UNIT: 5th

INSTITUTIONAL FINANCE TO SMALL INDUSTRIES:

Some of the important institutions financing small scale industries and their functions are discussed below.

Small Industries Development Bank of India (SIDBI):

SIDBI

SMALL INDUSTRIES DEVELOPMENT BANK OF INDIA

➢ The Government of India set up the Small Industries Development Bank of India under a special Act of Parliament in 1989 as a wholly owned subsidiary of the Industrial Development Bank of India with the objective of ensuring larger flow of financial **and non-financial assistance** to the small scale sector.

➢ The Bank commenced its **operations from April 2, 1990 with its Head Quarters at Lucknow.**

➢ In pursuance of the SIDBI (Amendment) Act 2000 and as approved by the Government of India, 51 per cent of equity shares of SIDBI subscribed and held by IDBI has since been transferred to the public sector banks, Life Insurance Corporation, General Insurance Corporation and other institutions owned and controlled by Central Government.

Commercial Banks

- ➢ The scheduled commercial banks in the country comprise the State Bank of India and its associated banks, Nationalised Banks, Private Sector Banks, Regional Rural Banks and Foreign Banks.

➢ for a long period, commercial banks did not come forward to extend financial assistance to the small scale industries because of the SSI's weak economic base.

➢ the first lead in this regard was taken by the State Bank of India in consultation with the Reserve Bank of India in March 1956 by setting up a pilot scheme for the provision of credit for small scale industries.

➢ **The commercial banks started taking initiation in financing small scale industries in a greater way only after the bank nationalization in July 1969.**

Regional Rural Banks Regional Rural Banks (RRBs)

➢ It provides **institutional credit to farmers and artisans in rural areas**.

➢ Initially **five regional rural banks** were set up on October 2, 1975, two in Uttar Pradesh and one each in Rajasthan, Madhya Pradesh and West Bengal.

➢ These banks were **sponsored by the Syndicate Bank, State Bank of India and the Punjab National Bank, United Commercial Bank and United Bank of India respectively.**

- ➢ each regional rural bank has an authorized capital of Rs. l crore and issued and paid up capital of Rs.25 lakhs.
- ➢ The **share capital of RRB** is subscribed by the **Central Government (50 percent), the State Government concerned (15 per cent) and the sponsoring Commercial Bank (35 per cent).**

Co-operative Banks

- Co-operative Banks combine the advantages of private ownership and public good.
- Co-operation is considered **as an instrument of economic development especially in the rural areas.**
- The merits of co-operation are their non-exploitative character, voluntary nature of membership, the principle of one man one vote, decentralized decision making and voluntary curbs on profits.
- Co-operative banks provide loans to agriculturists and rural artisans at low rates of interest and protect them from the clutches of money lenders.
- the organization of co-operative societies in India has a three-tier structure with primary co-operative societies at the village level, Central co-operative societies at the district level and State co-operative banks or apex banks at the state level.

State Financial Corporations (SFCs)

- The Government of India passed the **State Financial Corporations Act in 1951 and made it applicable to all the states.**
- The authorized capital of a SFC is fixed by the State Government within the minimum and maximum limits of Rs.50 lakhs and Rs.5 crores and is divided into shares of equal value which are taken by the respective State Governments, the Reserve Bank of India, scheduled banks, co-operative banks, other financial institutions such as insurance companies and investment trusts and private parties

The functions of the SFCs are to:-

(i) Guarantee loans raised by industrial concerns which are repayable within a period not exceeding 20 years and which are floated in the public market.

(ii) Underwrite the issue of stocks, shares, bonds or debentures of industrial concerns.

(iii) Grant loans or advances to industrial concerns repayable within a period not exceeding 20 years.

(iv) Subscribe to debentures floated by industrial concerns.

(v) Directly subscribe to shares and debentures. –

(vi) Refinance on behalf of SIDBI.

(vii) Discount bills of exchange and

(viii) Act as agents of both Central and State Governments, SIDBI, Industrial Finance Corporation of India, World Bank and other financial institutions in matters connected with the grant of loans or advances or subscription to debentures.

