Managerial Competence

In managerial competence appraisal the focus is on evaluating the level of competence of the people at the helm of affairs. The question is whether the management has the insight and ability to pull off a project. The emphasis is on the determination of the ability of the project to implement and carry on the business in a manner desired.

4. Ecological Analysis: Ecological analysis is a part of project appraisal and nowadays it has assumed specific importance. With the glaring problems like global warming, and climate change the attention is in those industries viz., pharmaceuticals, chemicals, leather processing etc. which do have an adverse impact on the environment. Also those industries that have a known history of creating detrimental effects on the environment are asked to correspond to mandatory norms and devise new techniques of production.

III.VARIOUS SOURCES OF FINANCING

VARIOUS SOURCES OF FINANCING

There are many sources of funding available for entrepreneurs.

1. The Founders:

If a co-founder or partner invests his/her hours in helping you start your business while also working his/her own job, that is also an investment. Or, what about a founder making an office, machines or a technology license available? All of these are sources of investment. Temporarily not paying yourself any wage is also an option.

When to choose this source of financing: Founders can obviously invest in their own company at any time. However, you usually see this happening when the company has just been founded. When a company is set up, in many cases, no revenues or external financing is available, yet there are always some start-up costs to cover.

What is the advantage of this form of investment? It can be perceived as positive by an external financier that a founder has some "skin in the game" as well. Why would another person take the risk of investing in your company if you have never been prepared to take the risk yourself?

2. The 3Fs: family, friends and fools:

Before you start approaching professional investors, it might be worthwhile to try to raise some funding within your network of family, friends and fools. These are often people from your family or social network who are close to you and mainly invest because they have faith in your idea or in you as a person/entrepreneur. As they are usually not professional investors, you should not expect a professional assessment of your company strategy from such an investor.

When to choose this source of financing: This type of financing is often pursued to cover the costs of setting up a new company or to bridge the gap to a first round of (pre-)seed funding. The advantage of this funding type is that it is a quick and cheap way of collecting cash, especially if you take into account the risk that the 3Fs take (which they are not always aware of themselves: hence, "fools").

Usually the amounts concerned with this type of investment are not too high and are typically repaid as a loan (with or even without interest) or are invested in exchange for a small equity share in the company. When the invested amounts, share percentages and level of professionalism increase, then we speak of angel investing.

3. Angels/Informals:

Angel or informal investors are experienced entrepreneurs who have some funds available (often from previously exited ventures) and invest those in new companies to help other entrepreneurs succeed in their business. Angel investments start around 40,000 Lakhs and can amount up to (or more than) 1Cr, as angels sometimes invest together in groups.

When to choose this source of financing: Go for an angel if you are looking for seed funding within the above-mentioned range. Angels typically offer "smart capital": not just money, but also networking opportunities and knowledge within specific sectors. Try to find an angel that fits with your company in terms of experience and sector knowledge. Angels spot new investment opportunities through their network, but (for instance) also through platforms such as **Angel List, Crunch base and F6s**

4. Crowd Funding:

Nowadays, it is hard to imagine that crowd funding once didn't exist. With crowd funding, the "crowd" finances the funding need of a company. Usually, crowd funding is performed via an online platform where entrepreneurs offer investment opportunities on one side of the platform and on the other side of the platform, a large group of people invest small amounts to meet the entrepreneur's investment need.

When to choose this source of financing: In general, there are **three** types of crowd funding

i) Loans,
ii) Pre-orders/donations and
iii) Convertible loans.

⇒ Are you looking for a loan, but having trouble securing one from the bank because your risk profile is too high? Then try loan crowd funding.

⇒ Do you have a prototype available, and do you want to test the product/market fit, but you cannot finance the production/delivery of the first batch of actual products? Then go for pre-orders/donations. Well-known examples of platforms offering these types of crowd funding are **Kickstarter and Indiegogo**. They are mainly suitable for products, projects or gadgets aimed at the consumer market and have a strong design element to them.

⇒ Convertible loans have the following advantages:

1) No shares are being issued,

2) Valuation discussions are postponed until the moment the value of a company can be better determined and

3) It is an easier, faster and cheaper process than an actual share transfer.

Since the people that invest via crowd funding platforms are not always professional investors, crowd funding is better suited for propositions that are not too complex or technical and that are easily understood by the general public (that's why it's called "crowd" funding). Think, for example, of consumer products.

There are also crowd funding platforms with a specific focus, so take that into account when making your choice. As an example, Dutch crowd funding platform **One planet crowd** focuses specifically on sustainable projects with a positive impact.

5. Subsidies:

A huge number of tax/financial schemes and subsidies exist. The aim of subsidies/schemes is typically to stimulate entrepreneurship, innovation/R&D or economic growth within a certain geographical area. That is why every region, every country and even, for instance, the entire European Union has its own subsidies.

When to choose this source of financing: ALWAYS, and we can be very brief about this. Subsidies are relevant during almost every company stage, from start-up to corporate, from freelancer to publicly traded company.

As mentioned before, many subsidies only focus on a certain geographical area and, often, there is also a specific sector focus. Therefore, it is important to look for a subsidy that fits with your company.

Keep in mind that administrative and reporting requirements often apply to subsidy applications and grants. You need to be able to justify the costs for which you request a subsidy and, sometimes, it is mandatory to have this justification audited as well.

6. Venture Capital/Private Equity:

Private equity is the collective name for professional investment firms that invest in companies that are not publicly listed. Venture capital (VC) is a type of private equity that focuses specifically on (from the investor's perspective) risky investments in early stage companies.

People often speak of private equity when investing in larger organizations that have existed for some time already. Venture capital, on the other hand, involves investing in growth capital of young companies. In general, VC firms have a fund available of a specific size (e.g., 10Cr etc) that has to be invested within a certain period of time (e.g., 10 years) in a number of companies with different risk profiles to spread the risk across the portfolio. The aim is to sell the shares after a couple of years for a certain return/profit.

When to choose this source of financing: Venture capital is mainly suitable for companies that have already passed the "seed stage" and are looking for series A or series B funding. This type of funding is therefore meant to help companies grow faster than they would if growing organically, for instance if a firm wants to internationalize.

VC firms typically invest in the range of about 10Cr to 25Cr etc. To raise funding from a VC, a company's product/market fit has to be already proven, and steadily growing revenue streams have to exist for several years. However, there are also venture capitalists with Seed funds that offer Seed capital to companies that have not met the abovementioned criteria yet.

The advantage of VC firms is that they can fund multiple rounds for the same company, where an angel or other seed investor is not always capable of doing so. Venture capitalists often also have a specific sector focus and good knowledge/network within this sector.

7. Debt financing: (The bank)

Even though there are banks around that have started venture capital funds, they are generally more risk averse than, for example, angels, seed investors and normal VC investors. This does not mean that banks do not finance entrepreneurs – on the contrary!

However, they are more likely to invest in small to medium businesses, in companies with lower risk profiles (than start-ups, for instance) and when companies can offer collateral. For an early-stage start-up that does not fit in the focus of the VC funds, it can thus be difficult to secure funding from a bank.

When to choose this source of financing: As mentioned, banks generally take less risk than, for example, VC investors and angels. However, if you can provide collateral, then a bank is a very good option. Or if you are looking for working capital financing, stock financing or financing to cover investments in buildings/machines, then a bank is a very good option to consider as well.

Companies generating stable income streams and that have been growing organically for a number of years (and are thus less risky) can certainly also turn to a bank. A big advantage of debt financing is that you do not have to give away a part of your company in terms of equity, which means that in the long term, it can turn out to be a much cheaper way of financing than, for example, securing funding from an angel investor or VC investor.

8. Factoring:

In short, *factoring is a way of financing working capital by lowering the size of accounts receivable*. Example: if you send an invoice to a customer, but it takes the client 60 days to pay, then you can decide to "sell" this invoice to a factoring company (against a certain payment, of course).

The factoring company will pay for the invoice (or provides you with a loan) so that you do not have to wait 60 days before the invoice is paid by the client. A factoring company can also take over the risk that the client does not pay at all.

When to choose this source of financing: First of all, it goes without saying that you must have clients in order to be eligible for factoring. If you do not have any paying customers, factoring is not an option. If you do have customers, factoring can be very useful if you have to deal with long payment terms.

Do you have large corporates as your customers? If so, it can take a while for invoices to be paid, and there is often not much you can do about it. In order to keep your working capital position healthy, factoring can be a good solution. Is accounts receivable management costing you a lot of time and effort? Do you often suffer from bad debtors? Then factoring could also be an outcome.

9. Leasing:

Do you have to make large investments in assets such as computers and/or machines? Why don't you lease instead of purchasing them? By leasing assets companies can spread payments over a longer period of time instead of having to fulfil the full payment of an investment the moment they decide to purchase an asset.

When to choose this source of financing: When a company is capital-intensive, meaning it is dependent on the use of (sometimes expensive) assets, such as machinery, leasing may be the way to go.

10. Suppliers:

Is our business heavily reliant on its supply chain? Then try to negotiate favourable payment terms with suppliers. If your customers have long payment terms, for instance, you can try to agree to longer payment terms with your suppliers as well so that you do not run into any problems concerning your working capital. On the other hand, you could also try to discuss discounts in the event you pay your suppliers very quickly.

When to choose this source of financing: Choose this form of financing if you have good relationships with your suppliers or if you have a good negotiating position with them (for example, if you are a large/important customer).

11. Initial Coin Offering:

For an Initial Coin Offering (ICO), a company typically writes a whitepaper to pitch a certain business idea and asks the general public to finance the idea using Bit coin and/or Altcoins (other Crypto currencies than Bit coin). In return, the investor receives an Altcoin newly generated by the company during the ICO.

