

PROCUREMENT OF FUNDS FOR SMALL SCALE INDUSTRIES IN RAJASTHAN FROM BANKS: STUDY OF NATIONALIZED BANKS AND PRIVATE SECTOR BANKS

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ABSTRACT

The Small-Scale Industries (SSI) gathered momentum along with industrialization and economic growth in India. It started growing due to the vision of our late Prime Minister Jawaharlal Nehru who sought to develop core industry and have a sustaining sector in the form of small-scale enterprises. Being a labor-intensive sector, they offer a higher productivity of capital than capital-intensive enterprises due to low investment per worker. The SSI today constitutes a very important segment of the Indian economy as they help in dispersal of industries, rural development, and the decentralization of economic power. Micro, Small and Medium enterprises (MSME) constitute the dominant form of business organization worldwide. For instance, 99% of enterprises in European Union and about 80% in USA were small enterprises. In India too, SSIs share is as high as 97%. Out of 42.12 million non-farm enterprises, 0.58 million are factory units. It is estimated that out of 5.8 lakh factory units, about 5 lakh are factory Small Scale Industries and Medium Enterprises as per the new definition of Micro Small and Medium Enterprises adopted by the Government of India in June 2006.

During the pre reform period there was 10.56 times increase in the number of sick SSI units in the country. After the liberalization period the number of sick units has decreased to 0.68 times. India's obligation as a member of WTO to bring down tariff and non-tariff barriers gave another competitive environment for SSI. Thus after reform SSI has been exposed to intense competition both in domestic and international levels. The SSI, which was not able to withstand competition, has gradually become sick. According to the report of RBI (3rd census of SSI) the criteria to measure sickness were: delay in repayment of loan over one year; decline in net worth by 50%; and decline in output during the last three years.

Keywords : Small Scale Industries, Nationalized Banks Private Sector Banks, Rajasthan Financial Corporation, Procurement of Funds, Micro, Small and Medium Enterprises (SMEs), Bank Credit

INTRODUCTION

Key Role of SSI in the Indian Economic Structure:

India has traditionally always had a very vibrant and competitive SSI. Even after the dawn of industrialization, British producers of textiles found hand made Indian textiles such a threat that they lobbied hard to have its import banned, succeeding in the late eighteenth century. During pre-economic liberalization period a wide variety of incentives, concessions and institutional facilities were extended for the development of SSIs. But these socialistic promotional policy measures, in many cases resulted in protection of weak units rather than the independent growth of units under competitive business environment. Such situation was continued up to the mid of 1991. Under the regime of economic liberalization, the focus was shifted from “protection” to “competitive promotion”. The public policy in India had been attaching lot of importance to village and SSI on the following grounds. SSI being labor-intensive, helped to increase the volume of employment, particularly in rural areas, it is estimated that about 2 crore persons are engaged in India in these industries. The handloom industry alone employs 50 lakh people. They account for 6% of GDP, 95 % of all industrial units, and 34% of total exports. Around 39 lakhs SSIs in India has emerged versatile producing over 8000 products, from traditional handicrafts to high-end technical instruments.

In developed economies, about 60 % of GDP is generated by small enterprises, i.e., enterprises with a maximum of 50 employees. The reason being large number of small enterprises guarantees a high degree of competition, and variety of economic activities that require millions of enterprises to be reasonable competitive and efficient. The indirect jobs created through forward and backward linkages are no less important. In real terms, the SSI recorded a growth rate of 10.1% in 1994-95 as against 7.1% in 1993-94 and 5.6% in 1992-93. By the year 2025, if not controlled, this sector will grow even more rapidly.

Generalizations are also difficult because though there are firms which are growing rapidly, there also exist 1, 38,000 sick units within the sector in India. The contribution of SSI in India to national development was meager as compared to the contribution of SSI in other countries of the world. India's SSI shared 95 % of all establishments, 40 % of output, 45% of employment and 35 % of exports. But Taiwan ranked first with a share of 97% of establishments, 81 % of output, 7% of employment, 48 % of exports followed by Japan contributing highly with 99 % of establishments, 52 % of output, 72 % of employment and 13 % of exports (SIDBI Report, 2000).

