Advances in Economics and Business Management (AEBM)
p-ISSN: 2394-1545; e-ISSN: 2394-1553; Volume 3, Issue 4; April-June, 2016, pp. 351-356

http://www.krishisanskriti.org/Publication.html

A Review of Profitability and Performance of Major Sectors of Small and Medium Enterprises in India

Gurpreet Singh[1] and Vineeta Mishra[2]

[1]*PGPM Student IBS-Gurgaon*
[2]*Amity University*
E-mail: [1]singh.gurpreet3194@gmail.com, [2]vineetamishra85@yahoo.com

Abstract—*The contribution of the MSME sector towards the growth of Indian economy has been significant in the past decade. RBI released the consolidated data of non-government non-financial (NGNF) private limited companies on 31st March 2016. This gives a great insight into the status of Indian economy. With the help of this data sectoral analysis of financial performance of six major sectors has been attempted through exploratory research and ratio analysis. The world economy has seen a significant slowdown however India has been affected less due to high local demand. MSMEs have been catering mainly to the local demand. The data shows that most of the industries have been showing a positive growth pattern in the past three financial years.*

1. INTRODUCTION

As per the statistics of data.gov.in, the Gross domestic product of Indian economy has risen over the years from 4.6% in 2012-13 to 7.3% in 2015-16 and account of about 6.8% of the global GDP. With a down-trend in the economy, it has still managed to sustain itself through continuous support of government. The global markets have also experienced an overall negative trend in growth of global GDP from 5.43% to 3.43% during 2010 to 2014.

The performance indicators such as Nifty, stock market indicators which access the performance of blue chip companies does not depicts full image of the industry performance because of the simple reason that small and medium enterprises which also contribute to the economic growth are not considered. With publishing of financial data of 237,398 non-government non-financial private limited companies by RBI, government has given an opportunity to track the trends of private limited companies by observing the changes that have been prevailing during the FY 2012-13 to 2014-15.

This data shows how the Micro, Small and Medium Enterprises (MSME) sector in driving the growth of the industry and adding up to the GDP of the country. It has finally ended the controversy by showing that smaller companies are performing far better than the giants of the industry.

2. METHODOLOGIES

The consolidated data of 2,37,398 Private Limited Companies for FY2012-13 to FY2014-15 comprises of growth rates of each financial item, financial ratios, consolidated income statement and balance sheet, statement of sources and uses of funds and industry-wise growth rates and financial ratios.

In our study we have considered specific industries on the basis of their scale and number of companies. The specific industries under consideration are Mining & quarrying, manufacturing industry (Food Products & Beverages, Pharmaceuticals & Medicines, Iron and Steel) and service industry (Trade Wholesale & Retail, real estate).

We have performed Year-To-year comparisons of specific growth ratios and financial ratios to find the area of change. The profitability ratios such as Operating profit to sales ratio, Profit after tax to sales ratio, Gross profit (EBIT) to total net assets ratio, Profit after tax to net worth ratio are taken into consideration for analysing the profitability of different industries.

We have also tried to identify the factors for the specific changes so as to justify our observations. This study will help in better understanding of the industry and its performance over the years for decision-making of stakeholders.

3.1 Mining & Quarrying

Key Indicators:

1. The Mining & Quarrying Industry has been one of the most important contributors towards the GDP of India. With the Government's vision to focus on overall infrastructural development including roads & dedicated freight corridors across the country, the industry

witnessed a positive growth rate in the Total Sales, Operating Profits and significant reduction in the liabilities. Part of this is also contributed by the fact that the Government is working towards building transparent and fair procedures in this segment which till date is majorly dominated by the Government owned units and has taken a major hit due to corruptions and scams.

