

Foreword

Indian economy which was gradually showing signs of uptick post the first wave of pandemic that hit last fiscal, got again impacted by the second wave recently. The economic impact of second wave of pandemic will be determined by covid caseload, nature of lockdowns, structural composition of output and pace of vaccination. Smaller firms and services continue to face pressure amid the second wave. Private consumption remained weak. The economy is down but not out as it walks on the recovery path. Second half of fiscal to be led by better-spread economic growth, owing to increased inoculations and better adaptability to the pandemic, which would support sectors that are lagging. Globally, pace of vaccination has acted as one of the key driving factor for recovery with US and UK recording GDP growth owing to faster vaccination while Japan witnessed decline in GDP owing to resurgence of cases and slow pace of vaccination.



Among key sectors which have a high MSME presence, auto OEMs took an early hit amid second wave and lockdown restriction in various states owing to supply chain related production challenges, thereby giving a blow to auto component MSMEs. Textiles readymade garment (RMG) sector witnessed traction on account of low base and ban of import from China which is positive for Indian MSME RMG players too.

In this edition of YES- MSME Dialogue, the focus is on the 'Pharmaceutical' sector and the MSME outlook of the same in the present scenario. Continued domestic and export demand for vaccines and related drugs are expected to boost the sales for the MSME sector. MSMEs, which have a moderate to high presence across the pharma value chain are likely to benefit from the PLI scheme for API aimed at increasing domestic manufacturing of key molecules to reduce dependency on China. Further, in view of our country's capacity to manufacture and supply over 3 billion vaccines annually at low cost and the rising export demand for the same, MSMEs are also expected to benefit from contract manufacturing opportunities that will arise.

Macro Monitor

INDUSTRIAL OUTPUT (y-o-y %)				Inflation (y-o-y %)				GDP (y-o-y %)				
Industrial (IIP)	Jan-21	Feb-21	Mar-21	CPI	Feb-21	Mar-21	Apr-21	Private consumption	Q2FY21	Q3FY21	Q4FY21	
	-0.9	-3.4	22.4		5.0	5.5	4.3		-11.3	-2.8	2.7	
CRUDE OIL (y-o-y %)				WPI				Government consumption				
	Brent Crude	Feb-21	Mar-21		Apr-21	4.2	7.4		10.5	-24	-1.0	28.3
									Fixed investment			
										-6.8	2.6	10.9
Exchange Rate				TRADE (y-o-y growth %)				GDP				
Rs/\$	Feb-21	Mar-21	Apr-21	Exports	Feb-21	Mar-21	Apr-21	Imports	Trade balance	-7.3	0.5	1.6
	72.8	72.8	74.5		-0.8	60.3	201.5			7.0	53.7	167.6

India's growth next fiscal to be a story of two halves

Macroeconomic outlook	FY18	FY19	FY20	FY21	FY22E	Rationale for FY22 outlook
GDP growth (%)	6.8	6.5	4.0	-7.3	9.5	The second wave and the resultant localised lockdowns has impeded the path to economic recovery, leading us to revise down our growth forecast for this fiscal to 9.5%, from 11.0% earlier. That said, expected pick-up in economic activity post-vaccination and support from global growth would act as positives.
Inflation CPI (%)	3.6	3.4	4.8	6.2	5.3	Upside risks on inflation are growing from surging international commodity prices. While producers are bearing a greater burden of rising input costs for now, these could get passed to retail prices once demand recovers. Food inflation could also face pressure from disruptions to rural economy due to the pandemic's spread, and rising global prices.
Exchange rate (Rs/\$, March)	65	70	74	74	75	Soaring Covid-19 cases posing a strong downside risk to India's growth forecast may weaken the rupee more against the dollar. Impact of a second wave amid inflationary pressures and stress on government finances are expected to weigh on sentiment.

Global Snapshot

US

Robust Q1 GDP growth in the US, but inflation concerns remain

- \$1.9 trillion fiscal stimulus finally passed in the US to positively impact demand.
- US CPI rose 1.6 percentage points to 4.2% on-year in April 2021. Sharp rise in inflation intensified concerns over the tapering of the quantitative easing policy implemented by the Fed, going ahead, implying demand-push inflationary pressures.
- US jobs data showed encouraging signs, with non-farm payrolls rising 260,000 in April, though down from massive gain in March.