Usually, this newly generated Altcoin is at the centre of the company's business activities and thus leveraged in a way that increases its value. As soon as this altcoin becomes tradable, investors can resell it (and hopefully make a profit). An ICO is therefore very similar to an IPO, but uses crypto currency instead of shares that can be converted into "normal cash"

When to choose this source of financing: It is possible to do an ICO as a non-crypto company, but currently, the majority of the companies that do an ICO are block chain/crypto currency companies. This is due to the fact that the new altcoin generated by an ICO often has a function within the company which increases its value. The speculation on the fact that the value of the new altcoin will indeed increase is what attracts investors.

12. Initial Public Offering (IPO):

The initial public offering (IPO)! An IPO is the public listing of a company, which means that it is the first time a company offers its shares to the general public (instead of to private individuals, investors or companies). This means that practically anyone in the world (individuals or institutional investors) can invest in the company by buying shares at a certain value.

Before an IPO, a company is private, which means that it often only has a limited number of investors that have invested early stage or growth capital. Think of the founders, angels and VC firms for instance.

When to choose this source of financing: For an initial public offering to be successful, a company must be able to demonstrate years of strong growth, and its proposition typically includes a certain network effect/scalability. Growth can be defined in several ways. This can be turnover or profit but also, for example, the number of customers or active users. For example, Spotify has been a loss-making company for years, but has been growing enormously in terms of turnover and users.

A company also has to demonstrate transparency and confidence that growth will continue in future years because it has to win the trust of the general public that the value of the shares (which are bought by the public during the IPO) will raise in the future so that they can make a profit on their investment.

For the investors that owned a share in the company already before the IPO, a public listing can turn out to be very attractive (financially). An IPO should not be underestimated though: it is a very costly process and results in many reporting requirements toward the public, imposed by strict government regulations.

13. Revenue based financing:

Revenue based financing is a funding mechanism in which an investor provides financing to a start-up and in return the investor will receive a percentage (e.g. between 2% - 5%) of the (future) revenues generated by the start-up. The future revenue-based interest payments are typically capped at two to three times the size of the initial funding amount.

When to choose this source of financing: This type of funding is typically offered at (pre-) seed stage. The benefits of this type of funding for start-ups are the following:

The founders do not have to give away any equity meaning they will not dilute their equity shares.

As opposed to a normal bank loan the interest payments for revenue based financing are linked to the generated revenues, which mean that if revenues decline required payments also decline. This reduces the chance of cash flow issues and potential illiquidity.

SOURCES OF FINANCE: (Broad Classification)

Sources of finance for business are equity, debt, debentures, retained earnings, term loans, working capital loans, letter of credit, euro issue, venture funding, etc. These sources of funds are used in different situations. They are classified based on time period, ownership and control, and their source of generation. It is ideal to evaluate each source of capital before opting for it.

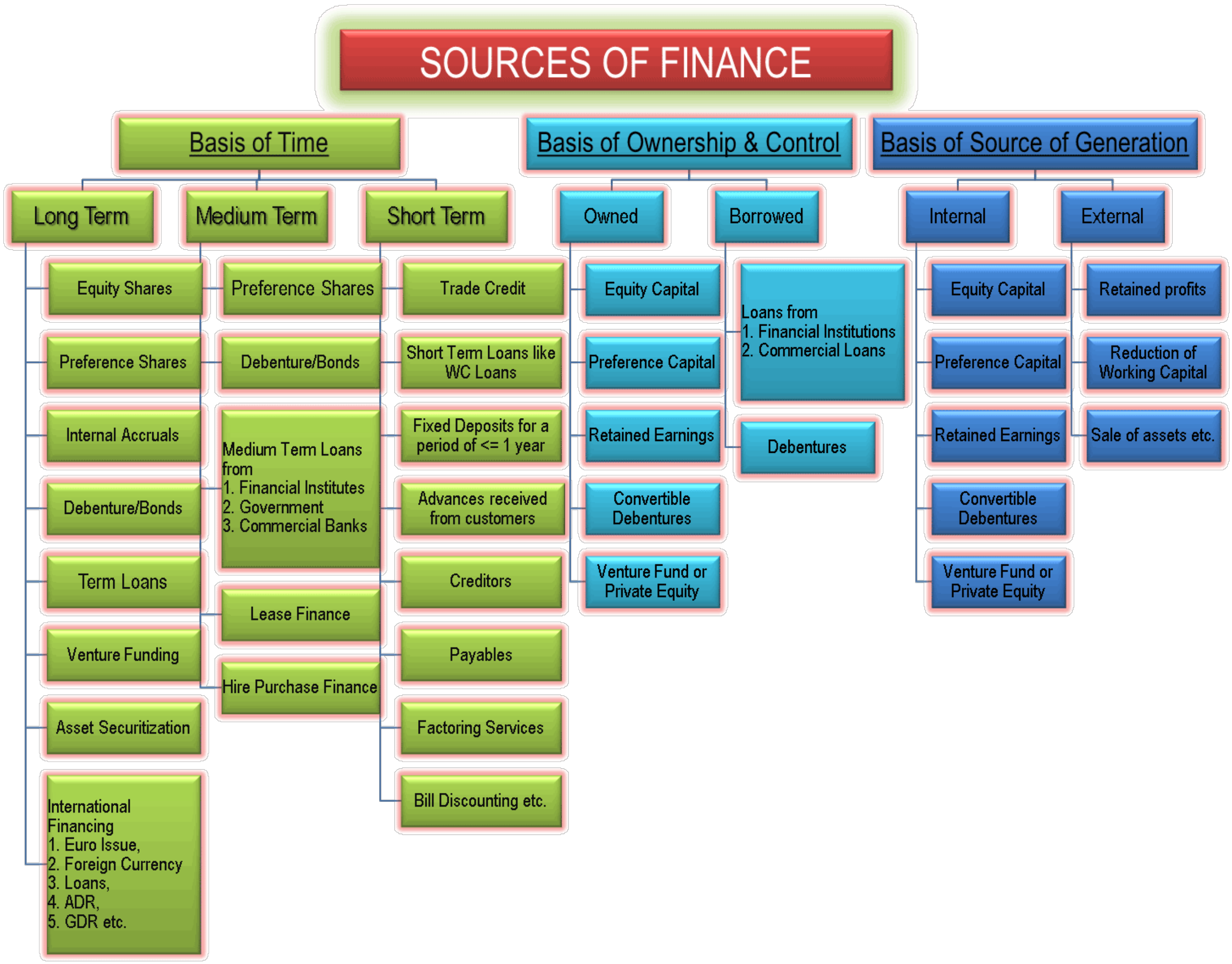
Sources of capital are the most explorable area, especially for the entrepreneurs who are about to start a new business. It is perhaps the most challenging part of all the efforts. There are various capital sources we can classify on the basis of different parameters.

Knowing that there are many alternatives to finance or capital a company can choose from. Choosing the right source and the right mix of finance is a crucial challenge for every finance manager. Selecting the right source of finance involves an in-depth analysis of each source of fund. For analyzing and comparing the sources, it needs an understanding of all the characteristics of the financing sources. There are many characteristics on the basis of which sources of finance are classified.

⇒ On the basis of a time period, sources are classified as long-term, medium-term, and short-term.

⇒ Ownership and control classify sources of finance into owned and borrowed capital.

⇒ Internal sources and external sources are the two sources of generation of capital. All the sources have different characteristics to suit different types of requirements. Let's understand them in a bit of depth.



According to Time Period

Sources of financing a business are classified based on the time period for which the money is required. The time period is commonly classified into the following three:

(i) Long-Term Sources of Finance

Long-term financing means capital requirements for a period of more than 5 years to 10, 15, 20 years or maybe more depending on other factors. Capital expenditures in fixed assets like plant and machinery, land and building, etc of business are funded using long-term sources of finance. Part of working capital which permanently stays with the business is also financed with long-term sources of funds. Long-term financing sources can be in the form of any of them:

- Share Capital or Equity Shares
- Preference Capital or Preference Shares
- Retained Earnings or Internal Accruals
- Debenture / Bonds
- Term Loans from Financial Institutes, Government, and Commercial Banks
- Venture Funding
- Asset Securitization

(ii) Medium Term Sources of Finance

Medium term financing means financing for a period of 3 to 5 years and is used generally for two reasons. One, when long-term capital is not available for the time being and second when deferred revenue expenditures like advertisements are made which are to be written off over a period of 3 to 5 years. Medium term financing sources can in the form of one of them:

- Preference Capital or Preference Shares
- Debenture / Bonds
- Medium Term Loans from
- Financial Institute
- Government, and
- Commercial Banks
- Medium Term Note
- Lease Finance
- Hire Purchase Finance

(iii) Short Term Sources of Finance

Short term financing means financing for a period of less than 1 year. The need for short-term finance arises to finance the current assets of a business like an inventory of raw material and finished goods, debtors, minimum cash and bank balance etc. Short-term financing is also named as working capital financing. Short term finances are available in the form of:

- Trade Credit
- Short Term Loans like Working Capital Loans from Commercial Banks
- Fixed Deposits for a period of 1 year or less
- Advances received from customers
- Creditors
- Payables
- Factoring Services
- Bill Discounting etc.

According to Ownership and Control:

Sources of finances are classified based on ownership and control over the business. These two parameters are an important consideration while selecting a source of funds for the business. Whenever we bring in capital, there are two types of costs – one is the interest and another is sharing ownership and control. Some entrepreneurs may not like to dilute their ownership rights in the business and others may believe in sharing the risk.

(i) Owned Capital

Owned capital also refers to equity. It is sourced from promoters of the company or from the general public by issuing new equity shares. Promoters start the business by bringing in the required money for a start-up. Following are the sources of Owned Capital:

- Equity
- Preference
- Retained Earnings
- Convertible Debentures
- Venture Fund or Private Equity

Further, when the business grows and internal accruals like profits of the company are not enough to satisfy financing requirements, the promoters have a choice of selecting ownership capital or non-ownership capital. This decision is up to the promoters. Still, to discuss, certain advantages of equity capital are as follows:

- It is a long-term capital which means it stays permanently with the business.
- There is no burden of paying interest or instalments like borrowed capital. So, the risk of bankruptcy also reduces. Businesses in infancy stages prefer equity for this reason.

