INTRODUCTION

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CHAPTER I

INTRODUCTION

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CHAPTER I

INTRODUCTION

I. 1 Introduction

Economic development is the primary objective of every nation. It is a continuous and comprehensive process. Rapid economic development basically depends on industrialisation. Industry is the process in which there is sharp increase in the industrial share of Gross Domestic Product and labour force. Industrialisation is considered an effective strategy for increasing the rates of economic development. The siginificance of Industrialisation as a means to increase the rates to attain rapid development and prosperity has been recognnized widely by planners, philosophers and economists from the very ancient period. The terms 'economic growth' and 'industrialisation' are synonymously used to a certain extent. A major share of the National Income of the country is from its industries. Further, industrialisation enhances foreign exchange earnings and creates better economic stability and facilities.

Industrialisation is associated with investment, i.e., deployment of credit. Every problem of the entrepreneur concerning production or materials, quality or marketing, in its ultimate analysis, is a financial one. Thus, finance is the essential input around which all activities gain momentum. Economic growth, therefore, certainly requires better deployment of credit. "The level of deployment of bank credit can be better assessed in comparison with the growth of economy-state income"[1]. In an underdeveloped economy like India, where economic development is a process to be planned and assisted by the Government, better deployment of credit is a sine qua non. Financial resources for industrial growth may come through two sources, viz., domestic capital formation and import of capital. Small Scale Industrial units which are predominantly organized as proprietary and partnership concerns have no access to capital market or imported capital. Hence, the complaint often made in various parts of the country is about the lack of finance to the small sector. It is to mitigate the financial problems of this sector that the Government has established various Development Financial Institutions. Institutional financing has been a unique source of domestic capital formation. "The readiness of financial institutions to adopt the objective of development - economic and social, and to bring about a great mobility of resources to meet the emerging needs of the economy is a necessary concomitant of development"[2]. With the launching of the Five Year Plans, there was need for enlarging the institutional structure to meet the needs of the industrial sector. "A rapid industrial development calls for heavy doses of finance. Development banks and financial corporations came into existence in India in the post-Independence period with the aim of accelerating economic growth through speeding up the process of industrialization and have come to the corporate sector"[3]. At present, India has a better network of DFIs at the national and State levels. Both, medium and long-term financial assistances are offered by these multipurpose financial institutions.

All India Financial Institutions (AIFIs) have been instrumental in accomplishing the overall national objective of economic growth. It is not possible for the AIFIs to bring about a balanced regional development in different States. Therefore, existence of different State Level Financial Institutions (SLFIs) with liberal and transparent norms, diversified schemes and wide coverage has become need of the hour. The SLFIs can come closer with entrepreneurs and free exchange of idea and feedback are possible. Thus, the establishment of various SLFIs was an action in the right direction. The Government of India passed the SFCs Act in 1951 facilitating the setting up of SFCs in different States. The primary objective of the Corporation is to give advances to the MSME segment, thereby to meet the medium-term and long-term credit requirements of this sector. In spite of the premier role assigned to the SFCs for financing small industries in the State concerned, small entrepreneurs still hesitate to approach them for various reasons. The difficulty in getting the right type of finance at the right time and in the right quantity continues to haunt the small entrepreneurs and still ranks first among the major problems faced by the small sector. This being the situation, it has become relevant to conduct a study aimed at evaluating the role and performance of the SFCs.

The role assessment of the SFCs is done at the micro level by restricting it to a single Corporation. This decision is prompted by the fact that the functions discharged by all SFCs are similar. Therefore, it is felt that a micro analysis would serve more than a macro analysis of the performance of all

SFCs. The Kerala Financial Corporation appears to be the best choice for the study not only due to the magnitude of its operation but also due to the fact that it is one of the oldest SFCs functioning in the country. Hence, the role of evaluation of DFIs is limited to the KFC.

