October 2013

SME INSIGHTS

A Newsletter from ONICRA

Onicra Credit Rating Agency of India Limited

ABOUT ONICRA CREDIT RATING AGENCY OF INDIA LIMITED (ONICRA)

Onicra Credit Rating Agency is an active player in the Credit and Performance Assessment space. It provides analytical risk assessment and rating solutions to MSMEs and Corporate.

These ratings enable the lender, service provider or any other stake holder to make smart, value based decisions on the Medium, Small and Micro Enterprises (MSME) or the corporate by arming them with essential information including financial, operational, 3-Dimensional analysis that provides a holistic view about the entity.

About Onicra MSME Ratings

The Ministry of MSME through NSIC has signed a memorandum of understanding with Onicra to provide performance and credit rating services to MSMEs. The rating creates awareness about the strengths, weaknesses, opportunities and threats, and assists in identifying areas of improvement for the MSME. Under this scheme, the MSME only pays 25% of the rating fee to Onicra while the remaining 75% is paid by NSIC as subsidy.

The company has rated around 22732 MSMEs since 2005.

NSIC scheme features

Benefits of NSIC- Onicra Performance and Credit Rating

- Assists in risk management by highlighting parameters measuring operational, financial and business risk.
- Enhances acceptability with Banks, Financial Institutions and provides access to cheaper and timely credit.
- It is a “holistic health check-up of the unit” that establishes credibility, goodwill and assists in dealing with large companies.
- Helps in marketing and serves as first point to generate interest among potential partners.

MANAGEMENT SPEAK: Improving SME financing: Key to Economic Recover

Indian economy is facing challenges specially in creating opportunities for inclusive growth. The role of SMEs and their importance in the growth story of the country is undeniable. By its less capital intensive and high labor absorption nature, the SME sector can easily become the thrust engine to infuse industrial growth with diversification. However the much needed transition required to strengthen the human and institutional capabilities to take advantage of trade and investment opportunities arising at domestic and global level has not taken place. SMEs are still struggling with traditional issues of financing, technology and human capital improvement.
Why Investing in SME Sector is the best bet?

Demand structure of Indian markets supports SMEs

As the economic slowdown casts it's shadow on capital goods and the stock markets, the small businesses are getting squeezed from all sides starting from delay in payments to huge gaps in financing and eventually loss of competitiveness. This is the time when institutional investors shy away and the small business has to rely on open market jeopardizing the long term interests of business for sustainability concerns in a shorter run. The key is to help the small business during this rough patch. This would certainly require policy initiatives coupled with institutional capacity building. The outlook for SME sector is positive, in-fact very promising. The optimism is based on an interesting feature of Indian market and its demand structure. India as a market has immense diversity in demand structures and production systems which will ensure long term co-existence of multiple layers of demand for products, technologies and processes. Markets for same product or process, differentiated by quality, value add and sophistication will always exist. This heterogeneous nature of the Indian market will always favour the growth of SMEs capitalizing on their niche.

Potential for Export

With a share of 36% in the total exports, Indian SME sector is an important pillar of economic activity supporting poised to be a part of the growth story. SME products in the export market are largely specialty products thus MSMEs will always enjoy the niche market. The depreciating rupee value and rising inflators pressure clearly indicate that we need to export more and at better quality. More than 60% the export related demand is from US and Europe. SMEs involved in export oriented goods need to invest more to understand these markets and diversify to new emerging markets to mitigate their risk. This will involve substantial investments. SMEs financing here would just not mean providing money for working capital but for capacity building.

Empowering the SMEs through Easy financing is the way-forward

Although Indian government has taken multiple initiatives like the Credit Guarantee Scheme & dedicated SME exchanges to improve financing to SMEs but these programs are still way behind their objectives of timely and affordable financing for SMEs especially to the micro enterprise segment. Banks and other institutional investors will have to come forward to share this responsibility with the government agencies and create an ecosystem that improves the flow of funds to the SMEs and thus empower them to be more competitive and sustainable. Empowering the SME sector will not only mean improvements at the industry or sector level but will also create catalytic effect for inclusive growth and overall improvement of the economy.

*Foot Note: The recommendations of the Prime Minister's Task Force on MSMEs (Chairman: Shri T.K.A. Nair, Principal Secretary) clearly cited SME financing as one of the major issues concerning the SME sector.

ECONOMIC PERSPECTIVE

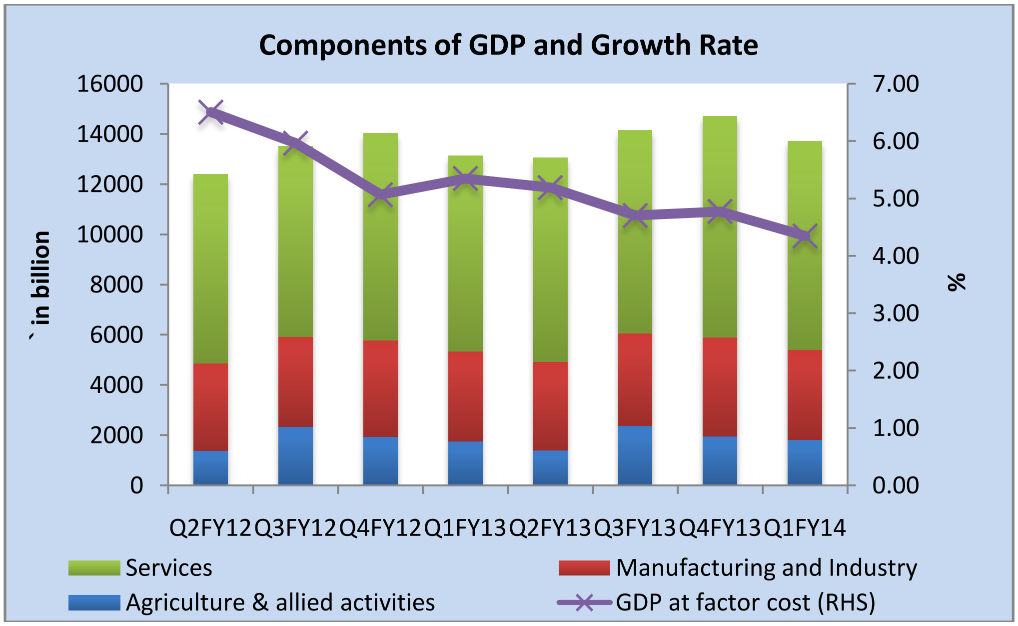
Executive Summary

Indian economy has witnessed a sluggish trend in the FY12 and the same story has continued in FY13 and Q1FY14 also. The economic growth has dropped from 6.48% in FY12 to 4.99% in FY13 and 4.35% in Q1FY14. Reasons for the decline have been partly global and partly domestic.

On the domestic front, Indian economy continued to decline in all its sectors. Rainfall played an important role in the agriculture sector, while the manufacturing and service sectors continued to decline in the wake of tighter monetary policies, delays in projects due to government regulations, weakening consumption and declining exports in Q1FY14. The mood of investments in the economy has weakened and the deployment of bank credit into corporate has increased at a declining rate. The challenge is to boost the investments into the economy while maintaining the inflation under control.

