

# APPENDICES

## APPENDIX – I

### BANKS' FINANCING OF SMALL SCALE INDUSTRIES IN TAMILNADU WITH SPECIAL REFERENCE TO SIVAGANGA DISTRICT

#### QUESTIONNAIRE

*(Administered to the owners of small scale industries)*

#### 1. PROFILE OF THE UNIT:

1.1 Date of establishment of the unit:

1.2 Industry Category: (tick  the relevant item )

- |   |                          |
|---|--------------------------|
| 1.2.1 Food products, Beverages, & Tobacco products  | <input type="checkbox"/> |
| 1.2.2 Textile products                              | <input type="checkbox"/> |
| 1.2.3 Wood, paper and leather products              | <input type="checkbox"/> |
| 1.2.4 Rubber, Plastic, Petroleum, and coal products | <input type="checkbox"/> |
| 1.2.5 Chemical products                             | <input type="checkbox"/> |
| 1.2.6 Non-Metallic mineral products                 | <input type="checkbox"/> |
| 1.2.7 Engineering products                          | <input type="checkbox"/> |
| 1.2.8 Other industries                              | <input type="checkbox"/> |

1.3 Investment category:

[ i.e., investment in plant and machinery ]

- |  |                          |
|--|--------------------------|
| 1.3.1 Very Low [Below Rs.1 Lakh ]              | <input type="checkbox"/> |
| 1.3.2 Low [Above Rs.1 Lakh to Rs.2 Lakhs]      | <input type="checkbox"/> |
| 1.3.3 Medium [Above Rs.2 Lakhs to Rs.5 Lakhs ] | <input type="checkbox"/> |
| 1.3.4 High [Above Rs.5 Lakhs to Rs.30 Lakhs ]  | <input type="checkbox"/> |
| 1.3.5 Very high [Above Rs.30 Lakhs ]           | <input type="checkbox"/> |

## 1.4 Form of Ownership:

	At the time of commencement/ Acquisition	At present
1.4.1 Proprietary	[ ]	[ ]
1.4.2 Partnership	[ ]	[ ]
1.4.3 Private Ltd., Company	[ ]	[ ]
1.4.4 Co-operative Society	[ ]	[ ]
1.4.5 Public Ltd., Company	[ ]	[ ]

## 1.5 Mode of acquisition of business:

- 1.5.1 Started by the Proprietor/Partners/Members [ ]
- 1.5.2 Inherited [ ]
- 1.5.3 Outright purchase [ ]
- 1.5.4 Taken on lease [ ]

## 1.6 Give reasons for starting the unit:

- 1.6.1 Possessing technical qualification [ ]
- 1.6.2 Possessing technical experience [ ]
- 1.6.3 Availability of concessions from the Government [ ]
- 1.6.4 Availability of finance from own resources [ ]
- 1.6.5 Financial accommodation from institutions other than banks [please specify the name of the institution] [ ]
- 1.6.6 Financial accommodation from banks [please mention the name of the bank and its address] [ ]
- 1.6.7 Market potential [ ]
- 1.6.8 Any other [please specify] [ ]

## 1.7 Location of the unit:

- 1.7.1 Semi-urban [ ]
- 1.7.2 Rural [ ]
- 1.7.3 Industrial estate [ ]

## 1.8 Factors which influenced the location of the unit:

- |   |     |
|---|-----|
| 1.8.1 Easy availability of land/building          | [ ] |
| 1.8.2 Own land / building                         | [ ] |
| 1.8.3 Government concession for industrial estate | [ ] |
| 1.8.4 Raw materials availability                  | [ ] |
| 1.8.5 Labour availability                         | [ ] |
| 1.8.6 Good market than in the other areas         | [ ] |
| 1.8.7 Availability of good infrastructure         | [ ] |

## 1.9 Nature of business:

- |                     |     |
|---------------------|-----|
| 1.9.1 Manufacturing | [ ] |
| 1.9.2 Job work      | [ ] |

## 1.10 Whether the unit is registered under Factories Act?

YES/NO

## 1.11 Do you have any other business other than this?

YES/NO

## 1.12 Number of persons employed in your unit:

Men

Women

- |                                 |  |  |
|---------------------------------|--|--|
| 1.12.1 Casual labour            |  |  |
| 1.12.2 Labour under muster roll |  |  |

