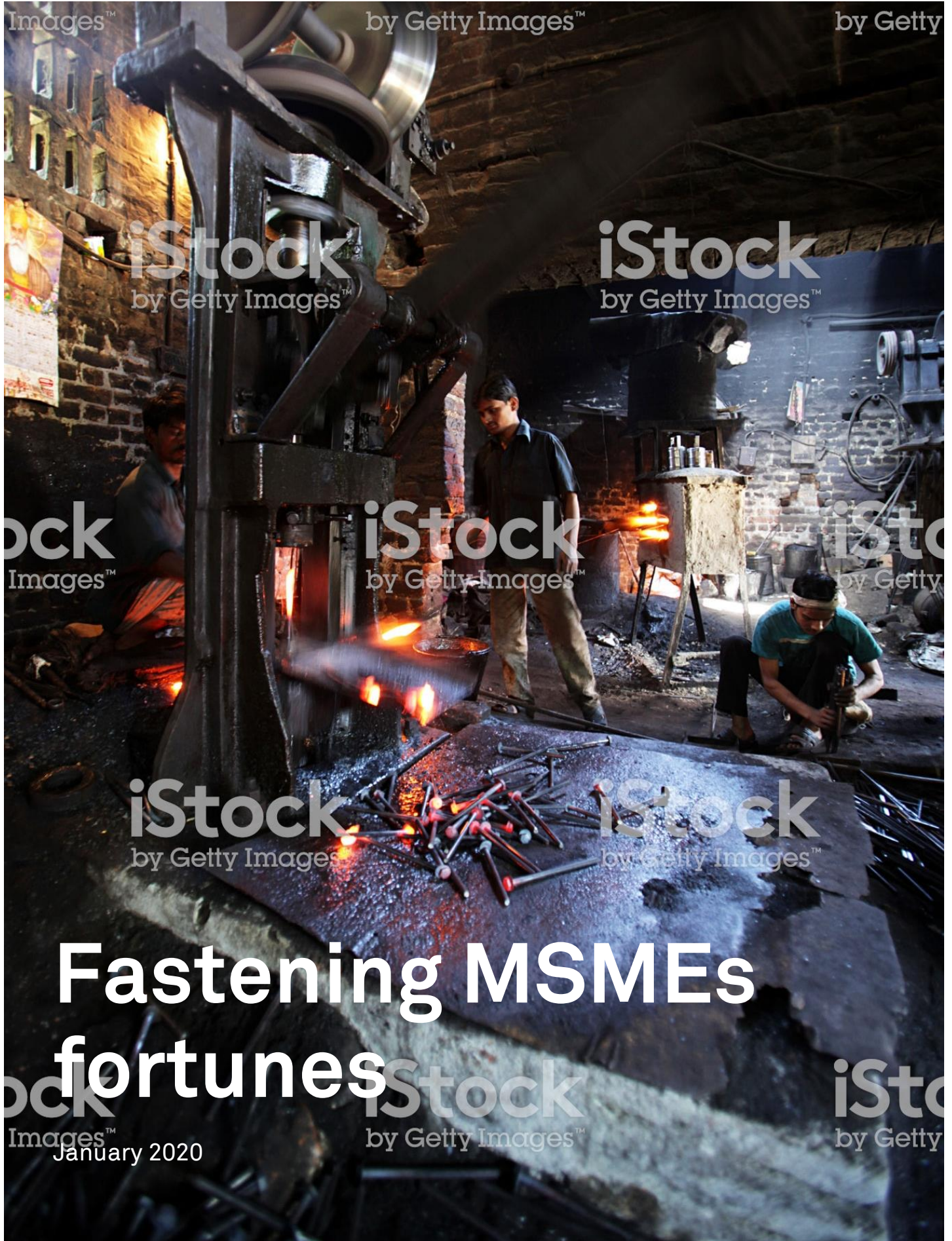




Fastening MSMEs fortunes

January 2020

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Message from CRISIL

The micro, small and medium enterprise (MSME) segment in India needs a multi-pronged heave-ho to increase its share in the gross domestic product to 50%, from around 30% today, as part of the government's avowed goal of becoming a \$5 trillion economy by 2024.

The imperatives on the government and regulatory side include building a comprehensive and quality centralised database, making additional allocation for cluster development, increasing the proportion of MSME book in priority sector lending, and improving transparency and ease of expanding business.

As for the MSMEs themselves, it is imperative that they ramp up their digital skills and bandwidth in order to tap the enormous opportunities available.

As per Ministry of MSME data, the sector comprises a whopping 90% of the total number of enterprises in the country, which account for around 60% of its jobs and almost half of its exports. As per CRISIL estimates, the MSME lending book will close fiscal 2020 at Rs 19 lakh crore, or ~28% of corporate credit.

Small wonder, MSMEs have been the backbone of this economy.

Yet, the segment has long been beset with woes – lack of capital due to inadequate access to finance, delayed payments from client segments, outdated underwriting process, unfavourable cost-competitiveness, lack of comprehensive quality database, deteriorating asset quality, high working capital requirement, and costly debt from informal sources, to name some.

All this has exacerbated the impact in the current milieu of an economic slowdown. Our analysis based on the CRISIL Quantix database of close to 15,000 MSMEs suggests revenue growth of the MSME segment will plunge to 2-3% this fiscal from 10% in fiscal 2019, a good 100 basis points sharper than the decline for corporate India overall. Given slower revenue growth, operating margins are expected to decline despite lower raw material costs.

The government has mounted several initiatives to help MSMEs overcome the hurdles. These include the 59 minute loan assurance, 2% interest subvention, MSME Sampark, MSME Sambandh, MSME Samadhan, Pradhan Mantri Mudra Yojana, Udyog Aadhar, TReDS and Credit Guarantee Fund Scheme – initiatives we have also discussed in this report. Some of these initiatives have been able to surpass their targets, though the majority have had only moderate success.

That said, the segment continues to offer attractive business opportunities for financiers. The challenge, however, lies in spotting the sectors and clusters that are likely to offer the desired risk-adjusted returns. The CRISIL SME Report, for one, covers 69 sectors and 147 clusters, and tracks the attractiveness and riskiness of sectors and clusters on a timely basis.



Hetal Gandhi

Director, CRISIL Research

Message from ASSOCHAM

Micro, Small and Medium Enterprises (MSMEs) is the second largest employment generating segment in India. With low investment requirements, flexibility in operations and the capacity to develop appropriate indigenous technology, these firms have the power to take India to new heights. They not only play a crucial role in providing employment opportunities at low cost than large industries, but also help in creating large employment opportunities. MSMEs further promote inclusive growth by creating jobs in rural areas. The year 2019 is truly a momentous year for the Indian economy. With the Hon'ble Prime Minister Shri Narendra Modi - led Government taking charge of its second stint at the Centre, India clearly has its vision set on becoming a US\$ 5 trillion economy over the next 5 years. The new government in its first budget lays down a 10-point roadmap for achieving its vision, which includes a renewed thrust on the growth of the MSME sector.

