CHAPTER - III

INDUSTRIAL SICKNESS : CONCEPT, CAUSES, INCIDENCE AND REMEDIES

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CHAPTER - III

INDUSTRIAL SICKNESS : CONCEPT, CAUSES, INCIDENCE AND REMEDIES

3.1 INTRODUCTION :

The previous chapter dealt with the aspects of industrial development of Indian economy in general with special reference to the state of Maharashtra and the Pune Region in particular.

One of the objectives of the present research has been to study the efforts made by nationalised banks towards rehabilitation of sick industries. These efforts interalia cover various stages from identifying the sickness by applying certain criteria on the basis of definitions, analysing the causes and symptoms, making viability study, preparing suitable rehabilitation package on the basis of certain guidelines given by the Reserve Bank of India etc. Hence initially it was considered necessary to study the conceptual frame work about sickness in industries.

In view of the above this chapter is designed to study the all aspects right form the concept of sickness to the remedial measures adopted from time to time to cure the sickness.

3.2 Industrial Sickness : Concept :

Industrial sickness being a technical concept means different things to different people. A sick unit is unhealthy unit to common men, a dividend postponing unit to
investors, a losing and discouraging unit to industrialists, a doubtful debtor and a weak borrower, a victim of technological changes to technocrats, a bad employer to workers and a great wastage of technical and human resources to the country. Thus the central reason of sickness lies with the constant inability of an industrial unit to generate an output larger than its inputs for which operational problems of liability, management and of past losses arise.

The treatment for sick industrial units in Japan is only liquidation of sick units, in U.K. it is state's role for nursing, in West Germany it is vital role of banks and state for financial reconstruction for regaining viability and in France it is a social evil and employment of labour in factories are more vitally guarded with nursing programme. Elimination due to financial weakness is unjust in comparison to protection and nursing sick units to avoid wastage of human and technical resources. The French approach towards sickness is similar to the Indian approach in last decade.

On going through the concept of sickness adopted by developed countries, it can be observed that more stress is given on the "cure" part i.e. rehabilitation. For which the important pre-requisite is proper identification of a sick unit. To identify sickness of a unit, certain criteria are applied by banks and different Financial Institutions. It is very natural that the degree of sickness may vary from unit to unit and industry to industry. Because of this at different situations sickness is identified from different angles. This is reflected in various definitions put forth
by different banks and Financial Institutions.

Different studies have defined the term of industrial sickness differently which is elaborated as under:

i) The first attempt to define a sick unit was made by the State bank of India in 1972 according to which "a unit which is chronically irregular and requires a study to evolve a nursing programme and close followup." This definition was based on the operations of accounts in the bank under Cash Credit Facilities. However, this definition seemed to be incomplete as it did not reflect about the major operations.

ii) The Study Team of the State Bank of India (1975) in its Report on Small-Scale Industry Advances defined a sick unit as "one which fails to generate internal surplus on a continuing basis and depends upon its survival on frequent infusion of external funds. The Finance Bill, 1977 contained a clause defining a sick unit as one whose 50 per cent or more capital and reserve were wiped out the losses. Industrial Development Bank of India (I.D.B.I.) has comprehensively categorised four symptoms of industrial sickness, whereas. Industrial Credit And Investment Corporation of India (I.C.I.C.I.) has laid emphasis on adverse financial viability of a concern.

The Sick Industrial Companies Act 1985 identified sickness in terms of cash losses for two consecutive financial years and accumulated losses equaling or exceeding the net worth of the company at the end of second financial year.
As per the definition given by the Reserve Bank of India, a sick unit is one if it incurs cash losses for one year and in the judgement of the banks is likely to incur cash losses for the current year as well as the following year and which has an imbalance on its financial structure such as current ratio less than 1:1 and a worsening debt-equity ratio (total outside liabilities to net worth).

This definition given by the RBI is widely accepted in banking industry itself and also in other organisations for the identification and rehabilitation of sick units.

At the level of Government of India, sickness gets forced recognition only when an enterprise closes its door or is on the brink of closure, creating a serious unemployment problem.

As per the Sick Industrial Companies Act, 1985 separate definitions are given according to type i.e. Non-SSI sick unit, Non-SSI weak unit and SSI sick unit which are described below.

3.2.2 Definitions in respect of sick industrial companies, weak industrial units and SSI sick units

(i) Non-SSI sick units

A Sick Industrial Company (as defined by the Sick Industrial Companies (Special Provisions) Act, 1985) (SICA) means an industrial company (being a company registered for not less than seven years) which has at the end of any financial year accumulated losses equal to or exceeding its entire net worth and has also suffered cash losses in such financial year and the financial year immediately preceding
such financial year.

For the purpose of this definition:

a) "cash loss" means loss as computed without providing for depreciation;

b) "net worth" is the sum total of the paid-up capital and free reserves;

c) "free reserves" means all reserves credited out of the profits and share premium account but does not include reserves credited out of re-valuation of assets, writeback of depreciation provisions and amalgamation.

The provisions of SICA do not apply to shipping companies and small scale industrial units/ancillary units.

