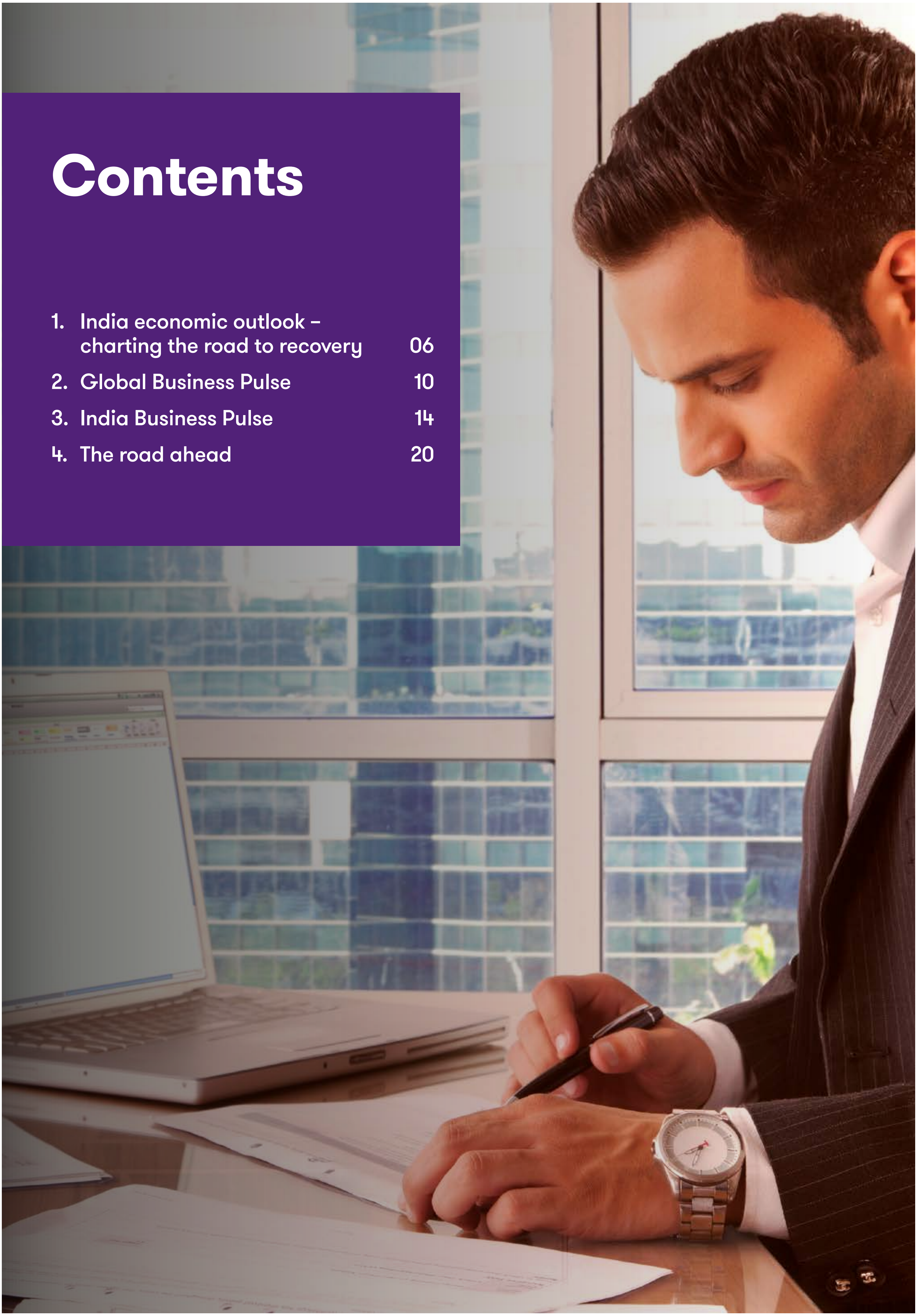
International Business Report

India mid-market survey: Insights and outlook for 2021

Contents



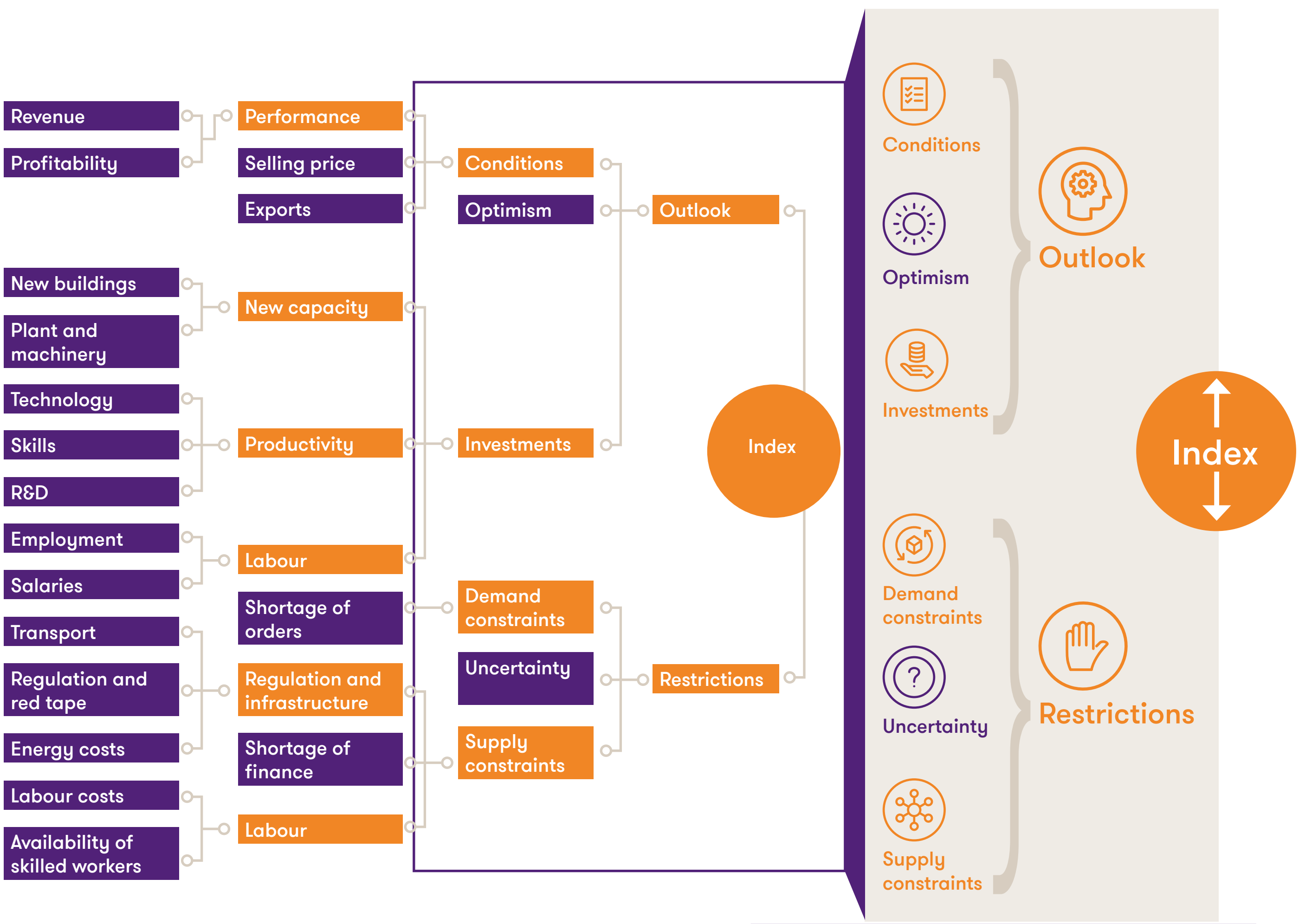
About the index

Grant Thornton's business pulse is the first index to track the health of mid-sized companies at a global, regional, country and sector level.

Developed in partnership with Oxford Economics, this index is calculated every six months and draws on the world's largest and longest-running research study into the mid-market, which interviews around 10,000 mid-market business leaders across 29 economies annually.

The Index provides a complete view of mid-market health and prospects at a global, regional, sector and country level, while sub-indices provide a view of several dimensions that contribute towards this health.

Analysis of the results, stretching back 10 years, show a strong positive correlation with real gross domestic product (GDP) growth. We believe that this shows the real contribution of the mid-market to economic growth and the importance of this unique index.



The final index value is the sum of these two sub-indices (Outlook and Restrictions) and ranges from -50 to +50. It can be read as follows:

A positive index value implies that the prospects from outlook indicators more than offset concerns over restrictions. A higher index score may be the result of an improving outlook or lower restrictions, or both. A score of +50 would represent perfect health with no restrictions and an ideal outlook, and the likelihood of high growth in the future.

A negative value, on the other hand, suggests that concerns about restrictions are overtaking prospects from outlook indicators. A lower index score may be the result of a worsening outlook or higher restrictions, or both. A score of -50 would represent dire health, with crushing restrictions and an appalling outlook, and the likelihood of decline in the future.

For the current edition of the Indian Business Pulse, 251 Indian business leaders were surveyed to provide insights on the views and expectations of Indian mid-market businesses.

Foreword

Increasing investment in infrastructure and reduction in tax and compliance costs have been highlighted as key pillars of recovery.

