



MSMEs back to the grind

April 2022

Contact us:

CRISIL

Bhushan Parekh

Director, SME Solutions

bhushan.parekh@crisil.com

Manasi Kulkarni

Associate Director, SME Solutions

manasi.kulkarni@crisil.com

Roosha Sengupta

Analyst, SME Solutions

roosha.sengupta@crisil.com

ASSOCHAM

Mohd Nahid Alam

Joint Director and Head MSMEs Department

nahid.alam@assocham.com

Deepanshu Shokeen

MSMEs Department

deepanshu.shokeen@assocham.com

Contents

Message from CRISIL	4
Message from ASSOCHAM	5
MSMEs backbone of the Indian economy	6
Lending scenario for MSMEs.....	9
Recent government policy intervention.....	13
Digitalisation of the sector.....	16
MSMEs going global	20
Growth drivers and roadblocks in global market	22
Key monitorables	26

Message from CRISIL

India has returned to a firm growth path after a rocky ride amid the lockdowns and restrictions to contain the Covid-19 pandemic last fiscal. A large part of the rebound is being supported by micro, small and medium enterprises (MSMEs), which are a crucial cog of the economy in terms of contribution to gross domestic product (GDP), employment generation, exports, and lending opportunities.

The going was tough for the segment for the better part of fiscal 2021. As per CRISIL estimates revenue of MSMEs declined 7-10% on-year in fiscal 2021. According to a Small Industries Development Bank of India (SIDBI) survey, ~67% MSMEs temporarily shuttered operations during the first three months of the fiscal because of nationwide and state-imposed lockdowns, with ~66% reporting contraction in profitability as revenue declined amid dogged fixed costs.

A raft of measures by the government under its Aatmanirbhar Bharat banner has provided reprieve to most MSME sectors in recent months. These include Rs 20,000 crore subordinate debt for stressed MSMEs, Rs 50,000 crore equity infusion through MSME Fund of Funds (SRI Fund), 3 lakh crore Emergency Credit Line Guarantee Scheme (ECLGS) for businesses, including MSMEs (which was subsequently increased to 5 lakh crore in Union Budget 2022-23, change in definition of what constitutes an MSME, and no global tenders for government procurement up to Rs 200 crore.

The cumulative force of these levers is expected to push up the sector's growth by 15-17% on-year in fiscal 2022, with the trajectory projected to sustain into fiscal 2023, albeit at a slightly slower pace. However, the quantification of the geo-political risk arising out of the Ukraine-Russia conflict is yet to be assessed.

In line with revenue growth, Ebitda margins are expected to improve, albeit a slower pace in fiscal 2022 as industry begins to normalise. A further improvement is expected in fiscal 2023 as input prices stabilise and realisations trend higher. However, the geo-political tension and rising crude oil prices can be a deterrent.

Supporting the MSMEs is increased credit, with bulk of the disbursements driven by the ECLGS. CRISIL Research expects overall MSME credit (from banks and non-banks) to grow at 8-9% on-year to Rs 18 lakh crore in fiscal 2022. In the long term as well, the segment will continue to offer attractive opportunities for financiers as the global economy recovers and adoption of China-plus-one strategy by large players to diversify their supply chains provides a boost to export-linked MSMEs.

However, the wave is unlikely to lift all boats. The challenge is in spotting the sectors and clusters that were relatively less affected during the peak of the pandemic and are likely to offer the desired risk-adjusted returns.

That entails timely tracking of performance and riskiness of sectors and clusters. Furthermore, opportunities may emerge with the rollout of the Production Linked Investment (PLI) scheme, with SMEs in a few sectors benefiting considerably.

While the future holds a lot of promise, the short-term uncertainties around geo-political tensions and rising global inflation could play spoilsport.

Bhushan Parekh
Director
CRISIL Research



Message from ASSOCHAM

The Micro, Small and Medium Enterprises (MSME) sector has been the key focus of policymakers from the central government and state governments as a valuable contributor to overall economic growth and development in terms of employment, value chain creation, foreign exchange earnings, critical supplier of large industries, promotion of regional balance and inclusive development etc. Keeping in mind the MSMEs' contribution and significance, ASSOCHAM has spearheaded many activities to support and handhold MSMEs. One of these critical initiatives was the 'ASSOCHAM MSMEs Excellence Awards & Summit' which was initiated in 2013. The objective of the award is to acknowledge the MSMEs for significant contributions to various sectors of the economy.

ASSOCHAM have more than 4,50,000 members, of which **MSMEs** represent a large segment. With a strong presence in states and key cities globally, ASSOCHAM also has more than 400 **associations, federations and regional chambers** in its fold. Aligned with the vision of creating a **New India**, ASSOCHAM works as a conduit between the industry and the Government.

Over the past five decades, the Indian **MSME sector** has become highly dynamic and vibrant. The sector contributes substantially to the economic and social development of the country by promoting **entrepreneurship** and creating large employment opportunities.

The country is home to more than **63 million MSMEs**, contributing nearly 30 per cent to the country's **GDP** and providing a source of livelihood to approximately 11 crore people. By 2025, the MSME Ministry targets to expand the sector's contribution to the country's GDP by up to 50 per cent. In 2021–2022 (April–September), MSME-related products accounted for 45.8 per cent of the country's total exports.

MSMEs play a crucial role in enabling the country's economic growth. Now that India hopes to establish itself as a USD 5 trillion economy, more focus is being placed on them. In Budget 2022–2023, allocation to the MSME sector was increased to INR 21,422 crore as compared to the INR 15,699.65 crore in the previous year.

Amidst the global pandemic, India has found its innate strength to brave the storm and focus on developing its domestic ecosystem, to support both the Indian and the global markets. The **Aatmanirbhar Bharat vision** that has been laid by the Hon'ble Prime Minister has enthused the Indian industry with confidence that will help us enhance our global play.

While the MSME segment was significantly hit by the COVID-19 pandemic, continued support from the Government has ensured that the stress is minimized, and their recovery is facilitated. The measures introduced by the Government to promote manufacturing through **Make in India, PLI schemes**, etc., will help Indian **MSMEs** gain a strong foothold in global value chains.

CRISIL was engaged as the 'Knowledge Partner' for the 8th ASSOCHAM MSMEs Excellence Awards & Summit, and we appreciate the CRISIL team for the knowledge report on "MSMEs back to Grind". ASSOCHAM congratulates all the awardees for their achievements and conveys our best wishes to the other participants for keeping up their good performance.



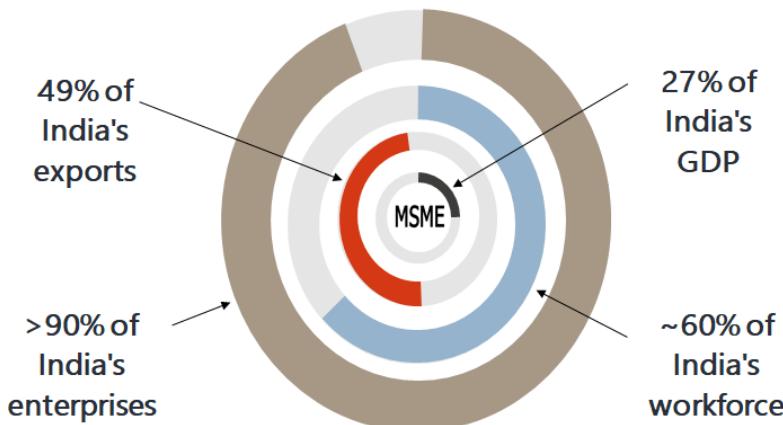
Deepak Sood
Secretary General
ASSOCHAM

MSMEs backbone of the Indian economy

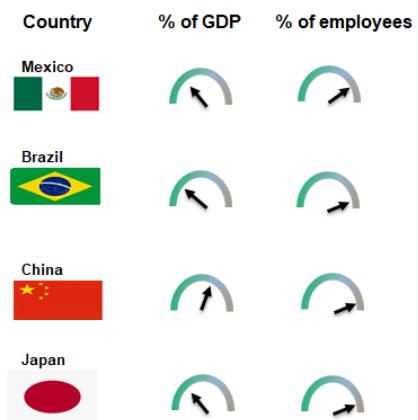
Despite Covid-19, MSMEs major contributors to India's economy

The MSME segment in India, with estimated 6.3 crore units, employing over 11.10 crore people, accounting for 27% of GDP, and comprising 49% of the export pie (as per MSME ministry), is crucial to the functioning of the economy. Even, globally, MSMEs are the engine of economies.