(ii) Non-SSI weak units

It is necessary to make a distinction between 'sick industrial company' as defined in the Act and other industrial units not covered by the Act, in whose cases also sickness will have to be monitored and rehabilitation efforts made for those found to be potentially viable. For the purpose of reporting to the Reserve Bank and taking action in accordance with its guidelines, industrial units in the latter category (excluding SSI units), irrespective of their constitution, have been termed as 'weak' units. An industrial undertaking was earlier classified as 'weak' if, at the end of any accounting year, it had:

a) accumulated losses equal to or exceeding 50 per cent of its peak net worth in the immediately preceding five accounting years.

b) a current ratio of loss than 1:1, and
c) suffered a cash loss in the immediately preceding accounting year.

The definition of non-SSI 'weak' unit has since been modified from March 1989. According to the revised definition, a unit (not being a sick unit) is to be termed as 'weak' if it has at the end of any accounting year accumulated losses equal to or exceeding 50 per cent of its peak net worth in the immediately preceding five accounting years. It is clarified that 'weak' units will include all categories of borrowers, i.e. limited companies, partnership firms, proprietary concerns, etc.

(iii) SSI sick units

Prior to June 1989, a SSI unit was considered 'sick' if it had

a) incurred cash loss in the previous accounting year and was likely to continue to incur cash loss in the current accounting year and has an erosion on account of cumulative cash losses to the extent of 50 per cent or more of its net worth and/or

b) continuously defaulted in meeting four consecutive quarterly instalments of interest or two half-yearly instalments of principal on term loans and there were persistent irregularities in the operation of its credit limits with the bank. While both the conditions (a) and (b) should be satisfied in the case of larger SSI units, it would suffice if either alternative (a) or (b) was satisfied in the case of the tiny and decentralised sector units.
The definition of sick SSI unit was modified in June 1989 as under:

A small Scale Industrial Unit should be considered as sick if it has at the end of any accounting year accumulated losses equal to or exceeding 50 per cent of its peak net worth in the immediately preceding five accounting years. In the case of the tiny decentralised sector also a unit may be considered as sick if it satisfied the above definition. However, in the case of such units, if it is difficult to get financial particulars, a unit may be considered as sick if it defaults continuously for a period of one year, in the payment of interest or instalment of principal and there are persistent irregularities in the operation of the credit limit with bank.

The modified definition of a sick SSI unit which has been given by the RBI in 1993 is as follows:

a) A SSI Unit may be classified as sick when:

Any of its borrowal accounts has been become a 'doubtful' advance i.e. principal or interest in respect of any of its borrowal accounts has remained overdue for a period exceeding 2 and 1/2 years, and

b) there is erosion in the net worth due to accumulated cash losses to the extent of 50 per cent or more of its peak net worth during the preceding two accounting years.

The classification of 'sick' and 'weak' units will not apply to SSI units.

On going through the definitions given by different
authorities and institutions it can be observed that all these definitions inter alia include some criteria for identification of sickness of a unit. The criteria is based on different norms such as financial as well as non-financial indicators. Some definitions exclusively rely on financial performance avoiding non-financial performance or physical health of the unit. Nationalised banks while identifying sickness in case of SSI and non-SSI sick unit takes into consideration the definition given by the RBI and as per the SICA, 1985.

Though there are different views regarding the definition of sickness the signals, symptoms and the causes of sickness are usually have a consensus.

3.3 SIGNALS OF SICKNESS:

The units do not become sick overnight. Sickness is a gradual process with various distant stages. At the early stages, the sickness is seen in the form of disorders in any of the functional areas such as production, marketing, finance, personal etc. which in turn may result in decline in production and sales returning of bills, accumulation of stocks etc. This is the stage when we may say the unit is tending towards sickness. Later on it takes the form of incipient sickness which may mean that the unit has started incurring losses but the financial imbalance i.e. the current ratio and debt equity ratio have not started deteriorating. It may be due to infusion of long term funds by the promoters or due to reserves already available with the unit. Later
on, the unit may reach the stage of sickness as per the criteria laid down by the Reserve Bank of India, and ultimately, to the stage of chronic sickness resulting in closure of the unit.

The Sickness Process

The sickness process is illustrated on next Page.

Initially, a healthy unit may show good cash profit and may have positive values of net working capital and net worth. As it tends towards sickness, the first (cash profit) may become negative although the unit may continue to pay its instalments to the term lending institutions. As sickness grows more and more through other stages, two or more financial parameters may become negative. The negative values do signal sickness. It is these initial stages that require careful monitoring.

3.3.1 Alarm signals for detection of incipient sickness

In most cases, banks are aware of the areas of the weakness even at the time of appraisal. The appraisal system involves balancing weaknesses and strengths. Banks depend on any or mix of the following tools/techniques to get reliable information about state of affairs prevailing in the assisted unit.

1. Position and conduct of accounts
2. Periodical progress reports
3. Visits
4. Reports of nominee-director
5. Miscellaneous - feedback from competitors/suppliers, employees etc.
THE SICKNESS PROCESS

Healthy Unit Criteria
1. Cash Profit +
2. Net Working Capital +
3. Net Worth +

Tending Towards Sickness Criteria
1. Cash Profit / Loss -
2. Net Working Capital +
3. Net Worth +

Incipient Sickness
2 or more - ve

Sick
All - ve

Increasing Sickness or Closure
These are explained below.

