CareEdge RATINGS

FORESIGHTS

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Lower Profitability Weighs on Corporate Performance in Q2 FY23

The financial performance of the corporates in Q2 FY23 was a mixed bag. While aggregate net sales grew in double digits, profitability suffered due to higher expenditure. Aggregate operating profits contracted for the first time in the past nine quarters as companies were not able to pass on the increased cost to their final consumers. While sectors such as automobiles, telecom, IT and logistics put up a good show, oil & gas, metals and cement dragged the overall corporate performance during the quarter.

Q2 GDP: Services Power Growth, Manufacturing Falters

Container Rail Volumes to Surge at 16% CAGR by FY25

Retail Asset Securitisation: FY23 volumes likely to cross ₹1.6 L Cr.

FOREWORD

SACHIN GUPTA

Chief Rating Officer
& Executive Director

The cover story for this month's edition talks about the impact on profitability in the last quarter. This was on the expected lines, and I had, in fact, also mentioned it in my earlier columns. The good thing however is that the global commodity price surge that had impacted profitability now seems to be abating. Crude oil at around USD 80, is about 20% lower than last quarter; similarly, other core commodities like steel and other metals are trending lower. The interest costs however are likely to remain high for the foreseeable future and that will have a moderating impact on profitability.

The other story in the current edition is on GDP. The annual growth of 6.3% for the second quarter was broadly on expected lines. It was driven by Services and Discretionary spending. We expect the growth to pick up from here on and end the full year at 6.9%. The key monitorable will be a further pick up in the domestic demand scenario, as the external sector would remain challenging.

Retail credit is seeing robust growth driven on one hand by the demand but more importantly by the confident lending by NBFCs and Banks. For many quarters most of the lenders were focussing on collections rather than disbursements.

Now, we see first time post-pandemic that lenders are confidently disbursing funds reflecting that collection issues relating to the pandemic are no longer troubling. In line with this, we are also seeing a sharp increase in the securitization of retail assets. As detailed in a story in this edition, we saw a 66% growth in the securitization volumes in H1 FY23.

As we end the calendar year, there are three trends for 2023 that are likely.

Firstly, the interest rates look to be plateauing with another 25-basis point hike likely in the policy rates. But they are unlikely to come off this high in the next year, meaning that corporates and individuals should get used to higher interest rates.

Secondly, the government will continue its focus on capex and infrastructure, supported by buoyant GDP, strong tax collections and not too bad a fiscal deficit position. This, along with the government's push on domestic manufacturing should drive the GDP growth.

Thirdly, and this is more of a hope, the private capex will finally kickstart, as the capacity utilization across the industry moves beyond 70-75%. The businesses are looking for signals that the demand growth is steady and not only a mere post-pandemic rush. We believe that we are about to turn that corner and that will give confidence to the business owners to invest in capacity expansion.

Overall, 2022 has been a very dramatic turnaround year and 2023 looks to be a brighter spot with the Covid-19 shadow completely behind us. However, the global headwinds will have to be closely monitored.

NOTE FROM
RAJANI SINHA
Chief Economist

RBI moderates rate hike, but remains cautious

RBI has moderated the pace of policy rate hike to 35 bps in December, taking cue from expected moderation in CPI inflation (supported by base effect) and easing of global commodity prices. Expectations of US Federal Reserve going slow with Fed fund rate hike and consequently lesser weakening pressure on Rupee also provided RBI the scope for moderation. However, the important aspect to note is that RBI has emphasized on the need to "**keep inflationary expectations anchored, break core inflation and contain the second-round effects**" of inflation.

Core inflation has remained sticky around 6% for the last one year or so. While supply related inflationary pressures are quick to reverse as the bottlenecks are eased, core inflation becomes difficult to reverse as it gets entrenched in the system. Moreover, food inflation in the economy is still high at around 7%, with high cereal inflation at 12%. This runs the risk of putting further upward pressure on inflationary expectations. As per the latest data, while household inflationary expectations have eased marginally, it is still at a high of 9.8%. With global uncertainties looming high and domestic inflationary concerns persisting, the RBI would remain vigilant on inflation front. It is important to note that while CPI inflation is likely to move below 6% by the end of FY23, it will be a challenge for the Central Bank to achieve the 4% target (mid of the 2-6% band) even in FY24.

With external headwinds accentuating, RBI has lowered the GDP growth projection for FY23 to 6.8%. While there is no denying that India is a bright spot currently in midst of the global turmoil, it cannot remain unscathed from the global slowdown. India's exports have contracted by 17% in October 2022, with widening of net exports being a critical factor shaving off from India's GDP in the first two quarters of FY23. Domestic demand indicators are showing resilience, with bounce back in sectors like travel, tourism and hospitality supported by pent up demand. Other high frequency indicators like GST collection, PMI (Manufacturing and Services), passenger vehicles sales, bank credit offtake are also indicating healthy domestic demand recovery. However, external demand is likely to weaken further, and domestic demand could also see some moderation as pent-up demand fizzles out and financing conditions tighten. As per the minutes of the September MPC meeting, some of the MPC members were concerned about rate hikes overshooting the requirement and hence denting growth. Even in the December meeting, there is divergence in views among the MPC members, with five out of six members voting in favour of a rate hike, while the decision to maintain stance at 'focus on withdrawal of accommodation' was supported by only four MPC members.

Going forward, the Central Bank will not just be watching the domestic data but will also be closely monitoring global developments like US Fed rate decisions, movement of global commodity prices and global currency movements. The RBI would also like to evaluate the impact of policy rate hikes so far. The transmission in lending rate is varied across sectors, with more complete transmission in the loans linked to EBLR (External Benchmark Lending Rate). However, the WADTDR (weighted average domestic term deposit rate) on outstanding deposit has increased by only 46 bps in the fiscal year so far in contrast to 225 bps rate hike in the repo rate (including the latest hike). With surplus liquidity in the system reducing and bank credit-deposit ratio increasing, the transmission through higher deposit rate is likely to pick up. This would improve effectiveness of the monetary policy tightening so far. With policy rate moving in the positive territory, RBI would be very cautious of further rate hikes. However, given the global uncertainties and persisting inflationary concerns, there are chances of another 25 bps rate hike in the February meeting, taking the terminal repo rate to 6.5%.

The above views were also published in Economic Times, issue dated December 8, 2022.

