

India: Economy, Public Policy and SMEs under the Pandemic

ISED Discussion Paper



by
**K. Laxminarayanan
&
P.M. Mathew**

Institute of Small Enterprises and Development



ISED House, ISED Road, Cochin - 682028
Email: info@isedonline.org, seo@isedonline.org
www.isedonline.org

India: Economy, Public Policy and SMEs under the Pandemic

India: Economy, Public Policy and SMEs under the Pandemic

by
K. Laxminarayanan
&
P.M.Mathew

ISED Small Enterprise Observatory
Jointly with
ISED Centre for Enterprise Development

© Institute of Small Enterprises and Development 2020

All rights reserved. No part of this document may be reproduced or utilised in any form or by any means, electronic or mechanical, including photocopying, recording or by any information storage or retrieval system, without permission in writing from the publisher.

Institute of Small Enterprises
and Development, ISED House,
ISED Enclave, ISED Road,
Cochin-682 028, India
URL: www.isedonline.org
Email: info@isedonline.org



ISED Small Enterprise Observatory,
ISED House, ISED Enclave,
ISED Road,
Cochin-682 028, India
URL: www.isedonline.org
Email: seo@isedonline.org

Published by P.M. Mathew, for Institute of Small Enterprises and Development.

Series: ISED Discussion Paper Series

Price: 490.00 (India); US \$ 10.00 (Overseas)

About ISED Discussion Paper Series

ISED Discussion Paper Series aims to accelerate the public availability of the research undertaken by ISED-associated people of all categories. It presents research results that, in whole or part, are suitable for submission to a refereed journal, to a sponsor, to a major conference or to the editor of a book. Our intention is to provide access to early results of research at ISED. Readers are encouraged to quote or reproduce material from ISED Discussion Papers for their own publications, as long as they are not being sold commercially. As copyright holder, ISED requests due acknowledgement and a copy of the publication. ISED publications seek to provide evidence and analysis that matters for entrepreneurial people and the planet.

Preface

The contemporary changes in science and technology has revolutionised resource allocation and capital formation, in many parts of the world, as also in India. However, entrepreneurship resources and their sustainable development did not get adequate attention in policy and practice. Despite the significant policy priority accorded to SMEs in India, the potential of the country's entrepreneurship resources still remains inadequately utilised. The experience of Covid-19 raises much wider questions on 'cohesive development' in general and local economic development strategies in specific, as something that needs closer examination.

Under the India MSME Communication Programme(IMCP), the Observatory, in co operation with the various Knowledge Centres of the Institute, makes a rigorous analysis of the latest currents in the MSME constituency, leading to a unique 'Development Report'. This study is a spill-over of this exercise of Development Reporting on micro, small and medium enterprises (MSMEs) at the ISED.

While the team of the Observatory did a meticulous job under the guidance and support of the Project Leaders, individual members of the Team, including the editors and the Associates, have made their special contribution in specific thematic areas. While this title is significant in the present context of the Indian economy , and of the MSME developments in specific, I hope it will contribute to wider discussions in the subject area.

As this title come out as a joint output of the Observatory and the ISED Centre for Enterprise Development, the Institute wishes to thank, without fail, the pains and efforts of the authors, and all who have supported it through inputs and suggestions. ISED has taken best efforts to ensure the quality and reliability of this paper. However, for the findings and views, the authors alone are responsible.



P.M.Mathew

Director, ISED Cochin

December 5, 2020

India: Economy, Public Policy and SMEs under the Pandemic

K. Laxminarayanan & P.M.Mathew

Abstract

The contemporary changes in science and technology has revolutionised resource allocation and capital formation, in many parts of the world, as also in India. However, entrepreneurship resources and their sustainable development did not get adequate attention in policy and practice. Despite the significant policy priority accorded to SMEs in India, the potential of the country's entrepreneurship resources still remains inadequately utilised. The experience of Covid-19 raises much wider questions on 'cohesive development' in general and local economic development strategies in specific, as something that needs closer examination.

Key Words: India, SME, Covid 19, economy

1.0. Introduction

The year 2020 marks a major watershed in the economic history of the world; in India also. While colonialism was the basis for economic inequalities among and within the countries, during the two crises around the First and Second World Wars, of late, digital divide and technology fetishism have been instrumental in sustaining such inequalities. Technology fetishism, in turn, has led to radical changes in resource allocation and capital formation, in many parts of the world, as also in India. As such entrepreneurship resources and their sustainable development did not get adequate attention in policy and practice. Naturally, in India, despite its huge potential relating to MSMEs, MSMEs did not get adequate attention both in public policy and in the popular eye. The experience of COVID-19 raises much wider questions on 'cohesive development' in general and local economic development strategies in specific, as something that needs closer examination. It is against this background that the ISED Small Enterprise Observatory has articulated a "tortoise and Hare strategy" as the way forward for India (ISED, 2019).

2.0. India's SME Scene in 2019: A Recap

The state of India's MSME sector, during this difficult year of a pandemic, need to be understood in relation to the overall trend and progress of the economy in the previous year. This has been reported in detail by the India MSME Report 2019. For a realistic understanding of where India is, and the path that the country is likely to take beyond this pandemic, let us have a recap of the same.

2.1. Overall State of the Economy

The major building blocks of the India MSME Report series, apart from the field evidences, are the official sources of information: documents of the Ministry of Finance, Ministry of MSME, and Reserve Bank of India, Labour Bureau, NSSO, and the CSO. These sources

of data enable us to draw the broad contours of the structure and direction of changes in the economy.