The impact of the pandemic on our economy has been unprecedented, with India's GDP contracting for the first time in 40 years. However, as cases decline and the vaccine roll-out gains momentum in India, there are visible signs of revival. Business leaders surveyed as part of Grant Thornton's global research believe that the government's strong push for 'Make in India' and growing interest from global companies and governments to meet their sourcing requirements from India will pave the way for robust exports. 71% of mid-market business leaders surveyed remain optimistic about the outlook of India's economy over the next 12 months, compared to 57% for global economic recovery.

Our research also highlights several measures businesses believe India needs to speed up recovery and become a viable cost competitive alternative for global supply chains. 61% of respondents cited ease of access to capital as the top enabler for attracting global companies to India. Increasing investment in infrastructure and reduction in tax and compliance costs have been highlighted as key pillars of recovery. Along with the Atmanirbhar (self-reliance) announcements of 2020, Budget 2021 has provided the economy with a big push – India is at a seminal moment and we now need to sustain the economic momentum that we will see this year throughout the rest of this decade.

We hope you will find the results of this report, based on survey findings from business leaders in India insightful. At Grant Thornton Bharat, we are working with the government and leading Indian and global businesses to maxmise the opportunity ahead of us, and helping shape a Vibrant Bharat.

Vishesh C. Chandiok
CEO
Grant Thornton Bharat

India economic outlook – charting the road to recovery

The impact of COVID-19 on the Indian economy has been multifarious. Affecting both formal and informal sectors – lowering consumption and causing significant unemployment – the pandemic hit at a time when the economy was already decelerating. However, reopening the economy has poised the country towards a gradual recovery, albeit slower.

Expectations about a rebound

In the International Business Report (IBR), while 30% of mid-market leaders expect a greater than 10% contraction, nearly 70% are still optimistic about the outlook, even though it may take at least six months to recover to pre-pandemic levels.

Figure 1: Growth expectations in 2021

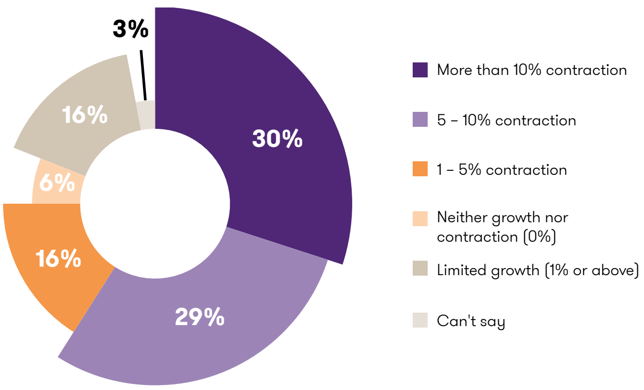
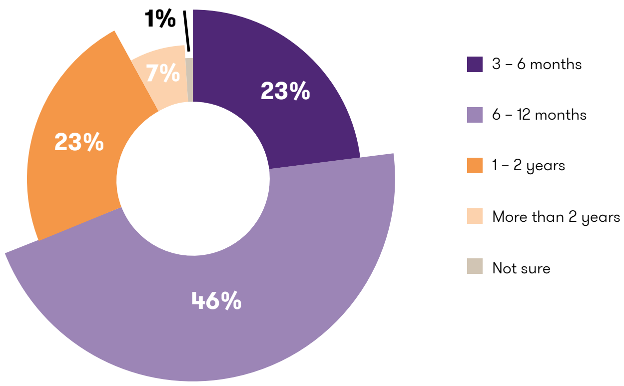


Figure 2: Expected time for economic recovery (to pre-COVID 19 levels)



Where have we fared well?

