CHAPTER - I

INTRODUCTION
Iron and Steel Industry is a basic and core industry and is the backbone of economic growth of any country. It provides basic raw-materials to a very large number of industries such as engineering, machine tools, ship-buildings, railways and many others. Development of iron and steel industry and per capita consumption of steel is considered as extremely reliable index of the level of economic development of a country. The per capita consumption of steel in India is only 24 Kgs which is much less when compared to a world average of 136 Kgs.¹

GROWTH OF IRON AND STEEL INDUSTRY:

Iron and steel is one of the ancient industries in India. The real beginning of this industry in India in the modern form can, however, be traced back to the first decade of the 20th century when the Tata Iron and Steel Company was established in 1907. This was followed by the Indian Iron and Steel Company set up in 1919; the Mysore Iron Works in 1923 and the Steel Corporation of Bengal in 1937.

¹ Business India, September 12-25, 1994.
DEVELOPMENT OF STEEL INDUSTRY DURING PLANNING:

Till the Second Five Year Plan (1956-61), the progress of the steel industry was slow and halting. The entry of the Government in this field in terms of Industrial Policy Resolution of 1948 and 1956. Although the private sector was allowed to expand the old big plants and set up new small ones, the 1956 resolution reserved the right to establish new plants by the Government.

The Second Five Year Plan period (1956-61) saw a remarkable progress in Iron and Steel Industry. During this period, three integrated steel plants were established in collaboration with foreign governments. They are Rourkela Steel Plant, established in 1954 in collaboration with West Germany, Bhilai Steel Plant in 1955 in collaboration with Soviet Union and Durgapur Steel Plant in collaboration with Britain.

In 1966, The Government of India started the 4th steel plant in public sector at Bokaro.

Later in early 1970's, the Government established two more steel plants at Salem (in Tamil Nadu) and Vishakapatnam (in Andhra Pradesh). With the establishment of the Steel Authority of India Limited (SAIL) in 1973, all the public sector steel plants were integrated.
Further Indian Iron and Steel Company (IISCO) in private sector also became fully owned subsidiary of SAIL. The main purpose of establishing SAIL was to centralise policy-making and decentralise administrative and operational responsibilities down to the plant level.

Besides the establishment of new plants by Government, there took place expansion of the old plants in the private sector, particularly during the Second plan period. The Tata Iron and Steel Co. (TISCO) and Indian Iron and Steel Company (IISCO) have planned to increase their production capacities substantially.

MINI STEEL PLANTS AND THEIR GROWTH:

Besides the establishment of public sector plants and expansion of old plants in the private sector, quite a number of mini-steel plants varying between the annual production capacity of 10,000 to 50,000 tonnes of steel came into existence. This is not only meant an addition to the production of steel but also created a new dimensions to the industry, namely the small plants requiring small expenditure of resources to set them up.² By the end of March 1989, there were 173 mini-steel plants with a total capacity of 5.4 million tonnes.

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Out of them, 166 units were in operation and produced 3.7 million tonnes of steel during 1992-93. These mini steel plants account for 30 per cent of steel production in the country.

Mini-steel plants are based not on virgin ore but on scrap. The plants use electric arc furnace. There are many advantages in setting up of mini-steel plants. The gestation period is about two years as against about seven years for integrated steel plants. As a result, the investment in setting up of mini-steel plants is far less prone to generate inflationary pressures on the economy. Mini-steel plants lend themselves to wide geographical dispersal, thus serving to redress regional imbalances in industrial development. These plants have the ability to meet small demands in various specifications which will not be economical for the main producers. The mini-plants have a flexibility in product upgradation.

The production performance of Iron and Steel Industry in India from 1989-90 to 1992-93 is present in the following table No. 1.1. The Iron and Steel Industry has made considerable progress from 1.5 million tonnes of crude steel in 1950-51 to more than 13 million tonnes in 1989-90. The performance of the industry improved further during 1990-91, 1991-92 and 1992-93 with the
## TABLE 1.1
PRODUCTION OF IRON AND STEEL
IN INDIA