## 1.13 Do you receive any concession for employing women for more than 30% of the work force ?

YES/NO

If yes, in what way? [please specify]

**2. LONG TERM FINANCE:**

2.1 Amount of long term finance obtained for purchase of fixed assets :

Source	At the beginning (Rs. lakhs)	At present (Rs. lakhs)
2.1.1 Own funds		
2.1.2 Commercial banks		
2.1.3 Financial institution		
2.1.4 Friends and Relatives		
2.1.5 Private financiers		
2.1.6 Other sources {pl. specify}		
Total		

2.2 Did you receive composite loan [both long term and working capital loan at a time] for setting up of the unit?

YES / NO

If yes, from which source?

Source:

Name:

Amount Rs.:

2.3 What special benefits you have availed of from this scheme?

- |   |     |
|---|-----|
| 2.3.1 Speedy sanction / release of loan | [ ] |
| 2.3.2 Low rate of interest              | [ ] |
| 2.3.3 High moratorium period            | [ ] |
| 2.3.4 Any other (Please specify)        | [ ] |

2.4 Please specify the time lag between the loan application and loan sanction :-

- |                            |     |
|----------------------------|-----|
| 2.4.1 Before 30 days       | [ ] |
| 2.4.2 After 30 days        | [ ] |
| 2.4.3 You did not remember | [ ] |

2.5 Subsidy received by your unit: - YES/NO  
Amount Rs.

2.6 Did you apply for bank/institutional loan for an existing unit or for a new unit to be set up.

2.6.1 For an existing unit

2.6.2 For a new unit

2.7 Purpose/utilisation of long term funds :

2.7.1 Acquisition of land

2.7.2 Construction of factory building

2.7.3 Purchase of machinery & equipment

2.7.4 Other [please specify]

2.8 Was there any diversion of long term loan for any purpose other than for which it was sanctioned?

YES / NO

2.9 What was the starting equity [own funds] to long term borrowings ratio?

2.10 What is the present equity ratio?

2.11 Do you know the basic requirements of capital structure – for instance proportion between own funds and borrowings, that the unit to have a strong equity, etc., ?

YES / NO

2.12 How much did the bank /financial institution insist as your contribution (give in percentage).

2.13 Are you aware of the following equity financial schemes of the SIDBI Government?

2.13.1 Seed capital assistance scheme

2.13.2 National equity fund scheme

2.13.3 Mahila Udayam Nidhi scheme of SIDBI

2.13.4 Special scheme of assistance of SIDBI to Ex-service men

2.14 Did you avail of any financial assistance from any of the above schemes mentioned?

YES/NO

If yes, how much? [please mention the name of the scheme]

2.15 What were the problems that you faced for getting term loan? (please rank the item as 1,2,3 ).

	Rank
2.15.1 Delay in processing the application	[ ]
2.15.2 More formalities	[ ]
2.15.3 High cost of financing	[ ]
2.15.4 Cumbersome procedures	[ ]
2.15.5 Security insistence	[ ]
2.15.6 No problems faced	[ ]
2.15.7 Any other (please specify)	[ ]

2.16 What are the problems that you faced in repaying the term loan? [please rank the item as 1,2,3 ].

	Rank
2.16.1 High cost of financing	[ ]
2.16.2 Low moratorium period	[ ]
2.16.3 High instalment due	[ ]
2.16.4 Under financing	[ ]
2.16.5 Non-realisation of accounts	[ ]
2.16.6 No problems faced	[ ]
2.16.7 Any other [please specify]	[ ]

2.17 Have you at any time failed to repay the loan instalment due?

YES/NO

If yes, state the reason -

2.18 Have you faced any recovery action from the lending institution?

YES/NO

2.19 Any harassment shown by bank officials in the recovery of loan?

YES / NO

If yes, can you say in what way?

