

# A study of Impact, Challenges and Risk Mitigation Strategies for MSMEs in India during COVID-19 pandemic

Ayush Tankha and Jatin Singh

## Abstract

MSMEs are considered to be the most important contributor to the Indian economy. It is responsible for creating more than 50% jobs in India. With coronavirus reaching a pandemic level threat and India having the 2<sup>nd</sup> largest population, it is inevitable for the MSME system to derail off track. In this study we analyze the different factors and challenges that have been pulling down the MSMEs. Nationwide lockdown is also not helping the already faltering MSME sector. The lockdown has changed the dynamics of market and several measures are adopted by the government to provide relief to the MSME sector. This study aims to provide alternative strategies to cope with the COVID-19 crisis and revive the MSME sector

## 1. Introduction

The novel coronavirus or COVID 19 outbreak started in Wuhan, China and has till now infected all the continents including Antarctica (in December, 2020). India registered its first ever COVID 19 infection which was reported in Kerala on 27<sup>th</sup> January 2020. As of 1<sup>st</sup> May 2021 India has reported approximately 19.6 million cases in which close to 216,000 people have died due to the novel virus.

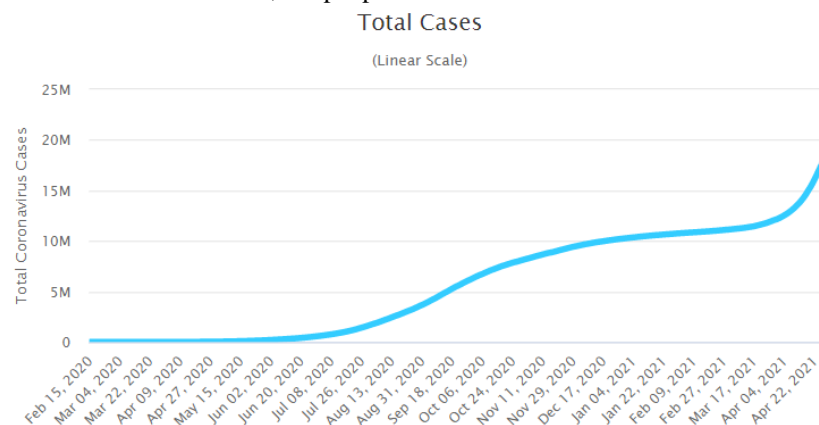


Fig.1 Linear Scale representation of COVID-19 cases in India

From Fig.1 we can observe an exponential growth rate of coronavirus infections in India. In response of the COVID 19 outbreak the Government of India has imposed strict lockdown procedures for states in order to minimize the spreading of this infectious virus. However, due to the lockdown, consumers shift their focus from luxury commodities to necessary commodities. This change in consumer behavior negatively effects the enterprises.

## Objectives of the Study

The research objectives intended to be covered through this paper are as follows –

- To provide an overview of the MSME industry in India
- To study the impact of COVID-19 outbreak on MSMEs in India
- To identify and study the challenges faced by MSMEs
- To list out strategies adopted by the government for MSMEs during pandemic

- To provide alternate strategies to mitigate the problems faced by MSMEs during the lockdown

## 2. Research Methodology

The study looks into the ramifications caused by pandemic on the functioning of MSMEs in India and its impact on them. It highlights the role of MSME as being an instrumental driver for the Indian economy. Descriptive methods are adopted to collect data from various published sources and websites. Different parameters like impact, barriers and challenges faced by MSMEs in India are discussed with the research and explanation of the data being more qualitative than quantitative.

## 3. Literature Review

Forecasting and prediction models have been used to predict the severity of the COVID-19 outbreak. One such study done in [1] uses Neural Network, Support Network Regression and Linear Regression models to predict and track the COVID-19 disease. The study uses publicly available dataset from the websites including <https://www.mygov.in/> and <https://www.pharmaceutical-technology.com/> which is further used to formulate the predictive forecasting model. The research integrates diverse predictive models in order to minimize the errors and increase precision.

Similarly other mathematical models were developed for analyzing the outbreak of coronavirus in India. In the research done in [2] a compartmental class of mathematical model is used that is known as Kermack-McKendrick Susceptible Infected Removed (SIR) model. This model divides the population into 3 compartments namely S (susceptible individuals), I (number of individuals infected) and R (individuals that have recovered and developed immunity to the infection). This model helps in computing the prediction of number of people infected with a contagious disease over time in a closed population. Forecasting is an essential step in calculating the impact of coronavirus on the MSMEs.