With an objective of acknowledging the significant contributions made by the MSMEs to various sectors of economy, The Associated Chambers of Commerce and Industry of India (ASSOCHAM), India's Apex Chamber for Commerce & Industry has constituted the **"ASSOCHAM's 7th MSMEs Excellence Awards & Summit"**. This award seeks to recognize the contribution of MSMEs who through their achievements and performance have empowered the nation.

We are confident the coming together of the MSMEs at this Annual Summit will highlight not only achievements but also their issues and the opportunities for the further growth.

I wish to thank the ASSOCHAM - CISIL Research Team for the background paper prepared for this occasion. I also wish to congratulate all the awardees for their achievement and convey my best wishes to the other participants for keeping up their good performance.

I extend my best wishes for the success of the Summit.



Dr. Niranjan Hiranandani
President
ASSOCHAM

Message from ASSOCHAM

The Associated Chambers of Commerce and Industry of India (ASSOCHAM) has always been proactive in encouraging and promoting MSME sector. It is well known that the most innovative business ideas come from the MSME sector; however MSMEs face a number of challenges including technological obsolescence, supply chain inefficiencies, increasing global competition, uncertain market scenario, and lack of funding.

ASSOCHAM firmly believes that it is critical to build upon the digital literacy in MSMEs to ensure that they make optimal use of the technology-enabled platforms. With their inherent capabilities to grow, digital ecosystem could be a suitable solution to help truly realize the potential of this sector.

The ASSOCHAM is organizing the Seventh Edition of the “MSMEs Excellence Awards & Summit”. The prime objective of Awards & Summit is to acknowledge the inestimable contributions made by the MSMEs to various sectors of the economy.

The **ASSOCHAM** jointly with **CRISIL Research** is bringing out this “Knowledge Paper” highlighting the “MSME’s: Growth Engine of Indian’s Economy”.

I take this opportunity to convey my best wishes to all the stakeholders and participants for the success of the **7th MSMEs Excellence Awards & Summit**.



Deepak Sood
Secretary General
ASSOCHAM

MSMEs, India's growth engine

The Indian MSME sector comprises ~630 lakh units and is estimated to employ ~11.10 crore workforce. It accounts for ~30% of India's gross domestic product (GDP) and ~48% of India's exports¹. Globally too, MSMEs are engines of growth, driving employment as well as revenue generation.

CRISIL Research defines micro small and medium enterprises (MSMEs) as entities with revenue of less than Rs 250 crore (existing definition is based on plant and machinery investment).

MSME sector is a major contributor to growth in India...



....and worldwide



Source: Press Information Bureau (PIB), 2019

Existing definition of MSMEs

Manufacturing sector		Service sector	
Investment in plant & machinery		Investment in equipment	
Micro	< Rs 25 lakh	Micro	< Rs 10 lakh
Small	> Rs 25 lakh & <Rs 5 crore	Small	> Rs10 lakh & < Rs 2 crore
Medium	> Rs 5 crore & <Rs 10 crore	Medium	> Rs 2 crore & < Rs 15 crore

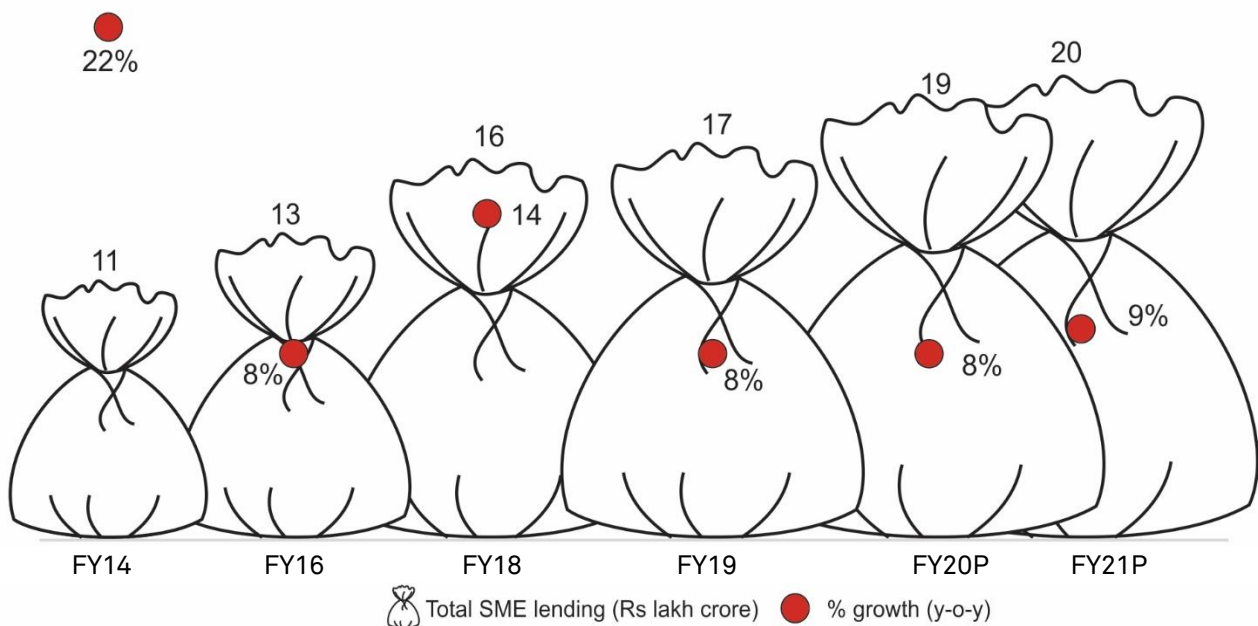
¹ as per the Ministry of MSME, data as of FY19

MSME lending book to reach Rs 19 lakh crore in fiscal 2020, comprising ~28% of corporate credit

MSME lending grew at double digits prior to fiscal 2015. Thereafter, it faced headwinds such as demonetisation and Goods and Services Tax (GST), and cautious stance of bankers amid rising non-performing assets (*Refer page 10*). Though, there was a pick-up in fiscal 2018 following recovery from demonetisation and streamlining of GST, the sector was once again drawn into the non-banking financial companies (NBFC) liquidity crisis from the second half of fiscal 2019.

CRISIL Research expects the MSME lending book growth (of banks and NBFCs) to moderate to 7-8% on-year to Rs 19 lakh crore in fiscal 2020, as the sector faces the double whammy of NBFC liquidity crisis and overall economic slowdown. We expect a marginal uptick to 8-9% in fiscal 2021, following some sentiment improvement.

MSME credit growth to hover at 7-9% CAGR in the near term



Note: CAGR: compound annual growth rate

Source: CRISIL Research

Between fiscals 2014 and 2019, MSME credit grew at 10% compound annual growth rate (CAGR), outpacing corporate credit growth of 8% CAGR. As a result, share of MSME credit in corporate credit rose.