Small Scale Industries Financing in India

Finance forms the most critical input for a business enterprise whether large or small. All firms require financing to grow and survive. Sources may be external, such as loans, equity infusions, subsidies and government grants, or internal such as generated cash flows. Many firms are self-financed in the beginning. Once the firms reach certain degree of maturity in the development of their product line and customer base, external finance becomes available. The flow of institutional finance is linked with the creditworthiness of the enterprise. Small enterprises, due to their small size and low capital base, generally find it difficult to satisfy the conditions laid down by the banks, particularly, in establishing the viability of the project, meeting collateral requirements and making timely repayment of loans. Hence, they do not find a place among the preferred clients of the banks.

Financial Aid for SSI

Credit is the prime input for sustained growth of SSI and its mobilization for meeting fixed and working capital needs poses the foremost problems. Credit provided for creation of fixed assets like land, building, plant and machinery is called long term credit. Credit provided for running the industry for its day-to-day requirement for purchasing raw material and other input like electricity and water etc. and for payment of wages and salaries is called short-term credit or working capital.

According to the 3rd All India Census of Small Scale Industries (2001- 02), of the total number of 10.5 million small enterprises in 2001- 02, about 87% units were unregistered while 2.95 lakh units were

factory units (employing more than 10 workers with power and registered under Factories Act). 99.5% of the SSI units were tiny units having investment in plant and machinery less than Rs. 25 lakh. While a registered unit employed on an average 4.48 persons, in the case of unregistered units this was only 2.05 persons per unit. Per unit investment in plant and machinery was found at Rs. 2.21 lakh in the case of registered units and Rs. 0.27 lakh in the case of unregistered units. Per unit fixed investment was Rs. 6.68 lakh for registered units and Rs.0.68 lakh for unregistered units. The average for the SSI sector was Rs. 1.47 lakh. Average per unit output for registered unit was Rs. 14.78 lakh and for unregistered unit it was Rs. 0.86 lakh. Average for SSI sector was Rs. 1.47 lakh. The Census of SSIs found that only 14.26% of the registered units availed bank finance, while only 3.09% of the unregistered units had access to bank finance. This means that 97% of the smaller among the small enterprises were deprived of the institutional credit. In other words, most of tiny and micro enterprises use self finance or borrowed funds from friends, relatives and moneylenders. Moneylenders continue to play important role after self-finance. The recent All India Debt and Investment Survey has revealed that the share of moneylenders in total dues of rural households rose from 17.5% in 1991 to 29.6% in 2002. A recent World Bank survey (August 2006) on the status of flow of credit to SME sector has revealed that in the start-up phase, family constitutes an extremely important source of funds for overwhelming majority (over 85%) of the respondents and trade credit came next in importance, representing extremely important source of funds for 27% of the respondents. In comparison, bank loans from state-owned banks make up an extremely important source for 15% and very important source for about 17% of the firms surveyed.