India's policy response to the pandemic was swift with government announcing INR 20,000 crore stimulus package through Aatmanirbhar Bharat Abhiyan and the Reserve Bank of India (RBI) expanding its balance sheet by 4.6% of the GDP (the most amongst the large emerging markets). The central bank also lowered rates by 115 basis points (bps) since the commencement of the lockdown and announced macro prudential measures to ensure financial stability. While 78% of the mid-market leaders are satisfied with RBI's loan restructuring measures, aimed at helping stressed companies across sectors mitigate COVID-19 impact, 14% could not decide if the government's policy measures to boost MSMEs were enough for the sector.

Figure 3: Are RBI's measures to help stressed companies adequate?

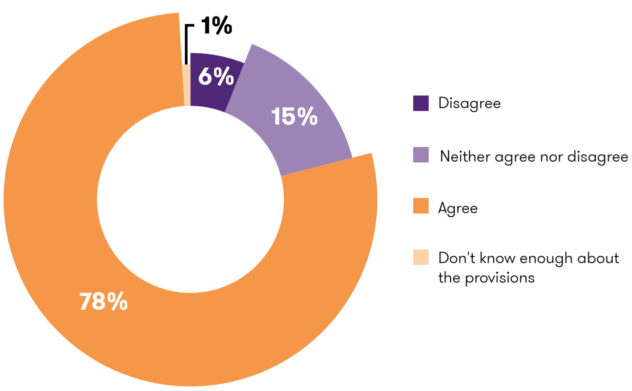
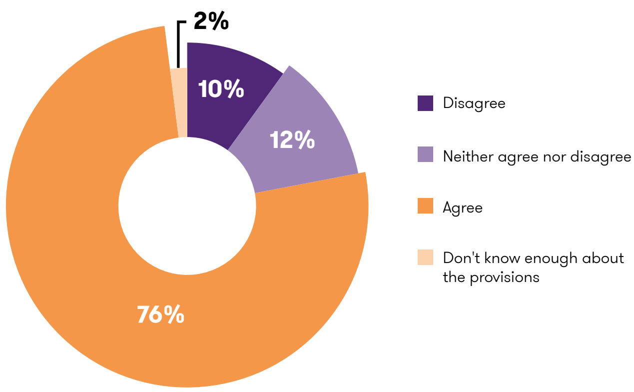


Figure 4: Are the government's MSME policy initiatives sufficient?



What more can we do to recover?

The Indian economy rebounded with a V-shaped recovery after the impact of one of the strictest lockdowns imposed due to the spread of COVID-19. The impact on the economy also meant that India will have to wait to achieve its target of emerging as a USD 5 trillion economy by 2026 - 27. The IBR also highlights measures the government can take to help India emerge as a cost competitive alternative for attracting companies looking to diversify their global manufacturing hubs and supply chains. Nearly two-thirds (61%) respondents cited ease of access to capital as the top enabler. While 59% respondents seek simplification of tax and labour laws, 55% see logistics and infrastructure development as game changers.

Figure 5: Additional measures to help the economy recover

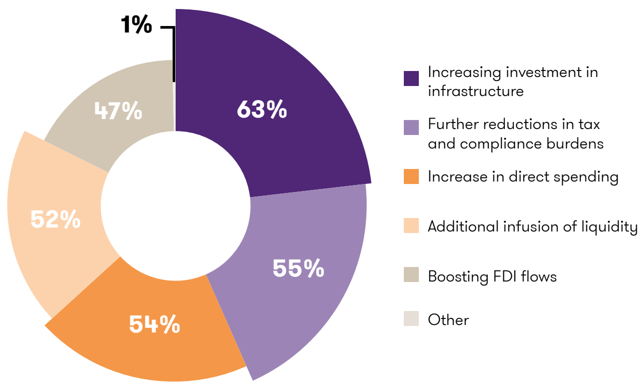
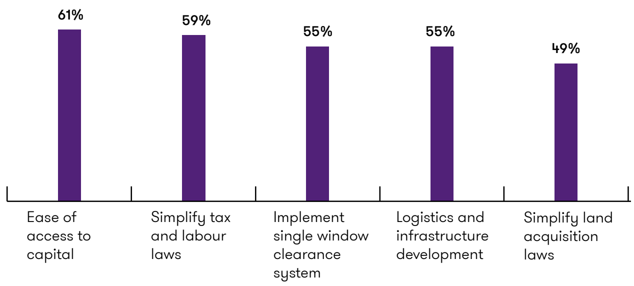


Figure 6: Measures for India to emerge as a global manufacturing hub



*multi-select option so percentages will not add to 100%

> In the backdrop of the pandemic, the government has announced a bold budget, with focus on providing impetus to the economy, boosting capital formation, increasing government spending, and stepping up the disinvestment process. There is further push for the administrative reforms such as faceless appeals in the Tax Tribunal, reduction in time period for re-opening of the tax assessments and further impetus on digital transactions. These measures should help India gain further traction on ease of doing business.

Vikas Vasal
National Managing Partner, Tax,
Grant Thornton Bharat

Reports suggest India is well placed to successfully roll out COVID-19 vaccines in 2021 as a manufacturer of majority of the world's vaccines and a 42-year-old vaccination programme that targets 55 million people each year.