1. Position and conduct of accounts

   This can be assessed by answering the following -

   a) Is the account generally fully drawn, indicating a hard core?

   b) Are there frequent excess drawings especially for larger amounts and is there considerable delay in their adjustment?

   c) Are there large drawings indicating diversion of funds for unapproved purposes?

   d) Are cheques for larger amounts issued/paid to parties who are not connected with the line of the borrower's business?

   e) Do the operations consist mainly of cash transactions?

   f) Are drawings mostly in round sums?

   g) Are many cheques drawn by the borrower return for want of funds?

   h) Do delays occur frequently as a result of last minute adjustments in replenishing the account with funds for meeting cheques?

   i) Are the fluctuations and turnover in the account unsatisfactory? If the debit summations are low, it may mean decline in production and/or accumulation of stocks, if credit summations are lower as compared to sales during the period under review, it may mean that the party is not routing entire sale proceeds through the account. It may
also mean party dealing with some other banks.

j) Non-payment of instalments of term loan and frequent requests for change in repayment schedule.

k) Decreasing number of bills tendered and/or frequent and high return of bills.

2. Periodical progress reports

Broadly, the reports obtained by the commercial banks are stock statements, monthly select operational data and quarterly reports under Quarterly Information System. Non-submission or late submission of reports itself may be a symptom of incipient sickness. It is now obligatory for banks to charge penal rate of interest for non-submission or late submission of reports. Besides banks and financial institutions should exchange information on the jointly assisted units. Scrutiny of stock statements may reveal (a) over-valuation of stocks or inclusion of unpaid stocks or obsolete stocks, (b) sluggish turnover of stocks, (c) obtainment of deliveries mostly against lodgement of other goods and (d) high portion of stocks-in-transit. The scrutiny of monthly select operational data and quarterly reports may give under-noted signals of sickness.

- Sales and production falling short of the budgeted figures
- Cost of sales as percentage of net sale on the increase
- Declining profitability as compared to the previous quarter
- Undue rise in creditors for purchases
- Accumulation of statutory liabilities

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- Decline in Net Working Capital as compared to previous quarter
- Large increase in receivables unwarranted by rise in gross sales
- Diversion of short term funds for purposes other than working capital.

3. Visits

As the periodical returns are not submitted by the sick borrowers regularly and promptly, visits by the bankers are regarded as the most important source of detecting disquieting developments. The visit team should be balanced to consist of experts from technical, financial and marketing fields. They should have discussion with Chief Executive Officer, Departmental Heads and key personnel at operating level to report on -

a) Adequancy of management set-up in coping up with the task involved in running the plant in an efficient manner.

b) Performance of plant in regard to daily production, utilisation of installed capacity, availability of essential inputs and utilities, adequacy of technical staff, imbalance in plant capacities, percentage of rejection and quality control system, and areas needing technological importance.

c) Labour relations,

d) Marketing problems,

e) Functioning of accounts and costing departments, and

f) A scrutiny of records kept by Secretary's departments.

The visit team is to give direct feedback to the bankers and its efforts should not be a mere duplication of
information already available with the lenders. It should also be able to detect if a unit has held back a week's output so that to visiting team it appears to be hive of activity.

4. Reports Of Nominee-Directors

The task of nominee-director is not merely to report to the bank about any developments which might affect adversely the interest of the lending bankers but also to identify himself as an active member in the board for helping the Chief Executive of the unit for the overall progress of the company. At the same time, he should not cause undue interference in the affairs of the assisted company. Some of the Do's are as under:

- Make himself acceptable to the other directors.
- Maintain rapport with promoters/executive directors.
- Take interest in company’s affairs to improve.
- Willingness to render all possible and timely assistance.

5. Miscellaneous - feed-back from competitors, suppliers, consumers, employees etc.

Non-financial symptoms are also displayed by the failing units. Low moral and furrowed brows and bad temper of top managers may be the cause of bad days of the unit. A visitor may notice, in case of such units dingy offices, poor maintenance and general air of financial stringency. Customers visiting the unit may notice decline in service, price cuts, firm's tightening credit policies. Suppliers of goods may notice running down stocks or reducing size of orders and taking longer time to pay. Employees might
experience greater resistance to pay increase, cuts in overtime, less generous treatment generally, delay in capital sanctions, rising stocks of outcomplaints and a increasing desperation among the top and later middle management.

A trained or knowledgeable observer could almost certainly see a great number of them of one follows the well-known advice "go there". Sixth Sense or hunch also helps him. However, unfortunately the general tendency is to wait and watch the developments. All those concerned do not assert and in a way conspire in the spread of sickness by being silent spectators. It suits the borrower as well because either he thinks that the bankers have been taken for a ride or he is too scared to discuss the problems with lenders for the fear of precipitation the matter. No doubt, commercial banks are definitely in far better position to receive and detect the signals of incipient sickness first. It has been rightly remarked that 50 per cent of the sickness could be avoided only if banks were alert. Detection of symptoms of sickness and early remedial measures are far more effective than clamouring for special recovery powers by the commercial banks on par with the SFCs and IFCI. In fact, a comparison of SFC assisted units with those which received assistance mostly from commercial banks revealed better overall performance by the latter than those with predominant SFC assistance. It was possible on account of better follow-up by banks.