Evaluation of Bank Credit for SSI

Some other disturbing trends noticed with regard to bank credit to MSMEs are: (i) inadequate working capital which is currently ranging between 10-13% against RBI norm of 20% of projected turnover to be given as working capital, (ii) high cost of credit normally ranging between 13-16% as against relatively lower rate of interest of 6 to 9% charged from large units on the ground of latter's better creditworthiness and 7% from agricultural sector, (iii) insistence on collaterals even on loan up to Rs. 5 lakh in spite of the RBI guidelines to this effect (loans without collateral out of total loan below Rs. 5 lakh to SSI was 25.9% in 2004-05), and (iv) neglect of small loan as the share of loan below Rs. 25000 had declined from 21% of total outstanding of banks credit in June 1985 to 3.7% in March, 2005. Scheduled commercial banks' credit to the large and medium industries was of the order of Rs. 290186 crore in the year 2004-05 which was 30% of the gross bank credit for that year. Though separate figure for medium industries is not available, it is assumed that about 20% this credit, amounting to Rs. 58083 crore might have gone to medium enterprises. Thus, the total credit from the scheduled commercial banks for the year 2004-05 was Rs. 141217 crore, including Rs. 83179 crore for SSI. To this, we may add Rs. 34313 crore being the credit to small business, retail trade, transport operation, etc in 2003-04. In addition, a sum of Rs. 37483 crore flowed to small enterprises including traditional industries and small business from sources like regional rural banks (Rs. 14393 crore), cooperative banks (Rs. 15117 crore), SIDBI direct finance (Rs. 2695 crore), SFCs (Rs 864 crore) and SIDCs and NSIC (Rs. 4414 crore) in the year 2003-04. Cooperative banks' credit is mostly going to handloom, handicraft and traditional cooperative industries. Thus it is expected that entire MSME Sector received a total credit of over Rs. 2 lakh crore (rough estimate) by the end of March 2005.

Banks, it seems, are not favourably inclined to finance the small enterprises, particularly, smaller among the small enterprises for various reasons. Notable among them are (i) inability of small entrepreneurs to meet collateral requirement (ii) high non-performing assets in SSI sector which is currently at 15% as against 8% for large industries (iii) high incidence of sickness (though official RBI data indicates a decline in the number of sick SSI units from 3.04 lakh in 2000 to 1.39 lakh in 2004 (iv) higher transaction cost to banks in processing large number of small loan applications. Normally, the cost of processing small loans has been found in the range of 18 to 21% whereas the rate of interest on small

loans below Rs. 25,000 is 12% and other loans up to Rs. 5 lakh is 15 to 16% (v) difficulty in establishing the creditworthiness of the project proposals. Poor borrowers do not require project finance; instead they need production, consumption and housing loan.

PROFILE OF SMALL SCALE INDUSTRIES IN RAJASTHAN

Industrial state of Rajasthan on the eve of independence was very poor. There were only 11 large and medium scale industries in the state comprising 7 textile units, 2 cement units and 2 sugar units.

Even today, Rajasthan is known as backward region in our economy. The Government at the centre as well as at the state level has made deliberate and concerned efforts to give the industrial structure a modern and mature look by promoting key and basic heavy industries, the small and medium industries, the handloom, cottage and village industries.

The State of Rajasthan has been marching ahead in terms of industrialization during the plan period. Due to consistent support and growth strategy adopted by the Government, the large, medium and small scale units are increasing every year. During 2004-05 in Rajasthan there were over 2.63 lakh small scale industries employing 10.07 lakhs people. Investment in the large and medium sector was estimated to be Rs. 16948/- crores and the figure stands at Rs. 4069 crores for the small scale sector.

Regional Variation & Industrial Development in Rajasthan

The study of industrial dispersal in Rajasthan indicates that there is a concentration of factories in the Jaipur district. In 2002-03 out of 4868 factories in the entire state were 960 factories (19.7%) in Jaipur district alone. In the table it is shown that there are sharp regional variations in the development of factories in Rajasthan. Some districts have more than 250 factories such as Ganganagar, Pali, Udaipur, Ajmer, Alwar, Jodhpur, Bhilwara and Jaipur; while others have less than 10 factories only; such as Baran, Karauli, Jaisalmer and Jalore. Jhunjhunu district had 12 factories in 2002-03. Dholpur and Jhalawar had each 11 factories only. Dungarpur had 10 factories. Jaisalmer and Jalore had only 1 factory each in 2002-03. Such disparities create tensions- economic, social and political. They should be reduced by adopting suitable policy measures in future. The following table shows that there is an unequal distribution of factories in 32 districts of Rajasthan. A comparative study for different districts has been made on the basis of number of factories and employment in factories for 1970 and 2002-03. The number of factories increased from 1022 in 1970 to 4868 in 2002-03. The total number of persons engaged (workers + employees) increased from 1.12 lakhs to 2.34 lakh during the period.