Other researches done in [3-4] provide key insight in the manufacturing sector, international trade and MSME sector post the COVID-19 outbreak. Even though the infectious virus proves to have a significant negative impact on the economy, the study suggests otherwise that India can capitalize on the change in the global perception of China's manufacturing sector following the virus outbreak and can emerge as the new global manufacturing giant.

Apart from India study has been conducted in other developing countries like Spain, Somalia, Pakistan and Malaysia. Studies conducted in [5-8] provide a comprehensive analysis of the influence COVID-19 has had on the SMEs operating in these states. They also show the different business survival strategies adopted by the SMEs to overcome the challenges posed by the spread of coronavirus and collapse of the market.

We can also look at [9] to further adopt crisis management strategies adopted by SMEs in Macau. Planning, Comprehensive Crisis Warning System, Leadership and HR, Timely Communication, Robustness and Flexibility are some of the major features that can inspire the Indian MSME sector to avert the COVID-19 crisis

## Overview of MSME sector in India

In 2006 Government of India introduced MSME or Micro, Small and Medium Enterprises in agreement with Micro, Small and Medium Enterprise Development (MSMED) Act. In 2018 an amendment was made in the Micro, Small and Medium Enterprise Bill to further redefine the definition of MSME and classify them on the basis of their turnover as manufacturing or service providing enterprises. According to the revised bill MSMEs include micro enterprises with annual turnover less than Rs. 5 crore, small enterprise

having turnover between Rs. 5 to 75 crore and medium enterprises having a market cap between Rs. 75 to 250 crore.

Classification	Manufacturing Enterprises*	Service Enterprises**
Micro	Rs. 2.5 million / Rs. 25 lakh	Rs. 1 million / Rs. 10 lakh
Small	Rs. 50 million / Rs. 5 crore	Rs. 20 million / Rs.2 crore
Medium	Rs. 100 million / Rs. 10 crore	Rs. 50 million / Rs. 5 crore

Fig. 1 Classification of Enterprises as Micro, Small and Medium

\*Investment limit in Plant and Machinery \*\*Investment limit in equipment

Source: MSME Annual report 2011-12 pp.316.

This sector creates employment for about 111 million individuals while also contributing about 45% to manufacturing output, more than 40% of exports and over 28% of the GDP as of the FY 2019. While MSMEs prove to be the major driving factor for the Indian economy, they often face various challenges that they need to overcome on their own or with the help of the government.

According to the NSS 73<sup>rd</sup> Round Survey (2015-16) on Micro, Small and Medium enterprises, there were 633.88 lakh unincorporated non agriculture MSMEs in the country. Figure 2 shows the distribution of MSMEs on the basis of their activity.

Activity Category	Rural (in lakhs)	Urban (in lakhs)	Total (in lakhs)	Share (%)
(1)	(2)	(3)	(4)	(5)
Manufacturing	114.14	82.5	<b>196.65</b>	<b>31</b>
Electricity	0.03	0.01	<b>0.04</b>	<b>0</b>
Trade	108.71	121.64	<b>230.35</b>	<b>36</b>
Other Services	102.00	104.85	<b>206.85</b>	<b>33</b>
All	<b>324.88</b>	<b>309.00</b>	<b>633.88</b>	<b>100</b>

Fig.2 Estimated Number of MSMEs (Activity Wise)

According to MSME industry reports from RBI, there is a need to identify components of the MSME ecosystem in order to draft policies and form decisions. The seven pillars of the MSME sector have been depicted in Figure.3 as shown below. All the existing and future policies related to MSME are aligned with these 7 pillars of MSME ecosystem.