2. The industry segment witnessed a significantly positive growth rate in 2014-15 over the previous year while the Production Value has gone down in comparison to the growth in Sales.
3. A significant observation related to expenses was made in this study. While the industry experienced increase in manufacturing and operational expenses which was expected with the growth, it was pleasing to see a sharp reduction in the expenditure in interests with a very steep decline in the Current Liabilities. This is definitely a sign of positive growth in the Industry which is expected to contribute up to 5% of National GDP in the next few years (reference FICCI Report).
4. Another important observation was that despite of a 34% increase in Depreciation Provisions in 2014-15 in comparison to 2013-14, the Earnings before Interest & Taxes (EBIT) continues to show an upward trend.
5. Since the production by private players was majorly on halt due to Stay Orders from the Honourable Courts, the industry was not able to cater to export orders and generate foreign earnings.

3.2 Food Products & Beverages

Key Indicators:

1. According to Industry Reports, the Food Products and Beverages Industry is one of the major contributors to India's GDP from the Agriculture & Manufacturing segment.
2. It is noteworthy that India has predominantly considered an Agricultural Economy and the Industry here in consideration is directly related/ impacted by the Agricultural Growth.
3. During the year 2014-15, the industry witnessed a negative growth where the Sales had fallen by 2% in comparison to previous year. The negative growth has primary been due to many natural disasters which has impacted the agricultural output and a very high percentage of wastage caused to due lack of adequate warehousing.
4. The manufacturing and total operating costs have declined with the adaptation of new technologies, innovation and automation of food processing and packaging. On the flip side, the remuneration costs continue to rise further due to shortage in skilled manpower.
5. On the positive side, the Industry witnessed a change in the Gross Profit growth from a negative growth (-2.3) in 2013-14 to a positive (7.6) in 2014-15. Further, the Profit after Tax has seen a significant growth from -21.4% in 2013-14 to 32.5% in 2014-15.
6. With new entrants in the industry and adoption of automated machinery, depreciation Provision had experienced a steady rise in growth rate on about two times during 2014-15. All the assets growth rates had turned from double digits to single digit growth rates during 2014-15.

3.3 Pharmaceuticals & Medicines

Key Indicators:

1. The pharmaceuticals industry has been one of the steadiest segments in India. The industry has constantly evolved since 1970's and more since 2000 with the Government reforms to regulate and organize the industry.
2. The major variables like Sales, Value of Growth and Total Income have been growing slowly but steadily over the two years.
3. While the industry has been able to keep a check on its total expenses, it was a delight to see a jump in the Gross Profits and Savings.
4. At the same time, the sharp decrease in Total Liabilities exhibit a positive trend in the industry with a strong capability to grow overtime. It is worth noting that the Pharmaceutical Industry has received the highest Foreign Direct Investment since 2000.

With the global economy improving over the last two years, the industry continues to recover in 2014-15 with a very high growth rate.

3.4 Iron & Steel

Key Indicators:

1. The Iron & Steel Industry is again one of the major contributors in the Economic Growth of the country. Many other industries like Construction, Automobiles and Machinery & Equipment are dependent significantly on the Iron & Steel industry. The industry has witnessed steady growth ever since the major reforms were adopted in 1991 and 1992 (http://steel.gov.in/overview.htm). India

continues to enjoy the status of being the 3rd largest Steel producer in the world in the last many years in a row.

2. According to CII report on Retail Sector, the Iron and Steel industry faces stiff competition especially in terms of pricing in imports from countries like China, Japan & Korea which have increased significantly over the last few years. The Government of India had been cognizant about this and has proactively been taking steps like imposing Anti-Dumping Duty, increasing Minimum Import Price etc. to support the industry.
3. With the support from the Government and growth in domestic market, the industry saw a single digit positive growth in Sales and Total Revenues.
4. On the contrary, with a steep rise in manufacturing and other operating expenses, the industry had to face a negative growth in Gross and Net Profits.
5. With no major investment add-on, the industry's Balance Sheet doesn't exhibit any significant change in the Assets and Liabilities.
6. Another important observation was a sharp rise in imports which definitely shows that the industry needs significant initiatives both from the Government and the players to face the stiff competition from international markets.