Despite a slow growth, India is poised to become the world's third largest economy by 2030, overtaking the UK in 2025, Germany in 2027 and Japan in 2030. Since June 2020, the country has been witnessing a V-shaped recovery with the return of consumer confidence, robust financial markets, an uptick in manufacturing and exporters braving it out in the global market.

The pandemic has disproportionately affected activity in the services sector, paralysed consumption and led to unemployment. Nearly a quarter of the country's economic activity was wiped out by the drying up of global demand and collapse of domestic demand due to lockdowns. The informal sector, which accounts for four-fifths of employment, also suffered severe income losses. While recent data indicates that the services sector is gaining momentum, overall growth is expected to touch 5.4% in 2021. The first advance estimates (AE) by the National Statistics Office (NSO) have projected a contraction of 7.7% in real GDP in 2020-21; a shallower decline than earlier expected and better than the projections by international agencies such as the World Bank and International Monetary Fund. To ensure the economy is given the requisite push, the fiscal deficit in FY22 is also budgeted at 6.8% of GDP.

The agriculture sector, with its bountiful harvest, has become an important driver of recovery. The sector witnessed accelerated tractor sales, healthy year-on-year growth of 2.9% in rabi sowing, and reservoirs' live storage stood at 122% of decadal average. Announcements for the sector in the Union Budget 2021 built on the existing initiatives and addressed priority areas by increasing outlay for road and rail logistics, expanding the scope of Operation Greens, increasing target for agriculture credit, doubling outlay for micro irrigation, strengthening infrastructure, etc.

In the current fiscal, the manufacturing sector is likely to see a contraction of 9.4%. Real estate too is seeing visible signs of recovery with residential sales rising significantly. An outlay of INR 15,700 crore, more than double the allocation in FY21, the micro, small and medium enterprises sector received the requisite push in the Union Budget 2021. Incentivising incorporation of one person company to boost start-ups, extending social security benefits to gig and platform workers, reducing custom tariffs for import of raw materials for certain goods, etc., are some of the provisions being seen as a means to propel the economy back on track.

Reports suggest India is well placed to successfully roll out COVID-19 vaccines in 2021 as a manufacturer of majority of the world's vaccines and a 42-year-old vaccination programme that targets 55 million people each year. The accruals of the economic benefits would be significant, especially to sectors, such as hospitality, transportation and entertainment, which were hit hard during the pandemic.

The government's Aatmanirbhar Bharat Abhiyan was a prudent measure at a time when the economy and various sectors were battling the aftereffects of a pandemic. The economy, however, has proved to be resilient with recent data being evidence of recovery. Auto sales, consumer durables, freight traffic and consumption of petroleum product, all have shown a marked acceleration in the last 3-4 months. The December 2020 goods and services tax (GST) figures at INR 1.25 lakh crore are being touted as the highest monthly collection with a year-on-year growth rate of 11.6%. With focus on reforms, disinvestment, status quo on tax rates and infrastructure development in the Union Budget, the government has stepped up expenditure on various large-scale projects to provide impetus to the economy.

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Global Business Pulse

The Global Business Pulse index fell into a negative territory in H1 2020 and although it rose in H2 2020, it still is in negative territory, registering a score of -4.

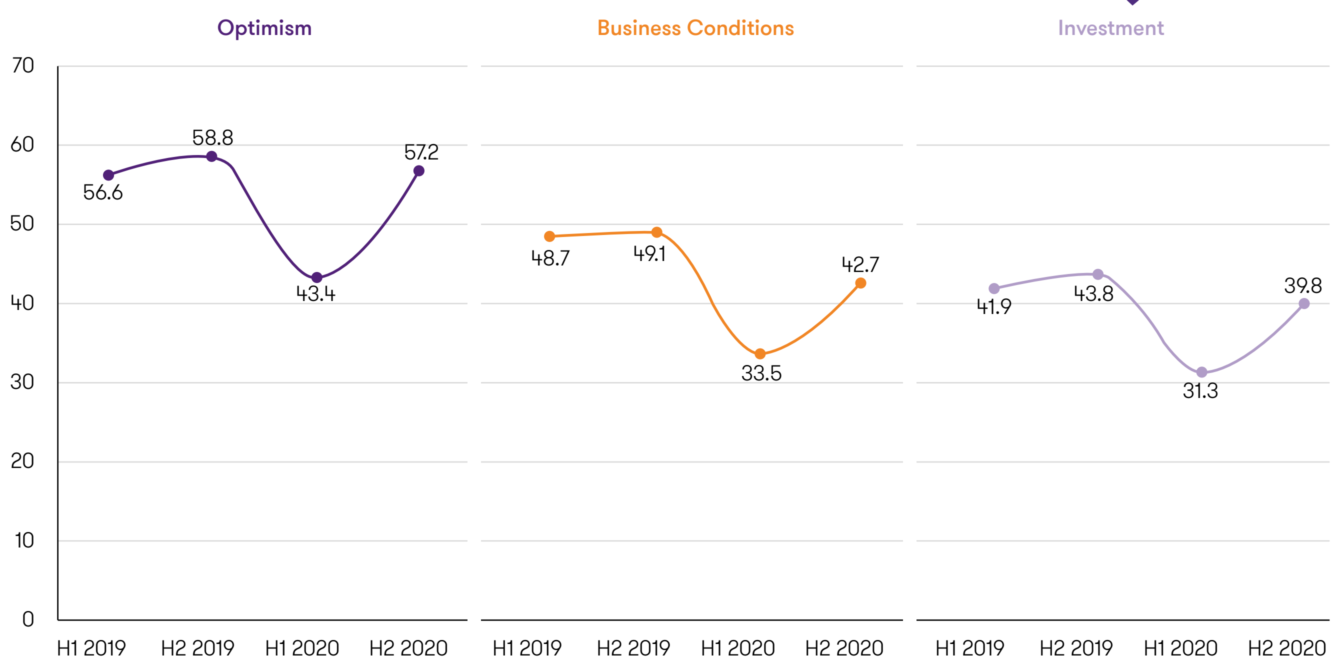
Improvement in outlook driven by high economic optimism, supported by improving growth expectations and investment intentions

Economic optimism improved over the last six months, up a strong 14 percentage points in comparison with H1 2020, with 57% of the firms reporting a slightly or very optimistic economic outlook for the next 12 months. This is only 2 percentage points off the pre-COVID-19 level in H2 2019 and comes off the back of a very weak H1 when global economic optimism was at its lowest level since the eurozone crisis of 2011-2012.

