

Study on Measures to Revitalize State Financial Corporations

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The SFC Act of 1951 was enacted resulting in establishment of 18 SFCs in the country. These Development Financial Institutions had large social mandate as per the prerogative of the State Government. They are the oldest financial institutions. Over the years, they are in poor financial health with question being raised on their efficiency and functioning. Thus, their role needs to be aligned with operational and decision making freedom, technocrat leadership and with diversification of product/service portfolio. This analytical paper focuses on solutions to be adopted by SFCs for improvement in their performances so that they turn into viable State-Level Developmental Financial Institutions. Annual reports of few SFCs and RBI reports have been referred for the analytical review.

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The necessity for the establishment of SFCs in different had been recognised because it was not possible for institution to satisfy the capital needs of the smaller concerns sprouting all over the country, thus, SFC Act, 1951 was passed. At present there are 18 SFCs operating in the country out of which 17 are constituted as Corporation with the exception of Tamil Nadu Financial Corporation which was registered under Companies Act 1956. Thus, SFCs basically acted as prime engine for growth for MSME sector.

Analysis of Problems and its Suggestions:- The growth of the activities of the SFCs had been show and hauling, because of responsible behaviour of SFCS irksome adherence to red-tapism and in-different attitude of government and apex bodies towards performance and development of SFCs yet they are rendering services to MSMEs. To improve the performance and functioning of State Financial Corporations the following suggestions have been given:

SFCs may be allowed either to open or operate a "Bank" like IDBI, ICICI or to function is a Commercial Bank to mobilize low cost funds under different types of deposits and to compete with the commercial banks and other financial intermediaries. It should be a National Level Public Sector Bank. This would help the SFCs to utilize their surplus manpower, which can conveniently be shifted to the banking subsidiaries.

The SFCs suffer from inadequacy of share capital. The SFC Act may suitably be amended creating sufficient scope for Government of India and international agencies for infusing of funds for recapitalisation of SFCs.

The Corporations should tap the capital market to the fullest possible, to meet the fund requirement, such finds should be raised through bonds and

securities.

SFCs may be allowed to float bond with State Government guarantee by entering into the market in a suitable tranche and in such a suitable time depending on favourable market conditions SFCS may be allowed to raise fund at a lower com from international channels too. It must not depend on traditional avenues of resources, the channels of which are dicing up. To cope up with the working capital finance, first hand arrangements should be insisted and a tie-up for working capital finance should be ensured simultaneously with the sanction of term loan to industrial units. If the SFCs are allowed to function as a commercial bank, the paucity of working capital can be solved.

SIDBI does not take any risk on credit given to SFCs as they provide loans to second grade entrepreneurs. It is suggested that the government should take steps to evolve some mechanism so that some relaxation is provided to SFCs in repayment of borrowings/refinance from SIDBI in tune with SFCS, non-recovery of these loans i.e. NPAs.

These development banks should also involve themselves assist the SFCs in timely realization of their loans and for this a joint task force can be more objective and of much use. To enhance the marketability of SFCs/la order to fill up the credit gaps, in case of direct financing by SIDBI, certain amount/limit may be earmarked for SFCs to finance. SFCs have to become more than a single product provider.

The Government of India/RBI should consider allocating substantial share of tax free bonds to SIDBI to ease their fund position, the proceed, of which should be exclusively used to provide refinance support to SFCs at a lower rate of interest.

To limit down NPAs, indiscriminate sanctioning of loans and large-scale concentration of loans in few industries should be avoided. The strategies for containment of NPA's should be to provide security related need based finance to potential/viable sick units for early revival. Separate guidelines for SFCs in the matter of income recognition, provisioning and assets classification should be made considering the default position and realizable market value of available assets. Two broad category of asset classification such as standard and bad & doubtful should be made and reviewed periodically to be realistic.

SFCs should make/evolve some system to identify potential Non-Performing Assets in the lines of commercial banks so that timely corrective/protective measures may be taken up, to reduce the spiral increase of NPAs. Discipline, loyalty and responsibility should be evolved and imposed on first line and second line manager to control the finance to non viable and infeasible projects, which ultimately leads to NPA.