3.5 Trade Wholesale & Retail

Key indicators:

1. According to CCI report, India has been the 5th most desirable destination in the world for retail business with almost 30% growth rate accounts about 14-15% of the country's GDP.
2. The growth in the retail and wholesale sector is driven by increased household incomes, emerging nuclear families, customer aspirations, increased expenditure for luxury goods and most importantly by liberalisation policies in the last decade.
3. With the continuous add-on in Liberalisation policy, the government had open up doors for foreign direct investments (FDI). Some of the key policies are 100% FDI in "single-brand" retail, up to 51% FDI in "multi-brand' retail and 100% FDI in cash-carry wholesale.
4. During the year 2014-15, the industry witnessed a growth in sales and also operating expenses as a result of ease of shopping through organised retail stores.
5. In contrast to increased sales, manufacturing and operating expenses had experienced a significant growth rate. As a result, industry had to face a negative growth in Gross and Net Profits. (EBIT 70.6% to -7.6%)
6. A positive trend has been observed with reduction in the growth rate of interest expense due to significant decrease in total borrowings of the industry.
7. Another important observation was the tremendous growth of import expenditure in foreign currency of about 10.8% in 2013-14 to 127.4% in 2014-15.

3.6 Real Estate

Key indicators:

1. Real estate sector has been one of the fastest growing markets in the world. It has 4 sector components retail, housing, commercial and hospitality. Among these, housing is the key sector comprising about 6% of country's GDP. Housing being the second largest sector providing employment.
2. With support of government new corporate parks, commercial spaces are constructed on land provided under SEZ policy (special economic zones) to attract business houses. Legality for entry of FDI has also structured for ease to attract more Private equities in the country, as said in IBEF in its report.
3. With increase in the aspirations of the society of purchasing new homes, emergence of nuclear families and shift in preference to high-risers over traditional low-rise apartments and commercial offices have shown an extra-ordinary increase in growth of sales during the year 2014-15.
4. An important observation was the rise in the growth in manufacturing and operating expenses with the positive sales trend. Expenses will grow as more and more real estate projects are being undertaken with higher construction costs and low supply of skilled manpower.
5. Industry's Interest expense has shown a growth (17.5% to 31.4%) due to increased borrowing from banks to finance its expansion plans. There has been no change in the interest rates by the government during the FY 2014-15, so as to support the industry with its expansion plans.

Table 1: Industry-wise profitability ratio sourced from RBI

Industry	Mining & Quarrying			Food & Beverages			Pharma & Medicine			Iron & Steel			Trade W & R			Real Estate		
Year	2012	2013	2014	2012	2013	2014	2012	2013	2014	2012	2013	2014	2012	2013	2014	2012	2013	2014
Operating profit to sales	5.4	6.2	6.5	4.8	4.8	5.2	12.7	12.3	12.5	2.5	3.1	3.3	0.2	1.5	0.8	-16.3	-4.7	0.2
Profit after tax to sales	1.4	1.9	2	1.9	1.4	1.7	7.8	7.4	8	0.5	1	0.9	0	1.1	0.4	-19.7	-10.5	-10
Gross profit (EBIT) to total net assets	4.3	4.3	4.8	7.1	6.3	6.5	11.9	11.5	11.3	4.6	5.5	5.4	1.4	2.2	1.8	-0.8	0.6	0.8
Profit after tax to net worth	2.6	3.3	3.7	8.3	6.2	7.8	18.6	16.7	17.3	2.5	4.9	4.5	0	1.1	0.4	-7.5	-4	-4.5

3. PROFITABILITY RATIO ANALYSIS

4.1 Operating profit (EBIT) to sales ratio

The operating profit margin ratio is calculated simply using:

Operating profit margin= $\frac{Operating\ Income}{Total\ Revenues}$ or $\frac{EBIT}{Total\ Revenues}$

It indicates how much profit a company makes after paying for variable costs of production such as wages, raw materials, etc. According to the graph below, Trade wholesale and retail industry has seen a volatile movement in its operating profit. Also Pharmaceuticals industry has consistently outperformed during 2012-13 to 2014-15 and Real estate sector has shown a positive recovery of profit.

