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Bharatiya Vidya Bhavan

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REPORT ON

THE FINANCIAL IMPACT OF COVID ON INDIAN MICRO, SMALL AND MEDIUM ENTERPRISES AND THEIR OUTLOOK AMIDST THE PANDEMIC

A MAGMA-SPJIMR REPORT

JUNE 2020

The Centre for Family Managed Business
SPJIMR
&
MAGMA FINCORP LTD.

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The authors acknowledge the support of Mr. Deepak Cherukuri - SME Business Head and Mr. Pranav Ranjan - SME Marketing Head from Magma in the execution of the questionnaire survey.

FOREWORD

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FOREWORD

The pandemic, COVID-19, has impacted health systems and economies the world over. In India, the ramifications of the pandemic can be expected to be particularly harsh on India's most economically vulnerable enterprise group - the Micro, Small and Medium Enterprises (MSMEs). The MSME sector has been redefined as of June 1, 2020 as part of the Atmanirbhar Bharat Abhiyaan relief package. The revised Micro, Small and Medium (MSME) enterprise classification is based on composite criteria including investment and annual turnover common to both Manufacturing and Services. The new definition has increased the limits for an enterprise to be categorized into one of the three categories. Even under the tighter earlier classification, the MSME sector comprised primarily of micro enterprises, accounting for 99.4 % of the 6.33 crore enterprises falling under this sector, while small and medium enterprises accounted for 0.52 per cent and 0.007 per cent of the MSME sector respectively.

While the Indian economy and Indian industry have been particularly hard hit due to COVID-19, the impact on the MSME sector is far more difficult to glean due to the very nature of these small, unorganized enterprises. A circular economy implies that the health of this sector will have an impact on the rest of the economy through both direct and indirect pathways. In light of the government's attempt to support the MSME sector through a relief package, comprising of debt relief through moratorium on payment of instalments of loans till August 31, 2020, two questions arise: One, What would be the impact of the moratorium on the lenders? Would it spell challenges in terms of an asset -liability mismatch? Two, what

would the demand side for these respondents look like? Will the business outlook and prospects have an impact on the quality of debt?

The joint report prepared by Magma and SPJIMR is an outcome of deep as well as extensive survey carried out over 98% of Magma Fincorp's SME customers, numbering 14,444 enterprises, across 70 locations between May 15- May 31, 2020. The report uses multi-level data points, with a combination of internal and external data. This is one of the largest sample sizes with precise structured and unstructured data coming from MSMEs and deploys the best of researching capabilities of SPJIMR to present a cogent and crisp response to understanding the financial impact of Covid on MSMEs[1].

Another key outcome of the report is the revelation of the deep transformation that will be required in the underwriting standards, which will need to deploy a plethora of data trails and data emerging from multiple variables arising out of structured and unstructured transactions which have been ignored hitherto. Conventional underwriting models will undergo a quiet requiem post the Covid pandemic, teaching us a few lessons along the way.

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[1] *Disclaimer: The research has been conducted by SPJIMR faculty: Dr. Tulsi Jayakumar and Dr. Anshul Verma purely for academic/research purposes. There were no commercial interests in carrying out this research.*

EXECUTIVE SUMMARY

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- 14,444 Micro, Small and Medium Enterprises across India were surveyed to understand the impact of the Covid on their earnings, business outlook, their perceived financial health score amidst the pandemic, their loan requirements and the moratorium availed from various lenders
- 73% of the respondents were from the micro and small sectors, while 6% were from the medium sector.
- The respondents were predominantly from the South and Western India, although all four zones were represented.
- 68% of the respondent firms were in the non-essentials business, 32% in the essentials business
- The respondent firms belonged to various industries
- Most firms stated that the impact of Covid on earnings was between 20-50%.
- About 83% of the respondents surveyed felt that the impact on their earnings would be less than 50%, while about half of the businesses surveyed said that impact on earnings would be between 20%- 50%.
- Overall the business outlook can be termed as 'Not Negative', with 62.67% responding saying they were neutral or positive regarding the business outlook.
- At the all-India level, 58% of the businesses surveyed had resumed operations during the survey period.
- On the Financial Health Score, 76% of the respondents gave themselves 3 (average) or above average (1 or 2) ratings.
- 51% of the respondents stated that they did not have any loan requirements
- 57% of the respondents have availed of the moratorium from other lenders, while almost 50% of the respondents have availed of moratorium from Magma.
- The proportion of respondents who have availed of moratorium from either Magma or other lenders is 53%.
- Size of the firm, measured by turnover, impacts the firm during a pandemic.

- The impact on earnings was marginally greater for smaller sized firms.
- Business outlook depends on the size of the firms, with smaller sized firms having more negative outlook.
- Larger-sized firms had started off their operations slightly more than smaller sized firms.
- The larger the size of the firm, the better is the perceived financial health, measured through the Financial Health Score.
- More than 50% of the smaller turnover businesses state that they will need to take a loan in the coming months.
- About 28% of the total respondents who have availed of moratorium from either Magma or other lenders are less than Rs. 10 crores in turnover. 12% of the moratorium availing businesses are between Rs. 10-Rs. 50 crores in turnover.
- Most of India - about 84%- was still under Red or Yellow Zones during the period under survey.
- The Western zone of India was worst afflicted, with 92.5% of the region being under Covid zones red and yellow in the West, while East was relatively better off.
- However, the Eastern zone respondents reported the greatest negative impact on earnings of 50% and more.
- A negative outlook was reported by 50% respondents in both North and East India, while in West India, this was about 40%.
- 70% of the businesses in South stated that they had resumed activities, as against, 55% in the East, 59% in the North and only 48% in the Western regions.
- The West accounts for the highest proportion of moratorium availed.
- The impact on earnings of less than 50% was expected to be the same for both essential and non-essential goods.
- 43% of the respondents in non-essential businesses have a negative outlook, compared to 25% for those in essentials businesses.
- Of the industries, Health care, Telecom, Oil & Gas, Pharmaceuticals and FMCG displayed highest positive outlook, while Tourism & Hospitality, Gems & Jewellery, Power & utilities, textiles and electronics displayed highest negative sentiments.
- Tourism and hospitality sector is the worst affected, while the pharma sector is the least affected.

CHAPTER 1

INTRODUCTION

INTRODUCTION

The MSME sector in India is an important sector contributing to inclusive industrial, economic and social development of the country over the last five decades. It fosters entrepreneurship and generates employment at comparatively lower capital cost, next only to agriculture. MSMEs complement large industries as ancillary units, and are an important element of the government's Atmanirbhar Bharat Abhiyaan.