2.20 Any long term loan received by your unit as the loan for expansion /diversification, etc.

YES/NO

If yes, give details -

Name of the institution:      Security given:      Amount of loan:  
(in rupees)

2.21 What are the measures taken by you to improve/strengthen the equity?

2.21.1 Making use of surplus profit to increase equity	[ ]
2.21.2 Increasing promoter's contribution	[ ]
2.21.3 Any other [please specify]	[ ]

2.22 What suggestions would you like to offer to strengthen equity?

1. \_\_\_\_\_

2. \_\_\_\_\_

3. \_\_\_\_\_

### 3.WORKING CAPITAL LOAN :

3.1 Which is the main factor deciding your working capital needs?

Raw materials/Wages/Stock of finished goods/Power / Any other  
(please specify).

3.2 What is the periodicity of your working capital need?

Per Month / Quarterly / Half yearly / Yearly

Rs.

3.3 How do you determine your working capital needs?

3.3.1 Past experience [ as a % of production / sales ]	[ ]
3.3.2 Some rule of thumb	[ ]
3.3.3 Any other [please specify]	[ ]

3.4 Do you have any accounting method to calculate your working capital needs?

YES/NO

If yes, what is it?

3.4.1 Cash flow statement / Fund flow statement

[ ]

3.4.2 Any other [please specify]

3.5 Bank loan:-

	1993	1994	1995
	Rs.	Rs.	Rs.

Sanctioned

3.6 Are you aware of the basic requirements of management of working capital - e.g., cash planning, inventory control, debtors management, etc.

YES/NO

3.7 Do you bring own money to the business for working capital?

YES/NO

3.8 Have you borrowed from relatives / friends/and other unorganised sector for meeting the working capital needs?

YES/NO

If yes, please mention the amount Rs.\_\_\_\_\_ and at what rate of interest?

3.9 What is the credit period you allow for your sales?

3.10 What is the credit period you avail of for the purchases?

3.11 The shortage of working capital is felt in the area of:

	Always	Seasonal
3.11.1 Cash		
3.11.2 Inventories		
3.11.3 Any other [please specify]		

3.12 The shortage of working capital affects the unit in:

- |   |     |
|---|-----|
| 3.12.1 The cost of production             | [ ] |
| 3.12.2 Delay in the process of production | [ ] |
| 3.12.3 Losing the sales opportunity       | [ ] |
| 3.12.4 Any other [ please specify ]       | [ ] |

3.13 Do you conduct periodic review of working capital?

YES/NO

3.14 Which of the following ways of financing for working capital do you consider as the best method?

Cash credit / Over draft / Bills finance / Export finance / Local money Lenders/ Friends and Relatives / working capital loan/own business source/ Others [please specify].

3.15 At what percentage of interest your bank sanctioned working capital loan?

3.16 What is the reason for slow repayment of loans ?  
(please rank the items as 1, 2,3]

- |   | Rank |
|---|------|
| 3.16.1 Slow moving stock                  | [ ]  |
| 3.16.2 Higher credit period for customers | [ ]  |
| 3.16.3 Lower credit period from suppliers | [ ]  |
| 3.16.4 Advance payment to suppliers       | [ ]  |
| 3.16.5 Any other [please specify]         | [ ]  |

3.17 What kind of problem did you encounter in raising working capital loan?

- |                                   | Rank |
|-----------------------------------|------|
| 3.17.1 Under financing            | [ ]  |
| 3.17.2 Delayed financing          | [ ]  |
| 3.17.3 High cost of financing     | [ ]  |
| 3.17.4 Untimely financing         | [ ]  |
| 3.17.5 More formalities           | [ ]  |
| 3.17.6 Insistence on security     | [ ]  |
| 3.17.7 Any other [please specify] | [ ]  |

3.18 In the light of the past experience what suggestions would you like to offer to improve the amount of working capital?

- 1.
- 2.
- 3.

#### 4. OPERATING PERFORMANCE:

4.1 Your unit's performance in terms of:

	1994	1995	1996
Net Sales	Rs.		
Gross Profit	Rs.		

4.2 What did you think as the reason for increase/ decrease in profit?  
[please specify]

4.3 Do you export your products? YES/NO

4.4 What was the amount of your exports during the past 3 years?

1993	1994	1995
Rs.	Rs.	Rs.

