Syllabus subtopic: Indian Economy and issues relating to Planning, Mobilization of Resources, Growth, Development and Employment.

Prelims and Mains focus: about the move and its implications; about force majeure clause

News: The government said supply chain disruptions caused by the novel coronavirus (Covid-19) outbreak in China would allow companies to invoke force majeure clause

Background

- The announcement comes a day after Finance Minister met several industry representatives to take stock of the situation, announcing the government would “speedily” formulate measures to minimise its impact on sectors.

- The Department of Expenditure in a notification dated February 19 advised ministries that the impact on supply chains due to the spread of the virus was a fit case for the invocation of the force majeure clause.

What is the force majeure clause?

- A ‘force majeure’ means extraordinary events or circumstances beyond human control, including events like natural calamities that could be described as an ‘act of god’. Other events include wars, strikes, riots and crimes. However, events like negligence or wrongdoing and predictable or seasonal rain are not considered force majeure.

- A force majeure clause in the contract frees both parties from contractual liability or obligation when they are prevented by such events from fulfilling their obligations. It is an extraordinary provision that allows them to wriggle out of liabilities in case they are unable to fulfill their contractual obligations.

Significance

The move is a potential relief for companies facing difficulty in receiving
Shipments from China due to issues like shutdown of operations there or a hold-up at the ports in India.

Sectors facing supply chain issues

- Sectors like pharmaceutical, chemicals (such as paints and tyre manufacturing) and solar equipment were “very vocal” about disruptions in their supply chain.

- Today, when their raw materials have to come, there is a delay, or the products come, but the papers (necessary paperwork from China for Indian customs) don’t come. So the disruption is felt increasingly by these three.

- Some micro, small and medium enterprises (MSMEs) had been facing delayed and staggered raw material supply, which had been impacting their ability to manufacture and send out their products. These MSMEs had sought flexibility from the banks, as their operations were affected due to the outbreak.

Impact of supply chain disruption (CII analysis)

- The Indian industry is heavily dependent on China, especially for raw materials for various products sold here and exported to other countries.

- China accounts for a significant share of the top 20 products that India imports from the world, according to an analysis paper by the Confederation of Indian Industry (CII).

- According to CII, this includes a 45 per cent share in India’s total electronics imports, a third of machinery and almost two-fifths of the country’s global organic chemical imports. India also sources about 65-70 per cent of active pharmaceutical ingredients used to make several medicines here as well as close to 90 per cent of certain mobile phone parts from China.

- “With supply chains disrupted, many enterprises will face working capital
shortages and be unable to meet their credit obligations. This will particularly impact smaller firms which can go under, leading to huge disruption in jobs and incomes,” stated CII’s analysis.

- The industry body had proposed a “one-time emergency waiver” of NPA regulations under a force majeure clause “given the exigencies of the situation” to quell fears of the impact of the outbreak on credit ratings of enterprises.