Reviving MSME sector

What is the issue?

A rescue plan for liquidity-hit MSMEs is the need of the hour to overcome the impacts of demonetisation and GST.

Why is there a liquidity crisis in the MSME sector?

- The GST was expected to boost manufacturing, capital expenditure, employment, tax revenue and formalisation of the informal sector.
- However, these objectives remain mostly unrealised due to disruptions in circulation of unaccounted/informal business capital/working funds following demonetisation and GST.
- The major reason for liquidity crisis in the system is attributed as the impact of GST.
- There is an acute shortage of liquidity in terms of formal business capital to finance GST transactions.
- This is because many MSME companies hold Unaccounted business capitalthat carries the stigma of black money.
- Its use in formal transactions carries risk and fear of income tax scrutiny, harassment and retrospective tax.
- Thus, unaccounted business capital/funds, whichhas not been circulated into the economy, is creating unprecedented liquidity crisis across businesses.
- Also, since these unaccounted capital were treated on par with black money under voluntary income disclosure schemes, it has furtherdisincentivised its conversion into formal money.
- Further, during demonetisation, a part of unaccounted business capital got deposited in bank accounts with relaxed KYC norms.
- But post-demonetisation, the withdrawal of these deposited amount requires full KYC compliance and subsequent monitoring by income tax authorities.
- Thus,these money have been left to remain in bank deposits by businesses.
- This shows that demonetisation has further reduced fund availability for businesses.

What are the measures needed to bring informal businesses under GST?

- All the unaccounted funds/cash holdings/bank deposits of a business need to be deposited in a designated current account of a bank linked to business activities under GST.

- It should be made mandatory that these deposits be used for business transactions only.
- Formalisation of MSMEs can work only if the conversion of unaccounted capital that are earned from legitimate business activities is formalised with a low penalty.
- Thus, once the unaccounted income gets deposited, a graded penalty upfront on the total declared deposits/cash may be imposed.
- Eg: 10% up to ₹50 lakh and 20% for ₹50 lakh to ₹2 crore.
- And this penalty provision should be allowed only to GST-registered firms, restricted up to deposits of ₹2 crore.
- This will enormously help businesses to increase their business under GST.

What will be the advantages of bringing MSME into formal net?

1. The supply chain financing network can be boosted without loss of time.
2. Transmission of liquidity and late payment shocks are controlled.
3. Revival of the unorganised sector will be faster, steady and efficient.
4. GST revenue will leapfrog with steady growth in turnover.
5. Formalisation of business transactions will be easy, faster and widespread.
6. Higher growth will mitigate NPA problems and lead to better NPA asset value.

Source: Business Line

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