Share of MSMEs' in corporate credit has risen

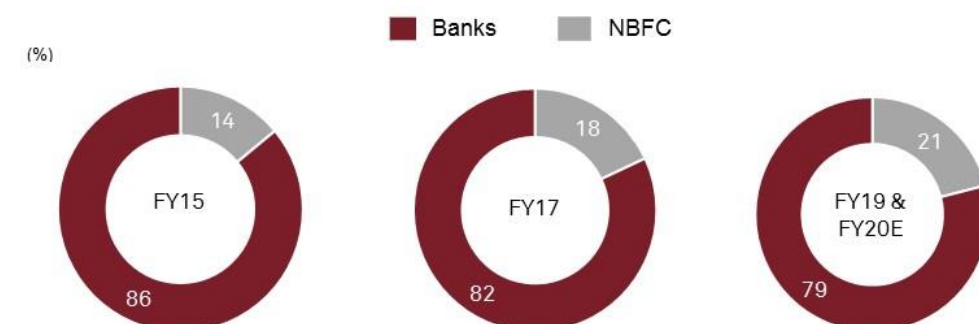


Source: CRISIL Research

Banks will continue to dominate MSME lending...

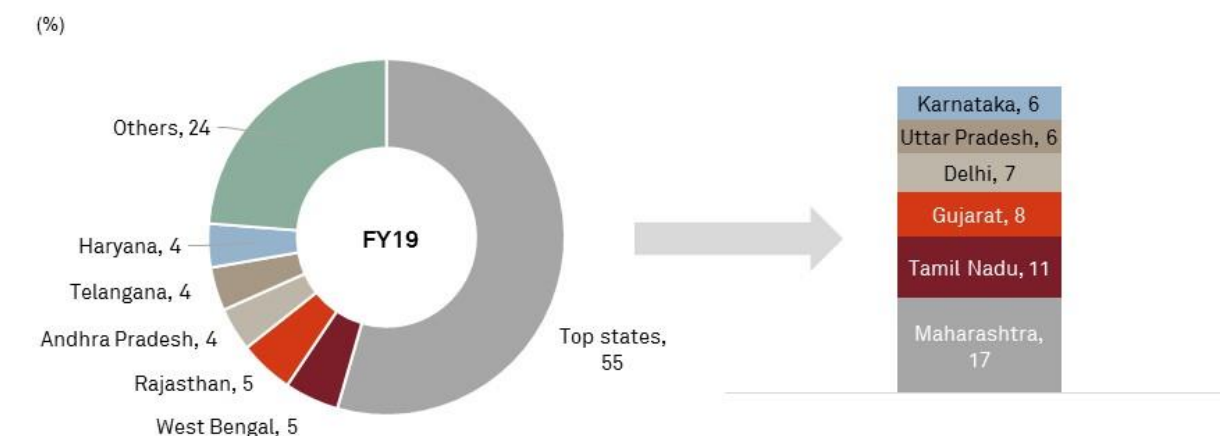
Banks dominate the MSME lending book, with a share of 79% as of fiscal 2019. Over the past three fiscals, NBFCs gained share by ~450 basis points (bps) to 21%, owing to aggressive lending. However, against the backdrop of continued funding challenges, we expect NBFCs' MSME lending growth to slow down, resulting in a constant share between banks and NBFCs, going forward.

...while NBFCs' rising share in past is likely to plateau in near term



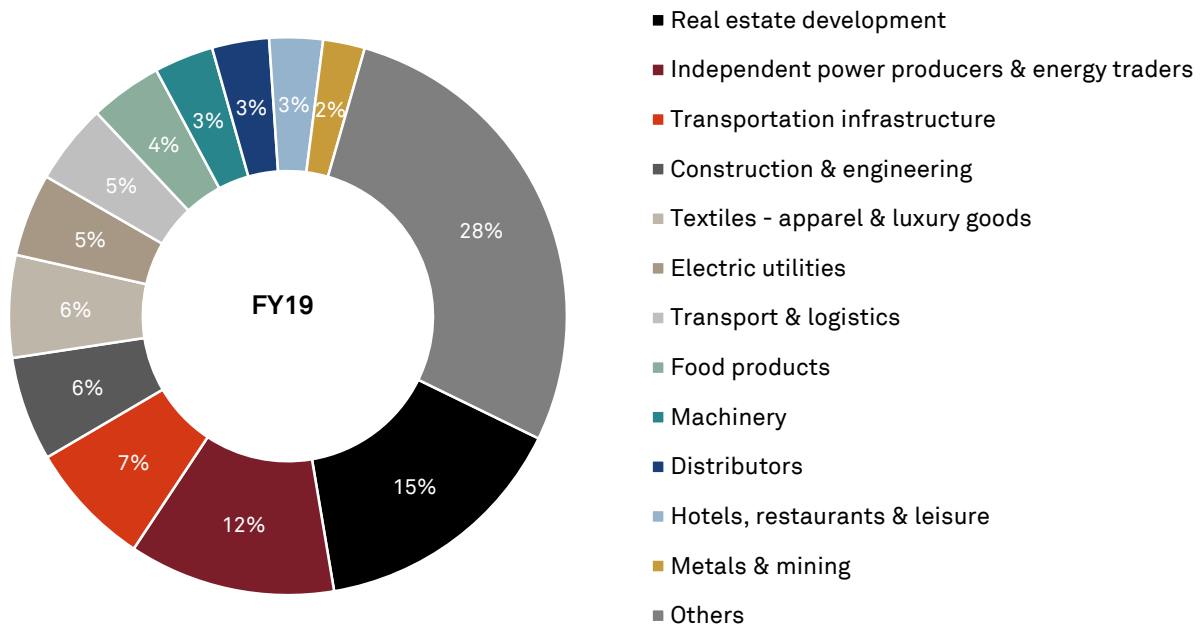
Source: CRISIL Research

Over half of bank lending to MSMEs is concentrated in six states



Source: Reserve Bank of India (RBI)

MSME credit fairly diversified across sectors

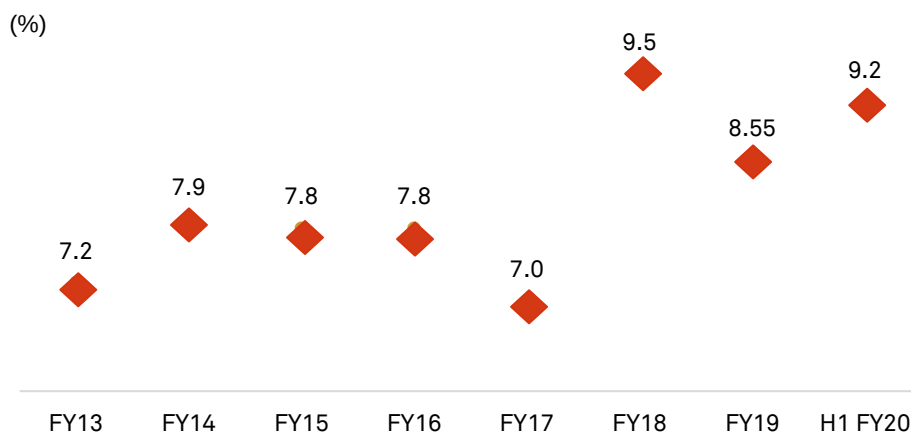


Source: CRISIL Quantix

Deteriorating asset quality a concern, moratorium to provide short term relief

Although lending to the sector has been growing at high single/double digits over the last decade, institutional lending remains under-penetrated. Lenders have not been able to deepen penetration owing to a significant increase in gross NPAs in the segment. The moratorium period (allowed in January 2019 and extended till March 2020) given to banks for not declaring any stressed account of MSME as NPA up to March 2020 provides a temporary relief. However, overall NPAs could shoot up post that.

