REPORTS ON

FINANCING OF ENTERPRISES IN THE UNORGANISED SECTOR

&

CREATION OF A NATIONAL FUND FOR THE UNORGANISED SECTOR (NAFUS)

सत्यमेव जयते

National Commission for Enterprises in the Unorganised Sector
16th & 19th Floor, Jawahar Vyapar Bhawan,
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November, 2007
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Previous Reports of National Commission for Enterprises in the Unorganised Sector

1. Social Security for Unorganised Workers, May 2006
2. National Policy on Urban Street Vendors, May 2006
3. Comprehensive Legislation for Minimum Conditions of Work and Social Security for Unorganised Workers, July 2007
4. Conditions of Work and Promotion of Livelihood in the Unorganised Sector, August 2007

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D.O.No.25021/21/2007/1

Dated: 5.11.2007

Dear Prime Minister,

The National Commission for Enterprises in the Unorganised Sector has prepared a set of two reports on 'Financing of Enterprises in the Unorganised Sector' and 'Creation of a National Fund for the Unorganised Sector'. The latter report flows from the first report. While the report on Financing is a part of our Commission's Terms of Reference, the report on 'Creation of a National Fund for the Unorganised Sector' (to be called NAFUS) was mandated by the Common Minimum Programme.

As you would notice, the first report focuses on the status of financing of the enterprises in the unorganised sector. It also deals with the deficiencies in institutional infrastructure and constraints on financing this sector as well as measures to overcome them. The Report, besides giving its recommendations on financing, makes a separate recommendation for the creation of a National Fund as a statutory body funded by the Government and Financial Institutions that will primarily focus on enterprises with an investment of less than Rs. five lakhs. The Commission's report reveals that this segment today gets approximately 2 percent of Net Bank Credit and virtually no support for marketing, technology and enterprise development even as they constitute 94 percent of all small enterprises. The Fund, as we have designed, is expected to meet these gaps.

Yours sincerely,

Arjun K. Sengupta

Arjun K. Sengupta

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Member

Dr. R.S. Srivastava
Member

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Acknowledgements

The Commission wishes to acknowledge the contribution made by a large number of persons and organisations in the finalization of these Reports.

The Commission benefited in particular from the "Report on the Financing of Unorganised Enterprises" submitted by the Task Force on Access to Finance, Raw Materials and Marketing constituted under the Chairmanship of Professor V. S. Vyas, Professor Emeritus and Chairman, Institute of Development Studies, Jaipur. This Report formed the basis of the current Reports. Further, two concept papers, prepared by Dr. S.L. Shetty, Director, Economic and Political Weekly Research Foundation and by Dr. C.S. Prasad, Consultant were highly useful in the preparation of the Report on Financing of Unorganised Sector Enterprises by the Commission. A special sub-group consisting of Mr. R. K. Das and Dr. S. L. Shetty, members of the Task Force also provided valuable inputs in the formulation of the Report on the Creation of a National Fund for the Unorganised Sector. Shri Joginder Kumar, Member, Advisery Board, NCEUS and President, Federation of Tiny and Small Scale Industries of India (FTSSI) along with Members of NCEUS, participated in and considerably helped arranging regional meetings with Micro Enterprise and other Associations and Federation.

Seven meetings were held at Delhi, Kolkata, Chennai, Guwahati, Kanpur, Pune and Mumbai with various stakeholders, including representatives from Central and State Governments, RBI, NABARD, SIDBI, Commercial Banks, Regional Rural Banks, Cooperative Banks, Micro Financing Institutions, SSIs, Micro Enterprise Associations and Federations and some micro enterprises. These meetings provided an insight on the status and the problems being faced by farm and non-farm enterprises at the field level as well as issues confronting the financial and development institutions. These meetings were coordinated by the Small Industries Service Institutes of the Ministry of Micro, Small and Medium Enterprises located in the above mentioned places, the National Institute of Bank Management at Pune, and the Tamil Nadu Association of Enterprises of Rural Industries and Micro Enterprises at Chennai. The Ministry of Finance, Government of India's letter to banks and financial institutions ensured the participation of financial institutions in the stakeholder meetings.

The Indira Gandhi Institute of Development and Research, Mumbai arranged a meeting with the representatives of RBI, NABARD, some selected banks and associations to discuss the draft report of the Commission. The Commission wishes to thank Prof. R. Radhakrishna, the then Director of IGIDR, and Dr. Srijit Mishra, for facilitating the organisation of this meeting.

The Commission also interacted closely with experts from the field of banking, finance and micro credit. Suggestions received by the Taskforce from Dr. Y.S.P. Thorat, CMD, NABARD, and subsequently other comments received from NABARD were very valuable.