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COVER STORY

Lower Profitability Weighs on Corporate Performance in Q2 FY23

The financial performance of the corporates in Q2 FY23 has been a mixed bag. While aggregate net sales recorded double-digit growth, profitability remained under pressure due to higher expenditure. As a consequence, aggregate operating profit was adversely impacted and saw a contraction for the first time in the last nine quarters. While sectors such as automobiles, telecom, IT and logistics put up a good show, sectors such as oil & gas, metals and cement dragged the overall corporate performance during the quarter. Further, the debt servicing capability of corporates fell to a multi-quarter low in Q2 due to rising borrowing costs and lower profitability.

Aggregate Analysis - Q2 FY23

Net sales in the second quarter grew at 26% (y-o-y), moderating from 44% growth in the previous quarter. The higher growth in Q1 FY23 was supported by a low base. On a sequential basis, net sales were almost flat at the previous quarters' level. Operating profit was hit during the second quarter as it contracted both on a sequential and annual basis. The contraction of about 7% (y-o-y) in Q2 FY23 has come after a gap of nine quarters.

The total expenditure of companies has shown a rising trend since Q2 FY22, though the pace of increase has moderated significantly in the second quarter. The total expenditure in Q2 FY23 was still 32.5% higher compared to the level a year ago. Both raw material and labour costs posted a double-digit growth adding to the expenses of companies. On a sequential basis, there was only a marginal fall in the raw materials costs as many companies had raw material inventory bought at higher prices.

Quarterly Corporate Performance

Particulars	**Unit**	**Q2 FY22**	**Q1 FY23**	**Q2 FY23**
Net Sales	₹ Lakh Cr	23.3	29.6	29.4
	% y-o-y	31.5	43.9	25.9
Expenditure	₹ Lakh Cr	19.7	25.9	26.1
	% y-o-y	33.2	50.4	32.5
Cost of Services and Raw Materials	₹ Lakh Cr	7.8	11.6	11.2
	% y-o-y	47.2	68.2	42.2
Employee Cost	₹ Lakh Cr	1.8	2.0	2.1
	% y-o-y	13.9	13.0	13.8
Operating Profit	₹ Lakh Cr	4.1	4.2	3.8
	% y-o-y	20.3	10.8	-7.4
Profit After Tax	₹ Lakh Cr	1.9	1.7	1.4
	% y-o-y	57.0	11.6	-26.2
Ratios		**Q2 FY22**	**Q1 FY23**	**Q2 FY23**
Operating Profit Margin	%	17.7	14.2	13.0
Interest Coverage Ratio (ICR)	-	6.3	5.8	4.9

Source: Ace Equity; CareEdge; Note: Based on analysis of 2,034 non-finance listed companies

Higher expenditure by the corporates during the quarter has weighed on the profit margin of the firms. The operating profit margin in Q2 FY23 declined to a low of 13% from 14.2% in the previous quarter and 17.7% a year ago. Interest costs in Q2 FY23 have seen a notable jump of 17.5% (y-o-y) and are at the highest level since Q4 FY20. After a pause of nearly two years, the Reserve Bank of India hiked the policy repo rate in May 2022. Till September, there has been a 190 basis points hike in the policy repo rate. This has resulted in a rise in domestic lending rates as well, leading to higher borrowing costs for the corporates. Consequently, the interest coverage ratio (ICR) has fallen to an eight-quarter low of 4.9 in Q2 FY23.

Sectoral Analysis - Q2 FY23

We have looked closely at 21 select sectors to get a sense of their performance in the second quarter. These sectors accounted for nearly 84% of the total turnover in Q2 FY23. Our analysis showed that there was a broad-based growth in net sales across the sectors. Sectors such as hospitality, aviation, retailing, oil & gas and automobiles have posted strong growth in their sales. However, the impact of slowing external demand was visible in sectors such as textile and iron & steel which grew at a much slower pace.

The y-o-y contraction in operating profit during the quarter has been led by sectors like oil & gas, iron & steel, non-ferrous metals, cement and textile. The profitability of oil companies was impacted in the second quarter due to the imposition of windfall taxes on crude oil production. Iron & steel and non-ferrous metals sectors have seen decline in operating profits in Q2 due to lower realisations owing to easing global metal prices, high input costs and imposition of export duty on iron & steel products. The global economic slowdown was another pain point which could have impacted the volume numbers. Both these sectors have also witnessed a significant decline in their operating profit margins as well, compared with the previous quarter and the quarter a year ago.

The sectors which have seen an improvement in their operating profit on both sequential as well as y-o-y basis are automobile & ancillaries, capital goods, infrastructure, telecom, IT and logistics.

The debt servicing capacity at the aggregate level has gone down in the second quarter. The decline is more for sectors (oil & gas, iron & steel and non-ferrous metals) whose profitability has been severely impacted during the quarter.

Growth in Net Sales (% y-o-y)

0 to 10	10 to 20	Above 20
Iron & Steel	FMCG	Hospitality
Pharmaceuticals & Drugs	Non - Ferrous Metals	Aviation
Textile	Capital Goods	Retailing
	Telecom	Oil & Gas
	Infrastructure	Automobile & Ancillaries
	White Goods	Power
	Cement & Construction Materials	Chemicals
	Realty	Logistics
		IT
		Media & Entertainment

Source: Ace Equity and CareEdge
Note: Sectors are presented in descending order of growth

Growth in Operating Profit (% y-o-y)

Less than 0	0 to 20	Above 20
Aviation	Logistics	Hospitality
White Goods	Capital Goods	Retailing
Pharmaceuticals & Drugs	Realty	Automobile & Ancillaries
Media & Entertainment	Power	Chemicals
Non - Ferrous Metals	Telecom	
Textile	FMCG	
Oil & Gas	IT	
Cement & Construction Materials	Infrastructure	
Iron & Steel		

Source: Ace Equity and CareEdge
Note: Sectors are presented in descending order of growth

Way Forward

While the easing of commodity prices has been beneficial for corporates, it has also resulted in lower realisations for some sectors. Moreover, some of the raw material prices are still high compared to a year ago level. A combination of these factors has weighed on the corporates' performance in the second quarter despite a healthy growth in net sales. The performance of these corporates in the coming quarters will depend to a large extent on the unfolding of demand conditions. A fall in global commodity prices is likely to get reflected in lower raw material prices in the coming quarters. This should help support their profitability provided the domestic demand growth is sustained. Lower external demand will continue to hamper the performance of export-dependent sectors.

