Foreword

The outlook for the global economy has turned a shade brighter because of faster vaccinations and ongoing stimuli in the advanced economies. Taking cue, S&P Global recently notched up its global gross domestic product (GDP) growth outlook for calendar year 2021 to 5.9% from 5.5% projected in March. It also raised its growth outlook for the United States (US) and the Eurozone by 20 basis points each.

But the flip side is, faster growth has been accompanied by rising inflation. To boot, recovery has been uneven across countries and sectors, which spawns its own set of risks.

For India, global growth is a double-edged sword. The sharper rebound in global growth has boosted India's exports, which has now surged past pre-pandemic levels – handily outpacing the GDP claw-back. And the recent uptick in the growth outlook of India's major trading partners augurs well for exports.

However, inflation continues to be of concern - the June print of retail inflation at 6.3% was lower than market expectations, but continues to be above the RBI's tolerance band of 2-6%. Inflation pressures are becoming broad-based with a number of producers beginning to pass on the rising input costs to end-consumers. The RBI considers high inflation as transitory (cost-push rather than demand pull) and growth a bigger risk in the near term.

The Pace of recovery hinges on the rate of vaccination. In this edition of YES- MSME Dialogue, the focus is on the 'Textiles' sector and the MSME outlook for the same in the present scenario. MSMEs in the textile sector is expected to recuperate this fiscal from the demand slowdown induced by COVID-19 lockdowns not just in the domestic market but also in the exports markets. Over the medium term, they would be supported by government initiatives such as the PLI scheme for technical textiles aimed at improving domestic production and the MITRA scheme that would provide direct and indirect opportunities to MSMEs in the sector.

Macro Monitor

INDUSTRIAL OUTPUT (y-o-y %)

	Mar-21	Apr-21	May-21
Industrial (IIP)	22.4	134.6	29.3

CRUDE OIL (y-o-y %)

	Apr-21	May-21	Jun-21
Brent Crude	171.3	113	77.4

Exchange Rate

	Apr-21	May-21	Jun-21
Rs/$	74.5	73.3	73.6

Inflation (y-o-y %)

	Apr-21	May-21	Jun-21
CPI	4.2	6.3	6.3
WPI	10.5	12.9	12.1

TRADE (y-o-y growth %)

	Apr-21	May-21	Jun-21
Exports	201.5	67.4	47.7
Imports	167.6	68.5	96.7
Trade balance	118.1	74.7	-1442.8

GDP (y-o-y %)

	Q2FY21	Q3FY21	Q4FY21
Private consumption	-11.3	-2.8	2.7
Government consumption	-24	-1.0	28.3
Fixed investment	-6.8	2.6	10.9
GDP	-7.3	0.5	1.6

India's growth sliced by second wave of infections

Macroeconomic outlook	FY18	FY19	FY20	FY21	FY22F	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.

YES MSME Dialogue

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Global Snapshot

US

US inflation spikes again, unemployment rate declines

- CPI increased sharply to 5.4% on-year in June, up from 5% in the previous month. It has trended upwards since January, when inflation was at 1.4%. However, the on-year inflation reading is largely attributed to the low base of the previous year (when prices rose 0.1%).
- Total non-farm payroll employment increased by 8.5 lakh in June, significantly up from 5.9 lakh in May.
- The unemployment rate was stable in June at 5.9%. Declined by 0.3% to 5.8%. Leisure and hospitality, education, and healthcare accounted for the largest gains.

UK

Eased restrictions support monthly uptrend in UK

- UK's GDP grew 0.8% in May, compared to 2.3% in April. Indicating growth momentum slowing down because of the pent-up demand now plateauing after surging in the previous months.
- With greater than 50% of the population vaccinated the overall growth prospects for the UK being strong.
- CPH linked inflation rose 2.1% in May on-year, up from 1.7% growth in April, but sequentially, inflation slowed to 0.5%, following a 0.7% increase the previous month.

