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A Principles-based Evaluation of Public MSME Credit Guarantee Schemes in India

Madhu Srinivas & Deepti George[1], Financial Systems Design, Dvara Research

Summary:

In this policy brief, we evaluate the design and operation of the public credit guarantee schemes for MSMEs present in India, the Credit Guarantee Fund Trust for Micro and Small Enterprises (CGTMSE) and the Credit Guarantee Fund for Micro Units (CGFMU), against the principles developed by the World Bank Group (WBG) and Financial Sector Reform and Strengthening (FIRST) Initiative for Public Credit Guarantee Schemes for MSMEs. Our evaluation reveals substantial gaps in the design and operation of these schemes along the dimensions of transparency, risk management, autonomy, and supervision when compared against the World Bank's principles. Drawing on insights from the evaluation, we conclude with some policy actions that the Government can take to strengthen these schemes, especially in light of the catalytic role played by these guarantee schemes in enabling credit access to MSMEs.

About Financial Systems Design Initiative:

The Financial System Design Initiative (FSD) within Dvara Research aims to build and further the vision of a well-functioning financial system for India that is built on three fundamental pillars: High Quality Origination, Orderly Risk Transmission, and Robust Risk Aggregation. Our mandate is to undertake research around extant and emerging themes, gaps, and risks in financial sector policy, and recommend regulatory responses, keeping in mind the need to increase meaningful financial access and depth in a manner that enhances systemic stability.

[1]The authors work with Dvara Research. Corresponding author's e-mail: madhu.srinivas@dvara.com

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1. Introduction

Micro, Small and Medium Enterprises (MSMEs) form a significant part of the Indian economy. They contribute to more than 30% of the country's GDP[2] and employ more than 11 Crore people[3]. Despite occupying a central place in the economy, SMEs face significant barriers in accessing credit. The credit market for MSMEs is plagued with market failures like information asymmetries, high transaction costs and lack of recognised collateral[4]. One way to mitigate this is through implementation of Credit Guarantees Schemes (CGS). A CG is a third party credit risk mitigant to lenders which absorbs a portion of the lender's losses on loans[5]. The CGS can also facilitate access to credit in two additional ways – 1. By expanding the information available on MSME borrowers; 2. By strengthening the risk management capacity of the lenders[6]. Most importantly, such schemes can be used to facilitate counter-cyclical financing to MSMEs during an economic downturn or credit crunch, like the present COVID crisis[7]. Considering the important role MSMEs play in the economy, governments worldwide have stepped in to provide such guarantees to ensure the sustenance and development of this sector[8].

India has 2 publicly funded CG schemes for MSMEs – Credit Guarantee Fund Trust for Micro and Small Enterprises (CGTMSE) and the Credit Guarantee Fund for Micro Units (CGFMU). The CGTMSE was launched by the Government of India (GOI) to strengthen the credit delivery system and facilitate the flow of credit to the MSME sector[9]. It aims to accomplish its objective by providing partial credit guarantees to eligible MSME loans originated by lending institutions[10]. The CGFMU was launched with the broad objective of guaranteeing loans sanctioned by financial intermediaries engaged in providing credit to eligible micro businesses[11]. In this piece, we evaluate the design and operation of these schemes against the principles developed by World Bank Group (WBG) and the Financial Sector Reform and Strengthening (FIRST) Initiative for public Credit Guarantee schemes for MSMEs[12]. Drawing on insights from the evaluation, we conclude with some policy actions that the Government can take to strengthen these schemes, especially in light of the recent COVID measures.

