CHAPTER IX

CONCLUSION: FINDINGS AND SUGGESTIONS

SOCIALIST INDUSTRIALISATION:

It is the logical strategy for India's economic development. The major hurdle in the way of its implementation is that of finance. Only the profits from public enterprises can be relied upon as the propellers of 'socialist industrialisation'. Though both the number and investment in public enterprises have grown fast since independence, they have neither been able to finance their own expansion programmes nor to contribute substantially to the economic growth of the economy as a whole. This state of affairs cannot be allowed to linger on for an indefinite period and the working of public enterprises has to be made such as may enable them to do justice to the oft-repeated saying: "...... socialist industrialisation rests on the profitability of public enterprises."¹

The "management" of the public sector enterprises have held the over-investment in fixed capital, under-utilisation of the capacity created, heavy expenditure on the provision of a township and social amenities, surplus staff and labour trouble responsible for the losses suffered by them. But the authorities on "Financial Management" are of opinion that one of the causes of losses incurred by an enterprise can be located in its imprudent management of working capital. According to them, the lack of an effective and efficient utilisation of working capital either does not permit a business enterprise to earn plausible rates of return on the capital invested or compels it to sustain continual losses.

¹ Om Prakash, The Theory and Working of State Corporations with Special Reference to India (George Allen & Unwin Ltd., London), 1962, p.182.
Public Sector in U.P. has taken rapid strides in recent years. There were only 11 public sector enterprises in 1970 but their number stands at 53 as on 31.3.83, excluding the Electricity Board which is a giant among the U.P. Public enterprises.

Unlike the centrally sponsored public sector enterprises of the Government of India, the U.P. State Enterprises are predominantly in the field of developmental activities. The Manufacturing enterprises exist today in the field of cement, sugar, textile, agro and resin and turpentine. The service enterprises cover the Electricity Board, Housing Board, Road Transport Corporation, Warehousing Corporation, Food and Essential Commodities Corporation and the latest addition is Nalkoop Nirman Corporation.

The Financing and Industrial Development Corporation comprise of the Finance Corporation, PICUP, Industrial Development Corporation, Small Industries Corporation, Panchayati Raj Finance Corporation and the latest addition, being the Industrial Consultants.

The study of working capital management in selected public enterprises has revealed that the imprudent management of working capital had been greatly responsible for the losses borne by them. The turnover of the current assets employed by these undertakings had been both very low and stagnant and the rate of net profit on the same ran in the negative. Thus, public enterprises completely missed the efficiency of the use of working capital which happens to be the most important condition for the running of a business enterprise into adequate profits. In other words, had the public sector enterprises managed to win over their working capital problems, they would have earned sufficient profits.
The study of the current assets-working capital relationship of the undertakings selected for study, points out that the problems of working capital of public enterprises related to the management of inventory, receivables, cash and working finance.

Cash is both the beginning and the end of the working capital cycle. Without cash, the Working capital cycle cannot start, move and function regularly and smoothly. A business unit always tries hard to secure larger cash at the end of working capital cycle than what is invested into it at the beginning in order to (i) benefit its owners (ii) make way for expansion (iii) introduce changes in production techniques and (iv) improve the working conditions of its employees. Inspite of this overwhelming importance, a business unit should also restrain itself from holding cash beyond the irreducible operating needs and observe constantly that its working capital cycle does not suffer from over investment. The carrying of excess cash brings down the rate of turnover of the working capital cycle and consequently the rate of return on capital employed.

Our study has shown that in the various public sector units, the size of cash was on the high side in the case of financial units; Servicing units had maintained satisfactory level of cash. Manufacturing units also maintained excessive cash. In terms of operational requirements also, the size of cash was found to be excessive. However, the working capital cycles were not suffering from over investments as judged by current ratio; this ratio for all units taken together had always been less than standard of 2:1. But this observation did not hold true to all categories of units. Financial units were having a current ratio of more than 2:1
showing that these units had been least zealous to minimise the cash holdings. But in terms of liquid ratio, there appeared a case of over investment in cash. Liquid ratio had always been more than the standard of 1:1. Again this did not apply to manufacturing units in whose cases, the ratio had been lower.

The lack of proper planning and control of cash in public sector units was mainly responsible for such a state of affairs. It is also found from the analysis that these units have strived to invest surplus cash, whenever they have, in fixed deposits so that there could be some sort of return. This would have affected their operational efficiency too.