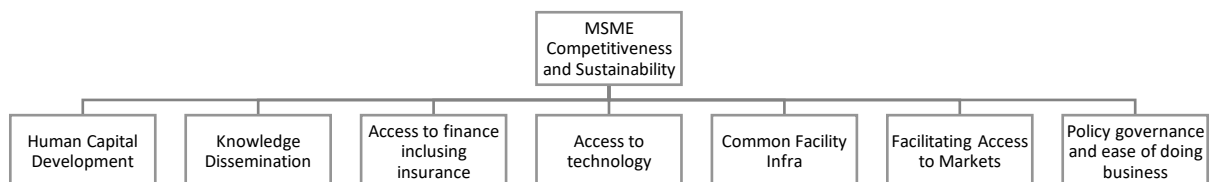


Fig.3 Seven Components of MSME Ecosystem

## Impact of COVID-19 outbreak on MSMEs in India

India having the 2<sup>nd</sup> largest population in the world has an evergreen demand for job creation. This huge demand is majorly fulfilled by the MSME sector which is also considered as the backbone of the Indian economy. However, COVID-19 has caused a disruption in the day to day activities and consumption patterns of India citizens. A brief study of the shift in paradigm of consumer behavior allows us to observe the ramifications of COVID-19 on MSME sector in India. Consumer behavior report provided in [10] suggest that consumer behavior will not follow a linear curve and it will take time to get back to the normal pre COVID-19 era.

We can observe a change in how consumers behave across the following 8 areas of life –

- **Work Life** – Rise of unemployment, Lack of job security and remote working are some of the prominent changes in the field.
- **Shopping and consumption** – Exponential increase in ecommerce, Increased preference for trusted brands, Decline in luxury shopping, Shift towards sustainable lifestyle, Shift to stores located close to home.
- **Education and Learning** – Online education is the new normal, Boom in e-learning platforms
- **Life at Home** – People will start recasting their homes as a new coffee shop, restaurant and entertainment center.
- **Media and Information** – Shift towards e-paper and digital media
- **Entertainment** – People start to shift from cinema to popular streaming platforms like Netflix, Hotstar, and Amazon Prime etc.
- **Travel and tourism** – Reduction in tourist spending and an increase in domestic tourism.
- **Health and wellbeing** – Focus on organic and high protein food products, Promotion of healthy lifestyle, Fitness on demand, increasing focus on personal hygiene.

From literature in [11], the nationwide lockdown has severely impacted the MSME sector in India. It has resulted in the choking up of the industry. The lockdown implemented by the government of India to prevent the spread of the novel virus has affected the MSME industry adversely. Figure 3 lists some of the major impacts of the lockdown.

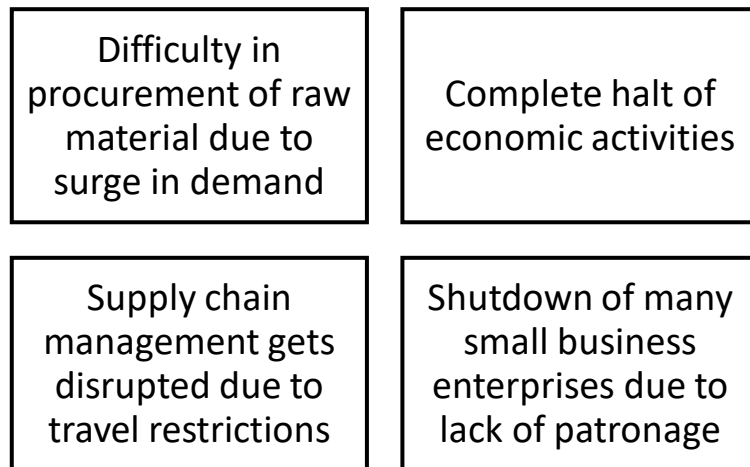


Figure 3. Impact of nationwide lockdown on MSMEs

Most of the MSMEs are not registered anywhere due to the fact that they are too small. As always every scenario has two sides to it. These unregistered MSMEs are not legally bounded to pay taxes, maintain accounts and adhere to regulatory norms as they lie outside the legal framework. But this keeps them out of the government radar who are provide subsidies and concessions at a time of crisis like this one. Another big issue faced by the MSMEs in India is financing. Most of the MSMEs derive their funding from informal sources which does not provide them security in case of a pandemic. Last but not the least, delay in payments is also one of the major issues plaguing this sector. Delay in payments can be from the side of the buyer or GST refunds or both. This only shows that MSME sector in India is very vulnerable and fragile. Although it has a potential to significantly boost India's economy, it can however play an equally instrumental role in collapsing the entire economy too. [12]

### Challenges faced by MSMEs

As per the survey and research conducted in [13] we can list the barriers hindering the growth of MSMEs in India -

- Lack of Human Resource Management
- Lack of Financing
- Lack of Market Research
- Improper government policies and procedures
- Lack of planning and strategy making
- Lack of infrastructure and technological know-how
- Lack of entrepreneurship and managerial skills

The above mentioned factors play a key role in the hindrance of growth of the enterprise by affecting different performance factors like product performance, innovation performance and sales performance.