MSME share hovering around 27-30% of GDP over past three years well



Engine of growth globally as well



Source: Press Information Bureau (PIB) 2021, Lok Sabha Questions, Ministry of MSME

A note: CRISIL has considered the new MSME definition passed by the Union Cabinet in June 2020, which classifies entities with turnover of less than Rs 250 crore and investment up to Rs 50 crore as MSMEs.

Definition of MSMEs

Existing MSME classification			
Criteria : Investment in plant & machinery or equipment			
Classification	Micro	Small	Medium
Manufacturing	Investment <Rs 25 lakh	Investment <Rs 5 crore	Investment <Rs 10 crore
Services	Investment <Rs 10 lakh	Investment <Rs 2 crore	Investment <Rs 5 crore

Revised MSME classification			
Composite criteria: Investment and annual turnover			
Classification	Micro	Small	Medium
Manufacturing and services	Investment <Rs 1 crore Turnover <Rs 5 crore	Investment Rs 1-10 crore Turnover Rs 5-50 crore	Investment Rs 10-50 crore Turnover Rs 50-250 crore

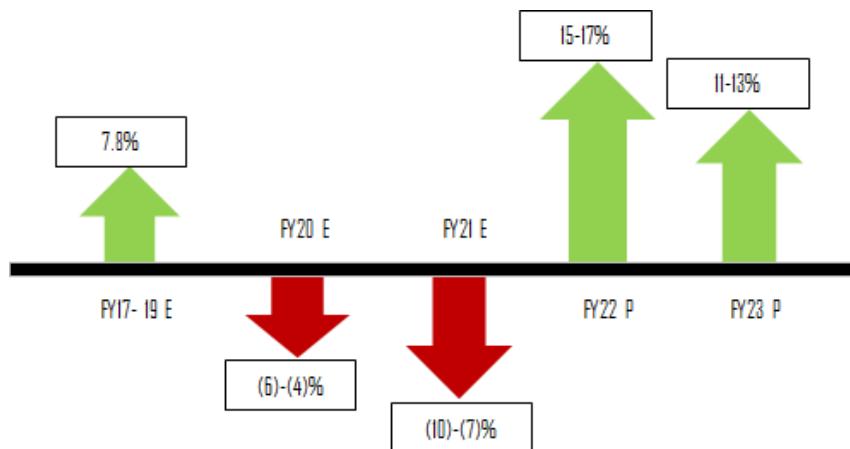
Source: Ministry of Micro, Small and Medium Enterprises

MSMEs have rebounded sharply in fiscal 2022 on a low base; profitability returning to pre-pandemic levels

The MSME segment is expected to post 15-17% on-year growth in fiscal 2022 as demand revives following pick-up in economic activity with gradual easing of restrictions. The government's thrust on infrastructure spending, along with gradual decline in Covid-19 infections, has translated into a sustained recovery in domestic demand. Export demand is also expected to rise sharply as global economies return to normalcy with Covid-19 infection rates also under control. Rising revenue will have a corresponding positive impact on Ebitda margin. The downside arising from the geo-political risk of the Ukraine-Russia conflict and rising inflation remains a key monitorable.

The segment will continue to post growth in fiscal 2023, albeit at a slightly lower rate. Ebitda margins are expected to improve as well as input prices stabilise and realisations trend higher.

MSME revenue on comeback trail



E: Estimated; P: Projected

Source: CRISIL Research, Quantix

In fiscal 2021, the revenue of the MSME segment fell owing to the pandemic and consequent lockdowns. Ebitda margin contracted as well, as weak demand and low utilisation more than offset benign commodity prices.

Size-wise financials

Parameters	Units	Rs 5-50 crore				Rs 50-250 crore			
		FY18	FY19	FY20	FY21*	FY18	FY19	FY20	FY21*
No. of companies	%	14347	12651	9941	1498	17533	16159	12743	2265
Ebitda margin	%	5.1	5.5	5.4	4.5	6.4	6.6	6.3	6.8
Net profit margin	%	0.9	1.1	1.1	1.1	1.2	1.4	1.3	2.0
Debt-equity ratio	Times	0.8	0.8	0.6	0.1	1.0	0.9	0.8	0.3
Interest coverage ratio	Times	1.4	1.6	1.5	1.1	2.0	2.2	2.2	2.6
Return on capital employed	%	7.7	8.1	7.3	4.3	9.9	10.2	9.5	8.6

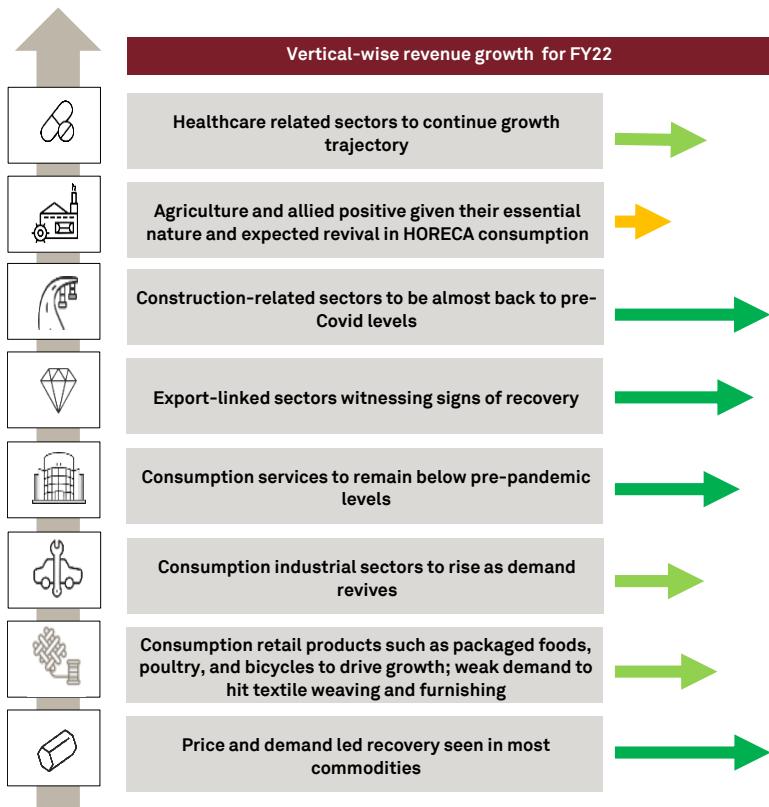
Parameters	Units	Rs 5-50 crore				Rs 50-250 crore			
		FY18	FY19	FY20	FY21*	FY18	FY19	FY20	FY21*
Asset turnover ratio	Times	3.5	3.9	3.5	2.4	2.9	3.1	2.9	2.4
Working capital days	Days	191	183	197	235	120	107	116	153
Debtor days	Days	62	65	67	65	60	58	58	68
Creditor days	Days	44	48	50	31	57	54	56	59
Inventory days	Days	39	43	44	27	42	43	44	49

Note: * Number of companies lower because of delay in filing by companies in Ministry of Corporate Affairs

For Rs 0-5 crore segment, data is not significant

Source: Quantix

Recovery seen across sectors; construction, commodities, exports, and consumption services leading the pack



Source: CRISIL Research

Lending scenario for MSMEs

MSME credit to reach Rs 18 lakh crore in fiscal 2022 propelled by ECLGS and other interventions

MSME lending by banks and non-banking finance companies (NBFCs) is expected to grow 7-9% on-year in fiscal 2022, supported by gradual improvement in demand amid rapid economic growth. Within the lending space, though, book growth of banks is projected to be higher at 8-10% on-year vis-à-vis NBFCs, which is forecast at 5-7%.

