Report
of
The Internal Group to Review Guidelines on Credit Flow
to
SME Sector

2005

RESERVE BANK OF INDIA
Central Office
Rural Planning and Credit Department
Mumbai

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Acknowledgement

On behalf of the Internal Group, I would like to express our deep gratitude to the Governor, the Deputy Governor (Shri V.Leeladhar) and the Executive Director (Shri A.V.Sardesai) for giving us this unique opportunity, and for their guidance and encouragement. They have spared their valuable time for holding several rounds of discussions with the Group on the issues involved, and provided us the necessary direction.

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The Regional Offices of Rural Planning & Credit Department conducted sample surveys of select bank branches and borrowers and also collected information from departments and agencies of the state governments. The Group wishes to thankfully acknowledge their painstaking efforts and valuable inputs.

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Finally, I would like to thank all the members of the Internal Group for their valuable contribution. The painstaking efforts put in by the Member-Secretary, Shri G.P.Borah in arranging for the meetings of the Group as also in preparing

this report need special mention.

C. S. Murthy
Chairman of the Internal Group
Mumbai
April 13, 2005

Executive Summary

Small and Medium Enterprises (SMEs) are the growth engines of the Indian economy due to their ability to create jobs, foster entrepreneurship, and to provide depth to the industrial base of the economy.

As per findings of the third census on SSI, the total SSI sector (registered and unregistered units) in India comprised 1,05,21,190 units, out of which over 44 lakh (42.26 per cent) were SSIs and the remaining 61 lakh (57.74 per cent) were SSSBEs. About 55.0 per cent of total SSI units were located in rural India. The number of ancillary units among SSIs at 1.32 lakh constituted 2.98 per cent of the total number of SSIs. Tiny units with original investment in plant & machinery up to Rs.25 lakh numbering 44.26 lakh formed a dominating 99.5 per cent of the total number of SSIs. About 10.11% of the SSI units were women enterprises.

The third census also revealed that about 44.0 per cent of the units were in the services sector, followed by 40.0 per cent of the units in manufacturing and allied activities sector and 16.0 per cent of units in repairing and maintenance sector. Thus, services sector emerged as the dominant component in the total SSI Sector.

As per the third census report, total output of the registered units in the year 2001-02 was estimated to be Rs. 70,861.73 crore. The SSI sector employed 2,49,32,763 persons during the reference period. There were 50,606 exporting units accounting for exports to the tune of Rs.14,19,956 lakh.

With the opening up of the Indian economy due to liberalization and globalization, this vital sector of the economy is facing huge challenges and competition from of the domestic as well as multi-national corporations. In view of the above, it is necessary to expeditiously consider issues relating to flow of credit to the sector, restructuring of borrowal accounts of SSI and Medium Enterprises, etc. Accordingly, an ‘Internal Group’ was constituted on February 2, 2005 under the Chairmanship of Shri C.S.Murthy, Chief General Manager-in-Charge, Rural Planning & Credit Department, Reserve Bank of India, Central Office, Mumbai. Apart from reviewing all circulars and guidelines issued by Reserve Bank in the past regarding financing of SSI and MEs, the Group was requested to suggest appropriate terms for restructuring of the borrowal accounts of SSI/Medium Enterprises. The Group was also requested to examine the guidelines issued by Reserve Bank for nursing sick SSIs and suggest suitable relaxation and liberalization of these norms.

The Group has interacted with SIDBI, select SSI Associations and banks to get their views and suggestions. A survey of select borrowers as well bank branches was conducted through the Regional Offices of Reserve Bank. Based on suggestions and feedback received, the Group has firmed up its recommendations. The salient recommendations of the Group are as under:

A. Review of Reserve Bank's guidelines regarding financing of SSI Sector

1. Definition

Current SSI/tiny definition may continue. Units with investment in plant and machinery in excess of SSI limit and up to Rs.10 crore may be treated as Medium Enterprises (ME). The definition may be reviewed after enactment of the Small and Medium Enterprises Development Bill. Only SSI financing will be included in Priority Sector.

2. Fixing of targets & sub-targets for SME financing

The existing instructions to banks to fix self-set targets for financing SSI may be made in respect of financing SME. However, they may so fix the targets as to reflect a higher disbursement over the immediately preceding year. The sub-targets for financing tiny units and smaller units to the extent of 40% and 20% respectively may continue. Similarly, the banks may also fix self-set target for financing of Medium Enterprises.

3. Institutional Arrangements

(i) The existing institutional arrangements for review of credit to SSI sector like the Standing Advisory Committee, cells at the bank head office level and at important regional centres may continue. However, they may review flow of credit to SME sector.

(ii) At the Regional offices of the Reserve Bank, empowered committees may be constituted with the Regional Director of the Reserve Bank as the Chairman and the SLBC Convenor, senior level officers from two banks having predominant share in SME financing in the state, representative of SIDBI Regional Office, the Director of Industries of the State Government, one or two senior level representatives from the SME/SSI Associations in the state, and a senior level officer from SFC/SIDC as members. The Committee will meet periodically and review the progress in SME financing. It will also coordinate with other banks/financial institutions and the state government in removing bottlenecks, if any, to ensure smooth flow of credit to the sector. The committees may decide the need to have similar committees at cluster/district levels.

(iii) The banks may open specialized SME branches in identified clusters/centres with preponderance of ME units to enable the entrepreneurs to have easy access to the bank credit and to equip bank personnel to develop the requisite expertise. The existing specialized SSI branches may, if need be, redesignated as SME branches. Though their core competence will be utilized for extending credit and other services to SME sector, they will have operational flexibility to extend finance/render other services to other sectors/borrowers.

(iv) The Boards of banks may review the progress in achieving the self-set targets as also rehabilitation and restructuring of SME accounts on a quarterly basis to ensure that the required emphasis at the highest forum of the banks is given to this sector. Accordingly, the banks may collect statistics relating to SME financing on a quarterly basis.

(v) At the branch level, the name of the nodal officer to help the SME entrepreneurs in complying with the bank's formalities may prominently be displayed.

(vi) For wider dissemination and easy accessibility, the policy guidelines formulated by Boards of banks as well as instructions/guidelines issued by Reserve Bank may be displayed on a centralized web-site.

4. Withdrawal of RBI’s circular instructions

The boards of banks may be empowered to frame their own policies in regard to SME financing. While formulating this policy, the board may, inter alia, cover the following aspects:

(a) limits up to which collateral free loans can be granted, taking into consideration the availability of guarantee facility under Credit Guarantee Trust for Small Industries for collateral-free loans up to Rs.25 lakh;
(b) limits up to which composite loans can be granted through a single window;
(c) basis for working out the term loan and working loan components;
(d) time limits within which the loan applications have to be disposed of;
(e) limits up to which officers at different levels can sanction different types of loans; and
(f) charges to be levied for different services, keeping in view the need to service small entrepreneurs.

The Group recommends withdrawing the instructions contained in six circulars of the Bank. It is expected that the policies formulated by banks will be more liberal than the existing policies. Till the Boards formulate their policies, the Reserve Bank guidelines will continue to be applicable to them.

B. Restructuring of borrowal accounts

1. Coverage

i) The revised restructuring mechanism will be applicable to all SME units, excepting corporate SME having aggregate credit limits of Rs.10 crore or more under multiple/consortium banking arrangements,
ii) It is proposed to leave the matter regarding formulation of rehabilitation/debt restructuring policies in respect of SMEs having credit

limits from a single bank to the banks concerned with the approval of their Board of directors. It is expected that the policies formulated by banks will be simple to comprehend and more liberal than the existing policies.

iii) In case of corporate borrowers in SME sector having credit limits of up to Rs.10 crore under multiple banking arrangements as also non-corporate borrowers having any credit limits under multiple banking arrangements, the bank with the maximum share in the limits, in association with the bank having second largest share may work out restructuring packages, provided the units are potentially viable.

iii) The restructuring may be done suo motu by the bank or on receipt of a request to that effect from the borrowing units.

iv) All accounts except those classified as 'loss assets' will be eligible for restructuring.

2. Viability criteria

The Boards of banks may decide on the acceptable viability benchmarks in such a way that the restructured amount together with interest thereon is recovered over a period of 7-10 years.

3. Time frame

While the bank should decide upon the eligibility of the unit and work out a restructuring package within a maximum period of 60 days, the sanctioned package should be implemented within a period of 30 days thereafter. The Boards of banks may consider fixing shorter time frame depending upon level of expertise within the bank.

4. Restructuring of accounts of corporate SME units with multiple banking arrangements

The Special Group to Review Corporate Debt Restructuring (CDR) Mechanism (Chairperson: Smt. S. Gopinath) has recommended that the

revised CDR Mechanism may be made applicable to corporate borrowers with credit limits of Rs.10 crore or more with multiple banking arrangements. Hence this Group recommends that restructuring of accounts of corporate

SSI/ME borrowers having credit limits aggregating Rs.10 crore or more under multiple banking arrangements may be covered under the revised CDR mechanism.

C. Review of Reserve Bank's guidelines on nursing sick SSIs

i) All the accounts of sick units may be restructured on the lines of proposed debt restructuring mechanism for SME sector;

ii) Extant guidelines on definition of a sick SSI unit will continue. All other instructions relating to viability and parameters for relief and concessions to be provided to sick SSI units, as prescribed by Reserve Bank may be withdrawn and banks may be given freedom to lay down their own guidelines with the approval of their Board of Directors. While formulating their guidelines, banks may consider the indicative guidelines suggested by the Working Group on Rehabilitation of Sick SSI Units (Chairman: Shri S.S.Kohli).

iii) As per extant guidelines, a unit is considered as sick when any of the borrowal accounts of the unit remains sub-standard for more than six months. The banks may consider restructuring accounts of units having financial problems even if the account has remained sub-standard for six months or less.

iv) It is expected that the policies formulated by banks in respect of (ii) and (iii) above will be more liberal than the existing policies.

v) Every attempt may be made by banks to implement the rehabilitation package in respect of the accounts of sick units at the earliest. In any case, it may not exceed a period of 3 months from the date of bank deciding suo motu to reconstruct the accounts or date of receipt of request to that effect from the borrowing unit concerned.

vi) Since the empowered committees to be constituted with the Regional Director of Reserve Bank as the Chairman, will also look into coordination issues between different agencies and banks, and in view of the above recommendations relating to restructuring of the accounts of sick SSI/ME, the future role of SLIIC may be reviewed.

Chapter I

Current Scenario of Small and Medium Enterprises Sector

Small and Medium Enterprises (SMEs) are the growth engines of the Indian economy due to their ability to create jobs, foster entrepreneurship, and to provide depth to the industrial base of the economy. With the opening up of the Indian economy due to liberalization and globalization, this vital sector of the economy is facing huge challenges and competition from the domestic as well as multi-national corporations. In view of the above, it has become necessary to consider measures for smoothening the flow of credit to this sector as also for instituting a liberalized mechanism for restructuring of borrowal accounts of Small Scale Industries (SSIs) and Medium Enterprises (MEs).

1.2 An 'Internal Group' (herein after referred to as "the Group") has, therefore, been constituted on February 2, 2005 in Rural Planning & Credit Department, Reserve Bank of India, Central Office, Mumbai with the following Terms of Reference**:**

- To review all circulars and guidelines issued by the RBI in the past regarding financing of SMEs and consider removal/substitution of these guidelines by simpler and more liberal terms;
- To suggest appropriate terms for restructuring of the borrowal accounts of SMEs;
- To examine the guidelines issued by the RBI for nursing sick SMEs and suggest suitable relaxation and liberalization of these terms; and
- To recommend measures on any other issue incidental to the above terms of reference.

The Group could, if deemed necessary, invite experts to the proceedings of the Committee.

1.3 The Group comprised the following:

Chairman

Shri C.S.Murthy, CGM-in-Charge, RPCD, Central Office

Members

Shri K.U.B.Rao, Director, DEAP, Central Office, Mumbai;
Shri D.N.Tripathi, Joint Legal Adviser, Legal Department, Central Office, Mumbai;
Shri A.P.Gaur, Director, DESACS, Central Office, Mumbai; and
Shri Rajinder Kumar, Deputy General Manager, DBOD, Central Office, Mumbai.

Member Secretary

Shri G.P.Borah, Deputy General Manager, RPCD, Central Office, Mumbai.

Methodology

1.4 The Group has prepared a concept paper covering recent developments in Small and Medium Enterprises (SMEs) sector, including cross-country perspectives. It is presented as Annexure I.

1.5 The Group has interacted with the CMD of SIDBI, Presidents of select SSI Associations and senior officials of select banks to get their views and suggestions. The Group has received valuable inputs from sample surveys of select bank branches and borrowers, conducted by the Regional Offices of Reserve Bank. The Group has received feedback from select banks which have been playing proactive role in extending finance to the SME sector. The Group has also received information from departments and agencies of the state governments, through the Regional Offices of Reserve Bank.

Organisation of the Report

1.6 This Report comprises six chapters. The next Chapter provides an overview of the SSI sector in India, while the various issues relating to promotion and development of SME sector are dealt with in Chapter III. A review of the extant guidelines of Reserve Bank relating to financing of SSI sector has been attempted in Chapter IV. The framework for restructuring of the borrowal accounts of SMEs has been presented in Chapter V. The concluding Chapter VI deals with restructuring of the borrowal accounts of sick SSI/Medium Enterprises. Summary of recommendations are given at the end of the report.

1.7 The Group analysed voluminous data, but incorporated in the report only the relevant areas at the appropriate places. The Group's recommendations on matters within the domain of Reserve Bank are presented in bold face.

Chapter II

Small-Scale Industry in India – A Profile

The small-scale industry occupies a unique position in the Indian economy due to its contribution to value addition, employment generation, and expansion of entrepreneurial base and diversification of the industrial sector.

2.1 Definition of small-scale industrial undertaking and Small Scale Business Enterprises

The Small Scale Sector owes its definition to the Industries (Development and Regulation) Act, 1951. Unlike most countries, which define small-scale industry in terms of employment levels, capital investment or turnover, in India the small-scale units are defined in terms of investment limits in plant and machinery. The definition of small-scale industries has undergone several changes over the years, in terms of investment limits. The investment limit in fixed assets was set at Rs. 5.0 lakh in 1950 with certain conditions on the number of persons employed. This definition was revised in a phased manner upwards. At present, a small scale industrial unit is an industrial undertaking in which the investment in fixed assets in plant and machinery, excluding land and building, whether held on ownership terms or on hire purchase, does not exceed Rs.100 lakh. The Government of India enhanced the investment limit of Rs.100 lakh for classification as SSI to Rs.500 lakh in respect of certain specified items under hosiery, hand tools, drugs and pharmaceuticals, stationery items and sports goods.

Food and agro-based processing units with investment in plant and machinery up to Rs.500 lakh were included under priority sector lending.
Small Scale units wherein investments in plant and machinery (excluding land and building) up to Rs.25 lakh are classified as tiny industries. All small-scale units, which export more than 50 per cent of their output, are classified as Export Oriented Units. Industry related service business enterprises with investment in fixed assets, excluding land and building up to Rs.10 lakh are registered under Small Scale Service Business Enterprises (SSSBEs).

2.2 Structure of small-scale industry

The small-scale sector structure may broadly be classified into “household enterprises (those establishments, which carry out their operations from their own residence)” and “non-household enterprises (all other establishments in the manufacturing sector)”. The household enterprises engage in the manufacture of a variety of products that include food products, beverages, tobacco products, cotton textiles, textile products, wood products, paper, leather, rubber, plastics, etc. The manufacturing sector may be classified into ‘registered’ and ‘unregistered’. Administratively, India's SSI is divided into seven industry groups - (1) handicrafts (2) handlooms (3) khadi, village and cottage industries (4) coir (5) sericulture (6) powerlooms and (7) residual small scale industries. The first five sub-sectors are collectively called the "traditional" sector whereas the last two are known as the "modern" sector. The small-scale industrial undertakings can also be classified into ancillary units, tiny units, export-oriented units and small-scale service business enterprises.