2. The World Bank Principles for Public Credit Guarantee Schemes

2.1. Objective and Scope

In January 2015, the WBG and the FIRST Initiative convened a global Task Force to identify and draft principles for the design, implementation, and evaluation of public CGSs to improve access to finance for SMEs. The Task Force developed these principles through consensus and consultations with several stakeholders, including central banks, CGSs and international organisations like the European Investment

[2]Section 2.1 MSME Annual Report 2020-21
[3]Section 2.2.4.1 Ibid
[4]Section 7.3 Report of the Expert Committee on Micro, Small and Medium Enterprises, RBI, June 2019
[5]The World Bank and FIRST Initiative. 2015. Principles for Public Credit Guarantee Schemes for SMEs. Washington, DC: World Bank
[6]Ibid, Part I Section I
[7]It should be noted here that the focus of this paper is not the Emergency Credit Line Guarantee Scheme (ECLGS), that provides 100% guarantee coverage, announced in FY2021, as part of the Atmanirbhar scheme, by the Government, but the partial credit guarantee schemes operated by the Government.
[8]Part I Section I, The World Bank and FIRST Initiative. 2015. Principles for Public Credit Guarantee Schemes for SMEs. Washington, DC: World Bank
[9]https://www.cgtmse.in/Home/VS/3 - Retrieved on 10-06-2021
[10]https://www.cgtmse.in/# - Retrieved on 10-06-2021
[11]CGFMU Gazette Notification, Ministry of Finance (Department of Financial Services) Notification, S.O. 1443(E) – April 2016
[12]Section II, The World Bank and FIRST Initiative. 2015. Principles for Public Credit Guarantee Schemes for SMEs. Washington, DC: World Bank

Banking Group. The principles seek to enhance the stability and inclusiveness of the global financial system. The report of the Task Force, hereafter referred to as the WBG report, outlining the principles and the methodology for assessing the implementation of the principles, was published by the WBG[13].

The rationale underlying these principles is to achieve economic and financial additionality in a financially sustainable manner. Economic additionality here refers to an increase in the economic welfare due to the mitigation of market failures by the CGS' operations, while financial additionality refers to increased availability of capital for MSMEs due to the operations of the CGS[14]. Thus, the principles, while recognising the welfare nature of CGS, also underline the importance of adequate funding, effective risk management and operational efficiency to ensure sustained outcomes.

2.2. The Principles

There are 16 principles that are spread across four dimensions[15] –

1. Legal and Regulatory Framework
2. Corporate Governance and Risk Management
3. Operational Framework
4. Monitoring and Evaluation

These principles lay down criteria covering the legal nature and objectives of the CGS, funding sources, risk management system and disclosures. An important point to be noted here is that these principles by themselves do not make a case for the establishment of public CGS. As mentioned earlier, the CGS is one way of overcoming market failures in a credit market. Thus, these principles come into focus only after a decision has been made to establish a CGS.

3. The Indian Context

3.1. Public CGS in India

India has 2 public CGSs for MSMEs – CGTMSE and CGFMU. The CGTMSE was launched in 2000 by the Government of India (GOI) and Small Industries Development Bank of India (SIDBI) as a trust to implement the CGS for Micro and Small enterprises with an initial corpus of Rs. 2500 Cr[16]. More contributions were made over the years, and the corpus amount stood at Rs. 7500 Cr as of March 2020[17] (See Figure 1). Similarly, for CGFMU, the available corpus stood at Rs. 2665.83 Cr of March 2020 (See Figure 2)[18]. The cumulative amount of guarantees sanctioned under CGTMSE was Rs 2.21 Lakh Cr as of March 2020[19] (See Figure 3). In terms of operations, the CGTMSE is a borrower level CG facility with CGTMSE approving individual loan applications for guarantee[20].