In fiscal 2021, credit to MSMEs rose 7% on-year, supported by favourable government measures. Given that banks comprise ~80% share in total lending to the segment, disbursements under ECLGS led to healthy growth of 8% in banks' credit, thus supporting overall credit growth.

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



P: Projected

Source: CRISIL Research

The MSME segment was severely affected by the first and second waves of the pandemic, i.e. in fiscal 2021 and in the first quarter of fiscal 2022, respectively. The magnitude of impact was because of the frequent lockdowns and restrictions, which impacted demand and supply, and, hence profitability across most sectors. This necessitated relief measures by the government, in the form of ECLGS in fiscal 2021.

As most of the disbursements under the scheme were by banks, they saw a book growth of 8% on-year, whereas for NBFCs, it was lower at 3%. Also supporting the overall book were moratoriums and standstill asset classification for MSMEs until March 2021. In the first quarter of fiscal 2022, there was lower impact as NBFCs' MSME book was flat.

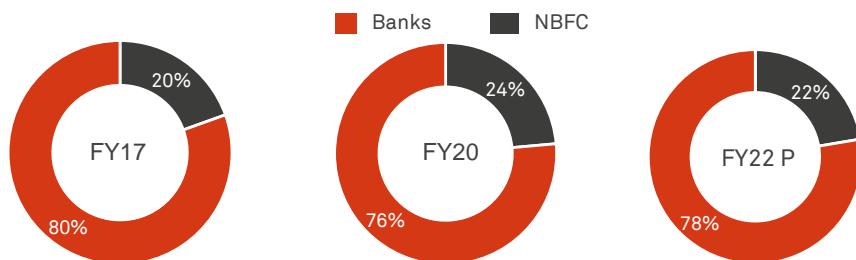
With revival in economic activity and strong export and domestic support, MSME demand is expected to see an uptick, resulting in higher disbursements.

Banks continue to dominate MSME lending

Banks dominate the MSME lending book, with a share of 77% as of fiscal 2021. However, over the past three fiscals, ending fiscal 2020, NBFCs increase their share by ~650 bps to 23%, owing to aggressive lending.

The trend is expected to reverse going forward, though. MSME lending is driven by ECLGS, with public and private sector banks providing bulk of the disbursements. NBFCs are going slow, given their already existing asset quality concerns. NBFCs are expected to conserve liquidity in such challenging times as well. The lower disbursal towards the scheme is also because of capping of interest rates on such additional lending, translating into thin margins. The interest rate under the scheme is capped at 9.25% for banks and financial institutions, and 14.0% for NBFCs.

Trend of rising NBFC share to reverse going forward



P: Projected

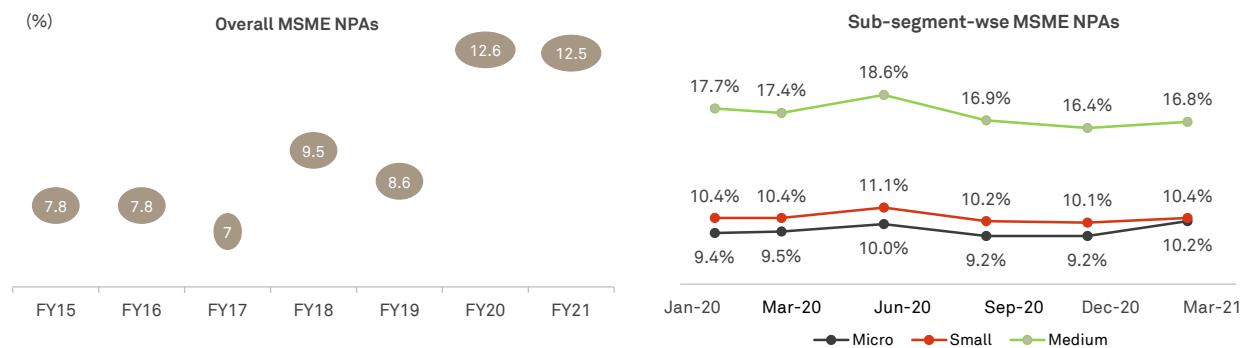
Source: CRISIL Research

Asset quality a monitorable for fiscal 2022

Lending to the MSME segment rose sharply in fiscal 2021, aided by support measures from the government, resulting in limiting of non-performing assets (NPAs) at 12.5%. Under ECLGS, loans of Rs 2.82 lakh crore were sanctioned till November 2021, of which ~81% was disbursed.

However, asset quality concerns increased in the first quarter of fiscal 2022 as the second wave once again affected MSMEs, impacting collections. Collections in April and May 2021 plunged, with high delinquencies. In fact, the NPA level rose steeply to 18.5% in September 2021 from 16.8% in March 2021-. The drop was largely in the sub-Rs 25 crore ticket size across major banks.

High credit disbursal led to stable NPAs in fiscal 2021; segment-wise NPAs mirrored the trend



Source: CRISIL Research and SIDBI TransUnion

Despite the post-Covid-19 recovery, asset quality of the MSME segment is expected to deteriorate in fiscal 2022 as stress continues in some MSME segments, leading to slippages. Bank credit deployment to MSMEs dipped in September 2021 as compared with March 2021, as the second wave of Covid-19 forced borrowers as well as lenders to tread cautiously, leading to a contraction in bank credit.

Bank credit to MSMEs declined in September 2021...

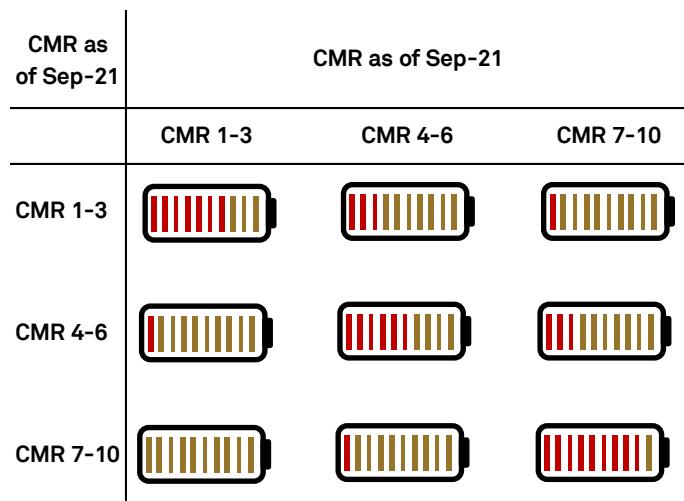
(y-o-y growth)	PSB		PVB		Total	
	Mar-21	Sep-21	Mar-21	Sep-21	Mar-21	Sep-21
Exposure < 25 crore	8.08	0.2	8.04	0.38	8.06	0.28
Aggregate MSME Exposure	0.89	1.01	9.23	2.98	4.5	1.9

Source: RBI Financial Stability report December 2021

Transition from low-risk to high-risk category seen during pandemic

There was noteworthy transition of low- and medium-risk MSME borrowers to the high-risk category owing to the second wave, as per CIBIL MSME Rank, which predicts the probability of an MSME loan turning into an NPA in the next 12 months.