China

China's manufacturing activity stumbles

- In June manufacturing PMI came in at 50.9, 0.1pp lower on-month, weighed down by higher raw material costs and global semiconductors shortage.
- The rate of increase in consumer prices slowed for the first time in three months, with CPI linked inflation at 1.1% in June, down from 1.3% the previous month.
- Exports increased by a robust 32.2% on-year. This is largely attributed to the base effect from 2020 and exporters from China benefitting from the relatively early reopening of the economy while international competitors faced pandemic related restrictions.

Japan

Renewed surge of infections in early 2021 weaken economic recovery

- Japan's trade surplus continued to narrow on-year to ¥189.4 billion in May, from ¥856.7 billion a year ago. Exports and imports grew 49.6% and 27.9%, respectively, owing to a low base last year.
- Japan seems to be yo-yo-ing in the deflation zone, as CPI in 2021 showed an up-and-down trend. CPI linked inflation declined by 0.1% on-year in May. (vs -0.4% in the previous month)
- Resurgence in cases and low vaccine coverage in Japan impede economic recovery.

MSME News & Developments

Non-Food Bank credit growing at a steady pace

Y-o-y growth	Jun-20	July-20	Aug-20	Sep-20	Oct-20	Nov-20	Dec-20	Jan-21	Feb-21	Mar-21	Apr-21	May-21	Jun-21
Non-Food Bank Credit	6.0%	6.7%	6.0%	5.8%	5.6%	6.0%	5.9%	5.7%	6.5%	5.5%	5.7%	5.9%	5.9%

Consumer durables IIP takes a hit due to second wave, non-durables IIP robust

IIP	Jun-20	July-20	Aug-20	Sep-20	Oct-20	Nov-20	Dec-20	Jan-21	Feb-21	Mar-21	Apr-21	May-21
Consumer durables	78.2	99.4	109.5	129.0	133.8	113.0	124.9	123.9	125.0	129.0	108.9	78.7
Consumer non-durables	147.5	149.3	140.0	147.4	148.7	149.1	161.1	149.8	147.6	159.7	141.7	136.4

Source: MOSPI, RBI , CRISIL Research

Pharmaceuticals exports took a hit due to the second wave

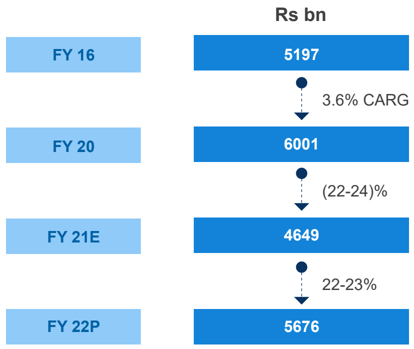
Y-o-y growth	May-20	Jun-20	July-20	Aug-20	Sep-20	Oct-20	Nov-20	Dec-20	Jan-21	Feb-21	Mar-21	Apr-21	May-21
Bulk Drugs	5%	15%	11%	12%	11%	16%	12%	17%	16%	5%	54%	18%	-7%
Formulation	23%	9%	22%	19%	28%	23%	10%	17%	16%	17%	47%	20%	-8%

Source: CRISIL Research

Textile industry growth to bounce back in FY22

Fiscal 2021 was a tough year for the textile industry as de-growth was witnessed across segments. Covid induced lockdowns had a significant impact on the industry as restricted trade activities and overall economic slump led to decrease in demand. Growth for the industry is expected to bounce back in fiscal 2022 over lower base of last year. Although, second wave of Covid has impacted the industry in early part of this year, demand is expected to be back because of improved consumer confidence and revival of global economy.

After getting hit by the pandemic, textile industry to witness sharp v-shaped recovery



Note: Figures in Rs bn | Source: Industry, CRISIL Research

Demand for readymade garments is expected to revive in Q2 ahead of the festive season in Q3 this fiscal. Also, domestic and exports demand for manmade fibres and cotton yarn is expected to be back amid recovery in global economy.