4.5 Any National /State / District level awards won by your unit:  
[please give details].

4.6 Which is the main constraint that prevents your organisation to develop further?

- |                                   |     |
|-----------------------------------|-----|
| 4.6.1 Financial constraints       | [ ] |
| 4.6.2 Technical obsolescence      | [ ] |
| 4.6.3 Poor market for the product | [ ] |
| 4.6.4 Stiff competition           | [ ] |
| 4.6.5 Shortage of raw materials   | [ ] |
| 4.6.6 Frequent power cut          | [ ] |
| 4.6.7 Any other [please specify]  | [ ] |

4.7 The problem of finance arises in your unit , due to:-

- |   |     |
|---|-----|
| 4.7.1 Inadequate bank credit                          | [ ] |
| 4.7.2 Higher cost of materials and operating expenses | [ ] |
| 4.7.3 Delayed payments by customers                   | [ ] |
| 4.7.4 High cost of borrowing                          | [ ] |
| 4.7.5 Any other [ please specify ]                    | [ ] |

## 5. MISCELLANEOUS:

5.1 In which bank the account of your unit is operated?

Name of the Bank	Current A/c	Savings Bank A/c
------------------	-------------	------------------

5.2 Do you operate the bank account of the unit in the name of the unit?

YES / NO

If not, state the reason

5.3 Do you have any personal account other than the account of unit for the unit's transactions?

YES / NO

5.4 Who looks after the accounting function of your unit?

Self / Accountant / Manager

5.5 If you do not adopt proper accounting system, is it because of the following factor [s]?

- |   |     |
|---|-----|
| 5.5.1 Not much business transactions                                    | [ ] |
| 5.5.2 Not necessary as the business and the personal money are the same | [ ] |
| 5.5.3 Highly expensive in the form of stationery and employees' salary  | [ ] |
| 5.5.4 Any other [please specify]  | [ ] |

5.6 Are you a member of any SSI Association/Chamber of Commerce or any other business association?

YES/NO

If yes, mention its name.

## APPENDIX - II

### BANKS' FINANCING OF SMALL SCALE INDUSTRIES IN TAMILNADU WITH SPECIAL REFERENCE TO SIVAGANGA DISTRICT

#### DATA SHEET

*(Administered to the bankers in Sivaganga district)*

#### PROFILE

1. Name of the bank:
2. Mailing Address:
3. Designation of the respondent:
4. Location of your branch:  
Semi-urban / Rural
5. Total no. of industrial accounts with your branch as on 31.3.96
6. Total no. of SSI loan accounts with your branch as on 31.3.96
7. No. of SSI units financed by your branch that were sick (with classification if any) as on 31.3.96.
8. Is your branch, a separate SSI branch ? YES / NO
9. If no, does your bank have a separate section for SSIs ?

#### FINANCIAL ASSISTANCE

1. Amount sanctioned, disbursed and outstanding by your branch to SSI units (i.e., to all categories under SSI sector).

( Rs. in lakhs )

	YEAR		
	1993-94	1994-95	1995-96
Sanctioned			
Disbursed			
Outstanding			

2. List the schemes that are in operation for financing SSI units in your branch.

I. Refinance scheme:

- (a) Single Window Scheme
- (b) General Schemes
- (c) Any other schemes (pl. specify)

II. Bills schemes

- (a) Bills Discounting
- (b) Any other schemes (pl. specify)

3. Where do you get refinance for advances made to SSI sector ?

SIDBI / NABARD / OTHERS (pl. specify)

4. Total amount of loan sanctioned to SSI units as on 31.3.96

No. of A/cs                      Amount Rs. (in lakhs)

- (a) Term loan only
- (b) Working Capital loan only
  - (i) Open Cash Credit
  - (ii) Cash credit
  - (iii) Overdraft
  - (iv) Any other (pl. specify)
- (c) Both term loan and working capital loan
- (d) Any other schemes of loan (pl. specify)

5. What kind of problem/hardship do you face in dealing with SSI loan accounts (please rank the important ones as 1,2,3, etc.)

	Working Capital	<b>RANK</b> Term Loan	Composite Loan
(i) Provision of inadequate security for loan			
(ii) Irregular repayment of principal and interest			
(iii) Closing down of units (due to poor management)			
(iv) Diversion (i.e., misuse) of loan/funds			
(v) Under utilisation of working capital limit			

- |  | Working<br>Capital | RANK<br>Term<br>Loan | Composite<br>Loan |
|--|--------------------|----------------------|-------------------|
| (vi) Not knowing the financial management or general management principles (as proper utilisation of funds, ploughing back of profits, etc.) |                    |                      |                   |
| (vii) Poor maintenance of accounts   |                    |                      |                   |
| (viii) Any other (pl. specify)   |                    |                      |                   |
6. What in your opinion, is the reason(s) for the low rate of recovery of bank loan, particularly with SSI accounts ?