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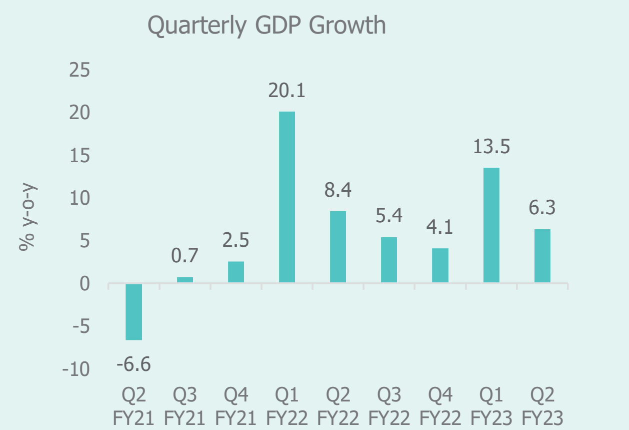
GDP Q2 FY23: Services Power Growth, Manufacturing Falters

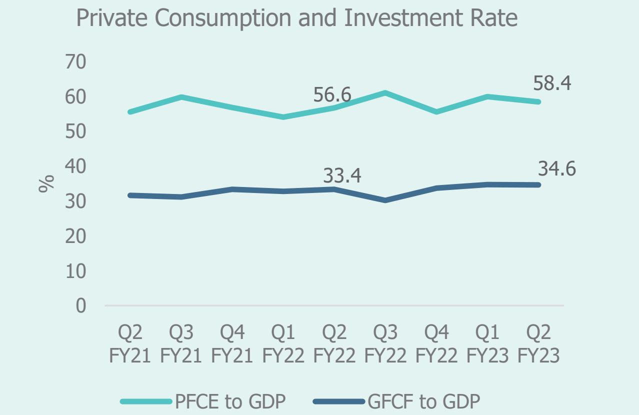
Economy grew by 6.3% in the second quarter of FY23 following a double-digit growth of 13.5% in the first quarter of this fiscal. The slowdown in growth compared with the first quarter was on account of the normalisation of the base and a contraction in the manufacturing sector's output. However, both sequential improvement and good growth over the pre-pandemic level (Q2 FY20) signal the economy's resilience despite global growth and financial uncertainties. The GDP growth in Q2 was only marginally higher than our expectation (6.2%) mainly because of higher-than-expected growth in trade, hotels, transport and communication-related sectors.

On a sequential basis, domestic economic output expanded by 3.6% reversing the contraction seen in the previous quarter with services gaining momentum. When compared with the pre-pandemic period, GDP has recorded a growth of 7.6% with a broad-based recovery across sectors. Increasing discretionary spending and higher mobility have boded well for the services sector. The industrial sector's performance was led down by the manufacturing sector which contracted by 4.3% (y-o-y).

Both private consumption and investment rate edged up in Q2 FY23 compared with the corresponding quarter of previous year supported by higher economic activity. However, the global growth slowdown has weighed on the net exports.



Source: MOSPI



Source: MOSPI

Sectoral Contribution

Agriculture sector grew at a pace of 4.6% in Q2 FY23 compared with a growth of 3.2% in the corresponding quarter a year ago. As per the first advance estimate (AE) of foodgrains production of kharif output (released in September) for 2022-23, total foodgrains output is estimated to be lower by 4% primarily due to lower rice production. This could have implications on the agriculture sector's output growth in the coming quarters.

Industrial output contracted by 0.8% in Q2 FY23 on y-o-y basis compared with a growth of 7% a year ago. This was mainly because of the poor performance by the manufacturing sector which has been marred by high input costs. We can expect the sector to fare well in coming quarters due to festive -push and easing of commodity prices.

Services sector, having the highest share in GDP, recorded a growth of 9.3% in Q2 FY23 owing to the revival of contact-intensive sectors. The output in the sectors related to trade, hotels, transport, communication and broadcasting witnessed a double-digit growth of 14.7% benefitting from the pent-up demand. However, compared to the pre-pandemic period, these sectors were only marginally better.

Sectoral Growth (% y-o-y)

	Q2 FY22	Q3 FY22	Q4 FY22	Q1 FY23	Q2 FY23
Agriculture, Forestry & Fishing	**3.2**	**2.5**	**4.1**	**4.5**	**4.6**
Industry	**7.0**	**0.3**	**1.3**	**8.6**	**-0.8**
Mining & Quarrying	14.5	9.2	6.7	6.5	-2.8
Manufacturing	5.6	0.3	-0.2	4.8	-4.3
Electricity, Gas, Water Supply & Other Utility Services	8.5	3.7	4.5	14.7	5.6
Construction	8.1	-2.8	2.0	16.8	6.6
Services	**10.2**	**8.1**	**5.5**	**17.6**	**9.3**
Trade, Hotels, Transport, Communication & Broadcasting	9.6	6.3	5.3	25.7	14.7
Financial, Real Estate & Professional Services	6.1	4.2	4.3	9.2	7.2
Public Administration, Defence and Other Services	19.4	16.7	7.7	26.3	6.5
GVA (at basic price)	**8.3**	**4.7**	**3.9**	**12.7**	**5.6**

Source: MOSPI

Consumption and Investments

The share of private consumption in GDP increased to 58.4% in Q2 FY23 from 56.6% in Q2 FY22. Most of the gain in consumption has come from the urban demand with indicators such as GST collections, retail credit, PV sales and petroleum consumption posting double-digit growth in Q2 FY23. Rural demand struggled to catch pace as two-three wheeler and tractor sales grew at a relatively muted pace whereas, production of consumer non-durables (measured by IIP) contracted by 6.5% in Q2. While private consumption has recorded a growth of 9.7% (y-o-y) in Q2, government consumption contacted on both an annual and sequential basis.

The investment to GDP ratio increased to 34.6% Q2 FY23 from 33.4% in Q2 FY22 owing to strong capital expenditure push by the government. Investment GDP has also recorded a strong jump of around 20% when compared to the pre-COVID period (Q2 FY20).

A sharp weakening of net exports in Q2 compared with a year ago level has also weighed on overall GDP growth. With fears of a global growth slowdown and weaker currency, the decline in net exports will remain a cause of concern.