CIBIL MSME rating



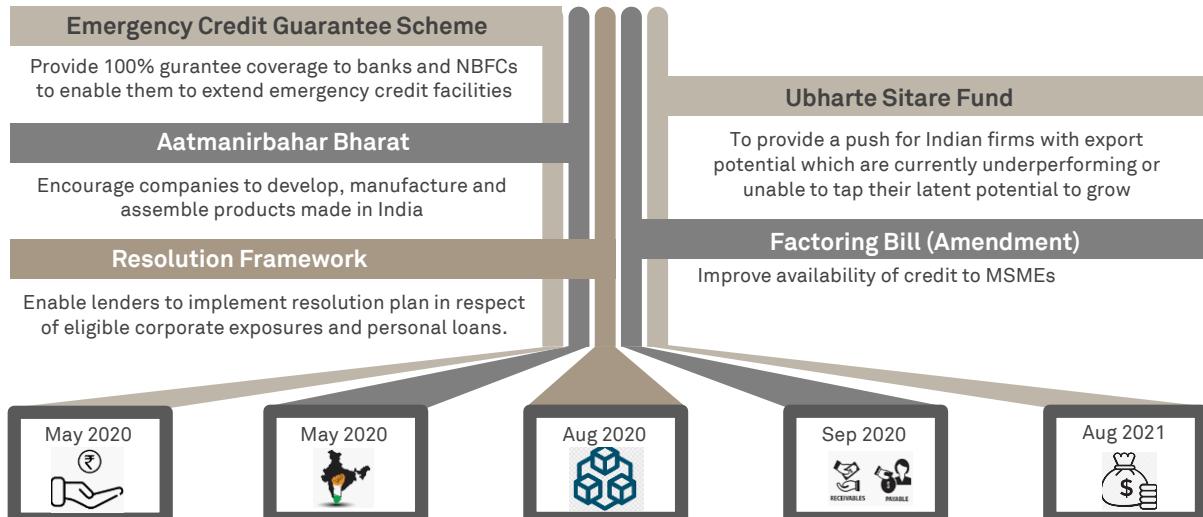
Source: RBI Financial Stability report December 2021

However, a faster-than-expected uptick in economic activity since relaxation of lockdowns, and pent-up and festive season demand, helped thereafter.

Recent government policy intervention

The Indian government, over the past two years, has initiated multiple steps to improve funding access of MSMEs in the aftermath of the Covid-19 crisis. However, effectiveness of most schemes remains muted.

Government's thrust to address MSME liquidity concerns post Covid-19 outbreak

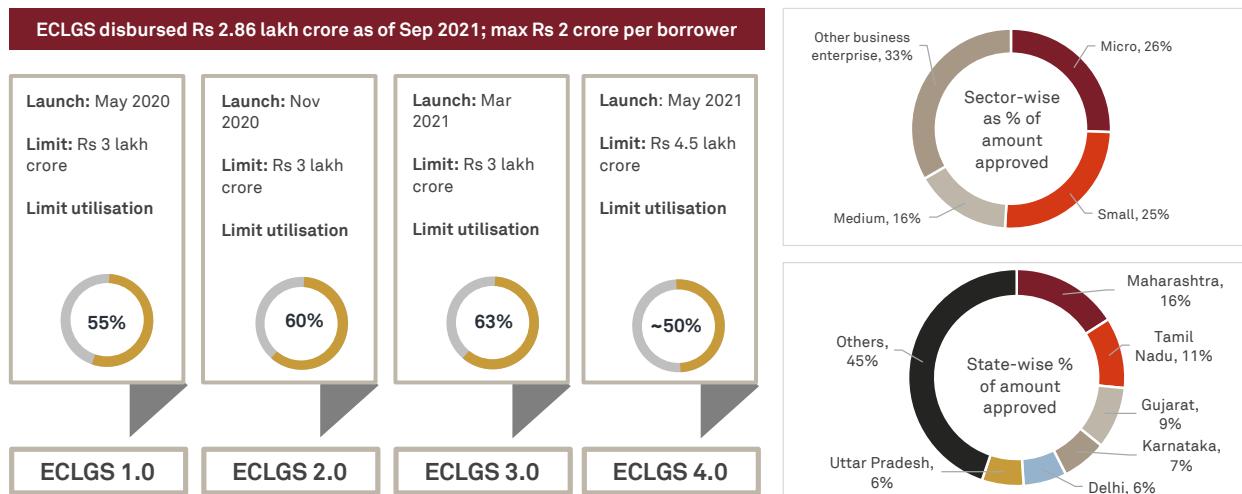


Source: CRISIL SME Solutions

- ECLGS timely addressed MSME funding requirements**

Launched as a part of the Covid-19 relief package, the scheme extends emergency credit facility by banks and NBFCs to MSMEs to meet their additional term loan/ working capital requirement. The scheme has played a crucial role, with ~43% on-year growth in disbursement in funds to MSME segments as of December 2021.

Large part of disbursements towards MSMEs driven by ECLGS



Source: SIDBI TransUnion, PIB, CRISIL SME Solutions

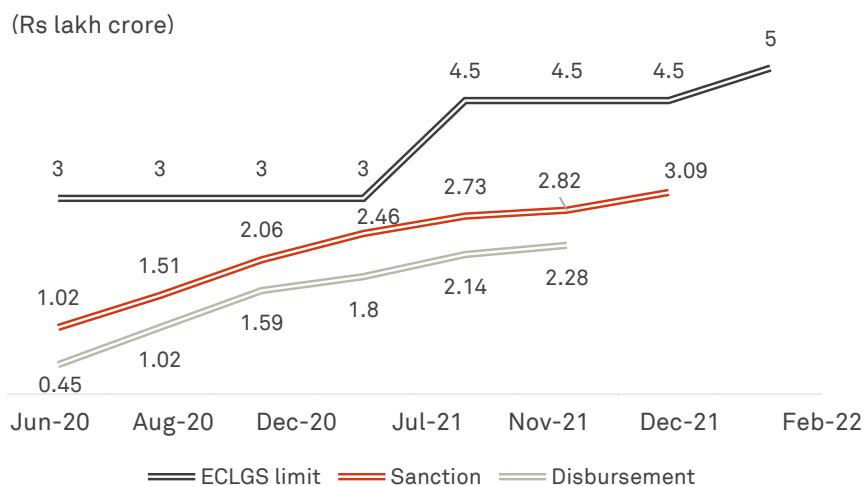
Given the second wave, the timeline of the scheme has been extended to March 2022 or till guarantees for Rs 4.5 lakh crore are issued under the scheme, whichever is earlier. The following changes have been incorporated following the second wave:

- Current borrowers under ECLGS 1.0 and 2.0 would be eligible for additional credit support of up to 10% of total credit outstanding as on March 2021, whichever is earlier
- Businesses that have not availed assistance under ECLGS 1.0 or 2.0 can avail credit support of up to 30% of their credit outstanding as on March 2021

In order to provide support to sectors like hospitality, travel and tourism, and leisure, which were among the most affected in the pandemic, the government announced ECLGS 3.0. ECLGS 3.0 involves the extension of credit from 20% to up to 40% of the total credit outstanding across all lending institutions as of February 2020.

Last date of disbursement under the scheme has been extended to March 2023 in Union Budget 2022-23, with guaranteed cover also extended by an additional Rs 50,000 crore. This takes total allotment under the scheme to Rs 5 lakh crore.

ECLGS progress up to February 2022



Note: Disbursement data for December 2021 is not provided by the respective authority

Source: SIDBI TransUnion, PIB, CRISIL Research

- **Aatmanirbhar Bharat – an impetus for growth for MSMEs**

This is a national programme launched by the government in fiscal 2020 to facilitate businesses and promote local manufacturing, giving special thrust to MSMEs. The following announcements were made under the scheme to benefit MSMEs buffeted by the pandemic:

- Rs 3 lakh crore collateral-free automatic loans to buy raw material, meet operational liabilities, and restart businesses
- Revision of MSME definition to extend maximum benefits to the sector
- Disallowing global tenders in procurement up to Rs 200 crore
- Clearing of MSME dues by the government and public sector units within 45 days

- **Resolution Framework to help MSMEs tide over Covid-19 crisis**

Resolution Framework 1, which was announced as a Covid-19 relief package in August 2020, enables lenders to mitigate the burden of debt and ensure continuity of businesses. It primarily covered:

- Requirements specific to resolution of advances to individuals and small businesses
- Working capital support for individuals who have availed of loans for business purposes, and small businesses, where resolution plans were implemented previously
- Disclosure requirements for lending institutions with respect to resolution plans implemented under this scheme
- Given the resurgence of the pandemic in April 2021 and consequent restrictions, the RBI announced Resolution Framework 2 with some modifications

- **Ubharte Sitare Fund to support export-oriented MSMEs**

Set-up by EXIM Bank and SIDBI, Ubharte Sitare Fund is an export-oriented fund with focus on MSMEs. It identifies Indian firms with potential advantage by way of technology, products, or processes, but are currently underperforming or unable to tap their latent potential to grow. The fund is a mix of structured support, financial as well as advisory services, through investments in equity or equity-like products, debt (funded and non-funded), and technical assistance (advisory services, grants and soft loans), with a corpus of Rs 250 crore. Export-oriented sectors such as gems and jewellery, IT-enabled services, etc with high potential, but facing issues due to the pandemic, will benefit from the scheme.