2.3 Role of small scale industry sector in Indian economy

2.3.1 In India, small-scale industry sector has remained high on the agenda of the Government since independence. The special thrust to this sector has been consistent with multiple objectives of employment generation, regional dispersal of industries and as a seedbed for entrepreneurship. The contribution of small-scale industries (SSIs) has been remarkable in the industrial development of the country. It has a share of over 40 per cent of the gross industrial value added in the economy. About 50 per cent of the total manufactured exports of the country are directly accounted for by the SSI sector. In terms of employment generated, this sector is next only to agriculture sector, employing approximately 283 lakh people. Today, the number of SSI units is estimated to be over 118 lakh in India. Being generally low capital intensive, the SSIs suit the Indian economic environment with scarce financial resources and large population base. In addition, it is highly labour intensive and has a scope for building upon the traditional skills and knowledge. The small-scale sector produces a wide range of products, from simple consumer goods to highly precision and sophisticated end products.

Some important indicators included in **Table 1** provide an idea about the precise role played by the SSI sector in India's economic development.

TABLE 1 : PERFORMANCE OF SSI SECTOR							
Year	**Units (No. lakh)**	**Production (Rs. Crore)**		**Employment (No. lakh)**	**Production per employee (Rs.000) at 1993-94 prices**	**SSI Exports**	
		At 1993-94 prices	**At current prices (2002-03)**			**Rs. crore**	**US $ million**
1990-91	67.9	68295	63518	158.3	43	9664	5386
1995-96	82.8	121649	148290	197.9	61	36470	10903
1996-97	86.2	135380	168413	205.9	66	39248	11056
1997-98	89.7	147824	189178	213.2	69	44442	11958
1998-99	93.4	159407	212901	220.6	72	48979	11642
1999-00	97.2	170709	234255	229.1	75	54200	12508
2000-01	101.1	184428	261289	239.1	77	69797	15278
2001-02	105.2	195613	282270	249.1	79	71244	14938
2002-03	109.5	210636	311993	260.1	81	86013	17773
2003-04P	114.0	228730	357733	271.4	83	.	.
2004-05P	118.53	245747*	399020	282.82	.	.	.

P Provisional.
*****: Based on the Growth rate of 7.44 per cent, which is the average growth of last year.
Note*: Data have been revised since 1990-91 on the basis of the findings of the Third All-India Census of SSI units.*
Source: Ministry of Small Scale Industries, Government of India.

2.3.2 The Government of India has been consciously developing policies and created a large public sector infrastructure to support the development of SSIs. The important elements of SSI promotion policies comprise features such as reservation of the items to be produced, preferential purchase of products, tax exemptions, provision of credit guarantee, subsidized support schemes, credit under priority sector lending from the banking system and a large network of public sector business and technical service providers. During the peak of protection granted to the SSI sector in the mid-1980s, about 900 products were reserved exclusively for SSI production. Protection policies have been essentially designed for small enterprises, whose products were targeted for the domestic market, while exporting and trading units have been exposed to competition. Support for the SSI sector, provided mainly through a large network of public sector agencies, is for entrepreneurship development, training, marketing, export, technology transfer and consultancy. Nodal implementing authorities have been continuously modulating the policy framework relating to SSI in tune with the developments in the sector. Besides providing credit facilities through the banking system and the term lending institutions, a variety of support measures and schemes have been conceived and made operational by the concerned authorities. Some of the recent important developments pertaining to the small-scale sector are briefly outlined below:

2.4 The structure of the small scale sector in India

2.4.1 Ministry of SSI, Government of India has conducted three all-India censuses so far to capture the developments taking place in the small-scale sector in India. The first and second censuses were conducted in 1972 and 1987 respectively. The third census was conducted during 2002-03 covering information up to 2001-02. For the purpose of the third census, the Indian SSI sector has been categorised into small-scale industrial undertakings (SSIs) and small scale service and business enterprises (SSSBEs).

2.4.2 Major findings of the Third Census

The total SSI sector (registered and unregistered units) comprises 1,05,21,190 units. About 55.0 per cent of these units were located in rural India. Over 44 lakh (42.26 per cent) in the total SSI sector were SSIs and the remaining 61 lakh (57.74 per cent) were SSSBEs. The number of ancillary units among SSIs at 1.32 lakh constituted 2.98 per cent of the total number of SSIs. Tiny units with original investment in plant & machinery up to Rs.25 lakh numbering 44.26 lakhs formed a dominating 99.5 per cent of the total number of SSIs. About 10.11 % of the SSI units were women enterprises.

2.4.3 In terms of State-wise spread, Uttar Pradesh (16.23 per cent), Andhra Pradesh (8.32 per cent), Maharashtra (7.64 per cent), Madhya

Pradesh (7.54 per cent) and Tamil Nadu (7.49 per cent) were the top five States having a total share of 47.22 per cent in terms of number of units.

2.4.4 About 44.0 per cent of the units were in the services sector, followed by 40.0 per cent of the units in manufacturing and allied activities sector and 16.0 per cent of units in repairing and maintenance sector. Thus, Services sector emerged as the dominant component in the total SSI Sector in the third census.

2.4.5 Although the registered SSI sector formed only 13.0 per cent, it contributed 72.0 per cent of the total production of the SSI sector.

2.4.6 Total output of the registered units in the year 2001-02 was estimated to be Rs. 70,861.73 crore.

2.4.7 The seven states, viz. Maharashtra (14.53 per cent), Uttar Pradesh (9.72 per cent), Punjab (9.21 per cent), Haryana (7.08 per cent), Andhra Pradesh (6.47 per cent), Punjab (7.67 per cent) and Tamil Nadu (6.47 per cent) together had a share of 53.48 per cent in the total gross output in the SSI Sector. While 89 per cent of the units had gross output of less than Rs. 10 lakh, large output units (with output more than Rs.1 crore) had a share of about 70 per cent of output. In terms of number of units, these units constitute a share of just 1.88 per cent. This indicates that there is a concentration of output in large units. A comparison of relevant data with earlier censuses reveals that the concentration of output in large units is increasing over years.

2.4.8 About 95.8 per cent of the units in the Total SSI Sector were found to be of proprietary type of ownership.

2.4.9 The SSI sector employed 2,49,32,763 persons during the reference period. The five States, viz., Uttar Pradesh (16.05 per cent), West Bengal (8.7 per cent), Andhra Pradesh (8.58 per cent), Maharashtra (8.23 per cent) and Tamil Nadu (8.09 per cent) had an aggregate share of 49.65 per cent in the total employment.

2.4.10 The fixed investment in the entire SSI Sector was estimated to be Rs.1,54,34,867 lakh. About 97 per cent of the units had a fixed investment up to Rs. 2 lakh and these units had a share of about 61.5 per cent in the total fixed investment in the sector. The six states, viz. Maharashtra (18.13 per cent), Uttar Pradesh (11.2 per cent), Andhra Pradesh (8.01 per cent), Punjab (7.67 per cent), Gujarat (7.15 per cent) and Tamil Nadu (7.12 per cent) together had a share of 59.28 per cent in the total fixed investment in the sector.

2.4.11 The total original value of investment in plant and machinery in the SSI Sector is estimated to be Rs.54,89,360 lakh. About 96 per cent of the units had the original investment in plant and machinery up to Rs. One lakh. The six states, Maharashtra (16.78 per cent), Uttar Pradesh (10.38 per cent), Andhra Pradesh (8.54 per cent), Tamil Nadu (8.45 per cent), Karnataka (6.35 per cent) and Gujarat (6.25 per cent) together had a share of 56.75 per cent in the total original value of investment in plant and machinery in the SSI Sector.

2.4.12 It was estimated that there were 50,606 exporting units accounting for exports to the tune of Rs.14,19,956 lakh. The registered SSI sector accounted for 87.0 per cent of the total SSI exports. The states like Madhya Pradesh, Uttar Pradesh, Jharkhand, Karnataka, West Bengal and Maharashtra together accounted for 55.4 per cent of the total exporting SSI units in the country. The states of Punjab, Tamil Nadu, Uttar Pradesh, Haryana, Maharashtra and Delhi together accounted for about 74.0 per cent of the total exports in the SSI sector.

2.5 Changing nature of the Small-Scale Sector in India

2.5.1 As compared to the second census, the third census brought out certain structural changes that have taken place in the 'registered' SSI sector. The percentage of working units to total units had declined from 62.75 per cent in second census to 60.77 per cent in third census. The percentage of working units in rural areas to total units had increased from 42.20 per cent in second census to 44.33 per cent in third census.

2.5.2 While the proportion of working units remained the same by and large, the domination of SSIs among the working units has been reduced considerably from 96 per cent to 66 per cent. This is mainly due to substantial increase in the number of units engaged in ‘services’ from 3.24 per cent to 34.45 per cent of total units.

2.5.3 The percentage of proprietorship working units to total SSI units had increased from 80.48 per cent in Second Census to 88.85 per cent in third census.

2.5.4 The per unit employment had gone down from 6.29 in second census to 4.48 in that of third census. This could be due to technological upgradation and advancement in the units.

2.5.5 The per unit production had substantially improved from Rs.7.38 lakh in second census to Rs.14.78 lakh in third census. The per unit fixed investment had gone up from Rs.1.60 lakh to 6.68 lakh. The per unit original investment in plant and machinery had also gone up from Rs. 0.95 lakh to 2.21 lakh.

2.5.6 Third census showed that the employment generated by the SSI sector per Rs. one lakh of investment was 1.62, as against only 0.20 in the manufacturing sector covered by the Annual survey of Industries. This means that the organized sector requires an investment of Rs.5 lakhs to generate employment to one person whereas the SSI sector generates employment for 8 persons with the same investment. With regard to investment-output ratio also, the SSI sector fared almost on par with the organized sector. An investment of about Rs.43,000 was required in the organized sector to generate an output worth Rs. one lakh, whereas in SSI sector, a marginally higher investment of Rs.48,000 would be required to generate the same amount of output. Thus, the above Census results highlight that the small-scale sector is evolving to be rural-oriented, self-employment-oriented, improving the technology and contributing to the development of services and exports.

2.6 Committees and Working Groups constituted by Reserve Bank

Recognizing the importance of the SSI sector, Reserve Bank had constituted several committees and working groups in the past to suggest measures for improving the credit flow to the sector. A gist of the major recommendations of these committees and working groups relating to flow of credit to the SSI sector are given hereunder:

2.6.1 Report of the Committee to Examine the Adequacy of Institutional Credit to SSI Sector and Related Aspects (Nayak Committee) (1992)

All the major recommendations of the Committee were accepted and the banks were advised, inter-alia, to:

i) give preference to village industries, tiny industries and other small-scale units in that order, while meeting the credit requirements of the small-scale sector;

ii) grant working capital credit limits to SSI units computed on the basis of minimum 20% of their estimated annual turnover whose credit limit in individual cases is up to Rs.2 crore [since raised to Rs.5 crore];

iii) prepare annual credit budget on the `bottom-up' basis to ensure that the legitimate requirements of SSI sector are met in full;

iv) extend 'Single Window Scheme' of SIDBI to all districts to meet the financial requirements (both working capital and term loan) of SSIs;

v) ensure that there are no delays in sanctioning and disbursal of credit. In case of rejection/curtailment of credit limit of the loan proposal, a reference to higher authorities should be made;

vi) not to insist on compulsory deposit as a `quid pro-quo' for sanctioning the credit;

vii) open specialized SSI bank branches or convert those branches, which have a fairly large number of SSI borrowal accounts, into specialized SSI branches;

viii) identify sick SSI units and take urgent action to put them on nursing programmes;

ix) standardize loan application forms for SSI borrowers; and

x) impart training to staff working at specialized branches to bring about attitudinal change in them.

2.6.2 Report of the High Level Committee on Credit to SSI (Kapur Committee, 1992)

The recommendations accepted and commended for implementation are as under:

i) delegation of more powers to branch managers to grant ad-hoc limits;

ii) simplification of loan application forms;

iii) freedom to banks to decide their own norms for assessment of credit requirements;

iv) opening of more specialized SSI branches;

v) enhancement in the limit for composite loans to Rs. 5 lakh. (Since enhanced to Rs.1 crore);

vi) strengthening the recovery mechanism;

vi) paying more attention to the backward states;

viii) conducting special programmes for training branch managers for appraising small projects;

ix) making customers grievance machinery more transparent and simplifying the procedures for handling complaints and monitoring thereof.

2.6.3 Report of the Working Group on Flow of Credit to SSI Sector (Ganguly Committee, 2004)

The following recommendations were commended to banks for implementation:

i) adoption of cluster based approach for financing SME sector;

ii) sponsoring specific projects as well as widely publicizing successful working models of NGOs by Lead Banks which service small and tiny industries and individual entrepreneurs;

iii) sanctioning of higher working capital limits by banks operating in the North East region to SSIs, based on their commercial judgement due to the peculiar situation of hilly terrain and frequent floods causing hindrance in the transportation system;

iv) exploring new instruments by banks for promoting rural industry and improving the flow of credit to rural artisans, rural industries and rural entrepreneurs, and

v) revision of tenure as also interest rate structure of deposits kept by foreign banks with SIDBI for their shortfall in priority sector lending.

2.7 Recent developments in the Indian SME sector

2.7.1 Setting up of National Commission on Enterprises

To address the concerns of the unorganized / informal sector enterprises, a four member National Commission on Enterprises in the Unorganized /Informal Sector was set up on September 21, 2004 under the Chairmanship of Dr. Arjun Sengupta. The mandate of the Commission is to examine the problems being faced by the enterprises in the unorganized / informal sector and to provide appropriate recommendations for technical, marketing and credit support to these enterprises. The Commission would function both as an advisory body and a watchdog for the informal sector.

2.7.2 Revamping of Khadi and Village Industries

For revamping the Khadi and Village Industries (KVI), the Government dissolved KVIC on October 14, 2004. The Ministry had set up a ten member Expert Committee (a) to review the existing structure, functioning and performance of the KVI since its inception (b) to review the KVIC Act, 1956, KVIC Rules, 1957 and the Regulation made thereunder (c) to recommend other measure(s) considered necessary by the Committee to revamp the KVI and (d) to launch new appropriate programmes/schemes.

2.7.3 Small Enterprises Development Bill

The Small Enterprises Development (SED) Bill has been approved by the Parliament. Enactment of this Bill is expected to remove the barriers to SSI growth by inculcating a hassle-free, user-friendly environment enabling SSI/MEs to diversify from the conventional product range to a broader contemporary product range. It will encourage exports and global integration and propel SSI/MEs towards the projected 12 per cent growth target. This would possibly help India to achieve its ambition of transforming into a global manufacturing hub, and a centre of excellence for small enterprise activities.

2.7.4 Credit Rating Scheme

A Credit Rating Scheme has been introduced to encourage the SSI units to get their credit rating done by the reputed credit rating agencies, with a view to facilitating credit flow to them and enhancing the comfort-level of the lending banks. The scheme, being implemented by the NSIC, envisages that 75 per cent of the cost of the credit rating exercise, with a maximum limit of Rs.40,000 per SSI unit, would be reimbursed to the SSI units availing of this one-time facility. Six credit rating agencies namely, CRISIL, ICRA, Dun and Bradstreet, Onicra, Care and Fitch which have agreed to credit rate SSI units through NSIC.

2.7.5 SME Fund

Looking to the credit needs of the SMEs in 1990, the Small Industries Development Bank of India (SIDBI) was launched to aid and finance small enterprises with a corpus of Rs.2500 crore. To further improve credit availability, a SME Fund of Rs.10,000 crore has been made operational under SIDBI from April 2004.

2.7.6 Improved Credit to SSI

In order to facilitate smooth flow of credit to SSIs, the composite loan limit that can be granted by banks to SSI entrepreneurs was increased from Rs. 50 lakh to Rs. 1 crore. Limits on collateral requirements have also been liberalized considerably.

2.7.7 Credit Cards

The Laghu Udyami Credit Card (LUCC) Scheme was liberalized by the Indian Banks' Association, enhancing the credit limit from Rs. 2 lakh to Rs. 10 lakh for borrowers who have a satisfactory track record.

2.7.8 SSI Clusters

Sixteen new industrial clusters were identified and taken up under Small Industries Development Programme during this year. These are:

Food Processing, Muzaffarpur, Bihar

Steel Re-rolling Mills, Raipur, Chhatisgarh

Agricultural Implements, Karnal, Haryana

General & Light Engineering, Parwanoo, Himachal Pradesh

Readymade Garments, Bangalore, Karnataka

Gold Ornaments, Thrissur, Kerala

Readymade garments, Indore, Madhya Pradesh

Brass & Bell metal, Khurda, Orissa

Agricultural Implements, Moga, Punjab

Ball Bearings, Jaipur, Rajasthan

Leather Footwear, Agra, Uttar Pradesh

Leather goods, Shantiniketan, Uttar Pradesh

Installation of Common Facility Centre in Brass/Bronze, Utensils, Manufacturing Cluster at Pareb, Bihar

Development of Whiteware Cluster at Khurja, U.P.