Rising gross NPAs of a large bank in MSME lending



Source: Listed players MSME lending book accounting for 12-15% of MSME lending in India

High working capital requirement, costly debt from informal sources act as pain points

MSMEs mostly borrow to meet working capital needs. Given tepid demand, the working capital requirement has got further stretched, for e.g. in segments such as textiles and gems and jewellery. Moreover, MSME face a high cost of debt with a large portion coming from informal sources.

No end to working capital woes for textile and gems and jewellery MSMEs

The Indian MSME textile industry is reeling under severe financial stress due to tepid demand growth, pressure on spreads due to high raw material prices, and lack of availability of working capital.

MSMEs in the textile value chain typically face long cash conversion cycle as funds are needed for the purchase of raw materials, inventory management, payment of wages, and other day to day operations. For exporters, any delay in refunds of integrated GST (IGST) and export benefits holds up working capital. By December 2019, the Central Board of Indirect Taxes and Customs paid IGST refund of Rs 1.12 lakh crore to ~83,500 exporters. However, refunds worth Rs 3,604 crore were pending, as these exporters were identified as 'risky' as per data analytics. This affected several MSMEs, including textile exporters, further stretching working capital needs.

On the other hand, MSMEs in gems and jewellery are facing working capital crunch on account of sluggish exports, high gold prices, weak domestic demand and stricter lending norms.

Working capital is expected to remain stretched in fiscals 2020 and 2021, too.

Source: CRISIL Research

MSME revenue growth estimated to slow in line with India Inc, recovery key to sentiment change

The current economic slowdown is the other major factor affecting MSMEs. The slowdown has been more cyclical than structural. Weakening demand across most consumption segments in rural and urban India has adversely impacted India Inc's growth. Add to that, the funding crisis at NBFCs, high real estate inventories and stuck projects, and the result is significant demand drag.

Consumption slowdown is estimated to impact corporate revenue growth by 600 bps in fiscal 2020. Following slower revenue growth, operating margins are expected to decline despite lower raw material costs. That would be on account of higher fixed cost for sectors such as auto and relatively higher weight of agri-commodity sector that has seen prices rising amid weak supply.

Revenue growth and EBITDA margin to slide this fiscal

Parameters	Units	Rs 0-250 crore			FY20
		FY17	FY18	FY19	
Common sample					
No of companies	Number	13182	13182	13182	2-3
Sales growth	%	5.7	9.3	10.0	
No of companies	Number	19928	18845	13697	↓
EBITDA margin	%	7.2	7.1	7.5	
Net profit margin	%	1.1	1.4	1.7	
Debt equity ratio	Times	1.1	1.1	1.0	↑
Interest coverage ratio	Times	2.2	2.3	2.6	
Return on capital employed	%	9.1	9.1	9.6	
Asset turnover ratio	Times	2.1	2.1	2.4	
Working capital days	Days	117	118	121	
Debtor days	Days	60	64	64	
Creditor days	Days	48	51	47	
Inventory days	Days	44	45	47	

Source: CRISIL Quantix, CRISIL Research SME Report

Size-wise financials

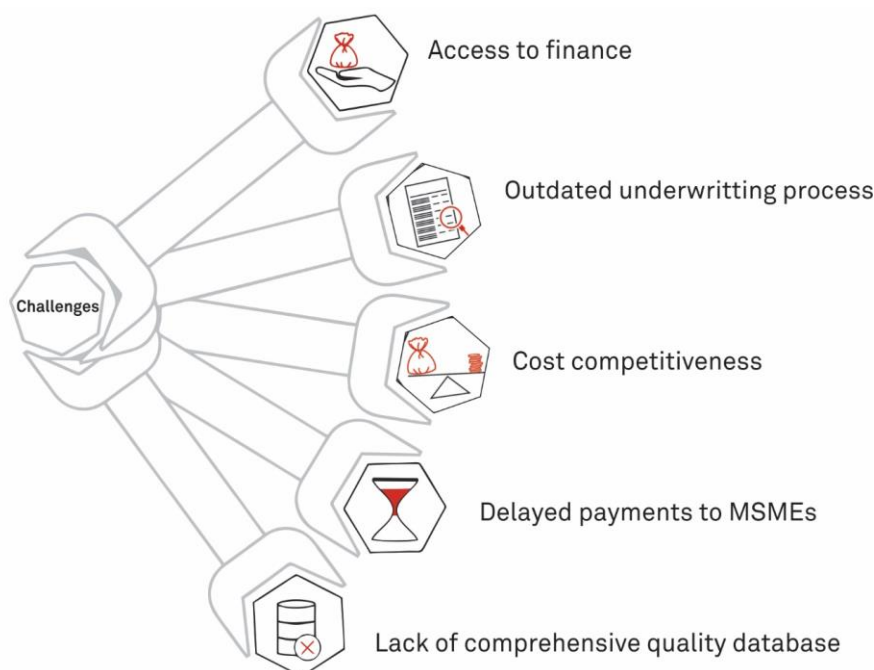
Parameters	Units	Rs 0-75 crore			Rs 75-150 crore			Rs 150-250 crore		
		FY17	FY18	FY19	FY17	FY18	FY19	FY17	FY18	FY19
No of companies	Number	15668	14415	10263	2839	2908	2191	1421	1523	1243
EBITDA margin	%	7.1	7.0	7.6	7.4	7.3	7.2	7.4	7.1	7.6
Net profit margin	%	1.0	1.1	1.5	1.7	1.9	2.3	2.2	2.2	2.5
Debt equity ratio	Times	1.2	1.1	1.1	1.0	1.0	0.9	0.9	0.9	0.7
Interest coverage ratio	Times	2.0	2.1	2.4	2.9	3.0	3.3	3.4	3.4	3.8
Return on capital employed	%	8.2	8.1	8.7	11.6	11.6	12.2	12.8	12.2	12.8
Asset turnover ratio	Times	1.7	1.7	2.0	3.4	3.4	3.5	3.5	3.6	3.6
Working capital days	Days	121	122	130	111	108	104	102	101	98
Debtor days	Days	60	65	66	62	66	62	57	62	59
Creditor days	Days	50	53	50	44	49	42	43	47	43
Inventory days	Days	42	43	47	50	51	47	49	48	47
Common sample										
No of companies	Number	9621	9621	9621	991	991	991	433	433	433
Sales growth	%	4.9	8.1	8.6	3.7	7.2	7.5	2.5	5.9	7.2

Source: CRISIL Quantix

Key challenges and opportunities

MSMEs in India continue to face a raft of challenges despite their critical contribution to employment generation and economic growth. We examine the major ones here:

MSMEs are beset by numerous hurdles



Challenges

- **Lack of access to finance** - A number of white papers from the likes of IFC have focussed on the funding issues faced by MSMEs. Total debt requirement of MSMEs in India is estimated at Rs 65-70 lakh crore, of which ~70% is for working capital requirements. CRISIL Research analysis of ~15,000 MSMEs shows their average trade receivables is over 65 days — a significant stretch that forces them to resort to high-cost debt to keep business running. This also substantiates that a large portion of the funding needs by MSMEs each year remains in working capital.