- **Factoring Bill to expand formal credit facilities for MSMEs**

Factoring Amendment Bill 2021 is stated to benefit MSMEs by monetising their receivables quickly and address cash-flow issues on time. Earlier, the RBI allowed NBFCs in factoring only if it was their principal business. However, the 2021 amendment removes this threshold for NBFCs. This led to a jump from two to nearly 5,000 NBFCs in the factoring business. While higher supply of funds will help lower costs for MSMEs, easier liquidity will help address working capital concerns.

Apart from these schemes, Make in India, which was launched by the government in 2014, acts as a catalyst for MSMEs. The policy is designed to facilitate investment, foster innovation, enhance skill development, and build a strong manufacturing infrastructure in the country. In line with this, the government has exempted over 350 items, phasing out concessional rates in capital goods as well as project import scheme, which would be critical in providing much-needed push to ease of doing business, thereby boosting Make in India and Aatmanirbhar Bharat initiatives.

Apart from these, the government announced Raising and Accelerating MSME Performance programme in the recent budget. Under this, Rs 6 lakh crore will be provided to MSMEs over the next five years to help them become more resilient, competitive and efficient.

Digitalisation of the sector

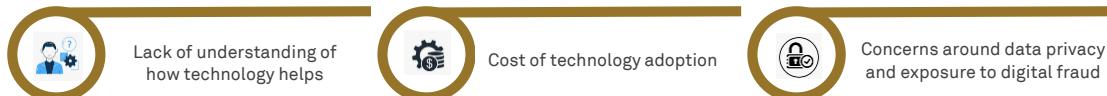
Digitalisation allows MSMEs to gain greater access to diverse global markets and mitigate supply chain risks

The Covid-induced lockdown and restrictions impacted MSME earnings by 7-10%. Only agile businesses have a better chance to succeed. Digitalisation can support MSMEs in the immediate to short run by helping manage transactions at a distance, deliver goods efficiently, and facilitate access to financial services. It can bring in tangible benefits such as enhanced customer acquisition, operational efficiency, workforce enhancement, risk management, innovation and reduction in manpower requirement for MSMEs. As per the CRISIL survey, currently, less than 10% of MSMEs are leveraging technology.

Digitalisation brings ample opportunities to MSMEs



Opportunities comes with challenges

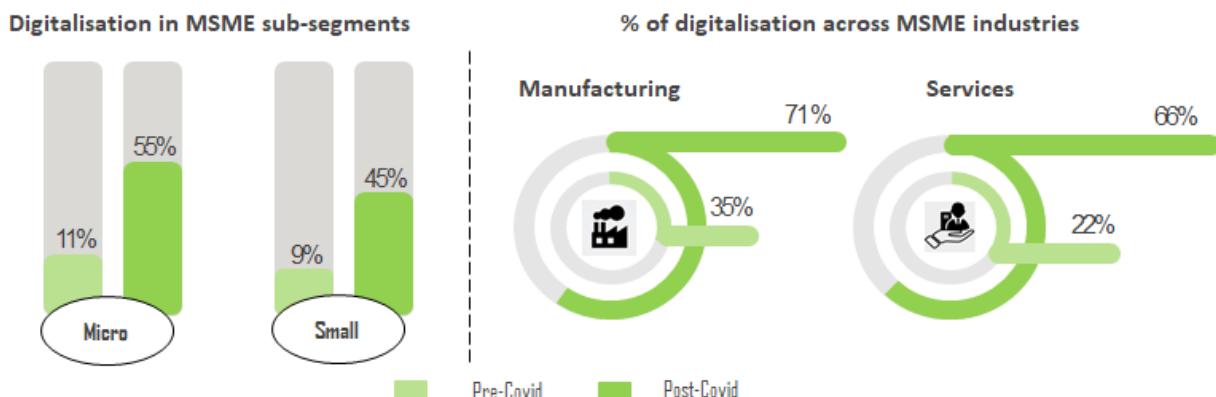


Source: CRISIL SME Solutions

Covid-19 has accelerated the digital transformation of MSMEs...

A CRISIL survey of over 500 MSMEs reveals that the digital footprint of MSMEs has expanded post Covid-19 disruption last year. The digital route to secure instant credit has helped the MSME loan book of digital platforms swell on-year.

Traction in digitalisation seen across MSME segments



Source: CRISIL SME Solutions

.....giving a boost to digital lending

The digital route to secure credit has helped MSMEs draw formal credit post pandemic. Increased internet penetration and growing adoption of affordable smartphone devices coupled with digital lenders plugging the information asymmetry gap have also pulled MSMEs towards the digital channel. Digital lending platforms have worked in partnership with banks to enable MSMEs sign up for the ECLGS.

Given the growing shift towards digital lending, neo-banks largely focussed on MSME lending comprising small ticket loans, and fintechs, are expected to witness rapid growth.

Basic information regarding MSME units is scattered across various databases such as the Udyog Aadhaar Memorandum (UAM), MSME Databank, and GSTN. There is an urgent need to formalise the sector in order to boost formal credit flow to the MSMEs. Various schemes such as Udyam, Open Credit Enablement Network (OCEN), and Trade Receivable Discounting System (TReDs) have been launched to address these issues.

In the latest budget, the government announced inter-linkage of the portals such as UDYAM, e-Shram, NCS and Aseem. These will act as live databases providing G2C, B2C and B2B services such as enhancing entrepreneurial opportunities and easy upskilling, benefiting the growth of MSMEs. A closer look at the progress and challenges in the usage of these platforms:

- **Udyam registration yet to pick-up**

Udyam registration replaced UAM in July 2020 following the revised definition of MSME by the government. The pandemic has underscored the need to move to a digital platform. By registering on the portal, MSMEs can benefit from the provisions under various existing schemes and incentives including priority sector lending. As of February 2022, ~75 lakh MSMEs have registered on the portal, of which 95% are micro, 4% small and 1% medium enterprises.

In an attempt to nudge more enterprises to become lifetime Udyam, the government has integrated the system with the TReDS and the Government e-Marketplace (GeM). The new Udyam registration process has boosted the ease of doing business for MSMEs by reducing transaction time and costs.

- **TReDS is gathering pace**

TReDs is an online bill discounting platform launched by the Reserve Bank of India (RBI) in 2014 with an aim to ease working capital. The RBI, in January 2022, allowed all non-deposit taking NBFC-investment and credit companies (NBFC-ICCs) with asset size of Rs 1,000 crore and above to carry on with factoring business, significantly boosting the number of such companies to 182 from seven earlier. This enables MSMEs to get immediate liquidity instead of waiting for the bills to be honoured by the customers.

As of January 2022, three entities are operating the TReDS platform in India (RXIL, M1xchange and Invoicemart) and have since collectively discounted invoices worth Rs 15,000 crore drawn by 25,000 MSMEs from Rs 6,700 crores in fiscal 2019.

- **OCEN yet to gain traction**

This network is a set of open standards to facilitate the various aspects of the lending value chain by providing consent-based access to verified information from multiple public and private data sources, it connects borrowers with lenders through an ecosystem that offers access to affordable credit.