The definition of the MSME sector has recently undergone a change. The revised MSME classification is based on composite criteria including investment and annual turnover common to both Manufacturing and Services. As per the new classification, Micro enterprises are those which involve an investment of up to Rs. 1 crore and turnover of up to Rs.5 crores; Small enterprises are those with investment of up to Rs.10 crore and turnover of up to Rs.50 crores and medium enterprises are those with investment of up to Rs. 50 crores and turnover of up to Rs. 250 crores.

The Annual Report of the Ministry of MSMEs provides the estimates of such MSMEs as per the old definition at 633.88 lakh unincorporated non- agriculture MSMEs in the country engaged in different economic activities. Of these 31% were in manufacturing, 36% in trading activities and 33% in other services. Out of 633.88 lakh estimated number of MSMEs, 324.88 lakh MSMEs (51.25%) were in rural areas and 309 lakh MSMEs (48.75%) were in the urban areas. The Micro sector with 630.52 lakh estimated enterprises accounts 99.4% of the total estimated number of MSMEs. The 'Small' sector with 3.31 lakh and Medium sector with 0.05 lakh estimated MSMEs account for 0.52 % and 0.01 % of total estimated MSMEs respectively.

SPJIMR analysed the data collected by Magma SME Business from 14,444 micro, small and medium enterprises as part of an exercise to understand the financial impact of Covid and the business outlook amongst this group amidst the pandemic conducted across the 4 zones of India: North, South, East, West. The survey was done between May 15- May 31 2020, when the lockdown had been declared partially lifted in some of the zones in India. This is one of the largest surveys that has been attempted during the pandemic for this sector, and as such has interesting findings.

SURVEY DETAILS

The survey was administered to 14,763 customers of Magma's SME Finance Group between May 15- May 31, 2020 upon partial lifting of the lockdown in several parts of India. Of these, 14,444 responded to the survey, providing a response rate of about 98%. The survey comprised of 8 questions to assess the nature of the business – essential vs. non-essential, whether the business had started and the expected date of commencement of business, their business outlook, impact of Covid on the business earnings, the moratorium availed from various lenders, their perceived financial health score and the loan requirements.

These questions were then analysed together with the demographics of the respondents.

The analysis was done at the following levels:

- Analysis of the demographic profile of the respondents
- Firm size (turnover) wise analysis of the respondents
- Geographical region-wise analysis of the respondents
- Nature of the goods/services (essential vs. non-essential) wise analysis
- Industry- wise analysis of respondents

CHAPTER 2

DEMOGRAPHIC PROFILE OF THE RESPONDENTS

DEMOGRAPHIC PROFILE OF THE RESPONDENTS

Majority of the enterprises are in the micro and small category (73%), while the medium category respondents are only 6%. These enterprises are predominantly in the western and southern parts of India, with the following being the geographic dispersion: North- 18%, South- 35%, East- 13% and West-34%. Of the 14,444 MSMEs surveyed, 68% were in the non-essentials business, while 32% were in the business of essentials.

Chart 1: Proportion of SMEs: Turnover-wise

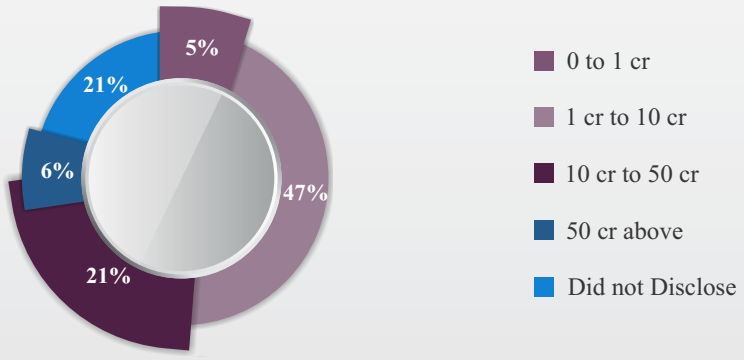


Chart 2: Geographical Dispersion of the Companies

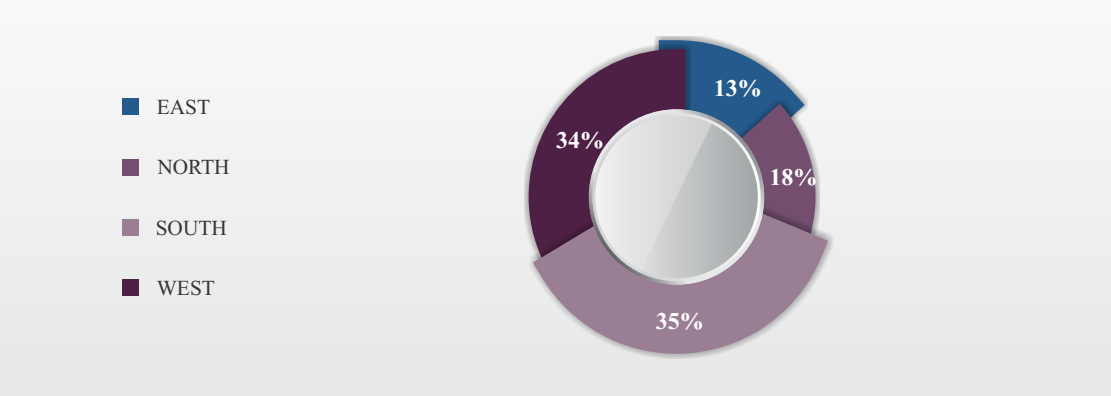
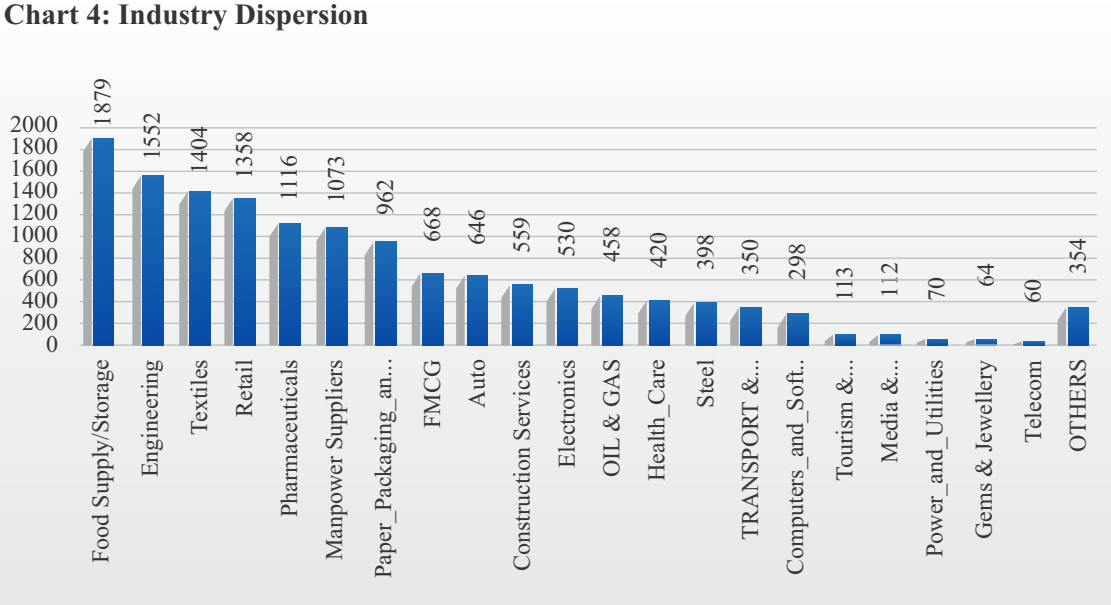