As per a SIBDI report, ~80% of MSMEs find it difficult to access funds from formal channels of lending. This is also evident from the fact that banks and NBFC outstanding to MSMEs is estimated at Rs 19 lakh crore, a miniscule proportion of their total funding need. While a number of support systems have been enabled, effectiveness remains low. For example, while the Trade and Receivables Discounting System, or TReDs, has been introduced since 2015, it has met with limited success.

- **Outdated underwriting process** - Financial institutions may not be spending adequate time on the ground with MSMEs, leading to outdated underwriting process of credit evaluation and placing emphasis on collateral.

It is time to improvise to innovative ways of underwriting, moving to cash flow-based lending from traditional bank lending on financial statements and collateral. State Bank of India is expected to shift to cash-flow based lending by April 2020. Moreover, surrogates such as bank statements, utility bills, etc. could be used to improvise credit underwriting. A central digital/credit rating scorecard, which would also act as a repository of income tax return, GST filings, bank statements, can be created.

- **Unfavourable cost competitiveness** - MSMEs suffer from high cost of financing, perceived high risk, and dependence on informal channels. CRISIL Research's analysis of 15,000 rated MSMEs finds their average financing cost was as high as ~12%. The number would be significantly higher for the larger non-rated universe.

Infrastructure bottlenecks such as inadequate availability of tool rooms, innovation hubs, etc., too affect competitiveness of MSMEs. Lack of scale and skill set acquisition, and limited understanding of modern methods of production lead to inability to compete on costs.

For instance, in the leather industry, as a CRISIL Research report said, India's recovery rate from carcasses is lower than global benchmarks. Increasing competition from Vietnam, Bangladesh and China is a major threat to leather exporters from India in terms of pricing. Even in textiles, India's overall spinning efficiency is much lower than that of neighboring countries such as Bangladesh, Vietnam and Pakistan, owing to old/obsolete technology in many MSME clusters.

- **Delayed payments to MSMEs** - MSMEs face delayed payments but are hesitate to enforce the legal route due to their limited bargaining power and fear of retaliation from buyers.

CRISIL Research analysis of MSME transport operators, for instance, revealed that by adhering to the stated credit period, end-users could potentially get 1-2% reduction in freight rate.

The government has mandated all companies who get supplies from MSMEs and whose payment exceeds 45 days from date of deemed acceptance, to submit half yearly returns to the Ministry of Corporate Affairs stating amount of payments due and reasons for delay. How this will be implemented would be a key monitorable.

- **Lack of comprehensive quality database, leading to low risk appetite of financial institutions** - A central platform for tracking data linked to MSMEs to enhance targeted effectiveness, is absent. GST implementation has brought turnover data into a single network. Udyog Aadhaar contains registration related information of MSMEs. However, there is no single central interface available for the lenders to triangulate data across categories. Even, district industrial centers (DICs)' information is not comprehensive.

Even assuming most of GST registrations are MSMEs, it would still cover less than 20% of MSME in India. This implies a large pool of MSMEs which are out of purview of GST. Moreover, non-reporting of revenue and financials for unrated companies makes it difficult for lenders to reach them.

Sector-specific MSME concerns and recommendations

Sector	Concern	Recommendation
Textile/readymade garments (RMG)	- Over the last few years, Indian RMG players have lost export opportunities. Market share of Indian RMG in European Union has eroded due to Vietnam's recent free trade agreement (FTA) with EU. India also has higher operating costs (labour costs contribute major share) vs Bangladesh, Vietnam, and Pakistan - Merchandise Exports from India Scheme (MEIS) incentives are likely to be withdrawn effective March 2020. Moreover, exporters have been unable to gain any incentives in past months due to dilemma between MEIS, Rebate of State Levies (RoSL), and Rebate of State and Central Tax Levies (RoSCTL). Without these benefits, Indian manufacturers find it difficult to compete with other nations in exports	- An FTA with major RMG importing economies like EU and US would significantly improve margins of exports - Announced Remission of Duties and Taxes on Export Products (RoDTEP) scheme should immediately be implemented, replacing both MEIS and ROSCTL, and compensating at least ~6% of apparel value
Edible oil	In December 2019, the government reduced import duty for crude palm oil from 40% to 37.5% and refined palm oil from 50% to 45%. This will impact domestic oilseeds demand such as groundnut and soybean. Reduction in import duty for refined palm oil will also severely impact the business of edible oil MSMEs processors, as the differential moves in favour of refined oil	Increase import duty for refined palm oil and crude oil to safeguard domestic oilseed demand and protect business of MSME edible oil processors

Source: CRISIL Research SME report

Opportunities

Notwithstanding the impediments, MSMEs could benefit from some plum opportunities before it:

- **Make in India**
 - 'Make in India' was initiated in 2014 with the objective of facilitating investment, improving manufacturing infrastructure, and enhancing skill development. While there is no provision for providing financial assistance to companies manufacturing products under the initiative, supportive policy actions can create the right ecosystem for incremental investment over the long term. Under the initiative, the government has identified 27 key sectors including textile and apparels, electronics system design and manufacturing, leather & footwear, gems and jewellery, and tourism and hospitality services. Many of these sectors are largely driven by MSMEs directly or through job works/contract manufacturing.

- In the same breath, the changes in foreign direct investment (FDI) policy, as announced in August 2019, will result in making India a more attractive FDI destination. Under the new norms announced, it has been decided that all procurement made from India by single brand retail trade entities would be counted towards local sourcing, irrespective of whether the goods procured were sold in India or exported. The impact of relaxation in this rule would be more pronounced in the apparel segment, as players in this category typically source requirement for their global operations from India. Home decor, footwear, and electronics segments too, are expected to benefit over the long term.

- **Gateways in global trade**

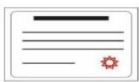
- The changing axis of international trade and opportunities in exports has partially supported growth in local manufacturing, with the impact seen in pockets of MSME-led sectors. For instance, the US-China trade tension has partially supported exports from India to the US in the past few quarters. Of India's total apparel exports, the US consumes ~26% (as of fiscal 2019). While the overall apparel exports from India remained muted declining 3% in fiscal 2019 on-year and growing marginal 1% in April-November 2019, exports to the US grew 8% and 6%, respectively. Over the medium term, any step towards FTAs with major export destinations such as EU or US can create huge business potential for local manufacturing thus benefiting MSMEs clusters involved in apparel manufacturing.
- Similarly, bulk drug exports increased ~10% on-year in fiscal 2019 (dollar terms), owing to a short-term opportunity in the export market because of supply disruption from China. Chinese players have been forced to shift their facilities inland on the back of government-led clampdown on polluting industries. Although Chinese capacities are slowly coming back onstream now, the cost competitiveness of Chinese players would reduce to a certain extent, as their cost of production increases. Further, recent quality issues from China prompted a global recall of several sartan (an active pharmaceutical ingredient mainly used in hypertension drug) products. Post this, multinationals are looking at sourcing from alternative locations like India. This would continue to provide some short-term opportunity for contract manufacturers (largely MSME players) in the medium term.