Factor	SA	A	N	D	SD*
(i) No assured marketing					
(ii) Sub-standard quality of Materials / goods					
(iii) Loopholes in recovery Acts/Laws					
(iv) Misuse of funds					
(v) Mis-identification of sick units					
(vi) Lack of integrity of borrower					
(vii) Under finance					
(viii) Lack of consortium advances					
(ix) Expecting some subsidy/concessions					
(x) Delay in sanction					
(xi) Under utilisation of plant capacity					
(xii) Low profitability					
(xiii) Vulnerable to sickness					
(xiv) Wilful default					
(xv) Any other (pl. specify)					

\* SA = Strongly agree, A = Agree, N = Neutral, D = Dis-agree, SD = Strongly dis-agree

7. How do you rate the recovery of loan to SSI units in your bank?

Excellent / Satisfactory / Poor

8. What is the percentage of recovery of loan against demand?

9. What are the services you render to SSI units other than loan facility?

- |                               |     |
|-------------------------------|-----|
| (i) Marketing assistance      | [ ] |
| (ii) Training programmes      | [ ] |
| (iii) Counseling services     | [ ] |
| (iv) Regular meetings         | [ ] |
| (v) Monitoring and follow-up  | [ ] |
| (vi) Technical assistance     | [ ] |
| (vii) Any other (pl. specify) | [ ] |

10. From your rich experience in the field, what suggestions would you like to offer to tackle the problems in financing the SSI units?

- |  |     |
|--|-----|
| (i) EDP training   | [ ] |
| (ii) Courses on financial management   | [ ] |
| (iii) Close monitoring of units which may turn sick  | [ ] |
| (iv) Power to inspect the premises and to have access to books of accounts of units which are irregular in repayment | [ ] |
| (v) Marketing assistance to units which find hard to market their products   | [ ] |
| (vi) To provide compulsory ombudsman services meant for SSI units  | [ ] |
| (vii) Any other (pl. specify)  | [ ] |

11. Have you ever before instituted any legal proceedings against the defaulting SSI units?

YES / NO

If Yes, give the number of suits in the legal courts during the previous 3 years.

12. No. of suits settled during the year 1995-1996 (if any)

In favour of the bank:

In favour of the borrower:

13. After how many defaults, have you resorted to legal action through courts?

14. If you do not file a suit against the defaulting borrowing units on the basis of number of defaults made, do you take legal action against the defaulting unit with reference to time period involved ?

YES / NO

If Yes, What is the time period after which you would prefer to resort to legal action ?

1 Year / 2 years / .....

15. How do you consider about the Law of Limitation ( in relation to SSI advances) ?

- (i) The law compels a banker to file a suit for default in repayment of bank loan. (i.e., within 3 years)
- (ii) The Law makes it necessary to renew the contract for loan every three years.
- (iii) There is a chance that the loan may become time barred.

16. Would you like to suggest that the law of limitation for loan from banks should be for more than 3 years ?

Yes / No

If Yes, suggest the time period.

## APPENDIX -III

## INDUSTRY CLASSIFICATION OF SMALL INDUSTRIES

MAJOR INDUSTRY GROUP CODE NUMBER OF SIDO	DETAILS OF INDUSTRY	PRESENT STUDY GROUPS
20 & 21	Food products	Food products and Beverages = 1
22	Beverages, tobacco and tobacco products	
23	Cotton textiles	Textile products = 2
24	Wool, silk & synthetic fiber textiles	
25	Jute hemp, & mesta textiles	
26	Textiles products (including Weaving apparels other than footwear)	
27	Wood and wood products, furniture and fixtures	Wood, paper and leather = 3
28	Paper and paper production, printing Publishing and allied activities	
29	Leather and fur products (except repair)	
30	Rubber, plastic, petroleum and coal products	Rubber, plastic, petroleum and coal products = 4
31	Chemical & chemical products (except Products of petroleum and coal)	Chemical & chemical products (except products of petroleum and coal) = 5
32	Non-metallic mineral products	Non-metallic mineral products = 6
33	Basic metal alloys	Engineering products = 7
34	Metal products and parts (except Machinery and transport equipments )	
35	Machinery and machine tools and parts (except electrical machinery)	
36	Manufacture of electrical machinery and Apparatus (and supplies and parts)	
37	Transport equipments and parts	
38	Other industries	Other industries = 8