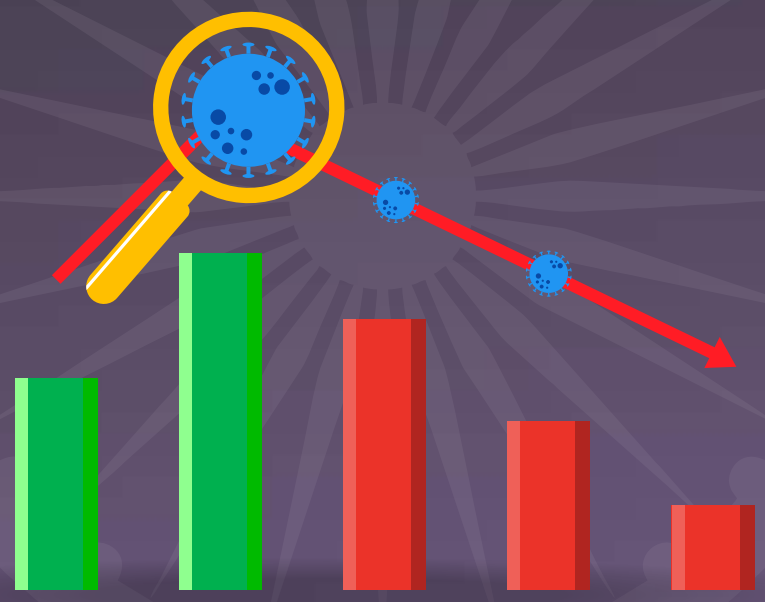
Chart 3: Proportion of Essential vs. Non-Essential Companies

Chart 4: Industry Dispersion



CHAPTER 3

SIZE OF RESPONDENT FIRMS (turnover basis) AND FINANCIAL IMPACT



SIZE OF RESPONDENT FIRMS (turnover basis) AND FINANCIAL IMPACT

The survey classifies respondents on the basis of their size in terms of turnover.

The impact of Covid on the earnings is marginally greater on smaller sized businesses. Thus, for instance , while 81% of the 0-1 crore turnover businesses stated a less than 50% impact on earnings, this proportion for the above 50 crores business was 85%.

Similarly, we can see that sentiments seem to improve with the size of the business, indicating that post Covid, businesses with higher turnover expect to withstand the Covid shocks better.

This may also be explained by the fact that more than 60% of the relatively larger-sized businesses (of turnover 10 crores and above) have started operating during the survey period.

More than 50% of the smaller turnover businesses state that they will need to take a loan in the coming months. This also can be seen through the self-rating on the Financial Health Score of 1-5, with 1 being the best and 5 being the worst. The proportion of respondents rating themselves 4 or 5 goes down as one looks at higher turnover businesses. *A higher turnover then is a panacea to good financial health.*

Chart 5: Impact on Earnings: Size-wise (turnover) Basis

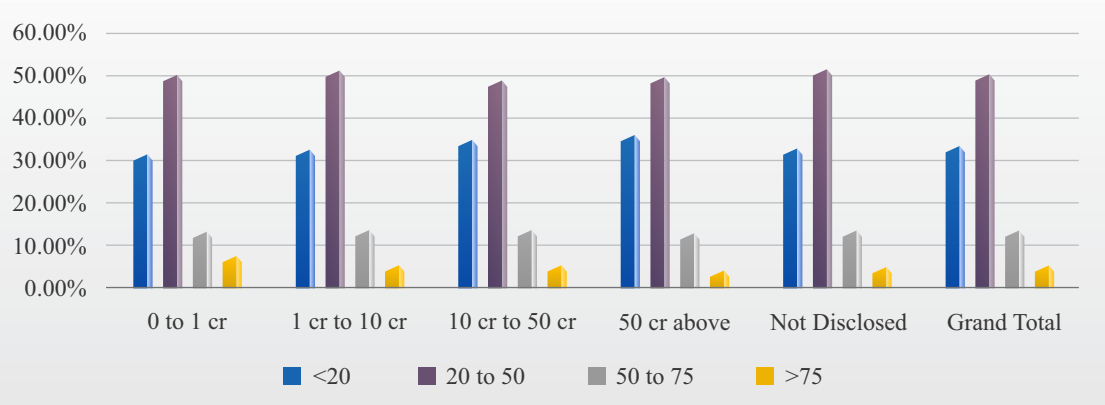


Chart 6: Business Outlook in Post Lockdown Era: Size-wise (Turnover basis)