Growth in Consumption and Investment (% y-o-y)

	Q2 FY22	Q3 FY22	Q4 FY22	Q1 FY23	Q2 FY23
Government Final Consumption Growth	8.9	3.0	4.8	1.3	-4.4
Private Final Consumption Growth	10.5	7.4	1.8	25.9	9.7
Gross Fixed Capital Formation	14.6	2.1	5.1	20.1	10.4
GDP (at constant prices)	8.4	5.4	4.1	13.5	6.3

Source: MOSPI

Way Forward

Going forward, the most critical aspect would be a further pick-up in the domestic demand scenario as the external environment would remain challenging. The pick-up in the private capex cycle would be contingent on continued improvement in the domestic demand scenario. The fall in global commodity prices should provide comfort to the manufacturing sector in the coming quarters. Services sector will continue to gain from rising discretionary demand and the festive season push. We expect GDP to grow at 6.9% for the full fiscal year.

Container Rail Volumes Set To Surge at 16% CAGR by FY25

Container cargo transported through railways grew by a healthy year-over-year rate of 17.63% to 74.38 million metric tonne (MMT) during FY22 as compared to 12.51% growth in overall container cargo volumes. The rail co-efficient also expanded by 115 bps to 26.70% during FY22, mainly supported by partial connectivity of the dedicated freight corridor (DFC) with Mundra and Pipavav ports on the western coast. This marks the beginning of the modal shift from roads to rail. Slated completion of the prestigious DFC project by June 2023, a growing movement of cost-effective double-stack container trains and incremental volumes of cement cargo through railways are prominent factors for the switch from roads to rail.

CareEdge Ratings believes that transit assurance under DFC with a reduction in transit period by 40-50% for some of the routes shall accelerate this transition. Based on estimates, inventory carrying cost constitutes 43% of the overall cost of logistics. Thus, a significant reduction in transit duration is expected to help in achieving Just-In-Time based inventory management thereby boosting the cost competitiveness of domestic goods. Nevertheless, establishing end-to-end connectivity through the electrification of feeder routes, container freight terminal and warehousing capacities are crucial for achieving the envisaged modal shift.

Modal shift expected in some of the bulk cargo categories

Indian railway's freight is dominated by a few bulk commodities like coal, fertilizers, iron-ore and other raw material for steel. The government of India allowed transportation of bulk cement through containers in FY22, which shall boost rail volume growth for containers and could add incremental annual volumes of 10-12 MMT by FY25. Thus, rail volumes are expected to be buoyant due to DFC benefits and cargo diversification in container volumes.

CareEdge Ratings estimates container rail volumes to grow at a healthy compounded annual growth rate (CAGR) of 15.60% for FY2022 to FY2025 with the steady improvement of rail-coefficient to 31% and incremental volumes from cement.

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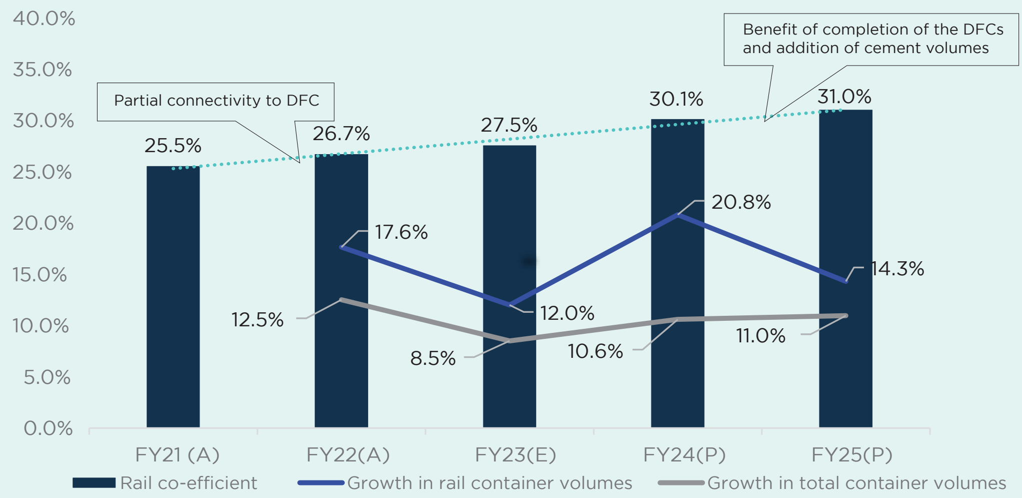


Higher land lease payment to Railways is one of the hurdles for the rail logistics segment. However, in September 2022, the Union cabinet approved a reduction in the railway land lease fee from 6% of the market rate of land per acre to 1.5%. The lease period has also been extended from the prevailing period of five years to 35 years. The new railways land lease policy is also a positive catalyst for privatising the rail logistics sector and developing 300 cargo terminals (in line with PM Gati Shakti framework).

National Logistics Policy (NLP) aims to bring down the logistics cost of India to less than 10% of Gross Domestic Product (GDP), in line with other developed countries from the existing level of 14%. The development of the Unified Logistics Interface Platform (ULIP) allows data exchange among stakeholders, which will improve work efficiency in the logistics sector by providing real-time information to all stakeholders and thus strengthen India's international competitiveness.

The haulage rates are periodically notified by the Indian Railways and the charges paid by container train operators form 65-75% of their total operating expenses. As per a World Bank report, while ~60% of the capacity of the rail network is deployed for passenger transport, the segment contributes only ~30% to Indian Railway's freight revenue. This translates into extensive cross-subsidisation of passenger fares with freight fares reducing the competitiveness of rail freight over roads.

CareEdge Ratings opines the need for an independent regulator in railways from three key perspectives: (i) rationalising the freight tariff by determining the optimum level of cross-subsidisation of the passenger segment with the freight segment (ii) facilitating private participation by ensuring the protection of their interests, and (iii) transparent dispute resolution mechanism.

Outlook

The rail co-efficient expanded by 115 bps to 26.70% during FY22, mainly supported by partial connectivity of the DFC with Mundra and Pipavav ports on the western coast.