The SFCs have been **entrusted with International Development Association (IDA) credit for assisting small and medium units**. The bulk of the assistance granted by SFCs is to small scale industries including road transport operators. The SFCs have continued to extend liberal financial assistance on concessional terms to industrial units in the specified backward areas.

State Industrial Development Corporations (SIDCs):

➢ The State Industrial Development Corporations were set up under the Companies Act, 1956 as **wholly owned undertakings of the State Governments.**

➢ The objectives of SIDCs are to promote and develop medium and large industries in their respective states or union territories.

➢ SIDCs extend financial assistance in the form of rupee loans, underwriting and direct subscriptions to shares and debentures, guarantees and inter-corporate deposits.

➢ SIDCs undertake a number of feasibility reports, conducting industrial potential surveys, entrepreneurship training and development programmes and developing industrial estates.

➢ Some SIDCs offer a package of developmental services that include technical guidance, assistance in plant location and co-ordination with other agencies.

➢ SIDC are involved in the setting up of industrial growth centres with a view to providing infrastructural facilities for the establishment of industrial units.

State Small Industries Development Corporations (SSIDCs):

State Small Industries Development Corporations were established under the Companies Act, 1956 as State Government undertakings with the specific objectives of promoting and developing small, tiny and village industries in the states and union territories.

SSIDCs perform the following functions:-

(i) Procurement and distribution of raw materials.

(ii) Supply of machinery on hire purchase basis.

(iii) Providing assistance for marketing of the products of small scale units.

(iv) Construction of industrial estates/sheds, providing allied infrastructure facilities and their maintenance.

(v) Extending seed capital assistance on behalf of the state Governments concerned and

(vi) Providing management assistance on behalf of the state Governments concerned.

National Bank for Agriculture and Rural Development (NABARD)

➢ The National Bank for Agriculture and Rural Development was set up on July 12, 1982 by an act of the Parliament.

➢ It is an apex development bank for promotion and development of agriculture, small scale industries, cottage and village industries, handicrafts and other allied economic activities in rural areas.

➢ The objective of NABARD is to promote integrated rural development necessary for the overall prosperity of rural areas in the country.

➢ The NABARD maintains two funds - the National Rural Credit (Long term operations) Fund and the National Rural Credit (Stabilisation) Fund.

➢ The Central and State Governments contribute to the funds.

- The NABARD operates throughout the country through its regional offices located in the capital of all major states.

NABARD

NATIONAL BANK FOR AGRICULTURE AND RURAL DEVELOPMENT

NABARD performing the following functions:

(i) It extends credit support by way of refinance to eligible institutions namely, State Co-operative Agriculture and Rural Development Banks, Commercial Banks, RRBs, and Primary Co-operative Banks for farm as well as nonfarm sectors.

(ii) NABARD provides long term investment credit to farm sector for agricultural and allied activities.

(iii) It extends medium term credit facilities to State Co-operative Banks and RRBs for agricultural purposes.

(iv) Short term credit facilities are extended to State Co-operatives and RRBs.

(v) Refinance is made to nonfarm sectors up to Rs. 0.15 crores to State Cooperative Banks, Primary Co-operative Banks and Commercial Banks enabling them to provide investment credit to rural enterprises.

(vi) Short term credit facilities are extended to RRBs for financing non agricultural activities.

(vii) NABARD extends refinance to banks for financing development of non conventional energy sources and Government programmes like Swarnajayanthi Rozgar Yojana, Prime Ministers Rozgar Yojana (PMRY) etc.

NABARD (Amendment) Bill, 2017

Parliament has passed the National Bank for Agriculture and Rural Development (Amendment) Bill, 2017 with the approval of Rajya Sabha. Lok Sabha already had passed the bill in August 2017.

Key Features of the Bill

- The Bill allows Union Government to increase capital of NABARD from Rs. 5000 crore to Rs 30,000 crore.