The assets of assisted units should be insured against comprehensive risk by collecting the premium from the borrowers. To improve the poor recovery mechanism, SFCs should cleanse their internal house-keeping and launch a vigorous drive for the recovery of overdue/NPAs. A team of senior executives should monitor the progress of the recovery campaign of NPAs. The staffs so appointed should establish direct contact with the defaulters and explore the possibilities of recovering the dues. Better coordination amongst appraisal, follow up and recovery functions in

SFCs should be evolved, which calls for strong Management Information System. The ABC analysis should be adopted for better results. Special incentive should be given to employees to achieve higher recovery targets. Emphasis on more recycling of own funds and

to improve customers service in terms of cutting down the time consuming lengthy procedure involved in sanction/legal documentation and speedy disbursement of loans, may enable the SFCs to face competition more aggressively. The Government should take necessary steps to provide coverage under Debt Recovery Tribunal to SFCs so that speedy disposal of loans may be ensured thus improving the position of recovery/reduction of NPAs etc.

SIDBI should issue uniform and comprehensive guidelines to SFCs for resorting to the system of "one time settlement" to compromise dues from individual borrowers. Mechanism should be improved to dispose of the assets acquired under Section 29 of the SFC Act 1951 at the earliest so as to get the best deal out of it. To overcome the delays in recoveries, the state government may set up special courts for disposal of applications made under Section 32 of the SFC Act.

To overcome the problem of project cost over run the procedure for granting loans needs to be stream lined, so that the interval between the receipt of an application and actual date of sanction and disbursement of loans be reduced to the minimum. The lending policy may be adjusted in the light of experience gained regarding the financial position of various industries operating in the respective regions. The Corporation's duty does not cease with provision of credit, but it should continue to exercise and constantly watch over the progress of customer enterprises for enabling them to proceed on right lines. The procedure of disbursement of loans for various projects should vary with their sizes.

The Corporations should coordinate with the government agencies e.g. pollution board, electricity board etc. for speedy compliance of their formalities. If the project is delayed from the borrowers end, close follow-up and in-depth/

step to step monitoring of implementation of project should be made by the SFCs.

SIDBI's criteria of re-finance do not favour SFCs and it is biased. SIDBI should not discriminate between refinance allowed to Commercial Banks and SFCs. SIDBI should raise the limit of refinance to 70% and 100% refinance for working capital. The interest charged or refinance should be the same as for commercial banks to provide level playing field to SFCs.

SFCs need to be nurtured and nourished by a single parent, i.e., single national level organization to make them vibrant and operationally viable, to infuse more accountability in the working. It should discharge its duties towards SFCs honestly and sincerely. SIDBI should be assigned with dual role, one operational and other one supervisory. Under the operational role SFCs should function within the operational ambit set by SIDBI, i.e., there should be limit set for SIDBI to provide finance below which SIDBI should not finance and only SFCs to finance below that limit. In its supervisory role, SIDBI should make SFCs function within the policy framework set by it.

Discretionary powers coupled with accountability could speed up credit delivery process. It is the need of the hour to impose accountability on the top-level management; the functionaries and authorities for sanctions and disbursement of loans and advances, Effective surveillance and punishment is not in operation. There should be a committee comprising of professionals and technocrats, which from time to time monitor and observe the appraisals made by the Corporation officials. External influence should be considered while taking a decision. It should be imposed to increase the sense of accountability and responsibility amongst the officials of the Corporations so that contaminated loan portfolio, alarming proportion of non-

performing assets and huge amount of assets in the bad and doubtful category could be controlled more effectively.

State Government/SIDBI should guide SFCs in functioning, administration, sanctioning and disbursement of loans. Political interference of the state government in day to day functioning should be stopped rather it should be on professional basis supported with more technical guidance and assistance from SIDBI, i.e. SIDBI should act as guide for SFCs for day to day functioning. SIDBI should take all possible steps to strengthen administrative mechanism and improve internal monitoring, so as to infuse more professionalism and increase more operational interference.

There is lack of close watch from SIDBI on credit appraisal, a system should be developed to re-examine/ re-appraise certain randomly selected cases which are not refinanced by the apex bodies. SIDBI should not only watch but involve themselves in credit appraisal in order to have more effective credit worthy appraisal.

To have a direct administrative control of the Apex Body/ RBI over the functioning of SFCs instead of bureaucratic administrative control of the State Government, a professional person from SIDBI should be appointed as managing director of SFCs and chairman may be appointed from state government. SIDBI officials comprising one from finance and other from technical side should conduct from time to time internal audit of certain randomly selected cases.