- **E-commerce boom**

- The Indian e-commerce sector has had a phenomenal run in the last few years. The sector has grown on the back of rising internet penetration, improved visibility and brand penetration, increasing awareness of online shopping, and lucrative deals offered by well-established players and start-ups. With regulatory vigilance and announced policy changes in the sector, participation of wider seller base is expected on online marketplaces.
- By going digital on these platforms, MSME companies can build their credentials and penetrate deeper into Tier II cities and beyond. In fact, more than 6 lakh sellers (most of which are entrepreneurs and MSMEs companies) are already offering their products through various e-commerce websites. With greater visibility, MSME companies can improve geographical reach and accessibility and also enable funding availability with better diversified sales mix.

Major government initiatives and their effectiveness

In addition to the above developments, the Government of India has launched multiple initiatives to improve funding access of MSMEs. However, effectiveness of most schemes remains moderate. A quick review of some of these:

		Launched	Objective	Effectiveness
59-minute loan		2018	In-principle approval of loans to MSME up to Rs 1 crore in 59 minutes	
2% interest subvention		2018	2% interest subvention for all GST registered MSMEs, on incremental loans	
MSME Sampark		2018	Build digital platform wherein job seekers (students of MSME Technology Centres) and recruiters register themselves	
MSME Sambandh		2017	Public procurement from MSMEs by central public sector enterprises of at least 25% of their annual procurement	
MSME Samadhan		2017	Establish Micro & Small Enterprise Facilitation Council (MSEFC) for settlement of disputes on delayed payments	
Pradhan Mantri Mudra Yojana		2015	Provide loan up to Rs 10 lakh	
Udyog Aadhar		2015	Registration process for MSMEs	
TReDS		2005	Create mechanism for financing trade receivables of MSMEs	
Credit Guarantee Fund Scheme (CGTMSE)		2000	Provide credit guarantee to financial institutions that provide loans to MSMEs	

 High
  Low / Moderate

Source: CRISIL Research

59 minute loan – In-principle approval quick, loan sanction slow

Since the launch of the 59 minute loan in November 2018, 2 lakh applications have been submitted, 1.5 lakh accorded in-principle approval, and 1.3 lakh sanctioned loans, up to July 2019. Out interactions with market participants indicate that though the in-principle approval is quick, time to obtain sanction remains high, thus not serving the purpose. Priority sector classification may help to push 59 minute loans (like in the case of 'mudra' loans).

2% interest rate subvention needs more time, support

The subvention on fresh loans for GST-registered MSMEs is estimated to benefit a fifth of MSMEs in India. But the Rs 350 crore allocation for this announced in Union Budget for fiscal 2020 would support only ~10% of incremental MSME lending. Nevertheless, extension of interest subvention scheme beyond March 2020 should increase support.

MSME Sampark doesn't really bridge the gap

Hardly 1% of jobseekers on this portal have got placement so far. Possible reasons for this could be skill set mismatch. If the curriculum is refreshed incorporating the feedback from MSME enterprises, it may see better conversion rate.

SME Sambandh overachieves its target

To overcome the constraints of small scale of MSMEs on sale of products, the government implemented a procurement policy in fiscal 2016, setting 20% mandatory procurement for government organisations from MSME sector. From a low of 12% in fiscal 2016, this proportion rose to 23% in fiscal 2018, as per PIB. In November 2018, there was an amendment to procurement policy where mandatory procurement for government organization from MSME sector was hiked from 20% to 25%. Commensurately, procurement share stood at 26% in fiscal 2019.

Samadhan settlements have been low

MSME Samadhan was introduced to resolve the delayed payment issue faced by MSMEs. Since its launch in October 2017 till date, about Rs 3,703 crore of claims have been filed by MSMEs. Of these, about 14% has been settled; while the rest are under various stages of hearing. Acceleration on resolving issues would be important.

Pradhan Mantri Mudra Yojana (PMMY) surpasses targets

PMMY has met targets every year since launch. One of the key reason for this is not only the government push, but more importantly, the benefit of classifying mudra loans as priority sector lending. Outstanding PMMY loan book stood at Rs 2.6 lakh crore in fiscal 2019, constituting ~14% of overall MSME lending in India.

Udyog Aadhar data self-certified, lenders not so convinced

Less than 15% of all MSMEs in India have registered on the Udyog Aadhar platform. The main drawback here is there is no single interface for lenders to triangulate data from several data sources such as Udyog Aadhar, GST, etc. Moreover, the data submitted on Udyog Aadhar is self-certified, and hence, does not act as a reliable source for lenders and buyers.

TReDS moving in the right direction, but yet to gather pace

TReDS, an online bill discounting platform was launched by the RBI in 2014 with the aim of bringing a structural solution to MSMEs' working capital problems. This, with initiatives taken in Union Budget 2019-20 such as allowing NBFCs as financiers, are positive. However, onboarding on the platform is low.

Total participants registered and invoices financed on TReDs as of March 2019

Participants registered				Invoices financed	
MSME sellers	Buyers	Banks	NBFC Factors	No of invoices	Amount (Rs crores)
3708	604	71	5	251988	6700

Source: RBI

The TReDS platform has grown tremendously and has the potential to take care of a significant proportion of requirement. In fiscal 2018, all three exchanges put together did business of ~Rs 800 crores, which jumped to Rs 6,700 crores in fiscal 2019, nearly 10x increase. Targets indicate that the exchanges plan to reach a size of Rs 30,000 crores by fiscal 2020. But that translates to merely ~3% of formal working capital lending and doesn't represent a meaningful share of total MSME needs.

One of the biggest deterrent for a pick-up in TReDs would be that only registered MSMEs can trade on it. Awareness about benefits to vendors may also not be fully known.

Ways to improve traction on TReDS:

- Faster linkage of the platform with GST system would enable automated authentication of the bills raised, as against the present system where the buyer needs to approve bills that can be discounted.
- Increasing MSME registrations and incentivising buyers would improve traction. For example, there are no incentives for large corporates to register as part of TReDS, given that transparency would result in highlighting any defaults to suppliers that remains under cover today
- Further, large conglomerates have their own financing arms which dissuades usage of a platform like TReDS, with no benefits against the threat of exposing the group clientele to other competitors
- The availability of alternative data can give MSMEs faster/cheaper access to finance. Also, tracking of alternative data (payment of utility bills, personal credit cards, mobile bills) through formal means such as CIBIL can add transparency to the segment.