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Pig Iron</th>
<th>Saleable Steel</th>
</tr>
</thead>
<tbody>
<tr>
<td>SAIL</td>
<td>991.8</td>
<td>565.1</td>
</tr>
<tr>
<td></td>
<td>(19.0)</td>
<td>(-43.0)</td>
</tr>
<tr>
<td>IISCO</td>
<td>243.1</td>
<td>307.8</td>
</tr>
<tr>
<td>TISCO</td>
<td>7.5</td>
<td>0.4</td>
</tr>
<tr>
<td>VSP</td>
<td>-</td>
<td>520.2</td>
</tr>
<tr>
<td></td>
<td>1242.4</td>
<td>1393.5</td>
</tr>
<tr>
<td></td>
<td>(23.8)</td>
<td>(+12.2)</td>
</tr>
<tr>
<td>Secondary Producers (mainly Mini steel plants)</td>
<td>92.0</td>
<td>102.0</td>
</tr>
<tr>
<td></td>
<td>(-11.0)</td>
<td>(+10.9)</td>
</tr>
<tr>
<td>Total production</td>
<td>1334.4</td>
<td>1495.5</td>
</tr>
<tr>
<td></td>
<td>(20.5)</td>
<td>(+12.1)</td>
</tr>
</tbody>
</table>

Note: Figures in brackets indicate percentage changes over previous year.
economic liberalisation measures taken by the Government such as decontrol, De-licencing of industries.

The output of saleable steel increased from 12.61 million tonnes in 1989-90 to 15 million tonnes in 1992-93 registering a higher increase of 5.9 per cent compared to 4.6 per cent in the previous year. Apart from private sector plants, SAIL plants also performed well in case of saleable steel. The output of mini-steel plants also slightly improved from 3.6 million tonnes in 1989-90 to 3.7 million tonnes in 1992-93. However, their performance was less when compared with 1990-91 when the production was 3.8 million tonnes.

PROBLEMS OF IRON AND STEEL INDUSTRY:

Though the Iron and Steel Industry has made impressive growth, its performance is not considered satisfactory as the country still remains to be the net-importer. This is because the industry is facing many problems. The increasing cost of inputs, technological obsolescence, increasing competition due to the free market economy adopted by the Government are posing serious problems to the Indian steel industry in general. The only way to overcome this situation is to improve its efficiency and be competitive.
The production in mini-steel plants has been reducing due to the fact that the main producers produced and sold more. Number of mini-steel plants became sick due to several factors like short supply of inputs, increased cost of inputs not followed by corresponding increase in their finished goods, inadequate power supply, constraint of working capital and poor management. By the end of March 1992, about 3403 small scale units in iron and steel industry remained sick with an outstanding bank credit of Rs.157.05 crores. In case of non-small scale sector, 114 iron and steel units remained sick with an outstanding Bank credit of Rs.366.98 crores. However, the Government of India has been providing number of facilities to come out of their sufferings.

Even though various reasons are attributed for the poor performance of units both in large-scale sector and secondary sector, like non-availability of coal, power-cuts etc., the inefficiency of management also must have played its role. Hence, there is a need to evaluate the performance of managerial efficiency. Of all the managerial functions, financial function plays an important role as it integrates various other

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functions of an organisation. Often business failures are attributed to financial failures. In the present study, an attempt has been made to evaluate the financial management function of Navakarnataka Steels Ltd., which is a mini-steel plant, located in Bellary of Karnataka State.

Before stating the objectives and methodology of the study, the function and scope of financial management is briefly presented here.

FINANCE FUNCTION:

The activities in any organisation can be broadly classified into three important functions, namely, finance, production, and marketing. Out of these, finance is a very significant function. Problems originating in various areas of organisation have financial implications. Finance is the base on which production and marketing stand. Hence, finance has to be systematically controlled and regulated so that it contributes to the efficiency of different functions of business administration.

Solomon Ezra defined the concept of financial management as "financial management is the blend of art and science through which firms make the important decision of what to invest in, how to finance it, and how to combine the two in order to maximise some appropriate objectives". This definition helps for analytical

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thinking of financial problems of a Firm. The financial management applies to any organisation irrespective of its size, form of organisation and whether it is a manufacturing or service organisation.

The scope of financial management may be divided into three broad areas of responsibility which are:

1. The management of long-term funds (capital structure) associated with the plans for development and expansion involving land, building, machinery, equipment, transport facilities, research projects and so on;

2. The management of short-term funds associated with the overall cycle of activities of an enterprise. These are the needs called working capital needs.

Discharging the above responsibilities is an important function of the financial management which is called "Investment Decision".

In order to invest into selected assets, the financial management decides about the sources and proportion of funds to be mobilised. This is called "Financing Decision". This is concerned with the judicious mix of long-term debt and common equity.
Funds are invested in different assets with an aim of earning profits. The financial management's responsibility extends over managing the profits so earned. It must take wise decisions relating to the allocation of business profits between the shareholders and retained earnings. This function is called "Dividend Decision".