The branch officials of the banks who are directly in touch with the operations in the borrower's accounts are
under an obligation to identify the early warning signals and report the irregularities noticed to the controlling offices within the specified time so as to enable the banks to initiate corrective steps promptly before the situation worsens.

3.3.2 Symptoms Of Sickness

Sick units start throwing up signals which need to be identified and monitored before the unit becomes gravely sick. A large number of signals are displayed by failing units initially. In the early stages of sickness the warning signs in several functional areas are termed as signals. The persistence of these signals over a long period become symptoms of sickness. The signals gradually merge into symptoms.

Following are some of the important symptoms

a) Continuous irregularity in cash credit accounts;

b) Profit fluctuations, downward trends in sales and stagnation or fall in profits followed by contraction in the share of the Market;

c) Reduction in credit summations - whenever the Companies are in financial difficulty, they open a separate account with another bank and deposit all collections therein;

d) Failure to pay statutory liabilities;

 e) Larger and longer outstanding in the bill accounts;

f) Longer period of credit allowed on sale documents negotiated through the Bank and frequent return by customers;
g) Constant utilisation of cash credit facilities to the hilt and failure to pay timely instalment of principal and interest or term loans and instalments credits;

h) Non-submission of periodical financial debt/stock/statement, etc. in time;

i) Financing capital expenditure out of funds provided for working capital purposes;

j) Decrease in working capital on account of :-

i) increase in debtors and particularly dues from selling agents

ii) increase in creditors

iii) increase in inventories which may include large number of slow or non-moving items;

k) A general decline in that particular industry combined with many failures;

l) Rapid turnover of key personnel;

m) Existence of large number of law suits against the company;

n) Rapid expansion and too much diversification within a short time;

o) Sudden/frequent changes in management - whether professional or otherwise and/or dominated by one man/fet individuals;

p) Diversion of funds for purposes other than running the unit;

q) Any major change in the shareholdings.

Symptoms give clues as to what might be wrong with the unit but they do not provide a guideline for management.
action. The medical analogy is apt: pain and fever are symptoms of an illness, not its cause, and the doctor who treats merely the symptoms may well find himself with a dead patient. So it is with a unit in crisis. What is important—if we are to help the sick unit to recover/rehabilitate—is to find out the basic causes of the unit's problems.

3.4 CAUSES OF SICKNESS:

A unit can become sick for a variety of reasons which can be divided into two main categories: Internal and external. The internal causes arise due to disorder in the unit's various functional areas and are generally controllable in nature provided the corporate management is effective and efficient. The external causes are due to changes in the environment which can be related to social, political, international and other factors which are beyond the control of the unit's management. Some of the important causes relating to the above two categories are:

A. Internal Causes:

1) Planning
   a) Technical feasibility
      Inadequate technical know-how
      Locational disadvantage
      Outdated production process
   b) Economic viability
      High cost of inputs
      Break-even point too high
      Uneconomic size of project
Unduly large investment in fixed assets
Over-estimation of demand.

2) Implementation
Cost overruns resulting from
Delays in getting licences/sanctions, etc.
Inadequate mobilisation of finance.

3) Production
a) Production Management
   Inappropriate product-mix
   Poor quality control
   Poor capacity utilisation
   High cost of production
   Poor inventory management
   Inadequate maintenance
   Lack of timely and adequate modernisation, etc.

b) Labour Management
   Exessively high wage structure
   Inefficient handling of labour problems
   Excessive manpower
   Poor labour productivity
   Poor labour relation

c) Marketing management
   Dependence on a single customer/single product
   Poor sales realisation
   Defective pricing policy
   Booking of large orders at fixed prices in an inflationary market
   Weak market organisation
Lack of market feedback and market research.

d) Financial management

- Poor resources management
- Faulty costing
- Liberal dividend policy
- General financial indiscipline
- Deficiency of funds
- Over-trading

Unfavourable gearing or keeping adverse debt-equity ratio

e) Administrative management

- Over centralisation
- Lack of professionalism
- Lack of feedback to management (Management Information System)
- Lack of controls
- Lack of timely diversification
- Excessive expenditure on R and D

Divided loyalties (where the same management has interest in more than one unit, cases are known where promoters of limited companies who also own private ownership firms tend to look after the interest of the latter, often at the cost of the former)

Dissension within the management
Incompetent management
Dishonest management

B. External Causes

a) Infrastructural bottlenecks

Non-availability of/irregular supply of critical raw
materials or other inputs.
Chronic power shortage
Transport bottlenecks

b) Financial bottlenecks
Non-availability of adequate finance at the right time

c) Government controls and policies, etc.
Government price controls
Abrupt change in Government policies
Procedural delays on the part of the financial/licensing/other controlling or regulating authorities (Banks, RBI, financial institutions, Government departments, licensing authorities, Monopolies and Restrictive Trade Practices Board, etc.)

d) Market constraints
Market saturation
Revolutionary technological advances rendering one's product obsolete

e) Extraneous Factors
Natural calamities, political situation (domestic as well as international) war sympathetic strikes, Multiplicity of labour unions.

