

Reviving MSME sector

What is the issue?

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MSME sector has been affected by credit and viability concerns and hence regulatory interventions are needed to address them.

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What is the background?

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- There are around 50 million MSMEs, both registered and unregistered, which stands as the biggest employer after agriculture sector.

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- MSME sector cumulatively contributes 37.5% of India's GDP and also account for 16% of bank lending.

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- However, around 8% of credit to manufacturing micro and small enterprises and 13% to medium enterprises are estimated to be gross NPAs.

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What are the concerns?

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- Pradhan Mantri Mudra Yojana (PMMY) is a scheme to extend collateral free loans by Banks, Non-Banking Financial Companies (NBFCs) and Micro Finance Institutions (MFIs) to Small/Micro business enterprises and individuals in the non-agricultural sector.

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- This was mainly done to enable MSMEs to setup or expand their business activities and to generate self-employment.

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- **Selection** - The scheme helped banks to push the services sector lending below Rs. 5 lakhs significantly.

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- However, there is also an evidence of moral hazard following the lending.
- This is mainly because of adverse selection as several enterprises are non-traceable at the location mentioned in the applications.

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- **Settlement delay** - The government has put in place measures like e-Invoice, TReDX, Samadhan, GeM to ensure prompt payment of bills from public sector undertakings and central government departments.

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- Even so, the State PSUs and state government departments continue to delay the bills of MSMEs, leading to NPAs.

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- **Loan disbursal** - Some banks follow a multi-layered approach to lend to the sector and as a result due diligence suffers.

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- The branch that disburses is also expected to monitor and supervise the credit but does not have the time or manpower for that.

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- There is hardly any communication between the entrepreneur and the credit authority until an irregularity in the account surfaces.

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What are the measures needed?

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- **Lending norms** - Under priority sector lending, the sub-target for bank lending to the micro enterprises has been 7.5% of adjusted net bank credit.

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- RBI has recently made that all loans to MSME will qualify as priority sector lending.

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- Previously, loans up to Rs 10 crore per MSME borrower was only considered for priority sector calculation.

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- Apart from increasing thresholds in priority sector portfolio, RBI should also frame credit risk assessment mechanism for the MSMEs.

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- **Revival** - Though MSMEs have been declared as NPAs, they have no exit route of the sort facilitated under the IBC code or the Industrial Disputes Act.

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- Innovative institutional interventions like the Industrial Health Clinics should be leveraged to revive and restructure sick enterprises.

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- Also, cluster development of MSMEs should be undertaken, thereby providing additional lending incentives.

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- **Credit Guarantee** - Credit Guarantee Fund Trust for Micro and Small Enterprise (CGTMSE) needs to be reviewed and redefined.

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- The premium rates charged by CGTMSE were found to be high and the claim settlement process getting unacceptably late.

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- It also has a role conflict with SIDBI as the latter is the promoter of MSME and at the same time secures its guarantee for the MSME enterprises financed directly by it.

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- **Asset registry** - Banks in India only accept fixed assets as collateral while giving loans to such companies, which have most of their capital invested in moveable assets. (raw materials/inventories)

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- Hence, setting up of a Movable Asset Registry will make it easier for larger units within the MSME segment to borrow from banks.

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- **Credit registry** - A public credit registry could be set up for MSMEs to distinguish between a bad and a good borrower and accordingly offer attractive interest rates to good borrowers from them.

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- Also, role of credit rating agencies and effectiveness of internal credit rating tools should be enhanced, apart from digitising MSME lending.

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- Since MSMEs are still largely debt driven and not equity driven, it is important that access to credit should be easier, cleaner, and faster.

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- Altogether, healthy growth of MSME is crucial for employment and growth of the manufacturing sector as a whole.

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Source: Business Line

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