UK

Faster vaccination and fewer Covid-19 cases propel economic activity in the UK

- GDP is estimated to have grown 2.1% in March 2021 as country eased restrictions, the fastest monthly pace since August 2020.
- Annual CPI inflation rose 0.7% in March, up from 0.4% in February due to rising prices of fuel and clothing.
- The services sector grew 1.9% in March, as schools re-opened and retail trade sales continued to show strength.

China

China's Q1 GDP numbers at record highs

- Q1 GDP grew by a record 18.3% on-year, driven by external and domestic demand recoveries and low base of last year.
- Manufacturing PMI came in at 51.1, 0.8pp lower on-month, since supply bottlenecks stifled production.
- Consumer prices continued to decline on-year, with deflation at -0.3%, slightly higher than -0.5% in the previous month. On a monthly basis too, inflation inched up, after three months of consecutive slowdown.

Japan

Private consumption remains a weak spot for Japan

- Private consumption remained weak, and export pace slowed in April. Consumption trends based on card spending showed goods spending remained stable, but services spending was weak.
- Trade surplus widened on-year, to ¥662.1 billion in March 2021 from ¥7.5 billion a year ago. Exports growth was faster than imports (at 16.1%, versus 5.8%).
- Deflation eased slightly, with CPI inflation declining 0.2% on-year (versus the 0.4% decline in February).

MSME News & developments



Auto components; Post marginal recovery, exports estimated to be under pressure again with second wave of COVID-19. MSME to feel the blow too

On - year Growth	%share to Auto component OEM segment	Mar-20	Apr-20	May-20	Jun-20	July-20	Aug-20	Sep-20	Oct-20	Nov-20	Dec-20	Jan-21	Feb-21	Mar-21	Apr-21
	51%	-38%	-100%	-90%	-58%	-24%	-2%	20%	35%	8%	28%	-2%*	13%	79%	-11%*
	26%	-28%	-99%	-86%	-50%	-28%	0%	15%	40%	4%	9%	13%	17%	68%	-23%*
	16%	-83%		-88%			-17%			12%			51%		
	5%	-18%	-100%	-53%	51%	14%	24%	29%	59%	46%	86%	42%	40%	85%	-15%*

Source: Industry, CRISIL Research | Note: *: m-o-m change in production data; Passenger Vehicle data for January-April 2021 does not include Tata Motors



Textiles RMG; Low base and ban of imports from China to fracture supply chain; textile MSMEs too expected to see some gain

On - year Growth (in value terms)	Mar-20	Apr-20	May-20	Jun-20	July-20	Aug-20	Sep-20	Oct-20	Nov-20	Dec-20	Jan-21	Feb-21	Mar-21E	Apr-21E
RMG (in %)	-30.2%	-90.1%	-63.4%	-28.9%	-15.0%	-9.8%	13.7%	10%	2.7%	-12.2%	-8.6%	-7.1%	26.4%	920.5%

Source: Department of commerce, Ministry of commerce & industry, CRISIL Research | Note: *: RMG stands for Readymade garments



Engineering & capital goods; export demand estimated to increase in Q1 FY22 over a lower base which is positive for MSMEs