Development of Auto Parts Clusters at Phagwara, Jallandhar and Ludhiana

Development of Cane & Bamboo Cluster at Dimapur, Nagaland.

The development of these clusters is at various stages of implementation.

2.7.9 WTO and SMEs

Under the World Trade Organization (WTO) regime, new opportunities are being created for linkages among SMEs across the globe. The dismantling of the textile quotas has been received by the SMEs in India with great enthusiasm. Export of garments is a dominant characteristic of Indian SMEs. Other sectors, such as bio-tech, IT and IT-enabled services, footwear, etc. have shown a promising potential. Closer connectivity of India's large agricultural resources affords growing opportunities for new ventures. India's vast pool of talented and educated persons and low-cost labour can translate into possibilities for foreign collaborations.

2.7.10 Product Reservation Policy

The need to review the policy of exclusive product reservation for the SSI sector has been well recognized and the exclusive list is accordingly being pruned in a progressive manner. In the recent past the Government had de-reserved 85 items from the list of items reserved for manufacture by the small-scale industries. The Union Budget 2005-06 has further de-reserved 108 items from the exclusive list reserved for the SSIs. After the aforesaid announcement, the number of items reserved for exclusive manufacture in the small-scale sector as on March 28, 2005 stands at 506.

2.7.11 Promotional Schemes

Keeping in view the dynamic role played by the small scale sector in economic growth, employment creation and exports, the Government of India and concerned authorities have evolved a number of schemes and provided incentives and credit facilities. Details of these facilities, incentives, schemes and funds are furnished in Annexure II.

Chapter III

Repositioning of the SME sector - Select Issues in the Development and promotion of SME sector

Although several measures have been initiated to assist the SMEs, it is well recognized that the potential of the Indian small-scale sector has not been fully tapped. An illustrative list of issues cited by the representatives of the small sector affecting its growth is given below.

3.1 Non-credit Issues

(i) Infrastructure facilities

Availability of adequate infrastructure facilities i.e. power, road connectivity, transport facilities, energy, water, ports and airports are important to the robust performance of the small-scale sector. Poor quality of power and interruptions in the power supply often damage the plant and machinery/ equipment of the units. In order, therefore, to cater to various infrastructure requirements of the small sector, the Government has established State Industrial and Infrastructure Development Corporations (SIIDCs), Small Industries Development Corporations (SIDCs) and Housing and Urban Development Corporation (HUDCO). These state level organizations are catering to the infrastructure requirements in select areas of their respective states. However, the penetration of these organizations appears to be inadequate in terms of geographical coverage and number of units as the benefits of the infrastructure provided by these institutions is by and large accruing to the small units in the organized sector (registered units), which are only a fraction of the total number of small units. Therefore, there appears to be a need for an extended coverage of the operations of these institutions to ensure that the small units in unorganized sector too secure the necessary basic infrastructure facilities for their operations. State Electricity Boards need to take a fresh look at their approach to the supply of power to the small sector, in terms of providing uninterrupted and quality power. Facilitating public-private partnerships, attracting FDI into basic infrastructure as well as for establishment of industrial parks for small sector are the options already under consideration by relevant authorities. These need to be expedited. One solution to the infrastructure problem lies in increased emphasis on cluster development, which will factor into account the development of required infrastructure facilities in an organized manner for the cluster as a whole. Therefore, there is a need to strengthening of the National Cluster Development Programme and setting up of functional industrial parks.

(ii) Quality of human resources and skill formation

Improvements to skill formation and learning mechanisms in small sector have a substantial impact on productivity and value addition. In the context of facing both domestic and external competition, the quality of workforce is an important factor in the productivity of small sector. There is a conspicuous shortage of qualified workforce in the Indian small sector, which has to cater to the sub-contracting work of large technology-oriented corporations in the new economic environment. The responsibility of skill up-gradation and providing training to the labour force in small sector is vested with a network of institutions like Small Industries Development Organization (SIDO), Small Industries Service Institutes (SISIs), Technical Consultancy Organizations (TCOs), Process & Product Development Centres (PPDCs), District Industries Centres (DICs), Regional Testing Centres (RTCs), Central Footwear Training Institutes (CFTIs) and Tool Rooms. These Institutes are expected to provide training to labour force in better and improved technologies at a nominal fee. The coverage of the training provided by these institutions is mainly to the city-based and registered units. Here also, **if a cluster-based approach is adopted to impart training, the outcome would be more productive. These Institutes have to monitor both registered and unregistered units functioning under their jurisdiction, make a continuous evaluation of their training and skill requirements and accordingly, evolve programmes.**

The surveys conducted by Reserve Bank revealed that majority of the banks are arranging sensitization programme for their branch level officials.

(iii) Entrepreneurship development and managerial competency

Establishment of a small unit in India continues to be on the basis of an already existing family venture or a venture similar to the existing family unit, rather than experimenting with a novel business idea through innovation. The majority of SME owners in India manage the enterprises themselves, with few possessing the skills to draft medium to long-term business plans. The lack of managerial and technical know-how seriously inhibits innovative start-ups and business diversification. Conceiving new business ideas, making viability studies and market research, scanning the domestic and external markets are a part of the entrepreneurship development programmes. In the changed economic environment with customer seeking diverse and efficient products, the various institutions cited in the previous paragraph, which foster entrepreneurship development in small scale sector in India, need to redefine their roles in entrepreneurship development and provide a dynamic focus to their programmes. Strengthening National Entrepreneurship Development Board, devising comprehensive plan for promotion of rural entrepreneurship, fostering close linkages with premier institutions engaged in management and entrepreneurial training and adoption of “turn-key concept” for entrepreneurship training may be considered on priority basis. Surveys conducted by Reserve Bank revealed that very few banks have a system of arranging entrepreneurship development programme.

(iv) Supply of raw materials

The problem of obtaining steady supply of raw materials of desirable quality at reasonable prices is one issue cited by the small units. In order to obtain these inputs, SMEs have to compete with export markets, as well as with larger firms. Moreover, tariffs imposed on high quality imported inputs, as well as lengthy import procedures place the Indian small units in a less competitive position. The Planning Commission had quoted in Ninth Plan Document that in actual practice, the small sector tends to get more or less a 'residuary' treatment in raw material distribution. The problem of raw material availability has been among the important factors responsible for under-utilization of the capacities in the small industries sector. In recent times the prices of various inputs like steel, coking coal, oil are on increase and unless price stabilization mechanism is conceived, the small units may not be able to cope with the volatile prices of critical inputs. In order to overcome the difficulties with respect to availability of various raw materials, earlier the Industrial Policy Statement had envisaged introduction of a scheme for building up of a buffer stock of essential and scarce raw materials. It was envisaged that the existing set-up of National Small Industries Corporation at the Centre and the Small Industries Development Corporations at the State level would be utilized to facilitate raw materials supply. These Corporations would have to make a precise assessment of the present and future needs of raw materials of small-scale units on some realistic norms, and arrange for distribution particularly at the places of concentration of units. Though these measures were prescribed long ago, the small units continue to complain about inadequate supply of raw materials. Probably, **the schemes in operation in this regard need to be reviewed**.

(v) Technology upgradation

Majority of the small units continue to use traditional methods of production and old technology. Given their poor access to equipment, the Indian small units lack quality control and product standardization. This leads to a situation, where the small sector products are less competitive in the national and international markets. The task of technology upgradation of small sector has been entrusted to National Small Industries Corporation (NSIC), Small Industries Development Organization (SIDO), Small Industries Service Institutes (SISIs), Regional Testing Centres (RTCs) and various Process & Product Development Centres (PPDCs). The development of suitable tools and proto-types is being undertaken by Prototype Development Centres. The Sericulture Research Institutes and stations attempt improvement in practices in mulbery cultivation and silkworm rearing. Besides, a host of other organizations like the Council for Scientific and Industrial Research, Indian Council of Agricultural Research, Institutes of Handloom Technology, etc., are also involved in small sector research activities. However, effective translation of these research and development efforts is still to be achieved and consequently, the impact remains insignificant. Efforts would, therefore, need to be made to identify a focal point to coordinate the research and development activities of various research organizations and boards engaged in the field of small industries.

(vi) Marketing issues

The marketing problems of small industries in India flow from their scale of operation, lack of standardization, inadequate market intelligence, competition from large-scale units and insufficient holding capacity. A large number of small units continue to depend substantially on middlemen for marketing of their products. Most small units are confined to markets that are within their immediate proximity. Bulk of the small units' production is done on an order basis with a small proportion done on a continuous basis. Small units suffer from the absence of a competitive network of wholesalers and trading companies that could introduce their products into domestic and foreign market, and provide them with pertinent market information. The available marketing and distribution channels are Government owned. The National Small Industries Corporation, the Small Industries Development Organization, the Small Industries Service Institutes and SIDCs provide market intelligence and assistance to small entrepreneurs to some extent. It is necessary to evolve a well coordinated approach in the direction of demand forecasting, collection and collation of market intelligence to strengthen and expand internal marketing infrastructure with a view to making it small sector producer-oriented. In the field of government purchases there is need for identifying more items for exclusive purchase from the small scale sector and developing a system for close monitoring at different levels. The policy of price preferences to the products of small-scale units would need be continued. While firm-level strategies are fundamental to development of exports by small units, there is a need to have a centralized co-coordinating body that would provide a range of services including establishment of international subcontract exchanges, conducting studies on export potential, market intelligence, exchanging of trade delegations, participating in international trade fairs, etc.

(vii) Issues related to globalization and economic reforms

The small sector has been exposed to certain challenges in the wake of globalization process taking place worldwide. Competition has become increasingly fierce among the global and regional economies and enterprises, including small units. The impact of the agreements under WTO to which

India is a signatory brought in certain challenges to the small-scale sector. The main outcomes of WTO-stipulated requirements will be brought about through reduction in export subsidies, greater market access, removal of non-tariff barriers and reduction in tariffs. There will also be tighter patent laws through regulation of intellectual property rights under the TRIPS Agreement which lays down what is to be patented, for what duration and on what terms. Programmes to establish and strengthen linkages between MNCs and Indian small sector units through improved technology and quality upgradation are critical in this context. Similarly, a programme for FDI-Small sector linkage needs to be considered. Such a linkage calls for a comprehensive and complex set of reviews and policy adjustments. In both developed and developing countries there is mounting evidence that clustering and networking helps small enterprises to raise their competitiveness. Strengthening of bilateral and international cooperation for ensuring international cooperation and promoting joint ventures, sector specific development programmes with the assistance of UNIDO and UNDP would be beneficial. It is also beneficial to establish a SME trade hub with various international and multilateral organizations in the region.

3.2 Credit related issues

Without adequate finance, small units cannot acquire or absorb new technologies nor can they expand to compete in global markets or even strike business linkages with larger firms. However, the small-scale sector faces significant barriers in getting institutional and financial resources to meet their fixed and working capital needs. As per the third census of SSI, only 4.55% of the units (4,78,404 units) had outstanding loans as on March 31, 2002 with institutional sources. Consequently, they are forced to rely on retained earnings and financial support from family and friends to launch or expand their business. Even when debt financing is available to small-scale sector, maturities of the loans are often too short to allow the small-scale sector to finance sizable investments.

The surveys conducted by Reserve Bank revealed that majority of the bank branches are adhering to the time frame prescribed by Reserve Bank for disposal of loan proposals. They are also adopting simplified method of computation of working capital requirement of SSI units, based on minimum 20% of the projected annual turnover of the borrowing unit for limits up to Rs. 5 crore except in a few cases where banks are adopting MPBF or actual turnover. The surveys further revealed that as per perception of the bankers, the branch managers have been delegated adequate powers, for sanctioning different types of credit facilities to SSI borrowers.

From the perspective of banks and other financial intermediaries, the main barriers to small-scale sector lending are diverse, some of them are as follows:

(i) High-risk perception

High-risk perception with small-scale sector stems from a number of factors such as weak financial strength, inability to provide adequate collateral and other factors. Inability to properly appraise the new projects, new firms and new activities by bankers often results in banks shunning a small borrower.

(ii) Asymmetry of information

Asymmetric information about the business prospects of small-scale projects and financial standing of the small borrowers arises because small-scale borrowers generally do not have a well-documented credit history.

(iii) Insistence on collateral

As a result of asymmetric information and high-risk perception, banks primarily prefer collateral-based lending rather than cash-flow analysis while working with small-scale sector borrowers. Although there is a threshold up to which bankers should not insist on collateral, they seldom assume the risk involved in non-collateralized lending.

The surveys conducted by Reserve Bank revealed that many bank branches are insisting on collaterals even for loans up to Rs.5 lakh.

(iv) Moral hazard issues

Moral hazard problems are associated with the possibility of small-scale sector diverting funds to alternative projects or develop the propensity to take excessive risks.

(v) High transaction costs

Due to the small amounts of each loan, the aggregate costs of information gathering, due diligence, loan processing and monitoring are much higher than for loans to large corporate borrowers.

(vi) Interest rates

The financial institutions charge relatively higher interest rates to small-scale sector than to larger companies in order to compensate for the higher costs of information collection, the smaller volume of external financing and perceived greater credit risk.

(vii) Strengthening the provisions of "Interest on Delayed Payment to Small Scale and Ancillary Industrial Undertakings Act"

Though the "Interest on Delayed Payment to Small Scale and Ancillary Industrial Undertakings Act" was enacted in 1993 and further amended in 1998 to ensure prompt and timely receipt of payments by the small scale units from the large corporates, implementation of the provisions of the Act remains ineffective. Ministry of SSI, Government of India is proposing certain amendments in the provisions of the said Act. Under the proposed amendments, active role for State Governments in the implementation of the provisions of the Act and a proactive role for the Industry Facilitation Councils (IFCs) for settlement of disputes with the buyers in regard to delay in payment etc. have been envisaged.

(viii) Miscellaneous

Other reasons stated by banks for the weak growth of SME credit are (i) the large number of unregistered enterprises, which require different lending and risk management techniques, processes, and skills; (ii) lack of a secured transactions law to regulate assignment and registry of movables; and (iii) the difficulty and high cost of registering property and enforcing contracts.

The surveys conducted by Reserve Bank revealed that majority of the banks are not having any periodical meetings with local SSI/SME Associations to sort out credit related issues. Regarding delayed payments to SSI and ME by large corporates, no information is available with the bank branches. Some of the banks have suggested for relaxation in NPA norms for SSI sector and enhancement in limit for coverage under CGTSI scheme. During the survey some of the borrowers suggested for setting up monitoring cell at controlling offices of banks to monitor credit flow to the sector. They also suggested for reduction in guarantee fee under CGTSI scheme.

The issues confronted by the SME sector are indeed diverse, and credit related issues, no doubt, are significant. The multifarious problems of the SME sector call for an integrated and multi-pronged approach from all concerned with the SME sector's development.

3.3 Current structure for provision of credit to small-scale sector

The entire network of the Indian banking sector extends credit to the small-scale sector. In addition, specialized financial institutions for industrial development have been established at the national and state levels with almost overlapping functions. For the small-scale units, the 'Small Industries Development Bank of India' (SIDBI) was set up in 1991. In the recent past, it has instituted special schemes for direct financing through its regional level branch network. One of the schemes introduced by SIDBI that has been particularly helpful in case of ancillaries and subcontracting with large firms is the 'Bill Discounting Scheme'. In general, majority of the schemes of SIDBI relate to small-scale sector. 'State Finance Corporations' (SFCs) and 'State Industrial Development Corporations' (SIDCs) have been set up at state level to primarily cater to the long term credit needs of the small and medium scale units and to participate in the venture through equity stake. These units get refinancing from SIDBI for the approved schemes and also generate their own funds through the state government and from the market borrowings as well.

These institutions are an important source of long-term credit, and of late SIDBI and SFCs have started providing funds for working capital as well. In line with the commercial banks, SFCs have remained a source of credit for small-scale sector in general.

The Indian banking system provided over 11 per cent of its overall net lending to SSIs in the recent years. While the aggregate SSI loan portfolio increased by 10 per cent during 2003-04, it grew far below the 16.9 per cent annual growth of net bank credit during the same period. (**Table 3**).

