

OUR VIEW



Economics Nobel: micro studies for macro policy

The prize for 2026 honours researchers whose work draws on microeconomic analysis for a macro framework that holds special relevance in a world of high flux and economic shocks

This year's Nobel Prize in Economic Sciences was awarded to Robert E. Hall of Stanford and Michael Woodford of Columbia for providing the "microeconomic foundations of macroeconomic stabilisation." The citation says it all: the duo developed new macro models "that have significantly improved our ability to implement effective stabilisation policy." Well-timed fiscal and monetary policy measures based on these models "can reduce the economy's peaks and troughs." As the awarding panel's chair John Hassler noted, the laureates' work has been of good use to central banks and governments in securing an economy from shocks like energy price spikes and sudden shifts in retail demand.

The interesting part this year is the award's recognition of work that uses micro analysis—at the level of firms and households—for a macro policy framework. The important part is the resonance that research by Hall and Woodford holds in today's world of frequent economic shocks. The panel puts it well: "The stabilisation of aggregate economic activity is a central goal of economic policy." This is especially so since such flux rarely hits people evenly; both recessions and inflation hit the poor harder. The relationship between key aggregate variables like inflation, unemployment and GDP were broadly mapped at a macro level, with a major role played by Keynes, best known for making a case for intervention in an economy. Today, policies to smoothen economic cycles are par for the course. The trouble was that the inner workings of those links were mostly a "black box," in the panel's words. Hall and Woodford helped open it up by delving into micro theory. The former focused on demand

and the latter on supply. Hall found that while household buying did depend on factors like expectations of the future, changes in it were unpredictable—like a 'random walk.' In a 1978 article, he showed that a theory of consumption-smoothing—the idea that consumers prefer to keep it stable over time—worked well for grasping movements in overall consumption captured by data. However, unforeseeable shocks implied that consumption could not be as easily manipulated by government policy as was once thought, thus potentially limiting the effects of macro policy. On his part, Woodford became the key architect of the so-called New Keynesian model: a full macro stabilization framework that has become the main tool for policymakers today. He studied key micro conditions that made the market mechanism rigid. Sticky prices, for example. Businesses usually do not vary prices on a daily basis as demand and supply fluctuate; instead they adjust prices in discrete steps based on various calculations. These adjustments are also forward-looking. Woodford examined micro-level behaviour and used its learnings to formulate his new model for the use of policy tools. While his original work was meant to sharpen monetary-policy analysis, the foundation it laid became a major tool for the analysis of fiscal policy as well. The duo's work can be said to have inspired today's market notion of 'reflexivity' or awkward feedback loops adding complexity to macro policies.

Together, this year's winners showed how aptly used fiscal and monetary policy can improve welfare by acting as a shock absorber. At a time of high uncertainty, with folks worried about the ability of authorities to cushion hard blows, the academic exertions of Hall and Woodford deserve policy-level attention.

THEIR VIEW

India's SME Growth Fund could spawn a new wave of champions

Its funding of promising enterprises can create a new generation of globally competitive exporters



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The Union Cabinet's approval of a ₹10,000 crore SME Growth Fund is among the most consequential recent initiatives for India's enterprise ecosystem. At a time when SMEs are navigating an uncertain global environment, the fund provides an important source of growth capital.

The importance of this intervention becomes evident when viewed against the central role that micro, small and medium enterprises (MSMEs) play in the economy. The sector contributes around 35.4% of manufacturing output, 48.6% of exports and 31.1% of gross domestic product, making it one of the most important drivers of growth, employment and entrepreneurship in the country. Within the broader MSME ecosystem, SMEs constitute the segment with the most potential to scale operations, raise productivity, integrate into global value chains and create high-quality domestic employment.

SMEs are also critical to India's export ambitions. They account for more than 70% of MSME exports, serving as important links between local production networks and global markets. As India seeks to deepen its participation in global value chains, SMEs can play an increasingly important role in driving exports and innovation, while creating stronger backward linkages with millions of micro enterprises.

India has put in place a strong and

steadily expanding architecture of bank and non-bank finance for MSMEs, complemented by credit guarantee mechanisms, digital lending, invoice financing and other initiatives. Debt finance is indispensable to meeting the working capital and investment requirements of SMEs. Equity capital serves a different purpose. For enterprises seeking to undertake capacity expansion, invest in technology, enter new markets or pursue longer-gestation growth opportunities, patient equity can strengthen the balance sheet and complement conventional debt financing.

Here, the SME Growth Fund can make a big difference. Existing support mechanisms have expanded funding opportunities for smaller enterprises, although much of the equity ecosystem has historically been oriented towards startups, early-stage ventures and micro enterprises. There remains considerable scope to deepen the availability of growth-stage equity for established SMEs that have demonstrated business viability and are ready for their next phase of expansion.

By providing patient risk-bearing capital, the fund can offer such enterprises another pathway to growth. Equity can also provide firms greater flexibility to invest in technology, strengthen supply chains, undertake research and development, improve product quality, enter new markets and enhance export competitiveness.

The significance of this approach goes beyond financing. It can help address the often-discussed "missing middle" in India's enterprise landscape. India has a vast base of micro enterprises and a strong cohort of large corporations. The opportunity now is to enable many more promising SMEs to transition to larger, more productive and globally competitive enterprises.

The fund can support this transition by backing enterprises with the potential to emerge as industry leaders across manufacturing, services, technology, innovation-driven sectors and strategic

value chains. In doing so, it could help create the next generation of Indian champions that can compete globally.

The timing is also important. Disruptions in West Asia have affected trade routes and increased shipping, insurance and energy costs, while supply chains adjust to these geopolitical developments. Export-oriented SMEs are further adapting to evolving compliance requirements and sustainability standards in key overseas markets. Long-term growth capital can provide enterprises with greater financial resilience to navigate such uncertainty.