Credit guarantee fund scheme (CGTMSE) a step in the right direction

As of March 31, 2019, a cumulative total of 34 lakh accounts have been accorded guarantee approvals for Rs 1.8 lakh crore. CGTMSE has so far settled 2 lakh claims amounting to Rs 5,362 crore.

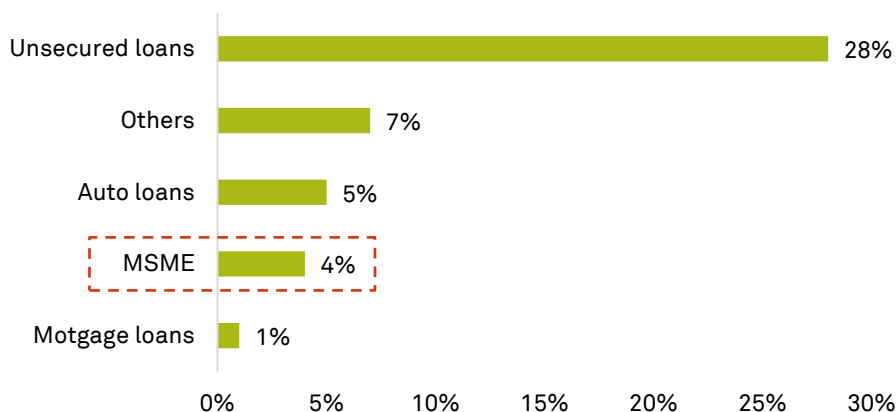
Leveraging technology for MSMEs

There is scope to leverage technology both in MSME lending and manufacturing.

Unleashing digital financial infrastructure

Lack of institutionalised MSME lending has led to ~350 innovative MSME digital fintech platforms coming in play in India. The number of fintech companies started picking up pace from 2015 onwards. In March 2018, the government formed a steering committee on how fintech can be leveraged to augment financial inclusion of MSMEs. The business model of innovative digital providers/fintechs, which are evolving at a rapid pace, would also need to be integrated. This serves as an additional mode of financing.

Digital lending is a small but rising pie in MSME lending



Note: As of FY19

Source: CRISIL Research

Fintechs offer various solutions in MSMEs lending, such as:

- Point of sale (POS) transactions-based lending – Using data from POS, fintech companies built proprietary technology platforms to offer unsecured loans. Example: Lendingkart, innoviti
- Bank-fintech partnership model – Fintech partners with data aggregators/marketplaces that provide transaction data to assess borrower risk profile. Example: Bank of Baroda's partnership with Fundstiger, CreditMantri, Kredx, Power2SME, etc.
- Invoice discounting exchanges – These enable MSMEs to achieve short term working capital needs by discounting invoices. Example: Kredx, Loanzen

Further, to support the fintech industry, the RBI released a draft 'regulatory sandbox' framework in April 2019. It facilitates a well-defined space and duration to experiment with fintech solutions, where consequences of failure can be obtained and reasons for failure can be analysed. Accordingly, the regulatory sandbox can benefit fintechs through reduced time to launch innovative products at a lower cost.

Technological infrastructure for MSMEs

Technological obsolescence affecting MSME segments such as textiles/RMG or medical devices. On the other hand, sectors such as seafood industry in south India, which typically deploy up-to-date technology, are well placed.

Technology levels differ across MSME sectors

	Seafood	Typically deploy technology in processing facility, cold storage, testing laboratories, etc.
	Textile	Technological innovation remains low, due to low capital, slower disbursements of incentives through Amended Technology Upgradation Fund Scheme
	Medical devices	Only few domestic players invest in R&D owing to limited incentives for this sector

	Low technological innovations
	Better technological innovations

Source: CRISIL Research SME Report

MSMEs must be incentivised to upgrade their existing capacities. This will improve production efficiency and reduce operating cost. In specific, sectors such as textiles spinning must be prioritised to undertake upgradation of capacities, as India ranks below neighbouring countries such as Bangladesh, Vietnam and Pakistan in terms of spinning efficiency.

Numerous government support initiatives have been taken, for instance, setting up 18 technology development centres and digital MSME scheme for promotion of information and communication technology. However, a very small fraction of these innovations are getting commercialised. From 2017 till date, 541 MSMEs registered on the digital MSME scheme but only 22 have been approved for subsidy. Digital MSME scheme insists on Udyog Aadhar, and given that MSME registrations of Udyog Aadhar is less than 15% of total MSMEs in India, this scheme is yet to pick up pace.

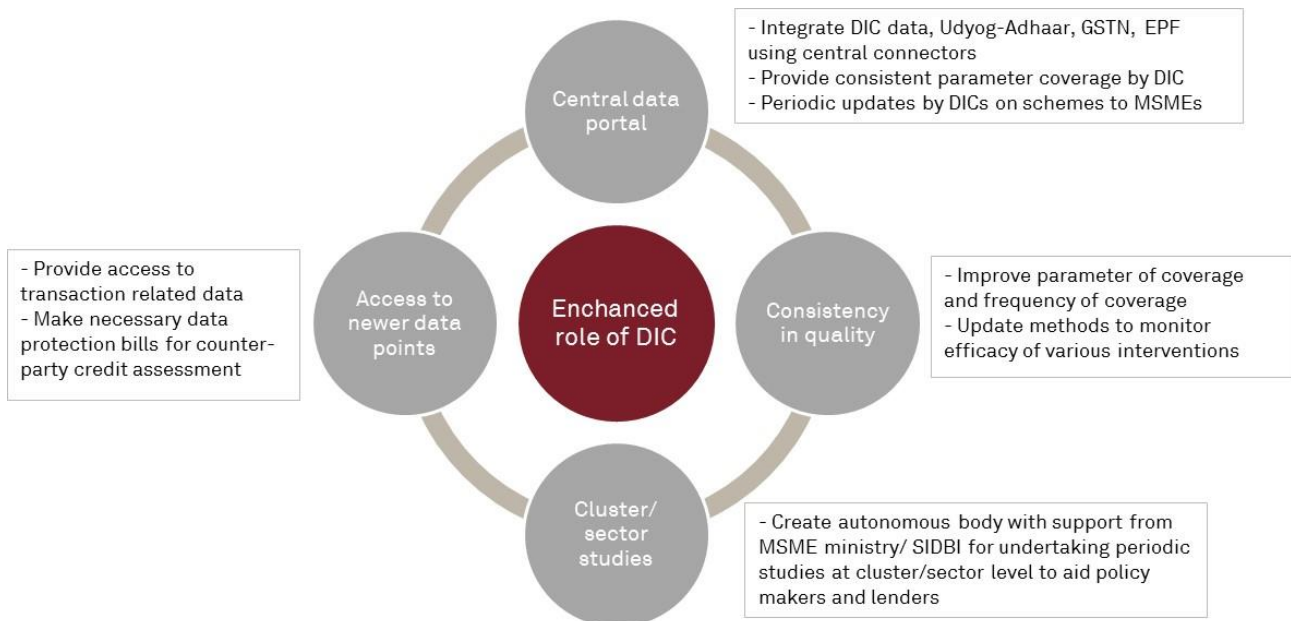
Focus areas

It is clear that nothing short of relentless reforms in MSME lending can tilt the balance in favour of the sector. The thrust areas going forward, where the government and regulators need to focus on, can be summed up as below:

Build a comprehensive and quality database to aid in decision making

- Create integrated and centralised data portal
- Improve quality through linkages and consistent parameters
- Make available newer data points (GST, CERSAI) with necessary data protection measures
- Conduct periodic cluster studies that will enable policy formulation

Enhance role of DIC



Source: CRISIL Research

Make additional allocation for cluster development

Most MSME clusters in India are fragmented and lack effective integration across value chains. By consolidating processes seamlessly, utilisation can be improved. Through government interventions, large scale sector specific manufacturing zones (like in case of food processing) can be identified and developed.