Table 3: Credit to SSI Sector by PSU Banks

Year	**Net Bank Credit (Rs. in cr.)**	**Credit To SSI (Rs. in cr.)**	**Share of SSI (%)**	**Growth Rate (%)**	
				NBC	**SSI**
Mar-95	169038	25,843	15.29	20.0	19.9
Mar-96	184,381	29,485	15.99	9.1	14.1
Mar-97	189,684	31,542	16.60	2.9	7.0
Mar-98	218,219	38,109	17.50	15.0	20.8
Mar-99	265,554	42,591	17.33	21.7	11.8
Mar-00	316,427	46,045	15.60	19.2	8.1
Mar-01	341,291	48,400	14.20	7.9	5.1
Mar-02	396,954	49,743	12.50	16.3	2.8
Mar-03	477,899	52,988	11.10	20.4	6.5
Mar-04	558,849	58,278	11.10	16.9	10.0

Source: *Report of the Trend and Progress of Banking in India (Various Issues)*

Chapter IV

Review of Reserve Bank's guidelines regarding financing of SSI Sector

4.1 Issues relating to definition of SME

4.4.1 Definition of SME

The Group suggests that current SSI/tiny definition may continue. Units with investment in plant and machinery in excess of SSI limit and up to Rs.10 crore may be treated as Medium Enterprises (ME). However, for the purpose of priority sector, the advances to SSI sector as per current definition alone may be considered. The definition may be reviewed after enactment of the Small and Medium Enterprises Development Bill.

4.4.2 Mandatory Lending Targets, Shortfall and SIDBI

Considering the importance of the SSI sector, lending to this sector was accorded priority sector status. Foreign banks were required to achieve with effect from July 1, 1993 a target of 10% of net bank credit (NBC) in respect of advances to SSI. In the event of foreign banks not attaining the target for priority sector lending, they have to make good the shortfall in the achievement of target by depositing an amount equivalent to the shortfall with SIDBI at a rate of interest inversely proportional to the percentage of deficit. Domestic banks do not have any such stipulations, but they were advised in June 2003 to fix self-set targets for lending to the SSI Sector. In order to ensure that credit is available to all segments of the SSI sector, banks were also advised to ensure that at least–

a. forty per cent of the total credit to small scale industry goes to the cottage industries, khadi & village industries, artisans and tiny industries with investment in plant and machinery up to Rs. 5 lakh;

b. twenty per cent of the total credit to small scale industry goes to SSI units with investment in plant and machinery between Rs. 5 lakh and Rs. 25 lakh; and

c. the balance of credit goes to other SSI units with investment exceeding Rs. 25 lakh.

The Group feels that domestic banks may continue to fix targets for themselves for disbursement to SSI Sector during the year. However, they may so fix the targets as to reflect a higher disbursement over the immediately preceding year. Similarly, banks may also set targets for themselves for financing of Medium Enterprises. In order to avoid crowding out effect the existing sub-targets of 40% and 20% to the tiny and small sectors may continue.

4.4.2 Institutional Arrangements.

The present institutional structure for policy formulation, disbursement and monitoring of the flow of credit to SSI Sector is as under:

Standing Advisory Committee on Flow of Credit to SSI sector is the highest forum under the aegis of the Reserve Bank for critically reviewing the flow of institutional credit to SSI sector. The Deputy Governor of Reserve Bank chairs the Committee and the Executive Director, Reserve Bank, Development Commissioner & Additional Secretary, Ministry of SSI, Government of India, Joint Secretary,
Ministry of ARI, Government of India, eminent bankers, representatives of SSI Associations, SIDBI, NABARD, KVIC and SFC are members of this forum.

Reserve Bank had earlier advised all scheduled commercial banks except RRBs to set up cells at important regional centres, beside the cell at Head Office, to deal with the sector and man them with expert staff including technical personnel. Banks were also advised to open at least one Specialized SSI branch in each district. Further banks were permitted to categorize their general banking branches having 60% or more of their advances to SSI sector as specialized SSI branches for providing better service to this sector. Banks were advised to put in place a machinery at the regional offices to entertain complaints from the borrowers regarding their service to SSI customers and to verify periodically that Reserve Bank guidelines are implemented by the branches in actual practice. The names and addresses of the officer with whom complaints are to be lodged were also to be displayed on the notice board of every branch.

The existing institutional arrangements for review of credit to SSI sector like the Standing Advisory Committee, cells at the bank head office level and at important regional centres may continue. However, they may review flow of credit to SME sector.

At the Regional offices of the Reserve Bank, empowered committees may be constituted with the Regional Director of the Reserve Bank as the Chairman and the SLBC Convenor, senior level officers from two banks having predominant share in SME financing in the state, representative of SIDBI Regional Office, the Director of Industries of the State Government, one or two senior level representatives from the SME/SSI Associations in the state, and a senior level officer from SFC/SIDC as members. The Committee will meet periodically and review the progress in SME financing. It will also coordinate with other banks/financial institutions and the state government in removing bottlenecks, if any, to ensure smooth flow of credit to the sector. The committees may decide the need to have similar committees at cluster/district levels.

The Group further suggests that banks may open specialized SME branches in identified clusters / centres with preponderance of Medium Enterprises to enable the SME entrepreneurs to have easy access to the bank credit and to equip bank personnel to develop requisite expertise. The existing specialised SSI branches may be redesignated as SME branches. Though the core competence of these SME branches will be utilized for extending finance and other services to SME sector, they will have operational flexibility to extend finance/render other services to other sectors/borrowers. Boards of banks may review the progress in achieving the self-set targets as also rehabilitation and restructuring of SME accounts on a quarterly basis to ensure that the required emphasis at the highest forum of the banks is given to this sector. The banks may, therefore, compile statistics of SME financing on a quarterly basis. Existing reporting formats/returns may be amended suitably for reporting progress in financing to tiny, SSI and medium enterprises.

At the branch level, a nodal officer may be designated to help the SME entrepreneurs in complying with the bank's formalities and his name may prominently be displayed.

4.4.3 Dissemination of guidelines

Representatives of Association felt that instructions relating to SSI financing do not percolate to the branch managers. But bank representatives were of the view that generally all Reserve Bank instructions are received at bank branches within a maximum period of one month.

The Group suggests that for wider dissemination of and easy accessibility to policy guidelines formulated by Boards of banks as well as instructions/guidelines issued by Reserve Bank, they may be placed on a centralized web-site.

4.4.4. Development of Human Resources

SSI Associations observed that banks are not sympathetic to the SSI entrepreneurs and also do not have the expertise to appraise their projects. They, therefore, felt the need for a change in the mind-set of bankers. Bankers also felt that due to staff attrition there is a need for training the staff in SME financing.

It is suggested that banks may evolve appropriate training modules to bring about attitudinal changes and to develop skills of their staff. They may also consider appropriate incentives to branch managers for financing the SME sector. SIDBI also offered technical appraisal services to banks, if required.
SIDBI is also in the process of forming a credit rating agency along with six public sector banks viz Bank of Baroda, Bank of India, Canara Bank, Oriental Bank of Commerce, Punjab National Bank, Union Bank of India and leading credit agencies. This is expected to be operationalized very soon. **Banks can avail of their services and enhance the quality of SME accounts.**

4.4.5 Capacity building of borrowers

The entrepreneurs who venture into the SME sector may not have the necessary expertise to comply with bank's procedures and formalities, and requisite financial discipline.

Banks may, in association with Associations, SISI etc., consider training the identified entrepreneur-borrowers in developing skills in pricing, marketing and accounting besides acquainting them with bank procedures and formalities so as to enable banks to sanction, disburse and monitor loans expeditiously and effectively.

4.4.6 Procedural Issues

The Group recommends that Boards of banks may be empowered to frame a transparent policy of their own in regard to SME financing. While formulating this policy the Board may, inter alia, cover the following aspects:

i) limits up to which collateral free loans can be extended by banks, taking into account the availability of guarantee facility under Credit Guarantee Trust for Small Industries for collateral- free loans up to an amount of Rs 25 Lakh (it should, however, be ensured that this limit is not less than Rs 5 lakh);

ii) limits up to which composite loans can be granted towards working capital and term loan requirements through a 'Single Window' to avoid the necessity of units approaching term lending institutions;

iii) determining the basis for assessment of the credit requirements of the SSI and ME towards working capital

and term loans to ensure that adequate finance is available for the SME borrowers;

iv) prescribing the time limits within which the loan applications shall be disposed off;

v) specifying the limits up to which the officers at different levels can sanction loans to facilitate quick disposal of the loan applications; and

vi) prescribing charges for different services, keeping in view the need to service small entrepreneurs.

All the representatives of the SSI associations and banks felt that the Reserve Bank's instructions are highly supportive of the sector and hence need no amendment or withdrawal. The only suggestion the banks had given was to withdraw the instructions relating to the composite loan limit of Rs. 1 crore and to empower the banks to decide such limits. The Group recommends withdrawing the instructions contained in six circulars of the Bank indicated in the Appendix to this chapter (A few more circulars will stand withdrawn/amended if the Group's recommendations relating to restructuring/rehabilitation of sick SME accounts are accepted). It is expected that the policies formulated by banks will be more liberal than the existing policies. Till the Boards formulate their policies, the Reserve Bank guidelines will continue to be applicable to them.

4.4.7 Income Recognition and Asset Classification norms

Reserve Bank introduced norms for income recognition, asset classification and provisioning for non-performing assets (NPA) as part of prudential framework for banks in 1992-93. No relaxation is granted for SSI advances.

There have been requests from SSI Associations to take a lenient view in this regard. Bankers also felt that NPA norms in respect of agro-processing units may be similar to that of agricultural advances.

As no direct link can be established between agricultural production and the functioning of agro-processing units and their cash flows, and taking into account the need for uniformity in approach **no relaxation is proposed by the Group, except to the extent suggested in case of restructuring of SME accounts.**

Appendix

Extant Reserve Bank Guidelines

- Banks have been advised to extend collateral free loans up to Rs.5 lakh to all SSI borrowers. Banks have further been advised to increase the exemption limit for obtention of collateral security for all SSI borrowal accounts up to Rs.25 lakh, based on good track record and financial position of the units, with the approval of their Board of Directors (Ref. RPCD.PLNFS.BC.No.39/06.02.80/2003-04 dated November 3, 2003 read with RPCD. PLNFS.BC.No.58/06.02.80/2001-02 dated January 23, 2002)
- Banks have been advised to enhance the composite loan limit from Rs.50 lakh to Rs. 1 crore in order to enable the SSI entrepreneur to avail of the their working capital and term loan requirement through "Single Window" (Ref. RPCD.PLNFS.BC.No.42/06.02.31 /2004-05 dated October 26, 2004)
- Banks have been advised to adopt the method of computation of working capital requirement of SSI units, on the basis of simplified method of minimum 20% of the projected annual turnover of the borrowing unit for limits up to Rs. 5 crore (Ref. RPCD.PLNFS.No.61/06.02.28(i)/2001-02 dated July 13, 2001)
- Time Schedule for Disposal of Loan Applications: Up to Rs.25000/: within 2 weeks and up to Rs.5 lakh: 4 weeks (Ref. RPCD.PLNFS.BC.No.24/06.02.77/2002-03 dated October 4, 2002)
- No service charges/inspection charges should be levied on priority sector loans up to Rs. 25,000/-. Loans above these limits, banks are free to charge service charges.(Ref.RPCD.PLNFS.BC.No.53 /04.09.01/2002-03 dated October 20, 2002)

Chapter V

Restructuring of the borrowal accounts of SMEs

5.1 Introduction

Considering the numerous problems and challenges being faced by the SME sector, including those arising out of globalization, and existence of a large number of sick but potentially viable SME units, there is a need to explore ways and means to reposition the SME sector through a formal restructuring process. While policies and measures have already been put in place for restructuring the loan accounts of large corporate borrowers, no such mechanism has been conceived to restructure the accounts of SMEs.

5.2 Frame-work for restructuring

It is observed from the Third Census of SSI sector that out of the estimated 1,05,21,190 units in the SSI sector, over 44 lakh units (42.26%) are small scale units, while the remaining 61 lakh (57.74%) are SSSBEs. The number of ancillary units among the SSI is 2.98%. The tiny units with original investment in plant and machinery up to Rs.25 lakh constituted a dominant 99.5% of the SSI units. It is also observed that 88.85% of the registered SSI units are proprietory units. About 7.21% of the units are run by partnerships, while private companies managed 2.42% of the units. The rest are owned by either co-operatives or trusts. In view of the foregoing, **the Group recommends that a simplified restructuring mechanism, covering all SSI units, irrespective of their constitution may be instituted as follows:**

i) **The revised restructuring mechanism will be applicable to all SME units, excepting corporate SME having aggregate credit limits of Rs.10 crore or more under multiple/consortium banking arrangements,**

ii) As the SSI units are not likely to have consortium or multiple banking borrowings, it is proposed to leave the matter regarding formulation of rehabilitation/debt restructuring policies in respect of SMEs having credit limits from a single bank to the banks concerned with the approval of their Board of directors. It is expected that the policies

formulated by banks will be simple to comprehend and more liberal than the existing policies.

iii) In case of corporate borrowers in SME sector having credit limits of up to Rs.10 crore under multiple banking arrangements as also non-corporate borrowers having any credit limits under multiple banking arrangements, the bank with the maximum share in the limits, in association with the bank having second largest share may work out restructuring packages, provided the units are potentially viable.

iv) The restructuring may be done suo motu by the bank or on receipt of a request to that effect from the borrowing units.

v) All accounts except those classified as 'loss assets' will be eligible for restructuring.

5.3 Viability criteria

The Boards of banks may decide on the acceptable viability benchmarks in such a way that the restructured amount together with interest thereon is recovered over a period of 7-10 years.

5.4 Time frame

While the bank should decide upon the eligibility of the unit and work out a restructuring package within a maximum period of 60 days, the sanctioned package should be implemented within a period of 30 days thereafter. The Boards of banks may consider fixing shorter time frame depending upon level of expertise within the bank.

5.5 Prudential Norms

The existing prudential norms continue to be applicable excepting to the extent of relaxations recommended hereunder:

a) A rescheduling of the instalments of principal alone, would not cause a standard/substandard asset to be classified in the downgraded category (i.e. sub-standard/doubtful), provided the loan/credit facility is fully secured. However, the condition of tangible security will not be applicable in cases of loans up to Rs.5 lakh.

b) A rescheduling of the instalments of principal alone, would render a sub-standard asset eligible to be continued in the sub-standard category for the specified period, provided the loan/credit facility is fully secured. However, the condition of tangible security will not be applicable for loans up to Rs.5 lakh.

In these cases, satisfactory performance of the accounts for one year of restructuring may be the criterion.

5.6 Effect of repeated restructuring

The freezing of asset classification of standard, sub-standard and doubtful assets for one year after restructuring, as indicated above, will be applicable only when the account is restructured for the first time. This is necessary to dissuade repeated restructuring.

5.7 Restructuring of accounts of corporate SME units with multiple banking arrangements

The Special Group to Review Corporate Debt Restructuring (CDR) Mechanism (Chairperson: Smt. S. Gopinath) has recommended that the revised CDR Mechanism may be made applicable to corporate borrowers with credit limits of Rs.10 crore or more with multiple banking arrangements. Hence **this Group recommends that restructuring of accounts of corporate SSI/ME borrowers having credit limits aggregating Rs.10 crore or more under multiple banking arrangements may be covered under the revised CDR mechanism.**

Chapter VI

Review of Reserve Bank's guidelines on nursing sick SSIs

Several internal and external factors affect the performance of the SSIs, resulting in a number of them becoming sick. Of late, the incidence of sickness in SSI sector is showing an increasing trend and a large number of SSI units, identified as sick, were also not found potentially viable.

As per findings of third census on SSI, out of the 4,78,404 units having loans outstanding with institutional sources like banks and financial institutions, about 19.6 per cent units in the registered SSI sector and 16.61 per cent units in the unregistered SSI sector were sick. In the total SSI sector, this percentage was 17.8. Sickness in the total SSI sector was of the order of 1 per cent, whereas in the registered and unregistered SSI sectors it was 3.38 per cent and 0.64 per cent respectively. The maximum number of sick units (59.53%) were located in West Bengal, Kerala, Maharashtra, Karnataka and Andhra Pradesh.