All these three decisions i.e., investment, financing, and dividend are inter-related and should be jointly taken so that financial decision making is optimal. The conceptual framework for optimum financial decision is the foundation of financial management.

In order to know whether the Firm has successfully carried out various functions of financial management, it is necessary to appraise various functions of financial management, namely, Financing, Investment etc. The present-study is an attempt in this direction. The objective of the financial appraisal is to get a deeper insight into the financial condition of a company which provides an overall view of past performance and a basis of future action.

For the purpose of financial appraisal of Navakarnataka Steels Ltd., the operational data contained
in the balance sheets and profit and loss accounts of Navakarnataka Steels Ltd., during the period has been analysed mainly by using the technique of ratio analysis.

A brief profile of Navakarnataka Steels Ltd., is presented here before stating the specific objectives, methodology, and the structure of the study.

PROFILE OF NAVAKARNATAKA STEELS LTD:

The Navakarnataka Steels Ltd., was incorporated on 4th September of 1972 as a private limited company with a primary objective of manufacturing Iron and Steel Ingots to meet the local requirements and providing employment opportunities. The company attained the status of a public limited company in the year 1979 as per the provisions of Sec.43(A) of the Indian Companies Act 1956, on account of its sales growth.

LOCATION:

The company's factory is located about 5 Kms from Bellary city on Anantapur road in a 6-acres site and later expanded on eastern and northern sides by acquiring additional land. Inspite of locational disadvantages, Bellary was choosen taking into consideration that the proposed Vijayanagara Steel Plant will be located at Tojanagal between Bellary and Hospet and Bellary.
would serve as a steel marketing centre serving large areas in Andhra Pradesh and Karnataka. The main disadvantage is the distance to metropolitan markets both in processing raw-materials as well as in selling the finished products.

ACTIVITIES:

With the development-conscious, the company started its activities in the year 1974 as a mini-steel unit. The company has two manufacturing divisions namely:

Melting Division, and
Rolling Division.

In melting division, the company started production in 1974 with a licenced capacity of 9000 M.Ts., and an installed capacity of 10,000 Mts., of carbon steel Ingots. In this division, the company manufactures carbon steel Ingots by melting different types of iron scrap. In order to suit the market needs and ISI specifications, the company undertakes the following range of Ingots production in melting division:

(A) 4" x 4" x 3\(\frac{3}{2}\)" x 4\(\frac{1}{2}\)" x 60" length M.S. Ingots.
(B) ISI specification No.2830.
Rolling Division:

To quench its thirst for further development, the company, in the year 1980, diversified its activities by establishing a rolling mill with a licensed capacity of 5700 M.Ts and with an installed capacity of 6500 M.Ts per year. By using Ingots certain rolled products like Tor Steel Rounds, Plain Rounds and Flats are manufactured in this rolling division. The company undertakes the production of the following range of rolled products.

(a) Tor Steel Rounds: 8 mm x 24 mm, ISI No.1786.
(b) Plain Rounds: 8 mm x 24 mm, ISI No.2062.
(c) Flats: 50 mm x 6 mm upto 125 x 6/8 mm, ISI No.2062.

On an average, the company is producing the rolled products at a maximum of 100 tonnes per day.

GROWTH OF NAVAKARNATAKA STEELS LTD:

Two decades old Navakarnataka Steels Ltd., as a business entity passed through different stages by enjoying success and experiencing grave hardships. In the beginning, it was running under losses but gained momentum and started earning profits by increasing the production and sales for some period. For instance;—
The company's production increased year after year. The production was substantially increased from 2370 M.Ts in 1974-75 to 8745 M.Ts in 1983-84 and reached a further level of 26676 M.Ts in 1992-93.

Similarly, the sales also increased both in terms of volume and value. In 1974-75, it sold Rs.28.97 lakhs worth 2177 M.Ts of ingots which reached a level of 7779 M.Ts worth Rs.325.55 lakhs in 1983-84. The sales in 1992-93 reached a further level of 20090 M.Ts worth Rs.2124.08 lakhs.

The promoters who were of company's development conscious made humble efforts to add to the share capital when necessitated. The company was incorporated with an authorised capital of Rs.20,00,000/- divided into 500 preference shares of Rs.1000/- each and 1500 equity shares of Rs.1000/- each. In 1974, the company started its activities with a paid up capital of Rs.3,00,000/- of 9.5 per cent redeemable cumulative preference share capital and Rs.11,85,000/- of equity capital.

