CHAPTER - III

FINANCIAL REQUIREMENT OF SSIs

Introduction; Capital structure in small-scale sector; Nature of finance; Credit needs of SSI and the changing role of commercial banks; The social control measure & nationalisation; Rate of interest; Lead-bank scheme; Priority sector; Branch expansion; Regional Rural banks; New committee; Co-ordination between commercial banks & SFCs; Government's policy.
CHAPTER III
FINANCIAL REQUIREMENT OF SMALL-SCALE INDUSTRIES

Introduction:

It is true to said that 'finance is the life-blood' of any industry. Like other industries small-scale and tiny units also require money for meeting various expenses. Most of the entrepreneurs or artisans in this sector are economically weak. "They are poorly placed in the matter of capital formation as they are not in a position to plough back much into the business because of limited profits."¹

The small-scale sector of Assam both modern and traditional is in crying need of finance. As a backward State, capital formation is meagre in Assam. "The local people do not have the necessary capital to start any industry. Entrepreneurs from other places are not attracted to Assam as there are sufficient investment opportunities at home, where the transport system is good, and the market is assured."² Under the circumstances local entrepreneurs are unable to start or run an unit with their own fund and they have to look to other sources for financing their units. It

¹ Dawar, Ram, - Institutional Finance to Small-Scale Industries, 1986, p.33
is true, of course, for all type of industrialists of modern days that it is almost impossible to run an unit entirely from one's own fund.

**Capital structure in small-scale sector:**

It is generally said that the capital structure of a SSI unit is quite simple. "A number of industries commence production without any capital worth mentioning. Even in cases where there is capital, it is invariably contributed by the entrepreneurs or by money borrowed from relatives and shown as capital." However, this does not necessarily imply that one can run a SSI unit without capital.

A small-scale unit generally requires credit (a) for meeting the expenses of acquisition of land and building and installation of plant and machinery and (b) for purchase of raw-materials and to meet other current expenses such as fuel, wages, marketing and production etc. etc. These two types of requirements are commonly known as fixed capital and working capital requirements respectively. The former needs are met by long term loans. While the later one is financed by short term advances, known as working capital loans.

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NATURE OF FINANCE:

Fixed Capital Finance as long term loans:

As already stated fixed capital finance which is required to meet the expenses of fixed assets such as plants and machineries are required by the entrepreneurs in the very beginning of their business. This type of loan is required for long period and generally they are repayable between 10 to 20 years. The entrepreneurs may raise loans from the term lending institutions, that are established for such purposes. "The fixed capital needs are generally met by the State Government (under the State Aid to Industries Act/Rule), SFCs, NSIC, SSICs, SDICs and SBI and other commercial banks." 4

The constituent parts of the fixed capital can be shown as follows:

<table>
<thead>
<tr>
<th>EXHIBIT - III.1</th>
</tr>
</thead>
<tbody>
<tr>
<td>Fixed Capital</td>
</tr>
<tr>
<td>Preliminary expenses</td>
</tr>
</tbody>
</table>

Outlays for factory buildings, plants and machineries etc. are generally planned in advance. But, as the Banking Commission of India, 1972 observed that many of the small-scale units do not maintain proper books of accounts, as a result, it is difficult to estimate the credit requirement for fixed and/or working capital purposes."

Land and building is a major as well as costly component of fixed assets. Most of our small-scale entrepreneurs are unable to construct a building or purchase land. Therefore, these industries are generally run in rented buildings. Although the Government has provided factory buildings under its industrial estates programmes, those units, which are not registered with the State Directorate of Industries and which are not economically or financially viable, cannot get such facilities.

Due to some difficulties only a few units in the small-scale sector are eligible to attain machineries on hire-purchase scheme which is provided by the NSIC and SSIDCs.

Generally, financial institutions provide term loans against securities. For example, SFCs generally...
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prescribe a margin of 25 percent and allow an initial holiday of two years for loan repayment (this period can be increased to 5 years in backward areas). The usual repayment period varies from 7 years to 10 years (to 12 years in backward districts).