We further observe the first hand challenges faced by owners of MSMEs through case study research done in [14]. It states that obstacles and challenges faced by MSMEs can come from internal and external environment. Internal environment problems include HR competencies, capital and production machinery while that of external environment revolve around marketing, production competitiveness and optimal utilization of information technology.

Meanwhile Official reports from [15] show 6 major challenges faced by the MSME due to the pandemic as can be seen in Figure 4.

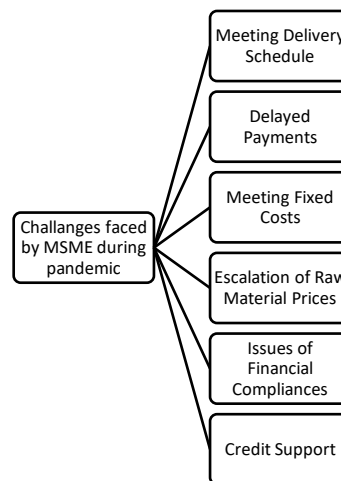


Fig.4 Challenges faced by MSMEs during COVID-19 pandemic

### Initiatives adopted by government to revive MSMEs affected by pandemic

The government of India had laid down Standard Operating Procedure (SOP) for MSMEs at workplace in order to promote functionality of the enterprises that work on a small scale and avoid a chaotic collapse of this industry. An important revival framework can be studied from [16]. It mentions that the government had announced collateral free loans to MSMEs and will be fully guaranteed by the government. These loans have a tenure of 4 years and the scheme available till 31<sup>st</sup> October 2020. An amount of 3 lakh crore has been allotted for the same by the Government of India. A partial credit guarantee scheme has also been announced to help MSME units to increase their equity for which a sum amounting to Rs. 20,000 crore will be transferred through the Credit Guarantee Fund Trust for Micro and Small Enterprises (CGTMSE).

On the other hand Non-Banking Financial Companies and micro finance institutions are finding it difficult to raise debt capital due to lack of confidence of consumers in the current market. The government has hence provided a special liquidity scheme of Rs. 30,000 crore to revive the low confidence cycle in the market for lending to the above category of borrowers.

To counter the challenges mentioned in the previous section, the Government of India has stated its policy advocacies in [15]. The proposed action is stated for each corresponding challenge faced by the MSME sector can be observed from Figure 5.

Challenge	Proposed Action
Meeting Delivery Schedule	Ministries have approached PSUs to allow relaxation in applicability of LD clause for a time span of 2 months from the scheduled date of delivery
Delayed Payments	Railway board to be approached for intervention and immediate release of all pending payments by railways and other authorities
Meeting Fixed Cost	State government to be held accountable for making exempt or reimburse the electricity and other fixed charges during this period
Escalation of Raw Material Prices	Communicate with ministry of finance to reduce the GST rates on raw materials in order to compensate for price inflation of raw materials
Issues of Financial Compliances	Department of Revenue to provide suitable relief measures
Credit Support	Department of Revenue and Department of Finance to be approached to provide suitable relief measures

Fig.5 List of Proposed Actions taken by government

### Mitigation Strategies to cope with COVID-19

According to our study and annual reports following strategies can be adopted to curb the ongoing distress in the MSME sector –

**Advancement in Research and Development** - Appropriate investment should be made in the Research and Development sector of India in order to come up with innovative technology to fight COVID-19 and keep the market functional.

**Increasing General Awareness related to new policies** - New policies and relief measures formulated by the government should be advertised properly in order to make people aware about it. The policies would not be effective if they are not being used by the people due to lack of awareness.

**Survey and Research** - Surveys should be conducted on a regular basis to identify the missing links and provide relief on a timely basis to the MSME sector. This will aid the government in making proper arrangements for the MSMEs in order to fulfill their needs.

**Setup a panel of consultants** - A panel of industry experts should be set up as consultants to help guide the government towards better and effective strategies. The panel can also help in formulating innovative strategies and their long industry driven experience can provide key insights to the problems faced by the MSMEs.