Combining the three yardsticks used to measure sickness, as recommended by the Kohli Committee viz., (a) delay in repayment of loan for over one year, (b) decline in net worth by 50 per cent, and (c) decline in output in last three years, about 13.98 per cent of the units in the registered SSI sector were identified to be either sick or incipient sick, while this percentage was only 6.89 in the case of unregistered units. In the entire SSI sector, this percentage was 7.82.

Incipient sickness identified in terms of continuous decline in gross output was 11.5 per cent in the registered SSI sector and 6.48 per cent in the unregistered SSI sector. In the total SSI sector, this percentage was 7.4 per cent.

6.2 Causes for Sickness: Many internal and external causes have been attributed to sickness in SSI sector. The major among the internal causes are limited financial sources, lack of organizational, financial and managerial skills and expertise. The external factors are non-availability of reliable uninterrupted power supply, shortage of raw materials, marketing difficulties, delayed and inadequate credit, labour problems, globalisation and liberalization of the economy, obsolete technology, inadequate infrastructure, etc. In most of the cases sickness is not confined to any single reason but a combination of different causes. According to the third census of Small Scale Industries , “lack of demand” and “shortage of working capital” were the main reasons for sickness/incipient sickness in both the registered and unregistered SSI sectors. Nearly 46% SSI units were found sick on account of “shortage of working capital”.

6.3 Magnitude of sickness

The following table gives the data on the number of accounts of units identified as sick by scheduled commercial banks:

Year	**No. of A/cs**	**Amt. o/s (Rs. in Cr.)**
1999	306221	4313.48
2000	304235	4608.43
2001	249630	4505.54
2002	177336	4818.92
2003	167980	5706.35
2004*	143369	5779.54

*Provisional

The above figures do not reveal the actual status of sickness since this includes only those units, which have obtained credit facilities from banks. Of the 143369 accounts as on March 31, 2004, only 2407 units were identified as potentially viable. Out of these 2407 units only 729 units were placed under nursing programme.

6.4 RBI Guidelines in dealing with sick SSI units

6.4.1 On the basis of Working Group on Rehabilitation of Sick SSI constituted under the chairmanship of Shri S.S.Kohli, RBI issued detailed guidelines to banks in January 2002 detailing, inter alia, steps to identify sick units, incipient sickness, viability norms, reliefs and concessions, etc., as enumerated below:

6.4.2 Definition of Sick SSI unit: A unit is considered as sick when any of the borrowal accounts of the unit remains substandard for more than 6 months or there is erosion in the net worth due to accumulated cash losses to the extent of 50% of its net worth during the previous accounting year and the unit has been in commercial production for at least two years.

6.4.3 Identification of incipient sickness: Banks can identify incipient sickness by taking into account any one or more of the following factors:

a) Continuous irregularities in cash credit/overdraft accounts such as inability to maintain stipulated margin on continuous basis or drawings frequently exceeding sanctioned limits, periodical interest remaining unrealized;

b) Outstanding balance in cash credit account remaining continuously at the maximum;

c) Failure to make timely payment of instalments of principal and interest on term loans;

d) Complaints from suppliers of raw materials, water, power, etc. about non-payment of bills;

e) Non-submission or undue delay in submission or submission of incorrect stock statements and other control statements;

f) Attempts to divert sale proceeds through accounts with other banks;

g) Downward trend in credit summations;

h) Frequent return of cheques or bills;

i) Steep decline in production figures;

j) Downward trends in sales and fall in profits;

k) Rising level of inventories, which may include large proportion of slow or non-moving items;

l) Larger and longer outstandings in bill accounts;

m) Longer period of credit allowed on sale documents negotiated through the bank and frequent return by the customers of the same as also allowing large discount on sales;

n) Failure to pay statutory liabilities;

o) Utilization of funds for purposes other than running the units.

p) Not furnishing the required information/data on operations in time.

q) Unreasonable/wide variations in sales/receivables levels vis-à-vis level of operations of the unit.

r) Non- cooperation for stock inspections, etc.

s) Delay in meeting commitments towards payment of instalments due, crystallized liabilities under LC/BGs, etc.

6.4.4 Viability of Sick SSI Units

Viability norms are decided on the basis of time taken to repay the structured debt and ability to function without the help of concessions after that period.

A unit may be regarded as potentially viable if it would be in a position, after implementing a relief package spread over a period not exceeding five years from the commencement of the package from banks, financial institutions, Government (Central / State) and other concerned agencies, as may be necessary, to continue to service its repayment obligations as agreed upon including those forming part of the package, without the help of the concessions after the aforesaid period. The repayment period for restructured (past) debts should not exceed seven years from the date of implementation of the package. In the case of tiny/decentralized sector units, the period of reliefs/concessions and repayment period of restructured debts should not exceed five and seven years respectively.

6.4.5 Time for deciding on viability and rehabilitation of sick SSI units: Viability of a unit identified as sick, should be decided quickly and made known to the unit and others concerned at the earliest. The rehabilitation package should be fully implemented within six months from the date the unit is declared as 'potentially viable' / 'viable'. While identifying and implementing the rehabilitation package, banks/financial institutions are advised to do ‘holding operation' for a period of six months. This will allow small-scale units to draw funds from the cash credit account at least to the extent of their deposit of sale proceeds during the period of such ‘holding operation'.

6.4.6 Broad Parameters of relief and concessions

The following are broad parameters for grant of relief and concessions for revival of potentially viable sick SSI units:

9Interest on Working Capital	1.5% below the prevailing fixed / prime lending rate, wherever applicable
Funded Interest Term Loan	Interest Free
Working Capital Term Loan	1.5% below the prevailing fixed / prime lending rate, wherever applicable
Term Loan	Concessions to be given not more than 2 % (not more than 3 % in the case of tiny / decentralised sector units) below the document rate.
Contingency Loan Assistance	The Concessional rate allowed for Working Capital Assistance

Relief / concessions detailed above are only indicative. It is for the banks / financial institutions to decide on the nature and extent of concessions necessary / warranted, depending upon the merits of each case. The banks have been given freedom for extension of relief / concessions even beyond the parameters, in cases where it is considered absolutely necessary.

6.5 In order to provide relief expeditiously to the potentially viable sick units, **the Group recommends that**

i) All the accounts of sick units may be restructured on the lines of proposed debt restructuring mechanism for SME sector;

ii) Extant guidelines on definition of a sick SSI unit may continue. All other instructions relating to viability and parameters for relief and concessions to be provided to sick SSI units, as prescribed by Reserve Bank may be withdrawn and banks may be given freedom to lay down their own guidelines with the approval of the Board of Directors. While formulating their guidelines, banks may consider the indicative guidelines suggested by the Working Group on Rehabilitation of Sick SSI Units (Chairman: Shri S.S.Kohli).

iii) As per the extant guidelines, a unit is considered as sick when any of the borrowal accounts of the unit remains sub-standard for more than six months. The banks may consider restructuring accounts of units having financial problems even if the account has remained sub-standard for six months or less.

iv) It is expected that the policies formulated by banks in respect of (ii) and (iii) above will be more liberal than the existing policies.

v) Every attempt may be made by banks to implement the rehabilitation package in respect of the accounts of sick units at the earliest. In any case, it may not exceed a period of 3 months from the date of bank deciding suo motu to reconstruct the accounts or date of receipt of request to that effect from the borrowing unit concerned.

6.7 State Level Inter-Institutional Committee

6.7.1 The **State Level Inter-Institutional Committee (**SLIIC) mechanism was initially set up in 1979 at all Regional Offices of RBI. Taking into consideration various suggestions received from certain State Governments and Ministry of SSI, Government of India, DBOD had issued detailed guidelines on March 26, 1981 on the constitution of SLIIC. As per above guidelines, the Secretary (Industries) of the concerned state government would be the Chairman of the Committee and Director, SISI, representatives of SFC, SIDC, IDBI and 3-4 banks with majority presence as members. Reserve Bank is the convenor. The major function of the forum was to monitor/review cases of rehabilitation of sick SSI units. It also provides a useful forum for interaction between state government officials and state level institutions on the hand, and term lending institutions and banks on the other hand. A sub-committee of SLIIC has also been set up wherein the borrowers and concerned banks discussed the issues of rehabilitation.

6.7.2 Since the empowered committees to be constituted with the Regional Director of Reserve Bank as the Chairman, will also look into coordination issues between different agencies and banks, and in the light of above facts and committee's recommendations relating to restructuring the accounts of sick SSI/ME, the future role of SLIIC may be reviewed.

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Annexure I

Recent Developments in Small and Medium Enterprises Sector – A Cross-country Perspective

1. Role of SMEs in an economy

Small and Medium Enterprises (SMEs) perform multiple functions for the society and economy of a country. SMEs in many countries account for an overwhelming number of business establishments and employees, and the sector is a major player in a country's economic activity. The SME labour market performs a stabilizing function in society. SMEs provide employment opportunities to many people, including unskilled labour, thereby distributing income from a macroeconomic perspective. SMEs are considered as a source of dynamism in market-oriented economic structure since the rate of entry and exit of small firms is generally high. Economic development, including the upgrading of industrial structure is achieved through a dynamic process of replacing inefficient enterprises with highly efficient enterprises. SMEs contribute immensely to exports and provide outsourced products and services. By supplying parts and components required by export-oriented assemblers, SMEs help to increase economic efficiency. Lastly, SMEs are key players in the regional economy.

2. Cross-country perspectives

Considering the vital role played by the SMEs in economic development, both developed and developing economies provide a host of incentives and financial and non-financial support them to ensure the smooth functioning of the sector. These facilities, incentives and special schemes broadly consist of providing financial support and promoting venture capital, offering consulting solutions, receivables financing, setting up of small business incubators, leasing finance, extending soft loans, grants, and government guarantees for entry into public tenders, setting up of special state-owned financing companies, providing interest subsidy schemes, creation of business angel networks (wealthy individuals who finance SMEs), promoting micro-finance programmes, extending tax concessions, etc.

The system of financing the small units differs from country to country. The North American financial systems are centered on stock markets where firms have better access to external equity financing. At the other end, the Continental Europe has a long tradition in loan financing due to the bank centered financing system. Increased competition in financial markets in developed countries, led banks and other financial institutions to launch a number of initiatives to serve financing needs of SMEs effectively. These include reducing information asymmetry of small units and high risks by using credit scoring systems (an automated statistical method to assess the risk of default of a credit applicant), reducing costs of lending by applying latest information technologies and improving financial services for small units.

New Zealand has introduced a scheme called ‘BIZ Investment Ready’ which aims at innovative businesses and entrepreneurs seeking funds to expand, diversify or commercialize a new concept. It helps businesses and entrepreneurs to develop a greater understanding of the issues around funding and can provide assistance to seek and secure private investment of up to NZD 5 million. European Union has devised a scheme to facilitate the contacts between SMEs and banks and other financial institutions, by making a beginning to develop a ‘code of good practice’. Philippines has instituted a financing programme called SME Force (SME Financing for Organizationally Competent and Excellent Franchise Businesses), which is a franchise development financing facility that will be implemented with the participation of the franchisers' organizations. Coupled with the captains of industry, this programme seeks to develop backward and forward linkages among and between leading businesses and SMEs in the domestic economy.

3. Venture capital funds

Various countries have promoted the venture capital investment for meeting the financing needs of SMEs. To widen the scope of venture investments, newer agents have been allowed to take part in venture financing. Japan has a framework for issuing bonds to family and friends to mitigate financing constraints faced by micro-enterprises and start-ups. Some local governments in Japan are providing support for enterprises issuing privately placed bonds for a small number of investors. Japan also used public funds to establish three Small and Medium Business Investment Consultation Co. Ltd. in 1963 to support the SMEs. Another innovative method to encourage commercial banks to provide loans to micro-enterprises can be found in Chile. The Chilean Social Investment Fund (CSIF), created in 1993, uses a market-based subsidy to induce banks to provide micro finance. In several countries, venture capital provides an important link between innovation and finance, providing capital market access to small innovative firms. Pension funds account for the largest source of Venture Capital Funds (VCFs) in the United States. Korea enacted the *Special Measures Law* in 1997 for promoting Venture Businesses by liberalizing provisions for venture capital investments by institutions, including banks and pension funds. The Korean government takes a more direct approach to alleviate the perceived funding gap of the sector by extending direct funding and provision of guarantees to strengthen the domestic venture capital industry. The presence of institutional investments in venture capital markets in Israel is barely visible because of strict restrictions on local institutions' investments in venture capital markets. Although the US venture capital market developed largely without government assistance, the government had established the Small Business Investment Company (SBIC) programme in 1958 to stimulate the development of the venture capital industry. SBICs are privately owned and managed investment firms, which have access to loan financing, called "leverage", by issuing debentures, which are guaranteed by the US Small Business Administration (SBA). A Loan Guarantee Programme, known as 7 A programme, was established to provide guarantees that will facilitate lending to small business which are unable to secure financing on reasonable terms through normal lending channels. The German BTU-scheme provides a number of lessons for countries interested in developing a national venture capital market. The BTU-refinancing scheme offers long term loans to investors combined with a partial default guarantee.

The pension funds in Finland have emerged as important sources of funds to SMEs. To attract prospective informal investors in venture funds, the Ministry of Economic Affairs of Netherlands, sponsors various road shows. UK has taken lead in promoting regional venture capital funds (RVCFs). There will be at least one RVCF in each of the nine English regions specializing in the provision of small-scale equity (less than GBP 500,000) on a strictly commercial basis to SME businesses with growth potential. The aim of RVCFs is to provide SMEs with growth potential, access to risk finance at the right time.

4. Loan guarantee schemes

Countries such as USA, France, etc. have set up 'guarantee funds', which are partly/fully financed by the State, in order to enable them to share part of the risk related to granting of credit by banks. In 2001, Mexico created a National Guarantee System that promotes collaboration between financial institutions and local Governments. In Canada a *Small Business Loans Act* (SBLA) programme was launched to fill the debt-financing gap for SMEs. The UK Small Firms Loan Guarantee Scheme (SFLG) was also devised to address a perceived market failure in SME financing by targeting viable business propositions that lack an established track record or collateral.

A unique two-tier structure of credit supplementation for SMEs exists in Japan. The Credit Guarantee Corporations (CGCs) provide financial institutions with credit guarantees on the repayment of SME loans. In return, SMEs pay guarantee fees to CGCs to secure credit guarantees. The Japan Small and Medium Enterprise Corporation (JASMEC) insures these guarantees on payment of insurance premiums by CGCs.

5. Tax incentives

Traditionally, a number of countries have granted direct tax incentives to promote venture capital. Canada has one of the most generous venture capital tax incentives, where investments in venture capital funds receive tax credits and qualify for tax deductions under the *Registered Retirement Savings Plan* (RRSP) rules. The United Kingdom provides tax relief to individuals or business angels who invest in ordinary shares of qualifying companies through the *Enterprise Investment Scheme* (EIS). The *Venture Capital Trust* (VCT) scheme in the United Kingdom also offers tax incentives to individuals investing in pooled investment funds, known as VCTs, which invest in unquoted companies. The capital gains tax concessions in the venture capital industry has also been recognized as an important policy incentive. Chinese Taipei's 1983 legislation allowed up to 20 per cent tax deduction for individuals investing in qualified VCFs. This was also extended to corporate investors in 1991. It has been recognized that these tax incentives have had a positive impact on the growth of venture capital industry in Chinese Taipei. Israel’s recent tax incentives exempt foreign investors from capital gains tax on investments in local VCFs and in high technology start-ups.

6. Other incentives

Many OECD countries have introduced special SME provisions in export credit systems to encourage small exporters. These include information programmes, simplified application procedures, special export insurance and guarantees.

Details of various types of financing facilities, incentives and special schemes in operation in different countries and availability or otherwise of similar facility in India are listed out in the *Appendix*.

