

Govt needs to strengthen State Finance Corporations to promote MSME credit

State Finance Corporations (SFCs) play an important role in meeting the financial needs of micro and small enterprises, including first generation entrepreneurs across various states. The role of these corporations assumed special importance in the current circumstance, when the pandemic and the subsequent lockdown posed an existential crisis for most MSMEs. These corporations support micro and small entrepreneurs by offering temporary respite from loan repayment, extending additional loan facility on concessional terms.

There are around 18 SFCs across different states that have been established under State Financial Corporations Act, 1951. These corporations have been notified as 'Public Financial Institutions' under Section 4-A of the Companies Act by the Government of India. These corporations were set up after the establishment of the first Development Finance Corporation, Industrial Finance Corporation of India, in 1948.

In order to strengthen the lending capacity of State Finance Corporation, Reserve Bank of India, the central and state governments should take various measures. In this regard, it is worth considering the suggestions of the Council of State Industrial Development and Investment Corporations of India (COSIDICI), which is the federation of state-level financial and investment corporations.

According to COSIDICI, Reserve Bank of India should treat lending by scheduled commercial banks to SFCs as priority sector lending (PSL). This is because State Finance Corporations use the funds borrowed from scheduled commercial banks for on-lending to micro and small enterprises, who are the target beneficiaries of the RBI's PSL norms. Until 2011, RBI allowed banks to classify their advances to State Finance Corporations under PSL. However, through a circular on July 05, 2011, RBI disallowed this practice. It is learnt that State Finance Corporations borrow funds from scheduled commercial banks for on-lending to micro and small enterprises and they also furnish the list of such borrowers to scheduled commercial banks. In this backdrop, COSIDICI has opined that RBI may restore the old practice of allowing banks to classify lending to SFCs as priority sector lending after considering the viability, financial position and end use of funds by SFCs.

COSIDICI also feels that Reserve Bank of India should relax guidelines for recognizing Non Performing Assets (NPAs) of State Finance Corporations. According to COSIDICI, State Finance Corporations should not be subject to the same NPA guideline, which is applicable to scheduled commercial banks as the nature of lending activity conducted by both the organisations are different. While State Finance Corporations lend exclusively for micro and small enterprises, including first generation entrepreneurs, who are considered risky, scheduled commercial banks extend loans to small, large and big corporate sector, including retails consumers. Thus,

scheduled commercial banks can hedge the credit risk by diversifying their loan portfolio, which is not the case with State Finance Corporations. Therefore, there is a need to introduce differentiated regulation on NPAs for State Finance Corporations, COSIDICI feels. Specifically, the RBI may reduce the risk weights and capital adequacy norms for State Finance Corporations so that these entities have higher capital to meet the borrowing needs of small entrepreneurs. Reducing the risk weight will reduce the amount of capital to be set aside against risky loans by these Corporations and hence make greater amount of capital available for lending.

COSIDICI has also made other suggestions to strengthen the capacity of State Finance Corporations to meet the credit needs of MSMEs. Some of these suggestions include: provision of additional capital by state governments to their State Finance Corporations and providing interest subsidy for loans extended by State Finance Corporations. Government of India can also set up a dedicated fund for MSME credit and State Finance Corporations can be declared implementing agencies for this fund.

Notifications

PIB

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<https://www.pib.gov.in/PressReleasePage.aspx?PRID=1686252>

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<https://www.pib.gov.in/PressReleasePage.aspx?PRID=1686172>

Indian Railways launches Freight Business Development Portal

<https://www.pib.gov.in/PressReleasePage.aspx?PRID=1686228>

CBIC

CBIC rescinds the Customs (Advance Rulings) Rules 2002

<https://www.cbic.gov.in/resources//htdocs-cbec/customs/cs-act/notifications/notfns-2021/cs-nt2021/csnt02-2021.pdf>



Customs Authority for Advance Rulings Regulations, 2021

<https://www.cbic.gov.in/resources//htdocs-cbec/customs/cs-act/notifications/notfns-2021/cs-nt2021/csnt01-2021.pdf>