In the year 1975, additional capital of Rs.3,25,000/- was raised by issuing 2000, 12 per cent redeemable preference shares of Rs.1000/- each and 125 equity shares of Rs.1000/- each totalling to Rs.18,25,000/-. In 1988-89, preference shares were redeemed.
by issuing further equity shares in 1987-88 and 1988-89, the company raised equity capital upto Rs.39,75,000/- and the same is maintained at present.

In the direction of maintaining reserves and surplus also the company made good efforts. By the end of 1984, the reserves and surplus reached Rs.43.12 lakhs which was 2 times more than its the then paid up capital.

PROBLEMS OF NAVAKARNATAKA STEELS LTD:

On account of the unsatisfactory business results in the recent years, the company could not increase the level of reserves and surplus. Though it could increase the level to Rs.44.77 lakhs in 1985-86, afterwards nothing is added to it. On the other hand, there is decrease in this level.

As already mentioned, though the Firm slipped by losses in the beginning, subsequently gained momentum and started earning profits. However, due to violent fluctuations in profits, the shareholders could not enjoy dividends regularly. The company used to declare dividends at varying rates between 10 and 12 per cents.

But, unfortunately, the profits started declining from 1980 owing to increased cost of raw-materials
and competition. Though the hike in raw-materials cost is very high, it was not balanced by proportionate increase in selling price. The problem is aggravated further by power-cut imposed by KEB and also frequent increase in power charges. Because, power charges constitute nearly 50 per cent of production expenses in Navakarnataka Steels Ltd. All these factors resulted in regular losses to the company. Such incessant losses in early 1980's caused working capital problem, due to which the firm faced tough scarcity of raw-materials etc., and company could not utilise its installation capacity reasonably and, consequently, the company was to incur continuous heavy losses. The situation turned to worse particularly after 1984 sending the company into sickness and financial distress.

The financial distress mechanism is not an overnight phenomenon. It is a process. It happens in stages. The stages are normally as follows.

Stage 1: The net surplus goes down.
Stage 2: Payment obligations are difficult to be met.
Stage 3: Capacity utilisation goes down.
Stage 4: Working capital position becomes adverse.
Stage 5: Strain in meeting even operational expenses.
Stage 6: Increased borrowed, finance charges and steep increase in outside liabilities.
### TABLE 1.2

**INDICATORS OF SICKNESS IN NAVAKARNATAKA STEELS LTD**

**(1983-84 TO 1992-93)**

<table>
<thead>
<tr>
<th>Year</th>
<th>Net surplus/loss (Rs. in lakhs)</th>
<th>Capacity utilisation</th>
<th>Net-working capital (Rs. in lakhs)</th>
<th>Financial charges (Rs. in lakhs)</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td>M.S. Ingots (in % of installed capacity)</td>
<td>Rolled products (in % of installed capacity)</td>
<td></td>
</tr>
<tr>
<td>1983-84</td>
<td>(-) 11.94</td>
<td>77.15</td>
<td>15.85</td>
<td>24.64</td>
</tr>
<tr>
<td>1984-85</td>
<td>(-) 1.40</td>
<td>64.36</td>
<td>77.68</td>
<td>34.86</td>
</tr>
<tr>
<td>1985-86</td>
<td>0.10</td>
<td>60.52</td>
<td>33.74</td>
<td>43.41</td>
</tr>
<tr>
<td>1986-87</td>
<td>(-) 39.86</td>
<td>64.58</td>
<td>23.62</td>
<td>28.80</td>
</tr>
<tr>
<td>1987-88</td>
<td>(-) 44.54</td>
<td>65.16</td>
<td>18.42</td>
<td>38.36</td>
</tr>
<tr>
<td>1988-89</td>
<td>(-) 83.53</td>
<td>68.94</td>
<td>29.58</td>
<td>95.39</td>
</tr>
<tr>
<td>1989-90</td>
<td>(-) 125.71</td>
<td>38.57</td>
<td>23.03</td>
<td>(-) 30.15</td>
</tr>
<tr>
<td>1990-91</td>
<td>(-) 146.60</td>
<td>43.34</td>
<td>-</td>
<td>(-) 80.78</td>
</tr>
<tr>
<td>1991-92</td>
<td>(-) 68.54</td>
<td>49.48</td>
<td>47.81</td>
<td>110.62</td>
</tr>
<tr>
<td>1992-93</td>
<td>(-) 25.04</td>
<td>64.16</td>
<td>76.91</td>
<td>365.42</td>
</tr>
</tbody>
</table>

Source: Annual Accounts of Navakarnataka Steels Ltd.