The Commission expresses its special thanks to Dr. Ashim Dasgupta, Finance Minister, Government of West Bengal for sparing his valuable time to discuss the draft report and for his valuable suggestions.

It is our pleasant duty to place on record our deep appreciation of the valuable services rendered by the staff of the Commission. Dr. C. S. Prasad, Consultant, who acted as Member Secretary of the Taskforce, also worked tirelessly in the preparation of this Report. We also wish to acknowledge the role played by various other officers, staff and researchers of the Commission, especially Mr. S. V. Ramana Murthy, and Mr. Mahesh Kumar, Directors of the Commission, and Ms. Swati Sachdev, Ms. T. Shobha and Mr. Ajay Kumar. Editorial support was provided by Mr. N. K. Nair and internal editorial assistance was provided by Ms. Miera Juneja.

The Commission takes this opportunity to thank the above individuals and organizations and all others who have contributed in the preparation of these Reports.

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Report on

FINANCING OF ENTERPRISES IN THE UNORGANISED SECTOR

1 Introduction

Background

1.1 The National Commission on Enterprises in the Unorganised Sector (NCEUS) was set up by the Government as an advisory body and a watchdog for the informal sector. The Commission has been asked to recommend measures considered necessary for bringing about improvements in the productivity of these enterprises, generation of large scale employment opportunities on a sustainable basis, particularly in the rural areas, enhancing the competitiveness of the sector in the emerging global environment, linkage of the sector with institutional framework in areas such as credit, raw material, infrastructure, technology upgradation, marketing and formulation of suitable arrangements for skill development.

1.2 As part of its Terms of Reference, the Commission is required to:

i. "Identify constraints faced by small enterprises with regard to freedom of carrying out the enterprise, access to raw materials, finance, skills, entrepreneurial development, infrastructure, technology and markets and suggest measures to provide institutional support and linkages to facilitate easy access to them"; and

ii. "Identify innovative legal and financing instruments to promote the growth of the informal sector".

1.3 Further, the National Common Minimum Programme (NCMP) announced by the present UPA Government in May 2004 stated that:

"The UPA government will establish a National Commission to examine the problems facing enterprises in the unorganised/informal sector. The Commission will be asked to make appropriate recommendations to provide technical, marketing and credit support to these enterprises. A National Fund will be created for this purpose."

1.4 The Terms of Reference of the NCEUS is given at Annexure 1. The list of the past and present composition as well as the composition of the Advisory Board to the Commission are given at Annexures 2 and 3 respectively.

1.5 To assist the Commission in carrying out its mandate given in the NCMP, as also in the above Terms of Reference, the Commission constituted a Task Force on Access to Finance, Raw material and Marketing relating to the unorganised sector under the Chairmanship of Prof. V S Vyas, Emeritus Professor, Institute of Development Studies, Jaipur. The Task Force has representatives from NABARD and SIDBI apart from eminent economists and NGOs. The Composition of the Task Force along with its Terms of Reference is at Annexure 4. The Task Force submitted the Report to the Commission on 13th April, 2007. The letter of transmittal of the Report is given as Annexure 5.

1.6 The Commission held regional level consultations with the stakeholders particularly of the RBI, financial institutions, commercial banks, State Governments, Micro Enterprise Associations/ Federations and micro entrepreneurs at seven places in the country. The details of the regional level participants and consultations are given at Annexures 6 and 7 respectively.

1.7 The Commission deliberated on the report and recommendations of the Task Force as also its own interaction with the stakeholders. Since NCMP had explicitly directed the Commission that it should suggest the modalities of a National Fund for the Unorganised Sector, the Commission has submitted a proposal for setting up such a Fund (NAFUS) in a separate report. This report deals with the issues of credit related matters for the sector.

Framework of the Report

1.8 The report has been set out in ten chapters. Chapter 2 deals with data base on the Non-Farm Unorganised Enterprises (NFUEs) in the country and makes an estimate of the size of such enterprises. Chapter 3 deals with the institutional arrangements for credit to enterprises in the Non-Farm Unorganised Sector. Chapter 4, gives the status of the flow of institutional credit to the NFUEs directly by the commercial banks and other sources. Chapter 5 traces the origin, growth and status of Micro Finance in India. It examines, among others, the problems and constraints and suggests measures to enable micro credit to graduate to micro-enterprise financing. Chapter 6 addresses itself to the possibility of introduction of some innovative financing instruments appropriate for the NFUEs including the role of instruments like Factoring Services and Venture Capital. Chapter 7 examines the policy initiatives taken by the Government and the RBI to improve the flow of credit. It goes into the details of the Government sponsored schemes aimed at augmenting the flow of credit to the non-farm unorganised sector enterprises. Chapter 8 brings out in brief, the international experiences relating to the non-farm unorganised enterprises financing. Chapter 9 deals with the constraints and issues relating to financing of the farm and non-farm unorganised sector. Chapter 10 contains the recommendations to improve access to credit by enterprises in the non-farm unorganised sector.

