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Restarting India | Fiscal measures 2.1

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Measures announced in India's fight against COVID-19: 13 May 2020

Following the Prime Minister's announcement on 12 May 2020 of a special economic and comprehensive package of INR 20 trillion (~US$ 267 billion)[1] (~ 10% of India's GDP) and the call for building a self-reliant India, the Finance Minister, in a press conference held on 13 May 2020, announced several measures aimed at supporting Micro Small and Medium Enterprises (MSMEs), Non-Banking Finance Companies (NBFCs), Housing Finance Companies (HFCs), Micro Finance Sector, Real Estate and Power Sector, with specific focus on infusing liquidity where it is most needed.

This is the first of several measures proposed to be announced in the next few days. Deloitte has summarized the key features of these announcements below:

Businesses and MSMEs

Automatic collateral free loans: INR 3 trillion (~ US$ 40 billion)

- **What:** Emergency credit line to businesses / MSMEs from banks and NBFCs, up to 20% of the outstanding credit as on 29 February 2020 for working capital requirement
- **Eligibility**: This facility will be available to units with up to INR 250 million (~ US$ 3.3 million) outstanding credit and turnover of up to INR 1 billion (~ US$ 13.33 million) whose accounts are classified as standard.
- **Form**: This will be in the form of a Term Loan at a concessional rate of interest provided by banks and NBFCs. The tenure of the loans will be 4 years with moratorium of 12 months on principal repayment.
- **Credit enhancement**: 100% credit guarantee cover will be given to Banks and NBFCs providing such loans. No additional collateral or guarantee fees are to be paid.
- **Validity**: Till 31 October 2020.

Comment:

The measure should enhance ability of banks and NBFCs to lend to businesses / MSMEs given the sovereign backing to such debt. The measure will also improve the overall quality of lending by banks / NBFCs and bring in much needed liquidity. The government's own outgo is back-ended in the eventuality that the borrower ultimately fails or defaults.

Subordinated debt for MSMEs: INR 200 billion (~ US$ 2.67 billion)

- **What**: Debt to be facilitated by the government as subordinated debt.
- **Eligibility**: For MSMEs that are stressed / NPAs; Promoters of such MSMEs will be lent by banks and the loan shall be infused into the company by promoters as equity.
- **Form**: Loan by banks. Up to 15% equity in a promoter's business subject to a maximum of INR 7.5 million.

[1] USD-INR rate considered as 1 USD = 75 INR

- **Credit enhancement**: The government will provide INR 40 billion (~US$ 533 million) to the Credit Guarantee Trust for Micro and Small Enterprises (CGTMSE). CGTMSE to provide partial credit guarantee support to banks.

Comment:

The move will protect those MSMEs that show signs of being able to revive despite being categorised as NPA. The measure will also protect jobs and prevent insolvencies in the near term. The lending by banks will have to be more careful and measured, so that the problem is addressed and not merely postponed. The actual outflow appears to be INR 40 billion (~US$ 533 million) upfront with the remainder being a guarantee and hence back-ended through CGTMSE.

Fund of funds for MSMEs: INR 500 billion (~ US$ 6.67 billion)

- **What**: Equity funding to MSMEs
- **Form:** Fund of Funds (FoF) will be set up by the government with a corpus of INR 100 billion (~US$ 1.33 billion) that will provide support to MSMEs in the form of equity. FoF will operate through a holding fund and few subsidiary funds. Leveraging of INR 500 billion (~ US$ 6.67 billion) will be done at the subsidiary fund level.

Comment:

This initiative is akin to the National Infrastructure Investment Fund (NIIF) which had been set up in 2015 to accelerate investment into Indian infrastructure. Since its inception, NIIF has been able to attract strong interest from investors and has built partnerships in the infrastructure space. This can also be an opportunity to display the healthy partnership among corporates, Indian government and other governments / Pensions Funds / Sovereign Wealth Funds, etc.

The funding will still be equity in nature and of long gestation; it would take longer time to execute and implement.

Relook at the MSME definition:

Classification	Micro	Small	Medium
Existing MSME classification			
Manufacturing	Investment <INR 2.5 million (~ USD 33,000)	Investment < INR 50 million (~ USD 667,000)	Investment < INR 100 million (~ USD 1.3 million)
Services	Investment < INR 1 million (~ USD 13,000)	Investment < INR 20 million (~ USD 267,000)	Investment < INR 50 million (~ USD 667,000)
Revised MSME classification			
Manufacturing and Services	Investment < INR 10 million (~ USD 133,000) and Turnover < INR 50 million (~ USD 667,000)	Investment < INR 100 millio (~ USD 1.3 million) and Turnover < INR 500 million (~ USD 6.67 million)	Investment < INR 200 million (~ USD 2.67 million) and Turnover < INR 1 billion (~ USD 13.33 million)

Suitable amendments will be made in the MSME Act.

Comment:

Wider coverage of units under the revised definition of MSME is a positive step.

Market access measures for Indian companies and MSMEs:

- e-market linkage for MSMEs will be promoted to act as replacement for trade fairs and exhibitions
- MSME receivables from government and Central Public Sector Enterprises will be released in 45 days
- Global tenders will be disallowed in government procurement tenders up to INR 2 billion (~ US$ 26.67 million). Such measure is aimed at supporting 'Make in India' initiative and will increase business for MSMEs.

Employee Provident Fund (EPF) support for business and organized workers

- **What:** Under Pradhan Mantri Garib Kalyan Package (PMGKP), payment of 12% of basic salary (as employer and employee contributions) was made into EPF accounts of eligible establishments for March, April and May 2020.
- **How:** This support has been extended for another three months for the months of June, July and August 2020.