All fixed assets are charged to the SFC as security for these advances. ⁶ Besides, they take guarantee of their loan from the promoters/partners or share holders. Again, there is the problem of filling up of a very elaborate application form, required by the financial institutions before giving any loan. Thus, the financial institutions have scrutinised the loan proposed from various points, viz., financial, technical, economic, human etc. so that the viability of the unit can be assessed. But, it has been found by the experience of various State financial corporations as well as Governmental agencies that SSIs are not regarded as sufficiently credit worthy because they are unable to fulfil the criteria laid down by the lending institutions or under the rules of State aid to industries. ⁷ On the other hand, small scale industrial borrowers find it difficult to deal with some factors, such as rigid approach, tight security requirement viability

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assessment of the loan application complicated nature of questionnaire required by the financial institutions.

In spite of these difficulties, specially with refinance facilities from the IDBI, AFC is providing long term loans to SSI sectors of the State. But, as the State Financial Corporations do not have a wide network of branches it was suggested by some policy makers that commercial banks should also provide term loans at the same rate of interest as charged by the SFCs. Observations also was made that the RBI has issued guidelines to banks on July, 1978 and December, 1986 regarding joint/simultaneous appraisal of term loan by State Financial Corporations and banks. However, the commercial banks are generally engaged in lending working capital loan only.

Working capital loan as short term loan:

Working capital loan is required to meet the day to day operations of an unit. 'A borrower needs fund for his operation mainly to buy and stock necessary quantities of raw-materials and stores and to stock necessary quantities of finished goods. If it is the market practice to give credit on sales, he would need funds for carrying his

8. Reserve Bank of India, Meeting of the Standing Advisory Committee to review the flow of industrial credit to SSI sector, 1987. P.2.20.
receivable too. He may also make advance payments for goods and services. All these constitute his needs for funds, to carry current assets.'

In other words, it is needed to complete a working cycle of an industrial unit. The constituent parts of the working capital can be exhibited as follows:

<table>
<thead>
<tr>
<th>EXHIBIT - III.2</th>
</tr>
</thead>
<tbody>
<tr>
<td>Working Capital</td>
</tr>
<tr>
<td>Raw-materials</td>
</tr>
</tbody>
</table>

The different constituent parts of working capital are disclosed by the current assets and current liabilities in the balance sheet of the industrial unit. Inventories,


10. "Working-Cycle", which is also known as operating cycle is characterised by a cycle of operation consisting of purchase of raw-materials, converting the raw-materials into finished goods, sale of finished goods and realising cash. Operating cycle is also called the cash to cash cycle and indicated how cash is converted into raw-materials, works-in-process finished goods, bills and finally back to cash." Sethumadhavi, R. - SSI - Essentials of Financial Management, p.10.
raw-materials, work-in-process, finished goods etc. are placed in current assets side and borrowing from banks other than those against own debentures etc. are placed in the current liabilities side. Working capital is classified into two categories viz., gross working capital and net working capital. Gross working capital refers to total current assets while the non working capital is the excess of current assets over current liabilities. The later concept is adopted by the financing bankers for assessing the requirement of the borrowers. "Ongoing review of gross working capital is essential for efficient management of current assets, however, for a long term view, we have to concentrate on net working capital."\(^{11}\) Gross working capital gives only the quantitative information while the net working capital gives the qualitative information.

It is very important to assess the requirement of working capital correctly. In assessing the requirement of working capital, it is essential to know the operating expenses of the unit, hence the financial statement of the earlier year. As the industrial unit does not require working capital equal to the amount of operating expenses some methods are used to determine the amount of working

\(^{11}\)Sethumadhavi, R. - SSI - Essentials of Financial Management, p.9.
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capital. On such method is as follows\textsuperscript{12} -

\[
\text{Total working capital requirement} = \\
= \frac{\text{Total operating expenses in the last year}}{\text{No. of operating cycles in the year}}
\]

Increase or decrease in prices of inputs are duly adjusted while calculating financial requirement of the next year.