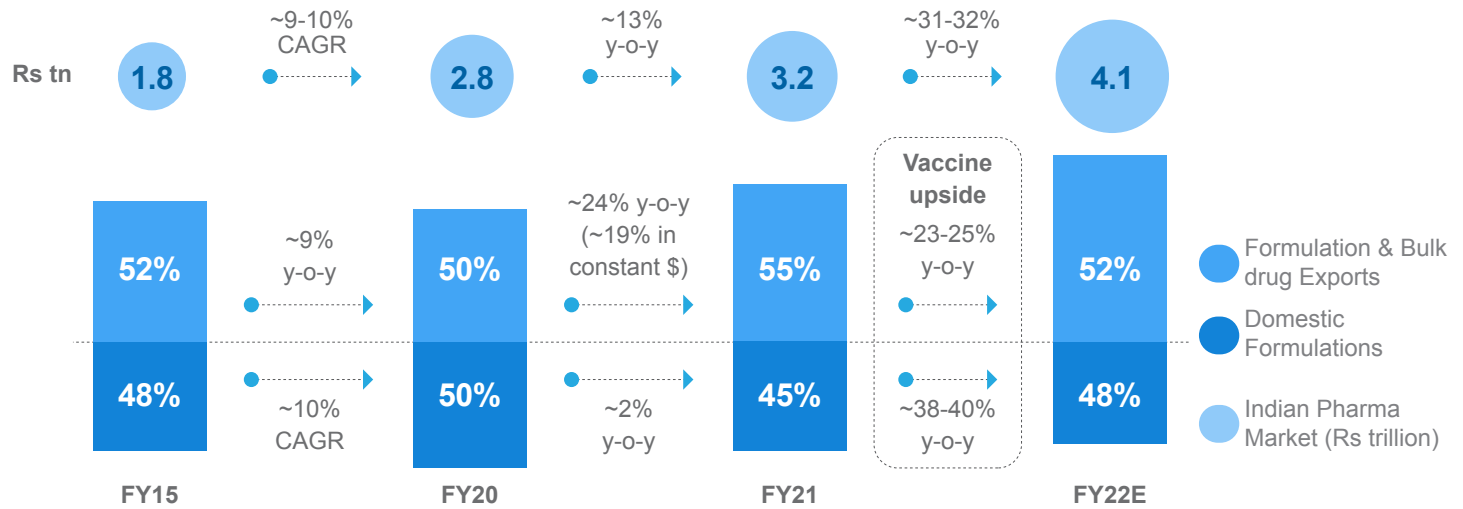
On - year Growth (in value terms)	Mar-20	Apr-20	May-20	Jun-20	July-20	Aug-20	Sep-20	Oct-20	Nov-20	Dec-20	Jan-21E	Feb-21	Mar-21E	Apr-21E
Engineering and Capital Goods export (in %)	-27.4%	-75.8%	-32.2%	-4.3%	14.2%	-2.8%	8.5%	0.1%	-13.8%	-1.2%	14.5%	-1.3%	70.3%	234.6%

Source: Department of commerce, CRISIL Research

Focused sector of this edition: PHARMACEUTICALS

Fundamental factors to drive pharmaceutical industry; MSME stand to benefit

Pharma resilient in FY21; strong upside in FY22 aided by vaccine and related drugs



Note: CAGR - Compound annual growth rate; y-o-y - year-on-year (INR terms)
 Source: Directorate General of Commercial intelligence & Statistics (DGCIS), CRISIL Research

Exports bulk drugs and formulations

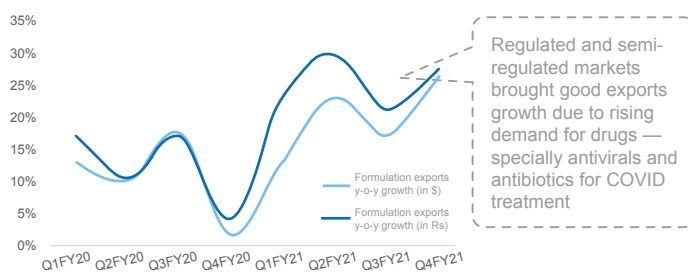
FY21: Continued demand of drug viz. antibiotics in wake of COVID, new product launches; drug shortages in the US augured well
FY22: COVID vaccine sales, continued product diversification and ramp-up in complex, specialty products

Domestic formulations

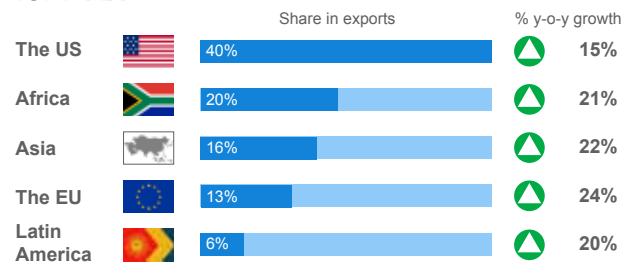
FY21: Closure of smaller clinics and hospital OPD, postponement of drugs led to slower drug sales
FY22: Growth led by COVID vaccines as drive gathers pace