Revival in growth is expected across segments

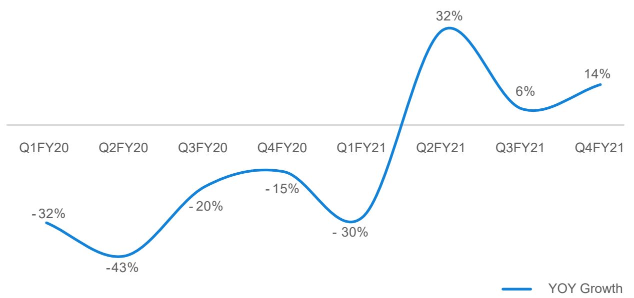
Textile sub-segments	FY20 markets size Rs bn	FY16-20 CAGR	FY21E	FY22 P
Readymade Garments	4659	4%	-23 to -25%	15-20%
Cotton yarn	785	2%	-12 to -14%	22-27%
Manmade fibers	557	5%	-26 to -28%	35-40%

Source: Industry, CRISIL Research

Cotton Yarn exports from India

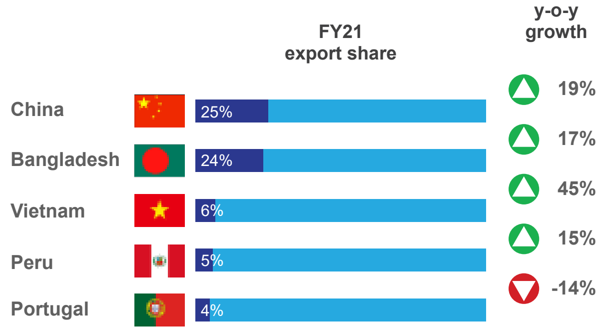
Pent up demand plus growth revival in key exports markets such as China, Bangladesh and Vietnam witnessed in fiscal 2021 on the low base of fiscal 2020. In fiscal 2020, India faced stiff competition from other exporting nations (such as Indonesia, Vietnam & Bangladesh) due to their cost competitiveness and FTAs with importing nations.

Cotton yarn exports revived from Q2FY21 onwards after 5 quarters of consecutive decline



Source: DGCIS, Industry, CRISIL Research

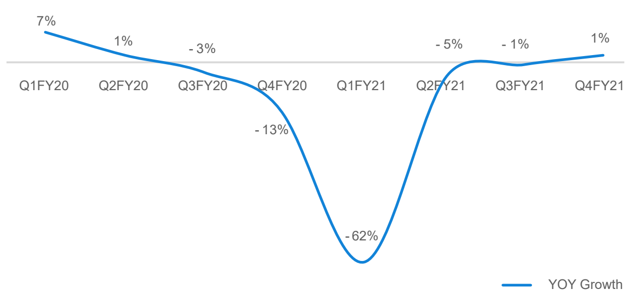
Exports to key countries also grew on low base of last fiscal



Ready Made Garments (RMG) exports from India

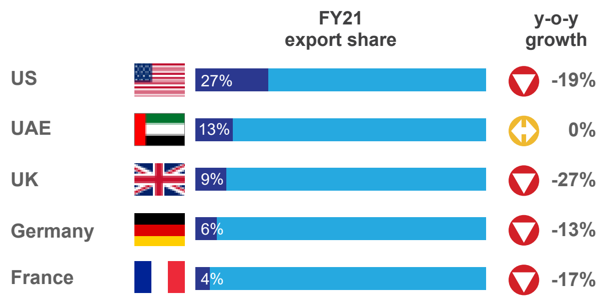
RMG exports from India saw sharp declines during peak COVID-19 induced lockdowns as major economies were faced with weak consumer sentiment.