The fiscal consolidation in US on the global front has been the most significant reason for the decline in the economic growth. While the US fiscal consolidation has begun, it has offered no respite to the Indian economy. Q1FY14 has not been good enough and the Q2FY14 numbers are not expected to be very encouraging due to the weakening rupee. The impact of US fiscal consolidation has led to an exodus of FIIs from the Indian market to the more resilient US economy. The demand for Indian goods has decreased and the CAD has increased due to rising import bill on account of increasing oil bill and gold and silver imports.

Economic Growth



Source: CSO

Note: GDP at constant price

Composition of Sub-Sectors of GDP

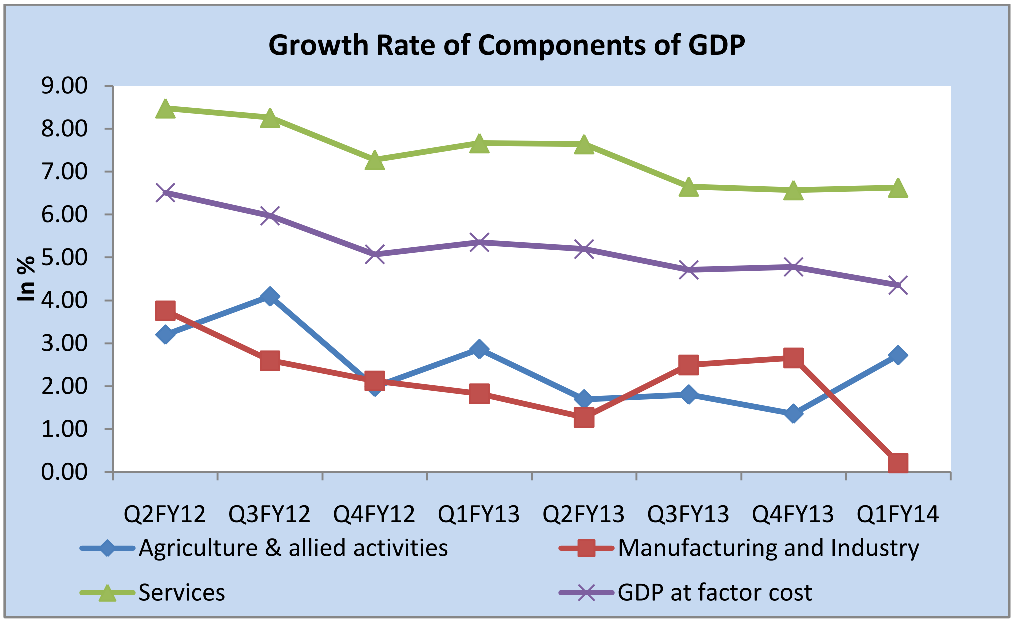
(Amount in ` Billion)

Sectors	Q2FY12	Q3FY12	Q4FY12	Q1FY13	Q2FY13	Q3FY13	Q4FY13	Q1FY14
Agriculture & allied activities	**1389.87**	**2338.94**	**1946.49**	**1768.88**	**1413.34**	**2381.06**	**1972.82**	**1817.05**
Manufacturing and Industry	**3475.81**	**3590.46**	**3833.99**	**3588.9**	**3519.99**	**3679.91**	**3935.81**	**3596.39**
Mining & Quarrying	239.42	273.45	307.58	263.02	243.45	271.57	298.15	255.68
Manufacturing	1998.73	2026.65	2171.36	2012.3	2000.01	2076.89	2227.28	1988.27
Electricity, Gas & Water Supply	245.99	246.86	250.2	260.18	253.86	257.98	257.16	269.78
Construction	991.67	1043.5	1104.85	1053.4	1022.67	1073.47	1153.22	1082.66
Services	**7545.4**	**7583.13**	**8256.78**	**7784.76**	**8121.96**	**8087.72**	**8799.18**	**8301.04**
Trade, Hotel, Transport and Communications	3464.52	3567.68	3881.89	3701.97	3699.96	3795.5	4122.91	3845.67
Finance, Insurance, Real Estate & Business Services	2344.6	2385.86	2461.24	2509.55	2539.96	2572.16	2685.16	2733.88
Community, Social & Personal Services	1736.28	1629.59	1913.65	1573.24	1882.04	1720.06	1991.11	1721.49
GDP at factor cost (RHS)	**12411.08**	**13512.53**	**14037.26**	**13142.54**	**13055.29**	**14148.69**	**14707.81**	**13714.48**

Growth Rate of Sub-Sectors of GDP

(In %)

Sectors	Q2FY12	Q3FY12	Q4FY12	Q1FY13	Q2FY13	Q3FY13	Q4FY13	Q1FY14
Agriculture & allied activities	3.20	4.09	1.98	2.86	1.69	1.80	1.35	2.72
Manufacturing and Industry	3.75	2.59	2.12	1.82	1.27	2.49	2.66	0.21
Mining & Quarrying	-5.33	-2.63	5.17	0.37	1.68	-0.69	-3.07	-2.79
Manufacturing	3.06	0.66	0.11	-1.04	0.06	2.48	2.58	-1.19
Electricity, Gas & Water Supply	8.44	7.66	3.54	6.16	3.20	4.50	2.78	3.69
Construction	6.52	6.89	5.09	7.04	3.13	2.87	4.38	2.78
Services	8.48	8.26	7.27	7.66	7.64	6.65	6.57	6.63
Trade, Hotel, Transport and Communications	7.00	6.88	5.07	6.10	6.80	6.39	6.21	3.88
Finance, Insurance, Real Estate & Business Services	12.34	11.42	11.35	9.28	8.33	7.81	9.10	8.94
Community, Social & Personal Services	6.47	6.84	6.81	8.86	8.39	5.55	4.05	9.42
GDP at factor cost	6.51	5.97	5.07	5.35	5.19	4.71	4.78	4.35

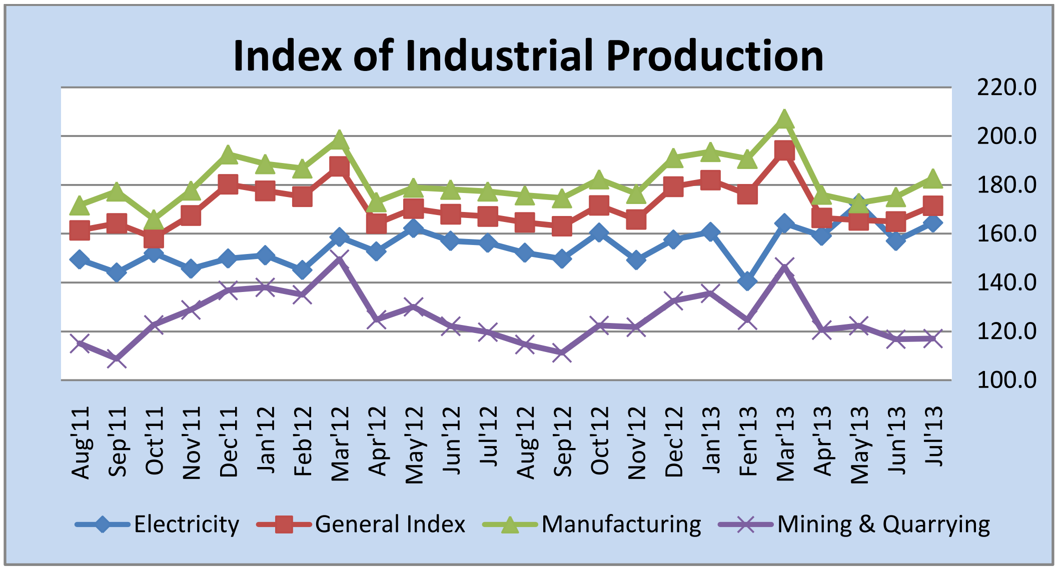


The declining growth rate of GDP over the last two years speaks poorly of the performance of the Indian economy. The stress on the manufacturing sector has been very high and has lead to an overall decrease in the economic growth rate. Except for community, social and personal services sub-sector, no other sub-sector has surpassed its performance over the last year. As a result, the services sector has been able to maintain its growth rate at approx. 7% p.a.