According to a survey conducted By Business Times, Bombay the reasons/causes of sickness are as under -

<table>
<thead>
<tr>
<th>Cause</th>
<th>per cent</th>
</tr>
</thead>
<tbody>
<tr>
<td>1. Marketing problem</td>
<td>914.3%</td>
</tr>
<tr>
<td>2. Non-availability of Raw Material</td>
<td>18.1%</td>
</tr>
<tr>
<td>3. Inadequacy of working capital</td>
<td>14.9%</td>
</tr>
</tbody>
</table>
4. Shortage of Power and other source of energy 14.9%
5. Labour trouble 6.8%
6. Faulty/obsolete technology 3.1%
7. High rates of taxes 3.1%
8. Personal Factors 5.0%
9. Other reasons including transport bottlenecks 18.8%

100.00%

The external factors usually affect all the industrial units in the same group while the internal factors may affect a particular unit only and not the whole industry. In such cases, the sickness has an origin followed by several stages of sickness.

Hence, appropriate remedial action would depend on the diagnosis of the causes of sickness and in the identification of the critical parameters responsible for it.

3.5 INCIDENCE OF SICKNESS:

The specter of industrial sickness is assuming frightening proportions and the policy makers and academicians are rightly concerned about it not only because billions of rupees are locked up in thousands of sick units, but because the fortunes of millions are affected by the phenomenon of sickness which pulls down the index of industrial production below the targets fixed by the planners. 7

The sickness of a unit is an event which brings a lot of
mental pain to entrepreneurs, managers and to their families. The society is also affected by this syndrome (sickness), as unemployment goes up availability of goods and services decreases and the cost goes up. The shareholders lose their savings, creditors lose their cash and future business. Ultimately this adversely affects on national income.

One way of measuring the incidence of sickness is to assess the extent of bank funds locked up in sick units.

It is observed from the data published by the RBI in its various Reports that the total amount of bank credit blocked in sick/weak units as at the end of March 1993 stood at Rs.12,500 crore approximately constituted 18.3 per cent of the total outstanding industrial credit, while in 1980 the said percentage was 7.5 per cent. As at the end March 1993 the amount outstanding against sick small-scale units stood at Rs.3,400 crores constituted 16.3 per cent of the total credit to small-scale industries. On the other hand, sick/weak units in the medium and large sector (i.e. non-SSI sick/weak units) constituted around three-fourth of total bank credit locked up in sick/weak units in the country, as on March 1993. The outstanding bank credit locked up in sick/weak medium and large scale units at Rs.9,089 crore constituted around 18 per cent of total industrial credit to medium and large units while at the end of March 1980 the said percentage stood at only 4.8 per cent.

At the end of March 1993 the major incidence of sickness was noticed in the engineering, textiles, chemicals,
paper, iron and steel industries. These five industrial groups accounted for 61.3 per cent of the total number of non-SSI sick units and 64.2 per cent of the total bank credit outstanding against them.

In case of non-SSI weak units, the two industrial groups viz. textiles (173 units - Rs. 567.20) and engineering (105 units - Rs. 457.38 crore) were predominantly affected.

In case of sick small scale industrial sector, though the number of units decreased from 2,45,575 as at the end September 1992 to 2,38,874 as at the end March 1993 the bank credit locked up in these units increased from Rs.3100 crore in September 1992 to Rs.3411 crore in March 1993.

According to observations made by the RBI for industry Ministry Public Sector Banks accounted for 94.3 per cent of aggregate advances to small scale industrial units and 99 per cent of the amount locked up in sick small scale industrial units. Outstanding bank credit to sick small scale industrial units as percentage of the total advances to the sector was highest in State Bank of India group (19.7 per cent) followed by nationalised banks (15.1 per cent) and private sector banks (14 per cent) whereas in the case of foreign banks it was (4.3 per cent) only.

Regionwise And statewise Sickness

a) Non-SSI Sick Units:

The Western Region of the country (comprising Gujarat, Maharashtra, Daman and Diu, Goa, Dadra Nagar Haveli and Madhya Pradesh) accounted for 36 per cent of the total non-SSI sick units and about 41.1 per cent of the total
outstanding bank credit as at the end of March 1993.

As regards state-wise position of non-SSI sick units, the largest number was in Maharashtra, followed by West Bengal, Gujarat, Andhra Pradesh, Tamil Nadu, Uttar Pradesh and Karnataka. These seven industrially advanced states accounted for 74.5 per cent of the total number of non-SSI sick units and 78.5 per cent of the total bank credit outstanding against them.

b) Non-SSI Weak Units:

Region-wise the Western Region accounted for the largest number (267 units) with outstanding bank credit of Rs.658.89 crore.

Statewise the number of non-SSI weak units was the highest in Maharashtra (130 units) with outstanding bank credit of Rs. 329.92 crore, followed by West Bengal (114 units), Uttar Pradesh (91 units) and Gujarat (76 units).

c) Sick SSI Units:

Region-wise, Majority of sick units was from southern Region (comprising Andhra Pradesh, Karnataka, Lakshadweep, Tamil Nadu, Kerla, Pondicherry) which stood at 32.2 per cent, followed by Northern Region (24.3 per cent), Eastern Region (23.2 per cent) and Western Region (20.3 per cent). However, in terms of outstanding bank credit Western Region ranked first (32.3 per cent), followed by Southern Region (29.9 per cent) Northern Region (23.4 per cent) and Eastern Region (14.4 per cent).

