CHAPTER I

INTRODUCTION

The corporate sector plays an important role in the economic development of a country. This sector is recognized as a model and democratic form of business enterprise and occupies a pivotal place not only in the industrially advanced economies, but also in the developing countries like India. The process of industrialisation and the development of business activities in these countries are inter-related and inter-dependent upon the growth of the corporate sector. This sector, in turn, operates within the framework of the economic environment, political and social philosophy, and industrial culture.

The corporate sector is the backbone of the Indian economy in so far as it provides a vital, effective and organised system for the growth of the industrial as well as non-industrial sectors of the economy. The contribution of the corporate sector towards the balanced development of various areas of an organised economic activity can easily be seen in the combined efforts of various companies in achieving the goal of industrialisation and increased production and ultimately the maximisation of the gross domestic product (GDP) and the tax revenue to the Government in the form of both direct and indirect taxes. The rapid growth of the joint stock companies in India and the increasing scale of their operations and investments have turned them into the most dominant form of economic organisation. Their impact on the economic and social

1 The corporate sector refers to public and private limited companies in the private sector and all Government companies and non-departmental public sector undertakings.

life of the people far transcends the immediate interests of their shareholders, creditors and employees.

From the ownership point of view, corporate sector may be divided into two categories: (i) private corporate sector, and (ii) public corporate sector. In the private corporate sector, the institutions and the individuals exercise and enjoy legal title, right of possession, control and disposal of assets of an enterprise in their own interest. In the case of the public corporate sector, these rights are vested in such political bodies as municipalities, State and Central Governments and the agencies created by them.3

A significant feature of the present day business in India is the co-existence of both the private and public sectors. The nation's Five Year Plans emphasise the need and importance of both these sectors in the economic development of the country. The role of the private corporate sector is broadly indicated in the development plans. It is expected to operate within the framework of national planning, licensing policies, exchange regulations, price and distribution controls, etc. The Government formulates and implements various policies to promote, regulate and canalise private investment in achieving plan objectives and priorities. It is important, therefore, to understand the economic factors that motivate private investment and other inter-related decisions such as capitalisation pattern; sources of finance (internal and external funds); uses of funds (asset and capital formation); trends in corporate profitability:

and management of earnings.

The ever increasing importance and role of the corporate sector in the economic growth of a country, particularly in developing economy, have attracted several academicians, professional institutions and administrators to conduct diversified studies in the area. Most of these studies relate to the

organisation, management and finances of the corporate sector in the country and selected states. There is hardly any literature on the private corporate sector in the Punjab State. This gap is sought to be filled up by the present investigation. This study has been designed particularly for the in-depth investigation of the financial operations of the private corporate sector in Punjab.

Objectives of the Study

The present investigation was taken up with a view to examining the financial growth and operations of the private corporate sector in the Punjab. Specifically, the study had the following objectives:

1. to investigate the pattern of capitalisation in the sample companies, the selected industries and the private corporate sector in Punjab;
2. to identify the internal and external sources of funds and their relative contribution in financing the business enterprises;
3. to study the extent of their fixed and current asset formation and capital formation.

4 to examine the trends and measure the quantum of their corporate earnings; and
5 to investigate their appropriation of earnings and the trends in the rates of dividends and amounts of retained earnings.

Scope of the Study

While the broad aspects of an organisation are (a) Organisational structure, (b) management, and (c) operations; the operational activities are executive and result from the taking of managerial and technical decisions. Again, the managerial decisions of planning and control are related to the operational activities\(^5\). In this perspective, a study into the financial operational performance indirectly relates to the managerial efficiency and the organisational set up. Moreover, the financial operation is such an important aspect of an organisation that it requires an in-depth study and consideration because the entire structure of any business unit rests on its financial base. Finance is said to be the circulatory system of an enterprise making possible the needed co-operation between diverse segments of activity. It is necessary to organise the finance function in such a way that it should help the business in achieving its objectives with minimum of costs. Keeping this in view, the present study was confined to the financial operations of working companies under the private corporate sector for the period 1967-68 to 1976-77.