I. 2 Statement of the Problem

The Kerala Financial Corporation has been established with a view to financing, promoting and rehabilitating the small and medium enterprises. It is the premier institution for industrial finance in the State. Also, in the absence of a developed capital market in Kerala, the DFIs are still the major source of the much needed long-term finance to the MSMEs. With the decline in the number of DFIs, due to the ceasing of the ICICI and the IDBI as DFIs, in the face of financial sector reforms, innovative financing mechanism of the remaining State level DFIs is expected to take care of the need of project financing. The KFC, therefore, has to be very seriously concerned with the development of the MSME segment which is one of the most dynamic and vibrant sectors in the Indian economy. Facts do reveal that the MSME segment is struggling hard even for its existence in spite of the assistance from various SLFIs like the KFC. Despite the sound financial background, the role of the KFC in extending finance to industries is still found to be confined to a particular limit. It has been observed that in the case of the KFC, there had been a concentration of industrial activity in a few already industrially developed districts of Kerala. This tendency has been so over time. A wide gap is existing between the demand for and supply of financial assistance from the KFC. In the year 2007, only 74.9% and in 2008 only 73.8% of the total demand were sanctioned. Such a diminishing trend is seen year by year. Also, many industrial units are found to be averse to approach the Corporation for further assistance. This situation calls for a diversified thinking by financial institutions like the KFC. A better consumer – suited programme has to be framed. Further, keeping pace with the higher global and domestic economic growth, the MSME segment has to accelerate its growth rate substantially, especially in a period of global recession. The DFIs do not give much attention in this regard. As far as the State of Kerala is concerned, it is the KFC which has to do more for the development of the MSME sector. The KFC has to be more efficient and vigilant in promoting this segment. A separate scheme, namely, the Micro and Small Enterprise Development Package –MSEDP –has to be formed. This study focuses on its necessity. Further, this study aims at bringing change in the procedure of the Corporation in its so-called concentration in a few industrially developed districts.

I. 3 Relevance of the Study

A detailed study on the role of the KFC in the industrialisation of Kerala is highly worthwhile especially in the period of global recession. Various provisions of the SFCs Act enjoin on the KFC to undertake the stupendous task of industrial development in the State concerned by providing long-term credit to the MSME segment. Hence, a detailed study on how far the KFC has succeeded in this regard is highly relevant. Further, the present study looks into the extent to which the Corporation has adjusted to the changed operating environment with its diversified schemes to satisfy the investors in industry.

Further, the study is more relevant as it makes an attempt to analyse the outcome of the results of Global Investor Meet (GIM) conducted by the Government of Kerala during the period of study. The study is highly relevant in a period of economic meltdown which results in overall crisis in the global employment scenario. The extent up to which the KFC has gone to rehabilitate the jobless people and the gulf returnees is a matter of concern. Also, it has relevance in a period of ceasing of the development status of various all India financial institutions like the IDBI and ICICI. In this context, the KFC has to play vital roles.

I. 4 Scope of the Study

This study is an attempt to note the changes having taken place in the industrial profile consequent on the intervention of the KFC in industrial development. It considers the issues and possibilities in this respect. Problems associated with lending, security, repayment, recovery, rehabilitation, feedback, follow-up, etc., are examined here. The study is confined to the KFC – aided units. The study also attempts to put forth some possibilities and recommendations for improvement of the performance of both the KFC and the beneficiary units.

I. 5 Period of Reference

The study covers a period of five Years from 2002-'03 to 2006-'07, which falls within the tenth plan period. However, for long-term analysis, data relating to the previous years and the data belonging to the years 2007-'08 and 2008-'09 are also taken into consideration

I. 6 Objectives

Primary Objectives :

1. To review the structure and pattern of industrial development in Kerala and the institutional support for industries.
2. To examine the role played by the KFC in promoting the MSME segment in the State.

Secondary Objectives :

1. To study the social background, organization, structure and working of the industrial units aided by the KFC.
2. To study the regional considerations on sanctions and disbursements of loan by the KFC.
3. To study the impact of factors like gender of the entrepreneurs, size and form of industrial units on sanctioning the loans.
4. To study the mode of disbursement of loans by the KFC, the trends of repayment of loan, etc.
5. To suggest suitable measures for improvement of functions of the KFC and the aided MSMEs.

I. 7 Hypotheses

As much as six main hypotheses (five null hypotheses and one alternate hypothesis) consisting of a total of sixteen sub-hypotheses have been formulated as elucidated below.

There is no significant relationship between the region of industrial units and the source of information about the service of the KFC, time lag in sanctioning and disbursing the loans, methods of loan disbursement and the assistance sought by the units from other sources.

From this null hypothesis, the following sub-hypotheses are formed.