Cluster Development Programme for MSMEs launched by the government has approved 140 common facility centres and 240 infrastructure development programs as of October 2019. However, MSME

clusters are still inadequately equipped for tool rooms, innovation centres, testing facility, etc. Cluster prioritisation and enhance funding are essential. Currently, a large portion of these cluster development initiatives are funded by public agencies. Additional allocation for cluster development and ways to increase private contribution through bonds, CD, etc., must be explored

Increase proportion of MSME book in priority sector lending; create sub-target for manufacturing within

At present, banks have a target of lending to MSMEs, which is just 7.5% of overall priority sector lending. Moreover, a large portion of this goes to services. There is a need to increase share of priority sector lending for MSME credit and assign a sub target for manufacturing within that.

Improve transparency and ease of expanding business

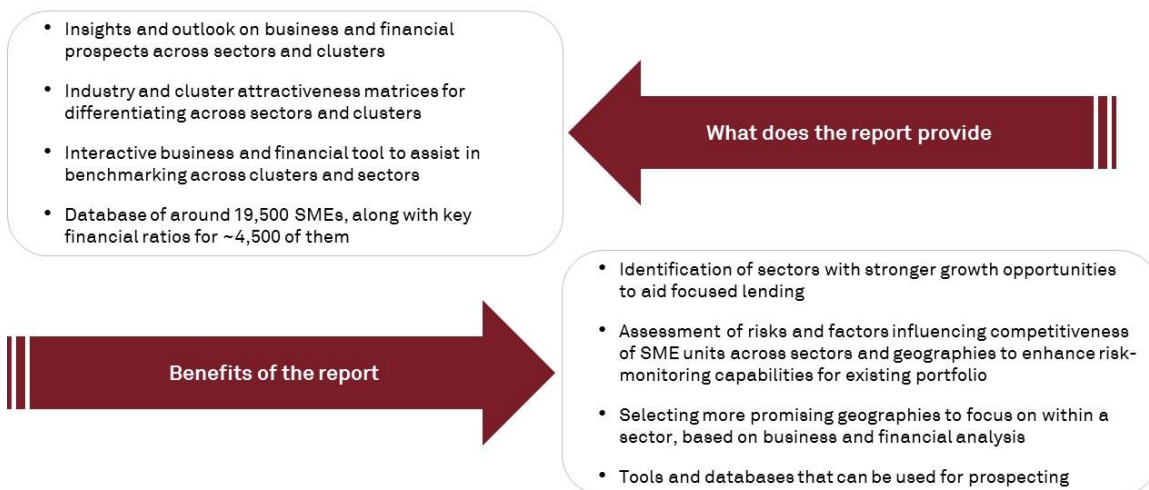
By improving transparency in business processes and timely compliance with statutory filing, MSMEs can improve their credit behaviour and hence, create ease of funding from lender's perspective. With digital commerce growing at a rapid pace, expansion through online channels opens up business opportunities to a larger audience. For sustainable growth of all stakeholders, the right policy framework will be essential.

CRISIL Research SME offerings

Operational Scorecards



SME Report



Sector / cluster / Geography assessment for selection and expansion decisions

- Trend in market size and growth outlook; sources of funding of SMEs
- Working capital loans utilization levels
- Customer profile and acquisition strategy
- Competitive scenario (share of private banks, public banks, NBFCs)

Competitive benchmarking

- Operational Parameters: Trend in AUM and disbursements, Product mix, Geographic and tier-wise mix of branches, AUM/disbursements mix by state/geography, etc.
- Financial Parameters: Yields, Net interest margins, Opex costs, GNPA's and credit costs, Capital adequacy, Leverage levels, Return on assets, return on equity, etc.



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- Industry benchmarks
- SME margins
- Advanced search



Credit Processing / Underwriting

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- Company Profile
- Detailed Financials



Risk Management / Monitoring

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- Credit Portfolio



Treasury / Wealth Management / Investment

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Key Facts



1958
Year of Establishment



4300 Crs
(2019-20)
Group Revenue



2.5%
(by value)
Moving India's GDP



6,000+
Employee Strength



1,400+
IT Enabled Own Offices



12Mn.
sq. ft.
Warehousing Space



12,000
(1,500 own trucks)
Trucks in Operations



TCI Foundation & TCI Institute of Logistics

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E-mail: corporate@tcil.com Web: www.tcil.com
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ASSOCHAM is seen as a forceful, proactive, forward looking institution equipping itself to meet the aspirations of corporate India in the new world of business. ASSOCHAM is working towards creating a conducive environment of India business to compete globally.

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ASSOCHAM represents the interests of more than 4,50,000 direct and indirect members across the country. Through its heterogeneous membership, ASSOCHAM combines the entrepreneurial spirit and business acumen of owners with management skills and expertise of professionals to set itself apart as a Chamber with a difference.

Currently, ASSOCHAM has more than 100 National Councils covering the entire gamut of economic activities in India. It has been especially acknowledged as a significant voice of Indian industry in the field of Biotechnology, Banking & Finance, Corporate Social Responsibility, Civil Aviation, Company Law, Corporate Finance, Competency Building & Skill Development, Corporate Governance, Defence, Environment & Safety, Energy & Power, Education, Economic and International Affairs, HR & Labour Affairs, Information Technology, Infrastructure, Luxury, Legal Reforms, Mergers & Acquisitions, Real Estate and Rural Development, Sports, Telecom, Tourism to mention a few.

ASSOCHAM has been a significant contributory factor in the emergence of new-age Indian Corporates, characterized by a new mindset and global ambition for dominating the international business. The Chamber has addressed itself to the key areas like India as Investment Destination, Achieving International Competitiveness, Promoting International Trade, Corporate Strategies for Enhancing Stakeholders Value, Government Policies in sustaining India's Development, Infrastructure Development for enhancing India's Competitiveness, Building Indian MNCs, Role of Financial Sector the Catalyst for India's Transformation.

ASSOCHAM derives its strengths from the following Promoter Chambers: Bombay Chamber of Commerce & Industry, Mumbai; Cochin Chambers of Commerce & Industry, Cochin; Indian Merchant's Chamber, Mumbai; The Madras Chamber of Commerce and Industry, Chennai; PHD Chamber of Commerce and Industry, New Delhi.

Together, we can make a significant difference to the burden that our nation carries and bring in a bright, new tomorrow for our nation.

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