On Sustainable Growth

Devendra Kumar Vyas, Managing Director, Srei Equipment Finance, elaborates on the key factors that drive the growth and the emerging market trends in equipment finance.

The infrastructure sector is a key driver for the Indian economy and is largely responsible for propelling India's overall development. The government is focused on initiating policies to ensure the creation of a world-class infrastructure in India. Sectors such as Railways, housing and urban affairs, and roads and highways have witnessed increased year-on-year (y-o-y) Interim Budget allocations (excluding IEBR) for FY 2020 by 21 per cent, 12 per cent, and 6 per cent, respectively. The north-east sector has received a special focus in the Interim Budget 2018-19 with an allocation of Rs 581.66 billion, an increase of 21 per cent over the previous budget. This increased allocation is expected to have a positive impact on the construction, mining and allied equipment (CME) sector. These investment plans and projects have the potential to create the requirement of capital goods on a large scale and increase in the number of contractors executing these projects. Demand for infrastructure equipment and hence equipment finance is expected to grow as a result of all these developments.

CME market overview

According to Feedback Consulting, the CME industry has witnessed a good revival since FY 2015-16, preceded by a decline in the previous three years. The industry which grew by 20 per cent in FY18 (101,900 units) compared to FY17 (83,600 units) in terms of unit sales and is expected to see heightened business activities as the government is likely to invest heavily in infrastructure sector, thereby lifting business prospects in construction equipment sector.

The growth in equipment in fiscal 2018 came largely from material handling, concrete, material processing, earthmoving and mining equipment categories. Earthmoving machines form the majority of the total CME sales. This is largely attributed to the positive movement in select sectors such as national highways, irrigation and railways.

CME market outlook

According to Feedback Consulting, the CME industry is expected to grow at a CAGR of 14-15 per cent for the next three years until fiscal 2021 to reach a volume of 153,000 units. Going forward, there may be some disruptions in the industry both from a product and service perspective. Some likely developments include growth in pre-fabricated concrete business, increased usage of specialised equipment, rising manual labour costs, and digital drive.

CME financing overview

CME finance caters to all types of earthmoving, concrete, material handling, road construction, material preparation, tunnelling and drilling, and warehousing equipment. CME finance in India is offered by NBFCs, banks and captive or private financiers.

As the segment requires large capital expenditure, financing accounts for approximately 80-85 per cent of the total equipment purchased, and in the case of overseas purchases, it accounts for approximately 90 per cent. Most financing is procured through loans while leasing is the second most common mode of financing. Though the cost of construction equipment is approximately 10-30 per cent of the project cost, the presence of CME financiers assists in productivity and efficiency.

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Feedback Consulting estimated the total CME finance disbursement for fiscal 2018 to be approximately Rs 374 billion. Over the last six years, disbursements to the sector have grown at a CAGR of 10.9 per cent. During the recovery period of fiscal 2015 onwards the industry grew at a rate of 24.4 per cent.

Currently, the equipment finance industry has approximately 20-25 organised companies (NBFCs and banks) offering various products and services for the infrastructure equipment segment. According to a report by Feedback Consulting, Srei Equipment Finance (SEFL) leads the construction equipment finance market with a market share of approximately 33 per cent in fiscal 2018, distantly followed by HDFC at 14.1 per cent. Currently, SEFL is the only end-to-end solution provider

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across the entire CME value chain, from asset acquisition through to deployment, management and resale of the asset, and managing the customer relations across the entire asset life cycle.

CME financing outlook

The construction equipment finance industry is expected to grow at a CAGR of 20-21 per cent for the next three years until fiscal 2021. With the current announced projects which mostly have started from the third quarter of fiscal 2018, demand will continue for the earthmoving equipment industry, which will have a share between 68-70 per cent of the overall CME finance market. Banks and NBFCs are expected to have an equal share in the CME finance industry for the next one to two years with the equipment leasing industry expected to grow at a CAGR of 15-16 per cent until fiscal 2020.

Major trends in the CME financing industry

Going forward, revolutionary trends appear to be emerging in the equipment financing sector. These include:

- ***Integrated offerings:*** Dealers and OEMs are expected to offer customers integrated choice, which will include the equipment finance (and could also cover the lifecycle financing of the equipment).
- ***Automation of process:*** The current equipment financing takes anywhere between 5-30 days before the machine is handed over to the customer. Equipment financing companies need to move to the automation route, to sustain and survive in this technology-led market. A major differentiator could be transparency with a process to manage documentation, including, for example, EMI payments.
- ***Platform-based offering:*** Currently, there are a few companies which provide a platform for equipment owners and customers to interact and avail of equipment services. This could be a good opportunity for finance companies to participate and ensure that all finance needs are met.
- ***Managed services:*** Customer demand for greater flexibility and convenience will augment the use of nonstandard financing agreements. Shifts in customer preference for managed services (bundling equipment, services, supplies and software), pay-per-use leases and alternative financing will encourage equipment finance companies to find innovative ways to meet the demand.
- ***OEM tie-ups:*** Another trend worth noticing is tie-up of construction equipment majors with banks and non-banking financial institutions exclusively for their customers. This arrangement helps the OEMs to meet the level of financing support expected by their customers. The preferred financiers collaborate with OEMs and their dealers to offer enhanced quote and credit approval turnaround, allied with competitive financial solutions. The OEM and financier tie-up can be exclusive alliance or preferred financier tie-ups with the OEMs to avoid risk/loss pool arrangement, loss sharing arrangements, and subvention and credit days.