The outlook for business growth expectations is less optimistic. Only 45% of firms are expecting an increase in revenues in the next 12 months. Although this is a significant improvement on the 34% reported in H1 2020, it remains below the historical average (before H1, a value below 50% has occurred only once before since the inception of the IBR survey, in 2016). 44% of the firms expect an increase in profitability; a marked improvement on H1. The depressed outlook for revenues and profits highlights the difficulties faced by the firms due to continued lockdowns and ongoing weaknesses in economic activity.

Half (51%) of the firms are expecting to increase investment in technology in the next 12 months, while 44% will increase R&D investment. Although this is a significant improvement from H1 2020, it has still not recovered up to pre-COVID-19 levels.

Figure 7: All three components of outlook – economic optimism, business conditions and investment intentions – have improved in H2 2020



Improvements seen in demand constraints and economic uncertainty, but restrictions remain high due to worsening supply constraints

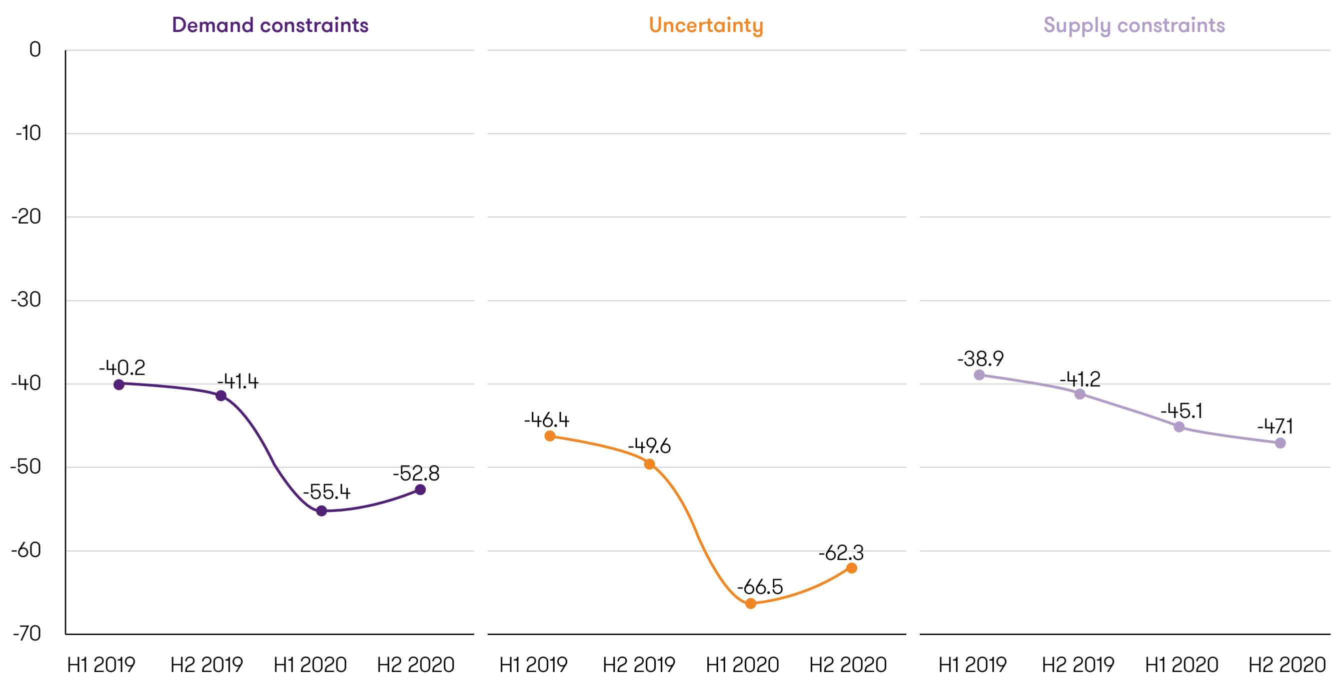
COVID-19 has led to a spike in economic uncertainty. Only a marginal improvement of 4 percentage points is apparent over the last six months, as 62% of the firms identified uncertainty as a business constraint (66% in H1 2020).

Shortage of finance remains a significant concern, with 46% of firms identifying it as a business constraint over the next 12 months. Meanwhile, those anticipating a shortage of orders to constrain business activity over the next 12 months dropped just 3 percentage points to 52% since H1 2020. This perhaps explains why expectations for revenues remain relatively low despite the pick-up in optimism.