Steep decline in exports witnessed during peak of the pandemic, slow revival



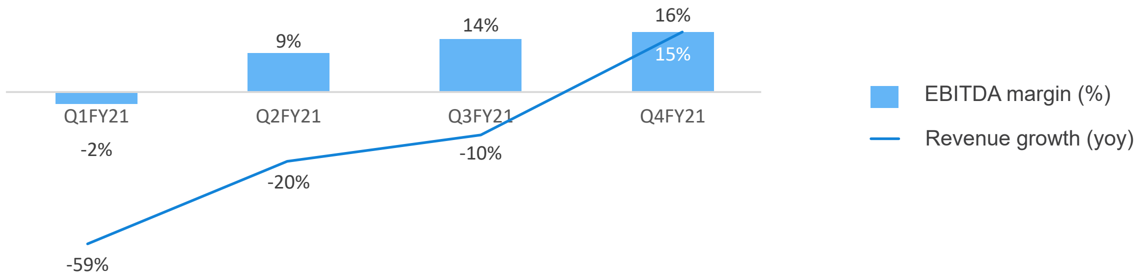
Source: DGCIS, Industry, CRISIL Research

Exports were in the red across key importing countries in FY21



Revenue growth of key players also indicate revival in Q4 fiscal 2021

Key players across RMG and Cotton Yarn segments witnessed steep revenue and EBITDA margin decline in Q1 in line with lockdown induced weak demand. However, sequential recovery has been seen, with Q4 witnessing increase in both revenue growth and EBITDA margins.



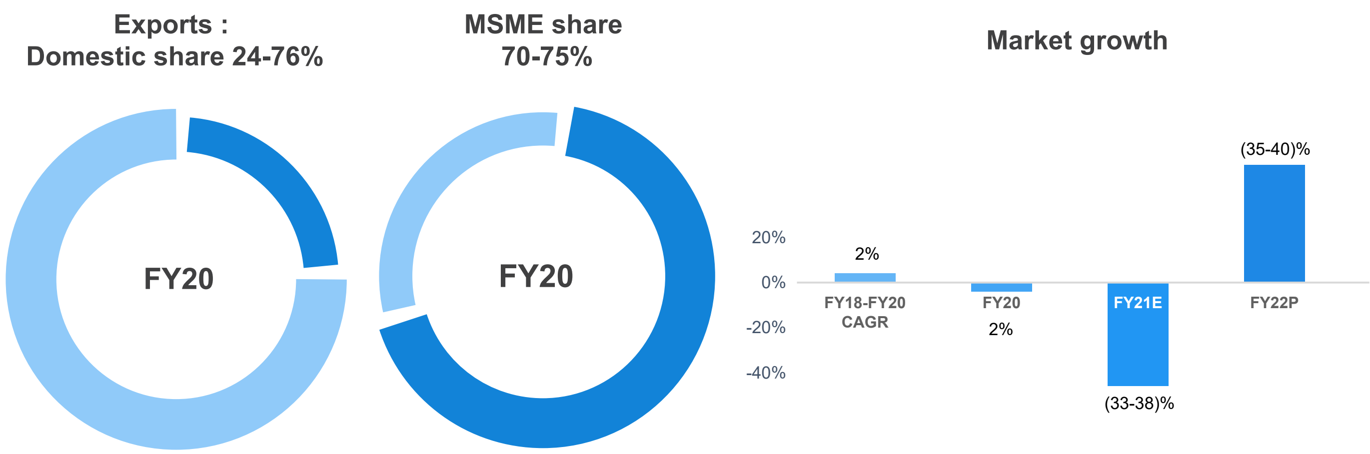
Note: Data for 20 companies accounting for ~30% of the market

Source: Company, CRISIL Research

MSMEs in the textile industry too, would recuperate

MSMEs have strong presence in the textiles industry with high focus towards readymade garments, cotton spinning, and home furnishing segments.