Receivable in the Public sector units accounted for the second major use of their working capital. It consisted of loans and advances and debtors. It has been found that the efficiency of the use of working funds in receivables had not been satisfactory in the public sector units. The analysis of the size of Receivables has shown that receivables were not managed, on the basis of sound commercial principles. The study of composition of receivables has pointed out that only manufacturing units have invested much of the amount of Receivable in Loans & advances just contrary to the policy of making minimum investments in this very constituent. A study of the size of debtors has shown that financial units have always increased their debtors; however, the rates of growth has been more significant in the case of manufacturing units.

The study of turnover of Accounts Receivables has disclosed that these public sector units have followed a very liberal credit collection policy with the result that the efficiency of collecting the past due accounts
has not been satisfactory. Moreover this observation is not tenable by the analysis of ageing of accounts receivable. It has been observed that servicing units, which were found to have very high collection period have a very low percentage of debtors due over by six months. But this is not the case with manufacturing units. It may be concluded that except manufacturing all other sector units have not been efficient in collecting their accounts.

Inventory constitutes the most important element of working capital of public sector units. It has been observed that inventory accumulation by these units has been at accelerating rates. such rates of accumulation were more pronounced in the case of Servicing Units. A study of both output-inventory and sales-inventory trend relationships has shown that additional investments have been made in inventory by public sector units and the concept of optimum level had never been followed by them. In order to examine the adequacy and effective use of inventory, three ratios were used, analysed and interpreted. An analysis of output-inventory ratio has disclosed that all units taken for study have maintained excessive inventory. Similarly the analysis of sales-inventory ratio had indicated that the bid of the public sector units to reduce over-stocking had been foiled. However, manufacturing units were found to have made effective use of inventory in terms of Sales-inventory ratio. A similar conclusion was arrived at when we analysed the current assets-inventory ratio. The overall analysis made us to conclude that manufacturing units had been trying to maintain a lower amount of inventory but servicing units have failed to do so.
The study of structure of inventory has revealed that raw materials and finished goods have assumed significant place in the case of manufacturing units and spare parts and tools were more significant for servicing units. The inventory of Works-in-progress had been found to be incidentally more important in the case of UPSIDC - a financial unit. The study further disclosed that over stocking existed in finished goods in the case of manufacturing units. In the case of financial units, over stocking was found in works-in-progress. As expected, stores and tools constituted a largest proportion of current assets in the case of servicing units. An analysis of sales - raw materials ratio revealed that manufacturing units had not made proper use of this component. However, these units have made effective use of works-in-progress. Finished goods have also not been properly utilised. Servicing units have failed to make effective use of stores and tools.

The internal as well as the external causes contributed to the overstocking of various types inventory. Internally, the defective inventory management, the uncongenial organisation and the lack of inventory control resulted in accumulation of inventories. Externally, the lack of initial experience in regard to the working of plants in the local conditions, the paucity of indigenous and imported supply and the time-consuming and inordinate delays in the release of foreign exchange and the issue of import licences were the reasons which pressed the public sector under takings to overstock the different types of inventory.

The overall analysis of current liabilities has revealed that the
increase in current liabilities has been very mild affecting adversely the working capital management. It is also found that these units have a major portion of current liabilities in the form of payables to others. It is also evident that manufacturing units have well managed the current liabilities but financial units have failed to do so. While servicing units have been found managing their current liabilities, these units have been found to be maintaining excessive current liabilities by the standard of current liabilities to total assets. In nutshell, the current liabilities management might have affected profitability adversely.

The volume of working capital has varied over the period of study but it has certainly disclosed an increasing trend. An analysis of the volume of working capital of public sector units via the percentage share of individual units had disclosed that the bigger the size of undertaking, the larger had been the size of working capital. Again this had been substantiated by the analysis of change in sales and value of production. It means that causes of the excessive size of working capital were at the root of the expansion in the size of business of public sector units. But this did appear to be true in the case of financial and servicing units.

Pace of transmutation of working capital also affects the size of working capital. Our analysis had shown that all units taken together and also manufacturing units have satisfactory pace of transmutation of working capital. But in the case of servicing units and financial units, transmutation of working capital had been very slow and this had caused the excessive size of working capital in their cases. In addition, the
unfavourable terms of purchases and sales had also inflated the size of working capital.

An analysis of Months Cost of production turnover also indicated that the size of working capital for all units had been more than double of their actual requirements. In terms of months' average Sales turnover, also, the size of working capital was found to be excessive. So far as the financing of working capital is concerned, the Governments directive made it clear that the public sector units were to meet cent per cent of their working capital needs by Cash credit arrangements with banks. The government did not favour the use of depreciation for financing working capital requirements.