H I. 1: *There is no significant association between the regions of industrial units and the source of their information about the service of the KFC.*

H I. 2: *There exists no dependence between the time lag in sanctioning the loans applied for and the locality of the industrial units.*

HI. 3 : *There is no significant dependence between the time lag in disbursing the loan sanctioned and the location where the industrial units are situated.*

HI. 4: *There exists no significant association between the methods of loan disbursement and the location of industrial units.*

H1.5: There is no significant relation between the financial assistance from sources other than the KFC and the location where the industrial units are situated.

There is no dependence across the form of business organisation, the purpose of loan availed of and the difficulties associated with starting / running the industrial unit.

From this null hypothesis, the following sub-hypotheses are formed.

H2.1 : The purpose of loan sanctioned is independent of the form of the industrial unit.

H2.2 : There is no dependence between the difficulties faced in obtaining loan from the KFC and the form of organisation of the beneficiary units.

There is no significant difference across the size of beneficiary units and type of security offered by loanees and the methods adopted for follow-up and recovery of loans by the KFC.

From this null hypothesis, the following sub-hypotheses are formed.

H3.1 : There is no significant relationship between the type of security and the size of industrial units.

H3. 2 : There is no dependence between the methods adopted by the KFC for *follow-up and recovery of loans and size of the industrial units.*

There is no variation across the regions and the amount of loan sanctioned to the units and the amount utilised by the units.

From this null hypothesis, the following sub-hypotheses are formed.

H4. 1 *: There is no variation in the amount of loan sanctioned to the units of various districts.*

H4. 2 *: There is no significant variation in the amount utilised by the industrial units of different districts.*

There is no variation in the opinions of the beneficiaries about the service rendered by the KFC, from the units of different districts, different form of organization and different size.

From this null hypothesis, the following sub-hypotheses are formed.

H 5. 1 *: There is no variation in the opinions of the beneficiaries of different districts about the service rendered to them by the Corporation.*

H5. 2: *There is no significant variation in the opinions of the beneficiary units of different forms of organisation about the service of the KFC.*

H5. 3 *: There is no significant difference between the opinions of beneficiary industrial units of different size about the service of the KFC provided to them.*

There is significant difference in sanctioning loans by the KFC to male and female entrepreneurs.

Two sub-hypotheses are formed on the basis of this alternate hypothesis.

H 6. 1 : *There is discrimination on the part of the KFC in sanctioning loans to male and female entrepreneurs.*

H 6. 2 : *There is significant difference between the utilisation of loans sanctioned and the gender of the entrepreneurs.*

I. 8 Methodology

The study requires both primary and secondary data. Primary data for the study were collected from the officials of KFC and from the sample beneficiary units, by the questionnaire method and the secondary data were collected from various official records and reports.

I. 9 Sampling Size and Techniques

Stage 1 : Selection of Sample Districts

The KFC itself has classified the State of Kerala into four categories, as shown in Table 1.1

Table 1 . 1

Categorisation of Revenue Districts by KFC

Backward Districts			Non-Backward Districts		
CATEGORY	A	Idukki	CATEGORY	D	Pathanamthitta
		Wayanad			Kollam
	B	Alappuzha			Kottayam
		Malappuram			Ernakulam
		Kannur			Palakkad
		Kasargode			Kozhikkode
	C	Thiruvananthapuram			
		Trissur			

Source : Annual Report of KFC 2002

In order to select four sample districts, the KFC's grouping of the 14 revenue districts into four categories, viz., A, B, C and D, was taken as the base. Selection of four out of 14 revenue districts was made using the *stratified* *sampling* method in such a way that one revenue district each from all four categories was included in the sample. Accordingly, four districts as given in Table 1. 2 were selected.

Table 1. 2

Selection of Sample Districts

Sl.No	Districts	Category
1.	Idukki	A
2.	Malappuram	B
3.	Thiruvananthapuram	C
4.	Ernakulam	D

Stage 2 : Selection of Sample Units

The total sanctions of financial assistance by the Corporation since its inception till 31-03-2008 amounted to Rs. 3,11,018.24 lakh, for a total of 39,814 industrial units across the State of Kerala[5]. As per the annual reports of the years under study (2002-'07), the KFC had financed a total of 2,493 units (696 units in 2002-'03, 581 units in 2003-'04, 387 units in 2004-'05, 368 units in 2005-'06 and 461 units in 2006-'07) which constitute the universe. From 2,493 units, 962 units belong to the districts under study. Therefore, the population for the study is tantamountig to 962 units. From the population, a total of 60 units, 15 each from the sample districts, was chosen on *simple random sampling* using the lottery method as follows.

