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# Plant & Machinery Valuations for MSME Projects

### Introduction:

Micro, Small, and Medium Enterprises (MSMEs) are vital to the economy, contributing significantly to employment and innovation. Accurately valuing plant and machinery is crucial for MSME projects, whether for securing financing, facilitating mergers, or conducting audits. This article explores the importance, methods, and challenges of

Valuing Plant and Machinery is a critical aspect of managing MSME projects. Accurate Valuations not only support financial reporting and compliance but also facilitate better decision-making for growth and sustainability. By understanding the methods, challenges, and best practices, MSMEs can navigate the Valuation process effectively, ensuring they harness the full potential of their assets.

### Importance of Valuation:

#### 01. Financial Reporting:

Accurate valuations help MSMEs comply with accounting standards and present a true financial picture, essential for stakeholders and investors.

#### 02. Securing Financing:

Lenders often require plant and machinery valuations as collateral for loans. A well-documented valuation can enhance the chances of securing funding.

#### 03. Mergers and Acquisitions:

In cases of buyouts or mergers, understanding the value of machinery can influence negotiations and strategic decisions.

#### **04. Insurance Purposes:**

Insuring plant and machinery requires accurate valuations to ensure adequate coverage and protection against losses.

#### **05. Taxation:**

Valuation impacts tax assessments, depreciation, and capital gains calculations, influencing the overall tax liability of the business.

### **Methods of Valuation:**

#### **01. Cost Approach:**

This method estimates the current cost of replacing the machinery minus depreciation. It's straightforward and often used when dealing with relatively new equipment.

#### **02. Market Approach:**

This method involves comparing the asset to similar assets sold in the market. It requires extensive market research and can be challenging due to the uniqueness of many MSME assets.

#### **03. Income Approach:**

This method calculates the expected income generated by the machinery, discounted to present value. It is particularly useful for specialized machinery that produces unique products.

#### **04. Hybrid Approaches:**

Sometimes, a combination of the above methods provides a more accurate valuation, particularly for complex assets.

### **Challenges in Valuation:**

#### **01. Lack of Standardization:**

The MSME sector often lacks standardized valuation practices, making it difficult to establish a benchmark.

#### **02. Data Availability:**

Access to reliable market data can be limited, hindering the market approach.

#### **03. Rapid Technological Changes:**

The fast pace of technological advancements can quickly render machinery obsolete, affecting valuations.

#### **04. Subjectivity:**

Valuations can sometimes be subjective, depending on the appraiser's expertise and experience, leading to potential discrepancies.

#### **05. Project Evaluation before approval:**

There is no evaluation process by a technical team or a Valuer before sanctioning any project from MSME for the exact value of the project for all the Plant &

Machinery and the technological feasibility of the equipment used for the project.

#### **06. Banks/ Financial Institutes:**

Banks or any financial institutes supporting the customer in such projects have not considered the Valuers support before sanction of the loan amount for the following evaluation:

- a. Whether the Value of the machineries presented in the project report/quotations by the vendors are fair if it aligns with the current market rates or inflated as compared with the average price for the similar models and specifications.
- b. Whether the machineries are suitable and technologically feasible to the current usage in similar manufacturing processes.
- c. Selected vendors are reliable in providing good services after sales and are technologically capable of supporting smooth operations in future etc.,

#### **Best Practices to be suggested/advised to MSME and Financial Institutes:**

Looking at the present processes at MSME and the financial Institutes, Plant & Machinery Valuers find following lacuna in the system, especially during the Valuation-subsidized projects, plants and machineries:

1. MSME Sanctioned Projects funded by banks based on the approval of subsidy scheme and Detailed Project Report (DPR) with quotations from the machinery vendors for the required machinery to set up a process / production plant and the other documents like KYC, Collateral assets etc., which legal department in the bank scrutinize and approve. During this process no valuer is involved in the system to evaluate the technical feasibility and the for the cost of the machineries. Once the Loan is sanctioned and equipment has arrived at site, only Bank people will do the inspection and take the pictures of the machines, releasing 100% of the loan amount.
2. If the Customer has got the sanctioned loan with Working Capital as well, Bankers then ask for the installation certificate from the Valuer. It is the responsibility of the Valuer then, to identify the equipment and its suitability for the process or manufacturing planned on that particular equipment and machinery. It was found that there is no relevance in the equipment installed to the information provided on the DPR before sanctioning the loan.
3. In some cases, customers have misused the loan amount by providing the fake invoices from a shell company and managed to sanction the loan, taking 100% disbursement on the invoice.
4. Valuer will come into picture at the stage of Installation of the machinery in some cases or otherwise, only when the revaluation of the machinery is required after a year or so, when the customer fails to repay a few installments.

To avoid such misuse of schemes made available by the Government like PMEGP, PMMY, SUI, CGTMSE, etc., either MSME or the Banks must install a system in the process to evaluate the Project Report submitted by the borrower with any scheme, sanctioned through MSME .

Or, the Valuer must be involved in the process of MSME sanctioning system for any such schemes for the evaluation and right budgeting of the proposed projects.

In this regard I would appreciate IOV, for taking initiative with the concerned MSME department and Indian Bank Association to implement the following:

### **01. Engage Qualified Valuers:**

Employ professional Valuers with expertise in MSME machinery to ensure accuracy and reliability. (at MSME dept. or FIs)

### **02. Document Thoroughly:**

Maintain detailed records of all machinery, including purchase invoices, maintenance records, and usage history, to support the valuation process.

### **03. Stay Updated:**

Regularly update valuations to reflect changes in market conditions, technology, and business operations.

### **04. Use Multiple Methods:**

Consider employing more than one valuation method to cross-verify results and increase reliability.

### **Conclusion:**

Valuing Plant and Machinery is a critical aspect of managing MSME projects. Accurate Valuations not only support financial reporting and compliance, but also facilitate better decision-making for growth and sustainability. By understanding the methods, challenges, and best practices, MSMEs can navigate the valuation process effectively, ensuring they harness the full potential of their schemes/assets.