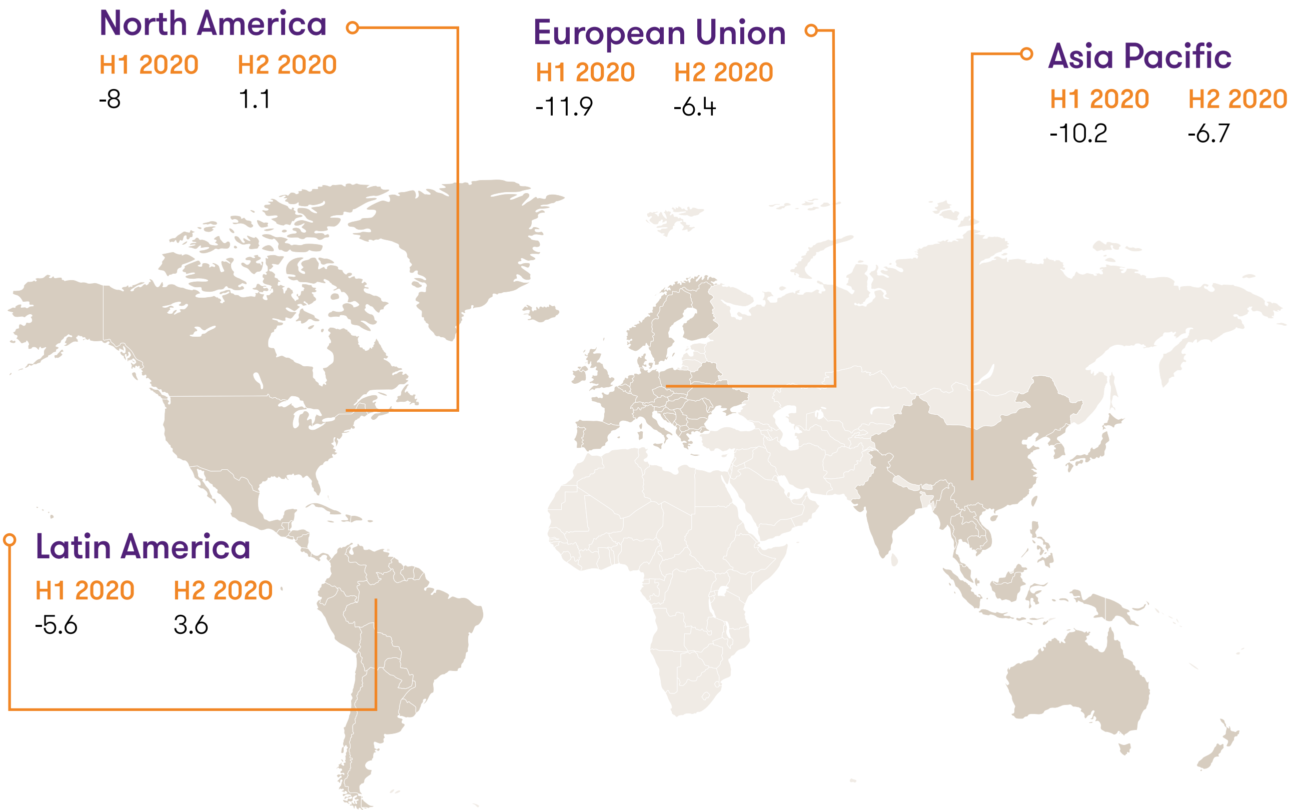
While many indicators have improved sharply over the last six months, it is important to note the context of these 'improvements, in many cases, is due to firms benchmarking the next 12 months against the very weak current environment due to the COVID-19 pandemic impact.

> "Challenge and Opportunity will mean the same in 2021. Organisations across the world are making long term investments in technology to keep operations going. Work from anywhere with flexible employment terms is now well-entrenched and organisations are also leveraging the growing ecosystem of gig workers. Organisations will need to be agile and learn to pivot quickly to cater to new markets, new products, or new customers. What we are sure of is more mid-market companies focusing on agility and sustainability to thrive in the age of disruption."
>
> **Pallavi Bakhru**
> Partner & Head – Private Client Services and Privately Held Business, India-UK corridor leader
> Grant Thornton Bharat

Figure 8: Improvements in demand constraints and economic uncertainty in H2 2020



Index negative in most key regions – besides North and Latin America – but improvement in all regions as mid-sized companies around the world start to recover

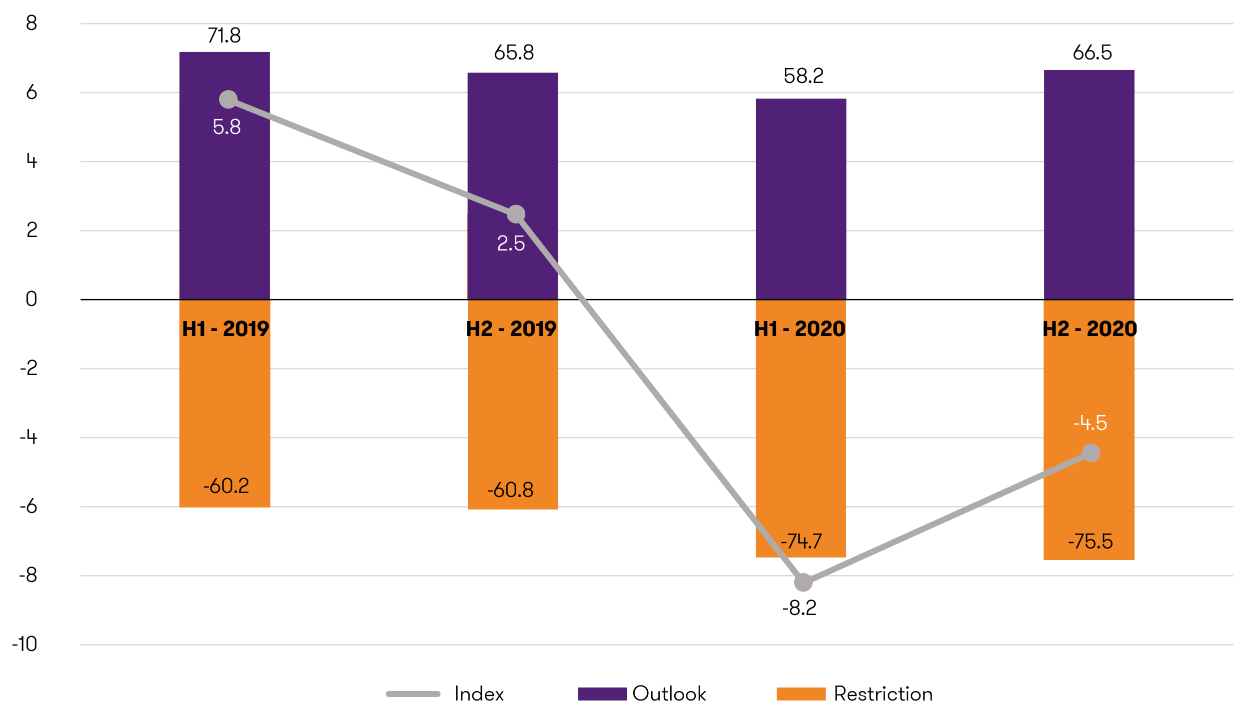


> India recorded a 13% growth in FDI in 2020, while fund flows declined in most major economies. Overall, deals between the US and India touched almost US$15 billion during the year, of which USD13 billion was inbound investment – increasing significantly from USD2.5 billion in the previous year, primarily driven by interest in the India tech stack, through two large ticket investments from Facebook and Google in Jio Platforms. Amidst the pandemic, India is being seen as a viable alternative for China in global supply chains. This change in outlook, coupled with accommodative foreign investment policies, is expected to further strengthen India's attractiveness as an investment destination.
>
> **Siddhartha Nigam**
> National Managing Partner,
> Growth and India-US corridor leader,
> Grant Thornton Advisory Private Limited

India Business Pulse

The India Business Pulse increased by 4 points in H2 2020, making up around 50% of the decline in H1 2020. It, however, remained in negative territory with a score of -4.5. The index turned negative in H1 2020, reflecting the impact of COVID-19 on business operating environments. As India has been one of the hardest hit nations by the pandemic, mid-market firms remain more cautious than other regions about the overall business outlook over the next 12 months.