(ii) Borrowed Capital

Borrowed or debt capital is the finance arranged from outside sources. These sources of debt financing include the following:

- Financial institutions,
- Commercial banks or
- The general public in case of debentures

In this type of capital, the borrower has a charge on the assets of the business which means the company will pay the borrower by selling the assets in case of liquidation. Another feature of the borrowed fund is a regular payment of fixed interest and repayment of capital. Certain advantages of borrowing are as follows:

- There is no dilution in ownership and control of the business.
- The cost of borrowed funds is low since it is a deductible expense for taxation purpose which ends up saving on taxes for the company.
- It gives the business the benefit of leverage.

According to Source of Generation:

Based on the source of generation, the following are the **internal and external sources of finance:**

(i) Internal Sources

The internal source of capital is the one which is generated internally by the business. These are as follows:

- Retained profits
- Reduction or controlling of working capital

- Sale of assets etc.

The internal source of funds has the same characteristics of owned capital. The best part of the internal sourcing of capital is that the business grows by itself and does not depend on outside parties. Disadvantages of both equity and debt are not present in this form of financing. Neither ownership dilutes nor fixed obligation/ bankruptcy risk arises.

(ii) External Sources

An external source of finance is the capital generated from outside the business. Apart from the internal sources of funds, all the sources are external sources.

Deciding the right source of funds is a crucial business decision taken by top-level finance managers. The usage of the wrong source increases the cost of funds which in turn would have a direct impact on the feasibility of the project under concern. Improper match of the type of capital with business requirements may go against the smooth functioning of the business. For instance, if fixed assets, which derive benefits after 2 years, are financed through short-term finances will create cash flow mismatch after one year and the manager will again have to look for finances and pay the fee for raising capital again.

LONG TERM FINANCES

Long-term financing means capital requirements for a period of more than 5 years to 10, 15, 20 years or maybe more depending on other factors. Capital expenditures in fixed assets like plant and machinery, land and building, etc of business are funded using long-term sources of finance. Part of working capital which permanently stays with the business is also financed with long-term sources of funds.

(i) Equity Share and its Types:

Equity share is a primary source of finance for any company giving investors rights to vote, share profits, and claim on assets. Various types of equity share capital are authorized, issued, subscribed, paid-up, rights, bonus, sweat equity, etc. The expression of the value of equity shares is in terms of the face value or par value, issue price, book value, market value, intrinsic value, stock market value, etc.

Usually, a company is started with equity finance as its first source of capital from the owners or promoters of that company (founder's stock). After a certain level of growth, there is a requirement for more capital for further growth. The company then finds an investor in the form of friends, relatives, venture capitalists, mutual funds, or any such small group of investors and issues new equity shares to these investors.

A point comes where the company reaches a very high level and requires enormous capital investment for business growth. An **Initial Public Offer (IPO**) is the offer of shares that the company makes to the general public for the first time. And **Follow on Public Offer (FPO)** is more such offers in the future to the public.

<u>Equity Shares:</u>

Types of Equity Shares:

There are various classes of shares (equity) dependent on multiple things. In the company's financial statements, we place the equity shares on the liability side of the balance sheet. Their classification into various categories is as follows:

a) Authorized Share Capital:

It is the maximum amount of capital that a company can issue. The companies can increase it from time to time. For that, we need to comply with some formalities and pay some fees to the legal bodies.

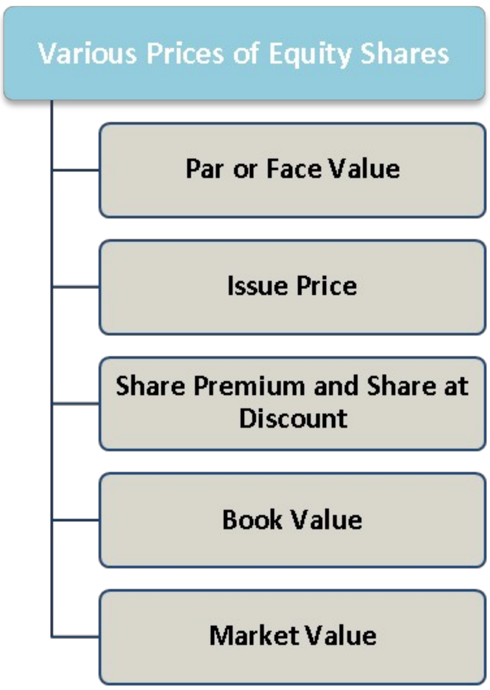
b) Issued Share Capital:

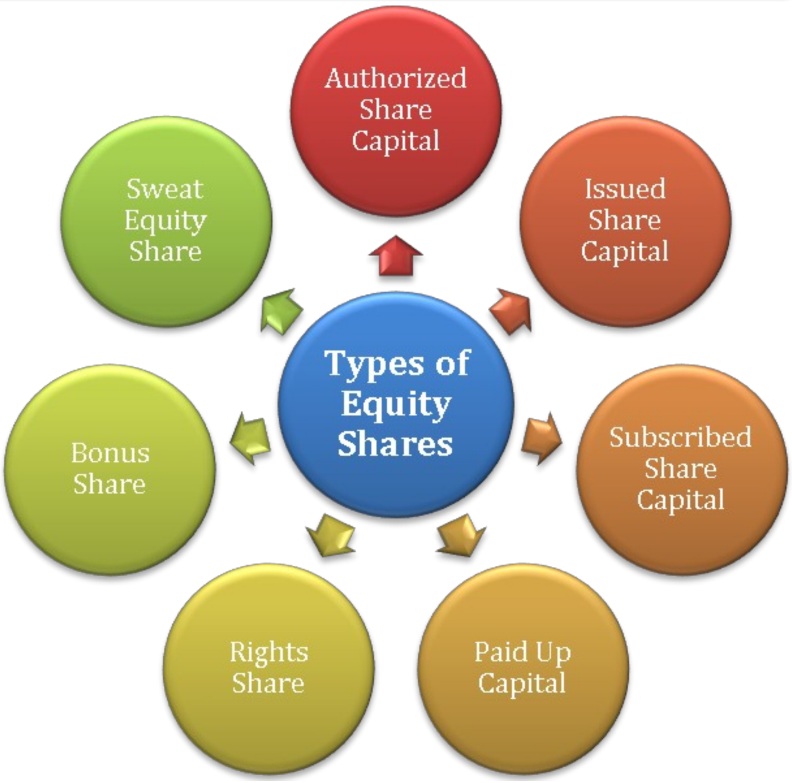
It is part of the authorized capital that the company offers to investors.

c) Subscribed Share Capital:

An investor accepts and agrees upon that part of the issued capital.

d) Paid Up Capital:





It is the part of the subscribed capital that the investors pay. Normally, all companies accept complete money in one shot, and therefore issued, subscribed, and paid capital becomes the same. Conceptually, paid-up capital is the amount of money a company invests in the business.

Other type of Shares:

a) Rights Shares:

Right shares are those that a company issues to its existing shareholders. The company issues such kinds of shares to protect the ownership rights of the existing investors.

b) Bonus Shares:

When the company issues share to its shareholders in the form of a dividend, we shall call them bonus shares. There are various advantages and disadvantages of bonus shares like dividend, capital gain, limited liability, high risk, fluctuation in the market, etc.

c) Sweat Equity Share:

Sweat equity shares are issued to exceptional employees or directors of the company for their exceptional job in terms of providing know-how or intellectual property rights to the company.

d) Treasury Stock:

Treasury stock means the share that the company has bought back.

(ii) Preference Capital or Preference Shares:

Preference shares are a long-term source of finance for a company. They are neither entirely similar to equity nor equivalent to debt. The law treats them as shares, but they have elements of both equity shares and debt. For this reason, they are also called 'hybrid financing instruments.' These are also known as preferred stock, preferred shares, or only preferred in a different part of the world. There are various types of preference shares used as a source of finance.

Features of Preference Shares Similar to Debt:

(a) Fixed Dividends:

Like debt carries a fixed interest rate, these shares have fixed dividends. But the obligation of paying a dividend is not as rigid as debt. Non-payment of a dividend would not amount to bankruptcy in the case of preference share.

(b) Preference over Equity:

These types of shares get preference over equity shares in sharing the income and claims on assets. Alternatively, this share dividend has to be paid before any dividend payment to ordinary equity shares. Similarly, at the time of liquidation, these shares would also be paid before equity shares.

(c) No Voting Rights:

Preference share capital is not allotted any voting rights usually. They are similar to debenture holders and do not have any say in the management of the company.

(d) No Share in Earnings:

Preference shareholders can only claim two things—one agreed-on percentage of dividend and second the amount of capital invested. Equity shares are entitled to share the residual earnings and residual assets in case of liquidation, which preference shares are not entitled to.

(e) Fixed Maturity:

Just like debt, these shares also have a fixed maturity date. The preference capital will have to be repaid to the preference shareholders on the date of maturity. A special type of shares, i.e., irredeemable preference shares, is an exception to this. They do not have any fixed maturity.

(iii) Term Loans/Debenture/Bonds:

Term Loans:

A term loan is comparatively the most uncomplicated type of business loan. You borrow a specific amount from the lender and, in return, agree to pay back the loan amount plus interest over a set period. Payments are usually made every month.

Lenders, usually banks or specialized institutions, assess the borrower's financial condition before lending the money. Significant benefits of a term loan are flexibility in repayment, quick disbursal of funds, and minimal documentation.

Types of Term Loans:

(a) Short Term Loans:

A short-term loan is usually for 1 to 2 years. A short-term loan is often required to meet the day-to-day business needs or the business's working capital requirements. There are several sources of short-term loans, including a loan from a Commercial bank, Trade Credit, Discounting Bills of Exchange, Factoring, and more.

