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The Impact of COVID-19 on Iran's SMEs: Policy Implications for Current and Post Pandemic

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Abstract

The spread of the COVID-19 in the world has not only affected the health sector but also had the greatest impact on the economy and businesses. Iran was one of the world's early COVID-19 hotspots. The combined death toll in Iran rose to 17,405 while the number of confirmed cases rose to 312,035 on 4 August 2020. Iran has been facing serious challenges to respond to the pandemic as well as the US sanctions imposed on its foreign trade, oil exports and bank system. Due to this global challenge, the COVID-19 pandemic hurt Iran's businesses and manufacturing enterprises, especially SMEs, more severely. Because of such difficulties imposed on the SMEs, a huge number of current jobs and job opportunities have been lost, which has led the production capacity to downsize sharply. Therefore, the Iranian government should support vulnerable enterprises to prevent the economic disaster although it has faced lack of financial resources due to budget deficit and the imposed sanctions.

The objective of this paper is to explore the impact of COVID-19 on the economic situation of Iran's SMEs and to roles for the country, including the government, to play a supportive part to secure the SMEs for both current and post-pandemic times. The government should take the approach of increasing demand, maintaining jobs with a policy of preventing the downsizing of the



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SMEs during the COVID-19 era. Based on the case study results, the reflection of the most SMEs has been towards banking support package, which is more applicable to indicate that most of them have problems in financing.

Keywords: COVID-19 Pandemic, SMEs

1. Introduction

COVID-19 presents a major threat to the global economy and the health of millions of people around the world, but its impact on Iran, one of the early epicenters of the outbreak, has been particularly severe. The Iranian labor market was already suffering from a higher rate of unemployment due to structural problems of the economy and imposed sanctions as well as the COVID-19 pandemic. The outbreak of the COVID-19 in February and March 2019 came very close to the Iranian New Year, an important period of time for many businesses. The COVID-19 pandemic caused many businesses to reduce working hours and in some cases complete closure to prevent its spread. These efforts caused ample financial losses for the companies, with the loss especially greater in services, tourism, retail, transportation, clothing, education, among others.

Small and Medium Enterprises (SMEs), which are among the most vulnerable sectors, have a lower level of resilience than others. They have suffered greatly from the COVID-19 pandemic.

The COVID-19 outbreak affects SMEs negatively upon both the supply and demand sides. On the supply side, companies experience a reduction in the supply of labor and on the demand side, a dramatic and sudden loss of demand due to consumers' fear of contagion and heightened uncertainty, which results in reduction in spending and consumption. Therefore, the pandemic decreases SMEs' revenues and severely affects their business activities in which they may face severe shortage of liquidity.

The objective of this paper is thus to study the impact of COVID-19 on the economic situation of Iran's SMEs and to identify proper roles for the country, including the government, to play in its supportive role to secure the SMEs for both current and post-pandemic times.

The remaining of this paper is classified into four sections. Section 2 comprehensively studies the effect of COVID-19 on Iran's economy. Section

3 concentrates on Iranian SMEs' actions in the COVID-19 pandemic, and Section 4 discusses the supportive packages which the society and the government have launched relevant policies to preserve the SMEs' roles in production and business activities. Section 5 concludes with some remarks.

2. Effect of COVID-19 on Iran's Economy

As previously discussed, Iran was already enduring huge trade and financial sanctions imposed mostly by the US government, and is suffering from the COVID-19 pandemic, leading so far to a fall of 15% of GDP, affecting 50% of Iran's workforce, particularly impacting the bottom 40% income-deciles of the population, deepening inequality and raising additional unemployment possibly by 2 million.¹

The outbreak of COVID-19 has plunged the Iranian economy into a state of ambiguity. Although its effects are important for all developed and developing countries, it seems that in the case of Iran, this issue will have different and more serious dimensions due to simultaneous incidences of the pandemic and the imposed sanctions. Based on the FM Global Resilience Index² in 2020, Iran ranks 125 among 130 countries and based on fragile states index annual report 2020, Iran's score is 83.4, which places the country in high warning countries' classification³ indicating that Iran is not able to adapt and act well in confronting with the economic shocks.

Due to withdrawal of the United States from the Joint Comprehensive Plan of Action (JCPOA) in 2018, Iran faced huge economic shocks; especially the country has experienced exchange rate fluctuations and laid the groundwork for unemployment and recession during the last two years. Iran's economic growth was -5.4% in 2018 and -7.6% in 2019. It indicates that COVID-19 outbreak deepened the economic difficulties in Iran. While it is predicted that the real GDP growth will reach -6% by the end of 2020.