Source : Directory of Category of Small Scale Industrial Units Registered (As on 31.12.1987)  
Small Industries Development Corporation of Tamilnadu, Chennai.

APPENDIX -IV

WORKERS' STRENGTH IN SAMPLE SMALL INDUSTRIAL UNITS (TALUK-WISE AND FINANCE UTILISATION-WISE)

No. of workers	FUC	Karaikudi		Sivaganga		Tiruppattur		Manamadurai		Devakottai		Elayangudi	
		M	F	M	F	M	F	M	F	M	F	M	F
Less than 5 workers	B	18	11	22	1	10	5	5	6	5	4	3	1
	F	3	3	3	1	2		1	1	1	1		
	O	11	2	2		7	2			3	4	1	
Above 5 less than 9 workers	B	8	3	3	1	1		10	2	3			
	F					2	1	1		2			
	O	3	2			2							
Above 9 less than 20 workers	B	11	1	1		1		4	3	2	1		
	F	1	1					1	1	1	1		
	O	4	2			2	1	2					
Above 20 workers	B	2				1	1	3		1	1		
	F	2	1				2						
	O		1		1								

Source: Primary data

## APPENDIX – V\*

### Management of Working Capital in Small Scale Industries in India

R. Neelamegam

R. Maria Inigo

In India a large majority of the sick industrial units representing 99.1% were in SSI sector. The most important reason of sickness in small scale industrial units was the insufficient amount of working capital, late receipt of working capital and heavy dependence on other sources of finance. It is evident that small scale industries sector is vulnerable to sickness mainly due to financial insufficiency. Hence, a proper management of finance in small scale industries sector assumes greater significance.

Financing describes the management of capital sources. Investing describes the management of capital uses. The set of management duties and responsibilities that centers around these two functions is referred to as financial management.

Many entrepreneurs are highly motivated to work for long hours, but their business concerns often collapse because they spend much time on performing non-management tasks and neglect the essential, more difficult and very challenging task of management, which brings the firm to a desired shape. Management of finance is an important function in a business concern. For a small industrial unit, with a low withstanding power, it is highly important to have a close look on the management of finance. In India, in March, 1992 of the total number of sick industrial units, (encompassing all scales of industrial units), a large majority of these sick industrial units representing 99.1% were in the SSI sector. A study conducted by the Federation of Indian Chamber of Commerce and Industry (FICCI) in 1988 identified that the most important reason of sickness in small scale industrial units was the insufficient amount of working capital, late receipt of working capital, and heavy dependence on other sources of finance. The study further disclosed that problems both in long term and short term finance accounted for 43 percent of sickness in SSI sector. It is evident that small scale industries sector is vulnerable to sickness mainly due to financial insufficiency. Hence, a proper management of finance in small scale industries sector assumes greater significance.

Working capital represents the portion of capital that circulates from one firm to another in the ordinary conduct of business. This idea embraces the recurring transition from cash to inventories to receivables to cash that forms a conventional chain of business operations.

#### Sources:

The sources of industrial finance (for long term and short term) may be conveniently grouped under two heads, namely, institutional finance and non-institutional finance. The institutional finance is directed and controlled by the central Government through the central banking system, namely, the Reserve Bank of India.

Working capital assistance to SSI is available from commercial banks, as well as from the specialised financing agencies like Small Industries Development Bank of India (SIDBI), State Financial Corporations (SFC) which earlier concentrated only on refinancing and term lending. Financial assistance to SSI units is available against pledge or hypothecation of stock of raw materials, semifinished goods and finished goods.