[13]Ibid
[14]Ibid, Section III
[15]Ibid
[16]CGTMSE Annual Report – 2019-20
[17]Ibid
[18]Respective NCGTC Annual Reports. The corpus fund value for FY 2018 has been assumed to be the same as FY17 as no fund infusion was made.
[19]CGTMSE Annual Report – 2019-20, Author's calculations
[20]CGTMSE Scheme Document

The CGFMU is a relatively new scheme which commenced its operations only in January 2017 and is operated by the National Credit Guarantee Trustee Company Limited[21]. It was started to provide guarantees for loans extended under the Pradhan Mantri Mudra Yojana (PMMY)[22]. As of 2020, the cumulative amount of guarantees sanctioned under CGFMU stood at Rs. 94216 Cr[23] (See Figure 4). Unlike CGTMSE, CGFMU is a portfolio level guarantee scheme where the Member Lending Institution (MLI) submits a portfolio of loans for guarantee cover[24].

Figure 1: Fund Infusion by SIDBI and GOI, CGTMSE

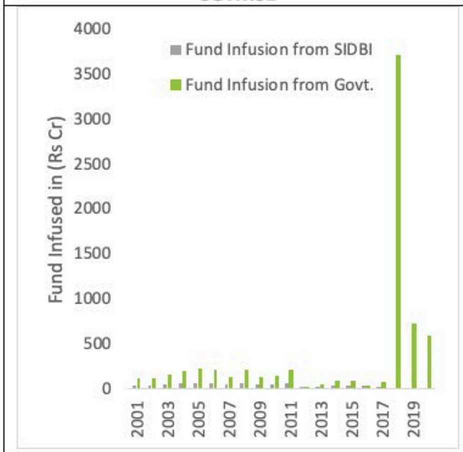


Figure 2: Available Corpus for CGFMU

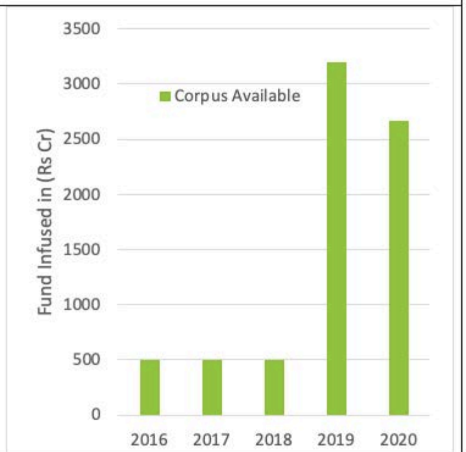


Figure 3: Cumulative Sanctioned Amount under Guarantee - CGTMSE (R. '000 Cr)

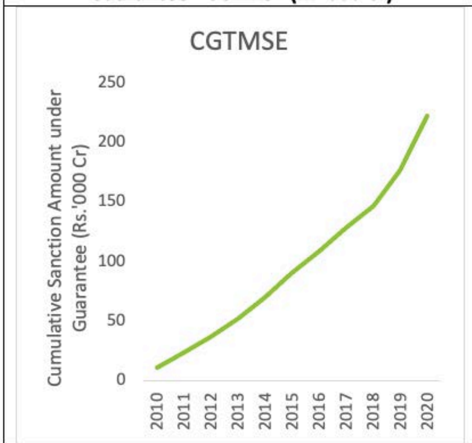
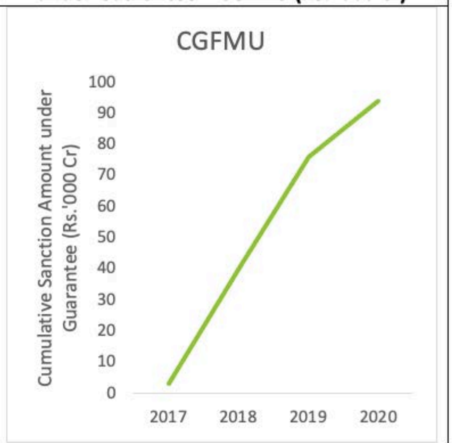


Figure 4: Cumulative Sanctioned Amount under Guarantee – CGFMU (Rs. '000 Cr)



[21]NCGTC Annual Report – 2019-20
[22]CGFMU Gazette Notification, Ministry of Finance (Department of Financial Services) Notification, S.0. 1443(E)
[23]NCGTC Annual Report – 2019-20
[24]CGFMU Gazette Notification, Ministry of Finance (Department of Financial Services) Notification, S.0. 1443(E)

While there is some overlap in the target segment of the two CG schemes, the respective scheme notifications explicitly bar loans covered under one scheme from being covered under the other. Also, the CGFMU is restricted to only PMMY loans, while CGTMSE covers all MSME loans up to Rs. 2 Cr[25].