Our analysis had shown that these units' dependence upon cash credit was found to be minimum; of course such dependence has improved in the latter years. These units had never approached to the State Govt. for short-term financing. As much as 95 percent of the total working capital was arranged out of depreciation fund or through the diversion of long-term capital funds.

An analysis of working capital's impact on profitability indicated that these units had either negative or low profitability. It was found that the gross profit earned by all units taken together had been very low rather extremely poor. The profitability in terms of return on networth had been low both in terms of standard laid down by Planning Commission as well as in terms of Standard returns earned by private sector enterprises.

Having pointed out the problems of Working Capital Management
of public sector units, we offer the following suggestions for their remedy:

(1) All suggestions regarding the improvement in the management of cash in the public enterprises may centre round the improvement in their techniques concerning planning and control of cash. Firstly, the public enterprise should centralise the administration of their cash funds in a true sense. Secondly, they should regularise their cash flows. Thirdly, they should determine the optimum cash balances to be kept. Fourthly, they should invest their excess cash balances in the short-term securities. In order that all this is done, the working of cash sections in the public enterprises should be modernised. Instead of having a routine and backward-looking approach (which may be taken care of by a clerk), cash sections in the public enterprise should make a forward-looking approach the basis of their functioning.

(2) The public enterprises should administer their credit on the basis of the certain well recognised and established principles of credit administration. This would require the public enterprises to make their credit and collection policies greatly comprehensive, allocate the authority in regard to the credit administration to some specific department, introduce an intelligent system in regard to credit investigation and formulate satisfactory collection policies.

(3) The reduction in overstocking to the normal extent in the public enterprises requires organisation, procedural and structural improvements. Organisationally, the public enterprises should maintain a separate integrated 'Inventory Management Department'. In the absence of such an 'Integrated Management Department', no business enterprise can achieve a substantial
reduction in its size of inventory. Such a department should be placed under the direct control of the managing directors/chairman of the undertakings. Only talented and trained personnel should be recruited to this department. It should be made clear to such persons that they should get a chance to show their skill and receive rewards for the same. This department may be assigned the responsibility of taking care of the following functions:

(i) Materials planning and programming
(ii) Purchasing
(iii) Receiving and warehousing
(iv) Inspection
(v) Stores keeping and issues
(vi) Inventory control
(vii) Disposal of scrap and surplus stores
(viii) Utilisation of by-products.

Procedural improvements may be carried out both at the enterprise and the Government levels in order to reduce the administrative lead time and delivery lead time in the procurement of materials. At the enterprise level, the reduction in administrative lead time necessitates heavy curtailment in the time which the purchasing departments of the public enterprises take in releasing a purchase order. In order that this is done, 'reference to finance' in an undue manner should be relinquished and for doing this, a purchase budget may be prepared in the presence of 'Finance'. In this purchase budget, the details of all categories of purchases should be given and powers to different types of officials
so delegated that the requisite purchases may be made without referring the matter to 'Finance'. Besides, indentors should be asked to submit their purchase requisitions complete in all respects. Moreover, to facilitate as well as control the purchases of very high amounts, the public enterprises may appoint standing committees. In these standing committees, members may be appointed from the 'Finance', 'Research and Development' greatly comprehensive, allocate the authority in regard to the credit administration to some specific department, introduce an intelligent system in regard to credit investigation and formulate satisfactory collection policies and procedures. The investments in loans and advances component of receivables would have to be minimised and for doing this those who got loans and advances would have to be asked to pay the cost of credit. The Government agencies like Port Trust, customs and railways, need not make it a rule for the public enterprises unnecessarily to block heavy funds with them in the form of deposits for long spells. They should change this attitude of theirs and treat the public enterprises on par with the other types of the users of their services. To promote the collection-efficiency in the public enterprises, a monthly report of the overdues may be prepared by the credit departments and submitted to the board of directors for taking suitable action. Likewise, the Central Government and the various State Government may instruct their departments/concerns, etc., to pay the dues of public enterprise in time and 'Production' sides. It should be seen to it that these standing committees meet at an interval of 15 days or so. Further, to reduce the administrative lead time, limits for each stage of purchasing may be laid down. These limits should be realistic.
At the official level, the Government of India and the Chief Controller of Exports and Imports should simplify their procedures relating to the grant of foreign exchange and issue of import licences to the public enterprises, so that they may considerably preune the long lead time in the case of imported materials. Foreign exchange should be granted on an individual basis to the public sector enterprises and after its grant the Ministry of Finance should not come into the picture. The Chief Controller of Exports and Imports should expedite the issue of import licences in not more than 15 days.