Short-term loans carry a higher interest rate when compared to a long-term loan. Also, it may involve even weekly repayment if the term of the loan is very short. It is a general rule – the shorter the term and the easier a loan is to get, the higher the interest rate. One must be very careful when going for this type of term loan as it not only involves a higher interest rate, but charges may also be on the higher side if you default on repayments.

(b) Medium-Term Loans:

A medium-term loan is usually for a period of 2 to 5 years and can be said to be a hybrid of short and long-term loans. Such a loan is often taken for carrying out repair or renovation of the fixed asset.

A medium-term loan is usually skipped when talking about the types of terms loans as people may go straight to the long-term loan after discussing the short-term loan. However, it is better to keep the duration of 2 to 5 years under medium-term as terms and condition for such a period is somewhat different from the long-term loan. Like, the interest rate is comparatively higher, while the documentation part is easier when compared to the long-term loans.

(c) Long Term Loans:

These types of term loans are for more than five years. Most of the long-term loans are secured, for instance, home loans, car loans, and loans against property. Since the loan is secured, the rate of interest is also lower. However, it can be unsecured as well. In an unsecured loan, no collateral or asset is needed, but the rate of interest is comparatively higher as the lender bears more risk.

EMI for such a loan is also quite low as the payment is spread over a long period. A long-term loan is credit-based, so the better your credit score is, the better the chances that you get a lower interest rate. The amount of the loan will also depend on your credit history and income.

Debentures:

Long-term debt financing is majorly categorized into term loans and debentures. Debentures are one of the familiar long-term sources of finance. They usually carry a fixed interest rate and a certain date of maturity. One has to pay interest every year and the principal on the maturity date. A term loan carries a fixed interest rate, and the payment is made in instalments, which consists of both principal and interest.

A financial institution or a bank lends the term loan, so the financier is the bank or financial institution. Whereas the debentures are issued to the general public, the financier is the general public. This is the fundamental difference between these two types of long-term sources of debt finance.

Advantages of Debt Financing- Debentures and Term Loan:

(a) Benefit of Tax:

Debt Financing' or 'Issuing of Debenture' results in interest expense for the borrower, which is a tax-deductible expense. A company can claim an interest as an expense against its profits. In contrast, dividends paid to equity or preference shareholders are paid out of net profits after taxes. In short, debt financing, such as debentures, term loans, etc., avails tax benefits to the borrower, which is not there in the case of equity.

(b) No Dilution of Control:

Issuing debentures or accepting bank loans does not dilute the control of the existing shareholders or the company's owners over their business. If there is a rise in the same fund using equity finance, there are chances of losing control of existing shareholders.

(c) No Dilution in Share of Profits:

Opting for debentures over equity as a source of finance keeps the profit-sharing percentage of existing shareholders intact. Debenture holders or financial institutions do not share profits with the company. They are liable to receive the agreed amount of interest only. Therefore, the same number of hands shares the profits before and after the new project.

However, in the case of convertible debentures (debentures that convert into equity shares after a certain time), this may no more remain an advantage as the debenture holders would then become equity shareholders receiving all the rights as of the equity shareholders.

(d) Low Issue Cost:

In the case of a term loan, there is a comparatively lower cost of the issuance. Whereas in the case of equity financing, there is a huge cost of issuance.

(e) Fixed Instalments:

Debt financing by term loan or debentures has fixed instalments/coupon payments until the loan's maturity. In a rising economy with increasing inflation, the effective cost of future instalments decreases due to a decline in the currency's value.

(f) No Harm in Communicating Critical Business Secrets:

In the case of a term loan, the company may have to reveal a lot of information about the company to the financial institutions. By entering into NDA (non-disclosure agreement), the company can ensure its secrets remain hidden from its competitors.

Bonds:

A bond is a financial instrument whereby its issuer raises (borrows) capital or funds at a certain cost for a certain time period and pays back the principal amount on maturity of the bond. Interest paid on bonds is usually referred to as coupons. In simple words, a bond is a loan taken at a certain rate of interest for a definite time period and repaid on maturity.

From a company's point of view, the bond or debenture falls under the liabilities section of the balance sheet under the heading of debt. And are distinguished on the basis of security (secured and unsecured bonds). A bond is similar to a loan in many aspects; however, it differs mainly with respect to its tradability. A bond is usually tradable and can change many hands before it matures, while a loan usually is not traded or transferred freely.

Different Types of Bonds:

(a) Plain Vanilla Bonds:

A plain vanilla bond is a bond without unusual features; it is one of the simplest forms of bond with a fixed coupon and a defined maturity and is usually issued and redeemed at face value. It is also known as a straight bond or a bullet bond.

(b) Zero-Coupon Bonds:

A zero-coupon bond is a type of bond with no coupon payments. It is not that there is no yield; the zero-coupon bonds are issued at a price lower than the face value (say 950$) and then pay the face value on maturity ($1000). The difference will be the yield for the investor. These are also called discount bonds or deep discount bonds if they are for a longer tenor.

(c) Deferred Coupon Bonds:

The deferred coupon bond is a blend of a coupon-bearing bond and a zero-coupon bond. These bonds do not pay any coupon in the initial years and, after that, pay a higher coupon to compensate for no coupon in the initial years. Such bonds are issued by corporates whose business model has a gestation period before the actual revenues start. Examples of companies that may issue such bonds include construction companies.

(d) Step-Up Bonds

The step-up bonds are where the coupon usually steps up after a certain period. They may also be designed to step up not once but in a series. Such bonds are usually issued by companies where revenues/ profits are expected to grow in a phased manner. These are also called dual coupon or multiple coupon bonds.

(e) Step Down Bonds:

The step-down bonds are just the opposite of Step-Up Bonds. These are bonds where the coupon usually steps down after a certain period. They may also be designed to step down not once but in a series. Such bonds are usually issued by companies where revenues/ profits are expected to decline in a phased manner; this may be due to wear and tear of the assets or machinery, as in the case of leasing.

(f) Floating Rate Bonds:

Floating rate bonds are so-called because they have a coupon that is not fixed but instead linked to a benchmark. For example, a company may issue a floating-rate bond as Treasury bond rate + 50 bps (100 bps = 1%). In such cases, on every interest payment date, the payment will be made 0.50% more than the Treasury bill rate prevailing on the fixing date.

(g) Inverse Floaters:

Inverse floaters are types of bonds that are similar to the floating rate bond in that the coupon is not fixed and is linked to a benchmark; however, the differentiating thing is that the rate is inversely related to the benchmark. In simple words, if the benchmark rate goes up, the coupon rate comes down and vice versa.

(h) Participatory Bonds:

A participatory bond is a bond whereby the issuer promises a fixed rate. Still, the coupon cash flow may increase if the profit/ income levels of the company rise to a pre-specified level and may reduce when income falls below a pre-specified level; thereby, the investor participates in the return enjoyed based on company revenues/ income.

(i) Income Bonds:

Income bonds are similar to participatory bonds; however, these types of bonds do not have a reduction in interest payments if income/ revenue reduces.

(j) Payment in Kind Bonds:

Payment in kind bonds are types of bonds that pay interest/coupon, not in terms of cash payouts but the form of additional bonds.

(k) Extendable Bonds:

Extendable bonds allow the holder to enjoy the right to extend the maturity if required. The holder has an additional benefit in this case because if the rate of interest in the market reduces, the holder may choose to extend the tenor and enjoy the higher rate of interest in terms of coupon payment. For this benefit, the holder may enjoy coupon rates that are usually lower than a plain vanilla bond.

(l) Exchangeable Bonds:

Exchangeable bonds are similar to convertible bonds but differ in one aspect; they can be exchanged for equity shares but not the issuer. These can be exchanged for equity shares of another company in which the issuer may have stake-holding.

(m) Callable Bonds:

Bonds that are issued with a specific feature where the issuer has the right to call back the bonds at a pre-agreed price and a pre-fixed date are called callable bonds. Since these bonds allow a suer to repay the liability before maturity, these bonds usually offer a coupon rate higher than a normal straight coupon-bearing bond.

(n) Puttable Bonds:

Bonds that are issued with a specific feature where the bondholder has the right to return the bonds at a pre-fixed date before maturity are called puttable bonds. Since these bonds allow a benefit to the bondholders to ask for the principal repayment before maturity, these bonds usually offer a coupon rate lower than a normal straight coupon-bearing bond.

Apart from above types, various other types of bonds are:

- Industrial revenue bonds
- Development impact bonds
- Indexed bonds
- Brady bonds
- Investment-grade bonds
- Junk bonds
- Green bonds
- Blue bonds
- Sushi bonds
- Variable rate demand bonds
- Social impact bonds

(iv) Venture Funding:

Venture funding is a funding process in which the venture funding companies manage the funds of the investors who want to invest in new businesses which have the potential for high growth in the future. The venture capital funding firms provide the funds to start-ups in exchange for the equity stake. Such a start-up generally possesses the ability to generate high returns. However, the risk for venture capitalists is high.

Venture Funding Stages

Venture Funding Stages
Stage 1: Seed Capital
Stage 2: Startup Capital
Stage 3: Early Stage/ Second Stage Capital
Stage 4: Expansion Stage
Stage 5: Bridge / Pre IPO Stage

Stage 1: Seed Capital:

In this first stage of venture funding, the venture or the start-up company in need of the funds contacts the venture capital firm or the investor. The venture firm shall share its business idea with the investors and convince them to invest in the project. The investor or venture capital firm shall then conduct research on the business idea and analyze its future potential. If the expected returns in the future are good, the investor (Venture capitalist) shall invest in the business.