Autonomy should be given to the board of SFCs to take decisions regarding resource mobilization policy and Human Resource Development matters, so that the functioning of SFCs could be more smooth and speedy.

Employees of SFCs may be allowed to purchase the shares of their concerned SFCs to boost up their involvement and belongingness towards the organization. Employees should

be represented in the board of SFCs so as to inculcate a sense of involvement/participation in the management of the affairs of the Corporation.

The employees are appointed by the Government so there is dearth of specialized technical staff resulting in inefficiency in implementing policies. SIDBI should prescribe guidelines in the matter of pay, perks and promotion for the employees of SFCs to be considered finally by the board of SFCs, i.e., a comprehensive system should be introduced for better HRD management. To develop a strong second line management based on professional re-orientation, possibility may be explored to accord priorities for selecting senior officers available in SFCs for filling up important posts of Director.

They lack corporate culture, the staff should be exposed to structural programmes to give their best. Such programmes should be two-tier, one for senior executives and the other for junior and middle level officers. The training module will differ, should be interpreted in nature with a mix of both, skill up-gradation and human resource development. It should cope with the new business environment i.e., merchant banking, lease and hire purchase and capital market services, industrial policy and development in science and technology, loan appraisal, recovery monitoring and loan accounting with necessary funding by SIDBI.

In future, persons having a degree in management with specialization in Engineering, Law, Economics, Statistics, Management Accounting, Finance, Costing etc. should be recruited for managerial position. Basic infrastructure should be developed in the backward regions, and programmes of entrepreneurship awareness should be campaigned in the backward regions so that people could be motivated to set-up more and more new industries and in turn

credit extension in those areas could be ensured.

For development of backward areas certain amount of deposits should be lent by commercial banks to SFCs at the rate 2% below their prime lending rate for infrastructure development of those areas by SFCs.

To co-ordinate between various agencies, SFCs should improve relations with the entrepreneurs, scheduled banks, cooperative banks, other financial institutions, and various agencies involved, which create hindrance to industries in particular, then, these SFCs shall be more effective. Such co-ordination would help, both SFCs and banks in numerous ways for e.g.- appraisal through common form, joint financing, disbursement of instalments, and recovery of instalments and watch over the affairs of the borrowers. The Commercial Bank's branch, act as an agent of the SFCs at a place where SFCs branch does not exist. SFCs must also coordinate with agencies like trade development authorities for market survey and feasibility reports to enable the beneficiaries to sell in foreign market to earn valuable foreign exchange by exporting the projects.

The Corporation should make endeavour to publicize their new policies/schemes regarding finance through various awareness promotional programmes, so that small industrial enterprises get the benefit.

There is a need for well thought-out range policy of branch expansions. It should not expand branches, and recruit non-professional staff without considering their impact on operations.

All branches should function as profit centres, besides looking at the objective of providing the services with better geographical spread. The follow-up format of the SFCs should be revised and it should also contain current operational parameter as well as the specific problems of the industry, so that cases they may

be taken care of, while sanctioning new cases and symptoms of sickness may be identified.

The SFCs should on a regular conduct Entrepreneur Programmes and give turn the industrialisation of the state. SFCs should continue playing the role of credit/service provider to MSMEs. The role of SFCs should not be confined to the traditional business to MSMEs. Its role need to be broad based to cater to the needs of large-scale sector with judicious mix of advantage with no cap on the limit of accommodation.

Conclusion:-

Presently, Indian financial system is passing through second generation reforms which lay emphasis on I.T. intervention, institutional up-gradation, strengthening internal system, attention in prudential norms, capital adequacy, containment of NPAs, functional autonomy and systematic improvements, aimed at developing effective credit delivery system, i.e., redressing of business processes. The future business canvas of SFCs is likely to be affected by stiff competition offered by commercial banks and sister institutions viz., SIDCs, etc. In the wake of WTO provisions coming into play, MSMEs will have to face new challenge. In this context, SFCs role and their institutional and resource raising capabilities will have to be upgraded accordingly.

As a long-term strategy, after re-structuring and re-capitalization as suggested by the Gupta Committee, even when SFCs attain better health, it is important that they should be self-sufficient and sustainable in the long run. Development Financial Institutions are moving towards gradually converting themselves into Universal Banks, i.e., those banks that offer a wide range of financial services, beyond commercial banking, investment banking such as Insurance.

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