February 09, 2018

MSME'S FINANCING LANDSCAPE SET TO UNDERGO A TRANSFORMATION

SMERA believes that the steps taken by the Government of India in the Union Budget 2018-19 and RBI in its latest regulatory policy review (Feb. 07, 2018) will make the business environment for micro, small and medium enterprises (MSMEs) significantly favourable. While GoI had taken steps in October 2017 to simplify the GST structure for small businesses and revision of tax rates for many products manufactured and distributed by MSMEs, RBI has additionally announced some measures to provide funding support to the sector.

RBI, in recognition of the cash flow mismatches being faced by many MSMEs in the wake of the transition to the GST environment, has provided regulatory dispensation for a delayed recognition of NPAs for enterprises which have aggregate exposures to banks and NBFCs not exceeding Rs. 25 Cr. Banks and NBFCs have been permitted a NPA classification period of 180 days instead of the standard 90 days if they have over dues between September- January 2018 and if the account was standard as on August 31, 2017. This is expected to support those MSMEs who have witnessed higher working capital requirements during the transition to GST in the current year. The lenders would be able to provide additional funding for such cash strapped enterprises to sustain their businesses which otherwise would not be the case if they were treated as a NPA or SMA account as per the standard definition.

Additionally, the priority sector exposure limits for MSMEs in the services sector have been removed by RBI which were earlier restricted to Rs. 5 Cr for a micro and small enterprise and Rs 10 Cr. for a medium enterprise. This will facilitate higher funding particularly from banks for growing and efficient service enterprises at competitive rates. RBI has also made the priority sector sub-targets for farmers and micro enterprises applicable for all foreign banks with 20 branches and above with effect from 2018-19. Such banks will need to provide 7.5% of their adjusted net bank credit (ANBC) for lending to micro enterprises which they are expected to achieve largely through securitisation transactions and purchase of MSME portfolios from NBFCs. The priority sector advances of banks towards micro and small enterprises (which stood at Rs. 8.95 lakh Cr as on Dec 31, 2017) has been witnessing muted growth with only 6.4% increase in FY 2017 and almost stagnant levels in FY2018. These steps along with the recapitalization of public sector banks, are expected to provide a strong thrust to bank lending to MSMEs.

Says Suman Chowdhury, President, Ratings, Acuité ***"Clearly, all these measures from RBI will ensure improved funding flow in the MSME ecosystem from both banks and NBFCs at competitive rates and will help well run enterprises in the sector to scale up their businesses, improve their margins and be globally competitive. We are expecting a significant pick-up in bank loans to the MSME segment with advance growth as high as 15% annualized over the next two years closely following the trend that has already been observed in the NBFC lending portfolio. One significant addition to the MSME funding ecosystem are the Small Finance Banks (SFBs) most of whom have converted***

from being microfinance lenders (MFI) but are set to play a very significant role in financing MSMEs in relatively remote areas going forward."

RBI steps closely follow the measures taken by the Government in the Union Budget 2018-19 to put MSMEs on fast track and enhance employment opportunities. The budget has trimmed the corporate tax rate for companies with turnover of less than Rs. 250 Cr to 25%; this will lower the tax burden for almost the entire MSME sector and encourage balance sheet scalability thereby making them more competitive. It has also allocated Rs. 3 lakh crore under MUDRA scheme to facilitate funding for the start-up companies. This will encourage entrepreneurship and a higher number of registrations with Udyog Aadhaar portal is expected. Higher customs duty announced in the budget for products in auto components, food processing, textile, electronic and footwear sectors will also support the "Make in India" agenda, facilitate scalability and higher investments in domestic manufacturing capacity by MSMEs.

Says Sankar Chakraborti, CEO, Acuité ***"The measures announced in the Union Budget and recently by RBI are indeed transformational for the MSME sector. They will not only help the sector to tide over the GST transition process but also to access funding on a much larger scale from the organized financial sector and capitalize on the visible growth opportunity. Our study on a sample of rated MSMEs already indicate a positive business sentiment with 11% and 13% average projected revenue and profitability growth over the period FY 2017-19. Acuité will continue to be part of the transformation process by supporting banks and NBFCs in their credit evaluation mechanisms through its significant expertise and decade long experience in MSME ratings."***

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SMERA was incorporated in 2005 as an initiative of Ministry of Finance, Govt. of India and the Reserve Bank of India to help Indian MSMEs grow and get access to credit through independent and unbiased credit opinion that banks can rely on. Thus SMERA became the world's first MSME focused rating agency and introduced the concept of SME Ratings in India. SMERA is now a division of Acuité Ratings & Research Limited (a SEBI Registered and RBI Accredited Credit Rating Agency).