-up Capital:

Start-up capital is the second stage of venture funding. If the venture is able to attract an investor, the idea of the business of the venture is brought into reality. A prototype product is developed and fully tested to know the actual potential of the product. Generally, a person from the venture capital firm takes a seat in the management of the business to monitor the operations regularly and keep a check that every activity is done as per the framed plan. Suppose the idea of the business meets the requirement of the investor and has sufficient market in the trial run. In that case, the investor agrees to participate in the future course of the business.

Stage 3: Early Stage / Second Stage Capital:

After the start-up capital stage comes the early/first/second stage capital. In this stage, the investor significantly increases the capital invested in the venture business. The capital increase is mainly towards increasing the production of goods, marketing, or other expansion, say building a network, etc. A company with a higher capital inflow moves towards profitability as it is able to reach a wide range of customers.

Stage 4: Expansion Stage

This is the fourth stage of venture funding. In this stage, the company expands its business by way of diversification and differentiation of its products. This is possible only if the company is earning good profits and revenue. To reach up to this stage, the company needs to be operational for at least 2 to 3 years. The expansion gives the venture new wings to enter into untapped markets.

Stage 5: Bridge / Pre IPO Stage

This is the last stage of venture funding. When the company has developed a substantial share in the market with its products, the company may opt for going public. One main reason for going public is that the investors can exit the company after earning profits for the risks they have taken all the years. The company mainly uses the amount received by way of IPO for various purposes like mergers, elimination of competitors, research and development, etc.

(v) Asset Securitization:

An asset-backed security (ABS) is a type of financial investment that is collateralized by an underlying pool of assets—usually ones that generate a cash flow from debt, such as loans, leases, credit card balances, or receivables. It takes the form of a bond or note, paying income at a fixed rate for a set amount of time, until maturity. For income-oriented investors, asset-backed securities can be an alternative to other debt instruments, like corporate bonds or bond funds.

Assume that Company X is in the business of making automobile loans. If a person wants to borrow money to buy a car, Company X gives that person the cash, and the person is obligated to repay the loan with a certain amount of interest. Perhaps Company X makes so many loans that it starts to run out of cash. Company X can then package its current loans and sell them to Investment Firm X, thus receiving the cash, which it can then use to make more loans.

(vi) Retained Earnings:

Retained earnings are the amount of profit a company has left over after paying all its direct costs, indirect costs, income taxes and its dividends to shareholders. This represents the portion of the company's equity that can be used, for instance, to invest in new equipment, R&D, and marketing. When accumulated year after year, retained earnings are known as "accumulated profits."

se:

Hire Purchase is defined as an agreement in which the owner of the assets lets them on hire for regular instalments paid by the hirer. The hirer has the option to purchase and own the asset once all the agreed payments have been made. These periodic payments also include an interest component paid towards the use of the asset apart from the asset's price.

In other words, it can be defined as an option of financing or acquiring an asset for use whereby the financing company lets the goods on hire to the buyer against small instalments called hire charges. The buyer gets the right to use the asset with an option to purchase the asset by paying all such instalments spread over a period of time. Hire purchase was very prominent for vehicle financing, whether a personal car, commercial vehicle, etc., but now equipment, machinery, etc., are also financed with hire purchase method.

Features and Characteristics of Hire Purchase:

- Rental payments are paid in instalments over the period of the agreement.
- Each rental payment is considered as a charge for hiring the asset. This means that if the hirer defaults on any payment, the seller has all the rights to take back the assets.
- All the required terms and conditions between both the parties involved are documented in a contract called a Hire-Purchase agreement.
- The frequency of the instalments may be annual, half-yearly, quarterly, monthly, etc., according to the terms of the agreement.
- Assets are instantly delivered to the hirer as soon as the agreement is signed.
- If the hirer uses the option to purchase, the assets are passed to him after the last instalment is paid.
- If the hirer does not want to own the asset, he can return the assets at any time and is not required to pay any instalment that falls due after the return.
- However, once the hirer returns the assets, he cannot claim back any payments already paid as they are the charges towards the hire and use of the assets.
- The hirer cannot pledge, sell or mortgage the assets as he is not the owner of the assets till the last payment is made.

  The hirer usually pays a certain amount as an initial deposit/down payment while signing the agreement.
- Generally, the hirer can terminate the hire purchase agreement any time before the ownership rights pass to him

Process of Hire Purchase:

Advantages of Hire Purchase:

The following are the advantages:

- Immediate use of assets without paying the entire amount.
- Expensive assets can be utilized as the payment is spread over a period of time.
- Fixed rental payments make budgeting easier as all the expenditures are known in advance.
- Easy accessibility as it is secured financing.
- There is no need to worry about the asset depreciating quickly in value as there is no obligation to buy the asset.

Disadvantages of Hire Purchase:

It suffers from the following disadvantages:

- The total amount paid towards the asset could be much higher than the asset's cost due to substantially high-interest rates.
- The long duration of the rental payments.
- Ownership only at the end of the agreement. The hirer cannot modify the asset till then.
- The addition of any covenants increases the cost.
- If the hired asset is no longer needed because of any change in the business strategy, there may be a resulting penalty.

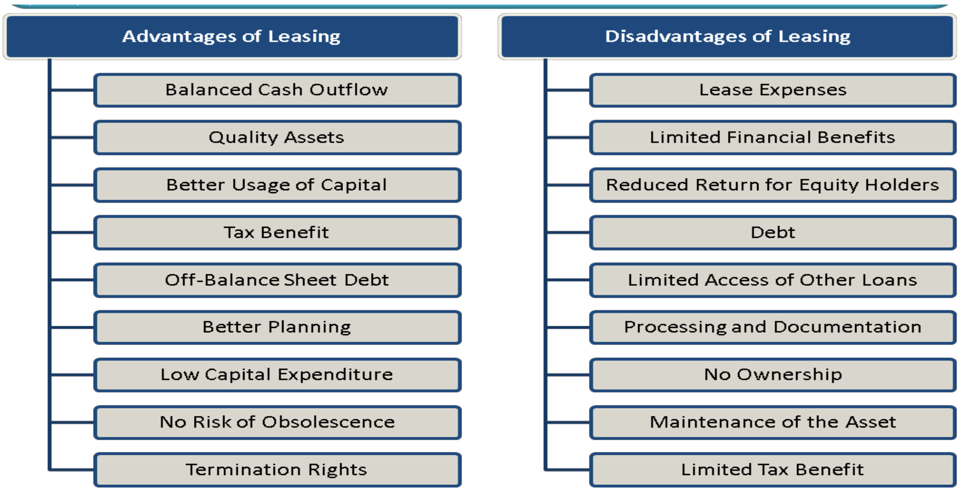
Leasing:

What is a Lease or Leasing?

A famous quote by Donald B. Grant says, "Why own a cow when the milk is so cheap? All you really need is milk and not the cow." This quote influences the concept of Lease. We can compare 'milk' with the 'rights to use an asset' and 'cow' with the 'asset' itself. Ultimately, a person who wants to manufacture a product using machinery can get to use that machinery under a leasing arrangement without owning it.

A lease can be defined as an arrangement between the lessor (owner of the asset) and the lessee (user of the asset). Whereby the lessor purchases an asset for the lessee and allows him to use r periodical payments. These payments are called lease rentals or minimum lease payments (MLP). Leasing is beneficial to both parties for availing tax benefits or doing tax planning. It is becoming the most preferred source of asset financing.

Advantages and Disadvantages of Leasing:



SHORT TERM FINANCES:

Short term financing means financing for a period of less than 1 year. The need for short-term finance arises to finance the current assets of a business like an inventory of raw material and finished goods, debtors, minimum cash and bank balance etc. Short-term financing is also named as working capital financing. Short term finances are available in the form of:

- Trade Credit
- Short Term Loans like Working Capital Loans from Commercial Banks
- Fixed Deposits for a period of 1 year or less
- Advances received from customers
- Creditors
- Payables
- Factoring Services
- Bill Discounting etc.

(i) Trade Credit:

It can be defined as ‘delay of payment’ permitted by the creditor or supplier of raw materials, consumables, etc., against the goods purchased from him. Any finance has three important parameters – the loan amount, rate of interest, and time period of a loan. In this case, the amount of credit is the bill amount, the interest rate is practically nil, and the period of credit is the credit period given in terms of payment.

Trade credit is also known as a spontaneous source of finance. It is a major source of working capital finance for most businesses, whether small or big. Amount and period of trade credit are dependent on two things. The customs and competition in the particular industry, and second, the buyer’s credibility in terms of the liquidity position, profit-making ability, past payment records, etc.

ment/Trade Credit Policy:

Trade credit terms are also known as terms of payment or trade credit policy. Whatever name they are called, the terms should be followed judiciously by both (creditors and buyers) to enjoy smooth workings and long-term relations. Buyers should release payment within the period specified, and creditors should encourage the buyer to abide by the agreed terms. There are three main terms of trade credit viz

(a) Maximum Credit Limit

It is the maximum amount of credit that a customer is allowed. Suppose $5,000 is the limit, and if the buyer has got one bill of $3,000, he will not be allowed another bill of more than $2,000 without clearing dues in the previous bill. The creditor determines the limit based on the credibility of the customer, the volume of its transactions, past payment track records, nature of business, etc.

(b) Credit Period

The credit cannot be allowed for an infinite time period. It is the maximum period of time before which a buyer is expected to make payment. Beyond this period, the creditor may ask for interest on the amount at the rate mentioned in terms of payment. The no. of days of credit is also determined similarly to the limit of credit amount.

(c) Cash Discount

It is the percentage of discount allowed by the creditor to the buyer to encourage him to pay as early as possible. It is specified as '5%/10 net 30'. This means a 5% discount is allowed for 10 days, i.e., on a bill of $100, the buyer can pay $95 if pays within 10 days. He can pay a net amount of $100 till the 30th day. If the payment is made after 30 days, the creditor will charge interest on the agreed rate.