Maharashtra was having 20332 sick SSI units at the end
of 1993 having an outstanding bank credit of Rs.561.86 crores. 9

Although total amount of outstanding bank credit blocked in sick units was available, no statistics was available about the number of man-hours lost by the industrial sickness, amount of export business lost due to stoppage/temporary closure due to sickness, number of workers unemployed, amount spent on imports of such items which could not be produced by the indigenous units etc. If this were available then the severity of incidence of industrial sickness would have been better manifested.

Also, no statistics was available on how many industrial units in the country were proned to sickness. If statistics were worked out on some criterion of an industrial unit being proned to sickness, it would more than likely indicate that industrial sickness has been growing at an alarming proportion.

3.5.1 Incidence on Banks/Financial Institutions

The effects on banks of a large volume of sick advances are invariably deleterious. They result in:

a) Erosion of profitability by interest write-offs, loan write-blows, revenue losses from reduced interest rates, and interest funding at zero rates. At the end of 1993-94 the cumulative losses of public sector banks in India were Rs. 8877.41 Crores. 10

b) Tying up substantial resources in problem loaning without definite repayment schedules. At the end of 1993-94 as against the total advances of Rs. 1,25,955 Crores of public
sector banks the overdues were Rs. 22,989 Crores constituting 18.5 percent of total outstanding advances. It is reported that these banks have to spend Rs. 700 Crores on an average per year towards write off of loans, bad debts, sacrifice towards compromise proposal.

c) Non-availability of funds for recycling and thus optimal profitability.

d) Increased share of management responsibilities: Banks are often compelled to assign senior personnel to the infructuous task of serving as nominee directors and exercising "hands-on" control over advances.

e) Loss from opportunity costs as funds blocked in sick industrial units can be more effectively and profitably deployed in normal commercial loaning.

The national economy also suffers as funds tied down in problem loaning are not available for financing development scheme/projects. New units/projects with growth potentials incorporating advanced technology are often denied adequate credit support due to resources constraints imposed on the banks by their failure to recycle their funds.

On this background the question comes that, Why then do banks/financial institutions attempt to revive and rehabilitate sick industrial units instead of simply enforcing their collateral and writing off the residue as a bad debt? The answer has socio-economic implications. In a capital-starved country like India, these capital resources have to be solved and gainfully employed instead of being
allowed to go down the drain. The interests of labour have got to be protected by ensuring adequate levels of employment and the technical skills it has developed is required to be preserved. Even in the developed economics of the west, industries generating high employment and possessing fund of well developed technical skills are kept alive, artificially if necessary, to serve longer national objectives. In developing countries the cost of establishing a new project almost always exceeds the cost of maintaining the existing plant. Social as well as economic reasons, therefore justify the concepts of industrial rehabilitation.

Keeping in view the growing incidence of industrial sickness and the resources blocked in sick units, it is realised that solutions are to be found to rehabilitate sick units and hence to overcome the problem of widespread sickness in Indian industry.

Rehabilitation is a remedy considered for industrial units which have already become sick and are on the verge of virtual collapse.

3.6 REMEDIES:

In a free economy, while such sickness may continues for some time in the hope that the unit would be revived, prolonged sickness would result in the closure and liquidation of the units. While a number of units may have been closed down especially in the small industry, this solution has not found favour as a policy matter. Here it is thought that where promotion of employment has been listed as
a high priority objectives the state is duty-bound at last to protect the existing employment. Secondly, some of the large sick units are located in or around small and medium-size units the economies of which would be dislocated severely by the closure of such units. In other cases powerful trade unions and political considerations do not permit their closures. There is, in the third place, a consideration that such closure will render infructuous capital investment and create an adverse climate for industrial growth. It is for these reasons that Government have adopted a number of measures to rehabilitate sick units to health.

Various Rehabilitation Measures taken at different levels are as under:

3.6.1 Government Measures in Reviving Industrial Sickness

Industrial sickness was first felt by the Government during the late sixties and early seventies. As early as 1965 some of the traditional industries, such as cotton, textiles, Jute, sugar etc. did not carry out replacement and modernisation in time. As a result they were sick and the Government examined the rehabilitation and modernisation needs of these industries. Further, in 1966-67, when the Government experienced industrial sickness, it was largely confined to the eastern region and in and around Calcutta.

It was a result of the Governments' first conscious and well defined policy that an institution named as Industrial Reconstruction Corporation of India was established in Calcutta in 1971. Through this institute, the Central
Government has extended necessary assistance to sick industrial units in the country. The magnitude of industrial sickness has become quite serious in recent years. To curve the dimension of industrial sickness the Government has taken several remedial measures. The objectives of such measures were to revive sick enterprises. Further, the Government has made certain policy pronouncements on sick units from time to time. The various policy measures taken by the Government to revive sick industrial units, are

e) Different Committees on Industrial sickness and f) Legal Framework like Sick Industrial Companies Act on Industrial Sickness and other measures.