Agriculture and Allied Activities

Agriculture contributed 13.25% of GDP in Q1FY14; and the growth rate of the sector has been better in this quarter vis-à-vis the last 12 month period. As per the data released by Department of Agriculture and Cooperation, improvement in the rainfall during the end of the FY13 has led to an improvement in the rabi crop production, which has continued the good effects during the Q1FY14 also. Although Rabi crops such as coarse cereals, pulses, and oilseeds registered growth, it was too insignificant to pull the sectoral growth rate.

Manufacturing and Industry



The manufacturing sector had shown some promise during the last two quarters in FY13. However, it has declined in Q1FY14. The decline is significant as even the base numbers (Q1FY13) are not very high. The manufacturing sector has been severely affected as the financial market has turned its face towards US and investment by the domestic players could not keep pace with the exodus of funds.

While Electricity, Gas and Water supply have seen slower growth, the mining and quarrying sub-sector has seen a fall in output. Failing health of the power companies, scarcity of production of resources like gas and delay in the implementation of new oil and gas projects has curbed the growth of electricity, gas and water supply sub-sector. Mining and quarrying sub-sector continues to suffer from infrastructural impingements and delays in regulatory and environmental clearances. The decline in output of mining and quarrying sub-sector has been significant at 3.07% in Q4FY13. The construction sub-sector had also contributed to the manufacturing and industry sector growth in Q4FY13 and has since slowed down.

Service

The service sector has seen a decline in its growth rate in Q1FY14 due to a decline in the growth of ‘Trade, Hotel, Transport and Communications’ and ‘Finance, Insurance, Real Estate, and Business Services’ sub-sector. The quarterly growth of community, social and personal services sub-sector has been good. The continual depreciation of rupee has led to a decrease in foreign trade of services, especially travel. A low market sentiment and declining global economy has led to low growth rate of the services sector.

Consumption Drivers

Growth in %	Q1FY13	Q1FY14
Production of Food Products and Beverages	-0.91	-1.63
Production of Apparel	-6.37	45.23
Production of Consumer Goods	3.95	-2.41
Deployment of Bank Credit to Housing	11.27	17.02

* Source: RBI

The above table indicates that there has been a significant growth in the apparel and a good growth in the housing sub-sector in the Indian economy. This is indicative of the increasing investment of the FDI in the textile and construction sector.

With the food inflation touching all times high, the growth in consumption and consequently production of food and beverages has been badly hit. The faltering economy has also lead to a decrease in the production of consumer goods.

Investment Drivers

Industry wise Deployment of Gross Bank Credit

Particulars	Share towards Deployment of Gross Bank Credit As on 26th July 2013 (%)	Growth % (YoY)	
		Jul-12	Jul-13
Infrastructure	34.43	17.53	21.78
Basic Metal & Metal Product	14.01	18.72	20.12
Textiles	8.05	12.65	14.52
Chemicals & Chemical Products	6.34	11.60	21.34
All Engineering	5.79	28.06	7.18
Food Processing	5.41	18.39	35.46
Gems & Jewellery	3.04	20.98	32.07
Vehicles, Vehicle Parts & Transport Equipment	2.65	17.98	4.86
Construction	2.35	23.56	5.61
Petroleum, Coal Products & Nuclear Fuels	2.35	16.80	3.40
Cement & Cement Products	2.11	15.83	28.77
Mining & Quarrying (incl. Coal)	1.41	23.39	-3.73
Rubber, Plastic & their Products	1.37	8.40	7.36
Paper & Paper Products	1.32	14.12	16.23
Beverage & Tobacco	0.69	2.01	6.32
Leather & Leather Products	0.39	6.18	7.82
Wood & Wood Products	0.35	19.52	21.79
Glass & Glassware	0.31	24.27	6.63
Other Industries	7.62	28.44	-7.70
Industries	**100.00**	**18.45**	**15.90**

* Source: RBI

Registering a growth of 15.90% (YoY) as on July 2013, vis-à-vis 18.45% for the corresponding period last year, credit deployment towards industry has remained subdued depicting entrepreneurs are not willing to take risk in these gloomy market conditions. Infrastructure (33.43%), basic metal and metal products (14.01%), textiles (8.05%), engineering (5.79%), chemical and chemical products (6.34%), food processing (5.41%) and gems and jewellery (3.04%) industries have accounted for major shares in overall credit to industry.

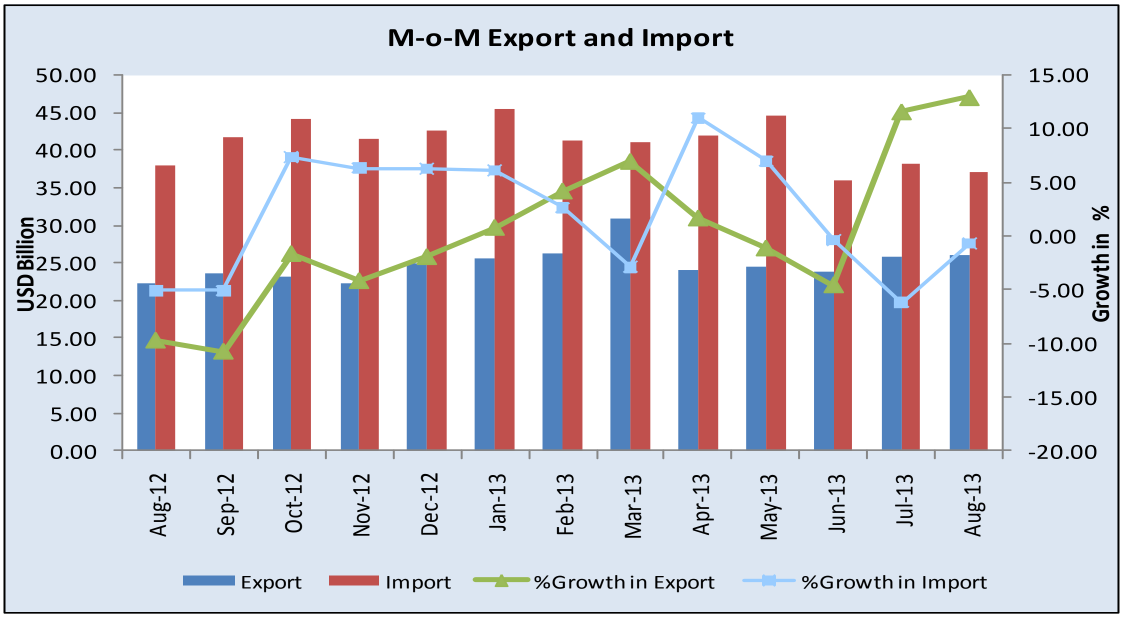
Credit deployment growth toward industry was slower this year as compared to last year in the same period, mainly due to slower pace or decline (in some cases) of credit deployment in industries like mining and quarrying, engineering, petroleum, coal & nuclear fuels and construction.