3.2. Evaluating CGTMSE and CGFMU

The 16 principles[26] outlined by World Bank cover both strategic and operational aspects of the design and functioning of public CG schemes. This piece adds to the extant literature on the evaluation of public CG schemes against the WB principles. Calice, 2016[27] uses a survey-based self-assessment approach to evaluate the implementation of the WB principles of 60 CG schemes, for SMEs, across 54 countries. However, India is not one of the countries surveyed. To that extent, this article fills a gap in the literature pertaining to India. In this article, we attempt to briefly evaluate the extent to which the design and functioning of CGTMSE and CGFMU are aligned with the eight principles, which, in our judgement, cover all the strategic aspects of the design and functioning of the CG schemes. We focus on the strategic principles as these have a continuing and long term impact on the ability of the CG scheme in achieving its intended objectives. These eight principles broadly cover the main design aspects relating to autonomy, risk management, supervision and transparency. It should be noted here that these principles are not completely mutually exclusive, and the implementation of some of these principles could mitigate the adverse effects caused by the non-implementation of others. For instance, the three principles under the Corporate Governance and Risk Management theme elaborate on the principle of separation of ownership and management that is mentioned in 3.2.1 (1). To that extent,

[25]The actual ceiling differs according to the type of MSME loan and the region of origination

[26]The 16 principles are –

1. The CGS should be established as an independent legal entity on the basis of a sound and clearly defined legal and regulatory framework to support the effective implementation of the CGS's operations and the achievement of its policy objectives.
2. The CGS should have adequate funding to achieve its policy objectives, and the sources of funding, including any reliance on explicit and implicit subsidies, should be transparent and publicly disclosed.
3. The legal and regulatory framework should promote mixed ownership of the CGS, ensuring equitable treatment of minority shareholders.
4. The CGS should be independently and effectively supervised on the basis of risk-proportionate regulation scaled by the products and services offered.
5. The CGS should have a clearly defined mandate supported by strategies and operational goals consistent with policy objectives
6. The CGS should have a sound corporate governance structure with an independent and competent board of directors appointed according to clearly defined criteria
7. The CGS should have a sound internal control framework to safeguard the integrity and efficiency of its governance and operations.
8. The CGS should have an effective and comprehensive enterprise risk management framework that identifies, assesses, and manages the risks related to CGS operations.
9. The CGS should adopt clearly defined and transparent eligibility and qualification criteria for SMEs, lenders, and credit instruments.
10. The CGS's guarantee delivery approach should appropriately reflect a trade-off between outreach, additionality, and financial sustainability, taking into account the level of financial sector development of the country.
11. The guarantees issued by the CGS should be partial, thus providing the right incentives for SME borrowers and lenders and should be designed to ensure compliance with the relevant prudential requirements for lenders, in particular with capital requirements for credit risk.
12. The CGS should adopt a transparent and consistent risk-based pricing policy to ensure that the guarantee program is financially sustainable and attractive for both SMEs and lenders.
13. The claim management process should be efficient, clearly documented, and transparent, providing incentives for loan loss recovery, and should align with the home country's legal and regulatory framework.
14. The CGS should be subject to rigorous financial reporting requirements and should have its financial statements audited externally
15. The CGS should periodically and publicly disclose nonfinancial information related to its operations
16. The performance of the CGS—in particular its outreach, additionality, and financial sustainability—should be systematically and periodically evaluated, and the findings from the evaluation publicly disclosed.