  • It allows Union Government to increase the capital more than Rs 30,000 crore in consultation with the Reserve Bank of India (RBI), if necessary. • The Bill provides that Union Government alone must hold at least 51% capital share of NABARD.
- It transfers share capital held by RBI valued at Rs. 20 crore to Union Government. Currently RBI holds 0.4% of paid-up capital of NABARD and remaining 99.6% is held by Union government and this causes conflict in RBI's role as banking regulator and shareholder in NABARD.
- The Bill replaces terms 'small-scale industry' and 'industry in tiny and decentralised sector' with terms 'micro enterprise', 'small enterprise' and 'medium enterprise' as defined in MSME Development Act, 2006.
- It allows NABARD to provide financial assistance to banks if they provide loans to the MSMEs.
- The Bill substitutes references to provisions of the Companies Act, 1956 with references to the Companies Act, 2013.
- It includes provisions dealing with definition of a government company and qualifications of auditors.

National Small Industries Corporation (NS1C): *The vision of NSIC is "To be premier organization fostering the growth of Micro, Small and Medium Enterprises in the country."*

The **main functions of the National Small Industries Corporation are**:

(i) To provide small scale industries with modern machines on a hire purchase basis.

(ii) To assist small enterprises to participate in the stores purchase programme of the Central Government

(iii) To develop small scale industries as ancillary units to large industries.

(iv) To arrange the marketing of products of small industries and promoting.

(v) To import and distribute components and parts to specific small scale units and

(vi) To construct industrial estates and establish and run prototype production cum training centres.

Industrial Reconstruction Bank of India

• The Government of India **set up the Industrial Reconstruction Corporation of India (IRCI) in April 1971,** under the Indian Companies Act

It was established mainly to look after special problems of sick units' and provide assistance for their speedy reconstruction and rehabilitation, if necessary, by undertaking the management of the units and developing infrastructure facilities like those of transport, marketing etc.

• In 1984, the Government of India passed an Act converting the Industrial Reconstruction Corporation of India (IRCI) into the Industrial Reconstruction Bank of India (IRBI).

• IRBI was established in March 1985 to take over IRCI.

• With a view to converting the institution into a full-fledged development financial institution, IRBI was incorporated under the Companies Act 1956, as Industrial Investment Bank of India Ltd. (IIBI) in March 1997.

➢ The National Small Industries Corporation Ltd. was **established in 1955** by the Government of India as per the recommendations of the International Planning Team of Ford Foundation, its objectives are to aid, assist, counsel, finance, protect and promote the industries in the country.

➢ The **NSIC assists small scale industries** through its various schemes such as hire purchase, equipment leasing, marketing, export, raw material assistance and single point registration scheme.

The following functions were laid down for the IRBI:

(i) To **provide financial assistance** to sick industrial units.

(ii) To **provide managerial and technical assistance** to sick industrial units,

(iii) To **secure the assistance** of other financial institutions and government agencies for the revival and revitalisation of sick industrial units,

(iv) To **provide merchant banking services** for amalgamation, merger, reconstruction, etc.,

(v) To **provide consultancy services** to the banks in the matter of sick units, and

(vi) To **undertake leasing business**.

Federation of Associations of Small Industries of India

- FASII is the **apex body of micro, small, village, cottage and rural enterprises in the country**.
- FASII was **ushered into existence in the year 1959** under the sponsorship of the Government of India in response to the recommendation of the "Ford Foundation Team" which visited India in the year 1953.

FASII's **Headquarter at Delhi** was inaugurated by Dr. Radhakrishnan, the then President of India in the year 1963.

- Owing to its dense membership strength FASII is given representation in all the councils and committees connected with Micro and Small Enterprises of the Centre as well as State governments.
- **Minister of State for External Affairs is the "Patron-in-Chief"** of the Federation of Association of Small Industries of India (FASII).

MICRO FINANCE:

Microfinance, also known as microcredit, is a financial service that offers loans, savings and insurance to entrepreneurs and small business owners who don't have access to traditional sources of capital, like banks or investors. The goal of micro financing is to provide individuals with money to invest in themselves or their business.