(ii) Factoring:

Factoring is a financial service in which the business entity sells its bill receivables to a third party at a discount in order to raise funds. This is a type of business loan. Factoring differs from invoice discounting. The concept of invoice discounting involves getting the invoice discounted at a certain rate to get the funds, whereas the concept of factoring is broader. Factoring involves the selling of all the accounts receivable to an outside agency. Such an agency is called a factor.

Types of Factoring:

There are various types of factoring, such as:

- Recourse and non-recourse factoring
- Advance and maturity factoring
- Full factoring
- Disclosed and undisclosed factoring
- Domestic and cross-border factoring

onal factoring

- Specialized factoring
- Reverse factoring

Advantages of Factoring:

- It reduces the credit risk of the seller.
- The working capital cycle runs smoothly as the factor immediately provides funds on the invoice.
- Sales ledger maintenance by the factor leads to a reduction in cost.
- Improves liquidity and cash flow in the organization.
- It leads to the improvement of cash in hand. This helps the business to pay its creditors on time which helps in negotiating better discount terms.
- It reduces the need for the introduction of new capital into the business.
- There is a saving on administration or collection costs.

Disadvantages of Factoring:

- Factor collecting the money on behalf of the company can lead to stress in the company and the client relationships.
- The cost of factoring is very high.
- Bad behaviour of factor with the debtors can hamper the company's goodwill.
- Factors often avoid taking responsibility for risky debtors. So the burden of managing such a debtor is always on the company.
- The company needs to show all the details about company customers and sales to factors.

(iii) Bills Discounting:

The terms 'invoice discounting' or 'bills discounting' or 'purchase of bills' are all same. Invoice discounting is a source of working capital finance for the seller of goods on credit. Bill discounting is an arrangement whereby the seller recovers an amount of the sales bill from the financial intermediaries before it is due. Such intermediaries charge a fee for the service. On the other side, it is a business vertical for financial intermediaries such as banks, financial institutions, NBFCs, etc.

Advantages of Bill / Invoice Discounting:

The business gets the cash instantaneously, giving the business cycle better momentum. It allows an entrepreneur to do business without funds. This works like a bank overdraft, and the borrower pays the interest only on the amount of money utilized. There is tough competition in the market to extend such credit, and hence there are plenty of different products to suit the client's needs. There are borrowers who even cover the risk of bad debt and the service. The charge may be a little more.

Disadvantages of Bill / Invoice Discounting n be an expensive form of financing compared to other modes of financing such as bank overdrafts, etc. In many countries like India, the central bank encouraged the bill discounting scheme and allowed a lower percentage of interest. But, it was not successful due to various misuses by financing brokers, banks, etc.

Suppose there are two sister companies, A & B. A draws bills on B without any judicious transaction. B accepts it, and A discounts it with the bank and utilizes the credit illegitimately. If the intentions are bad, A & B may default on payment, and the banks will have to suffer.

(iv) Fixed Deposits:

A fixed deposit, also known as an FD, is an investment instrument offered by banks, as well as non-banking financial companies (NBFC) to their customers to help them save money. With an FD account, we can invest a sizeable amount of money at a predetermined rate of interest for a fixed period. At the end of the tenure, we receive the lump sum, along with an interest, which is a good money-saving plan. Banks offers different rates of interest for a fixed deposit account.

We can choose a fixed deposit for a period ranging from minimum 7-14 days to maximum 10 years. This is why an FD is sometimes called a term deposit. When we open a fixed deposit account at a specific interest rate, it is guaranteed, for the rate of interest remains the same, irrespective of any changes, which happen due to market fluctuations.

The interest we earn is either paid at maturity or on periodic basis depending on our choice. We are not allowed to withdraw the money before the maturity. If we want to, we have to pay a penalty.

INSTITUTIONAL FINANCE TO ENTREPRENEURS

A number of support institutions set up by central and state governments help the entrepreneurial activities in various ways. The activities cover a wide range of services like financing, technical guidance, equipment support, training, marketing and providing subsidy and grants. The following institutions are available for providing the above-mentioned benefits.

Financial Institutions:

- Industrial Development Bank of India (IDBI)
- Industrial Finance Corporation of India (IFCI)
- Small Industries Development Bank of India (SIDBI)
- National Small Industries Corporation Ltd (NSIC)
- State Small Industries Corporation (SSIC)
- Regional Rural Banks (RRBs)
- State Financial Corporation’s (SFCs)
- State Industrial Development Corporations (SIDCs)
- Cooperative Banks and Gramin Banks

r technical guidance:

- Small Industries Development Organisation (SIDO)
- District Industries Centres (DICs)
- Technical Consultancy Organisations (TCOs)
- Small Industries Service Institutes (SISIs)
- State Small Industries Development Corporations (SSIDCs)
- Industrial Development Corporation (IDCo)
- Agricultural Promotion and Investment Corporation of Orissa Limited (APICOI)

Training Institutions:

- National Institute for Entrepreneurship and Small Business Development (NIESBUD)
- Entrepreneurship Development Institute of India (EDII)
- Small Industries Service Institute (SISI)
- National Bank for Agriculture and Rural Development (NABARD)
- Council for Advancement of Peoples Action and Rural Technology (CAPART)
- District Industries Centre (DIC)

State Financial Corporations:

State Financial Corporations (SFCs)
State Financial Corporations (SFCs) are the State level financial institutions which play a vital role in the growth of small & medium enterprises in the concerned States. They offer financial assistance in the form of direct subscription to debentures/equity, term loans, guarantees, discounting of bills of exchange & seed/ special capital, etc. SFCs have been set up with the purpose of catalysing higher investment, engendering greater employment & extending the ownership base of industries. They have also started aiding newer types of business activities like tissue culture, floriculture, poultry farming, services related to engineering, marketing and commercial complexes. In India, there are 18 State Financial Corporations (SFCs). These are:

Andhra Pradesh State Financial Corporation (APSFC)

- Himachal Pradesh Financial Corporation (HPFC)
- Madhya Pradesh Financial Corporation (MPFC)
- North Eastern Development Finance Corporation (NEDFI)
- Rajasthan Finance Corporation (RFC)
- Tamil Nadu Industrial Investment Corporation Limited
- Uttar Pradesh Financial Corporation (UPFC)
- Delhi Financial Corporation (DFC)
- Gujarat State Financial Corporation (GSFC)
- The Economic Development Corporation of Goa (EDC)
- Haryana Financial Corporation (HFC)
- Jammu & Kashmir State Financial Corporation (JKSFC)
- Karnataka State Financial Corporation (KSFC)
- Kerala Financial Corporation (KFC)
- Maharashtra State Financial Corporation (MSFC)

- West Bengal Financial Corporation (WBFC)

At present in India, there are 18 state finance corporations (out of which 17 SFCs were established under the SFC Act 1951). Tamil Nadu Industrial Investment Corporation Ltd. which is established under the Company Act, 1949, is also working as state finance corporation.

Organization and Management

A Board of ten directors manages the State Finance Corporations. The State Government appoints the managing director generally in consultation with the RBI and nominates the name of three other directors.

All insurance companies, scheduled banks, investment trusts, co-operative banks, and other financial institutions elect three directors. Thus, the state government and quasi-government institutions nominate the majority of the directors.

Functions of State Finance Corporations

The various important functions of State Finance Corporations are:
(i) The SFCs provides loans mainly for the acquisition of fixed assets like land, building, plant, and machinery.
(ii) The SFCs help financial assistance to industrial units whose paid-up capital and reserves do not exceed Rs. 3 crores (or such higher limit up to Rs. 30 crores as may be notified by the central government).
(iii) The SFCs underwrite new stocks, shares, debentures etc., of industrial units.
(iv) The SFCs grant guarantee loans raised in the capital market by scheduled banks, industrial concerns, and state co-operative banks to be repayable within 20 years.

Non-Banking Financial Corporations:

Financial Institutions:

(i) Industrial Development Bank of India (IDBI)

The IDBI was established on July 1, 1964 by the Government of India under an Act of Parliament as the principal financial institution in the country.

Main Functions of IDBI

- The IDB1 provides assistance to the small-scale sector through its scheme of refinance and bills rediscounting scheme.

ncial assistance has been indirect in the form of refinancing of loans and the State Financial Corporation's (SFCs).

- In order to assist the small-scale sector, the IDBI has set up Small Industries Development Fund (SIDF) in May 1986. This fund basically aims at providing a focal point to co-ordinate financial and non-financial inputs required for growth of small industries sector.
- In association with Government of India, IDB1 has constituted National Equity Fund (NEF) to prevail equity type of support to tiny and small-scale units which are engaged in manufacturing activities. The scheme is administered by IDB1 through nationalized banks.
- The IDBI has also introduced the single window assistance 'scheme for grant of term loans and working capital assistance to tiny, small and medium scale enterprises.
- The IDB1 has also set up a Voluntary Executive Corporation Cell (VECC) to use the services of experts, professionals for counselling small units and for providing consultancy support in specified areas.

(ii) Industrial Finance Corporation of India Ltd (IFCI):

The Industrial Finance Corporation of India was set up by the Government of India under IFC1 Act in July 1948. It is an important financial institution which gives financial assistance to the entrepreneurs through rupee and foreign currency loans, underwriting, direct subscriptions to shares, debentures and guarantees. It also extends other financial facilities like equipment procurement, equipment finance, buyer's and supplier's credit, equipment leasing and finance to leasing and hire-purchase companies.

The IFCI has devised new promotional schemes such as

- Consultancy fees, subsidy schemes for assisting small scale entrepreneurs in marketing sector.
- Interest subsidy schemes for women entrepreneurs.
- Pollution control in small and medium scale enterprises.
- Encouraging the modernization of tiny, small and medium scale industries

(iii) Small Industries Development Bank of India (SIDBI):

SIDBI was set up in April 1990 as a wholly owned subsidiary of IDBI (Industrial Development Bank of India) t provide financial assistance to the entrepreneurs under an Act of the Parliament, namely Small Industries Development Bank of India Act 1989.