Figure 10: India Business Pulse index



Improving business outlook propelled by increasing optimism

The outlook in H2 2020 is up by 8.3 points, propelled in large part by an improvement in economic optimism, with 71% of business leaders surveyed optimistic about the outlook of the country's economy over the next 12 months. This was up from 63% in H1 2020, at the height of the pandemic.

Despite the challenges caused by the pandemic, optimism levels in India remain well above the global levels of 57%. In fact, India ranked 3rd out of the 29 countries surveyed in terms of optimism on economic recovery.

Indian mid-market business growth expectations outperform global average

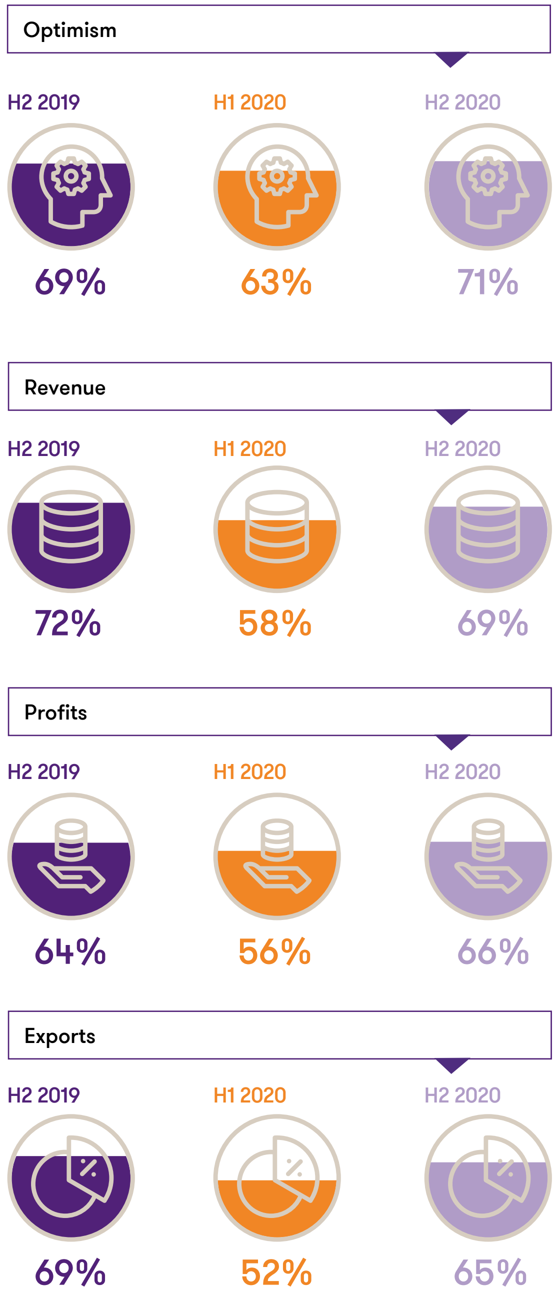
Revenue and profitability expectations are also up from H1 2020. Those firms expecting to increase revenue over the next 12 months is up 11 percentage points although still below 2019 figures. Profitability expectations improved by 10 percentage points from H1 2020 levels and have exceeded the expectations seen in H2 2019 with 66% of the Indian firms expecting to increase profits over the next 12 months.

External demand indicators have improved significantly, as export expectations over the next 12 months is up 13 percentage points from the first half of the year with 61% surveyed expecting to increase revenue from non-domestic markets over the next 12 months. India ranked highest out of the 29 countries surveyed in terms of increase in export expectations.

Indian mid-market intention to invest

The Indian mid-market firms also outperformed on intentions to invest. Over half of the firms surveyed intend to increase investment in both buildings and plant and machinery over the next 12 months. Investment intentions across intangible assets is also well above the global average, with 73% intending to increase investment in technology and 72% intending to increase investment in research and development (R&D). India ranked in the top three, out of the 29 countries surveyed, on percentage of business leaders expecting to increase investment across these areas.

Key expectations: Optimism, Revenue, Profits, Exports



Investment intent: Technology, R&D, New buildings, Plant & Machinery

Investment in technology

H2 2019	H1 2020	H2 2020
72%	68%	73%

Investment in R&D

H2 2019	H1 2020	H2 2020
66%	61%	72%

Investment in new buildings

H2 2019	H1 2020	H2 2020
57%	51%	58%

Investment in plant & machinery

H2 2019	H1 2020	H2 2020
61%	57%	61%

> “As a result of the COVID-19 pandemic, risk assessments in the current environment are unlike any others as businesses are dealing with significant changes to the economy, the environment and consequently their business and operations. Technology has been a key enabler to help organisations overcome many of the challenges caused by the pandemic. The survey shows that 73% of business leaders surveyed expect to increase investment in technology in the coming 12 months. The pandemic has also sped up the adoption of technology within the Audit profession, with auditors embracing and leveraging technology to drive comprehensive data analysis, perform additional audit procedures and to make professional judgements driven by a deeper understanding of the available information, in order to drive up audit quality and deliver a more efficient audit.”
>
> **Aasheesh Arjun Singh**
> Chartered Accountant, Bengaluru

Business constraints continue to worry mid-market businesses

Concerns over potential constraints remain elevated in India. As economic concerns stemming from the pandemic continue to worry the mid-market businesses in India, the restrictions, fell by 1 percentage point.