The Nayak Committee set up to look into the credit flow to SSIs has recommended that at least 20% of projected annual turn over subject to a limit of Rs. One crore (earlier Rs. 50 Lakhs, subsequently

\* This research paper, published in 'Abhigyan'-Autumn 1996 issue,

raised to this limit) shall be provided as working capital. The SSI units would be required to bring in 5% of projected annual turn over as margin, but in reality, tiny units get only 3% and even units with 5 to 10 lakhs turn over get only about 12 to 13% of their turn over on working capital. Whereas banks financing of working capital to total turn over in respect of large and medium industries was about 19.4 percent as in March, 1990, the similar ratio for SSI sector as a whole was only 8% percent which is not even a 50% requirement of the large and medium sectors.

#### **Determinants of Working Capital**

The Factors determining the working capital may differ from industry to industry. A careful approach has to be made to decide the optimum level of requirement of working capital. The following factors normally decide on the amount of working capital; they are, cost of raw materials, power, wages, credit period to customers, credit period of debtors, stock of finished goods, stock of raw materials required for uninterrupted and so forth.

#### **Cash**

Money required to meet the day today expenses is deemed here as cash. Besides the funds required for procuring raw materials, and the funds that would be locked up in semi-finished goods and finished goods, a minimum level of cash is required for miscellaneous expenses over the counter. It also decides on the level of working capital required for an enterprise.

#### **Inventory**

Inventory occupies the most important role in deciding the amount of working capital. It includes raw materials, semi-finished goods and finished stock of goods. The optimum allocation of working capital on inventories will maximise profit. Over investment or under investment may increase the cost of production. Hence, to bring down cost of production, inventory management becomes inevitable in a manufacturing industry; particularly in small scale industry which is most vulnerable to sickness. So, a small manager's concern with regard to inventory should be the following:-

- To find out the Economic Order Quantity [EOQ]. This will help in avoiding accumulation or shortage of raw materials. For deciding the above ordering level, consideration shall be given to the nature of the product, time taken for conversion of raw materials to finished goods, the prevailing market condition for raw materials and the like.

- The production cycle decides on the stock of finished goods as well as the "work in progress". The optimum level of working capital required to cope up with the situation shall be arranged by predicting the production cycle.

#### **Receivables**

Small business concerns suffer short of working capital because of non realisation of sales at the right time. Due to such difficulty faced by SSI units, the Delayed payments Act was passed. It enables the SSI units to get money within a period of 30 days from the date of sales to big units. But in practice, many units do not go for any litigation even if the payment is delayed beyond 30 days. The reason is they do not want to lose the large customers for this sole act.

A small entrepreneur is warned of to have a proper 'management of receivables'. If receivables are not realised within a reasonable time, the 'cost of interest' (on the amount locked with customer) will be an additional burden to the entrepreneur. Normally, small business owners meet such expenditures from their personal income or family money and they take back home the money so put, whenever there is enough cash inflow (i.e., after realisation of sales).

#### **Short Term Investments**

Many of the SSI units do not invest in short term securities, because already they are in financial shortage. May be few SSIs, resort to this way, as a source of working capital. Such securities may be useful

to a unit which can be realised to cash at a shorter notice when there is a short term financial shortage. But investment has to be made carefully only when there is enough cash inflows into the business.

### Current Liabilities

Working capital requirement is also decided by the current liabilities such as wages, power, debtors etc. The credit period allowed by debtors, the normal consumption of power, the expenditure on wages, taxes rent, etc., determine the short term liabilities of a business.

### Working Capital Required

In accounting terms, working capital may be classified as gross working capital and net working capital. While the former refers to the capital required for holding current assets, the latter refers to the excess of current assets over current liabilities. For practical purposes, working capital needs of a unit may be assessed as follows :-

Monthly expenses that may be required for purchase of raw materials, and payment for power, wages and other operating expenses has to be calculated by estimation based on past records.

Working capital required has to be calculated based on the average number of days required for keeping raw materials, finished goods etc. in stock. This can be calculated with an example.

#### Example :-

Minimum stock of raw materials	30 days
Production period taken to convert Raw materials into finished goods	5 days
Average stock period of finished goods	10days
Credit on sales	30 days
Total no. of days for an operating cycle	75 days

The number of days taken for an operating cycle (i.e., from purchase to sales realisation) has to be multiplied by total amount of expenses required for a month and divided by number of days in a month. If expenses of a unit for a month is Rs.50,000 then,

$$\frac{50,000 \times 75}{30} = 1,25,000$$

Here, Rs.1,25,000 would be the working capital required for an enterprise. But this limit is subject to an equity margin upto 25% by the enterprise. This working for the assessment of working capital is based on the recommendation made by Puri Committee to the Reserve Bank of India for the very small borrowers.