The fund forms part of a broader package announced in the Union budget for 2026-27. These measures seek to strengthen equity, liquidity and professional support for MSMEs. The proposed convergence between the fund and professional support mechanisms, including those for enterprises in tier-II and tier-III centres, can help create a stronger pipeline of investment-ready SMEs by improving governance, compliance capabilities and preparedness for external investment.

The fund's success will depend on speedy and effective implementation. As the government takes forward its commitment through an Alternative Investment Fund structure, a clear operational framework, professional fund management and a robust pipeline of eligible enterprises will be important. Equally, the investment approach should identify businesses with genuine potential to scale and innovate.

The fund, therefore, is more than just another financing initiative. It signals evolution in India's approach to enterprise development, from supporting the creation and survival of businesses to enabling promising enterprises to achieve scale. It can be a catalyst for enterprise growth, industrial expansion, employment and export competitiveness. It can also help India build globally competitive SMEs to anchor value chains, drive innovation and contribute meaningfully to the Viksit Bharat goal.

10 YEARS AGO



JUST A THOUGHT

Authorities shouldn't view stabilization of the economy as an exercise that is simply conducted by people pulling levers to control the economy independently of what people in the economy understand about this

MICHAEL WOODFORD

GUEST VIEW

Brics Bank: its loan book is too modest for its objectives

ALOK SHEEL



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In 2012, finance ministry officials of Brics members met in Rio de Janeiro. They were tasked with exploring the prospect of establishing an all-South (or Brics) bank. It was formally set up in 2015. Looking back, most of the fundamental issues confronting the New Development Bank (NDB or 'Brics Bank') today were already visible in 2012.

The rationale seemed compelling. Multilateral development banks (MDBs) were undercapitalized. Their major shareholders were facing fiscal pressures following the global financial crisis. Emerging and developing economies needed large infrastructure investments. Poorer countries needed more concessional soft loan financing on the lines of the World Bank's International Development Association (IDA). A Brics Bank could mobilize a savings glut, channel funds into the real economy and complement rather than substitute the World Bank and regional development banks (RDBs).

A number of hurdles were identified. Could the new institution breach the sover-

eign credit ratings of its shareholders and lower its borrowing costs to levels near those enjoyed by the established MDBs? Among the possibilities considered were a World Bank-type structure based on callable rather than paid-up capital, a mixture of hard and local-currency borrowing and preferred-creditor status for sovereign lending.

Fourteen years later, the picture is mixed. China had favoured shareholding broadly reflecting capital contribution, and would have dominated the institution, replicating the asymmetry of the MDB capital structure. Others wanted equal voting power among the Brics grouping's five founders. Equality prevailed. Each founder subscribed \$10 billion, of which \$2 billion was paid in.

After about a decade of operations, the Shanghai-based NDB has outstanding loans of only around \$22 billion, compared to its paid-up capital of \$10 billion. Unlike established MDBs, it has mobilized remarkably little lending relative to that capital. The World Bank, by comparison, had paid-in capital of just \$23 billion in June 2025 and loans outstanding of about \$280 billion, apart from \$231 billion of IDA lending.

This raises an uncomfortable question: How much financial intermediation has actually taken place? It begins to look

uncomfortably close to direct sovereign lending conducted through a multilateral institution. The great advantage of an MDB is precisely its capacity to leverage a relatively modest amount of shareholder capital into a much larger lending portfolio.

Like the World Bank, NDB has preferred-creditor status and very strong capitalization, but its principal international credit rating remains AA compared to the World Bank's AAA. So the question asked in Rio back in 2012—could the Bank breach the sovereign credit ratings of its shareholders?—has received a qualified 'yes' as an answer. NDB has created a credit standing above individual member sovereigns and can lend internationally on attractive terms at about 30-50 basis points over World Bank rates. The difference isn't enormous, but neither has the new bank established a clear cost parity with the institutions it was intended to complement.

A development bank is not simply a machine for borrowing money cheaply and

lending it on. One of the World Bank's greatest assets is its enormous accumulation of expertise in project identification, appraisal, procurement, environmental and social safeguards, apart from implementation and monitoring. It has highly qualified technical staff and maintains substantial country and sectoral expertise.

NDB has progressively constructed an evaluation architecture and in 2022 created an Independent Evaluation Office reporting directly to its board. Its evaluation system now explicitly draws upon international MDB evaluation standards. Its own independent evaluations of institutional capabilities, however, will take decades to accumulate.

The bank's object was to mobilize developing-country savings on a scale commensurate with their enormous infrastructural and other developmental requirements. On that criterion, a roughly \$22 billion loan-book is quite modest. Its impressive paid-in capital has not yet been leveraged into lending on anything approaching the scale of established MDBs.

Expansion could change the story. The NDB now includes the UAE, Bangladesh, Egypt, Uzbekistan and Algeria, with additional countries at various stages of accession. Richer non-founding members could enlarge its capital base and borrowing strength. But the original governance settlement deliberately limits any non-founding member to 7% of voting power. Arrangements designed to preserve Brics control to a minimum 55% vote share could constrain how much capital powerful new shareholders are ready to contribute.

After its first decade, it might be fair to say that the Brics Bank experiment has justified itself institutionally more clearly than financially. The group has demonstrated that emerging economies can design, capitalize and operate their own multilateral development institution without reproducing the unequal governance structure they criticized in Bretton Woods institutions. What they have not yet shown yet is that this institution can mobilize and intermediate capital on anything close to the scale, cost or technical depth of the World Bank.

Brics has built a financial institution. The question now is whether it can build a balance sheet and acquire expertise to match the project's original ambition.