## Conclusion

MSMEs have been at the heart of impact of COVID-19. To revive the faltering Indian economy, it is important to keep a check on the MSME sector. Both short term and long term policies should be formulated and implemented with regard to all the MSMEs. The performance of MSMEs still remains one of the most instrumental factors affecting the GDP of India. The government needs target tiny micro enterprises and get them registered. This will make them available for all the relief schemes proposed by the government and it will also ensure a transparency in the system. MSMEs have a long grueling journey ahead but timely action and adopting risk mitigation strategies can help overcome this. With the COVID-19 crisis at head and with no foreseeable end, enterprises and communities must stand together and help each other in order to avoid a further collapse of market. Strategies must be formulated and implemented quickly that are applicable to masses and effective to avoid any unnecessary slump in economic sector.

## REFERENCES

1. Ogundokun, Roseline & Bamidele, Awotunde. (2020). MACHINE LEARNING PREDICTION FOR COVID 19 PANDEMIC IN INDIA. 10.1101/2020.05.20.20107847.
2. Tewari, Amit. (2020). Temporal Analysis of COVID-19 Peak Outbreak. 10.1101/2020.09.11.20192229.
3. Sahoo, P., & Ashwani. (2020). COVID-19 and Indian Economy: Impact on Growth, Manufacturing, Trade and MSME Sector. *Global Business Review*, 21(5), 1159–1183. <https://doi.org/10.1177/0972150920945687>
4. Singh, Anukarsh, What About India's MSME Sector: COVID-19 Pandemic and Indian MSME Sector Outlook (June 12, 2020). Available at SSRN: <https://ssrn.com/abstract=3696778> or <http://dx.doi.org/10.2139/ssrn.3696778>
5. Pedauga, L., Sáez, F. & Delgado-Márquez, B.L. Macroeconomic lockdown and SMEs: the impact of the COVID-19 pandemic in Spain. *Small Bus Econ* (2021). <https://doi.org/10.1007/s11187-021-00476-7>
6. Warsame, Abdulkadir. (2020). The Impacts of COVID 19 on Small and Medium Enterprises. 12. 10.7176/EJBM/12-25-11.
7. Shafi, M., Liu, J., & Ren, W. (2020). Impact of COVID-19 pandemic on micro, small, and medium-sized Enterprises operating in Pakistan. *Research in Globalization*, 2, 100018. <https://doi.org/10.1016/j.resglo.2020.100018>
8. Rafliis, Ahmad & Ishak, Suraiya & Jusoh, Mohd. (2020). The impact of Covid-19 Movement Control Order on SMEs' businesses and survival strategies. *Malaysian Journal of Society and Space*. 16. 10.17576/geo-2020-1602-11.

9. ALVES, J. C., LOK, T. C., LUO, Y., & HAO, W. (2020). Crisis Management for Small Business during the COVID-19 Outbreak: Survival, Resilience and Renewal Strategies of Firms in Macau. Research Square. <https://doi.org/10.21203/rs.3.rs-34541/v1>
10. Kohli, S., Fabius, V. and Timelin, B., 2020. How COVID-19 is changing consumer behavior—now and forever. [online] Available at: <<https://www.mckinsey.com/industries/retail/our-insights/how-covid-19-is-changing-consumer-behavior-now-and-forever#>> [Accessed 4 May 2021].
11. Roy, A., Patnaik, B. C. M., & Satpathy, I. (2020). Impact of Covid-19 crisis on Indian MSME sector: A study on remedial measures. Eurasian Chemical Communications, 2(9). <https://doi.org/10.22034/ecc.2020.114672>
12. The Indian Express, e-paper: <https://indianexpress.com/>
13. Sharma, Rajiv & Kharub, Manjeet. (2015). Qualitative and quantitative evaluation of barriers hindering the growth of MSMEs. International Journal of Business Excellence. 8. 724-747. 10.1504/IJBEX.2015.072307.
14. Sugiarto, Irwan. (2018). Obstacles and Challenges in the Development of MSMEs: Case Study. Budapest International Research and Critics Institute (BIRCI-Journal) : Humanities and Social Sciences. 1. 93-98. 10.33258/birci.v1i4.97.
15. Ministry of Micro, Small and Medium Enterprises, GoI: <https://msme.gov.in>
16. Dr. Esra, Sipahi. (2020). COVID-19 and MSMEs: A Revival Framework. 1. 7-21.
17. The Economic Times, e-paper: <https://economictimes.indiatimes.com/>
18. Official website of Reserve Bank of India