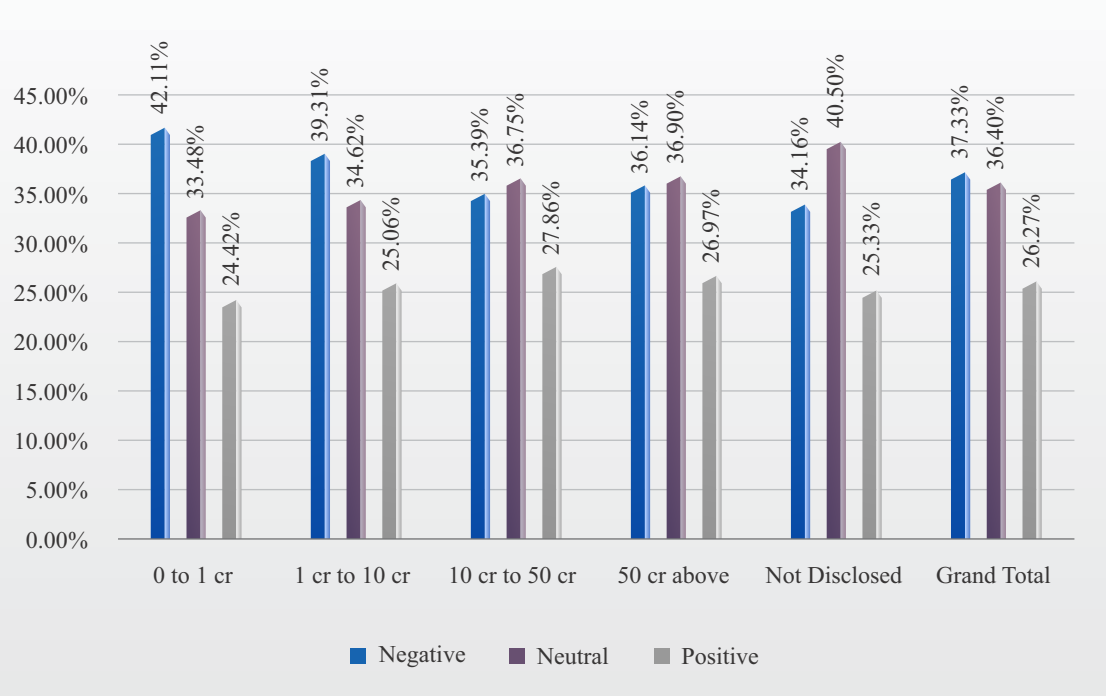


Chart 7: Business Start Status: Size (Turnover) wise

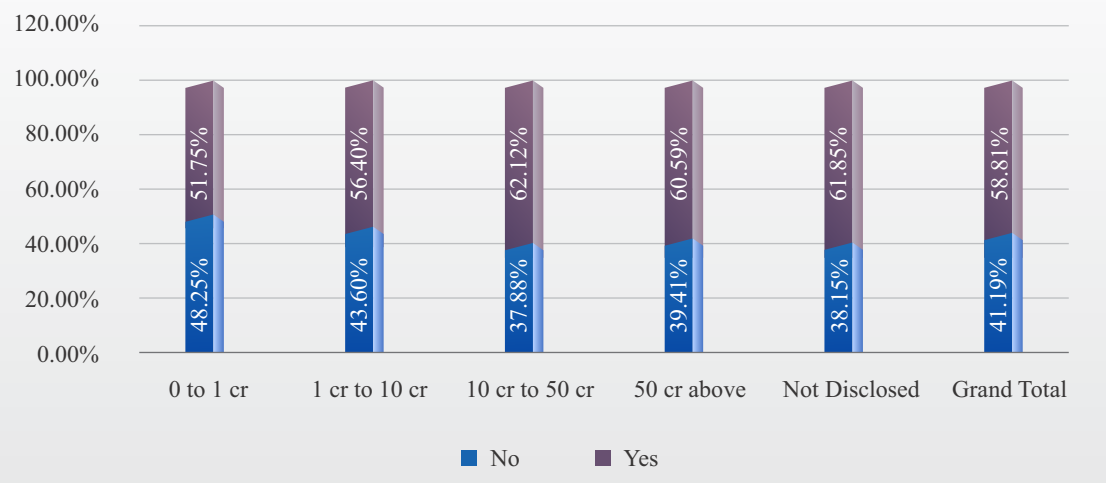


Chart 8: Financial Health Score: (Turnover) wise

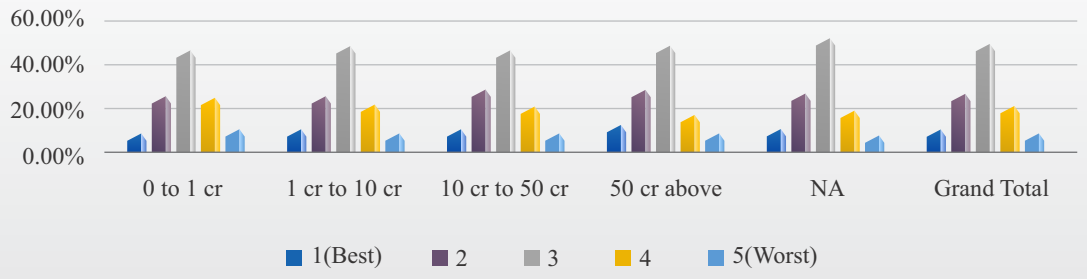


Chart 9: Loan Requirement: Size (Turnover) wise basis

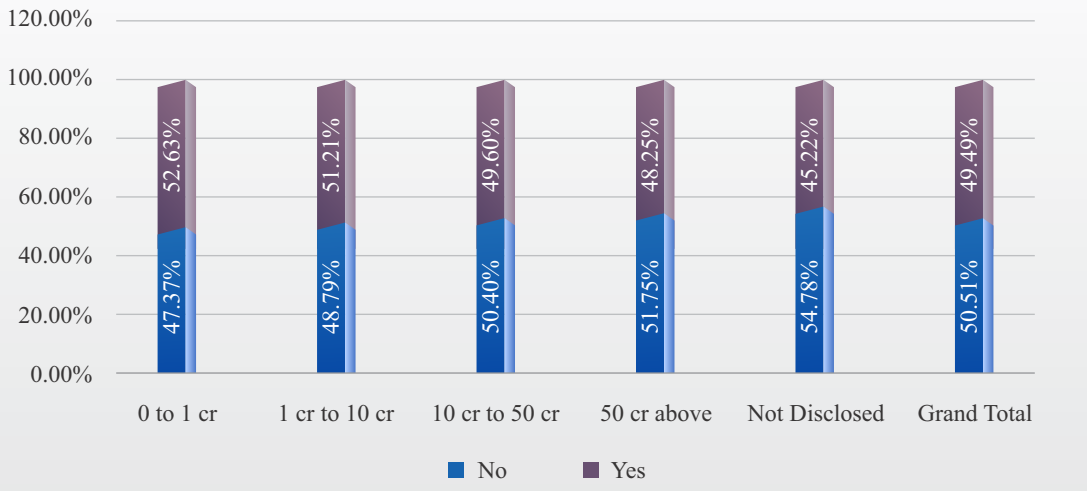
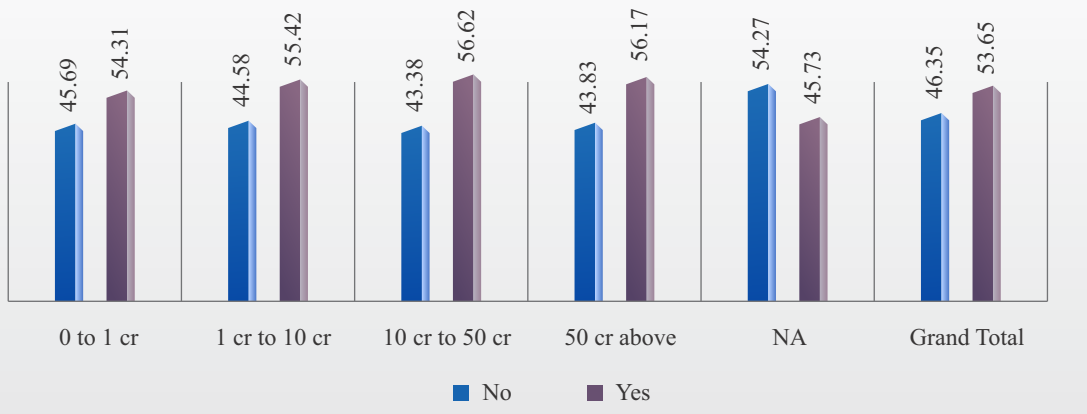