The Bank has been delinked from IDBI with effect from March 27, 2002. The Bank caters all SSIs –tiny, village and cottage—through its Head Official at Lucknow.

Channels of SIDBI's Assistance:

(a) Indirect Finance:

By way of refinance and bills discounting through more than 901 primary lending institutions having over 65000 outlets across the country.

(b) Direct Finance:

Direct finance is given through SIDBI's own 38 offices by means of several tailor-made schemes to reach assistance to specific target groups.

(c) Promotional and Development Activities:

Involving accredited Non-Government organizations voluntary organizations, Scientific and Research Institutions, Technology Institutions, Management Institutions, etc.

Thus, SIDBI is the principle financial institution for promotion, financing and development of small-scale industries in India. It co- ordinates functions of existing institutions engaged in similar activities.

Accordingly, SIDBI has taken over the responsibility of administering Small industries Development Fund and nation Equity fund which were earlier administered by IDBI.

Functions of SIDBI:

The important functions of SIDBI are:

- To initiate steps for technological up-gradation and modernization of existing units.
- To expand the cannels for marketing the products of SSI sector in domestic and international markets.
- To promote employment-oriented industries especially in semi- urban areas to create employment opportunities and thereby checking migration of people to urban areas.
- To refinance loans and advances extended by the primary lending institutions to SSI units and also provides resources to them.
- To discount and rediscount bills arising from sale of machinery to or manufactured by industrial units in the SSI sector.
- To provide services like leasing, factoring etc. to industrial concerns in the SSI sector.
- To expand financial support to State Small Industries Development Corporation for providing scare raw-materials to industrial units in SSI sector.
- To grant loan and advances to any person engaged in exporting or executing any turnkey project abroad.
- To subscribe to or purchasing stocks and shares, bonds and debentures of any state /financial Corporations.

Scope of SIDBI:

The SIDBI covers all industrial undertakings like any concern engaged in business activities and which is regarded as a small-scale undertaking under Section 11-B of the Industrial Development and Regulation Act, 1951.

The following business activities undertaken by small scale sector are covered under the scope of SIDBI:

- The manufacturing preservation or processing of goods;
- Shipping industry;
- Mining industry;
- Hotel industry
- Transport of passengers or goods by road/water/air;
- Generation or distribution of electricity or any other form of power;
- Maintenance, repair, testing or servicing of machinery of any description or vehicle or vessels or motor boats or trailers or tractors;
- Assembling, repairing or packing any article with the aid of machinery or power;
- The development of any contiguous area of land as an Industrial Estate;
- Fishing or providing stores facilities for fishing or maintenance thereof;

g special or technical knowledge or other services for the promotion of industrial growth; or

- The research and development of any process or product in relation to any of the matters aforesaid.
- The financial assistance of SIDBI is channelized through the existing credit delivery system comprising SFC, State Industrial Development Corporation, Commercial Banks and DRRBs.

(iv) National Small Industries Corporation Ltd (NSIC)

National Small Industries Corporation Limited (NSIC) is a PSU established by the Government of India in 1955. It falls under Ministry of Micro, Small & Medium Enterprises of India. It was established in 1955 to promote and develop micro and smalls scale industries and enterprises in the country.

They provide a wide range of services mostly promotional in character to small scale industries. The important functions NSIC performs are grouped as under:

- Provides financial assistance by way of hire-purchase scheme for purchase of machinery and equipment, required for the setting up industries.
- Provides various equipment on lease basis.
- Assists in marketing of the products of SSIs.
- Helps in exporting the product of SSIs.
- Provides training to workers of SSIs in various trades.
- Helps in the development and up gradation of technology and modernization of the industries.
- Undertakes construction of industrial estates.
- Purchases huge quantity of important raw materials and distribute the same to SSIs at reasonable rates.
- Develops prototype machines and equipment to pass on to SSIs for commercial production.
- Sets up small scale industries in other developing countries on turn-key basis.

So, in the above way NSIC plays a prominent role for the development of entrepreneurship as well as industrialization, in the country.

(v) Regional Rural Banks (RRBS)

Regional Rural Banks are local level banking organizations operating in different States of India. They have been created with a view to serve primarily the rural areas of India with basic banking and financial services. However, RRB's may have branches set up for urban operations and their area of operation may include urban areas too.

Regional Rural Banks were established under the provisions of an Ordinance passed on 26 September 1975 and the RRB Act. 1976 to provide sufficient banking and credit facility for agriculture and other rural sectors. These were set up on the recommendations of the Narasimham Working Group during the tenure of Indira Gandhi's government with a view to include rural areas into economic mainstream since that time about 70% of the Indian Population was of Rural Orientation. The development process of RRBs started on 2 October 1975 with the forming of the first RRB, the Prathama Bank. Also, on 2 October 1976 five regional rural banks were set up with a total authorized capital of Rs. 100 crore ($10 Million) which later augmented to 500 crores ($50 Million).

Organization of the RRB:

The authorized capital of an RRB is fixed at Rs. 1 crore and its issued capital at Rs. 2 lakhs. Of the issued capital, 50 per cent is to be subscribed by the Central Government, 15 per cent by the concerned State Government and the rest 35 per cent by the sponsoring bank.

The working and affairs of the RRB are directed and managed by a Board of Directors consists of a Chairman, three directors to be nominated by the Central Government, and not more than two directors to be nominated by the State Government concerned, and not more than 3 directors to be nominated by the sponsoring bank. The chairman is appointed by the Central Government and his term of office does not exceed five years.

Functions of the RRB:

The functions of the RRB are as follows:

- Granting of loans and advances to small and marginal farmers and agricultural laborer, whether individually or in groups, and to co-operative societies, agricultural processing societies, co-operative farming societies, primarily for agricultural purposes or for agricultural operations and other related purposes;
- Granting of loans and advances to artisans, small entrepreneurs and persons of small means engaged in trade, commerce and industry or other productive activities within its area of co-operation; and
- Accepting deposits.

(vi) State Financial Corporations (SFCS):

IFCI provides financial assistance only to large sized industrial undertakings. In order to cater to the needs of the small-scale units, the Government of India passed the State Financial Corporations Act in 1951 under which the State Financial Corporation's (SFCs) were set up. The first SFC was set up in Punjab in 1953. Today, there are 18 SFCs functioning in the country. State Financial Corporations are managed by a Managing Director, Board of Directors and the Executive Committee is headed by a chairman.

The functions of SFCs are as follows

- To advance term loans to small scale and medium scale industrial units.
- It underwrites the issue of stocks, shares, debentures and bonds of industrial units.
- It grants loans to the industrial concerns which is repayable within a period not more than 20 years.
- It subscribes to debentures floated by industrial concerns.
- It provides financial assistance to small road transport operators, tour operators, hoteliers, hospitals, nursing homes, etc.

(vii) State Industrial Development Corporations (SIDCS)

The State Industrial Development Corporations have been set up by the State Governments as companies wholly owned by them. At present, 22 such SIDCs are functioning in India. SIDCs are not merely financing agencies, but are intended to act as instruments for accelerating the pace of industrialization in the respective States.

providing financial assistance to industrial concerns by way of loans, guarantees and underwriting of or direct subscriptions to shares and debentures, the SIDCs undertake various promotional activities such as conducting techno-economic surveys, project identification, preparation of feasibility studies, selection and training of entrepreneurs. They also promote joint sector projects in association with private promoters. In such projects SIDCs take 26% private co-promoter takes 25% of the equity and the rest are offered to the investing public.

SIDCs also undertake the development of industrial areas, construction of sheds and provision of infrastructural facilities .and also the development of new growth centres. They also administer various State Government incentive schemes.

(viii) Cooperative Banks

The co-operative banks are small-sized units which operate both in urban and non-urban centres. They finance small borrowers in industrial and trade sectors besides professional and salary classes. Regulated by the Reserve Bank of India, they are governed by the Banking Regulations Act 1949 and banking laws (co- operative societies) act, 1965. The co-operative banking structure in India is divided into following 5 categories:

Primary Co-operative Credit Society

The primary co-operative credit society is an association of borrowers and non-borrowers residing in a particular locality. The funds of the society are derived from the share capital and deposits of members and loans from central co-operative banks. The borrowing powers of the members as well as of the society are fixed. The loans are given to members for the purchase of cattle, fodder, fertilizers, pesticides, etc.

Central Co-operative Banks

These are the federations of primary credit societies in a district and are of two types-those having a membership of primary societies only and those having a membership of societies as well as individuals. The funds of the bank consist of share capital, deposits, loans and overdrafts from state co-operative banks and joint stocks. These banks provide finance to member societies within the limits of the borrowing capacity of societies. They also conduct all the business of a joint stock bank.

State Co-operative Banks

The state co-operative bank is a federation of central co- operative bank and acts as a watchdog of the co-operative banking structure in the state. Its funds are obtained from share capital, deposits, loans and overdrafts from the Reserve Bank of India. The state co-operative banks lend money to central co-operative banks and primary societies and not directly to the farmers.

Land Development Banks

The Land development banks are organized in 3 tiers namely; state, central, and primary level and they meet the long-term credit requirements of the farmers for developmental purposes. The state land development banks oversee, the primary land development banks situated in the districts and tehsil areas in the state. They are governed both by the state government and Reserve Bank of India. Recently, the supervision of land development banks has been assumed by National Bank for l Rural development (NABARD). The sources of funds for these banks are the debentures subscribed by both central and state government. These banks do not accept deposits from the general public.

Urban Co-operative Banks

The term Urban Co-operative Banks (UCBs), though not formally defined, refers to primary co-operative banks located in urban and semi-urban areas. These banks, till 1996, were allowed to lend money only for non-agricultural purposes. This distinction does not hold today. These banks were traditionally centred on communities, localities, work place groups. They essentially lend to small borrowers and businesses. Today, their scope of operations has widened considerably.