The requirement of working capital of small-scale industries vary from unit to unit, depending on some factors such as (i) the size of the SSI unit (ii) the process of production i.e., short period or long (iii) the price of raw materials and other costs (iv) turn over of inventories, whether it is slow or quick, etc. In assessing the amount of working capital requirement for each level of operating cycle banks and financial institutions examine the above mentioned factors in classified manner. Thus, the operating cycle is very important factor in assessing the working capital needs. 'A manufacturing unit with a short operating cycle can manage comfortably with a relatively smaller amounts of working capital than the one having a large operating cycle and thus needing more working capital.\textsuperscript{13}

\textsuperscript{12}\text{Swaroop, Gopal - Advances to Small Industries and Small borrowers, p.122.}

\textsuperscript{13}\text{Natarajan, R. - Institutional Finance for Small-Scale Industries, p.112.}
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After considering the different components of the operating cycle i.e., the shortage period of raw-materials, stores and spares, finished goods and the factors that affect the period, the banks or financial institutions calculate the permissible limits\textsuperscript{14} for each component. It may be stated here that the whole requirements of working capital of units are not met solely by banks or financial institutions. These are met both by internal as well as external sources. The industrial unit has to arrange some part of the working capital requirement for its own resources and this part is called 'the margin'. Banks generally calculate the permissible limit for each item after deducting the necessary margins from the total working capital requirement. In this case, banks are guided by the Reserve Bank's policy guidelines\textsuperscript{15}.

Normally, commercially banks undertake flexible approach towards small-scale sector in financing working

\textsuperscript{14}The extent to which a bank shall finance is called the permissible limit" - Swaroop, Gopal, - Advances to small-scale industries and small borrowers. P.122.

\textsuperscript{15}For the purpose of assessment of working capital and computation of the permissible bank finance, banks are required to classify assets and liabilities as current and non-current in accordance with the guidelines given in DBOD Circular No. CAS BC 119/C-446-75 dated 31st December, 1975 and further classified in Circular No. IECD CAD(PMS) 101/C. 446(PMS)-85 dated 14th January, 1985 - Reserve Bank of India, Meeting of the Standing Advisory Committee to review the flow of institutional credit to SSI sector, 1987, p.2.14.
capital needs. But, units with working capital requirements above Rs.10 lakhs are required to keep the norms given the "Tandon Committee" and "Chore Committee" accepted by the Reserve Bank of India.

In its recommendation submitted in 1975, the Tandon Committee classified certain industries into distinct groups and fixed inventory/receivables norms for 15 industrial groups; the suggested norms are given in Annexure III.1. The Committee suggested that "these norms should apply to all industrial borrowers, including small-scale industries, with aggregate limits from the banking system in excess of Rs.10 lakhs and extended to smaller borrowers". The Committee recommended that only a part of the "working capital gap" be financed by banks. It suggested three

16. In July, 1974, a Committee was appointed by the RBI under the Chairmanship of Sri Prakash Lal Tandon, which is known as Tandon Committee. The main objective of this Committee were to frame guidelines for follow-up of bank credit, to make suggestion for prescribing inventory norms for different industries and indicate the broad criteria for deviating from these norms, to suggest criteria regarding satisfactory capital structure and sound financial basis in relation to borrowings, to recommend regarding the sources for financing the minimum working capital requirements. etc.

17. In 1979, another Committee was appointed by the RBI known as the Chore Committee, under the Chairmanship of K.B. Chore to examine the prevailing style of bank credit and effectiveness of monitoring and follow-up system adopted by the bank. In this light to suggest modifications in the system with a view to making the system more amenable to rational management of funds by the commercial banks and to suggest alternative types of credit facilities, that will ensure greater credit discipline.