Chart 10: Moratorium availed from Magma/other lenders: Size (turnover) wise basis



CHAPTER 4

GEOGRAPHICAL ANALYSIS OF FINANCIAL IMPACT

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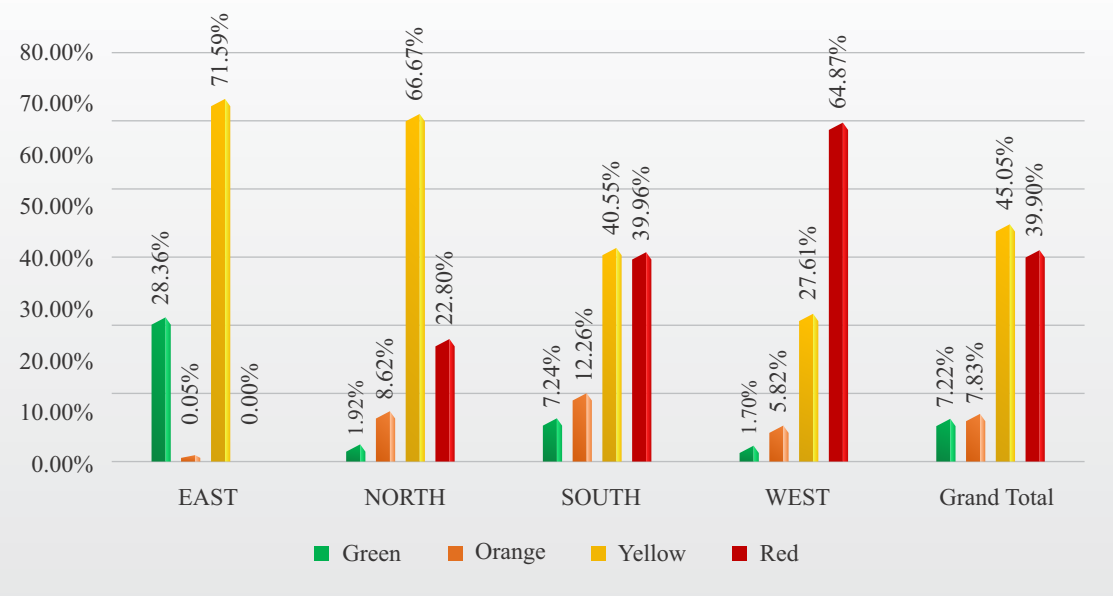
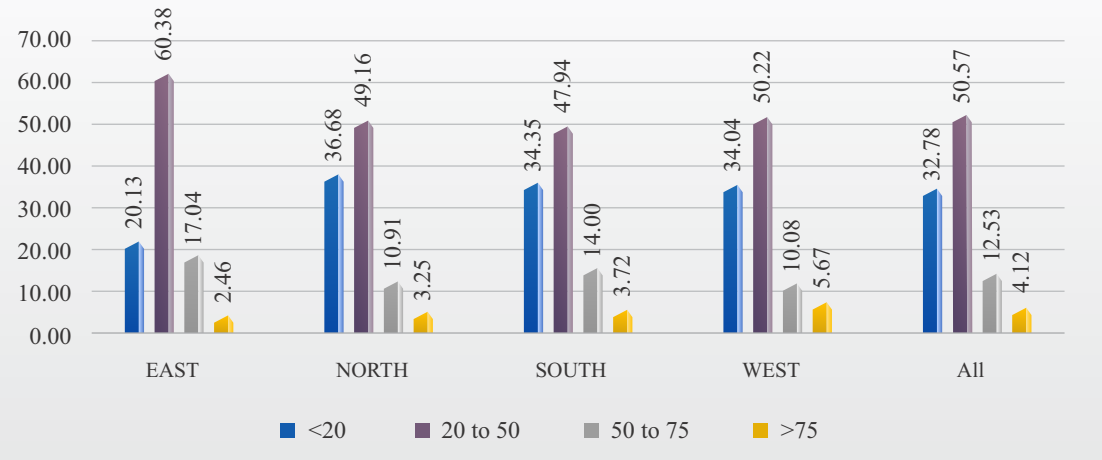
Most of India – about 84%- was still under Red or Yellow Zones during the period under survey. However, there was large geographical dispersion, with 92.5% of the region being under Covid zones red and yellow in the West, while East was relatively better off.

Chart 11: COVID Zone Dispersion Across Geographical Regions



Impact on Earnings: About 83% of the respondents surveyed felt that the impact on their earnings would be less than 50%, with 33% actually reporting an impact less than 20% . Most respondents across all four zones felt that the impact on their earnings would be between 20-50%

Chart 12: Geographical Dispersion of Impact on Earnings Due to COVID



Impact on Business Outlook due to COVID: Overall the business outlook can be termed as 'Not Negative', with 62.67% responding saying they were neutral or positive regarding the business outlook. However, there are regional variations. The North and East were almost similar in terms of the high proportion of respondents- more than 50%- with a negative outlook. The outlook in the South is largely neutral to positive, with only 23% expressing negative business sentiments. In the West, 40% still consider the business outlook to be negative.

This would also have to do with the proportion of businesses which have resumed activities. This proportion is the largest in South , with 70% of the businesses stating that they had resumed activities, as against, 55% in the East, 59% in the North and only 48% in the Western regions. At the All-India level, 58% businesses had resumed activities.