The origins of the urban co-operative banking movement in India can be traced to the close of nineteenth century. Inspired by the success of the experiments related to the co-operative movement in Britain and the co-operative credit movement in Germany, such societies were set up in India. Co-operative societies are based on the principles of cooperation, mutual help, democratic decision making, and open membership.

Co-operatives represented a new and alternative approach to organization as against proprietary firms, partnership firms, and joint stock companies which represent the dominant form of commercial organization. They mainly rely upon deposits from members and non-members and in case of need, they get finance from either the district central co-operative bank to which they are affiliated or from the apex co-operative bank if they work in big cities where the apex bank has its Head Office. They provide credit to small scale industrialists, salaried employees, and other urban and semi-urban residents.

Functions of Co-operative Banks

Co-operative banks also perform the basic banking functions of banking but they differ from commercial banks in the following respects

- Commercial banks are joint-stock companies under the companies' act of 1956, or public sector bank under a separate act of a parliament whereas co-operative banks were established under the co-operative society's acts of different states.
- Commercial bank structure is branch banking structure whereas co-operative banks have a three-tier setup, with state co- operative bank at apex level, central / district co-operative bank at district level, and primary co-operative societies at rural level.
- Only some of the sections of banking regulation act of 1949 (fully applicable to commercial banks), are applicable to co- operative banks, resulting only in partial control by RBI of co-operative banks and
- Co-operative banks function on the principle of cooperation and not entirely on commercial parameters.

<u>Training Institutions</u>

National Institute for Entrepreneurship and Small Business Development (NIESBUD)

s established in 1983 by the Ministry of Industry, Government of India. Its main functions and objectives are:

⇒ To serve as an apex national level resource institute to accelerate the process of entrepreneurship development.

⇒ To help and facilitate various agencies in carrying out training and other entrepreneurship development activities.

⇒ To provide vital information support to trainers, promoters and entrepreneurs.

⇒ To evolve effective training strategies.

⇒ To identify, train and assist potential entrepreneurs for setting up ventures.

This institute acts as a nodal agency. It organises about 29 national and 6 international training programmes every year.

Entrepreneurship Development Institute of India (EDII)

It was established in 1983 by financial institutions. It conducts research, training and institution-building activities for encouraging the participation of backward regions. The main objectives of EDII are:

❖ To increase the supply of trained entrepreneurs through training.
❖ To generate opportunities for self-employment.
❖ To improve managerial capabilities of small-scale industries.
❖ To promote small enterprises at rural level.
❖ To contribute to the dispersal of business ownership.

Small Industries Service Institute (SISI)

At the heart of all agencies dealing with development of small industry is small industries development organization, SIDO. It was originally known as central small industries organization (CSIO). Attached to the ministry, SIDO administers small industries service institute (SISI's).

The small industries service institutes (SISI's) are set-up one in each state to provide consultancy and training to small and prospective entrepreneurs. The activities of SISs are co-ordinate by the industrial management training division of the DC, SSI office (New Delhi). In all there are 28 SISI's and 30 Branch SISI's set up in state capitals and other places all over the country. SISI has wide spectrum of technological, management and administrative tasks to perform.

Functions of SISI

❖ To assist existing and prospective entrepreneurs through technical and managerial counseling such as help in selecting the appropriate machinery and equipment, adoption of recognized standards of testing, quality performance etc;
❖ Conducting EDPs all over the country;
❖ To advise the Central and State governments on policy matters relating to small industry development;
❖ To assist in testing of raw materials and products of SSIs, their inspection and quality control;

de market information to the SISI's;

- To recommend SSI's for financial assistance from financial institutions;
- To enlist entrepreneurs for partition in Government stores purchase programme;
- Conduct economic and technical surveys and prepare techno- economic feasible reports for selected areas and industries.
- Identify the potential for ancillary development through sub- contract exchanges;
- Organize seminars, Workshops and Industries Clinics for the benefit of entrepreneurs

National Bank for Agriculture and Rural Development (NABARD)

NABARD was established on the recommendations of Shivaraman Committee, (by act 61, 1981 of Parliament) on 12 July 1982 to implement the National Bank for Agriculture and Rural Development Act 1981. It replaced the Agricultural Credit Department (ACD) and Rural Planning and Credit Cell (RPCC) of Reserve Bank of India, and Agricultural Refinance and Development Corporation (ARDC). It is one of the premier agencies to provide credit in rural areas. NABARD is India's specialised bank for Agriculture and Rural Development in India.

The initial capital of NABARD was Rs. 100 crores. Consequent to the revision in the composition of share capital between Government of India and RBI, the paid-up capital as on 31 March 2013, stood at 4000 crores with Government of India holding 3,980 crore (99.50%) and Reserve Bank of India 20.00 crore (0.50%). As on 31 March 2014, NABARD paid up capital stood at Rs. 4700 crores (Rs. 4680 Crore of GoI and Rs. 20 Crore of RBI).

NATIONAL BANK FOR AGRICULTURE AND RURAL DEVELOPMENT (NABARD) is an apex development bank in India for all rural credit having headquarters based in Mumbai (Maharashtra) and other branches are all over the country. The Committee to Review Arrangements for Institutional Credit for Agriculture and Rural Development (CRAFICARD), set up by the Reserve Bank of India (RBI) under the Chairmanship of Shri B. Sivaraman, conceived and recommended the establishment of the National Bank for Agriculture and Rural Development (NABARD).

It was established on 12 July 1982 by a special act by the parliament and its main focus was to uplift rural India by increasing the credit flow for elevation of agriculture & rural non-farm sector and completed its 25 years on 12 July 2007. It has been accredited with "matters concerning policy, planning and operations in the field of credit for agriculture and other economic activities in rural areas in India". RBI sold its stake in NABARD to the Government of India, which now holds 99% stake. It is active in developing financial inclusion policy and is a member of the Alliance for Financial Inclusion.

Objectives of NABARD

NABARD was established in terms of the Preamble to the Act, "for providing credit for the promotion of agriculture, small scale industries, cottage and village industries, handicrafts and other rural crafts and other allied economic activities in rural areas with a view to promoting IRDP and securing prosperity of rural areas and for matters connected therewith in incidental thereto".

The main objectives of the NABARD as stated in the statement of objectives while placing the bill before the Lok Sabha were categorized as under onal Bank will be an apex organization in respect of all matters relating to policy, planning operational aspects in the field of credit for promotion of Agriculture, Small Scale Industries, Cottage and Village Industries, Handicrafts and other rural crafts and other allied economic activities in rural areas.

- The Bank will serve as a refinancing institution for institutional credit such as long-term, short-term for the promotion of activities in the rural areas.
- The Bank will also provide direct lending to any institution as may be approved by the Central Government.
- The Bank will have organic links with the Reserve Bank and maintain a close link with in.

Role and Functions of NABARD

NABARD is the apex institution in the country which looks after the development of the cottage industry, small industry and village industry, and other rural industries. NABARD also reaches out to allied economies and supports and promotes integrated development. And to help NABARD discharge its duty, it has been given certain roles as follows:

- Serves as an apex financing agency for the institutions providing investment and production credit for promoting the various developmental activities in rural areas
- Takes measures towards institution building for improving absorptive capacity of the credit delivery system, including monitoring, formulation of rehabilitation schemes, restructuring of credit institutions, training of personnel, etc.
- Co-ordinates the rural financing activities of all institutions engaged in developmental work at the field level and maintains liaison with Government of India, State Governments, Reserve Bank of India (RBI) and other national level institutions concerned with policy formulation
- Undertakes monitoring and evaluation of projects refinanced by it.
- NABARD refinances the financial institutions which finances the rural sector.

Council for Advancement of Peoples Action and Rural Technology (CAPART)

Recognizing the need for an organization that would coordinate and catalyse the development work of voluntary agencies in the country, particularly to ensure smooth flow of benefits to the underprivileged and socio-economically weaker sections of society, Government of India, in September, 1986 set up the Council for Advancement of People's Action and Rural Technology (CAPART), a registered society under the aegis of the Department of Rural Development, by merging two autonomous bodies, namely, People's Action for Development of India (PADI) and Council for Advancement of Rural Technology (CAPART).

The main objectives of the CAPART are: -

- To encourage, promote and assist voluntary action for the implementation of projects intending enhancement of rural prosperity.
- To Strengthen and promote voluntary efforts in rural development with focus on injecting new technological inputs;
- To act as a catalyst for the development of technology appropriate for rural areas.
- To promote, plan, undertake, develop, maintain and support projects/schemes aimed at all-round development, creation of employment opportunities, promotion of self-reliance, generation of awareness, organization and improvement in the quality of life of the people in rural areas through voluntary action.

District Industries Centre (DIC)

The 'District Industries Centre' (DICs) programme was started by the central government in 1978 with the objective of providing a focal point for promoting small, tiny, cottage and village industries in a particular area and to make available to them all necessary services and facilities at one place. The finances for setting up DICs in a state are contributed equally by the particular state government and the central government. To facilitate the process of small enterprise development, DICs have been entrusted with most of the administrative and financial powers. For purpose of allotment of land, work sheds, raw materials etc., DICs functions under the 'Directorate of Industries'. Each DIC is headed by a General Manager who is assisted by four functional managers and three project managers to look after the following activities: Activities of District Industries Centre (DIC):

- Economic Investigation
- Plant and Machinery
- Research, education and training
- Raw materials
- Credit facilities
- Marketing assistance
- Cottage industries

Objectives of District Industries Centre (DIC):

- The important objectives of DICs are as follow:
- Accelerate the overall efforts for industrialization of the district.
- Rural industrialization and development of rural industries and handicrafts.
- Attainment of economic equality in various regions of the district.
- Providing the benefit of the government schemes to the new entrepreneurs.
- Centralization of procedures required to start a new industrial unit and minimization- of the efforts and time required to obtain various permissions, licenses, registrations, subsidies etc.