The decline in credit deployment in mining & quarrying (incl. Coal) of around 3.73% against a growth of 23.39% in July 2013 has major effects on the overall scenario of credit deployment towards the industry. The pace of credit deployment towards engineering industry (from 28.06% in July 2012 to 7.18% in July 2013) has also declined along with fall in pace of credit deployment towards petroleum, coal & nuclear fuels and construction by more than 10 percentage points in both the industries.

The slowdown in domestic market due to slow pace of infrastructural development and various other regulatory issues ranging from stricter mining norms to slow speed of departmental clearances has affected the industry. The falling demand and volatility in rupee has further aggravated the situation and feared the players from making new investment.

Some industries like food processing, chemical and infrastructure (Power & Road) have shown some improvement as far as growth in credit deployment is concerned.

Export-Import Trend



Foreign Trade (USD Billion)

Month	Export	%Growth in Export (YOY)	Import	%Growth in Import (YOY)	Trade Balance
Jul-12	22.44	-14.80	37.94	-7.61	-15.49
Aug-12	22.33	-9.74	37.95	-5.08	-15.62
Sept-12	23.70	-10.78	41.78	-5.09	-18.08
Oct-12	23.25	-1.63	44.21	7.37	-20.96
Nov-12	22.30	-4.17	41.59	6.35	-19.29
Dec-12	24.88	-1.92	42.55	6.26	-17.67
Jan-13	25.59	0.82	45.58	6.12	-19.99
Feb-13	26.25	4.23	41.18	2.65	-14.92
Mar-13	30.85	7.00	41.16	-2.90	-10.31
April-13	24.16	1.70	41.95	11.00	-17.78
May-13	24.50	-1.11	44.64	6.99	-20.14
June-13	23.78	-4.56	36.03	-0.37	-12.25
July-13	25.83	11.64	38.10	-6.20	-12.27
Aug-13	26.14	12.97	37.05	-0.68	-10.92

Source: Ministry of Commerce & Industry

India's export has increased by around 12.97% to USD 26.14 billion in August 2013 as compared to the same period a year ago. Import on the other hand has fallen marginally by around 0.68% to USD 37.05 billion, one of the lowest in last few months. As a result the trade deficit (gap between export and import) has narrowed to a five month low of USD 10.92 billion in August 2013.

The free fall of rupee in last few months has made export more attractive for the traders and manufacturers, as they are generating higher realization on their products. Industries like Pharma, IT are generating good benefits; export from Engineering sector has also increased by around 2.00% in August 2013 but the sector could not gain much as the products have high import contents. The demand from US and Euro zone has also revived, due to growth in the US economy by 2.50% in the quarter ended June 2013, better than the 1.70% growth initially estimated. The Euro zone emerged from recession after nearly two years, growing at 0.30% in the second quarter of 2013.

India's import has marginally fallen in August 2013 by 0.68%, making it third straight month of continuous fall in import on YOY basis. The fall in non-oil import, by around 10.40% in August and 0.30% decrease on cumulative basis during the period April-August 2013 as compared to the same period last year, has led to the fall of total import in India. But the higher value of oil import is putting strain on the overall import scenario; it increased by around 17.88 % in August 2013 and 5.60% higher on cumulative basis during the period April-August 2013 as compared to same period during the last year. Such an increase in the value of oil import is because of combined effects of increase in the international crude oil prices as well as rupee depreciation.

Trade deficit scenario of the Indian economy is better, if we take into consideration the period between April – August 2013, as trade deficit is lowest of around USD 10.92 billion in August 2013. It has fallen from a high of USD 20.14 billion in May 2013 due to the various initiatives taken by the government to limit the gold import during the last few months along with the lower imported goods due to costlier dollar.

Interest Rate

Item/Week Ended	2012	2013		
	17-Apr	19-Mar	15-Jul	7-Oct
Cash Reserve Ratio	4.75	4.00	4.00	4.00
Bank Rate	9.00	8.50	10.25	9.00
Repo Rate	8.00	7.50	7.25	7.50
Reverse Repo Rate	7.00	6.50	6.25	6.50
Marginal Standing Facility (MSF)	9.00	8.50	10.25	9.00

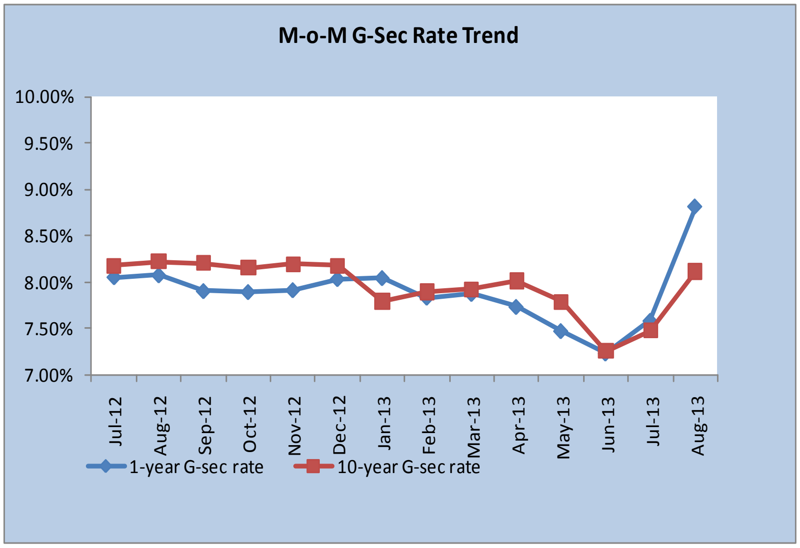
Source: RBI

Since July 2013 a number of measures have been put in place by RBI in order to reduce the volatility in the foreign exchange market. Based on an assessment of the current macroeconomic situation, the Reserve Bank of India has increased the policy repo rate under the liquidity adjustment facility (LAF) by 25 basis points from 7.25% to 7.50% on 20th September 2013. Consequently, the reverse repo rate under the LAF stands adjusted to 6.50% and the marginal standing facility rate and the Bank Rate to 9.50%. Furthermore, the minimum daily maintenance of the CRR prescribed by the RBI is brought down from 99 per cent of the requirement to 95 per cent.

On 7th October 2013, there has been a further cut in the MSF rate from 10.25% to 9.00% in the wake of strengthening of rupee and easing of money market operations.