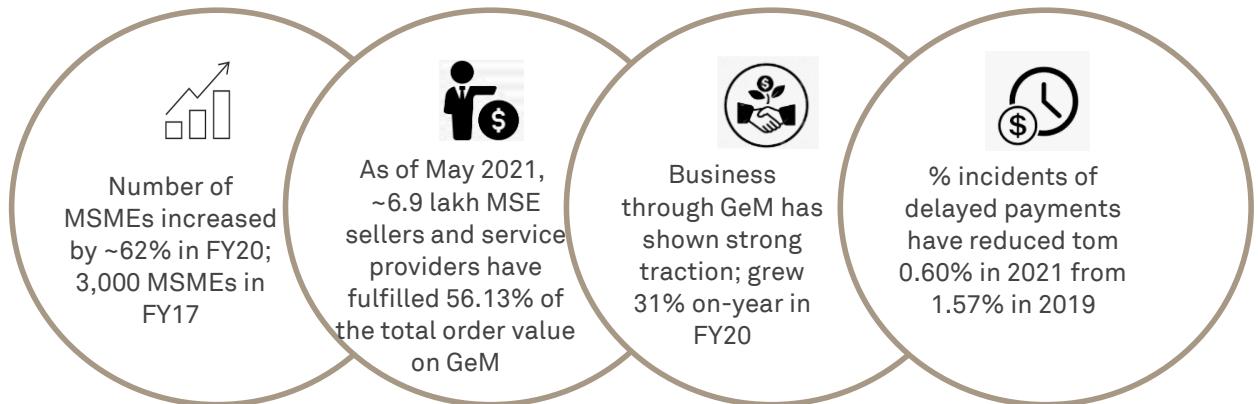
OCEN collects data through the digital space. Automation of all the process steps—from establishing the identity of the applicant, to document submission, underwriting, signing of loan agreement, lien marking of future receivables and repayment collection—makes it possible to disburse the loan in a short period of time and helps address the liquidity crunch faced by MSMEs.

However, given the low presence of MSMEs on the digital platform, realisation of the full potential of OCEN remains low.

- **GeM portal gains MSME interest**

The government had set up a dedicated e-market in 2016 for purchase of certain standard day to day use goods. It enables buyers and sellers to interact with each other and bid for services and products.

Momentum of GeM portal



Source: Press Information Bureau, Lok Sabha questions

In order to further smoothen the seller registration process for MSMEs on the portal, GeM has operationalised API integration with Udyam registration databases. Details of MSMEs, which have given their consent to share details with GeM, are auto imported on GeM for creation of their seller profile and notification. This would enable MSMEs gain a digital footprint, and thereby, access to formal lending.

- **Account aggregators (AAs)**

This is a new class of NBFCs approved by the RBI to manage consent for financial data sharing. It was created through an inter-regulatory decision by the RBI, SEBI, the IRDAI, the Pension Fund Regulatory and Development Authority (PFRDA) through the Financial Stability and Development Council (FSDC). Many AAs can compete to cater to different users in the Indian market, and data cannot be shared without user consent.

The AA system introduced recently will help individuals and small businesses procure loans from banks without hassles, by digitally sharing financial data across institutions.

The three important constituents in the AA framework are:

1. AA: Entities that facilitate structured financial data sharing from FIPs to FIUs, while retaining a record of the consent provided and offering the functionality to manage and rescind consent
2. Financial information provider (FIP): Any supervised financial sector institution that offers financial services and products such as banking, lending, asset management and insurance
3. Financial information user (FIU): An institution that is registered and supervised by any of the financial sector regulators such as RBI, SEBI, and IRDAI. FIUs can solicit consent from a user by providing details of the data to be captured through an AA identifier

The framework provides a good opportunity to MSMEs to avail of loans quickly.

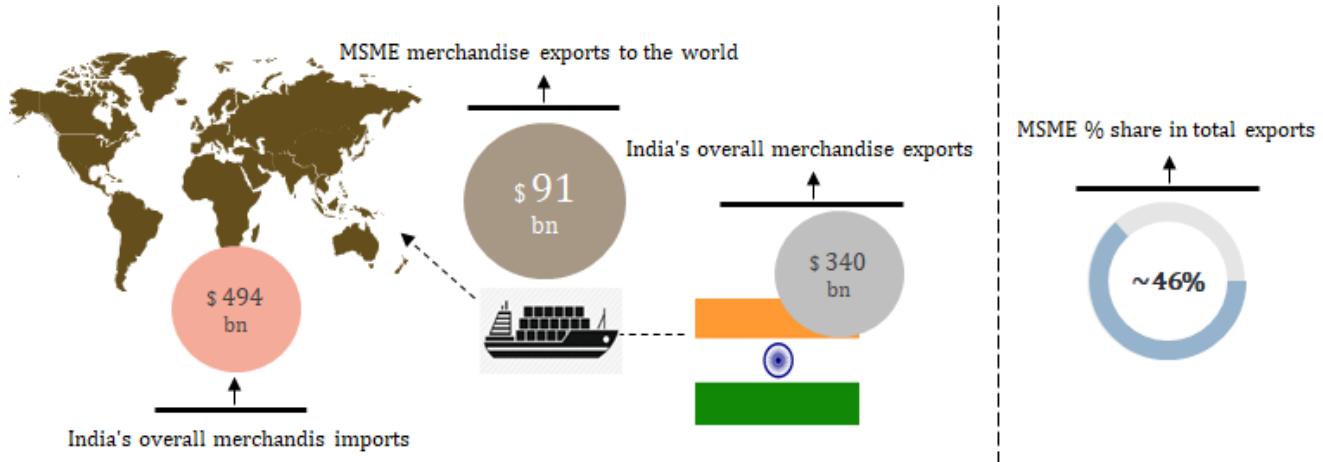
MSMEs going global

MSMEs' share in India's total exports at nearly 50% in past five years

MSME exports contracted 8% on-year in fiscal 2021 owing to Covid-induced lockdowns and an economic slowdown in importing nations.

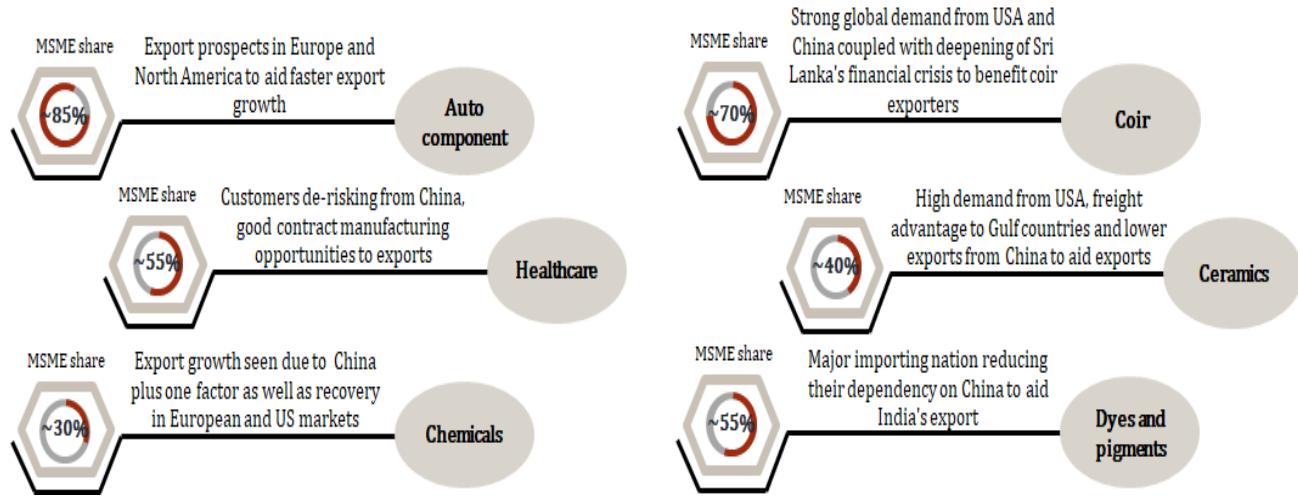
Recovery from the Covid-induced slump, coupled with growing external demand for Indian goods led to a revival in export demand for MSMEs across sectors this fiscal. MSMEs' share in total exports has been hovering at 48-49% from past five years. Exports-linked MSME sectors are on the path to recovery and we expect the trend to continue next fiscal.