[27]"Calice, Pietro. 2016. Assessing Implementation of the Principles for Public Credit Guarantees for SMEs: A Global Survey. Policy Research Working Paper;No. 7753. World Bank, Washington, DC. © World Bank. https://openknowledge.worldbank.org/handle/10986/24834

implementing these three principles would mitigate the moral hazard outlined in 3.2.1 (1). However, the difference is that 3.2.1(1) also underlines the importance of statutory backing for the effective and stable functioning of the CGS.

In performing this evaluation, we note that this is not a comprehensive evaluation as it is restricted to only 8 of the total 16 principles and is based only on information available in the public domain.

3.2.1. Legal and Regulatory Framework

1."The CGS should be established as an independent legal entity on the basis of a sound and clearly defined legal and regulatory framework to support the effective implementation of the CGS's operations and the achievement of its policy objectives"

The CGTMSE is established as a fund trust with SIDBI and GOI contributing to the corpus[28]. Thus, it has a legal existence independent of the Government. However, all its trustees are Government appointees and are employees of GOI in some form or the other[29]. Thus, there is no explicit separation between Government control and management of the fund. In such an arrangement, there is no clear demarcation of the objectives of the CGs and the operational targets of the management. The Government can thus arbitrarily shift goal posts and undermine the operational independence of the institution, with no mechanism to ensure managerial autonomy and accountability. More importantly, it should be noted that the powers and objectives of CGTMSE are not backed by any statute. The lack of a clear and strong legal foundation for its governance and operation translates to a lack of clarity in accountability and permanence of the scheme.

The NCGTC is a private limited company wholly owned by GOI[30]. In addition to CGFMU, it acts as a common trustee for multiple guarantee funds, including non-SME focussed funds[31]. Similar to CGTMSE, the board of NCGTC comprises officers from GOI, Public Sector Banks (PSBs) and SIDBI (4 in number)[32]. There is also no explicit separation in roles between the Government as the owner and the manager of the entity. However, unlike CGTMSE, the government notification giving effect to CGFMU explicitly specifies the constitution of the management committee responsible for reviewing the scheme and on matters related to the fund[33]. Of the seven committee members, five are government officers, and the remaining two members are experts in the field to be co-opted by the committee.[34]

2. "The CGS should be independently and effectively supervised on the basis of risk-proportionate regulation scaled by the products and services offered"

Both CGTMSE and NCGTC are audited by the Comptroller and Auditor General (CAG)[35], and its officers are under the jurisdiction of the Central Vigilance Commission (CVC)[36]. However, the oversight of CAG and the CVC is restricted to only preventing misuse of funds and corruption. They do not regulate or supervise the corporate governance, financial and risk management aspects of the entities. Also, these entities are not subject to any regulation or supervision by any of the financial regulators. This is a significant lacuna in the management and supervision of these entities. A compliance audit report by CAG on CGTMSE, hereafter referred to as the CAG report, also highlighted the absence of a regulatory framework and the consequent

[28]https://www.cgtmse.in/Home/VS/3 - Retrieved on 10-06-2021
[29]https://www.cgtmse.in/Home/VS/36 - Retrieved on 10-06-2021
[30]https://www.ncgtc.in/en/about-us/organization - Retrieved on 10-06-2021
[31]Ibid
[32]NCGTC Annual Report – 2019-20
[33]CGFMU Gazette Notification, Ministry of Finance (Department of Financial Services) Notification, S.0. 1443(E)
[34]Ibid
[35]NCGTC Annual Report – 2019-20 and CGTMSE Annual Report – 2019-20. For CGTMSE the external auditor is appointed on the recommendation of the CAG
[36]See Section 8 of the CVC Act, 2003

risks of fund mismanagement[37]. Given that these entities actively engage with participants in the credit market in a substantial manner, they should be under the regulation and supervision of the RBI. This ensures that the entities are run as efficiently as possible while minimising risks to taxpayer money. In this regard, the RBI, being the regulator of banks and NBFCs, will be best placed to assess the risks that CGSs are exposed to and to design an appropriate regulatory and supervisory framework. It should be noted here that having an independent regulator and supervisor would mitigate much of the moral hazard pointed out in 3.2.1 (1). However, unless a strict separation of ownership and management is achieved, the CGSs would still suffer as they could be used to push populist schemes that undermine their financial viability or run counter to the objectives for which they were created.

