

MSMEs and Economic Lockdown

What is the issue?

With economy on a standstill in times of the lockdown, here is a look at its impact on micro, small and medium enterprises (MSMEs) and the modes of financing them.

What comprises the MSME sector?

- MSME sector form the second-biggest employer in the country with a 31% share in India's GDP.
- Section 7 of the MSMEs Development Act, 2006 specifies the size of the MSMEs on the basis of investment.
- Among manufacturing units, micro enterprises are those that have invested up to Rs 25 lakh in plant and machinery.
- The comparable figure for small units is Rs 25 lakh-Rs 5 crore and for medium units, Rs 5 crore-Rs 10 crore.
- For services, the investment thresholds are lower - up to Rs 10 lakh, Rs 10 lakh-Rs 2 crore and Rs 2 crore-Rs 5 crore respectively for the categories.

Why do they need more attention now?

- Unlike big industries, the MSMEs' resilience during the current crisis is lower.
- Many of the MSMEs are probably eating into their capital to stay afloat.
- The RBI has already asked banks to offer a three-month moratorium on loan repayments by such units.
- Beside, the RBI has arranged for opening a window from where banks can borrow money and lend to the sector.
- However, banks are afraid of loans given to these units turning bad.

How has the credit support been?

- A recent study shows that the MSMEs' exposure to the financial system in December 2019 was Rs 11.04 trillion.
- Of these, the share of very small businesses (up to Rs 10 lakh exposure) is Rs 54,000 crore.
- In December, in commercial credit (excluding agriculture and retail), the share of MSMEs (up to Rs 50 crore exposure) was a little less than 28%.

- The maximum loans were in the Rs 1 crore-Rs 15 crore basket (Rs 8.74 trillion), followed by Rs 15 crore-Rs 50 crore (Rs 4.68 trillion).
- Notably, the corpus of less than Rs 10 lakh loans was the smallest, at Rs 93,000 crore.
- Maharashtra has the maximum share of MSME credit, 17.36%, followed by Tamil Nadu (10.77%), Gujarat (8.85%), Delhi (7.13%) and UP (6.5%).

How creditworthy are MSMEs?

- Loans to the MSME segment had grown 4.7% between December 2018 and December 2019.
- Indeed, the bad loans in the segment have been on the rise over the past few years and reached 12.6% in December 2019.
- The study keeps the Rs 2.32 trillion MSME exposure of banks in the highest risk bracket (of this, the micro units' share is just about Rs 13,600 crore).
- But there are millions of creditworthy borrowers outside this.
- The study has found that 74% of the close to 8.9 million MSMEs is creditworthy.
- The banks must grab this opportunity to fuel growth in the economy as well as their loan books.

What are the other hurdles in financing MSMEs?

- The banking system is the main source of money for the MSME segment.
- Added to this, the microfinance institutions (MFIs) meet the credit needs of retail borrowers at the so-called bottom of the pyramid.
- Notably, there is not much stress in the portfolio of micro loans offered by the MFIs and NBFCs (non-banking financial companies).
- So, presently, they are not suffering from risk aversion but most of them do not have the money to lend.
- Initially, the banks were reluctant to offer moratorium to the MFIs and NBFCs on their repayment of loans to the banks.
- They had felt that it was meant for the loans given for productive purposes and not to financial intermediaries.
- Now, most banks are offering the moratorium to MFIs too.
- But the Small Industries Development Bank of India (SIDBI) and Micro Units Development and Refinance Agency Ltd (MUDRA) are not that liberal.
- Notably, these two government agencies have around Rs 3,000 crore of exposure to the MFIs.
- Apparently, the NBFCs and MFIs borrow primarily from banks and on-lend to their customers.
- If the banks close the outlet, then NBFCs and MFIs cannot survive, which could in turn hamper the economy; this needs intervention.

Source: Business Standard