Appendix to Annexure I

SME FINANCING - INTERNATIONAL EXPERIENCES AND STATUS IN INDIA

Facilities/Schemes for SSI sector **A. FINANCING AND OTHER FACILITIES TO SMES**	**Country**	**Status in India (For a detailed description of various facilities in India please refer to Annex II)**	**Comments**
(1) DEVELOPMENT FINANCING AGENCY FOR SMES			
➢ The Business Development Bank of Canada (BDC) is a crown corporation, which is fully dedicated to filling the marketplace gaps by providing financial and consulting solutions. BDC is a complimentary source of SME financing.	**Canada**	SIDBI, established on April 2, 1990, is the principal Development Financial Institution for promotion, financing and development of industries in the small-scale sector and coordinating the functions of other institutions engaged in similar activities. The activities of SIDBI, as they have evolved over the period of time, now meet almost all the requirements of small scale industries which fall into a wide spectrum constituting modern and technologically superior units at one end and traditional units at the other.	Currently, there are a wide variety of institutions, which are providing various services to the small-scale sector. There appears to be no need for any new specialized institution to serve the small-scale sector at this juncture. What is required is a reassessment of the roles played by various institutions and adoption of a more focused approach towards the development of the small sector.
➢ The Japan Finance Corporation for Small Business supplies the long-term capital to develop SME businesses and offers SMEs long-term, fixed-interest, low-interest capital.	Japan		
➢ To facilitate SME access to bank loans, Korea established the Industrial Bank, which awards the bulk of its lending to SMEs. The SME Promotion Fund provides funds for restructuring projects to business start-ups and to SMEs less than three years old.	**Korea**		
➢ Development Bank of the Philippines (DBP) provides wholesale credit through Industrial Support Services Expansion Program (ISSEP). Through Industrial Guarantee and Loan Fund (IGLF), it provides credit supplementation support through the extension of guarantee schemes to stimulate the flow of credit to SMEs.	**Philippines**		
➢ The *ICO-PYME* (Official Credit Institute-SME) facility is meant to provide financing, under preferential conditions, for investment projects undertaken by SMEs in Spain.	**Spain**		

➢ Financial and advisory supports are provided through the newly established SME Development Bank. It provides various services to the SMEs in the economy, including debt financing, equity financing, SME counseling, or diversification of loan products and other financial services.	**Thailand**		

(2) VARIOUS FINANCING PROGRAMMES

➢ **CBFSA** programme has been extended in the form of a five year pilot project to capital leases called the **Capital Leasing Pilot Project**, which gives the SMEs an additional financing option, thereby serving the needs of smaller and younger firms, which were earlier, underserved.	**Canada**	Although lease finance is provided by NBFCs and banks, no separate leasing related schemes are operating in India. ***Composite Loan Scheme*** for equipment and/or working capital up to a limit of Rs. 1 crore. ***The SME Fund*** of Rs. 10,000 crore was operationalised by the SIDBI in April 2004 to, inter alia, address the problem of inadequacy of financial resources at highly competitive rates for SSI sector. **Scheme of Micro Finance Programme**: Micro-credit programme works through NGOs/SHGs. Micro-credit programmes are run primarily by NABARD in the field of agriculture and SIDBI in the field of Industry, Service and Business (ISB). Under the programme,	Currently, a variety of schemes including Priority Sector lending, Single Window Scheme, Composite Loan Scheme, Credit Guarantee Fund (Scheme), Credit Linked Capital Subsidy Scheme for Technology Upgradation, National Equity Fund Scheme, Equipment Finance Scheme, Micro Credit Scheme, Laghu Udyami Credit Card Scheme, etc., have already been put in place by the Government over years. What is desirable at this juncture is a review of these schemes to fine-tune them.
➢ The ***MARKET Programme*** awards assistance to SMEs by way of subsidized interest rates and grants for certification costs. ➢ The ***SMALL LOANS Programme*** was introduced for 2001-2004 with the aim to promote the development of small enterprises through access to the necessary capital.	**Czech Republic**		
➢ ***Danish Growth Fund (DGF***) has undertaken to expand investments to innovative SMEs by converting its DKK 2 billion bond holdings, in line with market developments, into equity or quasi-equity investments. Consequently, DGF has discontinued the provision of soft loans, marking a switch to a more commercial investment approach.	**Denmark**		

➢ In 2000, a new financing programme to promote the growth of micro-enterprises, **Pikara**, was launched, having been developed by Finnvera (specialized state owned financing company) in co-operation with Ministry of Trade and Industry, the Employment and Economic Development Centres and the entrepreneurs' organizations. Pikara is a financing programme set up to promote the growth of micro-enterprises.	**Finland**		

➢ Start-ups and existing companies are being assisted by programmes of two assistance banks – ***Deutsche Ausgleichs bank*** **and** ***Kreditanstalt für Wiederaufbau*** – which in 2001 gave more than EUR 10 billion to fund loans granted to SMEs. ➢ The introduction of the so-called ***start-up funding programme***, which was established for the special purpose of covering the capital needs of smaller start-ups (up to EUR 50 000) and gives borrowers' banks an 80% release from liability, has proved to be particularly helpful for start-up entrepreneurs. To help start-up entrepreneurs and SMEs gain access to bank loans, loan guarantees have also been made available as the security normally required by banks.	**Germany**	Rs. 191 crore has been sanctioned up to December 31, 2003, benefiting over 9 lakh beneficiaries. The Budgetary provision for the scheme in the Tenth Five Year Plan is Rs. 7 crore and the provision in the current financial year 2003-04 is Rs. 0.25 crore. ***Equipment Finance Scheme*:** Acquisition of machinery/ equipment including Diesel Generator Sets, which are not related to any specific project. ***Micro Credit Sc*heme** meets the requirement of well managed Voluntary Agencies that are in existence for at least 5 years, have a good track record and have established network and experience in small savings-cum-credit programmes with Self Help Groups (SHGs) individuals. ***Credit Linked Capital Subsidy Scheme for Technology Upgradation*** was approved in September 2000, wherein 12 per cent back ended capital subsidy would be admissible on loans advanced to SSI by the Scheduled Commercial Banks, designated SFCs for technology upgradation in certain sub sectors. ***Laghu Udyami Credit Card (LUCC) Scheme*** launched by Public Sector Banks for providing simplified & borrower friendly Credit facilities to SSI, tiny enterprises retail traders & artisans.	
➢ The Government raised the amount of micro credit issued by the ***Hungarian Foundation for Enterprise Promotion (HFEP)*** with the assistance of local entrepreneurial agencies. Since October 2001, the loan ceiling stands at HUF 6 million. ➢ To promote regional development, especially in some underprivileged areas, regional micro-loans are issued by the HFEP, co-financed by the European Phare resources. The loan conditions are the same as those of the Micro-Credit Programme.	**Hungary**		

National Equity Fund Scheme - the project cost limit of Rs. 50 lakhs. The soft loan limit retained at 25 per cent of the project cost subject to a maximum of Rs. 10 lakhs per project. Assistance under the NEF will be provided at a service charge of 5 per cent per annum.

➢ **Small Business Guarantee Fund Corporation** (SBGFC) has the following financing programmes: ➢ ***SME Force*** - SME Financing for Organizationally competent and Excellent Franchise Businesses is a franchise development financing facility that will be implemented with the participation of the franchisers' organizations. Coupled with the Captains of Industry, it will be used as a strategy to develop backward and forward linkages among and between leading businesses and SMEs in the domestic economy. ➢ ***FIRST LIGHT*** - A financing program for the best business ideas that will contribute to the development of the five priority industries. ➢ ***GUIDE*** - Guarantee Incubation for DTI Endorsed Enterprises is a P100 million direct lending facility of the Small Business Guarantee and Finance Corporation (SBGFC). ➢ ***Small Enterprise Financing Facility (SEFF)*** was established to supplement the financial system's resources for SME development financing. Under the SEFF, accredited financial institutions (AFIs), which are in need of funds for SME financing may approach the SBGFC and apply for accreditation as lending conduits. ➢ ***Rediscounting Facility for Small Enterprise Loans*** is a credit window where accredited financial institutions (AFIs) may negotiate their eligible SME loans/credit instruments with BGFC. ➢ ***Transactional Direct Financing Facility*** is a stopgap program, which immediately addresses the credit needs of SMEs, particularly in the export sector. ➢ ***Window III*** - the centerpiece of DBP's retail lending operations. It finances innovative and socially desirable projects with high developmental impact. Funds to Non-Government Organizations (NGOs) for re-lending to eligible micro-enterprises. ➢ ***Export Assistance Network*** (EXPONET) serves as a trade facilitation office that provides real and immediate assistance to existing and potential exporters.	**Philippines**		

➢ As part of the search for new financing instruments for SMEs, ENISA *(Empress Nacional de Innovación, S.A)*, a shell company of the Directorate General of SME Policy, has been developing participatory loans since 1997. A participatory loan is a financing instrument that is halfway between venture capital and a traditional loan.	**Spain**		
➢ The establishment of the ***Thailand Recovery Fund*** and the ***Fund for Venture Capital Investment in SMEs***, which form part of the equity investment measures as well as the restructuring of the Small Industry Credit Guarantee Corporation and the Small Industry Finance Corporation form part of the measures to improve SME financing.	**Thailand**		
➢ The ***UK High Technology Fund*** (UKHTF) was developed to encourage institutional investment in predominantly early stage high technology venture capital funds, and to increase the finance available for investment into technology-focused businesses. Managed by a professional fund manager, Westport Private Equity, the Fund was established on a "fund of funds" basis. This means it will not invest directly into small businesses but will invest in existing venture capital funds that have experience in early stage technology investments.	**UK**		
➢ The Micro-loan Program aims to increase the availability of very small loans to prospective small-business borrowers. The 504 ***Certified Development Company (CDC) Program*** provides growing businesses with long-term, fixed rate financing for major fixed assets, such as land and buildings. ***The Disaster Loan Program*** offers financial assistance to those who are trying to rebuild their homes and businesses in the aftermath of a disaster.	**USA**		

(3) OTHER FINANCING FACILITIES			
➢ Soft loans are granted for both investment and operations and guarantees for revolving loans have been provided, which also cover loans to refinance previous operational loans.	**Czech Republic**	Credit facilities for working capital and term loans are available from both banking sector and financial institutions. Please see Annex II for details in this regard.	
➢ Monies destined for interest subsidies to craft enterprises are gradually being transferred to micro-enterprises: the guarantees required of entrepreneurs are thus limited, and their principal place of residence is often protected.	**France**		
➢ The German Government supports start-up entrepreneurs and SMEs with a set of financing-assistance instruments tailored to their needs.	**Germany**		
➢ Finance measures provided to enterprises by development agencies in Ireland include, financial and capital measures (capital grants, feasibility studies, rent subsidies, seed capital, marketing grant, loan guarantees), labour-related measures (including employment grants, training grants, management development grant etc.) and technological and innovation support (technology transfer). ➢ Ireland's new Regional Development Growth Strategy puts strong emphasis on the creation of new business incubators to house high-potential start-ups. Funding of over EUR 2.5 million is being provided for the development of campus incubators and 46 new community enterprise centres are being built to complement the 70 which currently exist.	**Ireland**		
➢ **With a view to complementing the role of private-sector financial institutions, the Government financial institutions are doing what they can to ensure smooth access to capital for SMEs.** ➢ The ***Shoko Chukin Bank*** is a full-service financial institution with funds not only from the Government but also from SME co-operatives and other organizations that serve the co-operatives, their members, and other clients. ➢ The ***National Life Finance Corporation*** offers primarily small, unsecured loans for very small companies.	**Japan**		

➢ The Korean Government is focusing on the improvement of direct financing for SMEs. ➢ Where venture capital was provided by way of loans in the past, now SMEs receive financing in the form of investment. The investment-to-loan ratio of venture capital has surged from 1.1 in 1997 to 35.4 in 2001. ➢ Top-ranking small companies with high growth and profit performance are listed on the Kosdaq secondary capital market for direct financing. ➢ For micro-businesses not eligible for bank loans, the SMBA plans to raise about KRW 5-6 trillion in policy funds, which are used by micro-businesses in making facilities investments. ➢ A financial safety net is being established to help small businesses overcome the financing shortage stemming from temporary decreases in sales and management risks.	**Korea**		
➢ The Ministry of Economy encourages collaborative agreements with international financial institutions to support enterprise development and strengthen the production capacity of SMEs.	**Mexico**		
➢ BIZ Investment Ready is a scheme aimed at innovative businesses and entrepreneurs seeking funds to expand, diversify or commercialise a new concept. It helps businesses and entrepreneurs to develop a greater understanding of the issues around funding and can provide assistance to seek and secure private investment of up to NZD 5 million. No direct funding is provided to businesses.	**New Zealand**		

➢ Apart from bank loans, SMEs also avail themselves of support instruments such as leasing, guarantees, sureties and factoring. Another options available to these companies are venture capital funds, although these are geared more to firms with high growth potential. Loans are granted by banks and various institutions such as regional development agencies, micro-loan institutions, saving and loan coops, loan funds and others. ➢ The Government's SME policy envisages various actions to increase SME access to external sources of finance: bank loans and credits, credit guarantee funds, leasing, and venture capital funds. A lease agreement was included in the Civil Code and the Investment Funds Bill was amended, foreseeing the opening of specialised closed investment funds whose operations are similar to those of venture capital funds. ➢ In January 2001, changes to the Public Securities Trading Law came into effect, making it easier for enterprises to be listed on regulated and non-regulated securities markets. To improve entrepreneur familiarity with the capital market, a national information and education campaign aimed at SMEs and regional institutions was started in 2000. ➢ The Government implements schemes for various types of loans and preferential credits. SMEs that create employment for ex-employees of restructuring industrial sectors and farmers can avail of low interest loans.	**Poland**		
➢ In light of the difficulties faced by SMEs in finding financing suited to their needs in terms of cost and time, the Government's policy has been geared, first of all, to easing access to existing sources of financing (by reducing costs, extending terms and providing guarantees) and secondly, to promoting new financing facilities and instruments. ➢ Loans are granted through banks and savings banks and they are available to SMEs for investment in fixed assets, whether tangible or intangible, with a financing ceiling of 70% of the net investment project. ➢ In 2001, special attention was given to micro-loans, such as loans backed without requiring supplementary counter-guarantees. These loans are granted to very small enterprises.	**Spain**		
➢ The Government has devised a set of measures to encourage private investment, to improve financing for SMEs.	**Thailand**		

➢ The UK Government is working to improve relationships between banks and small businesses and to enhance access to financing through setting up business angel networks and providing tax relief to investors in smaller companies through the Enterprise Investment Scheme and Venture Capital Trusts. ➢ Finance markets provide billions of GBP for SMEs, but not all needs are being met to the same extent. It is acknowledged that there is an equity gap at the lower end of the market. The Government's intervention is designed to be the minimum necessary to stimulate private sector investors to provide small-scale risk finance for SMEs with growth potential. ➢ The Government has been working with the main banks and others since 1998 to bring the informal investment market to full operation in order that business angels can become a mainstream source of finance for SMEs. Together, they jointly support the National Business Angels Network (NBAN) in England, launched in 1999 and designed to act as a resource for the whole industry, operating as a national conduit through which any company seeking investment can be put in touch with investors.	**UK**		
➢ While many small businesses are self-financed or borrow from friends and relatives, those that enter financial markets typically turn to commercial banks. Banks are leading suppliers of credit to small businesses, accounting for 54 per cent of total traditional small firm credit used, according to the 1993 National Survey of Small Business Finances. ➢ In addition, Small Business Administration has a large number of loan and loan guarantee programmes to assist small business in their financing needs.	**USA**		

➢ The overall issue of access to finance is dealt with in the framework of the Financial Services Action Plan, which aims at removing any unnecessary administrative or legal barriers to the raising of capital on a cross-border basis. ➢ The European Commission also has a number of different measures to facilitate SMEs' access to financing. These measures are targeted at all the stages of the business cycle. They include improving the access to seed financing, support of increasingly specialised venture capital funds, and measures to facilitate SMEs' relations with the banking sector. ➢ On seed capital, the aim is to stimulate the supply of capital for the creation of innovative new businesses. Support is provided to seed funds, incubators and similar organizations. The objective is to support the long-term recruitment of additional investment managers, thereby reinforcing the capacity of the venture capital industry to cater for investments in seed capital. ➢ To facilitate the contacts between SMEs and banks and other financial institutions, the European Union has recently begun to develop a code of good practice.	**European Commissi on**		