The list consisting of 962 industrial units (Idukki - 145, Malappuram - 145, Thiruvananthapuram - 227, and Ernakulam - 445) incepted during the period under study was collected from the respective district offices of the Corporation. From this list, 15 units were selected from each district by simple random sampling, applying the lottery method. Accordingly, all the units in each district were numbered consecutively and these numbers were written on separate slips of identical size and shape, made of yellow paper. These paper slips were folded uniformly and mixed thoroughly in a box. A blindfold selection of 15 slips was made then for each district. The population and sample size of the study are presented in Table 1. 3.

Table 1.3

Population and Sample Size

Sl.No	Sample districts	Population for the study	Sample units
1.	Idukki	145	15
2.	Malappuram	145	15
3.	Thiruvananthapuram	227	15
4.	Ernakulam	445	15
Total		**962**	**60**

Source: Annual Reports of KFC and hearsay from KFC officials.

Stage 3 : Selection of KFC officials.

Thirteen officials of the KFC were selected - by judgement sampling - and consulted. Their distribution is tabulated below.

Table 1. 4

List of Officials Consulted for Information

Sl. No.	Office	Number of officials
1.	Head Office, Thiruvananthapuram	01
	IDUKKI DISTRICT	
2.	Thodupuzha Branch	02
3.	Kattappana Branch	01
4.	Malappuram Branch	03
5.	Thiruvananthapuram Branch	03
	ERNAKULAM DISTRICT	
6.	Ernakulam Branch	01
7.	Perumbavoor Branch	02
Total		**13**

I. 10 Methods of Data Collection

Both primary and secondary data were collected for the study.

I. 10. 1 Collection of Primary Data

Primary data for the study were collected from the officials of the KFC and from the sample beneficiary units, by the questionnaire method. Two separate sets of questionnaire were made for this purpose (APPENDICES I & II). Discussions in person and over the phone were also made whenever necessary. Both the sets of questionnaire were pre-tested in Ernakulam district by conducting a pilot survey. The tentative questionnaires were revised on the basis of the experience of the pilot survey. The collection of primary data was carried out in eight months from April to November 2006.

I. 10. 2 Collection of Secondary Data

Secondary data were collected from various official records and reports as listed below:

Annual Reports of AIFIs like IDBI, ICICI, SIDBI, IFCI, etc., Annual Reports of KFC and KSIDC, RBI Bulletin, Economic Review of the Planning Board (Govt of Kerala), Periodicals of the Planning Commission of India, IDBI Report on Development Banking, Copies of Budget Speeches of Ministers in the State Assembly and Parliament, Study Reports of the Department of Economics and Statistics of the Government of Kerala, Plan Documents of Central and State Governments, White Paper Published by the Government of Kerala, Statistical statements on the performance of the small-scale sector published by various agencies, Report of Academics on the institutional finance field, Texts dealing with industrial and institutional finance, and other available periodicals dealing with the subject.

In addition to the above-mentioned sources, data were collected from various websites like: www.kfc.org; www.rbi.org.in; www.ifin@hathway.com; www.infinserv@bol.net.in;www.ksidc.org;www.idbi.com;http://www.ifciltd.com; and http://www.sidbi.com.

I.11 Tools of Data Analysis

Various statistical methods were applied for analysis. The objectively collected data were suitably classified and arranged in tables and included in appropritate chapters. Various tools like percentages, ratios, averages, growth indices, co-efficeint of variation, Chi-square, F test, t test, etc., were mainly used for analysis and interpretation. The analysis was carried out by using the statistical software SPSS.