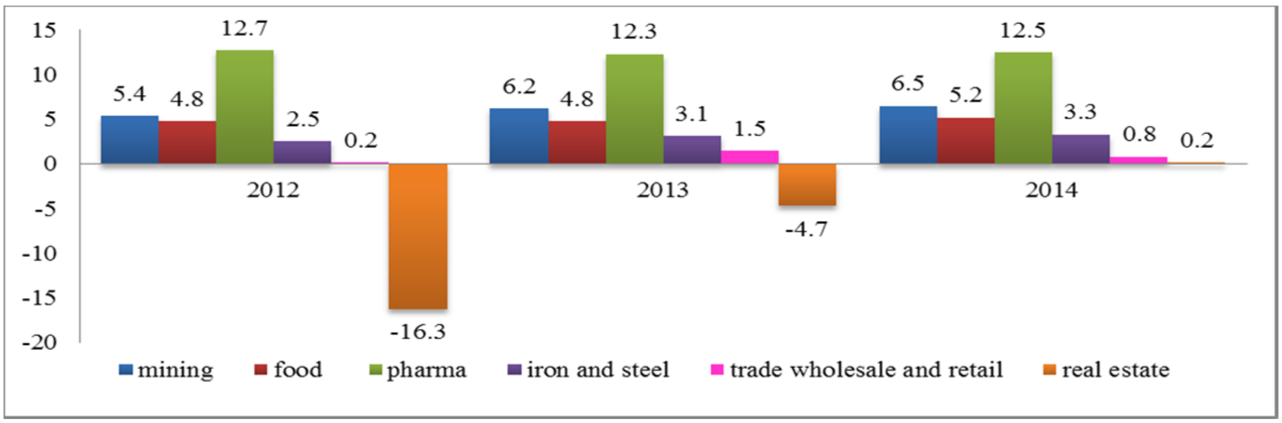

Fig. 1: Operating profit to sales ratio of different industries

4.2 Profit after tax to sales

Profit after tax to sales=

$$\frac{Net\ Profit}{Net\ Sales}\ X\ 100$$

It shows ratio of after-tax profits to net sales. It shows how much profit is left after deducting all the costs of production, administration financing and income taxes. It is one of the best measures of the overall results of a firm. Pharmaceuticals industry has a consistent profitability margin over the years with its constant growth sales.

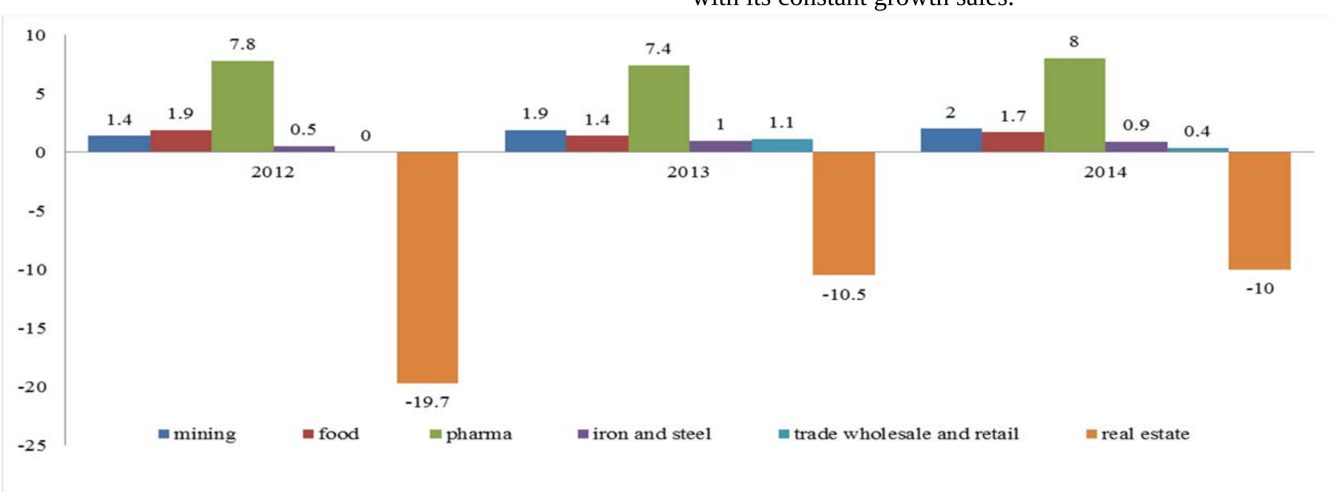

Fig. 2: Profit after tax to sales ratio of different industries

4.3 Gross profit (EBIT) to net Sales

The calculation is:

$$\frac{Net\ Profit}{Fixed\ Assets + Net\ Working\ Capital}$$

It shows how well a company is able to utilize its asset base to create profits. A high ratio of assets to profits is an indicator of excellent management performance. Real Estate industry's significant sales growth had recovered its profit base trend to positive and increasing.

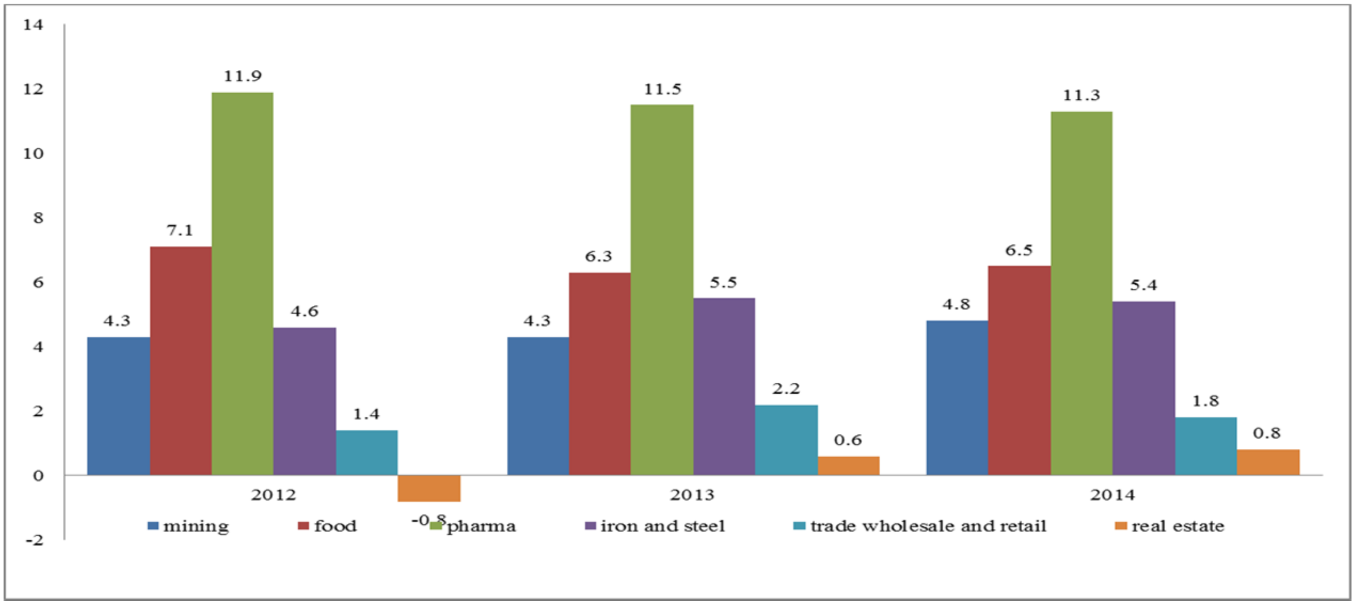

Fig. 3: Gross profit to sales ratio of different industries

4.4 Profit after tax to net worth

The net worth ratio states the return a shareholder will receive at 100% payout ratio. Thus, the ratio is developed from the perspective of the shareholder, to analyse investor returns.

The formula is:

$$\frac{Net\ After - tax\ Profits}{Shareholder\ Capital + Retained\ Earnings}$$

According to the graph below, shareholders of pharmaceuticals industry are earning higher consistent returns. It has been observed that earnings in iron and steel industry have increased with steadily during 2013-14.