**Different Committees on Industrial Sickness**

The Government has from time to time, constituted various committees to examine the problems of growing industrial sickness, namely:

1. **Standing Committee on Industrial Sickness**
2. State Levels Inter Institutional Committee


**Legal Framework** : The provisions available in various statues to achieve the objectives of revival of sick units are namely:

1. Relief Undertaking Act
2. Industries Development and Regulation Act of 1951
3. Companies Act, 1956
4. Income-Tax Act
5. IRBI Act of 1984

Other Measures

For rescheduling of the past excise duties a maximum of two per cent reduction in interest on term loans and waiver of penalty and damage applied to cash credit are among the series of new measures being taken by the Union Finance Ministry and the Reserve Bank of India to rehabilitate sick Industrial units.

Modernisation Funds

Lack of modernisation has been identified as an important cause for industrial sickness. In view of the urgent need for modernisation in the textiles and jute sectors, which also account for major share of industrial sickness, Government has set up two funds viz., the Textile Modernisation Fund (effective from 1-8-1986) and the Jute Modernisation Fund (effective from 1-11-1986). Under these two funds, assistance at concessional rates of interest are provided not only to the healthy units but also to sick but potentially viable units. Special loans on softest terms are given to the weak units for meeting a part of the promoters' contribution. The IDBI is the nodal agency for Textile Modernisation Fund and Jute Modernisation Fund. Further, the government has created the Sugar Development Fund (SDF) which is to be used inter alia for providing assistance to sugar
mills for modernisation and rehabilitation of their plant and machinery. The assistance is deemed as "Promoters contribution" by the financial institutions for the purpose of considering need-based modernisation/rehabilitation proposals.

Non-Resident Indians and Industrial Sickness

The Government has encouraged the non-resident Indians to participate in the revival and rehabilitation programmes of sick industrial undertakings. Further, the Government has decided to permit non-resident Indians to invest bulk funds on repatriable basis in existing sick companies. The bulk investment by the non-resident Indians can either be in the form of sale of shares to them or by issue of fresh capital.

Role of BIFR (Board For Industrial And Financial Reconstruction)

In order to make timely identification and expeditious enforcement of corrective measures in respect of sick industrial companies BIFR has set up in 1987 under the provisions of SICA (Sick Industrial Companies (Special Provisions) Act) 1985. BIFR has wide ranging powers, including change of management, sale or lease of the whole or part of the industrial undertaking, reconstruction including restructuring of share capital by reduction of the interest or rights of share holders, amalgamations and winding up. The Rehabilitation schemes, as sanctioned under the orders of BIFR, with the consent of the banks and financial institutions are binding on all concerned. BIFR operates through 12 operating agencies which are generally the
financial institutions or the banks having maximum exposure in the sick industrial companies and are best placed to work on the viability and rehabilitation schemes.

Under the provisions of SICA, sick and potentially sick companies and banks are required to make reference to BIFR under section 15(1) (2) and under section 23(1), within 60 days. Thereafter, BIFR initiates proceedings, by issuing a notice of enquiry under section 16 and after hearings and necessary correspondences, schemes are formulated in the case of viable units.

During the period 15.5.1987 to 31.12.1994 BIFR registered 1639 sick industrial companies out of these 469 (37 per cent) cases were sanctioned rehabilitation packages.

A perusal of the cases finally decided by BIFR revealed that these units had been spread over 20 state/union territories. The largest number of such cases pertained to Maharashtra (86) followed by Andhra Pradesh (69), Tamil Nadu (53) and others. Looking at the industrywise breakup of the cases decided by BIFR, it is observed that the largest number pertained to textile (85) followed by Metallurgical (78), paper and pulp (38) and chemicals (30).

The analysis about the working of BIFR indicates that it had been playing an important role in tackling the problem of industrial sickness.

3.6.2 Role of the Reserve Bank of India And Banks

The RBI has been taking keen interest in reviving the industrial sickness of the country. It has also influenced
financial institutions to provide rehabilitation packages for
the sick undertakings. The first organised attempt to tackle
the problem was made when the Reserve Bank of India conducted
a seminar on sick industrial units in April 1976. As a
consequence of the seminar, the Reserve Bank of India created
a sick industrial undertaking cell in 1976 in its department
of operation and development. The cell has taken the
following steps in the direction of rehabilitating sick
industrial units:

a) Re-orientation of the attitude and approach of
commercial banks in dealing with the problems of sick
industries so that the large social objectives are not lost
sight of by them.

b) Building up within necessary organisational framework
and expertise to pay specialised attention to sick
industries.

c) Furnishing guidelines and equipping the banks with
the necessary systems to identify the sickness at an early
stage and to take corrective action.

d) Coordinating the efforts of the banks, financial
institutions and other agencies in rehabilitating the
potential viable sick units.

The RBI in order to have a broad idea of the extent of
sickness asked the commercial banks in November 1976 to
furnish it with a quarterly statement showing particulars of
all sick units enjoying aggregate credit limits of Rs. 1
crore and above from the banking system.

The RBI has asked each bank to create a cell at the
central office and regional offices to watch the position of sick industrial units on an on-going basis. The cell is required to find out the reasons for sickness. It has to ascertain whether the unit is viable and if so, to determine the various steps necessary for its rehabilitation.