MSMEs' share in India's total exports has stayed consistent



CRISIL Research expects export-linked sectors such as gems and jewellery, seafood, IT-enabled services, dyes and pigments, and readymade garments to witness double-digit growth this fiscal, aided by a revival in demand on a low base and restoration of supply chains. These sectors posted a revenue decline in fiscal 2021 owing to the ripple effects of the pandemic and the consequent slowdown in the global economy.

Export-linked MSME sectors to post a strong recovery this fiscal

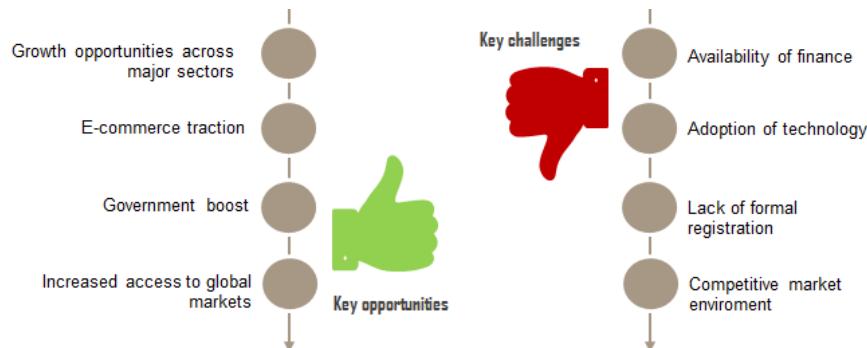


Source: CRISIL Research

With the Covid situation normalising for now and the economies slowly recovering, India's export demand is likely to improve. Moreover, the China-plus one strategy is prompting international players to invest in India, which is expected to benefit Indian MSME exporters.

Growth drivers and roadblocks in global market

Key opportunities and challenges faced by MSMEs in global quest



Source: CRISIL SME Solutions

MSMEs benefit from the following export opportunities:

- Presence and opportunities across major sectors

MSME can provide a strong backbone for the growth by acting as a quality supplier and vendor as well as customer for large companies in various sectors. Towards realising this dream and as a part of Covid-relief, the government launched the Production Linked Incentive (PLI) scheme in April 2020 which aims to produce indigenous products, reduce dependence on a single market or geographical region, cut down on imports and make domestic industries globally competitive. The scheme has a total outlay of Rs 40,995 crore.

PLI in telecom, food products and pharmaceuticals most attractive for MSMEs

Sectors	Total incentives	Scheme period	Direct benefit for MSMEs	Current penetration of MSMEs	Opportunity for MSMEs
Electronics	Rs 12,350 crore	4 years	👎	↗	Outsourcing component manufacturing by large companies such as Lava, and Dixon Tech
Pharmaceuticals- drugs	Rs 15,000 crore	6 years	👍	↗	Direct manufacturing/ value additions
Telecom	Rs 12,195 crore	5 years	👍	↗	Higher incentives, component manufacturing outsourced by large players
Food products	Rs 10,900 crore	6 years	👍	↗	Foster innovation, promote organic products, outsourcing by large branded players

Source: Scheme documents, CRISIL Research

The PLI scheme was launched for a total of 13 sectors which include auto components, automobiles, aviation (drones), chemicals, medical devices, metals and mining, renewable energy, textile and apparel, white goods (consumer durables) and semiconductors.

- **Government support**

To enhance exports and increase localisation, the government has approved a capital infusion of Rs 4,400 crore into the ECGC (earlier known as Export Credit Guarantee Corporation of India) over fiscals 2022 to 2026, among measures to boost exports. It provides insurance covers to banks against risks in export credit lending to the exporter borrowers.

- Leather is an example. Exporters of finished leather are entitled to a duty drawback of 2.36% as against the earlier rate of 1.2%. This would provide a boost to leather exports, which accounts for close to 50% of the overall revenue
- Similarly, The National Programme on Artificial Intelligence provides an impetus to the IT-enabled services (ITeS) sector, as it aims to provide a roadmap to improve skill-sets of Indians, invest in research and sectors that can maximise economic growth, and scale-up Indian-made AI solutions for developing countries. Exports account for 90% of ITeS

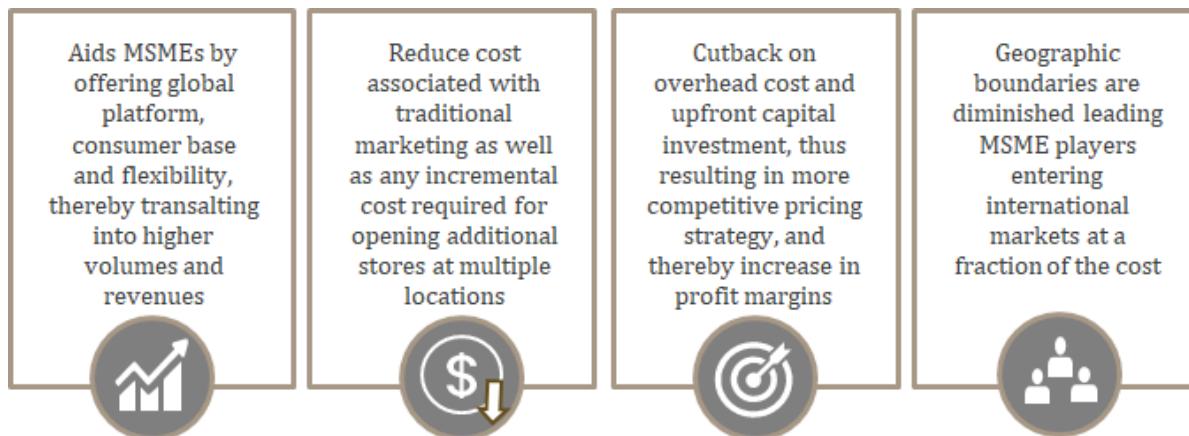
In the Budget 2022-23, the government announced reduced import tariffs on inputs and increased/imposed tariffs on end products. CRISIL expects this to lead to a higher degree of protection and improved competitiveness for MSMEs. Reduction in customs duty and exemptions on inputs, such as steel scrap, despite a 7% duty on finished capital goods, would provide a push to MSMEs. Reduced import tariffs for sectors such as textiles and leather products would spur growth.

Apart from these, the government also announced schemes such as PLI, International Corporation Scheme, ZED Certification Scheme Entrepreneurship and Skill Development Programme, Export Promotion Council Membership Reimbursement Scheme and Ubharte Sitare Fund to boost the contribution of manufacturing output to exports, which has largely been stagnant at ~10% for the past five years.

- **E-commerce traction**

Post-pandemic, e-commerce has gained a vast footprint in India. This is coupled with rising internet penetration, improved visibility, brand penetration and shifting consumer demand to online shopping. By going digital on these platforms, MSMEs can enhance their income-generating capabilities, earn higher profit margins, reach out to a wider market and receive continuous consumer feedback to help improve their products and services.

Potential benefits to MSMEs from e-commerce



Source: CRISIL SME Solutions

On the other hand, MSMEs face huge challenges with respect to exports:

- **Availability of finance**

Credit availability during the pandemic remained key to keeping small businesses afloat. MSMEs have been less resilient to the pandemic, especially the micro segment which is more financially fragile and has smaller cash buffers. CRISIL Research analysis of ~4,600 MSMEs indicates that average debtor days has gone up to 60 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 need by MSMEs each year remains in working capital.

Access to affordable trade finance is key for MSMEs to remain export competitive. This is needed to cover costly product standards and certification procedures as well as logistics costs involving air/shipping costs.