Problems Faced by Small Scale Industries

The problems faced by small scale industries when trying to obtain funds are as follows:

- ◆ SME's rarely have a long history or successful track record that potential investors can rely on in making an investment;
- ◆ Larger companies (particularly those quoted on a stock exchange) are required to prepare and publish much more detailed financial information- which can actually assist the finance- raising process;
- ◆ Banks are particularly nervous of smaller businesses due to a perception that they represent a greater credit risk.

Conclusion:

For the need of credit support to small scale industries in Rajasthan

- On the basis of research it is observed that out of total small scale industries, 98% of SSIs are aware about the credit facility provided by the banks and 2 % are not aware because they are financing their business from own capital.

- On the basis of research it is observed that maximum numbers of small scale industries are taking loan from nationalized banks and private sector banks .The need of credit support to small scale industries from both sector of bank is feasible.
- The problem faced by the small scale industries to find business finance from the banks are:
 - a) Small scale industries are not having good track record for the loan, because they are suffering from the losses and few industries are newly established.
 - b) Small scale industries are not having collateral security which is demanded by the bank for loan.
 - c) Small scale industries are saying that hidden charges of banks are high which is taken by the bank from industries
 - d) Banks are not providing without security credit support to small scale industries which is available for SSIs as per RBI rule.
- Small scale industries' expectations from the bank in order to fulfill the need of credit support are listed below:
 - a) Provide credit on the basis of present working and not on the basis of past performance.
 - b) Provide loan at reduce collateral security or without collateral security, so that SSIs can perform better with the help of bank credit.
 - c) The total loan procedure of bank should be transparent and there should be no hidden charges.
 - d) As per the guidelines of RBI for SSI, bank should provide adequate payments, timely credit, without security credit support and loan at lower interest rate.

For Nationalized Banks and Private Sector Banks:

- All the nationalized banks and private sector banks are providing or interested to give loan to small scale industries, for the purpose of start up, expansion, diversification and rehabilitation of industries.
- Nationalized banks and private sector banks are providing timely credit, loan at low interest rate and without security credit support to small scale industries.
- All the banks are providing credit support to small scale industries in the form of start-up loan, bill finance, export finance and working capital finance
- The following are the criteria on the basis of which banks are interested to increase the loan amount:
 1. Business model
 2. Cost of the project (for term loan).
 3. Turn over of the business (for working capital loan).
 4. Financial position of the business (on the basis of Balance sheet, Profit & Loss account, book debt etc.)
 5. Security provided by the small scale industries.
 6. Repayment track record of the small scale industries.
 7. Relation of small scale industries with bank.
 8. Location of the project.
 9. Capital contribution by small scale industries.
- The following are the formalities required by the banks from small scale industries for credit support:
 - Project report.
 - All relevant documents related to project and loan.
 - Pre-sanction survey by the banks.

- Know your customers (KYC) norms (Identity proof, address proof, stability proof, qualification of entrepreneurs, experience of entrepreneurs etc.).
 - Security available for credit.
 - Analysis of firm, project, industry, market etc.
 - Registration under small scale industries units.
 - Other clearance from respective departments.
 - Repayment of loan record by small scale industries if available.
 - Capital contribution by entrepreneurs.
 - Requirement of the industry for loan.
- Suggestions provided by the banks to small scale industries about their repayment of loan and performance if they need credit support from banks:
- Small scale industries should give genuine reason for loan and does not provide any missing or wrong information.
 - Small scale industries should have proper financial discipline, all the sales through books of account and should not save themselves from paying tax.
 - They should not over stretch about loan.
 - Small scale industries should increase awareness about the bank functioning/ paperwork that bank undertake.
 - A disciplined approach on part of industry with regards to account conduct and maintenance will also enable industry to leverage opportunities.
 - Business of the small scale industries is depend on the economic conditions, now a day there is tough competition amongst the industry, small scale industries have to work hard for their smooth working. There is no bar for the banking sector for financing to small scale industries.

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