3.2.2. Corporate Governance and Risk Management Framework

1."The CGS should have a clearly defined mandate supported by strategies and operational goals consistent with policy objectives"

While the objectives of CGTMSE and CGFMU are laid out explicitly[38], there is less clarity on the strategies and the operational goals that these entities seek to employ to achieve their stated objectives. The lack of a legal mandate, outlining their objects and powers, is one of the main reasons for this lack of clarity.

2. "The CGS should have a sound corporate governance structure with an independent and competent board of directors appointed according to clearly defined criteria"

The CGTMSE is a trust with all its trustees being officers of GOI. While NCGTC, being a private limited company, has almost all of its board members being officers of the GOI. Thus, the boards of neither company are truly independent. With regard to CGTMSE, the CAG report noted that the trust had not established an Audit Committee or a Risk Management Committee and also did not have a Chief Risk Officer[39]. Also, it is unclear if the persons are appointed to the board according to any pre-defined criteria, assessing their competency to manage the fund. However, as noted earlier, the managing committee of CGFMU needs to have two members who are experts in the field, though no qualification criteria have been set for assessing the competence of these experts.

3. "The CGS should have an effective and comprehensive enterprise risk management framework that identifies, assesses, and manages the risks related to CGS operations"

It is unclear if CGTMSE and NCGTC have a comprehensive enterprise risk management framework. Indeed, for CGTMSE, the CAG report noted that the present system of approval of guarantees is inadequate and does not take into consideration the financial capacity of the borrower, project feasibility or management ability of the borrower. It also noted that CGTMSE was approving guarantees solely on the basis of the appraisal done by the MLI without putting in place an adequate control system to minimise moral hazard by the MLIs[40]. The

[37]"There are no laws to regulate many aspects of the Trust like scope of operations, governance, capital and operating requirements, as well as their access to the state-owned funds.", and "..external supervision would provide a positive effect on the guarantee system, since it will reduce the risk of fund mismanagement." - Section 4.1.2.3, Report of the CAG, No. 10 of 2020 for the year ended March 2019, Compliance Audit Observations – Sep 2020

[38]https://www.cgtmse.in/Home/VS/3 - Retrieved on 10-06-2021 and CGFMU Gazette Notification, Ministry of Finance (Department of Financial Services) Notification, S.O. 1443(E) – April 2016

[39]"..the Trust has not established/ framed Audit Committee, Risk Management Committee, Human Resource Policy, etc. Also, there is no Chief Risk Officer for ensuring that risks relating to credit, market, operations and liquidity of the corpus fund are identified, assessed, managed, monitored and reported to the senior management and the Board." - Section 4.1.2.3, Report of the CAG, No. 10 of 2020 for the year ended March 2019, Compliance Audit Observations – Sep 2020

[40]"Approval/ issue of guarantees on this basis did not take into consideration the management of the borrower unit, technical feasibility of the project and financial capacity of the borrower/ promoters." and "The above shortcomings indicate lack of responsibility and accountability of the MLIs in appraisal of loan applications prior to sanction and disbursement of loans. As such, the Trust needs to put in place an adequate control system consisting of quantitative and qualitative criterion prior to issue of guarantees to minimise moral hazard and NPAs on account of above reasons." - Section 4.1.4.1, Ibid

absence of a clear regulatory and supervisory oversight by a financial sector regulator and the lack of information on risk management processes and operations add to the lack of clarity[41]. For instance, Scheduled Commercial Banks (SCBs), regulated by RBI, are required to disclose the compensation and remuneration structure of Whole Time Directors/Chief Executive Officers/Material Risk Takers and Control staff as part of their disclosure on risk management practices[42].