B. GUARANTEE PROGRAMMES			
➢ Government enacted Canada Small Business Financing Act **(CSFBA**) on April 1999, which facilitates access to debt financing to increase the availability for small businesses. Under the scheme, the Govt. partially guarantees loans to most of the small business units with an annual gross revenue of less than CAD 5 million. The Govt. compensates up to 85 per cent of the sanctioned amount to the Banks and FIs, in case of default.	**Canada**	**Credit Guarantee Scheme**: The Government approved Credit Guarantee Fund Scheme for Small Industries in May, 2000 with the objective of making available credit to SSI units, particularly tiny units, for loans up to Rs. 10 lakhs without collateral/third party guarantees. The Credit Guarantee Trust Fund for Small Industries (CGTSI) set-up by Government of India and SIDBI is operating this Scheme. The Scheme has been operationalised with effect from 1st January 2001. Subsequently, the Government decided to increase the eligibility limit of loans to be guaranteed from Rs. 10 lakhs to Rs. 25 lakhs. Necessary modifications have been carried out in the indenture of the Trust to enable CGTSI to guarantee loans up to Rs. 25 lakhs and to provide for counter guarantees to other institutions.	
➢ The main support instruments applied in the field of access to capital are guarantees for bank credits and leasing, guarantees for capital entry, low-interest loans, reimbursable grants, interest rate subsidies, and subsidies towards the costs of implementing certification systems. ➢ Under the GUARANTEE Programme, SMEs can apply for a subsidized loan or a leasing guarantee for viable projects – both investment and operational loans can be assisted. ➢ A new instrument used since 2001 to support SMEs is a guarantee for entry into public tenders and for certification of products.	**Czech Republic**		
➢ In a move to achieve a forward-looking, integrated approach to public support for SMEs' access to finance, several initiatives have been set up within the realm of the Danish Growth Fund (DGF), a Government-funded investment fund. A loan guarantee scheme, managed by DGF and backed by the European Investment Fund, has boosted bank lending to SMEs.	**Denmark**		
➢ In view of the bank's reluctance to support such enterprises, in particular as regards their creation, transfer or development projects, the focus has been on guarantee mechanisms enabling enterprises to have easier access to credit by facilitating risk-taking by banks.	**France**		
➢ **Sofaris** (a French company which guarantees the funding of SMEs) facilitates SMEs' access to financing, by guaranteeing the loans, and in certain cases equity capital, allocated to them by different financial institutions. Sofaris administers guarantee funds, financed essentially by the state, in order to assume part of the risk related to the granting of credit as well as equity funding (25% of the annual budget) to SMEs. This system, based on close co-operation with banks and venture-capital agencies, is an important tool in the Government's industrial policy.	**France**		
➢ The Credit Guarantee Corporation plays an active role in the implementation of the Government's programme to promote SME development and improve SME competitiveness. The programme features are being simplified, resulting in faster and simpler evaluation, and greatly reduced guarantee fees.	**Hungary**		

➢ **The credit complementation system helps speed up financing for SMEs as the Credit Guarantee Association acts as guarantor for SMEs without sufficient credit or collateral when, for example, the same firm borrows capital from a bank or other financial institution and the Japan Small and Medium Enterprise Corporation then backs these guarantees.**	**Japan**		
➢ The SME Credit Guarantee Scheme provides guarantees for bank loans through the Korea Credit Guarantee Fund (KCGF) and the Korea Technology Credit Guarantee Fund (KTCGF). The KCGF has provided over KRW 30 trillion in loan guarantees to export-oriented and knowledge-based SMEs. The KTCGF targets high-technology firms. ➢ The Science and Technology Fund (STF) aimed to invest KRW 50 billion in 2001 in technology-intensive start-ups. The Korea Technology Credit Guarantee Fund (KTCGF) provides (up to 100%) guarantees on venture capital investments.	**Korea**		
➢ The Ministry of Economy, in co-ordination with local Governments and development and commercial banks, encourages SMEs to seek risk capital, provides guarantee funds to allow SMEs access to loans, and fosters the establishment of non-banking intermediaries. It is Government policy to create, adapt, and/or consolidate programmes that facilitates the access of micro, and SMEs to financing. ➢ In 2001, the National Guarantee System was created that promotes collaboration between financial institutions and local Governments.	Mexico		
➢ Guarantee Program was designed to encourage financial institutions to lend to SMEs by providing a guarantee cover of up to a maximum of 90 per cent on the loans of qualified entrepreneurs. Such a scheme is aimed at increasing the flow of funds from the formal lending institutions to the SME sector, especially those without collateral. The guarantee works as a collateral substitute or as a collateral supplement.	Philippines		

➢ Amendments to the Law on Guarantees and Sureties Granted by the State Treasury and certain legal entities include, expanding the scope of sureties given from the *Bank Gospodarstwa Krajowego* (BGK) Credit Guarantee Fund and the introduction of new instruments that will allow the BGK to financially support regional and local guarantee institutions. ➢ A Government priority is the development of loan guarantees involving advisory services and co-financing of local and regional credit guarantee funds.	Poland		
➢ The Spanish guarantee system comprises Mutual Guarantee Companies (SGRs), whose corporate object is to provide guarantees to lending entities for the loans requested by SMEs, and also comprises the public refinancing company, CERSA *(Compañía Española de Refianzamiento, S.A.)* which shares the risk in the loans that are granted. CERSA is a company with a majority of state capital, under the aegis of the Directorate General of SME Policy, and collaborates with SMEs to solve financial difficulties they experience for financing innovation projects. Special attention is paid to small enterprises and to recently created businesses. Refinancing is granted to SGRs by means of an agreement establishing different percentage coverage according to the characteristics of the SME and of the assets financed by means of the guarantee operations.	Spain		
➢ The *Cautionnement des arts et métiers* is a credit guarantee system aimed primarily at traditional SMEs. It involves a network with a central office and ten independent regional co-operatives linked by co-operation agreements. Credit guarantees (up to CHF 150 000) are provided by the regional co-operatives. In cases where higher credit is needed, the regional co-operative can apply to the central office for a further CHF 300 000 (CHF 500 000 in mountainous areas). The Government covers 50% to 60% of losses (90% in mountainous areas).	Switzerland		
➢ *The Small Firms Loan Guarantee Scheme (SFLGS)* was created in 1981 to facilitate the supply of finance to small firms with viable projects but which are unable to obtain conventional finance because of lack of assets to offer as security against a loan or overdraft.	UK		
➢ The 7A Loan Guarantee Program was established to provide guarantees that will facilitate lending to small business unable to secure financing on reasonable terms through normal lending channels. In terms of US Government small business lending in 2001, private commercial lenders using the Small Business Administration loan guarantee made almost 43 000 loans worth nearly USD 10 billion.	USA		

C. VENTURE CAPITAL

➢ Australian Government to encourage VC has allowed exemption on capital gains for VC investments made by non-resident pension funds from select countries. Access to VC is also offered through Innovation Investment Fund, which provides VC to assist small companies in early stage of development.	**Australia**	**Venture Capital Scheme**: The objective of this scheme is to encourage SSI ventures/sub-contracting units to acquire capital equipment, as also requisite technology for building up of export capabilities/import substitution including cost of total quality management and acquisition of ISO-9000 certification and for expansion of capacity. A Venture Capital Scheme was launched by SIDBI in October 1992 and a separate VC fund with an initial corpus of Rs.10 crore was set up for the purpose. Till date SIDBI has committed an aggregate contribution of Rs. 433.09 crore to 24 Venture Capital Funds.	It needs to be acknowledged that the current situation in India in providing venture capital needs a comprehensive look to encourage the venture capital funding activity.
➢ The Business Development Bank of Canada (BDC) invested CAD 114 million of venture capital in 71 investments.	Canada		
➢ Equity guarantees to venture capital companies were launched in 1994. The Government has supported the creation of a viable, commercial market for subordinated debt used for active financing of SMEs. By funding part of a feasibility analysis, the Government similarly helped pave the way for a second-tier marketplace for trading shares in SMEs.	**Denmark**		
➢ There are large private venture investments, mainly by pension funds. The actual number of new venture-backed companies, which amounted to more than 300 in 2000, also emphasizes the expansion of venture capital in Finland. Forty venture capital firms are active, including both privately and publicly funded companies. ➢ The public actors – SITRA (The Finnish National Fund for Research and Development), TESI (Finnish Industry Investment) and regional authorities – have joint owner interests in different venture capital firms. SITRA co-invests in 20 domestic venture capital funds with ten related management companies and is involved in 13 technology transfer companies. TESI is a co-investor in nine regional venture capital firms. These patterns illustrate the public sector involvement in the Finnish venture capital industry. Regarding the venture capital firms' preferred investment stages, one-third of the investments are made in the seed capital segment.	**Finland**		
➢ In the field of risk capital, the German Government makes available, in considerable volumes, venture capital for young technology companies especially via the VTC – Venture Capital for Small Technology Companies. The funds are provided either as direct co-investment via the *Deutsch Ausgleichsbank*'s technology venture capital fund association or as venture capital via the venture capital donors refinanced by the *Kreditanstalt für Wiederaufbau*. Through this programme, over EUR 500 million in risk capital was mobilised in 2000 for some 1000 young companies.	**Germany**		
➢ The Irish venture capital market continues to show strong growth ensuring critical support for the development and expansion of Irish business. Enterprise Ireland has also established a database of more than 70 high "net worth" individuals, or business angels", with over EUR 12.7 million available to invest in SMEs.	**Ireland**		

➢ In 2001, the SME Promotion Fund established a special venture capital company, the Dasan Venture, with KRW 50 billion in funds. The Dasan Venture identifies promising start-ups in early stage and provides them with seed money as well as management knowhow, under close co-operation with business incubating centres across the country. ➢ The Cultural Industry Promotion Fund (CIPF) and the Film Promotion Fund (FPF) also support limited partnerships, providing venture capital mainly for start-ups in digital content and film sector projects. In 2001, CIPF planned to invest KRW 10 billion in digital content projects, and the FPF planned to invest KRW 10 billion in film projects.	**Korea**		
➢ Increase the scope for raising venture capital by increasing the budget for the SME Credit Guarantee Scheme (BBMKB): Two important initiatives are: ➢ *Angel Road shows*, which involve the organization of ten regional meetings for innovative entrepreneurs and informal investors. The Ministry of Economic Affairs sponsors the road shows. ➢ *7th Heaven* comprises 20 meetings organised by the Nebib and several other parties, such as Biopartner (Ministry of Economic Affairs Life Science Initiative), Dreamstart (platform for technological starters) and Syntens. These meetings are not directly sponsored.	**Netherlands**		
➢ The New Zealand Venture Investment Fund (VIF) is an intervention aimed at stimulating investment at the seed and early stages of the business life cycle. These funds will have certain restrictions around how they can invest, to push more equity investment toward earlier stages of the business life cycle.	**New Zealand**		
➢ The law on venture capital companies was passed in May 2000, which aims to promote business creation by facilitating access to venture capital. It provides tax reliefs to venture capital companies and private investors (business angels).	**Switzerland**		
➢ The regional venture capital funds (RVCFs) are being set up to address a national market weakness in risk capital provision for investment within the equity gap. There will be at least one RVCF in each of the nine English regions specializing in the provision of small-scale equity (less than GBP 500 000) on a strictly commercial basis to SME businesses with growth potential. The aim of RVCFs is to provide SMEs with growth potential, access to risk finance at the right time.	**UK**		
➢ The National Venture Capital Association, a non-Governmental organization, estimates that the value of venture capital financing zoomed from USD 20 billion to USD 100 billion between 1998 and 2000. One source of venture capital is made available exclusively to small businesses through private companies licensed by SBA. Called Small Business Investment Companies, these take investment positions in small business.	**USA**		
➢ The ETF Start-up Scheme is also targeted at innovative SMEs and the availability of risk capital for start-up and early-stage phases. The EIF invests on equal terms with other equity investors in specialized venture capital funds. The focus is on smaller or newly established funds. These specialized funds tend to be operating at a regional level, focusing on specific industries or technologies and aimed at financing the exploitation of R&D results.	**European Commission**		

D. FISCAL CONCESSIONS			
➢ Australian Government provides an annual funding of AUD 5 million to assist the establishment and maintenance of *small business incubators (SBUs)*, which assists new and growing businesses get established. Under the scheme, 90 SBUs were funded throughout Australia. ➢ Reduction in Personal and company income tax Capital gains tax exemptions and fuel Excise reductions for small businesses.	Australia	Excise ceiling for SSI exemption based on turnover raised from Rs.3 crore per year to Rs.4 crore per year. Income-tax exemption was granted to the income of the Credit Guarantee Fund Trust for Small Industries for 5 years. Provision for "Promotion of SSI Schemes" enhanced to Rs.173 crore in 2005-06; The corpus fund set up under the Credit Guarantee Fund Scheme has been raised to Rs. 200 crore.	The small sector has been provided with preferential treatment in terms of reservation of products and preferential purchase arrangements. The Union Budget 2005-06 has announced certain fiscal concessions to the small sector (see Annex II). The present incentives appear to be adequate.
➢ Tax reduction or exemption privileges for the restructuring SMEs ➢ The angel investment is not subject to tax audit and tax reduction and exemption privileges are available for angel investors. ➢ Start-up companies using their own technology, holders of intellectual property assets and new firms with a corporate history of less three years are exempt from paying corporate tax, income tax, acquisition tax, registration tax and comprehensive land tax. ➢ To increase investment funds, venture capital companies and limited partnerships for venture capital are eligible for several preferential tax incentives: dividend income from start-ups or venture businesses is exempt from corporate income tax; various deductions are allowed; and capital gain taxes and securities transaction taxes can be waived under certain conditions.	Korea		

➢ Measures like simplification and co-ordination of the tax systems, reduction of corporate tax on small enterprises, the possibility of transmitting family enterprises with virtually no fiscal cost, and the promotion of innovation and development activities relating to the environment and internationalization. These measures have resulted in a fiscal framework that is considered adequate by the Spanish authorities for the special characteristics of SMEs.	Spain		
➢ To promote SMEs, new tax schemes for SMEs have been devised which include reduction in corporate income tax rates and tax-deductible incentive for investments in certain plants and machinery.	Thailand		
E. TECHNOLOGY RELATED FACILITIES			
➢ To further the commercialization of research and spur the creation of technology-based start-ups, eight technology incubators have been established that have all received financial support from the Government.	**Denmark**	**Technology Development & Modernization Fund Scheme:** Providing finance to existing SSI units for technology upgradation. In July 1996, SIDBI had permitted SFCs and promotional banks to grant loans for modernization projects costing up to Rs. 50 lakh. The Coverage of the TDMF scheme has been enlarged in 1997. Non-exporting units and units which are graduating out of SSI sector are now eligible.	
➢ To help SMEs improve their technological capabilities, various programmes have been developed, some of them involving the collaboration of Government, academia, and research organizations. The principal funds that are dedicated to these objectives are: The Information Promotion Fund (IPF), which supports information and communications technology (ICT)-related projects and start-ups, and is involved in establishing limited partnerships. IPF invested KRW 126.2 billion in 22 limited partnerships that generated KRW 369.5 billion in funds for	**Korea**		

<table>
<tr><td colspan="4">E. OTHER CONCESSIONS</td></tr>
<tr>
<td>➢ For increased international investment in Australia and improved access for Australian small businesses to overseas expertise for start-up and expanding businesses, a new arrangement has been started from July 2002. Under which Non-resident pension funds are exempt from capital gains tax on venture capital investments.</td>
<td>Australia</td>
<td rowspan="3">ISO 9000 Scheme: Meet the expenses on consultancy, documentation, audit, certification fee, equipment and calibrating instruments required for obtaining ISO 9000 certification.
Scheme for financing activities relating to marketing of SSI products: Provides assistance for undertaking various marketing related activities such as marketing research, R&D, product upgradation, participation in trade fairs and exhibitions, advertising branding, establishing distribution networks including show room, retail outlet, warehousing facility, etc.
Small Industry Cluster Development Programme: For promoting technology upgradation in clusters for a group of SSI units of one industry. It covers a comprehensive range of issues related to technology upgradation, improvement of productivity, energy conservation, pollution control, product diversification and their marketing, training needs etc.</td>
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<td>➢ Grants can be awarded towards certification costs – the MARKET Programme (compliance with various standards, ISO 9000, ISO 1400, EMAS Programme); and cost of creating new job opportunities – the SPECIAL programme (targeting social groups requiring special attention).</td>
<td>Czech Republic</td>
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<tr>
<td>➢ Capital for Small Technology Companies programme (VTC), the VTC Early Phase programme, established in June 2001, helps start-up entrepreneurs even if there has not yet been any involvement by commercial stakeholders.
➢ Through these programmes, the federal Government is assisting the development of a private risk capital market in Germany, and in addition, providing supplementary support for these direct measures by strengthening the business angels market.
➢ Under the Business Angel Network Germany, 40 business angel networks, which were created in the past few years, have been merged.</td>
<td>Germany</td>
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➢ Established in 1963, the **Small Business Investment Company** is a Government policy institution engaged in investing in and otherwise supporting SMEs to promote the enhancement and sound development of SMEs' shareholder equity capital.	Japan		
➢ Support for Small Business Enterprises and Women-owned business ➢ Monitoring of SMEs and the Relaxation of Regulations ➢ Support for Manpower Development ➢ Support for Marketing: The central government, local autonomous authorities and state-run corporations and organizations are encouraged to expand procurement from SMEs.	Korea		
➢ The SME Account *(MKBalans)* is an instrument developed by the Ministry of Economic Affairs in close co-operation with the representative of the accounting organizations, the *Nivra*. The SME Account was introduced in June 2001.	Netherlands		
➢ Preferential treatment in the procurement of raw materials. SMEs are entitled to a share of at least ten percent of total procurement value of goods and services to all Government offices.	Philippines		

Annexure II

Credit Related and Other Facilities Available to SSI

- Priority Sector Lending: Credit to the small-scale sector is regarded as part of the priority sector lending by banks. In order to ensure that credit is available to all segments of SSI sector, RBI has issued instructions that out of the funds normally available to SSI sector, 40 per cent be given to units with investment in plant and machinery up to Rs.5 lakh, 20 per cent for units with investment between Rs.5 lakh to Rs.25 lakh and remaining 40 per cent for other units.