19. 'Working Capital Gap' is defined as the current assets minus current liabilities excluding bank borrowings.
methods for computing the maximum permissible level of bank borrowings. The first method stipulated that banks would finance 75 percent of working capital gap. Remaining 25 percent should come from own funds or other long term sources. According to the second method, the borrower should provide for a minimum of 25 percent of the gross current assets out of long term funds. The rest to be provided by the trade credit, other current liabilities and the bank. The third method is similar to the second method, but excluding core current assets, it should be taken out from the total current assets and separately funded from long term funds.

In its recommendation, the Chore Committee suggested that the borrowers having aggregate working capital limit of Rs.50 lakhs and over would require to conform to second method of lending recommended by the Tandon Committee that will ensure a minimum current ratio of 1.33:1.20 Thus, this method has been made applicable to all borrowers with aggregate credit limit of Rs.50 lakhs and over since December, 1980. The first method of lending continues to apply to all borrowers enjoying aggregate credit limit between Rs.10 lakhs and Rs.50 lakhs and large number of SSI units are enjoying credit limits within the above range.21

20.Report of the working group to review the system of cash-credit, 1979, p.50.
21.Reserve Bank of India, Meeting of the Standing Advisory Committee to review the flow of institutional credit to SSI sector, 1987, p.2.10.
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It is said that this has been prescribed so as to reduce over dependence on bank credit for working capital requirements and to ensure that the basic financial structure is satisfactory. After considering the marketability, fluctuations in prices, possibility of damage etc. banks prescribe the margin on raw-materials, stock-in-process, finished goods, book debts etc. The norms suggested for the North Eastern Region are on very liberal side. In view of the various difficulties encountered by the industrial units set up in the North Eastern Region, the banks are required to take into account the special problems faced by these units in the small-scale sector and allow deviations wherever justified.22

Credit needs of SSI and the changing Role of Commercial Bank

Although the banking activities in an organised manner can be stated to have started with the three presidency banks,23 the industrial sector obtained little attention even during the first few years after independence. "Banks did not give much attention to the credit needs of the small-scale sector of industries."24

22.Ibid. P.2.18.
23.Presidency Banks, viz. the Bank of Bengal, the Bank of Bombay and the Bank of Madras were established in 1909, 1840 and 1843 respectively.
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overcome this problem and also to make bank finance available to the farmers and artisans the Imperial Bank of India has nationalised, which become known as the State Bank of India. The State Bank of India in collaboration with other institutional agencies has instituted the "Pilot Scheme" at nine selected centres, viz., Bombay, Surat, Kolhapur, Delhi, Ludhiana, Agra, Madras, Vijayawada and Coimbatore,\(^{25}\) to provide working capital assistance to small scale industries. Afterwards, the scheme was extended to some more centres. Upto December, 1959, the State Bank of India sanctioned an amount of \textls{5} crores to 1496 small scale units all over the country.\(^{26}\) Different studies conducted by prominent economists reveal that the data related to financial assistance by other commercial banks to SSI in India prior to 1960 is not available. According to the data available with the Reserve Bank of India's Bulletin, financial assistance to small scale sector from the commercial banks including the State Bank of India, during the sixties shows a slow and steady growth. The total amount of commercial bank's outstanding loan with the SSI unit has increased to \textls{194.42} crores in June, 1968 from \textls{27.54} crores in December, 1960. The percentage share of SSI unit in total advances has only 2.5 in 1960, which increased to 3.5 and 6.3 in 1965 and 1968 respectively.\(^{27}\)

\(^{25}\) RBI, Trend and Progress of Banking in India, 1956, p.22.
\(^{26}\) Data collected from the Annual Report of Reserve Bank of India.
\(^{27}\) Ibid.
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The social control measure & nationalisation:

It was observed by the policy makers that the sectoral distribution of credit by the commercial banks was uneven and a major portion of the credit facilities was enjoyed by the large industries and big business houses. "Therefore, to bring about a wider diffusion of banking facilities and changes in the pattern of bank lending, the scheme of social control over banks was initiated by the Government of India in December, 1967."\textsuperscript{28} In order to assess the credit needs and to fix the amount of credit to be granted to different sectors by the banks, the 'National Credit Council' was set up in February, 1968. Further, the council had set up different study groups to prepare proper guidelines of lending to different sectors. Observing the security oriented lending by the commercial banks, one of these study group, viz., the "Dehejia Committee" recommended that "banks should turn to financing of industry on the basis of a total study of the operations rather than on security considerations alone."\textsuperscript{29} Because of the security oriented approach of lending of commercial banks, the small artisans approached the indigenous bankers, moneylenders and friends and relatives for credit at a very high rate of interest. Against this background, the central banking

\textsuperscript{28} Reserve Bank of India, Functions and Working. 4th ed. 1983, p.6.  
\textsuperscript{29} State Bank of India, Monthly Review, June, 1988, p.278.
authority and the Government of India decided to take some concrete steps like opening of more bank offices in the unbanked areas and to cover more and more people in the banking network and to provide finance to neglected areas like small scale industries. Consequently, fourteen commercial banks were nationalised in July, 1969. The subsequent nationalisation of six more commercial banks in April, 1980 brought the total number of nationalised commercial banks to twenty. It is said that after nationalisation, the whole scenario of the banking sector has changed from class banking to mass banking. To encourage the commercial banks in attaining the goals of bank nationalisation, the Central Banking Authority has introduced various facilities, such as provision of refinance at concessional rates of interest, provision of guarantee cover, provision of consultancy facilities, training of the bank staff etc. 30 Besides, the Reserve Bank of India has set up a large number of working groups or committees to study the problems of commercial banks advances to SSI sector, regarding application forms, lending procedure, etc. and suggest measures to curb these bottlenecks, which we have stated earlier.

30. Ibid. P.386.
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Rate of Interest:

In case of SSI units an important aspect of interest rate is that all commercial banks follow an uniform rate. Banks have generally been charging all borrowers who are within the official definition of SSI, a rate \( \frac{1}{3} \) to 1 percent lower than that charged to other sectors. However the rate of interest for SSI differs in accordance with the size of loan, or area of operation. Further, these rates are revised from time to time.

In the meeting of the Standing Advisory Committee, it was suggested that SSI units should be charged 2 percent lower rate of interest than the normal lending rate of interest decided by the RBI, irrespective of the credit limits enjoyed by the unit. But the observation of the meeting was that the "lending rate of scheduled commercial bank are determined taking into account a number of factors such as the growth of the economy and it's sub-sectors, plan-priorities, inflation rate, the pace of monetary expansion, reserve requirements, cost of funds to the banking system and the profitability of the banks etc. so reducing all small-scale industries lending rate to the lowest of the present slab would not be possible as it would jeopardise the viability of banks."\(^{33}\)

33. Reserve Bank of India,-Report of the Meeting of the Standing Advisory Committee to review the flow of institutional credit to SSI sector, 1987, p.2.25.
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On the contrary, steep hike of interest rates is announced by the Reserve Bank of India with effect from 9th October, 1991. These new rates raised by 1.5 percentage point would range from 11.5 percent to 20.0 percent as against the former range from 10.0 percent to 18.0 percent. In case of term loans to agriculture, small-scale industries and transport operators owning up to two vehicles, however, the lending rate for loans between Rs.25,000/- and up to Rs.2 lakhs will be raised by only one percentage point; for loans to these sectors of over Rs.2 lakhs, the rate will be 15 percent (minimum) as in the case of term lending institutions. The effective interest rates on discounting of bills of exchange for borrowers subject to the lending rate of 20.0 percent (minimum) will be one percentage point below the lending rate charged to borrowers in this category and, as such, the effective interest rate on discounting of bills of exchange for such category of borrowers will be 19.0 percent (minimum). 34

The interest rate structure, effective from October, 1, 1991 is stated in Annexure No. III.2.

Although, the rate of interest has been raised, the RBI has suggested the commercial banks to observe 'interest

rate discipline' and asked 'not to starve the small-scale industries of adequate credit.'