A sharp deterioration is also noted in economic uncertainty, supply and demand constraints in 2020 due to the impact of the pandemic. While the outlook index has modestly improved, the restrictions index has fallen 1 percentage point from six months ago and 15 percentage points from the same time last year (H2 2019).

The spike in economic uncertainty can be attributed to the pandemic and its impact in 2020. The H2 2020 results show only a marginal improvement of 1 percentage point, apparent over the last six months, with 80% of the firms stating uncertainty as a business constraint (81% in H1).

Almost 75% of the firms surveyed see a shortage of orders as a potential constraint to business activity, highlighting that demand conditions remain subdued despite the easing of lockdowns in H2 2020.

Shortage of finance remains a significant concern, with 75% identifying it as a business constraint over the next 12 months, followed by transport infrastructure and regulations at 73% and 71%, respectively. These results suggest that the underlying business operating environment remains challenging and the overall risk environment remains elevated, despite some cautious optimism.

> “Over the last year, companies have navigated uncharted territory and witnessed a range of new or magnified risks because of the pandemic. Cybersecurity was a key threat before COVID-19, and as digital transformation accelerates within organisations, it has become a vital focus area. Operations and supply chains face disruption and new third-party risks, while risks pertaining to finance and liquidity challenges are also heightened. Robust risk management practices are essential as businesses adapt their operating models and business processes to embrace the ‘new normal’, while also preparing to combat future challenges with greater resilience.”
>
> **Dinesh Anand**
> National Managing Partner - Risk & Private Equity
> Grant Thornton Bharat

Key business constraints

Constraint	H2 2019	H1 2020	H2 2020
Economic uncertainty	61%	81%	80%
Red tape	61%	72%	71%
Shortage of finance	58%	71%	75%
Availability of skilled labour	64%	69%	73%
Shortage of orders	60%	73%	75%
Transport infrastructure	58%	74%	73%

The road ahead

As businesses embrace the ‘new normal’ and expect a challenging economic scenario in the next 12 months, they are cautiously optimistic of recovery in the next 12 months. The return of consumer confidence, robust financial markets and an uptick in export growth expectations have been a key driver of this optimism.

With economy showing signs of V-shaped recovery, the rollout of COVID-19 vaccine will only boost the path. The pandemic has demonstrated the challenges and what needs to be done further to ensure the country does not lose its sight towards becoming a USD 5 trillion economy. The government through its budget announcements has sent a strong message to investors globally. It is committed to a long-term low tax rate regime, broad tax policy framework, boost the start-up ecosystem and adopt digital technology, innovation as well as research and development.

“Despite being one of the hardest hit by the pandemic, business leaders’ expectations for growth in revenue and profitability in India has improved from the first half of 2020, as they innovate and embrace the post-pandemic scenario. The announcements made in Budget 2021 will also give the country much-needed growth impetus. The government has stressed on ‘self-reliance’ with a focus on building robust infrastructure and domestic trade though capital expenditure, to revive economic growth and achieve India’s aspiration to become a USD5-trillion economy by 2026-27.”

Siddhartha Nigam
National Managing Partner,
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Grant Thornton Bharat is a member of Grant Thornton International Ltd. It has 4,500+ people across 15 offices around the country, including major metros. Grant Thornton Bharat is at the forefront of helping reshape the values in our profession and in the process help shape a more vibrant Indian economy. Grant Thornton Bharat aims to be the most promoted firm in providing robust compliance services to dynamic Indian global companies, and to help them navigate the challenges of growth as they globalise. Firm's proactive teams, led by accessible and approachable partners, use insights, experience and instinct to understand complex issues for privately owned, publicly listed and public sector clients, and help them find growth solutions.

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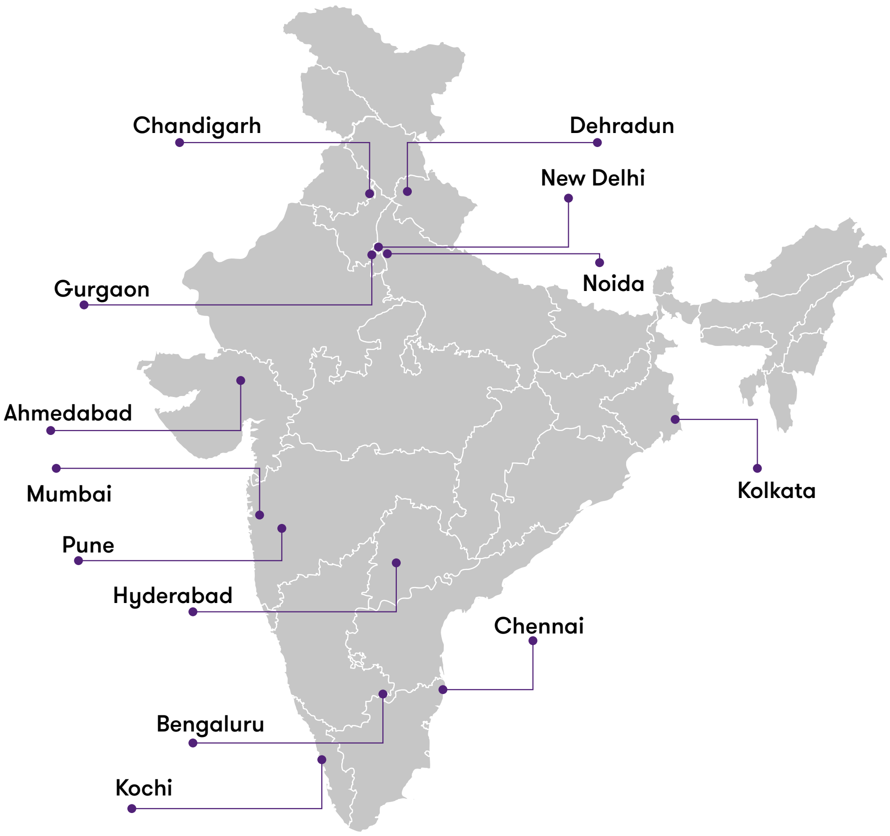

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