- Public sector banks have been advised to operationalise more specialized SSI branches at centres where there is a potential for financing many SSI borrowers. As on March 2004, 497 specialized SSI branches are working in the country.

- Single Window Scheme: Banks provide composite loan up to Rs 1 core towards both term loan and working capital components.

- With a view to moderating the cost of credit to SSI units, banks have been advised to accord SSI units with a good track record, the benefit of lower spreads over the prime-lending rate.

- In order to take expeditious decision on credit proposals of SSI units, banks have been advised to delegate enhanced powers to the branch managers of the specialized SSI branches so that most of the credit proposals are decided at the branch level.

- A sub-target of 10 per cent of net bank credit was fixed for foreign banks for lending to SSI sector under priority sector. Shortfall, if any, has to be deposited with SIDBI in a 3 year deposit. Interest on the deposit to be paid in inverse proportion to the extent of deficits.

- The Union Budget 2003-04 announced that banks would provide credit to SSI sector within an interest rate band of 2 per cent above and below their

Prime Lending Rates (PLR) for secured loans. All public sector banks have adopted this norm.

- In its Mid-term Review of Monetary and Credit Policy 2003-04, the RBI announced that banks may enhance the limit of dispensation of collateral requirement for loans from the existing Rs.15 lakh to Rs.25 lakh on the basis of good track record and financial position of the units.

- Institutional Arrangement: Small Industries Development Bank of India (SIDBI) was set up as the apex refinance institution. Term loans and working capital finance are provided by State Financial Corporations (SFCs) and banks.

- SME Growth Fund : In line with the announcement made in the Interim Budget for 2004-2005, SIDBI sanctioned a contribution of Rs.100 crore to the Rs.500 crore corpus of SME Growth Fund (SGF). This is a unique initiative taken by SIDBI jointly with major public sector banks (PSBs) such as State Bank of India, Punjab National Bank, Bank of Baroda and several other PSBs. Aggregate commitment of Rs.475 crore has already been received. The SGF shall make primarily equity/ equity related capital investments in accordance with SEBI guidelines in units operating in various growing sectors such as life science, biotechnology, retailing, pharmaceuticals, light engineering, food processing, information technology, infrastructure related to services such as health care, logistics and distributions. It has started its operations by sanctioning investments to two companies. It expects to commit major portion in next 3 to 4 years.

- Small and Medium Enterprises Fund (SME Fund): Pursuant to announcement made in the interim budget for 2004-2005, SIDBI has launched the SME Fund of Rs.10, 000 crore, with a view to giving impetus to the fund flow to the SME sector. SIDBI has operationalised the Fund with effect from April 2004. Under the Fund, assistance is provided to SMEs at SIDBI PLR minus 2 per cent (i.e. 9.5% p.a. at present). Direct assistance is being extended to SMEs through SIDBI's network of branches. While refinance to State Financial Corporations (SFCs) is made available in the interest rate band of 7.5 per cent to 8 per cent, for scheduled commercial banks, the band is 6.25% to 7.25%, depending upon the loan amount and categorization of the bank.

- Credit Guarantee Scheme*:* The Government approved Credit Guarantee Fund Scheme for Small Industries on 19th May, 2000 with the objective of making available credit to SSI units, particularly tiny units, for loans up to Rs. 10 lakhs without collateral/third party guarantees. The Credit Guarantee Trust Fund for Small Industries (CGTSI) set-up by Government of India and SIDBI is operating the Scheme. The Scheme has been operationalised with effect from 1st January 2001. It helps new and existing small scale/ tiny units in getting credit both term loan and working capital without collateral security or third-party guarantee for their viable projects, from eligible Member Lending Institutions (MLI). As on March 31, 2004, there were 45 MLI including National Small Industries Corporation Ltd. and SIDBI. These MLIs include schedule commercial banks, regional rural banks and such institutions as may be approved by Government of India. CGTSI extends guarantee cover for mitigating credit risk in respect of cases up to a loan limit of Rs.25 lakh. The scheme provides guarantee cover up to 75 per cent of the collateral free credit extended by MLI. CGTSI has broadened the ambit of eligible activities to provide guarantee cover to SSI/ tiny units engaged in service based activities also as per the definition of Small Scale Service and Business Enterprises (industry related), in addition to those engaged in manufacturing and IT based activities.

- Credit Linked Capital Subsidy Scheme for Technology Upgradation of SSIs: The Government of India has launched the Credit Linked Capital Subsidy Scheme (CLCSS) which aims at facilitating technology upgradation of the SSI units in the specified products / sub-sectors by providing 12 per cent capital subsidy for induction of well established and improved technologies approved under the Scheme. The Scheme is to be in operation for 5 years from October 01, 2000 to September 30, 2005 or till the time sanctions of capital subsidy by the Nodal Agency reach Rs. 600 crore, whichever is earlier. SIDBI operates the scheme through its branches directly and also indirectly through eligible Primary Lending Institutions (PLIs). Approval for releasing subsidy corresponding to the term loan, both for direct and indirect cases, is being processed at SIDBI's Head Office.

- National Equity Fund Scheme: The objective is to provide equity type support to entrepreneurs for setting up new projects in tiny/small scale sector for undertaking expansion, modernization, technology upgradation and diversification by existing tiny, SSI and service enterprises and for rehabilitation of viable sick units in the SSI sector which fulfil the specified eligibility criteria, irrespective of location. The ceiling on project cost is Rs. 50 lakh, with equity type assistance from SIDBI at 25 per cent of the project cost up to a ceiling of Rs. 10 lakh. Assistance from NEF helps the small scale units in strengthening their equity base and thereby improving their acceptability for term financing by PLIs like the State Finance Corporations, State Industrial Development Corporations, scheduled commercial banks and select urban and state co-operative banks.
- Technology upgradation, modernization and marketing support - Technology Upgradation Fund Scheme (TUFS): With a view to improving the competitiveness and overall long term viability of textile industry through modernization, the TUF Scheme was launched by Ministry of Textiles, Government of India on April 01, 1999 and SIDBI has been designated as the nodal agency for SSIs to channelise the benefits under the Scheme. An option was provided to the small-scale textile and jute industries to avail of either 12 per cent credit linked capital subsidy or the existing 5 per cent interest reimbursement under the Technology Upgradation Fund Scheme. This facility under the Scheme was introduced in January 2002.
- Deferred Payment Guarantee (DPG) Scheme under TUF Scheme was introduced in March 2002 in respect of rupee loans. Additional option of 20% credit linked capital subsidy on machinery cost, was launched in January 2004 under TUF Scheme exclusively for power loom units in SSI Sector. SIDBI has co-opted 205 institutions [PSBs, SFCs, private banks, scheduled urban co-operative banks, other co-operative banks, NSIC and Exim Bank] under TUF Scheme to various SSI clusters. The Scheme has been extended up to the financial year 2007.

- Technology Development and Modernization Fund Scheme*:* Providing finance to existing SSI units for technology upgradation. In July 1996, SIDBI had permitted SFCs and promotional banks to grant loans for modernization projects costing up to Rs. 50 lakh. The Coverage of the TDMF scheme has been enlarged in 1997. Non-exporting units and units which are graduating out of SSI sector are now eligible.
- Laghu Udyami Credit Card (LUCC) Scheme launched by public sector banks for providing simplified & borrower friendly Credit facilities to SSI, tiny enterprises retail traders & artisans.
- Scheme for financing activities relating to marketing of SSI products: Provides assistance for undertaking various marketing related activities such as marketing research, R&D, product upgradation, participation in trade fairs and exhibitions, advertising branding, establishing distribution networks including show room, retail outlet, warehousing facility, etc.
- ISO 9000 Scheme**:** This scheme meets the expenses on consultancy, documentation, audit, certification fee, equipment and calibrating instruments required for obtaining ISO 9000 certification.
- Purchase and Price Preference Policy: This is administered through the Single Point Registration Scheme of NSIC. Under this, 358 items are reserved for exclusive purchase from SSI by Central Government. Other facilities include tender documents free of cost, exemption from earnest money and security deposit and 15% price preference in Central Government purchases.

- SSI Market Development Assistance: The scheme offers funding up to 90 per cent in respect of to and fro airfare for participation by SSI Entrepreneurs in overseas fairs/trade delegations. The scheme also provides for funding for producing publicity material (up to 25 per cent of costs), sector specific studies (up to Rs. 2 lakh) and for contesting anti-dumping cases (50 per cent up to Rs. 1 lakh).
- Marketing Support: Keeping in view the criticality of marketing initiatives for SSI products. SIDBI extends support to SSI units, for undertaking

various marketing related activities like marketing research, advertising, branding, participation in trade fairs, etc.

- Venture Capital Scheme: Venture Capital Scheme was launched by SIDBI in October 1992 and a separate VC fund with an initial corpus of Rs.10 crore was set up for the purpose. Further allocations to the corpus have been made on an annual basis from SIDBI's profits. As on date, SIDBI has committed an aggregate contribution of Rs. 433.09 crore to 24 Venture Capital Funds. The fund was initially utilized for direct VC assistance to SSI units. Over the years, the focus changed and in order to enlarge the reach for extending VC assistance to small-scale units, SIDBI assumed the role of "Fund of funds" by contributing to the corpus of National/ Regional VC Funds for extending assistance to SSI units. The venture capital strategy of SIDBI has been to create a three-tier venture capital structure viz. at the Regional, National and International levels so as to effectively integrate and enhance the opportunities for the SMEs. It may be mentioned that SIDBI and the funds promoted by it are the institutions largely extending VC assistance to SME Sector. Other funds presently focus on larger investments of about Rs.15-20 crore per unit. In September 1999, SIDBI promoted SIDBI Venture Capital Ltd. (SVCL) and SIDBI Trustee Company Ltd. (STCL), as wholly owned subsidiaries of SIDBI primarily to be the Investment Manager and Trustee of the National Venture Fund for Software and IT Industry (NFSIT) respectively. SVCL currently manages the Rs.100 crore NFSIT, which has contributions from SIDBI (Rs. 50 crore), Ministry of Communications and Information Technology, Government of India (Rs.30 crore) and IDBI (Rs.20 crore). The entire fund corpus has been drawn by SVCL from the contributors. SVCL works actively with its investee companies in implementing systems, MIS, corporate governance and other hand-holding and mentoring services. It also provides visibility to the assisted units in both domestic and international fora.

- Scheme of Micro Credit Programme: The Scheme of micro-Credit has been found as an effective instrument for lifting the poor above the level of poverty by providing them increased self-employment opportunities and making them credit worthy. Total requirement of micro-credit in the country has been assessed at Rs.50,000 crore. Micro-credit programme works through NGOs/SHGs and the merit lies in weekly monitoring and refund of instalments. In India, micro-credit programmes are run primarily by NABARD in the field of agriculture and SIDBI in the field of Industry, Service and Business (ISB). Under the programme, NGOs/MFIs are supposed to provide equity support in order to avail SIDBI finance.

- SIDBI Foundation for Micro Credit (SFMC)**:** SFMC is a department of SIDBI and has been identifying and developing select potential Micro Finance Institutions (MFIs) as long term partners and providing them credit and capacity building support for their micro credit initiatives. SFMC pursues capacity building of MFIs and NGOs (informal agencies) as a part of institution building exercise. MFIs are provided need-based capacity building support in the form of grant for, development of credit delivery techniques, MIS development and automation, training and capacity building. In addition, SFMC also extends Transformation Loan to MFIs on very flexible basis to enable them to transform into formal and sustainable institutions. Besides capacity building support to MFIs / NGOs, the SIDBI also extends assistance for the overall development of the micro finance sector.

- World Bank Project on SME Financing and Development**:** With a view to upscale the credit flow to the sector and raising resources for the SME Fund, SIDBI has recently negotiated a line of credit with the World Bank for financing and development of SMEs in India. The other multilateral/ bilateral agencies associated with the project are KfW and GTZ Germany, DFID, UK and SECO, Switzerland. The Project has three components - [i] Line of Credit, [ii] Risk Sharing Facility, and [iii] Technical Assistance. The negotiations for a Line of Credit of USD 120 million from WB have been completed and the Project has been approved by the World Bank.

- KfW (Germany) Line of Credit: SIDBI has negotiated a Line of Credit from Kreditanstalt Fur Weideraufbau, the German Institution, which would be utilized to finance the cleaner production measures under select sectors of leather tanning & finishing, textile wet processing, metal finishing, electroplating, foundries and common effluent treatment plants. The assistance under this Line of Credit is extended at concessional terms and is coupled with provision of free consultancy services to the eligible SSI units.

- Small Industry Cluster Development Programme: For promoting technology upgradation in clusters for a group of SSI units of one industry. The Office of the Development Commissioner (SSI) has launched a scheme called the ‘Integrated Technology Upgradation and Management Programme’ (UPTECH), in 1998, now renamed as 'Small Industry Cluster Development Programme'. The scheme applies to any cluster of industries where there is a commonality in the method of production, quality control and testing, energy conservation, pollution control, etc. among the units of the cluster. The scheme aims to take care of the modernization and technological needs of the cluster. It covers a comprehensive range of issues related to technology upgradation, improvement of productivity, energy conservation, pollution control, product diversification and the units’ marketing, training needs, etc.

- Cluster-based Lending: Ministry of SSI has identified 60 SME clusters for credit concentration. The RBI Working Group on Credit Flow to SSI Sector, under the Chairmanship of Dr A.S. Ganguly, has recommended that the banks should have a full service approach to cater to the diverse needs of the SME sector. This could well be achieved by way of identification of clusters. SIDBI, under the above mentioned World Bank led Project on financing and development of SMEs, proposes to identify 20-25 clusters in different parts of the country and address the issues being confronted by SMEs with a view to scaling up the opportunities for credit deployment, output and employment.

- Setting up of a dedicated Credit Rating Agency for SMEs: With a view to providing credit enhancement and comfort to the bank officials at the field level in their taking bona fide credit decisions, SIDBI, in association with leading public sector banks, has taken an initiative to launch a dedicated credit rating agency for SMEs. The agency would be offering a variety of rating products, including cluster and sub-sectoral ratings. Over the period, the operations of the agency are expected to give boost to the flow of credit to the sector.

- Setting up of Technology Bank : In order to build and disseminate information on technologies and undertake match making, technology transfer and fund syndication services, the SIDBI has taken steps to upgrade its existing Technology Bureau for Small Enterprises (TBSE), set up in association with United Nations- Asian & Pacific Centre for Transfer of Technology (UN-APCTT), into an independent Technology Bank. SIDBI has approached some public sector banks soliciting equity participation. Indian Bank, Oriental Bank of Commerce and State Bank of India have issued firm commitments to associate with SIDBI in setting up the Technology Bank.