I. 12 Variables Used in the Study

I ***To review the structure and pattern of industrial development in Kerala :***

1. Contribution of major industries
2. Industrial investment proposals
3. Investment attractiveness
4. Gross State Domestic Product
5. Regional dispersal of SSIs (MSMEs)
6. Promotion of working SSIs (MSMEs)

7. Number and production of SSIs in Kerala against the total SSIs in India
8. State-wise distribution of sick/incipiently sick units
9. District-wise distribution of medium and large-scale industries
10. Index of industrial production
11. Lending by financial institutions

II *To examine the financial profile of the KFC :*

12. Capital structure
13. Owned capital
14. Composition of shareholdings
15. Break-up of sharecapital
16. Loan Capital
17. Debt Equity

III *To examine the role played by the KFC in promoting the MSME segment:*

18. Summary of loan operations
19. Total revenue
20. District-wise classification of loans sanctioned
21. Amount-wise classification of loans sanctioned
22. Industry-wise classification of loans disbursed
23. Rate of interest
24. Total sanctions
25. Total disbursements

IV *To Examine the operations of the KFC :*

26. Sanctions of loans as a percentage of applications
27. Disbursements of loans as a percentage of sanctions
28. Recovery as a percentage of loans disbursed
29. Current recovery
30. Net Profit / Loss

V *To study the social aspects of entrepreneurs :*

31. Gender of entrepreneurs
32. Educational qualification
33. Previous experience in industrial activity
34. Family background

VI *To study the nature, form, size, manpower, etc., of the units :*

35. Nature of business
36. Nature of product
37. Size of the unit
38. Form of organisation
39. Ownership of premises
40. Employment provided
41. Number of mandays generated

VII *To study the financial aspects of the units :*

42. Total capital
43. Working capital
44. Fixed capital

45. Own capital

46. Debt capital

47. Current assets

48. Current liabilities

49. Sales revenue

50. Fixed cost

51. Variable cost

52. Total cost

53. Operating expense

54. Gross Profit

55. Net Profit

VIII *To study the level of performance of the units :*

56. Current Ratio

57. G/P ratio

58. N/P ratio

59. Operating ratio

60. Operating profit ratio

61. D:E ratio

62. ROI

63. Break-Even Sales

64. Contribution

65. P/V Ratio

66. Margin of safety

IX *To study the perceptions of loanees on the lending operations of the KFC :*

67. Amount required
68. Amount of loan applied for
69. Amount of loan sanctioned
70. Purpose of loan
71. Cost of borrowings
72. Types of security insisted
73. Other sources of finance of the loanees
74. Time lag in sanctioning the loans
75. Time lag in disbursing the loans
76. Mode of disbursement
77. Adequacy of working capital loan
78. Utilisation of working capital loan
79. Repayment of loans
80. Premature closing of loans

I.13 Limitations of the Study

The study has the following limitations:

1. The KFC does not have adequate or systematic information about the working of the industrial units financed by it.
2. Some of the industrial units selected for the study are found to be not existing. Such short-lived units and some defunct units in the sample were replaced with other units.

3. Many of the assisted units do not maintain systematic books of account and other records. It is so more in the case of sole proprietorship units. This creates difficulties in gathering the required information. This situation necessitated the collection of some data by the observation method.

4. In some cases, entrepreneurs give information from their memory. Such information may not be reliable.

I.14 Synoptic View of the Report

This study consists of ***six*** chapters

Chapter One: The introductory chapter deals with the significance of the industrial sector in economic growth. It consists of the problem statement, relevance, scope, period, objectives, hypotheses, variables used, methodology, sampling size, methods of data collection, tools of data analysis, limitations of the study, and the synoptic view of the Report.

Chapter Two: This chapter attempts a review of the available literature relating to the present study.

Chapter Three: This chapter explains the trends of industrialization in the State and the role of various promotional agencies for the industrial development of Kerala.

Chapter Four : This chapter deals with the role of the Kerala Financial Corporation in the promotion of MSMEs in Kerala. It has three parts, viz., A, B and C. Part A is concerned with the profile of the Corporation: its establishment, organisation and management; capital structure and purpose, functions and schemes of financial assistance. Part B deals with summary of loan operations of the Corporation during the period under study. Total loan operations and district-wise, amount-wise, size-wise and industry-wise break-up of operations are also included in this part. Part C is concerned with the loan disbursement and repayment systems of the KFC.

Chapter Five : This chapter analyses the pattern, organisation and working of beneficiary units in four parts, viz., A, B, C and D. Part A deals with the demographic profile of the units; part B is concerned with the profile of borrower units, part C deals with the working of beneficiary units and realization of their objectives and part D is concerned with testing of various hypotheses formulated.

Chapter Six : This chapter summarises the findings of the previous chapters. Some measures for improving the performance of the KFC and for attaining fruitful results by the aided untis are alos included in this chapter.

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