Robust demand from most economies boost formulation exports

Formulation exports witnessing robust growth



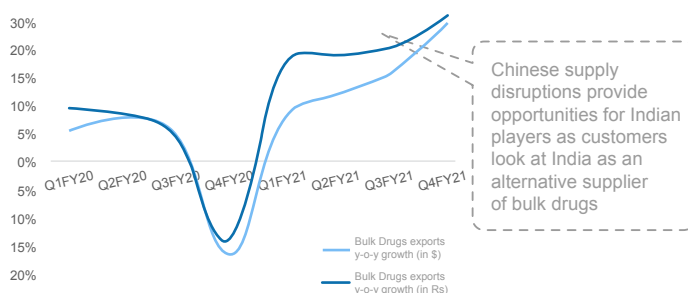
Formulation exports rise across top regions for FY21



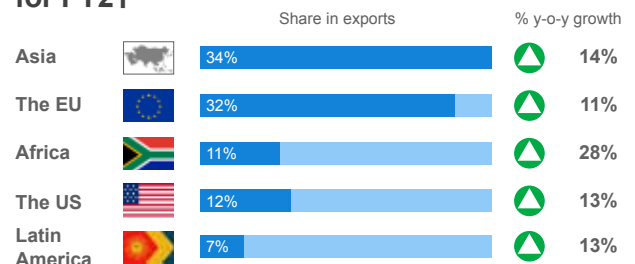
Source: DGCIS | Note: Above growth is in constant currency

Global de-risking of supply chain bodes well for Indian bulk drug exports

Strong demand boost Bulk drug exports as well

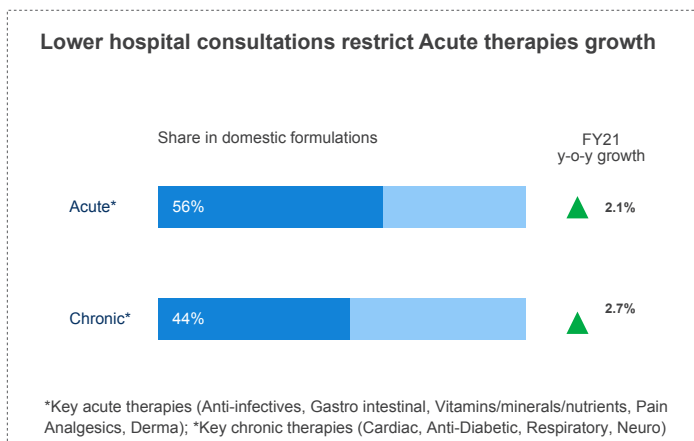
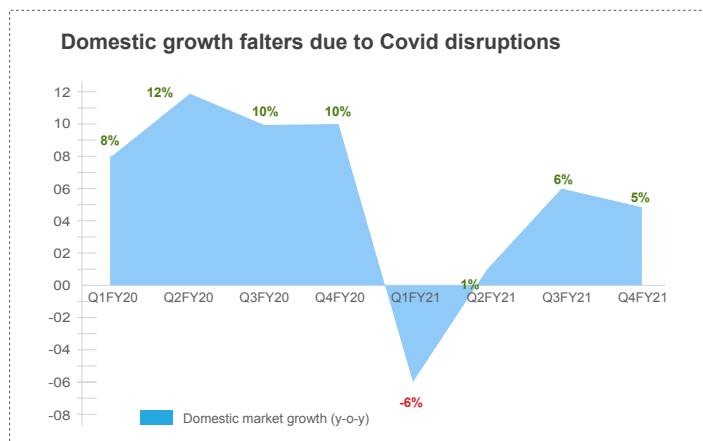