The trend and progress of India's GDP rates has been a subject of active debates during recent years. However, arguments on estimation procedures apart, it was generally agreed that the economy was slowing down during the year 2019.

The RBI, in its Annual Report 2019, could not arrive at a conclusive position on the slowdown in the economy. The Central Bank had cut its key rates by 1.10 per cent in 2019 to a nine-year low of 5.4 per cent in four such successive cuts to help revive the sagging growth. Reviving consumption and private investment were the "highest priority" for the RBI today. It viewed that this can be done by strengthening both the banking and non-banking sectors, a "big push" to infrastructure spends and implementation of the much-needed structural reforms in labour laws, taxation, and other legal reforms.

2.2. State of the MSME Sector

Considering the nature of the ongoing pandemic, no systematic ground level studies on the MSME economy has taken place so far. But, there are some estimates that indicate a grim picture of the economy. In the changed global scenario, MSMEs in India need to operate in a competitive environment, on par with the large enterprises, except for the limited support measures offered by the government. These support measures belong to the following major functional domains: (1) technology up gradation support; (2) information and facilitation; (3) credit facilitation; (4) infrastructural support; (5) market development support; and (6) public procurement. While a discussion on these various support areas is crucial, it is important to distinguish them in relation to their potential impact on MSMEs. Market intervention, such as purchase preference policy and public procurement, have a significant discretionary element, the others are more facilitative in nature.

For the sustainable development of enterprises, as also for cultivating a culture and environment of enterprise growth and entrepreneurship development, support systems and programmes have only a partial role. The major role and impact emerges from the market signals sent out by such programmes. While MSMEs are the base of the enterprise pyramid, the logic of the market dynamics, irrespective of size, is common.

It is pertinent to circumscribe India's MSME experience today, around some focal themes. While, these themes, by no means, cover an exhaustive list, an understanding on them may help us to draw the contours of current practices and policy imperatives. The key MSME issues of the year have been reported by the India MSME Report 2019, as follows:

2.2.1. Public Policy Thrusts: Unlike in the past, MSME policy has been increasingly integrated with the overall macroeconomic policy, and more specifically with the 'Vision of the Decade', as outlined by the Union Budget 2019.

2.2.2. Private sector Engagement Strategies: Private sector engagement strategies were, increasingly broad based, with an enhanced focus on the MSME sector. This has happened in the form of broad basing of schemes, step up of start-up promotion measures, and enhanced steps for cultivating trust and mutual respect.

2.2.3. Economic Slowdown and Confidence Crisis: The anti-cyclical and anti-recessionary role of the MSME sector is critical. Though the Union Budget announced some proactive steps and more vigorous efforts in this area.

2.2.4. Density of Credit Delivery: Credit delivery remained the focal MSME issue of the year. But, apart from the unsatisfactory role of financial institutions, poor quality of non-credit services remains.

2.2.5. Morbidity Statics of the MSME Sector: Within the integrated framework of 'enterprise security', climate change stands out as a key issue of the year.

2.2.6. 'Millennium Dualism' and Issues around That: A key issue of the MSME sector, globally, and more specifically in India, is the Millennium dualism, where, a small technology savvy modern sector, on the one side, and the huge traditional sector on the other, constrains the chances of innovation and growth. Hence, a "tortoise and hare strategy", as an alternative, has been proposed.

2.2.7. Knowledge Gap: Bridging the knowledge gap, and evidence-based policy making, are advocated for facilitating the MSME sector to harness its full potential.

2.2.8. Scale to Scope Paradigm shift: While the arguments

in favour of the MSME sector are traditionally based on social aspects such as employment and balanced regional development, the emergence of technology as a major third force, has made scope economies, a crucial dimension. This demands meaningful policies on the basis of strong evidence base.

2.2.9. Macro Policy Base to Meso Base: 'Subsectors', as the focal point of policy and development practice, need to be highlighted.

In Bihar, weavers in the Bhagalpur silk industry were badly affected by the Pandemic related disruption of activity. They turned to making of masks for a survival.

2.3. Broad Policy Initiatives in 2019

The new policy perspectives and directional changes, that have come through the Union Budget-2019 and the Economic Survey that preceded it, were important. A deep dive into the Budget statements offer indications on the government's intention to look at the MSME sector from a different angle, and to engage it differently.

To start with, the government's budgetary allocation for the MSME Ministry, at Rs 7,011.29 crores, was the highest thus far. Besides, the focus on start-ups was a different way of looking at its latent opportunities.

The need for a flexible official definition for the MSME sector was in the air for the last several years. The Government of India proposed a new turnover-based classification of MSMEs in February 2018. The Union Cabinet approved the proposal for Amendment to the Micro, Small and Medium Enterprises Development Act-2006 to change the criteria of classification. The 'turnover criterion' was intended to ensure synchronisation with the GST Network (GSTN) and other formats of segregating the MSMEs.

Several steps were taken by the Government of India in 2018, and in early 2019, for improving the credit flow situation. For the MSME sector, Rs 350 crores was allocated for FY 2019-20 under the Interest Subvention Scheme, for 2% interest subvention for all GST registered MSMEs, on fresh or incremental loans. An External Benchmark Based Lending was announced by the RBI. As a step in that direction, it was announced that all new floating rate personal or retail loans, including MSME loans, was extended by banks from April 1, 2019, shall be linked to external benchmarks. Subsequently, it was announced in the first bi-monthly Monetary Policy Statement for 2019-20, to hold further consultations with stakeholders and to work out an effective mechanism for transmission of rates.

To ease the liquidity crisis in NBFCs, the Budget had taken some important steps. Fundamentally sound NBFCs were ensured to get funding from banks and