1. United Nations (June 2020)

2. <https://www.fmglobal.com/>. This index is the definitive ranking of nearly 130 countries by the resilience of their business environments. It provides companies with objective information about countries' economic, risk quality and supply chain resilience.

3. <https://fragilestatesindex.org/wp-content/uploads/2019/03/9511904-fragilestatesindex.pdf>

Additionally, the unemployment rate increased during 2018-2019, while it is predicted that the rate will increase to 16.3% and 16.7% in 2020 and 2021, respectively, not only due to sanction but also due to COVID-19 outbreak and industries' lockdown. As people's purchase power decreased during recent years due to the economic problems and COVID-19 outbreak, many jobs in both manufacturing and services industries, particularly related to the SMEs, may close down where it results in further unemployment. In addition, the COVID-19 outbreak caused Iran's neighboring countries such as Iraq, Turkey, Turkmenistan, Afghanistan and Pakistan to close their borders, causing obstacles for Iran to trade and export goods to these countries.

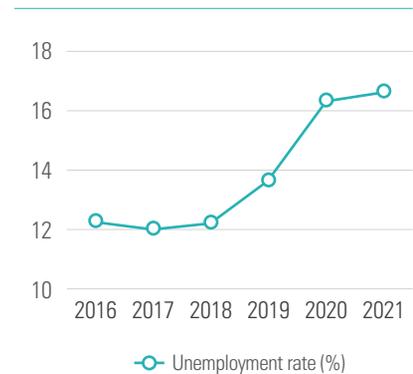
However, closure of businesses in the field of domestic and foreign tourism, which was one of the engines of employment and growth during the embargo, intensifies the economic problems in Iran. Therefore, a chain of bounced checks is created and many businesses are faced with bankruptcy, which increases unemployment in Iran.

Figure 1.
Real GDP growth (%)



Source: <https://www.imf.org/>

Figure 2.
Unemployment rate (%)



Source: <https://www.imf.org/>

3. Impact of COVID-19 on the Iranian SMEs: A Case Study

In most countries around the world, especially developing countries, SMEs are recognized as an important factor in socio-economic development.

SMEs play a major role in creating job opportunities with low investment, regional growth and development, and organizational development of knowledge-based companies. In recent years, most governments, including Iran, have prepared special and various programs for the growth and development of SMEs, which also support the emergence and creation of this type (Keskin et al., 2010).

According to a report provided by the Iranian Ministry of Industry, Mines and Trade, SMEs account for 92 percent of the total number of active units in Iran's industrial sector. Iranian SMEs exported US\$1.5 billion worth of commodities in the first eight months of the current Iranian calendar year (March 21-November 23, 2019). Iran's Small Industries and Industrial Parks Organization (ISIPO)⁴ also announced that, before the COVID-19 pandemic, over 33,000 SMEs were active in Iran of which 1,100 were exporting their products and services to foreign destinations indicating the important role of SMEs in Iran's economy especially in considering long time of the sanctions imposed.

However, SMEs have been more fragile in counter with economic shocks than large enterprises (LEs). SMEs have been affected severely by the COVID-19 pandemic and the smaller the company, the harder the hit because SMEs are typically faced with lack of cash flow and capital. Consequently, it is supposed that a majority of SMEs, particularly in the services sector, will have to close or disappear from the economy forever.

To study the impact of the COVID-19 outbreak on Iranian SMEs, a questionnaire was designed in order to distribute it randomly to a sample of 60 SMEs registered by the Isfahan Chamber of Commerce, Industries, Mines and agriculture (ICCIMA) located in Isfahan province. The questionnaire included a number of questions to ask the impacts of COVID-19 on their production - sales, production factors, and job lose etc. Figures (3) to (9) presented their responses.

According to Figure (3), 32% of SMEs have experienced more than 50% reduction in their sale and 46% between 25%-50% reduction in their sale. In addition, 47% of SMEs in services sector have more than 50% decline in their sales especially in tourism and hoteling subsectors because people prefer not to travel and not eat out in the COVID-19 pandemic situation.

