020-21[54], to have a clause to state the provenance of the 'country of origin' for goods being imported into India. This also serves to institutionalise ethical trade practices.
- **Enforce and track Rule 4 of ASEAN-India Free Trade Agreement (AIFTA):** To revive the manufacturing sector and protect domestic industries from dumped imported goods, the Government of India (GoI) must urgently enforce and track the 35 per cent minimum value addition requirement as per rule number 4 of the AIFTA[55].

STRATEGIC

This is a trade/diplomatic intervention requiring no financial outlay.

TIMELINE	This measure should be implemented immediately as most of the Asian countries are having an early recovery from the COVID pandemic and will rapidly liquidate their built-up inventories at a discounted price.
IMPLEMENTERS	The Ministry of Commerce and Industry (MoC&I) needs to immediately revise the *Customs Tariff Act* to empower customs officials to track and confirm any origin fraud. Both the MoC&I and Ministry of External Affairs (MEA) should enforce the FTAs and take necessary steps to safeguard Indian businesses.
JOBS	Implementing this protection measure would: - Prevent the immediate risk of collapse of India's domestic industries and, at least temporarily, protect their employment base, and - Provide an opportunity to grow the manufacturing base, and create additional jobs.
GROWTH	The domestic manufacturing sector is in transition, moving away from low- to medium-value to high-value manufacturing. Hence, it is crucial to provide the industry a level playing field by blocking any '*origin fraud*' in the existing FTAs. But this needs to be done thoughtfully, to protect against non-competitive trade practices while avoiding the temptation to indefinitely support inefficient industries. The case for growth rests on fair competition — at home and abroad.
SUSTAINABILITY	This initiative has no direct impact on sustainability.
TRADE-OFFS	The GoI tightened its trade norms on 18 April 2020 by amending its foreign direct investment (FDI) policy. Now, entities of countries that share a land border with India can invest in greenfield projects or existing ones only with GoI approval, irrespective of the sector or the amount of FDI allowed via automatic route. It also restricts transfer of investments / future FDI resulting in beneficial ownership, thus safeguarding against round-tripping of investment. This change impacts citizens, companies and investing entities of seven neighbouring countries, but is expected to mainly address apprehensions of Chinese firms taking over financially stressed Indian firms in the wake of the pandemic. Further, in May 2020, the GoI notified amendments to the *General Financial Rules 2017* to henceforth disallow global tenders up to INR 200 crore (USD 27.3 million) in government procurement. The influx of low-cost imports that circumvent intercountry taxation has created huge business ecosystems in India. Imposing restrictions on supply chains, especially during an economic crisis, would adversely impact these enterprises as well as suppress demand from buyers due to increased prices. Increased scrutiny could also upset the balance of relationships with trading partners.