The Lead Bank Scheme:

Lead Bank Scheme is the outcome of the recommendations made by one of the 'Study Group of the National Credit Council' and the 'Bankers Committee' appointed by the Reserve Bank of India, soon after nationalisation. According to the Reserve Bank of India, "the Lead Bank Scheme introduced in December, 1969, represents a major step in the appointment of the two-fold objectives of mobilisation of deposits on a massive scale and of setting up of lending to the weak sectors." Under this scheme, all the districts in the country except the metropolitan cities of greater Bombay, Calcutta and Madras and the Union Territories of Delhi, Chandigarh were allotted among the public sector banks and a few private sector banks. The concerned commercial banks were designated as the 'Lead Bank' for that district with a lot of responsibilities to do the needful for the banking development of the concerned district.

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The concept of priority sector:

The concept of priority sector came to be evolved in India in the late sixties to focus attention on the credit needs of certain neglected sectors of the economy—particularly in the rural areas and to ensure adequate credit facilities to them.\(^{37}\) Priority sector consists of Agriculture, small-scale industries, road and water transport operators, retail trade and small business, professional and self-employed, education and setting up of industrial estate upto June, 1980. From June, 1981 onwards it also includes indirect finance to other priority sectors, pure consumption loans and housing loans to weavers and SC/ST.\(^{38}\) After nationalisation, the RBI had introduced various incentives in the form of refinance to commercial banks to increase their lending to the priority sectors. In November, 1974, the public sector banks were advised by the Government of India, that their priority sector lending should reach a level not less than one-third of their outstanding credit by March, 1979.\(^{39}\) The Reserve Bank of India advised the private sector banks also to follow the same guidelines. The RBI set up different committees to suggest norms and guidelines for priority sector lending from time to time. One of such committee is "Ghosh

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\(^{37}\) Dikshit, B.D.-"Financing of small-scale industries and experience of the SBI"—an article published in the Monthly Review,SBI. August, 1988, p.385


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Committee", that was set up on the basis of the decisions taken by the Government of India in March, 1980. Accordingly, the "Ghosh Committee" suggested certain changes in the approach to the priority sector lending. It also introduced a new concept of "weaker-section" within the purview of the priority sector in the two main categories of agriculture and small-scale industries. Accordingly, "all SSIs with credit limit upto and inclusive of ₹25,000/- are to be treated as "weaker-section", in the category advances to "weaker-section" SSIs should constitute 12.5 percent of the total advances to SSIs by 1985."40 Above all, the committee suggested that priority sector advances should constitute 40 percent of aggregate bank advances. On the basis of the recommendation of "Puri Committee", the RBI suggested all commercial banks to make the application forms for loan available in regional languages to the priority sector. Terms and conditions for margin and security for small-scale sectors loans are suggested as follows41-

a) **Margin Money**

<table>
<thead>
<tr>
<th>AMOUNT OF CREDIT LIMIT</th>
<th>MARGIN TO BE MAINTAINED</th>
</tr>
</thead>
<tbody>
<tr>
<td>i) Credit limit upto and inclusive of ₹25,000/-</td>
<td>NIL</td>
</tr>
<tr>
<td>ii) Credit limit over ₹25,000/-</td>
<td>15 to 25 percent (depending upon the purpose and quantum of loan).</td>
</tr>
</tbody>
</table>

41. Reserve Bank of India, Guidelines for advances to Priority Sector, Rural Planning & Credit Deptt., Bombay,1984 p.7.
### b) Security Norms

<table>
<thead>
<tr>
<th>TYPE OF BORROWERS</th>
<th>LOAN/CREDIT LIMIT</th>
<th>SECURITY TO BE FURNISHED</th>
</tr>
</thead>
<tbody>
<tr>
<td>i) Artisan, Village &amp; Cottage Industries</td>
<td>Composite loan upto ₹.25,000/-</td>
<td>Pledge/hypothecation. Mortgage of assets created out of the loans.</td>
</tr>
<tr>
<td>ii) Other Small-Scale Industries</td>
<td>Limit upto &amp; inclusive of ₹.25,000/-</td>
<td>Collateral security/third party guarantee should not be taken.</td>
</tr>
<tr>
<td>iii) - DO -</td>
<td>Limit over ₹.25,000/-</td>
<td>As determined by the bank on the merit of each case.</td>
</tr>
</tbody>
</table>