4. <http://isipo.ir/>

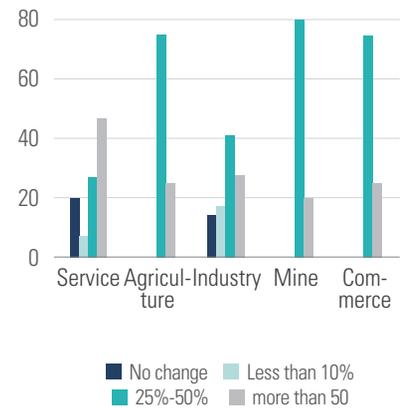
In the commerce sector also 75% of SMEs have been faced with 25%-50% decrease and 25% of them have more than 50% decline in sale due to Iran neighbor's countries border.

Figure 3.
COVID-19 impact on SMEs sale



Source: Questioners compiled with ICCIMA

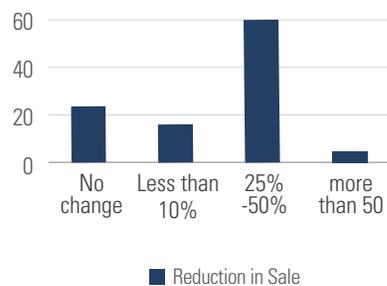
Figure 4.
COVID-19 impact on SMEs sale in each sector



Source: Questioners compiled with ICCIMA

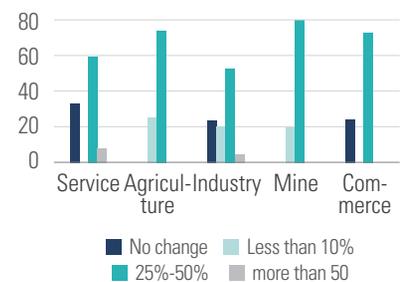
Figure (5) shows that 60% of SMEs have faced an increase in inputs' prices and about 23% of them did not have any problem during the pandemic. However, 80%, 75%, 75% and 60% of SMEs in mines, agriculture, commerce and service have faced 25%- 50% increases in inputs' prices, respectively. In the industry sector, 52% of SMEs experience 25%- 50% increase in inputs'

Figure 5.
COVID-19 impact on SMEs input's price



Source: Questioners compiled with ICCIMA

Figure 6.
COVID-19 impact on SMEs input's price in each sector



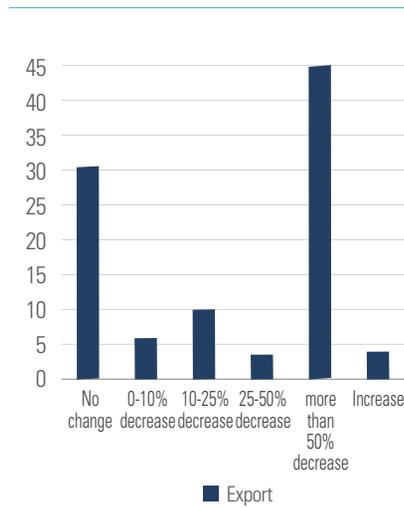
Source: Questioners compiled with ICCIMA

prices while 4% of them have more than 50% increase in such prices.

Figure (7) reveals the fact that 45% of the SMEs have had a decrease in their exports by more than 50%, while 3% of SMEs have experienced an increase in their exports, mostly in the area of sanitary products.

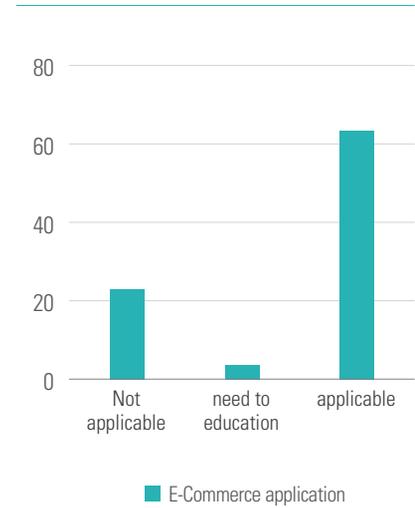
According to Figure (8), as e-commerce and virtual technology are the useful tools to control COVID-19 pandemic problems, 65% of SMEs have replied that such tools are appropriate to manage the relevant impacts.