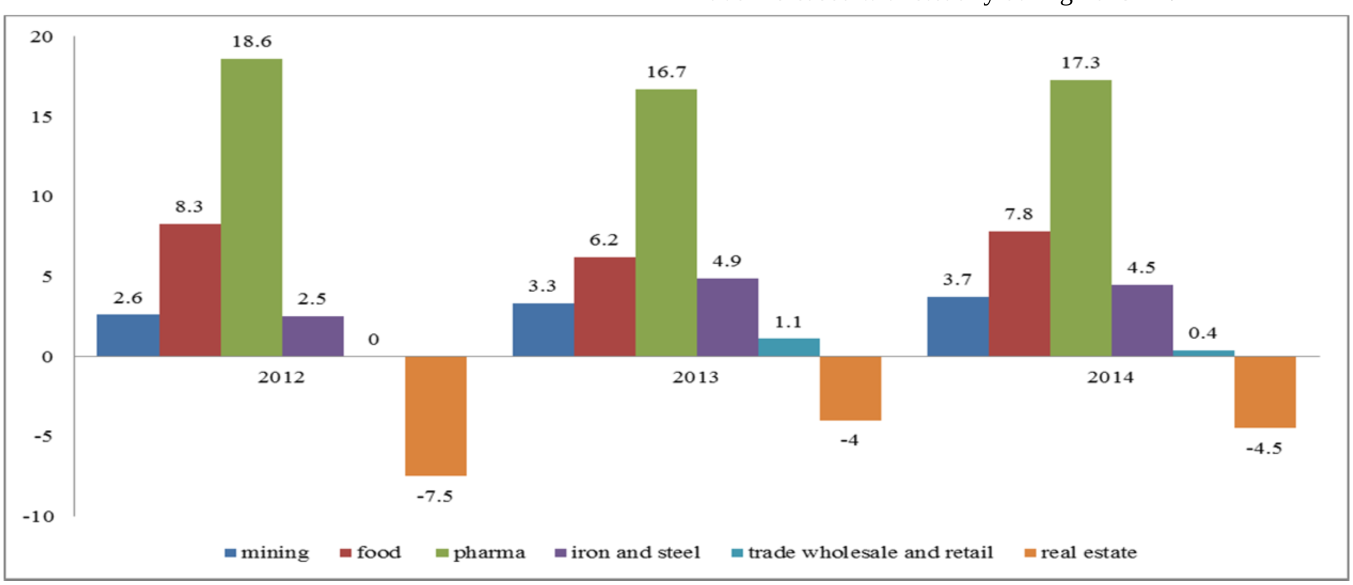

Fig. 4: Profit after tax to net worth ratio of different industries

4. CONCLUSION

With this overall study we have observed that Pharmaceuticals and medicines industry has out-performed with higher profitability rate consistently. The Mining and Quarrying industry has shown a magnificent growth in earnings with the support of government. An important observation was the recovery of Real Estate industry.

REFERENCES

[1] The data is been sourced form RBI website (https://www.rbi.org.in/).
[2] Otto, J. (2004). International Comparative Tax Regimes. 50 Rocky Mountain Mineral Law Institute, 17, 1-45.
[3] Grant Thornton Report on CII – food and beverages sector- the new wave. 2014
[4] "Development of Indian Mining Industry – The Way Forward" by FICCI, October 2013.
[5] monthlyreview.org › 2009 › Volume 61, Issue 03 (July-August)
[6] Report on "food Processing" by IBEF, august 2015.
[7] CCI Report "Iron and Steel Industry in India", July 2015.
[8] CCI report "Retail Sector in India", January 2015.
[9] http://jllapsites.com/real-estate-compass/2015/12/indian-real-estate-an-analysis-of-2015-and-gazing-into-2016/
[10] http://www.ibef.org/industry/real-estate-india.aspx
[11] Many newspaper reports were also referred to understand the trends in different industries such as www.mining.com tenders.tradeindia.com, www.miningweekly.com, www.thepharmatimes.in, ,https://www.theguardian.com/business/pharmaceuticals-industry, http://www.pharmaceutical-technology.com/news/legal-regulatory/ , http://economictimes.indiatimes.com/.