Methodology

The present study was aimed at the examination of the financial operations of the private corporate sector of the Punjab State. A three-stage approach was adopted in this study. The collection and tabulation of the data according to individual companies comprised the first stage; data aggregation by industries, the second stage; and compilation of data for the private corporate sector of the State as a whole, the third stage.

Selection of the Sample

In order to select the sample for the present study, the existing joint stock companies registered with the Registrar, Joint Stock Companies, Punjab, H.P. and U.T. Chandigarh located at Jullundur up to 31st March, 1977 were listed and stratified according to standard industrial classification.

It is evident from Table 1.1 that the processing and manufacturing companies accounted for 71.9% of the entire paid-up capital (PUC) of the corporate sector of the Punjab State, while the remaining industrial groups accounted for 28.1%. The average size of the PUC of a company in the former group came out to be Rs. 4.58 lakhs, whereas it was Rs. 1.10 lakhs in the latter groups. Keeping in view the volume of paid-up capital, processing and manufacturing companies were selected for the

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6 The same criterion was adopted by the Reserve Bank of India in its studies on 'Finances of Joint Stock Companies in India'. The studies are being regularly reported in the Reserve Bank of India Bulletins.
<table>
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<th>Code No.</th>
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Table 1.1

### Table 1.1: Industrial Pattern of Joint Stock Companies in Punjab as on 31 March, 1977.

*Source: Government of India, Ministry of Law, Justice and Company Affairs, Department of Company Affairs, New Delhi.*
present inquiry.

In the processing and manufacturing group, there were 54 public and 409 private limited companies. These companies had a PUC of Rs.1,475 and Rs.645 lakhs accounting for 69.6 and 30.4% of the total PUC of the private corporate sector as on March 31, 1977. The average size of the PUC of the public limited companies was estimated at Rs.27.31 lakhs, while that of the private limited companies at Rs.1.58 lakhs. Based on the consideration of volume of the PUC, the public limited companies were selected for the present study. Again, these companies were classified into two categories, (i) those which had operated for 10 years and above and (ii) those which had operated for less than 10 years. The objective of the study being the investigation of the financial operations of the private corporate sector for 10 years the companies in category (ii) were left out of consideration of the present investigation. The companies in category (i) were further categorised into (a) those which were under liquidation and reconstruction, and (b) those which were operating normally. The present study was limited to those public limited companies which functioned normally at the time of the sample selection (viz. category b).

Thus, a sample of 21 public limited companies (Appendix 1.1) was selected for examining the financial operations of the processing and manufacturing group of the private corporate sector of the Punjab State. These companies belonged to such industries as food, sugar, breweries and distilleries, textiles, iron and steel, chemical and pharmaceutical, leather
and leather products, hardboard and printing industries.

**Period of Study**

The present State of Punjab came into existence on November 1, 1966 as a consequence of the division of the erstwhile Punjab into Haryana, Punjab, Union Territory of Chandigarh and transfer of its certain areas to Himachal Pradesh. The present study, therefore, concentrated on the financial operations of the selected companies from the year 1967-68. The study was designed to cover the period from 1967-68 through 1976-77. It was observed that various companies had adopted different accounting periods. Some of them had even changed their accounting year during the decade under study. In such cases the accounts closing on or before 30th June were included in the previous year. In the case of the companies where the accounting year covered more or less than 12 months period, the estimates of the profit and loss were reduced to or blown up to the level of 12 months for rendering them comparable with those of other companies.

**Collection of Data**

The operational activities of the selected business enterprises were studied from their financial statements. These statements brought out the results of the operational activities of the concern over a period of time. To appreciate the operational performance of the private corporate sector, the data were obtained from the annual reports of the sample companies for the years 1967-68 to 1976-77. The information was compiled from the office of the Registrar of Companies, Punjab,
Himachal Pradesh and Union Territory of Chandigarh, located at Jullundur. The senior executives of the sample companies were interviewed to seek clarification. The data available in the annual reports on the working and administration of the Companies Act, 1956 for the years 1967-68 to 1976-77 were also used.

Analysis of the Data

An attempt was made to analyse the financial operations of the private corporate sector as a whole and examine the inter-industry and the inter-company variations in the context of these operations. For this purpose, the available data were studied by computing compound growth rates, ratios, averages, analysis of variance, decomposition measures and common-size profit and loss statements.