Rajashree Murkute, Senior Director, CareEdge, said, "Container rail volumes are likely to grow at a healthy CAGR of 15.60% for FY2022 to FY2025 with a steady improvement of rail-coefficient by 430 bps to 31% and incremental freight volumes primarily cement. The transit assurance under DFC aiming to squeeze the travel period by 40-50% for some of the major routes and over 3x growth in the movement of cost-effective double stacker container trains by FY25 shall accelerate this transition. Prevailing high haulage rates for operating container trains due to extensive cross-subsidization with passenger freight, challenges in establishing end-to-end connectivity and the absence of regulator in Railways unlike other key infrastructure segments are impeding the modal shift of cargo from roads to rail."

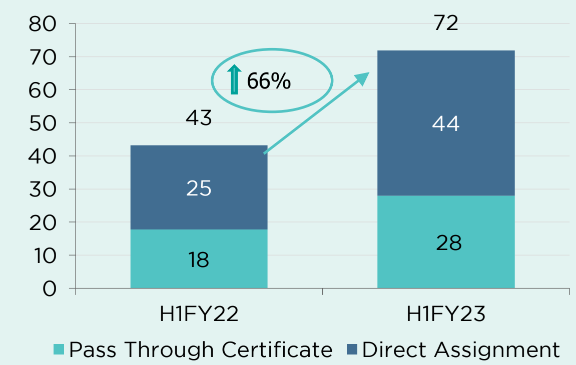
Retail Asset Securitisation: FY23 Volumes to Cross ₹1.6 lakh crore

The retail asset securitisation market in India has bounced back from lows seen during the pandemic-led credit slowdown and risk aversion. The market has registered a growth of 66% in H1FY23 compared to the same period last year.

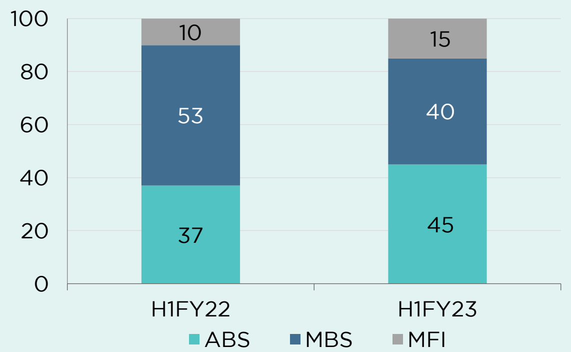
"The rated securitisation market has shown resilience in terms of rating stability and is attracting new investors to the market. We expect the market to continue this momentum and see yearly volumes in excess of ₹1.6 lakh crore aided by relatively stable domestic macros amidst global uncertainty around growth and inflation while global rates are inching up," said Vineet Jain, Senior Director, CareEdge Ratings.

The securitisation market showed no signs of stopping with overall volume growth continuing into Q2FY23. The overall H1FY23 market volume grew by 66%. The securitisation market kept up the momentum gained in Q1FY23, with the overall volume of around ₹39,000 crore (CareEdge estimate) in the second quarter of the fiscal (39% growth over Q2FY22). Direct assignment (DA) transactions accounted for the bulk of the volume at ₹16,500 crore with securitisation (pass-through certificate [PTC]) transactions making up the rest.

Securitisation Volumes (Rs. Thousand Cr)



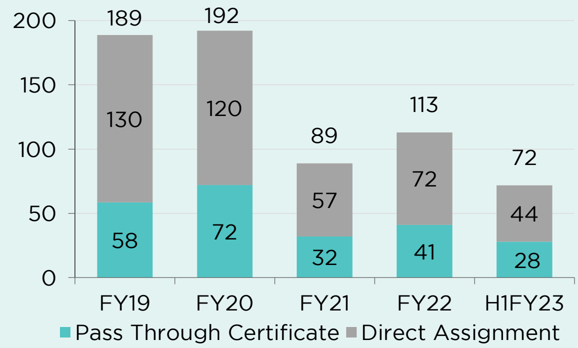
Quarterly Asset Class wise breakup (in %)



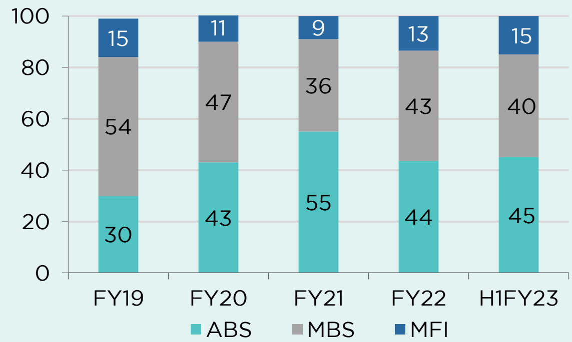
Source: CareEdge

Retail Securitisation Volumes and Asset Class-wise Breakup

Securitisation Volumes (₹ Thousand Cr)



Retail Asset Class wise breakup (in %)



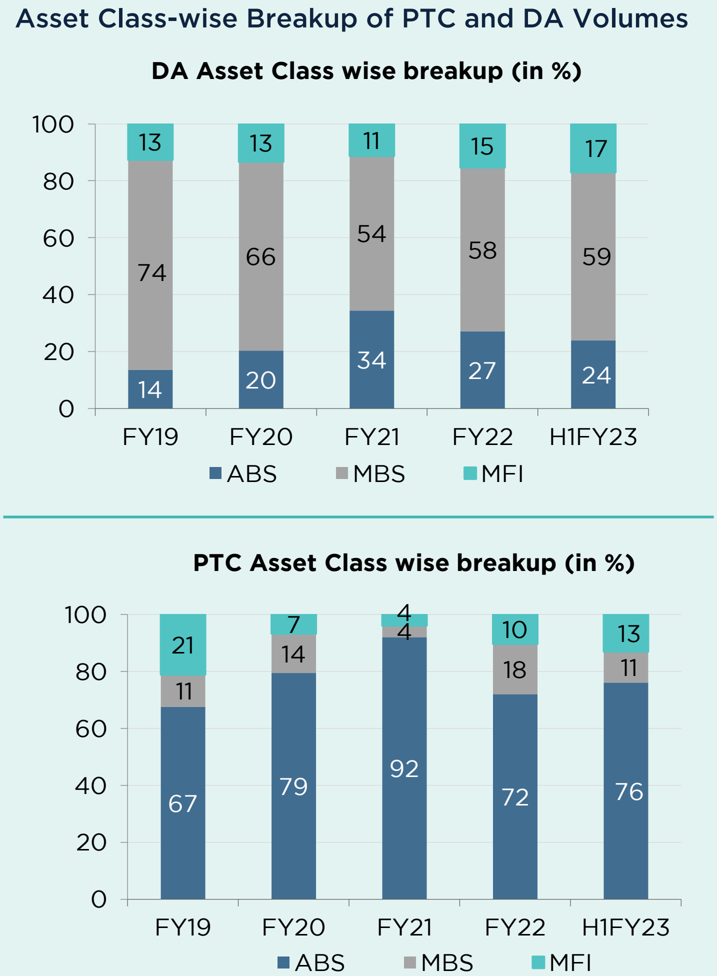
Source: CareEdge

Asset Class-wise Break-up

DA transactions continued to dominate the retail securitisation market volume with a share of 61% of the overall volume in H1FY23.