It is reported every now and then that the banks have already achieved their targets as recommended by the Reserve Bank of India, some banks even lend more to the SSI than the targetted 40 percent of their total advances. Despite this, some changes with reduced priority sector lending obligations of public sector banks are expected to be announced as the Narasimham Committee on financial sector reforms had suggested drastic cut on priority sector lending.
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Branch Expansion:

Branch expansion is one of the main policy measures to fulfil the credit needs of the weaker section and to achieve the goal of mass banking. The number of commercial bank officials in India increased to 58,901 in March, 1990 from 8262 in June, 1969. In other words, it is said that after nationalisation, commercial banks have registered a tremendous growth in branch expansion.

Regional Rural Banks:

The all India Rural Credit Review Committee had observed that despite its speedy implementation of branch expansion programme, the nationalised banks had miserably failed to meet the credit needs of the rural people. It is also observed that till 1974, 60 percent of the production credit needs of the rural people was met by the village money lenders. Against this backward, the Government of India appointed a working group in 1975 and in the month of October of the same year the first five rural banks were established following the Regional Rural Banks Ordinance of September, 1975. The Regional Rural Banks Act was undertaken in 1976 which empowered the public sector banks to sponsor

42. Sitharamayya, C. - "Financing Tiny, Artisan/Village Entreprises" - an unpublished reading material from NISIET, Hyderabad. p.66.
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the RRBs. "A RRB is basically a scheduled commercial bank\textsuperscript{43} but differs from the existing commercial bank in the sense that its area of operation is limited to a specific region in any State."\textsuperscript{44} The rural banks provide assistances to economically weaker sections in meeting their credit requirement.

\textbf{New Committee to look into the credit needs of SSI :}

The RBI has appointed a Committee headed by the Deputy Governor, RBI, Sri P.R. Nayak to review the arrangement of or meeting the working capital needs of SSI, which will also examine any other related matters including the rehabilitation of sick SSI.\textsuperscript{45} The Committee was asked to examine the adequacy of the institutional credit for working capital to the small-scale sector, particularly, with

\textsuperscript{43} Scheduled commercial banks means those which carry on the banking business in India and which (a) have paid-up capital and reserves of an aggregate real or exchangeable value of not less than 8.5 lakhs, (b) are either State Co-operative Banks or companies as defined in section 3 of the Companies Act, 1956, or corporation or companies incorporated by or under any law in force in any place outside India or institutions notified by the Central Government in this behalf and (c) satisfy the RBI that their affairs are not being conducted in a manner detrimental to the interest of thier depositors are eligible for inclusion in the second schedule to the RBI Act, 1934 and when so included."

-Report of the Banking Commission, 1972, p.44.

\textsuperscript{44} Sitharamayya, C. - "Financing tiny, Artisan/Village Enterprises." - an unpublished reading material from NISIET, Hyderabad, p.67.

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reference to the increase in the cost of raw-materials and delayed payments. The Committee will also examine the need for making any modification in the norms of Tandon/Chore Committee.

Co-ordination between Commercial Banks and SFSs:

The question of co-ordination does not arise if the SSI unit borrows its total requirement, long term as well as short term from a non-institutional source. But, as the entrepreneurs borrow different kinds of loans from different institutions, so, reconciliation between different streams is necessary.

If the unit gets inadequate working capital, the fixed capital investment will be useless and vice-versa. This may lead to industrial sickness. Therefore, "it is necessary to ensure that credit given by a lending agency for a viable sick SSI units is not wasted owing to lack of supplemental credit support for other lending agencies." With a view to examine the problems of co-ordination between State Financial Corporations and Commercial Banks, the RBI appointed a Commission in 1971, with R.K. Talwar as

Chairman. On the basis of this Committee's recommendation, RBI issued guidelines in 1974 to all SFCs and Banks for co-ordination.