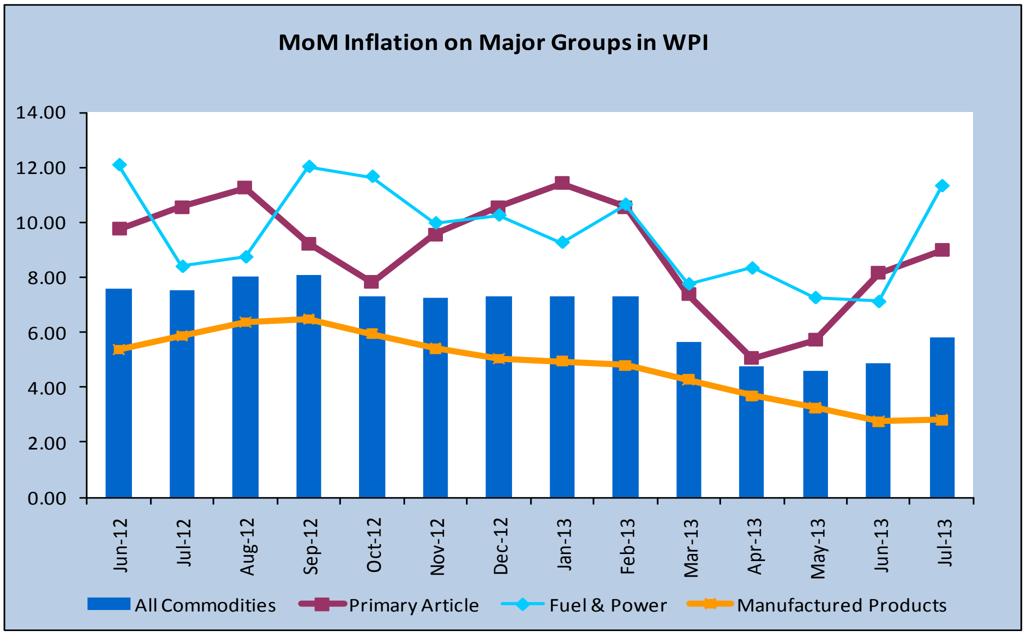
Wholesale inflation has started rising again as the fuel price increase has been compounded by the sharp depreciation of the rupee and rising international commodity prices, which pushed RBI to alter the policy rates.

The rates of Indian government bonds have shown an upward trend since June 2013. There has been a sharp increase in the rate for August 2013 on account of sudden fall in the value of rupee and increased attractiveness of US securities, on the back of improvement in the US economy and hopes of possible partial withdrawal of US Federal Reserves' liquidity infusion measures.



Source: FIMMDA

Inflation



Source: RBI

WHOLESALE PRICE INFLATION (%)

Commodity	Weight	Jun 2012	Jul 2012	Aug 2012	Sep 2012	Oct 2012	Nov 2012	Dec 2012	Jan 2013	Feb 2013	Mar 2013	Apr 2013	May 2013	Jun 2013*	Jul 2013*
ALL COMMODITIES	100.00	7.58	7.52	8.01	8.07	7.32	7.24	7.31	7.31	7.28	5.65	4.77	4.58	4.86	5.79
Primary Articles	20.12	9.75	10.54	11.23	9.22	7.81	9.56	10.56	11.41	10.54	7.36	5.06	5.72	8.14	8.99
Food Articles	14.34	10.91	10.17	9.34	8.06	6.72	8.80	10.63	12.35	11.95	8.63	6.08	8.25	9.74	11.91
Non-Food Articles	4.26	7.18	13.34	14.08	10.43	11.43	14.04	13.56	13.00	10.71	9.32	7.59	4.88	7.57	5.51
Minerals	1.52	7.58	8.65	18.12	13.87	8.63	6.88	5.57	4.03	2.79	-1.95	-4.52	-7.03	-0.52	-2.38
Fuel & Power	14.91	12.07	8.39	8.74	12.00	11.65	9.97	10.25	9.27	10.64	7.76	8.33	7.27	7.12	11.31
Manufactured Products	64.97	5.37	5.87	6.36	6.47	5.95	5.41	5.04	4.95	4.80	4.28	3.69	3.25	2.75	2.81

* Provisional

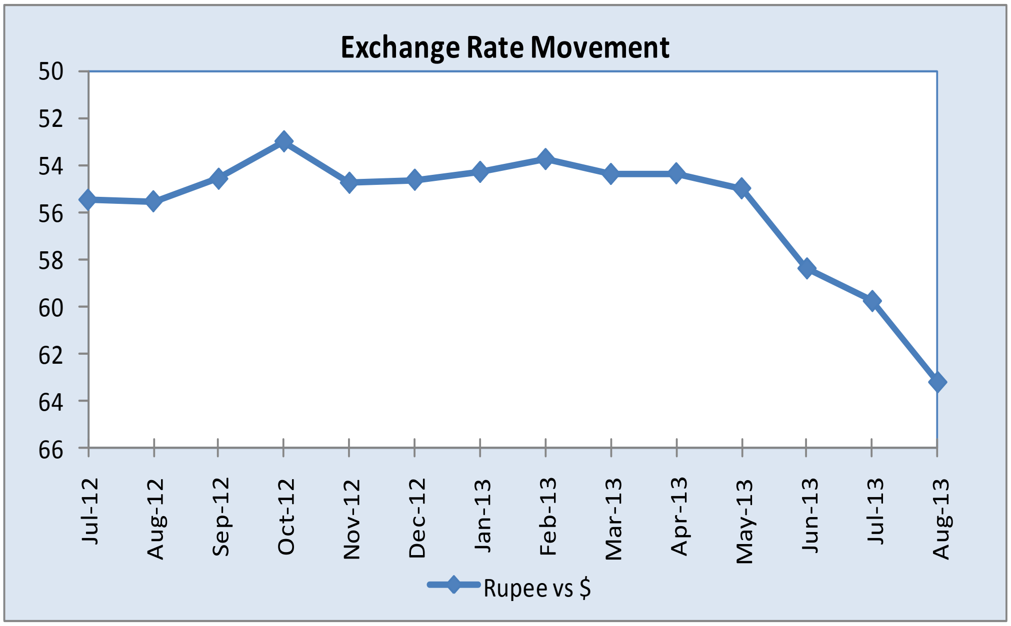
Since March 2013, the wholesale inflation was within 6.00%. The RBI steps have shown its effects as the WPI inflation was less than 5% (Comfort Zone for RBI) during three months i.e. April, May and June 2013. There has been an increase in the wholesale inflation in July 2013 to 5.79% on the back of increasing prices of food articles and fuel & power.

The inflation recorded on primary article was more than 8.00% in June 2013 as well as in July 2013, mainly driven by increasing prices of food articles. Inflation for food articles is continuously increasing over the last few months and it reached to 11.91% in July 2013, on the back of increasing prices of fruits & vegetables and cereals. Inflation for power & fuel has increased by four percentage points in July 2013 as compared to June 2013, mainly due to increased prices of mineral oils which has a weight of around 9.36% on the WPI index.

The inflation on power & fuel and manufactured articles was lower in YoY terms; for manufactured products it was around 2.81% in July 2013 in comparison to 5.87% of July 2012. The WPI inflation for manufactured products was slightly higher in July 2013 as compared to June 2013, driven by increase in the prices of textile products, leather & leather products and rubber & plastic products.