Bulk drug exports rise across top regions for FY21

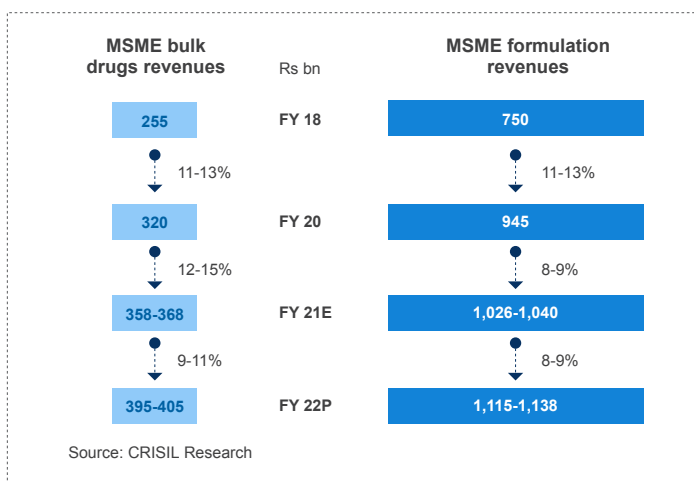
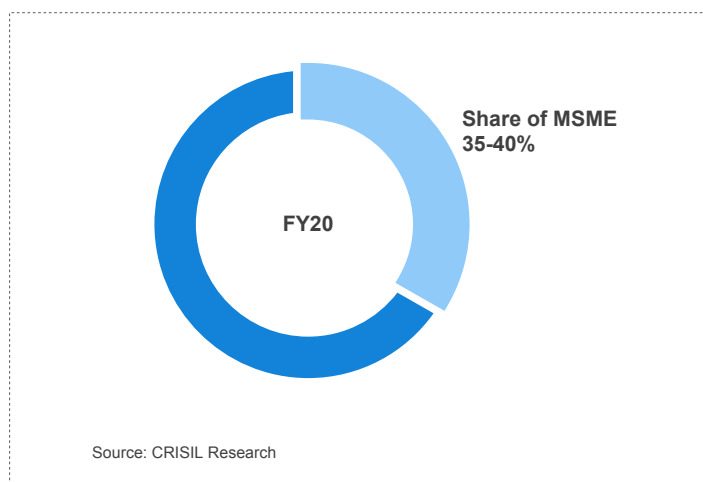


Source: DGCIS | Note: Above growth is in constant currency

Domestic formulation market sees normalization from Q3FY21 onwards



MSME account for 75-80% in volumes and 35-40% by value in both bulk drugs and formulations



Bulk drugs MSME revenue outlook

FY21: To see rise in both exports and domestic sales. Customer de-risking from China to prove beneficial

FY22: Continued demand for drug to boost domestic sales. Export demand to increase as demand for Indian API rises

Formulations MSME revenue outlook

FY21: To witness growth slowdown in domestic revenues. Export growth to be robust

FY22: Domestic and export demand to grow at healthy pace on new opportunities (contract manufacturing of drugs in COVID treatment) and continued demand

Margin outlook for MSME bulk drugs

FY21: To decrease by 50-100 bps owing to increase in raw material

FY22: Capacity utilisation to be back to normal levels and stabilisation of raw material prices to elevate margins by 100 bps

Margin outlook for MSME formulations

FY21: To reduce by 50-100 bps owing to an increase in raw material prices for some products, thanks to supply disruptions from China

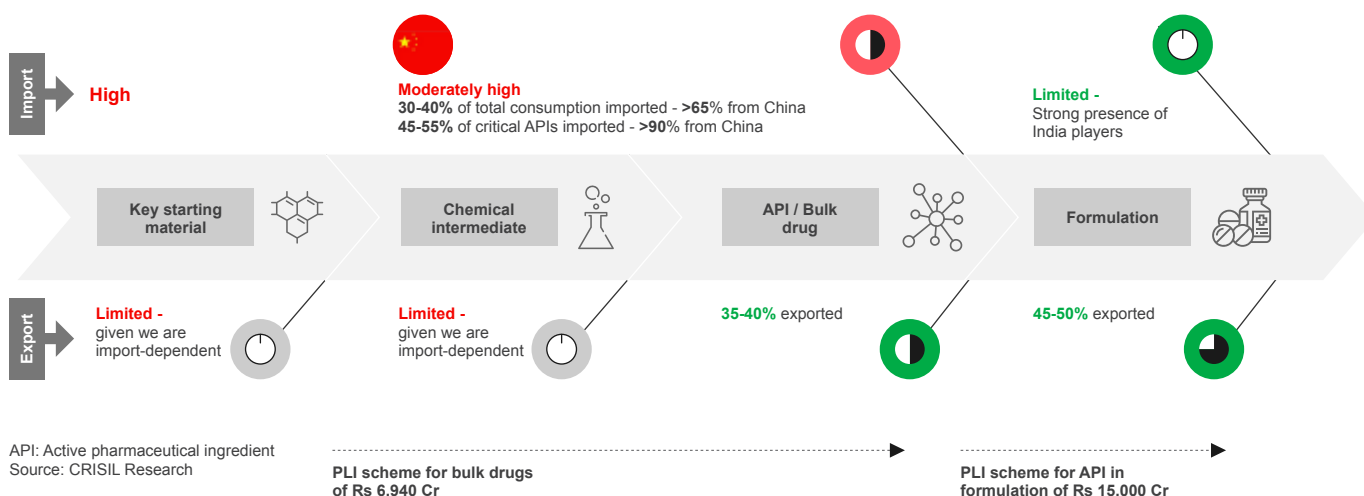
FY22: To rise by 50-100 bps following stabilisation in raw material prices