Chart 13: Region-wise business Outlook

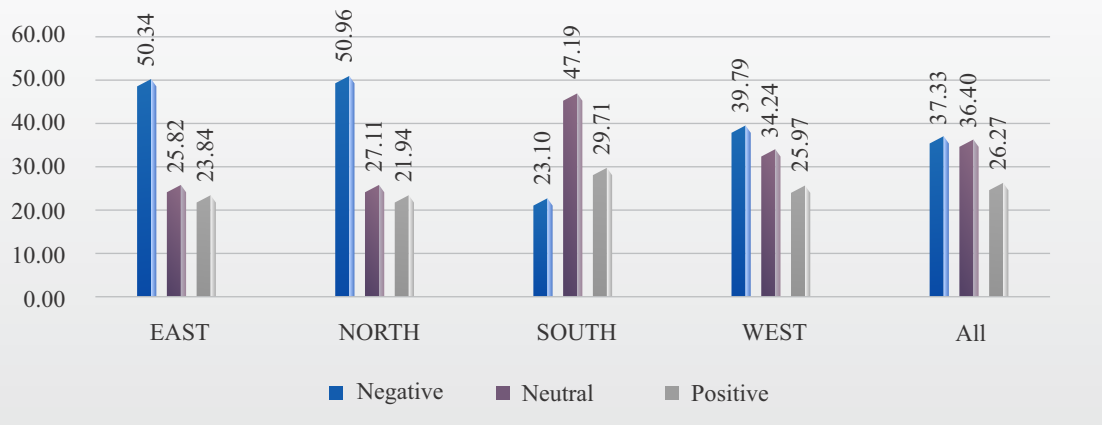
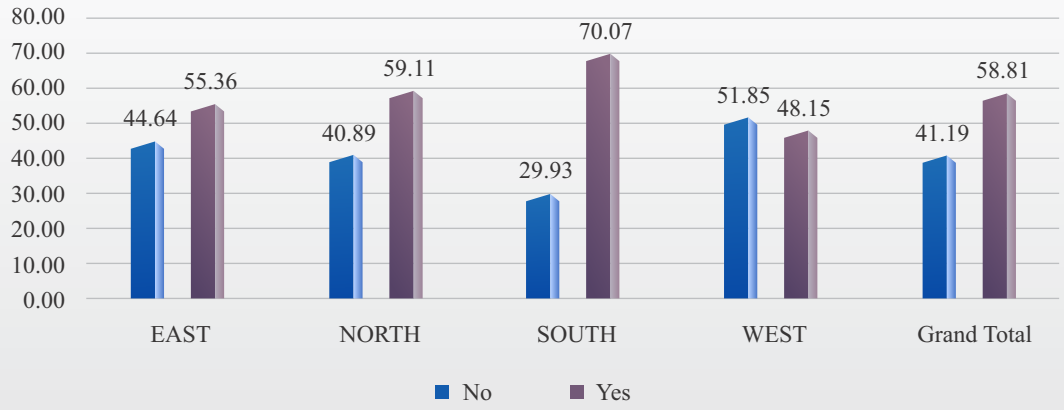


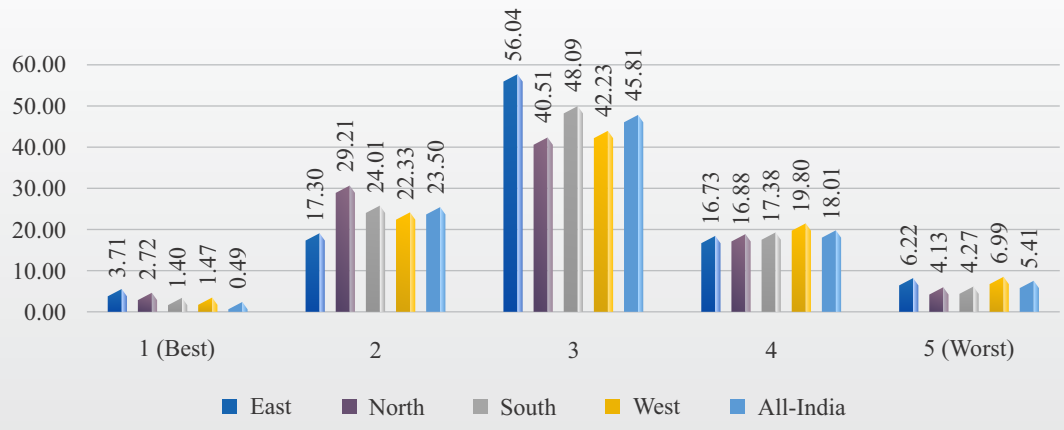
Chart 14: Proportion of businesses which have resumed activities



Financial Health Score vs. Loan Requirement

The survey looked at the financial health score that the respondents rated themselves on, using a scale of 1-5, with 1 being the best and 5 being the worst. 7.26% of the respondents across the various geographical regions rated themselves 1 . The proportion of the respondents who gave themselves 2, 3, 4 and 5 ratings were respectively, 23.5%, 45.8%, 18.01% and 5.41% respectively. Across all the four zones, majority of the respondents rated themselves middle of the scale. However, this also implies that about 76% of the respondents gave themselves average to above average financial ratings.

Chart 15: Geographical Dispersion of Financial Health Score



The proportion of respondents stating that they had a loan requirement was 49%; 51% respondents stated that they did not have a loan requirement. Such reluctance to borrow, when combined with the moratorium taken may indicate businesses which are trying to survive rather than those which borrow to invest for future growth (i.e. thrive). Thus, 57% of the respondents have availed of the moratorium from other lenders, while almost 50% of the respondents have availed of moratorium from Magma. The proportion of respondents who have availed of moratorium from either Magma or other lenders is 53%.

Chart 16: Geographical Dispersion of Loan Requirements

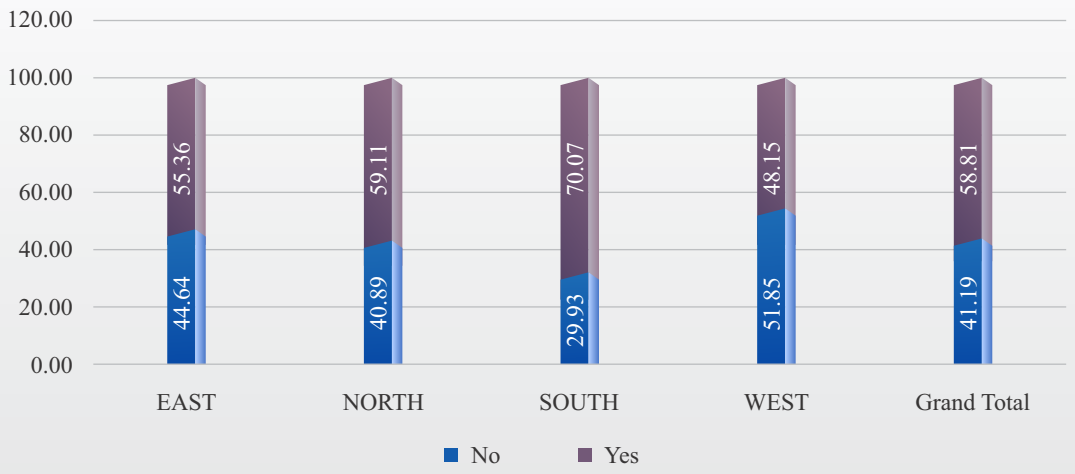
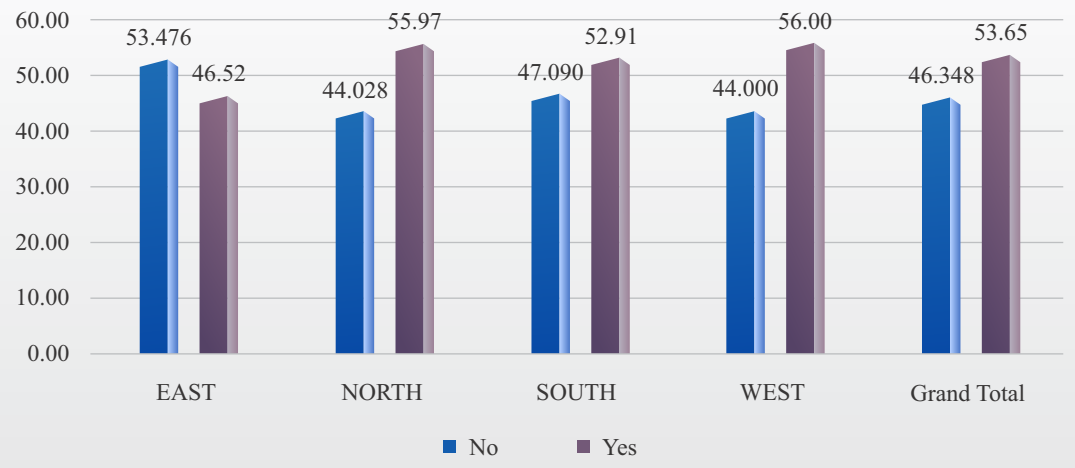