Readymade garment
(FY20 market size: Rs 4845-4855 bn)



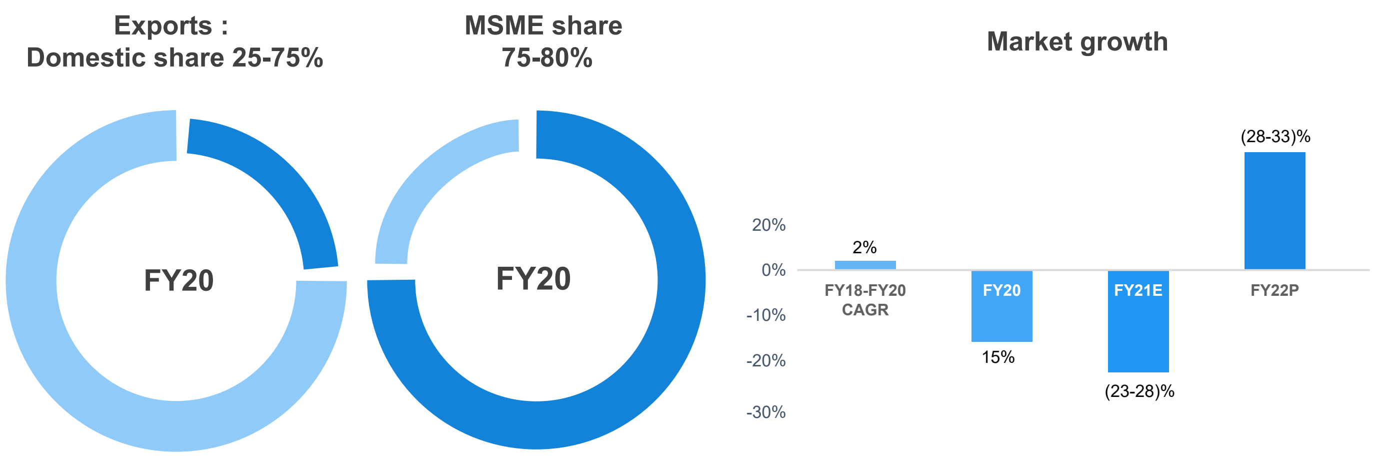
Source: Industry, CRISIL Research

Revenue and margin outlook for MSMEs in RMG:

FY21: Industry growth declined due to Covid-19 induced economic slowdown. Margins declined along with decrease in topline due to higher fixed cost obligation

FY22: Market size is expected to increase over low base of FY21. Margins expected to improve with increase in revenue and decline in fixed cost obligation

Cotton spinning
(FY20 market size: Rs 710-715 bn)