Opportunities galore for MSME pharmaceutical entities

1. Indirect and direct benefit via PLI scheme in bulk drugs and formulations

PLI scheme for API aim at increasing domestic manufacturing of key molecules and reduce dependency on China. PLI scheme for formulations will boost pharma manufacturing and provide value addition in exports. Total incremental sales of Rs 2,94,000 crore and total incremental exports of Rs.1,96,000 crore are estimated during 2022-23 to 2027-28. PLI scheme for formulations will help in creating employment and is expected to contribute to availability of wider range of affordable medicines for consumers. PLI to benefit even MSMEs as MSME have moderate-to-high presence across pharma value chain.

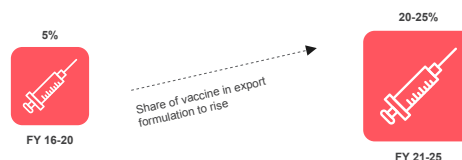
Pharma: Dependence on imports high for key raw materials; PLI to encourage domestic manufacturing



2. COVID-19 vaccine – Scope to enhance pie in export formulation

India has capability to manufacture and supply vaccines to most nations at a relatively lower costs. Over 3 billion doses are likely to be produced annually in India. This can lead to contract manufacturing prospects for MSME.

Contract manufacturing opportunities for MSME emerge with rise in share of vaccine in export formulation



3. Pent up demand to drive domestic formulation growth

Recovery in footfalls, hospitals growth to increase demand in FY22. Further, Covid-19 vaccine sales are largely likely to drive domestic market growth to 28-29% in FY22.

Key risks / monitorable

MEIS withdrawal and its impact

- Government announced capping of incentive under scheme to Rs 2 crore per exporter from Sep 1, 2020 to Dec 31, 2020 due to fund shortfall. With incentives under Merchandise Export from India Scheme (MEIS) accounting ~2% of revenue for pharma players in FY20, large exporters will lose much of these incentives for FY21. Export focused MSME may lose more.
- Remission of Duties and Taxes on Exported Products (RoDTEP) is likely to replace MEIS; guidelines awaited.

Shocks from second pandemic wave and vaccination drive full implementation

- Second pandemic wave is not likely to be severe. With vaccination gathering pace, situation is expected to normalize. However, it is monitorable.
- Vaccine drive commenced Jan 16, 2021 phase-wise. As on May 21, 2021, over 19 Cr doses have been administered in India so far. Vaccine drive full implementation to be a monitorable.

YES BANK MSME solution

Solution provided to a pharmaceutical company for sales order received from Arshiya FTWZ Gujarat

Challenges faced by customer:

Customer had received a sales order for supply to a company located in Arshiya FTWZ, Gujarat. Buyer wanted the invoice to be raised in FCY. Client was looking for resolution as was not sure of Foreign Currency Invoice could be raised for supply within the country.



Solution offered by YES BANK:

In this case, customer's sale was from a domestic tariff area (DTA) to an FTWZ (similar as SEZ). This transaction is considered an export and customer is eligible to take export financing against the same. We have advised the client about the invoicing sales in FCY. The client was advised further that he can avail Post Shipment Bill Discounting in FCY (Export Finance) at a lower cost than INR funding.



How it has helped the customer:

Customers could raise invoices in FCY and also have the bills discounted at lower ROI as compared to INR.

Export benefit could be taken for the sale

Customer could get repetitive order from the same customer and increase his export sales.



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