Mortgage-backed securitisation (MBS) transactions constituted around 59% of the DA volume, while asset-backed securitisation (ABS) transactions at around ₹10,800 crore, which includes pools backed by all the asset classes (except mortgage loans and microfinance [MFI] loans). MFI loans made up around 17% of the DA volume.

PTC volume was mainly driven by ABS pools contributing around 76% of the total issuances. Vehicle loan financing continued to be the main asset class driving PTC issuances at around ₹16,400 crore accounting for around 59%.



Source: CareEdge

Outlook

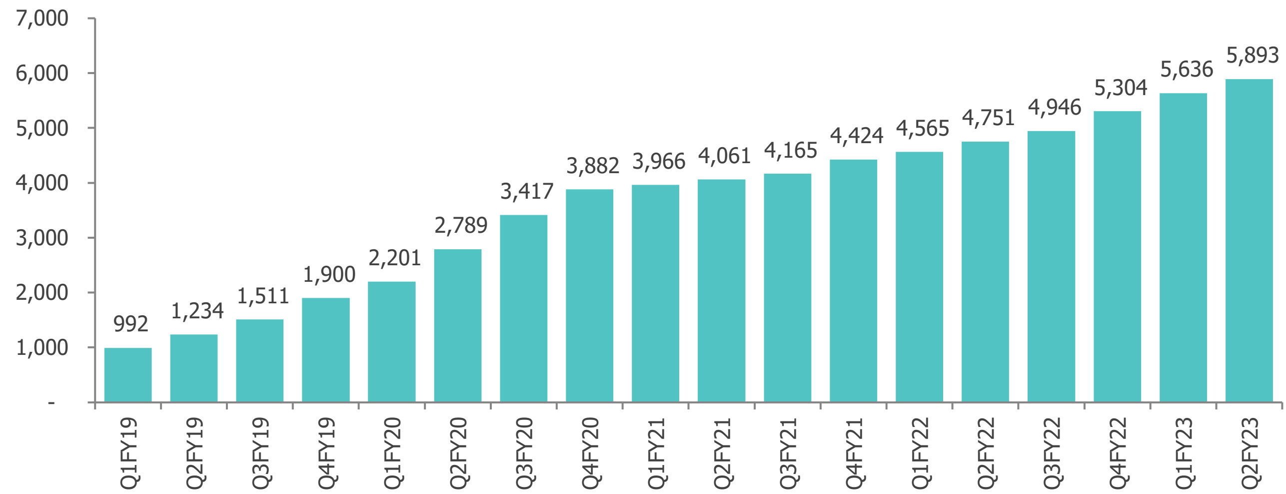
Amid economic uncertainty, fears of a global recession, and the domestic inflation that is driving the current interest rate scenario, credit growth has been strong through the festive season. There has been robust domestic demand with increased household consumption spending as well as passenger vehicle sales have reached pre-Covid levels. CareEdge Ratings believes the healthy growth in credit bodes well for the securitisation market.

Sriram Rajagopalan, Associate Director at CareEdge Ratings, said, “Securitisation continues to be a promising avenue for inorganically growing the retail portfolio for both banks and NBFCs. The regulatory requirement to meet priority sector lending norms for banks will also fuel the growth of the securitisation market. The continued growth in the securitisation market volume is along the expected lines. Given the momentum, the full-year volume for FY23 is expected to grow by 40%-50% over FY22.”

IBC Remains Popular Despite Haircuts of ~70%, Delayed Resolution Time

After slowing in H2FY21 and FY22, the number of insolvency cases increased by 24% y-o-y in Q2FY23. However, despite the increase, the number of cases admitted to the insolvency process continued to be lower compared to earlier quarters in FY19/20. The distribution of cases across sectors has remained broadly similar, compared to earlier periods.

CIRPs: Movement and Stakeholder-wise Distribution

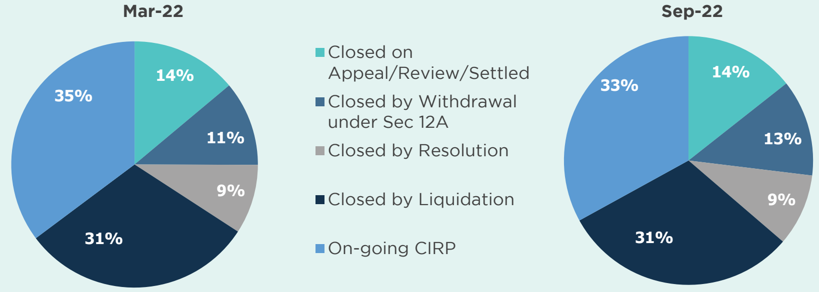


Source: IBBI

The number of cases admitted for Corporate Insolvency Resolution Process (CIRPs) has increased each quarter since the launch of the Insolvency and Bankruptcy Code in 2016., highlighting the rising acceptance of IBC as an effective debt resolution mechanism. The admission of cases has increased y-o-y in Q2FY23 by around 24% after reducing in the last few quarters in FY21 and FY22, however, despite the increase, the number of cases admitted to the insolvency process continues to be lower compared to earlier quarters in FY19/20. IBC has continued to gain in popularity, with close to 6,000 companies being admitted and a significant number of these cases on a cumulative basis being filed by the financial creditors (2,531 cases) and the operational creditors (3,008 cases). As of September 2022, the share of financial creditors has decreased, while that of operational creditors has increased. The share of corporate debtors has continued to remain the smallest over the same period. The share of the various sectors has largely remained constant compared with the previous period. The manufacturing sector accounts for the highest share at 39% of the overall cases, followed by the real estate (21%), construction (11%) and trading sectors (10%).