Micro financing institutions

Microfinance is available through microfinance institutions, which range from small non-profit organizations to larger banks. These institutions include for-profit companies, like General Electric Consumer Finance and Citi Microfinance, as well as non-profit organizations, such as Kiva, Accion and BRAC. They offer small loans and help set up and maintain a savings account, and they assist borrowers in obtaining insurance for a variety of needs, such as death, illness or loss of property.

Pradhan Mantri mud₹a Yojna

Micro Units Development & Refinance Agency Ltd (MUDRA)

Micro Units Development & Refinance Agency Ltd. (MUDRA) is a new institution set up by Government of India to provide funding to the non-corporate, non-farm sector income generating activities of micro and small enterprises whose credit needs are **below ₹10 Lakh**.

MUDRA has been initially **formed as a wholly owned subsidiary of Small Industries Development bank of India (SIDBI)** with 100% capital being contributed by it. Presently, the authorized capital of MUDRA is 1000 crores and paid up capital is 750 crore, fully subscribed by SIDBI. More capital is expected to enhance the functioning of MUDRA.

Agency would be responsible for **developing and refinancing** all Micro-enterprises sector by supporting the finance Institutions which are in the business of lending to micro / small business entities engaged in manufacturing, trading and service activities. MUDRA would partner with Banks, MFIs and other lending institutions at state level / regional level to provide micro finance support to the micro enterprise sector in the country.

Pradhan Mantri Mudra Yojana (PMMY)

Pradhan Mantri Mudra Yojana (MUDRA) has been launched by the Hon'ble Prime Minister on 8th April, 2015 to provide loans to Micro Enterprises /units those are in manufacturing,

trading and Services sector including allied agricultural activities with credit limits of up to Rs.10 Lakhs.

Under the aegis of Pradhan Mantri MUDRA Yojana (PMMY), MUDRA has created three products i.e. 'Shishu', 'Kishore' and 'Tarun' as per the stage of growth and funding needs of the beneficiary micro unit. These schemes cover loan amounts as below:

- Shishu: covering loans up to ₹50,000
- Kishore: covering loans above ₹50,000 and up to ₹5,00,000
- Tarun: covering loans above ₹5,00,000 and up to ₹10,00,000

Venture Capital:

Venture Capital is an important source of finance for those small and medium- sized firms, which have very few avenues for raising funds. Although such a business firm may possess a huge potential for earning large profits in the future and establish itself into a larger enterprise. But the common investors are generally unwilling to invest their funds in them due to risk involved in these types of investments. In order to provide financial support to such entrepreneurial talent and business skills, the concept of venture capital emerged. In a way, venture capital is a commitment of capital, or shareholdings, for the formation and setting-up of small scale enterprises at the early stages of their lifecycle.

The term venture capital comprises of two words, namely, 'venture' and 'capital'. The term venture literally means a course or proceeding, the outcome of which is uncertain but which is uncertain but which is attended by the risk of danger of 'loss'. On the other hand, the term capital refers to the resources to start the enterprise. However, the term venture capital can be understood in two ways.

Venture Capital:

These are funds from third parties used to finance developing business ventures. The third parties could be banks, pension funds, insurance companies, financial institutions not to mention high net worth persons.

Although most known for the financial assistance in businesses, venture capitalists also assist in business networking, product development, sales expertise and advertising strategies. Forms of venture capital can be income notes, equity financing, conditional loan and participating debenture.

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Venture capital is the investment of long-term equity finance where the venture capitalist earns his returns primarily in the form of capital gain.

According to Jame Koloski Morries, " Venture capital is defined as providing seed, startup, and first stage financing and also funding expansion of companies that have already demonstrated their business potential but do not yet have access to the public securities market or to credit-oriented institutional funding sources, Venture Capital also provides management in leveraged buyout financing".
Startup financing refers to the primary introduction of funds, through various sources of finance, to convert the idea into the product or service,

by commencing the business. Angel Investor and Venture Capital are the two major alternatives to startup financing. **Angel Investors** are wealthy individuals who facilitate young entrepreneurs and startups with financial backing in the early stages.