The Industrial Development Bank of India also constituted a working group in 1976 under the Chairmanship of Sri V.M. Bhide to examine the same problem. The Committee has made several recommendations for commercial banks and financial institutions such as cutting down procedural delays, adoption of common application forms, free exchange of information, stipulation of similar conditions by SFCs and Banks to the extent possible, disbursement of SFCs assistance through Banks, joint efforts for recovery of overdues, diagnostic studies of units facing difficulties etc. etc.

In July, 1978 the RBI again issued detailed guidelines on co-ordination between commercial banks and state financial corporation on the basis of the report of the inter-institutional group. 47

This Committee suggested guidelines on standardisation of documents, exchange of information,

47. This group was constituted with A.K. Bhuchar as convenor and five other members by the RBI.
sharing of cash-flows, nursing of sick-units and asked to constitute a Standing Co-ordination Committee at a high-level comprising representative of the RBI, Commercial Banks and term lending institutions. 48

The RBI again had called a meeting of the Chief Executives of selected SFCs and major commercial banks including IDBI in February, 1986. On the basis of various decisions taken in this meeting, fresh instructions were again issued to banks in December, 1986. In this suggestion, banks were asked to strictly follow the guidelines issued in 1978 in all cases without fail. It is also suggested to sort out any differences that may arised between the SFCs and concerned banks at the initial stage. In case, where the bank concerned is not in a position to take-up appraisal along with SFC, the appraisal taken by the SFC should be accepted by the bank. Banks are also asked to assess the working capital requirement of the units in advance and sanction the working capital three or four months before the units go into production etc.

Again in a circular dated 30th July, 1988, the RBI had emphasised the need to discuss in the SLIIC the cases

where the SFC had sanctioned term loans, but there was delay on the part of the commercial banks, in sanctioning loans and working capital.

It can be observed from the report of the meetings of the SLIIC in Assam the guidelines and suggestions issued by the RBI are not followed by the financial institutions including the commercial banks.

Government's recent policy measures towards the credit needs of the SSI sector:

On August 6, 1991 the Government of India has announced new policy measures for small, tiny and village industries. The main features of this policy regarding financial side is that it is allowed 24 percent equity participation for other than SSI industrial units including foreign companies also. Although, the Government has claimed that this will ensure availability of the much-needed capital for the SSI units besides underwriting their financial viability and technology upgradation and providing marketing support for the SSI units, it might indirectly help the large unit and would lead to destruction of the entire SSI structure policy. As stated by the Indian Council of Small Industries this will be a "backdoor entry of the
large industries into the arena of the SSI sector." However, the Government has assured that this will foster a more practical relationship between the large and the small.

The policy for the first time promises to meet 100 percent credit demand of the SSI and tiny-units. The Government has proposed to withdraw the concessional finance to SSI stating that the primary need is adequate finance, rather than concessional finance. Therefore, it will establish a monitoring cell to observe the genuine credit needs of the small-scale sector.

A limited partnership act is proposed to be introduced to enhance the supply of risk-capital to the SSI sector. It is stated that the proposed act would limit the financial liability of the new and non-active partners/entrepreneurs to the capital invested. In addition, a suitable legislation is also proposed to be introduced to ensure prompt payment of small industries bills. Again, to solve the problem of delayed payments to small-scale sector, it will start, the factoring services through the SIDBI and it proposes to set up a network of such services throughout the country to be operated through commercial banks.
The policy measures also include identification of select industries in large clusters which would be provided financial support by SIDBI for modernisation on a priority basis. The policy also announced the rules and procedures related to establishment and functioning of SSI will be simplified.

There is no doubt that the policy measures contain some encouraging features regarding the credit-needs of SSI sector, however, it will be too early to pass any comment as it's success depends to a great degree on the quality of the downstream action that is required.