Various measures such as the CGSSD, 59-minute loan approval schemes, and MUDRA loans have seen a good amount of traction. A special MSME-centric VC fund was also recently launched with a corpus of Rs 10,000 crore by the National Small Industries Corporation (NSIC). The main purpose of this fund is to identify champion sectors and provide growth capital/debt to those with huge potential but are underperforming owing to lack of support. In addition to this, the ECLGS scheme has been addressing MSME funding needs in a timely manner since its launch.

- **Adoption of technology**

Technology is increasingly seen as a business enabler and vital tool for bringing in process efficiencies and a higher degree of standardisation. It plays an important role in scaling up MSME operations and becoming part of global value chains. CRISIL Research's report on MSMEs indicates that technological infrastructure is obsolete for majority of the sectors. Lack of innovation, low-value addition and poor packaging due to low level of technology adoption are some of the key factors impacting MSME exports. MSMEs also face a hurdle in the form of meeting importer's quality standards.

For MSMEs to develop a competitive advantage to operate in the global market, a strong focus on implementing new-age technology, developing indigenous technology as well as technological collaboration with global partners is expected to play a crucial role.

- **Lack of formal registration**

Out of the 6.3 crore MSME units, only ~12% are registered on the Udyam registration portal as of February 2022. Thus, the foremost challenge is to get all MSMEs out of the net registered to be eligible for a service package.

According to RBI's mandate, from August 2020, lenders may demand the Udyam registration for credit purposes. The Udyam portal is also integrated with GeM and TReDS so that enterprises can participate in government procurement and have a mechanism for discounting their bills. Increased credit would provide a huge opportunity to MSMEs and ease operations for export-oriented players.

Apart from this, MSMEs are required to fill-in time-consuming and cumbersome documents to comply with foreign market regulations.

- **Competitive market environment**

Post the pandemic, global markets are recovering from economic disruption in the form of labour shortages, persistent supply chain issues and rising inflationary pressures. Coupled with this, international markets are highly competitive and gauging customer demand becomes difficult. Added to this are other countries exporting similar products at a more competitive price.

CRISIL Research assessment of readymade garment manufacturers suggests that MSMEs are unable to scale-up their presence in the global markets due to higher prices compared with Bangladesh and Vietnam, which are able to sell at lower prices, given the lower cost of production.

Similarly, assessment of tobacco processors indicate that MSMEs have been witnessing stiff global competition from Brazil and China in terms of better quality of flue cured Virginia tobacco, and slowdown in importing nations.

Key monitorables

Getting MSMEs ready to cash in on opportunities

To create a sustainable export ecosystem for MSMEs, the following steps need to be taken:

- Evaluate preparedness of MSMEs to export their products and services
- Recognise areas where improvements are required in order to be able to export effectively and efficiently
- Integrate MSMEs into the global value chain

This would enable MSMEs to scale up and take advantage of the export opportunities.

Unblocking the potential of MSME exports

Though MSMEs account for a sizeable chunk in overall exports, they are often faced with challenges that prevent them from growing faster that restrict their entry in the global market. To develop and strengthen the orientation of MSMEs towards exports, awareness programmes focusing on topics such as global trade scenarios, advantages of exporting products and services, the role of DGFT, customs and excise, and taxation are required. So is a focus on exploring newer markets and developing inter-linkages between MSMEs and large firms.

Export capabilities and competitiveness of MSMEs must be enhanced by assisting exporters in linking them with financial institutions such as NBFCs and new fintech start-ups, and helping them avail of credit at competitive rates.

Finally, it requires leveraging the existing technology network by guiding exporters on selecting advanced manufacturing technologies, and adopting modern methods of international marketing for exploring and capturing new trade markets.

Reducing dependence on imports

India's import dependence is high given that the country imported \$435 billion worth of goods this fiscal so far (April-December 2021), a 67.5% on-year rise from the previous year. Products imported by MSMEs have been largely bags, auto components, iron and steel cast items, furniture, leather goods, plastic items, vehicle accessories, etc.

Through a combination of strategies such as Make in India and Aatmanirbhar Bharat Abhiyan, the government has built a sectoral strategy to reduce India's dependence on imports by building local capacities, creating end-to-end integrated supply chain and disincentivise import of goods.

Apart from the above, the geo-political risk arising from the Ukraine-Russia conflict may dampen the progress of MSMEs in fiscal 2022 and remains a key monitorable

About ASSOCHAM

The Associated Chambers of Commerce & Industry of India (ASSOCHAM) is the country's oldest apex chamber. It brings in actionable insights to strengthen the Indian ecosystem, leveraging its network of more than 4,50,000 members, of which MSMEs represent a large segment. With a strong presence in states, and key cities globally, ASSOCHAM also has more than 400 associations, federations and regional chambers in its fold.

Aligned with the vision of creating a New India, ASSOCHAM works as a conduit between the industry and the Government. The Chamber is an agile and forward looking institution, leading various initiatives to enhance the global competitiveness of the Indian industry, while strengthening the domestic ecosystem.

With more than 100 national and regional sector councils, ASSOCHAM is an impactful representative of the Indian industry. These Councils are led by well-known industry leaders, academicians, economists and independent professionals. The Chamber focuses on aligning critical needs and interests of the industry with the growth aspirations of the nation.

ASSOCHAM is driving four strategic priorities - Sustainability, Empowerment, Entrepreneurship and Digitisation. The Chamber believes that affirmative action in these areas would help drive an inclusive and sustainable socio-economic growth for the country.

ASSOCHAM is working hand in hand with the government, regulators and national and international think tanks to contribute to the policy making process and share vital feedback on implementation of decisions of far-reaching consequences. In line with its focus on being future-ready, the Chamber is building a strong network of knowledge architects. Thus, ASSOCHAM is all set to redefine the dynamics of growth and development in the technology-driven 'Knowledge-Based Economy. The Chamber aims to empower stakeholders in the Indian economy by inculcating knowledge that will be the catalyst of growth in the dynamic global environment.

The Chamber also supports civil society through citizenship programmes, to drive inclusive development. ASSOCHAM's member network leads initiatives in various segments such as empowerment, healthcare, education and skilling, hygiene, affirmative action, road safety, livelihood, life skills, sustainability, to name a few.

About CRISIL Limited

CRISIL is a leading, agile and innovative global analytics company driven by its mission of making markets function better.

It is India's foremost provider of ratings, data, research, analytics and solutions with a strong track record of growth, culture of innovation, and global footprint.

It has delivered independent opinions, actionable insights, and efficient solutions to over 100,000 customers through businesses that operate from India, the US, the UK, Argentina, Poland, China, Hong Kong and Singapore.

It is majority owned by S&P Global Inc, a leading provider of transparent and independent ratings, benchmarks, analytics and data to the capital and commodity markets worldwide.

CRISIL Privacy

CRISIL respects your privacy. We may use your contact information, such as your name, address, and email id to fulfil your request and service your account and to provide you with additional information from CRISIL. For further information on CRISIL's privacy policy please visit www.crisil.com/privacy.

The Associated Chambers of Commerce and Industry of India (ASSOCHAM)

4th Floor, YMCA Cultural Centre and Library Building,

01 Jai Singh Road, New Delhi -110001

www.assocham.org



Argentina | China | Hong Kong | India | Poland | Singapore | UAE | UK | USA

CRISIL Limited: CRISIL House, Central Avenue, Hiranandani Business Park, Powai, Mumbai – 400076. India

Phone: + 91 22 3342 3000 | Fax: + 91 22 3342 3001 | www.crisil.com

in/company/crisil [@CRISILLimited](https://twitter.com/CRISILLimited) [f/CRISILLimited](https://facebook.com/CRISILLimited) [You Tube/user/CRISILLimited](https://youtube.com/user/CRISILLimited) [@lifeatcrisil](https://www.instagram.com/lifeatcrisil) Follow us on @lifeatcrisil

CRISIL

An S&P Global Company