Venture capitalist is a firm, comprising of a team of financial experts or a professional person, who derive their investments from annuity funds, insurance companies, and provident funds.
Venture Capitalist is a part of a large organization or a professional person, who uses funds of third parties to invest in the new or rapidly growing venture, often risky by infusing capital to the firm, called as **venture capital**.

The **third parties** are the investors in venture capital firms such as banks, financial institution, insurance companies, pension funds, corporations and high net worth individuals. It is like funding startup firms or small businesses, who are not able to raise funds from the financial market.

Angel Capital / Investor: An angel investor (also known as a private investor, seed investor or angel funder) is a high-net-worth individual who provides financial backing for small startups or entrepreneurs, typically in exchange for ownership equity in the company. Angel investors are found among an entrepreneur's family and friends. The funds that angel investors provide may be a one-time investment to help the business get off the ground or an ongoing injection to support and carry the company through its difficult early stages.

Difference between Venture capitalist and Angel investor

[redacted]

BASIS FOR COMPARISON	ANGEL INVESTOR	VENTURE CAPITALIST
Meaning	Angel Investors are affluent individuals, who help startup founders in starting their business by infusing their money, in exchange for an ownership stake or convertible debt.	Venture Capitalist refers to an organization or a part of an organization or a professional person who invests in budding companies, by providing them capital, to help them grow and expand.
What is it?	Individual investors, who are often successful businessmen.	Professionally managed public or private firm.
Investment	Investment is made in the pre-revenue business.	Investment is made in the pre-profitability business.
Money	Use their own money to make investment.	Pools money from insurance companies, funds, foundations, and corporations, to make an investment.
Investment size	Less	Comparatively large
Screening	Undertaken by the angel investor according to their own experience.	Undertaken by a team of experts or by an outside firm which specializes in the same.

BASIS FOR COMPARISON	ANGEL INVESTOR	VENTURE CAPITALIST
Post Investment role	Active	Strategic
Stresses on	Investment criteria related to ex-post involvement.	Investment criteria related to initial screening of investment opportunities.
Approach to agency risk control	Incomplete contracts approach	Principal-agent approach

TECHNICAL CONSULTANCY ORGANISATION (TCOs)

It was established in different parts of the country to provide consultancy services to small and medium enterprise at reasonable costs. The TCO was established in Kerala (KITCO) in June 1972.

Technical Consultancy Organizations (TCOs) provide a complete set of consultancy services to small and medium enterprises, individual entrepreneurs, Government Departments and agencies, various state level institutions, commercial banks etc. they provide consultancy services and counsel small scale units in preparation of techno-economic feasibility reports, market survey, modernization and diversification programmers, revival of sick units, etc over 18 TCO's are functioning in various states of India
All India financial institutions and state Govt. have set up network of TCOs.
• TCOs Were established by the all India financial Institutions (IDBI, ICICI, IFCL etc)
• In the collaboration the state level financial/development organization's and Commercial banks.
• There are in all 18 state-level TCOs across India and Nine have been sponsored by IDBI, 5 by IFCI 3 by ICICI bank and one by the Govt. Of Karnataka
• TCOs have transformed being consultancy firm handling project reports, market

surveys, etc to Multi-functional, multi-disciplinary organization's Offering a wide range of services to the industrial and infrastructure sector

Functions and activities of TCOs include:

- Industrial potential surveys.
- Identification of project ideas.
- Project identification and formulation.
- Evaluation of projects
- Project report
- Preparation of profits and feasibility studies.
- Preparation of project reports and implementation
- Conduct area development and marketing surveys.
- Assist entrepreneurs in their modernization ,technical upgradation programme
- Conduct of EDPs programme.
- Diagnostic studies on sick units
- Organise awareness camps.
- Identify potential entrepreneurs and provide them with technical and management assistance.
- Undertaking market research and surveys for specific products.
  Offering merchant banking services.