3.2.3. Operational Framework

1."The claim management process should be efficient, clearly documented, and transparent, providing incentives for loan loss recovery, and should align with the home country's legal and regulatory framework"

There is little clarity on the claim management process for the CGTMSE and CGFMU, or the latter's parent, the NCGTC. While CGTMSE reports the figures on the amount and number of claims processed[43], there is no information on how efficient the claims process has been or other aspects of the process for either entity. The CAG report identified discrepancies in the claim management process, particularly on the classification of NPAs. For instance, the CAG report found that in many instances, the MLI reported the NPA status of a loan to the CGTMSE portal only on the quarter subsequent to the actual date on which the loan became an NPA, in violation of RBI guidelines and the CG operating guidelines[44]. The lack of public information on metrics like time taken to process claims, claim rejection rate, or distribution of rejected claims by reasons for rejection further undermine the credibility of the process. However, there is data on amount recovered due to loan loss recovery processes, and the operating guidelines for CGTMSE provide some incentive to the MLIs to actively pursue loan loss recovery operations[45].

3.2.4. Monitoring and Evaluation Framework

1."The CGS should periodically and publicly disclose non-financial information related to its operations"

The WBG report mention 3 types of non-financial information that a public CGS entity should disclose at a minimum – a) social and economic commitments made by the CGS; b) social and economic outcomes achieved by the CGS and c) any other material engagement that the CGS has entered as a result of its government ownership. However, there is very little, or no disclosure of any of these types of non-financial information by either CGTMSE or CGFMU. There is only a stray mention of the social impact that these schemes have had, in their annual reports[46]. Almost all of the information disclosed by these entities, with regard to their performance, is only financial in nature. Further, there is no disclosure even with regard to other non-financial information like borrower/MLI appraisal process, performance efficiency of the claims or loan recovery processes.

[41]In the absence of a regulatory authority or a statute, the operation of CGTMSE would be guided by its trust deed. However, we could not find a public copy of the trust deed. Also, it is unlikely that a trust deed would have guidelines and covenants equivalent to regulations issued by an appropriate authority.

[42]Guidelines on Compensation of Whole Time Directors/ Chief Executive Officers/ Material Risk Takers and Control Function staff - https://www.rbi.org.in/scripts/NotificationUser.aspx?Mode=0&Id=11720

[43]CGTMSE Annual Report – 2019-20

[44]"Audit, however, noticed that the Trust had allowed (November 2009) the MLIs to mark NPAs in a particular calendar quarter, by end of subsequent quarter, which is not as per RBI directions. Further, the MLIs did not mark NPAs even as per scheme and the delay was condoned by the Trust." – Section 4.1.5.1, Report of the CAG, No. 10 of 2020 for the year ended March 2019, Compliance Audit Observations – Sep 2020

[45]CGTMSE Scheme Notification

[46]See CGTMSE Annual Report – 2017-18 which mentions the % of women beneficiaries of the scheme.
See NCGTC Annual Report – 2018-19 which gives the breakup of social categories benefitting from the CGFMU scheme

2. "The performance of the CGS—in particular, its outreach, additionality, and financial sustainability—should be systematically and periodically evaluated, and the findings from the evaluation publicly disclosed"

The annual reports of CGTMSE and NCGTC provide some information about the outreach achieved by the CG schemes as measured by the amount and number of guarantees issued. However, beyond outreach, there is currently no systematic or periodic evaluation of the performance of CGTMSE or CGFMU in terms of its additionality and financial sustainability[47]. Additionality here refers to the incremental credit that is enabled to MSMEs through the activities of the CG schemes. It also includes the impact on other variables like loan size, pricing, need for collateral and the like. And financial sustainability refers to the ability of the entities running the CG schemes to function as going concerns with adequate capital. While financial additionality is mentioned in the annual report of CGTMSE[48], there is no evaluation of the same by either CG scheme. Indeed, the CAG report mentions that CGTMSE based its numbers on additionality only on information provided by the MLI at the time of application. There was no attempt by CGTMSE to verify these numbers independently[49].