The status of the cases has largely remained constant compared with the previous period. Of the total 5,889 cases admitted into CIRP at the end of September 2022, only 9% have ended in approval of resolution plans, while 33% remain in the resolution process vs. 35% as of the end of March 2022. Meanwhile, 1,807 have ended in liquidation (31% of the total cases admitted). Meanwhile, 76% of such cases were either BIFR cases and/or defunct. Further, around 14% (846 CIRPs) have been closed on appeal /review /settled, while 11% have been withdrawn under Section 12A. A significant number of withdrawn cases (around 54%) were less than ₹ 1 crore, while the primary reason for withdrawal has been either the full settlement with the applicant (40.6%) or other settlement with creditors (24%).

Status of CIRPs



Total cases: 5,258

Source: IBBI

Total cases: 5,889

Summary of CIRPs Yielding Resolution

Particulars	Up to Mar. 2022	For Q2FY23	Up to Sep. 2022
Total admitted claims of Financial Creditors (₹ Cr.)	684,901.3	10,121.5	790,626.2
Liquidation value (₹ Cr.)	131,447.9	2,793.2	137,118.8
Realisable by FCs (₹ Cr.)	225,293.8	3,054.4	243,452.5
Realizable by FCs as a % of their claims admitted	32.9	30.18	30.8
Realisable by FCs as a % of their liquidation value	171.4	109.4	177.6

Source: IBBI

Post the implementation of the IBC, as can be seen above, the overall recovery rate till Q4FY22 in India reached 32.9% which has been on a declining trend.

The recovery rate for Q2FY22 stood at 49.2%, which increased to 30.2% in Q2FY23, resulting in aggregate recovery reaching 30.8% by Q2FY23 end.

Consequently, for the cases which have been resolved, the creditors have faced a haircut of approximately 70% on admitted claims.

Of the 1,944 going ongoing CIRPs, there has been a delay of more than 270 days for the completion of the process of 63% of ongoing CIRPs in September 2022 which is a decline of 10% as compared to 73% in September 2021. Further the 'more than 90 days but less than 180 days' segment is the second largest indicating that quite a few cases have commenced in the last quarter, while the other two categories continue to have quite a few cases in them highlighting the significant delays in the process. The delays for closure of CIRP/ Liquidation are similar across various categories of stakeholders, but the corporate debtor segment takes somewhat lesser time for resolution compared to the other two stakeholders (financial creditor and operational creditor). The pendency even for cases which have gone into liquidation is high with around 50% of the cases pending for more than two years and another 23% of the cases pending for more than one year. According to the report of the Standing Committee on Finance, the delay in resolution can be attributed to 1) delay in admitting cases to NCLT, 2) unsolicited bids outside the process which delay resolution, 3) subsequent litigations after the resolution plan has been approved, and 4) short-staffed NCLT and to the fact that NCLTs also handle cases relating to corporate affairs, M&As, etc.

Insolvency Resolution of Personal Guarantors

Of the 1,403 applications for insolvency resolution and bankruptcy proceedings related to personal guarantees, 53 were withdrawn/rejected/dismissed before the appointment of a resolution professional. Meanwhile, resolution professionals were appointed in 597 cases out of which 123 cases have been admitted and 18 cases have been withdrawn/rejected/dismissed

Avoidance Transactions

Under the IBC, resolution professionals (RP) can reverse any transaction entered by the debtor company before the IBC is invoked if the RP can prove that the transaction was intended to divert funds or alienate assets. These provisions are generally used on related party transactions, fund diversions and other relevant corporate actions and any money so recovered is distributed amongst the lenders. However, such claims can only be done after approval by the NCLT. RPs have filed 809 applications for avoidance transactions amounting to approximately ₹ 2.2 lakh crore. Of these, only 98 transactions involving over ₹ 18,100 crore (approximately 7.9% of the amount involved) were disposed of and only ₹ 64.3 crore (only 0.3% of the amount disposed) have been recovered. Further, in one case 758 acres of land out of 858 acres earlier valued at ₹ 5,500 crore has been recovered by a company which is under the resolution process.

India's Readymade Garment (RMG) Exports Likely to Cross US$ 30 billion by 2027

RMG constituted a major share of around US$ 500 billion in the global textile & RMG trade of around US$ 850 billion in CY21. The global RMG market is expected to reach around US$ 650 billion by CY27. The global RMG market majorly comprises the European Union (EU), the United States of America (US), the UK, Japan, Canada and South Korea together accounting for nearly 60% of the total global imports.

Countries such as China, Bangladesh, Vietnam, Germany, Italy, Turkey, Spain and India dominate the export market, with China accounting for a lion's share of 33% of the total RMG exports backed by high labour productivity along with economies of scale.

Share in global RMG market (%)

Countries	CY17	CY18	CY19	CY20	CY21
China	35.58	33.36	31.68	31.66	32.58
Bangladesh	6.52	6.95	7.00	6.57	7.08
Vietnam	5.45	5.94	6.36	6.47	6.70
Germany	4.54	4.93	5.04	5.41	5.02
Italy	4.78	4.94	5.12	4.99	4.91
Turkey	3.30	3.23	3.40	3.59	3.62
Spain	3.08	2.98	3.02	2.78	3.05
India	3.88	3.30	3.44	2.92	3.01
ROTW	32.87	34.37	34.94	35.61	34.03

Source: ITC Trade Map; Compiled by CareEdge

India's share in global RMG exports has remained sluggish from CY17 to CY21 with RMG exports at around US$ 15 billion in CY21. Countries such as Bangladesh and Vietnam have captured a large part of China's declining share in the global RMG exports. Competing nations have gained due to duty-free access to key export markets, i.e., EU, the UK and Canada apart from their higher labour productivity and economies of scale. India's dependency on cotton-based textiles as against the high share of man-made fibres in the global RMG market also impacted its RMG exports.

Government Push to Boost Competitiveness of Indian Textile Players

The government has set an ambitious target of taking Indian textile exports to US$ 100 billion by 2030 to boost foreign exchange inflow and generate employment. To create a level-playing field for Indian exporters in the global market, the Government of India has rolled out various schemes such as Remission of Duties and Taxes on Exported Products (RoDTEP), Rebate of State and Central Taxes and Levies (RoSCTL), Production Linked Incentive (PLI) scheme, PM Mega Integrated Textile Region and Apparel (PM MITRA) park etc. PLI scheme aims to boost presence in man-made fibre and technical textile, PM-MITRA park is expected to bring scale while RoDTEP and RoSCTL ensure stability of incentives. The government has also entered into the Comprehensive Economic Partnership Agreement (CEPA) with UAE and the Economic Cooperation and Trade Agreement (ECTA) with Australia and is in an advanced stage of discussion for FTA with the UK while discussion for FTA with EU is ongoing.