The study team of State Bank of India which was headed by Mr. J.S. Varshaeya, conducted a study during 1975, identified that, extensive sickness in small industry was due to lack of management expertise and lack of adoption of sound business principles in running the enterprise. Hence, proper management of working capital with some principles of accounting may save the small businesses from running sick.

### Current Problem In Working Capital Finance

The small scale industrial units with a reasonable capital base (i.e., above Rs 5 lakhs investment) have a general access to working capital finance of banks. But smaller units in SSI sector(i.e., Tiny units) have very little access to working capital. The reasons for it are, (i) they require only very little amount of working capital finance, which the bankers do not prefer to finance; moreover, the bankers insist on collateral security along with the accounts of the business with regard to sales, stock books,etc. which the tiny units do not normally have (ii) The tiny units do not like to run pillar to post for a meagre amount, which is

available to them from the non-institutional sources. But here, it is disheartening to note that they pay interest ranging between 24% to 60% p.a. for the loan amount. The tiny entrepreneurs willy-nilly go for this source of finance (i.e. local money lenders) only for the reason that, it is available at the right time. So, the banks should be ready to finance small units with a minimum possible procedures/time. Small units shall try to equip themselves to have a sound accounting methods wherever possible (ii) smaller units approach banks, only at the time of starting the unit, their link with the banks ends immediately after the repayment of the seed loan. They do not move to the banks for two reasons, one is the bitter experience with the banks in availing of and repayment of loan and second is that the banks are not ready to provide further term loans or working capital loan to such 'little irregular' units. For this, there is only one remedy on the bank side that is, to have a close monitor on the units financed and to establish a rapport with them in financing and repayment. They also have to guide and train tiny units to maintain proper accounts and adoption of sound principles of accounting. The units should also counsel with bank officials. They should take every reasonable step to keep the units financially stable. Misuse or diversion of funds should be avoided. The above said suggestions would greatly help the banks in financing the smaller units.

The general complaint of other units in small scale industries sector is, banks insist on collateral security despite the properties of the unit as security. It has become quite normal with many of the entrepreneurs to pledge their residential houses, lands, etc., as security for bank loan. Small scale industrial units with sound financial position were able to get adequate credit. But it is very difficult to see such situations in many cases. These units may be called 'outstanding SSI units'; they are able to dictate terms of credit due to favourable business conditions they enjoy.

Sometimes even units with a good track record of sales, were forced to go for 'money lender' finance to adjust with the short term crunch in funds. Hence, to augment free flow of working capital and management of finance the following suggestion are made:-

#### **On The Part Of The SSIs**

- To maintain proper accounts as to sales, stock etc.
- To feel free to talk with the bank officials of the problems in working capital, and consult as to the remedy for the financial problems.
- Not to misuse or divert funds.
- To manage finance with proper accounting principles.
- As far as possible to be regular in repayment.
- To avoid money lenders' finance carrying high interest.

#### **On The Part Of The Bankers**

- To closely monitor the units financed.
- To make speedy disposal of loan applications and simplify procedures.
- To finance SSIs at the right time.
- Not to insist on collateral security.
- To provide working capital with little equity margin (i.e., 5% as per Nayak Committee's recommendations)
- To finance even small amounts without hesitation
- To Call for counselling and provide training and technical advice to SSIs

If the above things are put into action, by availing of credit at favourable terms, the small scale industries sector with great contributions in terms of increased production, employment, export and so forth, would strengthen our economy.

*ABHIGYAN*

A Quarterly Journal of FORE and FORE School of Management

Autumn 1996



FOUNDATION FOR ORGANISATIONAL RESEARCH AND EDUCATION  
ADHITAM KENDRA, B-18, QUTAB INSTITUTIONAL AREA, NEW DELHI - 110016  
PHONES : 686 3396, 686 6216 FAX : 91-11-685 6294 TELEEX : 31-73215 FORE IN