4. Areas for Policy Action

It should be noted here that we have evaluated the CG schemes on only a subset of 8 strategic principles broadly covering the main design and operational aspects relating to autonomy, risk management, supervision, and transparency, out of the overall 16 principles. This evaluation is thus not comprehensive. The above analysis, with all its shortcomings, highlights the gaps between the current functioning of our CG schemes and the global benchmark on important strategic and operational dimensions. We recommend the following policy actions that the Government can take to strengthen these CG schemes –

4.1. Provide a concrete legal framework clearly defining their powers and objectives

These schemes should be backed by a statute specifying the powers, objectives, sources of funds and the governance framework for these schemes[50]. This would ensure its financial and operational independence and clearly place accountability. Such a framework should also include the regulatory and supervisory mechanism these entities would be subject to. Being grounded in such a legal framework would also make it difficult for CG schemes to be used for populist measures.

4.2. Make the separation of Government as owner and manager more effective

The CG schemes should have a governance structure with an independent and competent board of directors, selected through a transparent and structured appointment process. This should be reflected in the legal framework governing the CGS. This would further strengthen the independence of the entity and ensure that it does not deviate from its objectives.

[47]It should be noted here that the CAG report referenced in this brief was based on a one-time compliance audit and is not a regular audit.
[48]See CGTMSE Annual Report – 2017-18
[49]"Audit noticed that the turnover, exports and employment figures were all estimated based on the information furnished by MLIs at the time of lodging application with the Trust for seeking guarantee cover and the data were not realistic or actual. The Trust also did not call for the details or get the details uploaded from the MLIs in its portal after commencement of business by the MSEs or close of a MSE unit after making default." - Section 4.1.2.5, Report of the CAG, No. 10 of 2020 for the year ended March 2019, Compliance Audit Observations – Sep 2020
[50]We have used the word 'statute' instead of 'decree' as the word 'decree', in India, could include a government order. But a government order could easily be revoked or modified, thereby negating the much needed legal stability.

4.3. Strengthen the risk management process and enhance transparency

The CG schemes should have an effective and comprehensive enterprise risk management framework that identifies, assesses, and manages the risks related to its operations. Such a framework should cover all aspects of the operations –a) MLI/borrower appraisal; b) Underwriting of claims; c) Investment management; d) Claim disbursements process, and e) Loan recovery process.

Implementing this risk management framework should be complemented with greater disclosures by the entities on these aspects.

4.4. Institute a system of periodic audit of performance

Financial performance should not be the only metric to assess the performance of the CG schemes. The objectives of outreach and economic additionality are equally important. Given the direct impact these schemes have on the exchequer, it is imperative that the CG schemes are able to achieve their stated goals. To that end, the Government needs to institute a system of periodic independent audits of the economic additionality and the financial sustainability of these programs. This assumes greater significance in the light of the recent COVID related CG schemes announced by the Government[51].

5. Conclusion

Our evaluation of the design and operational principles of the CG schemes reveals that there are substantial gaps along the dimensions of transparency, risk management, autonomy, and supervision when compared against the WB principles. These gaps are not insurmountable, and the policy actions suggested above, if implemented, would bridge these gaps to a large extent. The CG schemes play a catalytic role in enabling credit access to MSMEs, and their effective functioning is thus of utmost importance in financially including MSMEs.

[51]https://pib.gov.in/PressReleasePage.aspx?PRID=1623601 – Retrieved on 20-05-2020