The importance of the detection of sickness at the incipient stage has been emphasised by RBI. RBI has also emphasised the importance of proper co-ordination between the commercial banks and term-lending institution in the formulation and implementation of rehabilitation packages. Another important measures taken by RBI is the introduction of health code system to categories of various borrowal accounts according to the quality of account for better monitoring and for facilitating preventive action where necessary.

The standing co-ordination committee was appointed in January, 1979 following the recommendations of the inter-institutional group (Bhucher Committee) to consider issues pertaining to co-ordination between banks and term lending institutions. A Committee was appointed by the RBI under the chairmanship of Shri T. Tiwari (the then Chairman, IRCl Ltd.) to look into legal and other difficulties faced by banks and other financial institutions in rehabilitation of sick industrial undertaking and to suggest remedial measures including change in law.

In view of the growing incidence of sickness in the industrial sector, the Chairman and Chief Executives of the commercial banks were advised, in February, 1985 to take, all
possible measures to minimise rising incidence of sickness in their advances portfolio. The need for detection of sickness at an early stage and for undertaking studies to determine the viability as well as formulation of the package programme for rehabilitation of potentially viable units without loss of time was reiterated. The commercial banks were also advised by the Reserve Bank of India to set up a small task-force comprising concerned senior officials to have a detailed critical review of each of the large sick unit for determining the viability and evolving acceptable package of rehabilitation of the viable units.

In 1985 for the first time, the Reserve Bank of India has laid down certain parameters for aid to sick SSI and non-SSI units which were to be followed by banks and financial institutions. These parameters were aimed at accelerating the pace of revival of sick units.

The parameters were further revised in 1987, 1991 and 1995. Those were specially for SSI and non-SSI sick units. Following are the broad contents of these parameters:

a) Interest reduction on loans not more than 2 per cent of prevailing rates charged by bank/financial institutions.

b) Interest @ 10 per cent to be charged on funded interest (subject to annual review);

c) Fresh cash inputs required for meeting part of overdue statutory liabilities, workers' pressing creditors, etc. may be shared by participating banks and financial institutions on 50:50 basis;
d) Further cash losses till break-even and margin for working capital be borne by financial institutions and where non-financial institution is involved, such requirement shall be made by IRBI.

e) Interest on fresh working capital be charged at prevailing commercial rate. Interest at lower rate on such advanced may be charged if concessions from state Government are available;

f) Rehabilitation programme should have an outer limit of 7 years and 10 years in certain special and deserving case;

g) Matching Promoters' contribution in cases involving change of management of professional management and others.

h) Cost of rationalisation of labour be shared by banks and financial institutions;

i) On sick units turning the corner, sacrifices made by banks and financial institutions could be recouped from future profit and cash accruals Alternatively, there may be provision for equity participation.

3.6.3 Role of All-India Financial Institutions in Reviving Sick Industrial Units

All-India financial institutions like IDBI, IFCI, ICICI, LIC, UTI and operating at the All-India level are generally meant for financing comparatively large projects. Out of the above six financial institutions three are all-indian development banks (IDBI, IFCI and ICICI) and the other three are investment institutions, (LIC, GIC and UTI). From amongst the all-India financial institutions the development
banks (IDBI, IFCI and ICICI) have established separate departments for looking into the sick problem cases in their portfolios.

A co-ordinated approach by the all-India financial institutions is made to revive the sick units. The grant of additional assistance/reliefs/concessions in the form of a package which may consist of:

a) Rescheduling of existing loans including funding of interest overdues;

b) Grant of additional loans normally for renovation, modernisation, diversification or balancing equipment;

c) Provisions for additional working capital finance from bank including regularising of existing irregular accounts by transferring the excess borrowing to working capital term loan;

d) Concession in the rate of interest for existing as well as new loan;

e) Strengthening of day-to-day management by appointment of key executives at the top-senior level, constitution of management committee or even change of management committee;

f) Appointment of nominee director;

g) Matching promoters' contribution;

h) Opinion for converting loans into equity (a must);

i) Writing off a part of past dues (done only in very special cases);

j) Seeking assistance of the State Government for
protection under the Relief Undertaking Act, uninterrupted power supply, phased payment of arrears of sales tax and electricity dues, maintenance of industrial peace, rationalisation of about strength, etc.

Rehabilitation Scheme for Small Industries

IDBI has formulated separate schemes for rehabilitation of sick small industries. Assistance is provided through the State level agencies and commercial banks. Further, a Soft Loan Assistance Fund (SLAF) was created by the IDBI for funding the nursing of sick small units. A significant event took place during 1986, when IDBI created a Small Industries Development Fund to provide financial assistance to the small scale sector. The fund is charged with the responsibility of providing refinance assistances not only for development, expansion and modernisation, but also for the rehabilitation of the small scale sick industries.

To sum up, it is observed that time is the essence of any diagnosis and provision of supplementary assistance. But prompt help should only be given to those sick industrial units which show promise of revival. The rehabilitation of sick units is a job that requires patience, firmness and sympathy. No two sick units are alike and therefore, the task of reviving of sick units has to be done by case to case basis. Commercial banks, by virtue of their close contacts with an industrial unit, are in a position to perform this job in a very right manner.
Select References : Chapter - III

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