EPF Contribution to be reduced for Employers and Employees for 3 months

- **What:** With a view to provide more liquidity and to ensure more take-home salary for employees and in order to give relief to employers in the payment of PF dues, the statutory PF contribution of both the employer and employee is reduced to 10%, from existing 12%, for all establishments covered by EPFO for the next three months.
- Once the amendments in PF laws are notified, it would be clear whether a choice will be available to continue with the old PF contribution rate (12%) for those who would like to maintain status quo. In case of those employers, where contribution to PF is included as part of the employee's "Cost-to-company" package (CTC) and where the employer has otherwise not made any cuts to fixed pay, the employees may expect to be compensated for this reduction in PF contribution by way of a taxable cash allowance.
- **Eligibility:** Scheme will be applicable for workers who are not eligible for 24% EPF support under PM Garib Kalyan Package and its extension.

Comment:

The above measures aim at putting more cash in the hands of employees while reducing some cost for their employers. Further, such measures will form yet another mechanism to infuse funds into the system while not directly impairingretirement benefits available to individuals. However, it will lead to increase in tax liability in the hands of employees.

Special Liquidity Scheme for Non-Banking Finance Companies (NBFCs), Housing Finance Companies (HFCs) and Micro Financial Institutions (MFIs)

- **What:** Government will launch an INR 300 billion (~ US$ 4 billion) Special Liquidity Scheme.
- **Eligibility:** NBFCs, HFCs and MFIs
- **Form:** Investments will be made through primary and secondary market transactions, in investment grade debt paper of NBFCs/HFCs/MFIs, which will be fully guaranteed by the government. Such a move will supplement other measures by RBI and the government to enhance liquidity in the economy.

Comment:

This could be a substantial route to improve liquidity and encourage lending. With INR 300 billion (~ US$ 4 billion) categorised as government paper, the move could help improve lenders' balance sheets and that of the overall health of institutions, including banks and mutual funds and even possibly public borrowers, if the instruments are held by the public and such instruments are eligible to participate in this scheme. However, the modalities on how primary transactions will work, needsto be seen.

Partial credit guarantee scheme 2.0 for liabilities of NBFCs/MFIs: INR 450 billion (~ US$ 6 billion)

- **What:** Existing Partial Credit Guarantee Scheme will be revamped and will be now extended to cover borrowings, such as primary issuance of bonds/ commercial paper (CPs)
- **Eligibility:** AA rated or lower rated NBFCs, HFCs and MFIs, including unrated paper
- **Form:** The Government will provide 20% first loss guarantee

Comment:

Such a measure should provide relief to public sector banks

It changes the profile of borrowers immediately and can also change provisioning requirements. This can add to regulatory capital and release further liquidity into the system. Once risk has been passed on to the government, the paper could trade as a sovereign paper.

Liquidity injection for Power Distribution Companies (DISCOMs): INR 900 billion (~ US$ 12 billion)

- **What:** Purchase of receivables of DISCOMS for cash
- **Eligibility:** It is expected that this amount will be used by DISCOMS to pay their outstanding dues to transmission and generation companies. Central Public Sector Generation Companies shall offer rebate to DISCOMS which will pass-on benefits to end customers (i.e. industries) as relief towards fixed charges.
- **Form:** Funds equivalent to INR 900 billion (~ US$ 12 billion) shall be infused into DISCOMS in tranches, through Power Finance Corporation and Rural Electrical Corporation, to acquire receivables owed to such DISCOMs.
- **Credit enhancement**: State guarantees

Comment:

This scheme will provide liquidity to DISCOMS and to generation companies and other downstream units.

Relief to Contractors

- Relief to contractors by way of extension of up to 6 months, for completion of contractual obligations of central agencies such as Railways, Ministry of Road Transport and Highways, Central Public Works Dept., etc., including in respect of EPC and concession agreements.
- Government agencies shall partially release bank guarantees of contractors, to the extent that contracts are partially completed, to ease cash flows.

Relief to Real Estate

- Relief to be provided by state governments by way of extension of up to 6 months for registration and completion date suo-moto of all RERA-registered real estate projects expiring on or after 25 March 2020. This may be further extended by another 3 months based on the situation in the state.
- COVID-19 to be considered as an event necessitating invocation of the *'force majeure'* clause under RERA. It is also proposed to extend timelines for various statutory compliances under RERA.

Comment:

The move is expected to provide clarity on existing timelines and help avoid subsequent litigation.

The relief package introduced by the Government is the need of the hour. This may lead to various benefits to start-ups as well as businesses which satisfy the expanded definition of MSMEs; in order to recuperate their businesses in this unprecedented situation and its aftermath.

The revision in the criteria for MSMEs and elimination of distinction between service and manufacturing sectors will cover a wider section of start-up businesses and the relief measures could certainly boost the marginal businesses by: (a) reducing burden of additional cash outflow; (b) getting easy financial assistance and (c) result in a higher take home salary for its workers; etc.

Therefore, small scale start-ups/ promoter based businessess segments will be benefited at large.

However, there are certain ambiguities in the above measures and a detailed clarification/ understanding of these measures in terms of eligibility criteria, applicable conditions, procedures, point of contacts, etc. from the government could help foster the implementation of the measures in a smooth and speedy manner.

Source: Press Release issued by Ministry of Finance dated 13 May 2020.

The Finance Minister also announced certain tax reliefs. The link to our alert on these announcements is here.

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