The compound growth rates were worked out for the investigation of the trends in paid-up share capital, reserves and surplus, debentures, sources of long-term loans, total borrowings, debt, equity, total gross assets, components of current assets, gross fixed assets and current liabilities. These rates were computed by fitting exponential function of the type.

\[ Y = a b^x \]

where \( Y \) is the value of the character under study; \( x \) the time period and \( a \) and \( b \) the parameters of the equation estimated by the least square method. The compound growth rates were derived from this equation using the relationship:

\[ r = (b-1) \times 100 \]

where \( r \) is the per cent compound growth rate. The significance of \( r \) was tested by applying the student's 't' test as follows:
Despite the fact that the decomposition measures have not been widely used as a tool of analysis, it may be gainfully used for measuring structural changes over the period of years. In many studies relating to financial analysis, this important aspect has not been subjected to rigorous analysis, if not ignored. That is the reason why decomposition measures as a tool was specially chosen for analysing the structural changes in different sources of paid-up share capital, long-term loans, components of gross fixed assets and total current assets which are supposed to have a direct bearing on overall growth, profitability, liquidity and financial position of a company. The following references have been added on page 11 in the Thesis:


2. Lev, B., Accounting and Information Theory, American Accounting Association, Illinois, 1969, Ch. 3 and Appendix A.

Investigate the structural changes in different sources of paid-up share capital, long-term loans, components of gross fixed assets and total current assets. In the decomposition analysis, the total liability of asset portfolios were regarded as given and changes over time in the shares of the total to various portfolios were studied to detect the factors that caused the changes. A summary of the procedure involved in the decomposition analysis is presented in Table 1.2.

Common-size profit and loss statements, often called component percentage or 100 per cent statements, are devices for studying profit and loss statements and changes therein. The data in these statements are shown in analytical percentages by reducing the total revenue to 100 and by stating each individual item as percentage of the total of 100. This technique provides a common basis for the absolute figures and facilitates comparison between two or more years, or between two or more companies, industries or between a single company/industry and between the aggregate statement for the entire industry or the private corporate sector as a whole.

Limitations of the Study

1 The present study dealt only with the public limited companies in the processing and manufacturing industrial classification group of the private corporate sector and excluded private limited companies and companies limited

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\left( \frac{I_d}{I_c} \right) \frac{\log}{\log} \left( \frac{I_d}{I_c} \right) = \frac{I_d}{I_c} \log \left( \frac{I_d}{I_c} \right) \frac{I_d}{I_c}
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The procedure for decomposition measures

Table 1.2
Since the investigation was conducted into the financial operations of the processing and manufacturing companies of the private corporate sector, its results would be applicable to this group of companies alone. The conclusion can however, be extended to other enterprises where similar operational conditions prevail.

The selected companies did not follow uniform accounting period. The financial data were therefore, so organised that they related to twelve months of the relevant year.

The published accounts of the sample companies represented the position as on a particular date at historical prices and did not indicate the average situation for the year.

The present inquiry relied upon the statutory financial statements and published accounts which did not reflect the inside information.

The industry-wise data were generated by clubbing together the sample companies in a particular industry while those of the private corporate sector by pooling the information in respect of selected industries. On the basis of these exercises the industry-wise and corporate sectoral conclusions were drawn, which might not conform to the real situations.

Form of Presentation

The results of the present study have been presented in eight chapters. Chapter I is introductory in nature and
incorporates the objectives, scope, methodology and limitations of the study.

Chapter II discusses the trends in the capitalisation pattern of the sample companies, the selected industries and the private corporate sector of Punjab as a whole.

Chapter III deals with the trends and contribution of internal and external sources of funds in financing their total gross assets.

Chapter IV examines their growth of total gross assets in general and structure and components of fixed assets in particular.

Chapter V analyses their growth of current assets and their components, liquidity position and gross and net capital formation.

Chapter VI investigates the trends and measures the quantum of their corporate earnings.

Chapter VII attempts their appropriation of earnings and highlights the issues related to the provision for depreciation, development rebate reserve, dividend payments and retained earnings.

Chapter VIII summarises the findings.