Chart 17: Moratorium Availed from Magma/Other Lenders



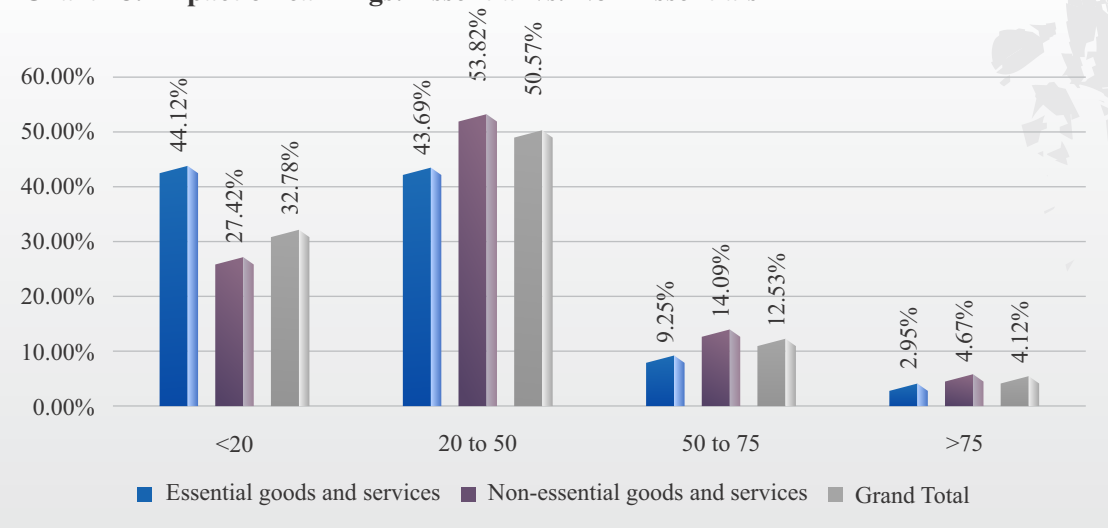
CHAPTER 5

NATURE OF THE GOODS/services- ESSENTIAL *VS.* NON-ESSENTIALS

NATURE OF THE GOODS/SERVICES- ESSENTIAL *VS.* NON-ESSENTIALS

Impact on Earnings: Of the 14,444 MSMEs surveyed, 68% were in the non-essentials business, while 32% were in the business of essentials. Both essential and non-essential businesses stated their impact on earnings as being in the less than 20% or 20-50% range. Of the total businesses surveyed, About 50% of the businesses surveyed said that impact on earnings would be between 20%- 50%, while 83% felt that the impact would be less than 50%. Interestingly enough, such a response towards the impact on earnings is shared by both essential and non-essential goods.

Chart 18: Impact on earnings: Essential vs. Non-Essentials

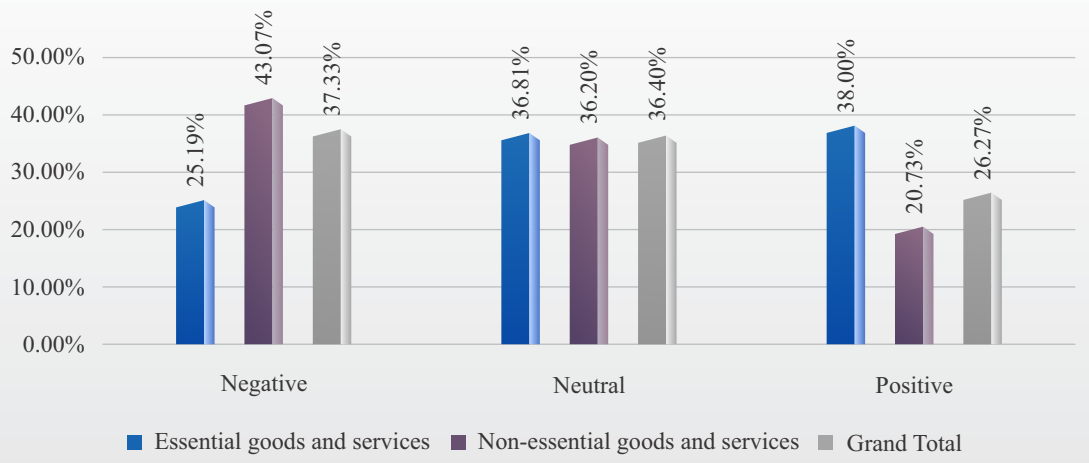


Outlook not negative:

Respondents were asked to state their outlook for the future. While the majority outlook was negative at 37%, it also turns out that businesses with either neutral or positive outlook is almost 73%.

The proportion of businesses in the non-essentials with a negative outlook is relatively far greater at 43% as compared to that in the essentials business at 25%. Thus, about 75% of the businesses in the essentials goods sector are actually positive (38%) or neutral (37%). Of the businesses in the non-essential sector, 57% are either positive (21%) or neutral (36%).