Financial Market

Currency Market



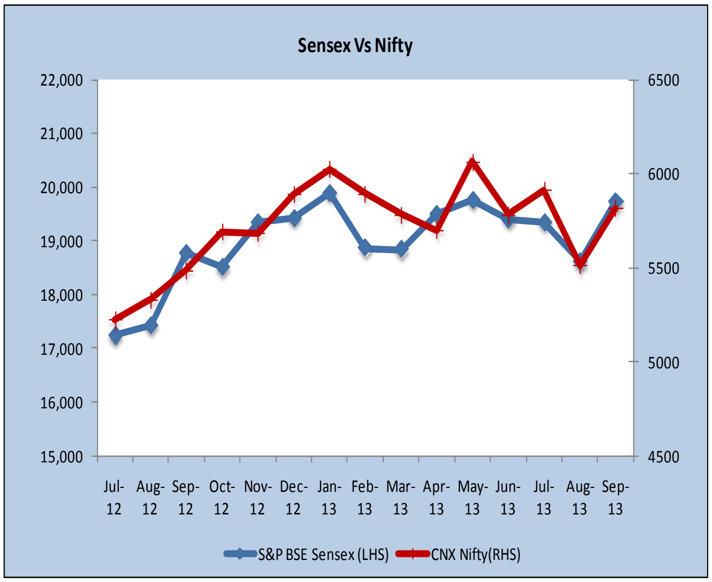
Source: RBI

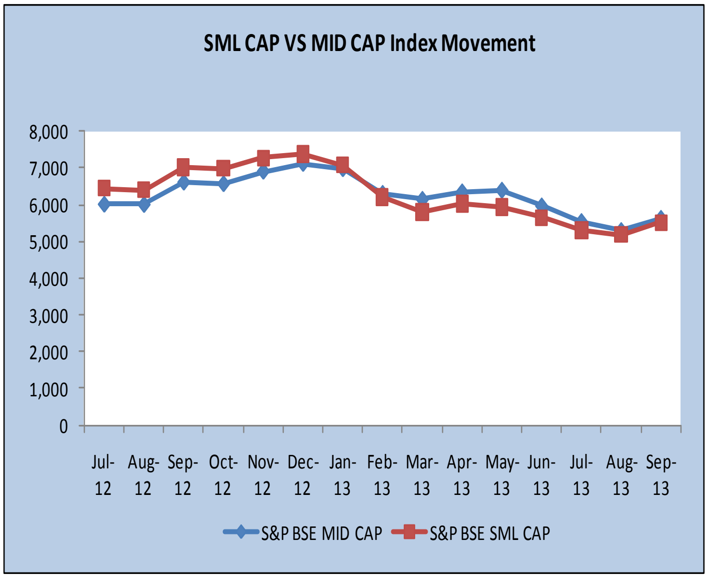
* Units on y-axis in reverse scale

The rupee leads the losers' chart among Asian currencies in the April-August by plunging 16.24%, during the period due to massive capital outflows on worries of withdrawal of the US stimulus. The fall in rupee also lead to capital erosion as foreign investors pulled out their investment. Apart from this, speculation in the currency market, rising CAD and uncertain policy regime have aggravated the situation. Rupee has reached all time low of USD 68.36 on 28th August 2013.

During the current quarter ending September 2013, the FII have been a net seller of around ` 193.10 billion on the cumulative basis for June, July and August. The government and RBI have taken various steps ranging from special swap window for oil marketing companies so that they can directly borrow dollar from RBI, increased borrowing limit for the banks, attracting NRI deposits. The rupee has started improving since 5th September 2013 (Dr. Raghuram Rajan assumed charge as RBI governor on 4th September 2013); on the hope of market friendly policy and expected delay in withdrawal of quantitative stimulus of US Federal Reserve.

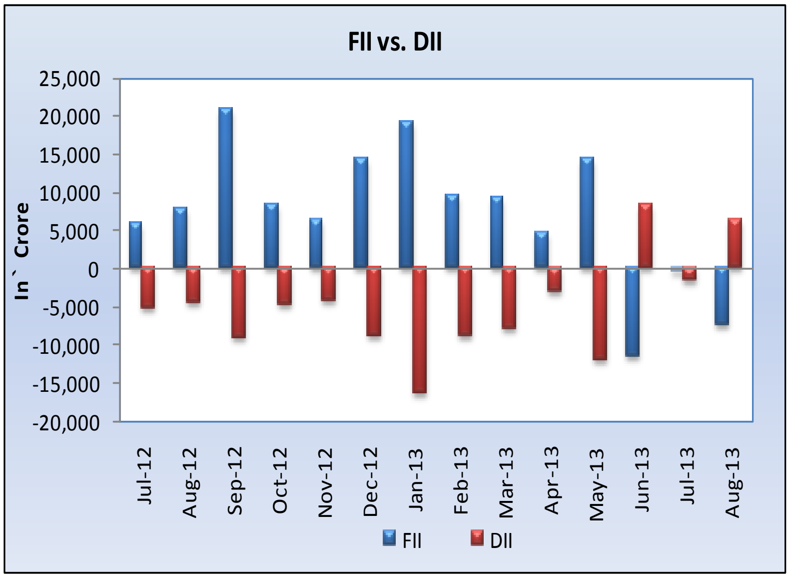
Equity Market





Source: BSE & NSE

FII vs. DII Movement



Source: SEBI

After the stability during the last two quarters of 2013, the domestic equity market has been fluctuating during the current quarter ending in September, on the back of the various news and developments in the national and international markets; like probability of withdrawal of bond buying scheme of US Federal Reserve, change of RBI governor, political uncertainty and major policy changes (such as food security bill).

If we see monthly trend in 2013, in the month of June, July and August market was affected by bearish sentiments and was trending on a lower side as compared to past few months. In the month of June the market was mainly affected by FII movement as they were the net seller of their investments of around ` 114.25 billion. In the month of July 2013, domestic investors also joined the selling spree as they tried to minimize their losses.

However in September 2013, market seems to be improving, on the back of appreciation and stability in rupee; FIIs have also shown interest in Indian equity market during the month of September, as they were the net buyers during the month of September (till Sept. 18). Mid cap and Small cap indices were also trending in the similar direction as of other main indices like Sensex and Nifty, showing an upswing in September.

Outlook

India's economic growth rate slipped to a decade low of 4.35% in Q1FY14 on account of poor performance of manufacturing and mining sectors. The past few years have seen a poor performance and the Q2FY14 is also not expected to be good on account of outflow of forex via FIIs, depreciation of rupee and a heavy import bill. High inflation has been witnessed in the Q2FY14 on oil, food and gold. Some measures have been taken in Q2FY14 such as oil prices have been deregulated more than ever before and measures have been taken to curb gold imports. There are innovative ideas such as asking the religious bodies to have their gold reserves, which are enormous by any standards, to be converted for national use.

With the new RBI governor, there is hope that some new measures shall be announced that can at least arrest the further fall in the Indian economy. With the elections round the corner in FY14, the government has also initiated some measures, some of which are expected to be pro-reforms. It is expected that the problem in mining shall be soon resolved along with the improvement in the infrastructure industry and increase in export. However, some of the other measures such as the new food bill may have an impact on the economic growth.

FOOD SECURITY ACT (FSA) – A POLICY REVIEW

Introduction

The glaring reality about India is that while India has been maintaining food-grain stock surplus at an average of 69.3 Million Tonnes (MT) as on 1st August 2013, she is ranked 15th amongst all the countries of the world on the Global Hunger Index 2011. Under-nutrition and malnutrition are a common form of depravity affecting children under 5 years and pregnant women and lactating mothers in both Urban and Rural India. To bridge this gap, United Progressive Alliance (UPA) proposed New Food Security Bill (NFSB) that was given the parliamentary nod on September 2, 2013 and the presidential acceptance on September 10, 2013. After a debate of about 9 hours, the Lok Sabha passed the NFSB, now FSA amidst a lot of questions but not much opposition.

