CHAPTER VI

SUMMARY AND FINDINGS

Right from the inception of the planning era, there has been tremendous change in the industrial front. On account of sound economic policy pursued over the years, tremendous amount of growth and development has taken place in Indian industries. With the advent of New Economic Policy (NEP) in 1991, the economy witnessed transformation of drastic nature undergoing a paradigm shift from one of the most highly regulated economy of the world to a market oriented system contracting the role of government in making economic decisions as the means to achieve higher growth of the economy and its rapid integration with the rest of the world.

In the process of economic liberalization and globalization the role of industrial units especially the Large Industries of U.P. in general and Kanpur large industrial units in particular have stellar role to play which they seems to have played in the past. From the fore-
going discussion it has emerged that the large industries of Kanpur including (Nagar and Dehat) both have been contributing tremendously in terms of employment, investments, and infrastructural development.

In presenting capital budgeting of Large Industries of Kanpur, the Research Scholar is well aware of its utility and significance. The plethora of existing literature on the topic is scaling and inadequate to resolve the problem of 21st century. The world is turning the point of homogenous political and economic systems with global trading and financial institutions. The world is segmented into market for investments. The number of the corporations is getting smaller. The problem is not supply of natural resources or the size of the market. The real problem is management of capital budgeting for project in new market for ever higher profit.

The objective of the thesis is implementation of capital budgeting with new parameters by fusing together the divergent perceptions of management of MNCs and supplies of funds. The new approach and hypothesis make the study
significant contribution to the existing stock of knowledge in changing socio-economic global milieu.

The cost of equity is high with explicit cost of 1.4 per cent and implicit cost of 20 per cent. It does not fulfil the equity holders expectations. The main reliance of Large Industries of Kanpur for capital budgeting has made it suffer heavy cost of loan (Kd.) i.e. 15 per cent. The cost of equity and cost of loans both have given a high over all cost of capital of 13 per cent. The impact of high over all cost of capital is the reduced value of equity in the market. It does not conform to the ideal goal of capital budgeting to maximise the owner's wealth. The pay out ratio for Large Industries does not justify the mode of financing of projects. Most of the earnings have been retained while cost of capital is greater than rate of return. The retention policy to finance projects is justified when rate of return is greater than cost of capital.

The ratio analysis brings into sharp focus the impact of capital budgeting on financial status of Large Industries of Kanpur. Large Industries have not been able to generate
internal resources to finance the projects. The profit margin is thin and most of the funds meant for prospect have gone into current assets. As a result the rate of return has been adversely affected.

These are two extreme examples of Large Industries of Kanpur. LML Ltd. which is a successful venture and on the other hand. J.K. Jute Mills which is an unsuccessful firm. LML Ltd has made substantial games in Net Present Value (NPV) because of low cost of financing the projects. successful generation of internal resources and judicious application of financial leverage. On the same counts. J.K. Jute Mills has faltered. It has resorted to heavy borrowing allowed erosion in the value of equity shares and generated little internal resources to finance the projects. It has followed. conservative policy to build up high level current assets.

Large Industries of Kanpur are highly risky and suffer from traditional philosophy of investment. The aggressive management of the modern Large Industries does not bother about equity base. As a result, the
degree of riskiness has crossed all safe bonds for equity holders and financial institutions. It is a case for restructuring capital, making capital budgeting for maximum return at low cost and minimum risk.

The low rate of return of Large Industries does not justify the investment of the magnitude it is holding. It calls for remedial measures in the form of restructuring the fixed assets. The Large Industries have lost net present value because of escalating cost of projects and high anticipated rate of return. The industry is under pressure to do sound screening of the projects, raise its IRR and have strict administration of capital budgeting. Net present value of Large Industries has been eroding during the whole period of study with exceptions far and between. Net present value truly reflects the fallacies of the management in selecting the project for capital budgeting without serious regard for their contribution to net present value. A Large Industries of Kanpur have got to shun from acquiring non performing assets. The Large Industries of Kanpur have not been able to maintain book value in the stock market. The value of the equity shares is depleting
in the stock market. The market goes by net-worth, liquidity, dividend and future growth. The Large Industries do not hold a bright picture to enthuse the investors with encouraging response. The equity holder stock are being exposed to an unabated erosion when it is couched in terms of disparity between the book value and market value. Restructuring of equity capital of Large Industries seems to be a logical panacea to cure the ills. The only silver lining in the overcast sky of Large Industries of Kanpur is the accumulating net worth though at varying rates and in divergent directions. For a growing firm like LML Ltd. is the useful internal sources to accelerate the growth rates. LML Ltd. has done better than J.K. Jute Mills. It has taken off to the break even level and making accretion to the value of the shares. value of the firm in contrast with J.K. Jute Mills which is decaying. LML Ltd. and J.K. Jute Mills would have to take better care of their projects and their execution to improve net present value.
Findings:

The foregoing discussions raise the following issues:

* The cost of project is very high;
* The projects are classified as risky;
* The additional income from the project is marginal;
* The financing of working capital is done from the permanent sources;
* The Large Industries of Kanpur are saddled with Non-Performing Assets (NPAs).
* There is a disparity between the book value and market value of stocks;
* Accounting Rate of Return (ARR) is far less than the expect Rate of Return ($K_u > r$);
* Internal sources are generated inadequately.
• The equity-debt ratio is high and the funding of project takes place under rigid terms and conditions of the money market.