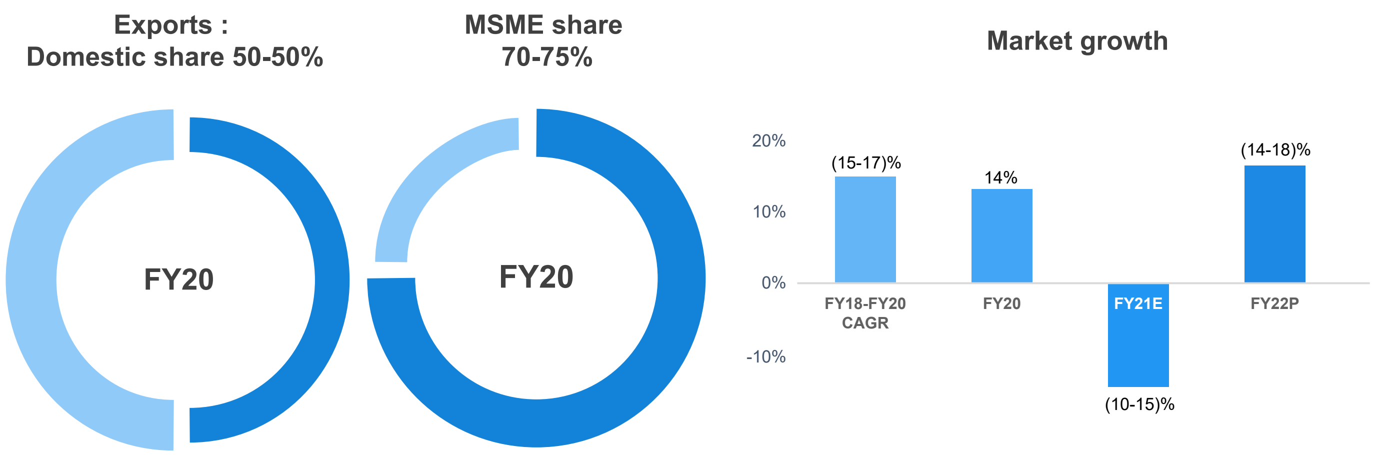


Source: Industry, CRISIL Research

Revenue and margins outlook for MSMEs in Cotton Spinning:

FY21: Global and domestic economic slowdown affected demand, higher yarn prices further affected exports. Fall in spreads between cotton yarn and cotton prices hit margins of players along with decline in topline
FY22: Demand expected to pick up on low base of FY21. Margins expected to improve along with increase in cotton yarn prices

Home furnishing
(FY20 market size: Rs 753-758 bn)



Source: Industry, CRISIL Research

Revenue and margin outlook for MSMEs in Home furnishings:

FY21: Witnessed sharp decline in revenue owing to lockdowns in domestic markets, poor economic environment. Margins plummeted due to decline in duty drawback
FY22: Healthy growth on low base expected. Margins to improve

Opportunities for MSMEs in the Textile industry

1. PLI scheme for textile: an opportunity of Rs 150,000 crore revenue generation in Man Made Fibres-based textiles:

The textile sector will receive Rs ~10,683 crores under the Production Linked Incentive scheme which translates into a revenue potential of 1.5 lakh crore at an average 9% incentive. The scheme would provide incentives to both brownfield and greenfield capacity expansion in the sector. The brownfield capacity expansion includes two categories, player earning turnover of 100-400 crore where incentive is fixed at 9% and players earning more than 400 crore for which incentive stands at 7% for the first year. For greenfield capacity expansion projects, players need to commit minimum Rs 500 crore investment and will be incentivized at higher rate at 11% in first year. The incentive rates will decline by 1% over the next 5 years.

2. Removal of GSP status of Pakistan by EU:

The recent removal of Pakistan from the European Union's Generalised Scheme of Preferences (GSP), will benefit Indian players (including MSMEs) in the home textiles exports segment that suffered competition from Pakistan due to duty benefits they received under the scheme. Pakistan held 45% of EU's home textile imports as they enjoyed 0% duty in this segment. Now Indian players, who have a lion's share in the US market, would have a level playing field in the EU as well, where Indian home textile products currently attract 9.5% duty in EU.

3. Mega Investment Textile Parks (MITRA) scheme:

The government has proposed a scheme of Mega Investment Textile Parks (MITRA) to enable the textile industry to become globally competitive, attract large investments, boost employment generation and exports. 7 mega textile parks will be launched in three years as part of the scheme. These will have integrated facilities and quick turnaround time for minimizing transportation losses, along with uninterrupted water and power supply, common utilities and research and development labs.

Key risks / monitorables

1. Lack of FTAs with major importers:

India lacks FTAs with major importers like US, EU, Canada and China while other exporting countries like Bangladesh, Vietnam and Pakistan stay competitive in the world garment trade due to FTAs despite lacking raw material.

2. Increase in raw material prices:

High fragmentation in the industry makes it difficult to pass on volatile raw material prices to the customers.

YES BANK MSME solution

Solution provided to a leading auto-ancillary component exporter for capacity expansion

Problems faced by customer :

A client from North India who had SBLC and Importing financing limits with us wanted to procure import financing- loan against import (LAI) for a document which was launched in a competitor bank.

Solution offered :

We obtained NOC from the competitor bank, and after required due diligence we have funded Nostro account of the competitor bank and bill payment has been done. After the transaction we have taken SWIFT of the transaction from our customer to ensure end use of import financing.

How it has helped the Customer :

With this we have been able to provide the customer with access to funds as per their requirement.

Email : yestrademsme@yesbank.in