Near-term Headwinds Partially Offset by Crisis in Neighbouring Nations

India's garment exports and order book have taken a hit in recent times due to high inventory with retailers in the US and the energy crisis in the EU. However, it is noteworthy that the 7.78% y-o-y growth in US monthly apparel store sales in 9MCY22 reduces the imminent recession in the US. Furthermore, a crisis in RMG exporting nations of Sri Lanka, Myanmar and Pakistan (cumulative RMG exports of US$ 17 billion in CY21) is expected to shift some orders to India, Bangladesh and Vietnam. The benefits may however be limited due to resistance by global brands to change sourcing amidst demand pressure on the back of high inflation and high depreciation of currencies of these countries compared to the depreciation of the Indian rupee.

RMG Opportunities in Offing for India

China is expected to continue losing its share in the global RMG markets due to its declining competitiveness and the 'China Plus One' sourcing strategy adopted by global brands and retailers. This, in turn, could be beneficial for India as increasing competitiveness and favourable policy regime serve as positives. With trade agreements, India's share in UAE and Australian markets are expected to increase and the FTA with the UK would be a game changer as it will create a level-playing field in around US$ 21 billion RMG market. Currently, India has a market share of 4-5% in EU and UK as Bangladesh, Vietnam and Pakistan have a tariff advantage of around 10% vis-à-vis India in some of these markets.

Outlook

"Having adequate raw material and a large labour workforce, India is well poised to grab the opportunity in the global RMG market. India has a very good presence across the cotton textile value chain from fibre to fabric, while it has a limited presence in man-made fibre, which is expected to get a boost by expected FTA with the UK and PLI scheme. Furthermore, having a presence across entire-value chain reduces transportation costs and lead time, thereby providing a cost-effective solution to the customers. With all these, Indian RMG exports are expected to surpass the US$ 30 billion mark by CY27. This shall translate into 4.6-4.9% share in world RMG exports as against the current share of around 3%," said Krunal Modi, Associate Director, CareEdge Ratings.

CareEdge RATINGS

ECONOMY DASH BOARD

HEAT MAP AND PROJECTION TABLE

		Jan-22	Feb-22	Mar-22	Apr-22	May-22	Jun-22	Jul-22	Aug-22	Sep-22	Oct-22	Nov-22
PMI-M	Unit	54.0	54.9	54.0	54.7	54.6	53.9	56.4	56.2	55.1	55.3	55.7
PMI-S	Unit	51.5	51.8	53.6	57.9	58.9	59.2	55.5	57.2	54.3	55.1	56.4
GST Collections	Rs lakh crore	1.4	1.3	1.4	1.7	1.4	1.4	1.5	1.4	1.5	1.5	1.5
E-Way Bill	Crore	6.9	6.9	7.8	7.5	7.4	7.4	7.6	7.8	8.4	7.7	8.1
Air Passenger Traffic	Crore	1.5	1.8	2.4	2.4	2.7	2.5	2.4	2.5	2.5	2.7	
Railways Passenger Traffic	Crore	34.5	41.4	48.4	45.6	50.1	50.1	51.6	54.0	54.8	55.2	57.0
PV Sales	Lakh	3.0	3.1	3.4	3.0	3.1	3.3	3.5	3.4	3.6	3.4	
2-3 Wheeler Sales	Lakh	15.7	14.8	16.1	16.1	16.6	17.4	18.1	19.4	21.1	19.5	
Tractor Sales	Lakh	0.6	0.6	0.8	1.0	0.9	1.1	0.7	0.6	1.3	1.3	0.8
IIP	y-o-y%	2.0	1.2	2.2	6.7	19.7	12.6	2.2	-0.7	3.5	-4.0	
Core Sector	y-o-y%	4.0	5.9	4.8	9.5	19.3	13.1	4.8	4.1	7.8	0.1	
Power Consumption	y-o-y%	1.1	4.5	5.9	11.5	23.2	16.2	2.3	0.6	11.3	0.5	12.3
Petroleum Consumption	y-o-y%	2.5	5.6	6.7	9.6	23.7	17.9	6.0	16.2	8.2	3.3	10.2
Outstanding Bank Credit - Total	y-o-y%	8.2	7.9	8.6	11.1	12.1	13.2	14.5	14.3	15.3	16.7	
Capital Goods Import	y-o-y%	24.6	14.5	18.8	17.1	17.2	18.6	27.4	26.5	17.8	3.9	
Merchandise Exports	y-o-y%	27.9	34.5	26.4	29.2	20.8	30.4	8.4	10.4	4.8	-16.7	

Note: Data for some Indicators are high in April-June quarter due to base effect

Indicator	FY18	FY19	FY20	FY21	FY22	FY23 Forecast
Gross Domestic Product (y-o-y%)	6.8	6.5	3.7	-6.6	8.7	6.9
CPI Inflation (y-o-y%)	3.6	3.4	4.8	6.2	5.5	6.8
Fiscal Deficit (As % of GDP)	3.5	3.4	4.7	9.2	6.7	6.5
Current Account Balance (As % of GDP)*	-1.8	-2.1	-0.9	0.9	-1.2	-3.6
Rupee (USD/ INR) (Fiscal year-end)	65.0	69.2	75.4	73.5	75.8	81-83
10-Year G-Sec Yield (%) (Fiscal year-end)	7.3	7.5	6.1	6.3	6.8	7.5

* Note: (-) Deficit / (+) Surplus

ABOUT US

CareEdge is a knowledge-based analytical group that aims to provide superior insights based on technology, data analytics and detailed research. CARE Ratings Ltd, the parent company in the group, is one of the leading credit rating agencies in India. Established in 1993, it has a credible track record of rating companies across multiple sectors and has played a pivotal role in developing the corporate debt market in India. The wholly-owned subsidiaries of CARE Ratings are (I) CARE Advisory, Research & Training Ltd, which offers customised advisory services, credible business research and analytical services (II) CARE Risk Solutions Private Ltd, which provides risk management solutions.

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