• There is a problem of loss of the value of the firm in Large Industries of Kanpur;

• Net worth and Liquidity position of Large Industries of Kanpur is not satisfactory;

• The assets are not being used effectively and efficiently.

**Suggestions:**

The analysis of the cost of the projects has highlighted the problems of high cost of projects of Large Industries of Kanpur. The cost can be reduced by trying to extract favourable terms from the suppliers of technology, plant and machinery provided big financial institutions stand by as guarantors of the payment of the cost of the machine. The cost is also high because these are a few countries to enter into joint ventures with Large Industries of Kanpur
viz. Japan and Italy in automobile, U.K. in Jute Mills and Textile Mills. Further, the cost of the project is high because of the slackness in the implementation of the projects due to bureaucratic control, red tapism and procedural delay. The power must be vested with the states for projects.

The investors perception about Large Industries of Kanpur is that the capitalized value of the firm is less than the investments because of poor performance. It is, therefore, necessary that the firm must resort to restructuring of capital so that the problem of disparity between the capitalised value and the investments disappears.

Large Industries of Kanpur have not evaluated the projects on the marginal return and marginal cost of capital invested in the projects. It requires, selection of projects on the basis of the contribution to income. No projects should be selected if marginal income from the project is less than the marginal cost. The extreme point of investment in the project should be determined by equity between marginal income and marginal cost of the
additional projects.

There is little disagreement among experts of financial management that long term investment is not meant for financing current assets. The fair degree of permanent funds for working capital is set by the size of permanent working capital. The excess over the permanent working capital (Temporary or Short term requirements) must be garnered from short term sources.

The term Non Performing Assets (NPAs) is used for non-factory building and large tracts of lands in possession of Large Industries which are unrelated to the real nature of their operations. It is not productive projects for investment to build up Non Performing Assets (NPA). It has the effect of reducing the rate of return having far reaching negative ramifications on Net Present Value (NPV) of the firm. The capital budgeting is justified for investment in productive assets which directly generate income.

The analysis of book value and market value of stocks
reveal a wide disparity. The disparity can disappear after re-evaluating the shares at a level of capitalised value of earning per share. The response of the market would be favourable when market value is either at par or at premium with the face value. The premium is the capital gain for the investors.

\( K \) is determined by the norm for the industry as a whole. For the textile industry, it is around 30 per cent, and for the automobile industry, it is 40 per cent. The Large Industries of Kanpur are far behind the norm. The rate of return of these industries is less than 2 per cent as against the \( K_0 \) (the Average Rate of interest from fixed deposits) 14 per cent. The disparity has got to disappear provided the management proceeds to improve the equity debt ratio and raise the earning.

Large Industries of Kanpur are caught in the vortex of recession since 1990-91. It seems to be the onslaught of global changes in the product market. The capital is not freely accessible. Under such circumstances, equity and reserves must replace the loans and borrowings. At present,
substantial part of the income is hogged by fixed charges to serve loans. It should be possible for Large Industries to build up reserves and equity by restructuring capital and recompositing the assets. The ideal ratio of working capital to fixed assets of Large Industries of Kanpur seems to be 4:1. The internal resources, would take care of high cost of financing ($K_o$).

The high equity debt ratio makes the recompositioning of assets difficult. The low earning make the financial Institutions disinclined to assume high risk which they cover by imposing unfavourable terms and conditions like high rate of 8 per cent return, short term of loan, big margin of safety, first lien, etc. All the problem shave their roots in high debts-equity ratio. The problem would be amenable to solution provided Large Industries of Kanpur proceeds with widening the equity base, reducing the debts and restructuring the capital to make it dynamic and adjustable.

The problem of fast eroding value of the firm is caused by unfulfilled expectations of the investors. The
stocks are selling in the stock market at discount beyond 5 per cent. The problem can be resolved by conversion of the existing equities in the new ones of smaller denominations and by raising Earning Per Share (EPS) ratio.

The capital budgeting of Large Industries is not contributing positively to net worth and liquidity because of limited generation of cash income. It requires revamping of credit policy and economising the cost of operations in addition to getting rid of high debt equity proportion and Non-Performing Assets (NPAs).

The Large Industries of Kanpur suffer from inefficient use of assets as shown by excessive over capitalisation after each successive capital budgeting. The problem can be effectively resolved by changing the composition of the fixed assets and keeping the current assets within fair limits of fixed assets.

In conclusion, the conservative policy learned from the experience of operating in protective market must be discarded. The global tough competition in product market, technology and money market spells out its own dictates
of net worth, sound liquidity, higher IRR, Low K^ and steady cash income generation. Such are the pre-conditions of survival. The capital budgeting alone is guarantee for success of Large Industries of Kanpur provided a hard look is taken by a management to change in accordance with global business environment and its dictates.