Month'2013	January	February	March	April	May	June	July	August
Food grain Stock (MT)	66.693	66.283	62.943	59.758	77.544	77.74	73.744	69.653

Source: FCI

It is not that the country has suddenly woken up to the call of hungry millions. Earlier also, there were schemes being run and successfully so, for the needy. Provision of highly subsidized food grain, free midday meals are some of the examples of such schemes. States like Chhatisgarh, Tamil Nadu and Rajasthan have already set up some successful examples. The FSA only tries to consolidate the various schemes, bring them into one umbrella and give it a legal status. Only, it is more exigent in the sense that it proposes to increase the benefits and the coverage i.e. the number of beneficiaries. This entails pressure on the agriculture, prices of the produce and exchequer.

Salient Features of the ACT

1. 75 percent of rural and 50 percent of the urban population are entitled for three years from enactment to five kg food grains per month at ₹3, ₹2, ₹1 per kg for rice, wheat and coarse grains (millet) respectively;
2. The states are responsible for determining eligibility;
3. Pregnant women and lactating mothers are entitled to a nutritious "take home ration" of 600 calories and a maternity benefit of at least `6,000 per month for six months;
4. Children between the age of 6 months to 14 years are to receive free hot meals or "take home ration";
5. The central government will provide funds to states in case of short supplies of food grains;
6. The current food grain allocation of the states will be protected by the central government for at least six months;
7. The state governments will provide a food security allowance to the beneficiaries in case of non-supply of food grains;
8. The Public Distribution System is to be reformed;
9. The eldest woman in the household, 18 years or above, is the head of the household for the issuance of the ration card;
10. There will be state and district-level redressal mechanisms; and
11. State Food Commissions will be formed for implementation and monitoring of the provisions of the Act.

Implementation of the FSA

The bill, now an act has been controversial due to its social, political and financial impact on the economy. To facilitate the implementation of the act, state governments have been given adequate control. Consequently some states shall be implementing the same pre-elections and some have postponed the action till the next fiscal year. As a result, the effects of the act will be fully visible only by FY14-15.

Controversy around the Bill

The bill has been surrounded by controversies of various natures. On political front, the opposition parties attacked the bill for the timings of its passage due to upcoming elections. Socially, the bill has been claimed as a welfare act for covering the under nutrition and malnutrition in the country. However, it poses a big challenge on the financial front. Just before the passage of the bill, there were concerns of India's ratings to be deteriorated to a non-investment grade. Questions were raised on how is the extra costs of the food-grain to be provided under the new act, cost of warehousing, transportation is to be financed? Concerns on inflation, agriculture machinery and its producing capacity, distribution mechanism are still to be fully addressed. The money markets have given a very cold reception to the bill and further depreciation of rupee post the passage of the bill had been attributed to the same.

Impact of the FSA

Agriculture Machinery

The challenge in implementing the bill starts from the production of food grain. As per the National Advisory Council based on the population of October 2011, FSA would have required a food grain reserve of approx. 63.98 MT in FY13. Now with the increase in the population, the number of people under the coverage of the new act also goes up. Presently, the Food Corporation of India (FCI) claims to have enough reserves to meet the requirements of the act, but does not leave any stock as reserved surplus, i.e. the stock held as reserve for rainy days. Moreover, with increase in the requirements, extra stock will be needed for which our present agricultural machinery is not fully equipped. Producing extra food grain will involve:

- Increasing the per hectare output of the area under cultivation – which is not possible in the short term. A lot is dependent on the quality of seeds, monsoons, crop rotation and capital availability with the farmers. Monsoons have been benign this year but may not always be the case.
- Increasing the area under cultivation – This will come at a cost of area under cultivation of proteins (cereals and pulses) and can have an adverse impact on the production of protein crop.

Import of food grains cannot be considered as an option as India's entry into international market as an importer will exert upward pressure on the food prices as well as the current account deficit.

Inflation

As the states increase the procurement of food grains to meet the requirements under the FSA, the supply for the open market sale diminishes. This would lead to an increase in the prices of food grains in the open market. With food inflation already hovering at 18.18% for August 2013 already, this may not auger well for the economic growth and the investment climate in India.

Public Distribution Network (PDS)

The targeted public distribution system (TPDS) is hauled by lot of ailments such as leakages, inadequate availability of food grains and insufficient monitoring. Ensuring that the right person gets the intended benefit may not be easy even though the act is preceded by the successful examples of states such as Chhattisgarh, Andhra Pradesh and Rajasthan. The allocation of Unique Identity Cards (UIDs or Smart cards), adequate number of fair price shops and public awareness has been the pillars in these states. The FSA legalizes the redressal mechanism to lend strength to the Targeted Public Distribution System and to ensure effective distribution of benefits to the intended recipients. Certain steps have been proposed that can facilitate the implementation of FSA. These include bar coding food grain packets, SMS Alerts on food grain availability, automation of PDS, use of GPS etc.

Cost of Infrastructure

The present food-grain warehousing capacity in India is 78MT. With the implementation of FSA the warehousing capacity needs to be upgraded every year. This implies that there is scope for private participation. As per a Rabobank report, the construction of larger godowns require more than` 15 crore, which is better suited for larger players. However, due to the fragmentation in the grain market and the excessive government control, the private investors stay away.

Infrastructural support will be required for administrative set up, scaling up of operations, enhancement of production, storage, movement, processing and market infrastructure etc.

The Commission on Agriculture Costs and Prices (CACP) has calculated that the economic cost of FCI for acquiring, storing and distributing food grains is approx. 40 percent of the total food subsidy. Essentially this implies that for the total food subsidy of `130 bn, the administration cost shall be `52 bn.

Fiscal Deficit

According to official estimates, the food subsidy will increase from the present actual figure of `85,369 Cr to `1.3 Lakh Cr. as the number of beneficiaries increase after the FSA is implemented.

S. No.	Particulars	Unit	2012-13
A	Present Fiscal Deficit	` Cr.	4,89,890
B	Fiscal Deficit to GDP	%	5.1
C	Present Food Subsidy	` Cr.	85,369
D	New Food Subsidy	` Cr.	1,30,000
E: D-C	Extra Charge on Exchequer	` Cr.	44631
A+E	Post FSA Fiscal Deficit*	` Cr.	5,34,521
	Post FSA Fiscal Deficit to GDP	%	5.6

* Calculations are based on the assumption that no extra revenue or expenses are incurred after the FSA is introduced. Calculations ignore any increase in transportation, supply chain, storage and warehousing costs.

Conclusion

Implementing the FSA is a herculean task, but once done successfully, the benefits will accrue for generations to come. It will help to put India at a respectable place on the Global Hunger Index. Challenge lies in overcoming the inefficiencies of the TPDS and simultaneously maintaining the fiscal deficit. Ironically, the government is silent about how to implement the Act and has been quoted as '*we have to figure out the means (to implement the scheme)*'. With elections round the corner many states would like to postpone the implementation of the FSA for the next year, till such time the means to implement the bill is '*figured out*'.

INDUSTRY UPDATE

Indian Readymade Garment Industry

With the increase in the disposable income of Indian people it is expected that the garment industry will grow at double digit in the coming decade. The domestic apparel industry is expected to record a compound annual growth rate of 9% over 2011-21. The recent change in the government policies has fuelled the growth of the garment industry. Some of the major initiatives taken by the government are 100% FDI, de-reservation of readymade garment, hosiery and knit wear from the SSI sector, relaxation in export duties and several other effective measures have been taken by the government of India in recent past. Due to abolition of 12% excise duty by GOI the Indian garment industry is expecting a growth of 12-15% in the coming days. This initiative was taken because of negligible growth in the industry from 2011-13.