Note: 1. Figures in (-) in 2nd column indicate net loss and figures in (-) in fifth column indicate negative net working capital.
Stage 7: Total financial distress.\(^5\)

Many of the above said symptoms of sickness are confirmed in the case of Navakarnataka Steels Ltd. Further the Table 1.2. also indicates certain causes that led the company to sickness.

As is indicated in table 1.2 the company suffered more by shortage of working capital due to which capacity could not be utilised sufficiently for which the company was not able to recover the overhead costs fully and cost of production was not controlled. The capacity utilisation reduced year by year in melting Division. The reduction of capacity utilisation is acute in Rolling Division which is reduced to the lowest of 18.42 per cent of its installed capacity. Further in 1990-91 the production in Rolling Division become nil and during this year the business losses were also very high at Rs.146.60 lakhs. The company could not meet its current obligations which is reflected by negative net working capital position at Rs.30.15 lakhs and Rs.80.78 lakhs in 1989-90 and 1990-91 respectively.

Due to continuous losses the company was not able to meet short-term and long-term loans which resulted in mounting interest charges which interrelatedly became another factor to aggravate losses.

All the above said factors resulted in total financial distress sending the unit into sickness. Due to this protracted financial distress, which started after 1983-84 itself, the unit would have been closed somewhere between 1985-86 and 1990-91 and, primarily, all the employees would have been thrown out of employment creating further socio-economic problems. But, the promoters and members of the old management who had great concern for their unit and employees and creditors made sincere efforts to avert this danger of the unit being closed.

By virtue of the social and political reputation of the promoters and their personal creditworthiness, even though it was difficult, some banks continued to co-operate with the company atleast to maintain its operations. This helped the management to somehow continue with the existence of Navakarnataka Steels Ltd. But, atlast, when it was difficult to manage, the Management moved the Board for Industrial and Financial Reconstruction to declare the unit as sick and save it from being closed.

After studying the problems of the company, the BIFR in 1992 declared Navakarnataka Steels Ltd., as a sick unit in accordance with the provisions of the
On appointing the Canara Bank as operating Agency, the BIFR approved and sanctioned a scheme of Rehabilitation of Navakarnataka Steels Ltd.

According to the above scheme of Rehabilitation, the Management of Navakarnataka Steels Ltd., is taken-over by M/s Bhuwalkas of Bangalore, a stalwart entrepreneurs. The promoters have transferred their shareholdings in favour of M/s Bhuwalkas who were required to bring in sufficient amount to carryout the rehabilitation programme. So also the other financial institution like Canara Bank, KSFC, KSIDC, IRBI have given their consent for rehabilitation scheme and continue their assistance in the form of meeting working capital and long-term needs.

OBJECTIVES OF THE STUDY:

The present study is undertaken with the following specific objectives.

1. To analyse the working capital position in Navakarnataka Steels Ltd., in order to know:
(a) whether the investment in current assets is excessive or shortage;
(b) the financing trend of working capital, and
(c) liquidity position in order to judge the efficiency in working capital management in Navakarnataka Steels Ltd.,

2. To analyse the capital structure of Navakarnataka Steels Ltd., in order to measure the long-term solvency;

3. To analyse the efficiency of Navakarnataka Steels Ltd., in utilizing fixed assets, capital employed and also its profitability.

SCOPE AND PERIOD OF THE STUDY:

The study covers important aspects of financial management in Navakarnataka Steels Ltd., like the management of working capital and liquidity, capital structure, efficiency and profitability. The study covers a period of ten years from 1983-84 to 1992-93.

DATA AND METHODOLOGY:

The study mainly depends on secondary data collected from the annual reports of Navakarnataka Steels
In order to understand various management policies relating to working capital management, fixed assets management, informal discussions with managerial staff were also held.

The data was analysed mainly by using the technique of ratio analysis.

**STRUCTURE OF THE PRESENT STUDY:**

The study is divided into five chapters.

Chapter I deals with the importance of Iron and Steel Industry, need for the present study and objectives and methodology.

Chapter II evaluates the working capital management in Navakarnataka Steels Ltd., by analysing the size, efficiency, adequacy and financing pattern of working capital and liquidity in Navakarnataka Steels Ltd.

Chapter III deals with the analysis of capital structure in Navakarnataka Steels Ltd.

Chapter IV attempts to evaluate the efficiency and profitability of Navakarnataka Steels Ltd.

Chapter V summarises the findings of the study and offers suggestions for the efficient management of financial operations.