Figure 7.
COVID-19 impact on SMEs export



Source: Questioners compiled with ICCIMA

Figure 8.
E-commerce solution in confronting with COVID-19



Source: Questioners compiled with ICCIMA

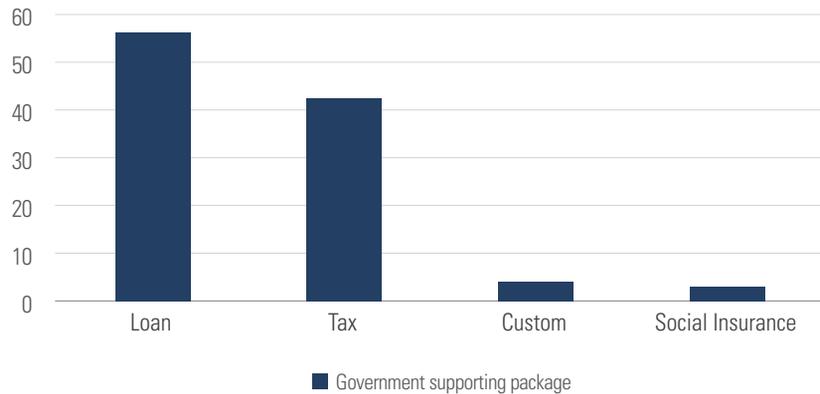
4. Iran's Supportive Packages

To control impacts of the COVID-19 pandemic on Iranian households and the SMEs in particular, the government and the private sector have launched several attempts.

Figure (9) indicates that more than 55% of SMEs have shown their satisfaction with a devoted loan support package arising from the bank system, which is useful for confronting the COVID-19 crisis. However,

41.8% of the SMEs have chosen a tax package and 2.8% have selected a custom package applicable to solve their financing problems. It indicates that most of the SMEs have been restricted in liquidity and financing.

Figure 9.
Assessing government supporting package in COVID-19 era



Source: Questioners compiled with ICCIMA

In priority, the health sector started providing guidelines and sanitary protocol for people and small business and all media started encouraging people to take care of social distance and wear facemasks, especially at the work. It is obligatory for those businesses, like supermarkets, groceries, health centers, etc., could not lock down, as they have to supply necessary goods and services. In addition, the government forced all business to decrease working hours and decrease the number of employees who work in joint at the office at the same time. In confronting with the demand side of COVID-19 crisis, Iranian government allocated cash transfer to 4.3 million households in addition to provide cheap micro/small loans on demand (for a four member family, at near equivalence to minimum wage). Additionally, to support supply side Iranian government provide recovery stimulus package of 1,000 trillion IRR (circa 5% of Iran's GDP) to support businesses and households. To support business, this recovery stimulus package includes⁵:

⁵. United Nations (June 2020)

- Loan package to business (75% of the total amount) – at cheap (4%) interest rates for small businesses not firing workers
- Moratorium on all payments by the business community to Government for a three-month period (including taxes, employment insurance contributions, interest rates on loans, utility bills etc.);
- Enabling trade in Justice Shares : prompting small capital holders into capital markets
- Financial asset sales; capital market support; capital gains tax law in the parliament of Iran

To support households, this recovery stimulus package includes:

- Allocation of free rate of interest amounted for 10 million Rials loan for all households upon their requests
- Allocation of free rate of interest amounted for 20 million Rials loan to women-headed households
- 120 Trillion Rials allocated for purchasing medical equipment
- 50 Trillion Rials allocated to unemployment insurance fund
- Raising of the legal minimum wage by 20%

5. Conclusion and Policy Implications

The COVID-19 pandemic has made unprecedented difficulties to all countries around the world. The crisis has hurt Iran intensively in the time of heavy financial and trade sanctions imposed. This is because the country has witnessed a 40% inflation rate, a higher rate of unemployment of about 16%, severe volatilities in exchange rates and the foreign trade slowdown. Although having partly supported financially by the government, the Iranian households and the SMEs require further support in current time and during the post-pandemic as predictable. Investment and finance in the SMEs look quite required in order to enhance their production capacities. One significant step that the government should take is to provide a strategic plan for the SMEs financial collateral, in which the SMEs face often as the serious challenge.

Meanwhile, as most of selected SMEs have mentioned in their interviews, e-commerce enhancement is an effective way to remove partly difficulties made by the COVID-19 pandemic. Hence the Iranian government should provide necessary technological infrastructure and invest more on this sector. The COVID-19 pandemic has made vastly the use of digitalization

in business to take care of social distance and decrease people's direct contact to control the pandemic and prevent more infections. In this respect, governments can make the benefit of this situation in order to enhance electronic government, move towards digital government and put all services online. Additionally, the economic sectors have the chance to expand their activity chains including production and sales lines via digitalization. To this end, all Iranian companies especially SMEs should train their staff to apply internet and social networks in distance working and empower their staff in different jobs.

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<https://www.fmglobal.com/>. This index is the definitive ranking of nearly 130 countries by the resilience of their business environments. It provides companies with objective information about countries' economic, risk quality and supply chain resilience.
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