So far as the delivery lead time is concerned, steps should be taken to cut it short by installing a regular and standard follow-up procedure in regard to the purchase orders placed with suppliers. Suppliers who do not follow the agreed supply schedules, should be charged severe penalty. More 'sources of supply' should also be developed. In order to reduce the delivery lead time, an attempt should also be made to see that the process of 'inspection of materials' does not take a very long time and the procedure of receiving the goods at the factory does not unnecessarily delay the reaching of materials to the stores.

Structurally, many suggestions merit consideration. To begin with, it may be recommended that an inventory management department should be established by every industrial and commercial public enterprise from its very inception. This must result in the exercise of a technical audit over the recommendations of suppliers with regard to initial and subsequent purchases of stores and spares. Moreover, the coordination among the construction activities at different stages and among the various units
of a plant may also help in solving the problem of 'excessive construction stores.'

The most important structural change, however, relates to the adoption of the various techniques concerning inventory control. It is essential that all the selected public undertakings prepare a list of stores items and then classify and codify them. Standardisation and variety reduction of the stores items should be achieved as early as possible. In order to put these proposals into practice, a separate "cell" in the inventory management department of each public enterprise should be established which should function continuously. The help of the Indian Statistical Institute and other research and development organisations may also be sought in this matter. After the completion of variety reduction and standardisation, an attempt should be made to identify the stores items into 'A', 'B' and 'C' categories. The stock control sections of the different enterprises, after this identification, should fix minimum and maximum levels of items, their ordering frequencies and standard order quantities.

The stores sections in the public enterprises should try their level best to keep correct accounts without committing any unnecessary duplication. In companies like HSL, FCI and HE(I)L, where the number of items in stock is very large, computers may be installed to do the work of stores accounting. Besides, the stores section should evolve satisfactory methods of determining the extent of surplus stores as well as the ways of their disposal. Once the extent of surplus is decided, no time should be lost in disposing of the same.
To reduce the raw materials inventory norms, both for the consumption and stocking of various raw materials should be laid down on a scientific basis and in no case should they be violated in practice.

For reducing the goods-in-process inventory, attempts should be made to shorten the manufacturing cycle of various products of the public enterprises. Further, the goods-in-process should not be allowed to increase on account of the unsound management-labour relations and mismanagement in the plant-level operations.

To reduce the overstocking in the finished goods inventory, the public enterprises should activate their sales departments, improve their demand estimations, carefully decide upon the range of manufacture and enter into firm contracts with customers.

For reducing the overstocking in the stores and spares component of inventory, the public enterprises should promote the import substitution programmes. Ancillary industries should be established and economic and technical help should be rendered to them. Repair facilities in the departments and different units of a concern will have to be allowed to play a vital role in the control of inventories of spares. Further, if the spares inventory is to be reduced, then they will have to be classified according to the nature of consumption, e.g., fast-moving, slow-moving and risk insurance items.
(4) Not to keep a very large amount of working finance during the initial years of their operation, the public enterprises should formulate optimum credit and collection policies, an inventory policy and the policy in regard to the management of cash at their very inception and make it a point to see that they are rightly implemented thereafter. To avoid an excessive size of working finance during the subsequent years of their operation, the public enterprises should accelerate the pace of the transmutation of working capital and bring the debtors'-creditors' ratios to their own advantage.

So far as the financing of working capital is concerned, it would be inappropriate to think that the public enterprises should finance their total working capital requirements from cash credit arrangements with the SBI only. The permanent part of the working capital requirements of the public enterprises should be arranged by the Government in the form of the equity. The variable part of their working capital requirements may be permitted to be financed from the cash credit arrangements with any scheduled bank that has deposits above a certain limit, depreciation reserves and tax provisions, and short-term loans from the Government as and when required. The development of 'factoring institutions' in India may also go a long way in solving the problem of financing the variable needs of working capital of the public enterprises. Simultaneously, the Government should instruct the SBI to cover the needs of the variable working capital of public enterprises to the maximum possible extent expeditiously, at a reasonable cost and without the Government guarantee.

The best course for the public enterprises to finance their perma-
ment and variable working capital needs is to take recourse to profits. But it is no secret that the profitability of the public sector enterprises has remained awfully low in India. Both the Government and the public sector enterprises will have to take a number of measures to reverse this situation.