Chart 19: Business Outlook Post Covid: Essentials Vs. Non-essentials



CHAPTER 6

INDUSTRY WISE ANALYSIS

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INDUSTRY WISE ANALYSIS

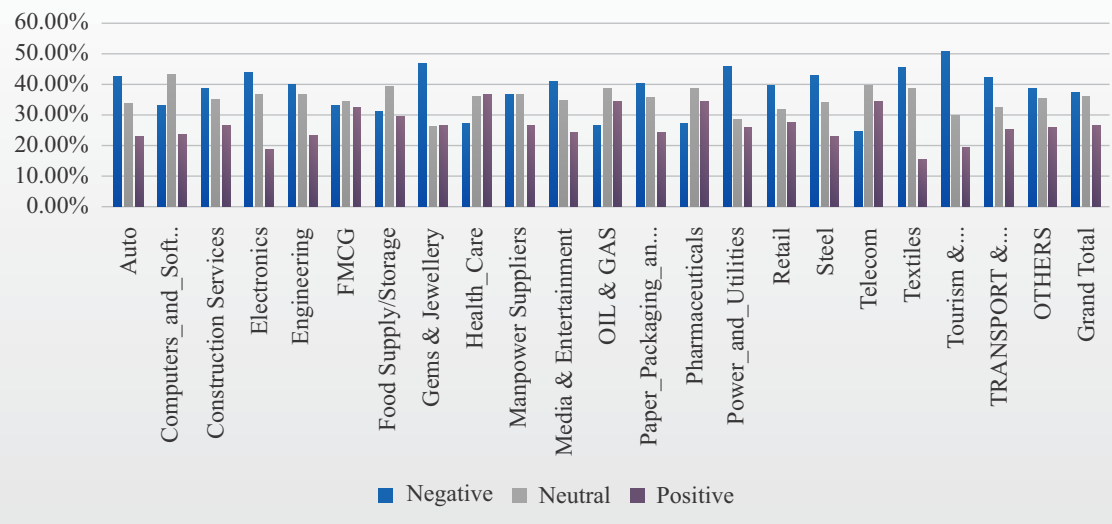
The top 5 sectors in terms of business outlook , in that order, were:

1. Health care
2. Telecom
3. Oil & Gas
4. Pharmaceuticals
5. FMCG

The businesses which have responded with negative outlook are (in the order of negative sentiments):

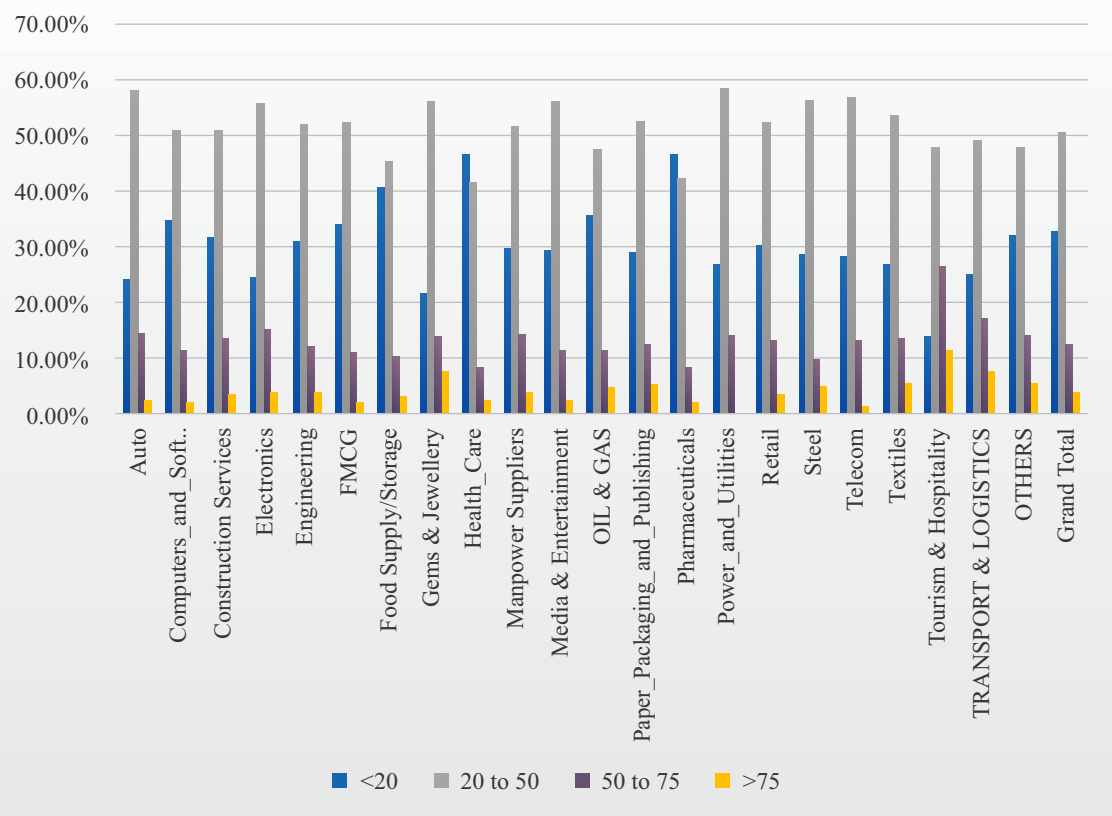
1. Tourism & Hospitality
2. Gems & Jewellery
3. Power & utilities
4. Textiles and
5. Electronics

Chart 20: Business Outlook: Industry-wise



The tourism and hospitality sector is the worst affected, with 38% respondents claiming a hit of 50% and above in their earnings. 89% of the pharma respondents stated an impact on earnings of less than 50%, making it the least affected.

Chart 21: Impact on Earnings: Industry-wise



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Message from Magma Fincorp Ltd.

MR. MANISH JAISWAL

MD & CEO
Magma Housing Finance &
SME Business
Mumbai

We are extremely happy to collaborate with SPJIMR, one of the top business schools of India, for bringing out this publication. The report aims to identify the financial impact of the Covid pandemic on MSMEs and the outlook of these MSMEs. Such an analysis will help in identifying the key pain points of this sector, which forms the backbone of the Indian economy.

We look at this report as an attempt to build industry-academia partnerships in identifying the key challenges which face India in the wake of the pandemic.

Message from SPJIMR

DR. RANJAN BANERJEE

Dean & Professor, Marketing
SPJIMR
Mumbai

We, at SPJIMR, are delighted to partner with MAGMA- a leading financial services company with special focus on MSMEs, in bringing out this survey report on "The Financial Impact of COVID on Indian Micro and Small Enterprises and their Outlook amidst the pandemic".

As a School of Management, SPJIMR has always been proactive in taking initiative for work which can Influence Practice in a significant way by providing insights into contemporary issues. The Centre for Family Managed Business has been a pioneer in supporting and fostering growth of MSMEs in India , which are essentially Family Managed Businesses, through both academic and advisory and consulting inputs. Initiatives such as this report are just a reiteration of our commitment to the SME sector.

I am sure that this report will go a long way in providing valuable insights to practitioners and policy-makers interested in the MSME sector and may provide the basis for further action to help this sector tide through these difficult times.

As a leading school of management, SPJIMR stands ready to play its part and help contribute to creating the conditions for growth that is robust, inclusive and sustainable.

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