The readymade garment industry in India is the second largest industry trailing agriculture. It contributes to approximately 14% of Indian Industrial Production (IIP) and is one of the largest contributing sectors of India's exports worldwide and contributes to 4% of India's GDP. The largest segment for the readymade garment includes the age group of 16-35 years old people who are very brand conscious and gives priority to high quality products due to which the preference of the consumer have changed from need base to experienced base. Branded readymade garment accounts for over 21% of the garment industry.

Export of garment products from India has increased steadily over the last few years particularly after 2004, when textile export quota was discontinued. Export of readymade garment depicted a robust 24.8% growth in FY12 to reach `62,630 Cr. against 5.4% growth in FY11. However, India's position in global arena is on a shaky platform as it is facing tough competition from its neighboring countries such as China and Bangladesh. The technology of China and labor in Bangladesh are the major concerns for Indian manufacturers.

Marking the recent trends, liberalized economic policies and change in FDI norms, the SMEs sector is participating more and more to the total production. Due to low entry level barriers many SME are trying their fortune in the garment industry. In this endeavor the government is supporting them by providing subsidy to establish and run the unit. However, a lot has to be done in context of infrastructure, developed logistics, easy availability of funds for SME, research & development and imparting training to workforce.

ONICRA RATED ENTITIES

PROFILE OF ONICRA RATED MSMEs (For the Period – 1st July 2013 to 30th September 2013)

Geographical Distribution of Ratings

State	Percentage Wise
Andhra Pradesh	9.51
Arunachal Pradesh	0.00
Assam	5.31
Bihar	2.51
Chandigarh	0.00
Chhattisgarh	0.99
Delhi	2.16
Gujarat	4.67
Haryana	1.11
Himachal Pradesh	0.41
Jharkhand	0.58
Karnataka	9.39
Kerala	0.23
Madhya Pradesh	5.19
Maharashtra	7.00
Manipur	0.00
Meghalaya	1.05
Nagaland	0.00
Orissa	1.87
Punjab	3.33
Rajasthan	5.95
Tamil Nadu	9.04
Tripura	0.00
Uttar Pradesh	15.05
Uttarakhand	1.52
West Bengal	13.13
Total	**100.00**

Onicra- Rated MSME: Industry Wise Distributions

Industry	Number of Cases	Percentage Wise
Agriculture & Allied Products	124	7.23
Auto & Auto Components	30	1.75
Chemicals	43	2.51
Construction & Engineering	88	5.13
Construction-Materials	80	4.67
Consumer Durables	49	2.86
Containers & Packaging	61	3.56
Educational Services	29	1.69
Electrical Components & Equipments	81	4.73
Food Products	97	5.66
Health Care	21	1.23
Hospitality	20	1.17
Household & Personal Products	21	1.23
Information Technology & Telecommunications	15	0.88
Iron and Steel	73	4.26
Jewellery	15	0.88
Machinery and Equipments	162	9.45
Media & Printing	35	2.04
Metal and Metal Products	44	2.57
Paper & Forest Products	35	2.04
Pharmaceuticals	33	1.93
Plastic & Plastic Products	46	2.68
Power & Energy	21	1.23
Retailing	81	4.73
Services	82	4.78
Textile	157	9.16
Transportation	7	0.41
Others	164	9.57
Total	**1714**	**100.00**

NSIC-ONICRA Rating Definition

NSIC-Onicra Rating reflects Onicra's opinion on the company's performance capability and financial strength. Ratings are assigned on the scale given below.

Performance Capability	Financial Strength		
	High	Moderate	Low
Highest	SE1A	SE1B	SE1C
High	SE2A	SE2B	SE2C
Moderate	SE3A	SE3B	SE3C
Weak	SE4A	SE4B	SE4C
Poor	SE5A	SE5B	SE5C

Rating Distribution: Onicra Rating

The benefit of getting a SME unit credit rating goes beyond procuring finance at competitive rates. While drawing business from a client located in dispersed geographies or from large corporate and multinationals, the rating exercise also serves as an independent due diligence activity. Further, since Onicra examines the aspects of the SME units, management highlights the shortcoming and areas which requires further improvement. All these benefits create confidence in the client and that has enabled ONICRA to achieve significant growth in the numbers of rating done.

Quarterly Rating Distribution

Rating	Q3FY13 (%)	Q4FY13 (%)	Q1FY14 (%)	Q2FY14 (%)
SE 1A	0.12	0.43	0.43	0.35
SE 1B	0.67	1.05	0.66	0.82
SE 1C	0.55	0.43	0.38	1.11
SE 2A	9.37	10.05	2.75	3.97
SE 2B	31.41	32.38	19.51	17.91
SE 2C	18.98	14.02	16.24	20.48
SE 3A	14.57	15.54	4.02	3.97
SE 3B	18.31	20.31	29.92	26.25
SE 3C	5.57	5.49	19.37	15.05
SE 4A	0.00	0.00	0.09	0.41
SE 4B	0.43	0.30	4.50	7.70
SE 4C	0.00	0.00	2.13	1.98
Total	**100.00**	**100.00**	**100.00**	**100.00**

Quarterly Geographical Distribution

State	Q3FY13 (%)	Q4FY13 (%)	Q1FY14 (%)	Q2FY14 (%)
Andhra Pradesh	6.92	6.43	8.81	9.51
Arunachal Pradesh	0.43	0.00	0.09	0.00
Assam	4.35	5.64	5.82	5.31
Bihar	4.23	2.28	3.88	2.51
Chandigarh	0.00	0.58	0.14	0.00
Chhattisgarh	1.78	1.73	1.33	0.99
Daman	0.00	0.00	0.00	0.00
Delhi	4.65	2.06	1.94	2.16
Goa	0.18	0.00	0.00	0.00
Gujarat	4.53	4.26	3.41	4.67
Haryana	2.33	3.18	2.13	1.11
Himachal Pradesh	0.92	0.14	0.19	0.41
Jammu & Kashmir	0.12	0.07	0.00	0.00
Jharkhand	2.33	0.61	0.71	0.58
Karnataka	7.90	8.75	8.57	9.39
Kerala	0.55	0.14	0.00	0.23
Madhya Pradesh	5.76	5.78	4.07	5.19
Maharashtra	7.96	6.18	4.69	7.00
Manipur	0.00	0.00	0.09	0.00
Meghalaya	0.49	0.43	0.38	1.05
Mizoram	0.00	0.00	0.00	0.00
Nagaland	0.00	0.00	0.24	0.00
Orissa	1.71	1.23	2.32	1.87
Punjab	3.00	2.57	3.65	3.33
Rajasthan	4.65	3.14	3.93	5.95
Tamil Nadu	10.41	14.96	12.74	9.04
Tripura	0.00	0.00	0.14	0.00
Uttar Pradesh	15.86	18.54	17.76	15.05
Uttarakhand	1.22	2.49	2.04	1.52
West Bengal	7.72	8.78	10.93	13.13
Pondicherry	0.00	0.00	0.00	0.00
Total	**100.00**	**100.00**	**100.00**	**100.00**

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