2 Enterprises in the Non-Farm Unorganised Sector: Size and Characteristics

Concept of Unorganised Sector

2.1 The informal sector, as per international definition (SNA-1993, UNSC), consists of units engaged in the production of goods and services with the primary objective of generating employment and incomes to the persons engaged in the activity. These units form part of the household sector as un-incorporated enterprises owned by individual or households and having employment size below a certain threshold.

2.2 In line with the international definition and the characteristics of Indian industries, the 'Task Force on Definitions and Statistical Issues' constituted by the NCEUS recommended the following definition for the unorganised /informal sector:

2.3 *The unorganised/informal sector consists of all unincorporated private enterprises owned by individual or households engaged in the sale and production of goods and services operated on a proprietary or partnership basis and with less than ten total workers.*

2.4 The above definition applies equally to all the sectors of the economy including agriculture. However, statistical operations in India so far have been covering only non-agricultural enterprises in the unorganised sector surveys, except that agricultural enterprises other than crop production were covered in the Economic Censuses.

2.5 Though the above definition does not make any distinction between agricultural and non-agricultural enterprises, the concept of enterprise is generally so far being used in India in the context of the non-agricultural sector. Such a restrictive meaning for enterprises, it is felt, would lead to the exclusion of a large number of workers in the agricultural sector, not engaged directly in cultivation. Hence, the non-farm sector may be defined as one not engaged in crop production, plantation and forestry. Thus, it may include enterprises that engage in animal husbandry, fisheries, poultry and piggery, even though these form part of the primary sector of the economy.

2.6 Though the Task Force has recommended a harmonized definition of unorganised/informal sector, the subject ministries/ departments of the Government have been using different definitions to signify specific segments of the industry within their purview. These segments generally overlap with the informal sector as defined by the Task Force. For example, the Ministry of Small Scale Industries has been earlier using a term 'Small Scale Industries (SSI),' defined in terms of investment in plant and machinery. The enterprises with an investment of Rupees one crore in plant and machinery were categorized as 'Small Scale Industries' for the period 1990 to 2001. There after, the limit was raised to Rs. 5 crores for high-tech and certain export industries. A sub-segment of enterprises with investment in plant and machinery not exceeding Rs 25 lakhs within the SSI sector was termed as 'tiny units'. A minor segment of enterprises in the service sector also existed within the SSI fold, which was defined in terms of fixed investment not exceeding Rs 10 lakhs. The segment was named as 'Small Scale Service and Business Enterprises' (SSSBE).

2.7 The Micro, Small and Medium Enterprises Development (MSMED Act, 2006) introduced new definitions of manufacturing and service enterprises based on investment in plant and machinery or equipments as given below:

Enterprises engaged in manufacturing

- ***Micro Enterprises***: With investment in plant and machinery up to Rs. 25 lakhs.
- ***Small Enterprises***: With investment in plant and machinery between Rs. 25 lakhs and Rs. 500 lakhs.
- ***Medium Enterprises***: With investment in plant and machinery between Rs. 500 lakhs and Rs. 000 lakhs.

Enterprises engaged in service activities

- ***Micro Enterprises***: With investment in equipment up to Rs. 10 lakhs.
- ***Small Enterprises***: With investment in equipment between Rs.10 lakhs to Rs. 200 lakhs.
- ***Medium Enterprises***: With investment in equipment between Rs. 200 lakhs to Rs. 500 lakhs.

2.8 Unorganised sector enterprises (USE), form an important part of the non-farm unorganised enterprises. Merging the definitions of the MSMED Act and that of the NCEUS, micro enterprises could be defined as unincorporated enterprises with an investment in plant and machinery up to Rs. 25 lakhs and employing less than 10 workers.

Size of Non-farm Unorganised_Enterprises (NFUEs) as Estimated by Surveys and Census

2.9 The main sources of data relating to un-organised sector enterprises are: (i) Economic Census (ii) Census of Small Scale Industries and (iii) Surveys conducted by the National Sample Survey Organisation on informal sector, unorganised manufacturing and unorganised services sector enterprises. The estimated number of enterprises varies from survey to survey essentially because of the coverage.

The Fifth Economic Census

2.10 The Fifth Economic Census was conducted during 2005 and as per the provisional results published in June 2006 there were about 42.12 million non-farm enterprises in the country at the time of the Census. It included 0.58 million enterprises employing ten or more workers and the remaining 41.54 million establishments were with employment size of less than ten workers. These establishments with less than 10 workers employed about 98.97 per cent of persons in the aggregate of whom 52.4 per cent were hired workers. Between the Economic Census conducted in 1998 and the Fifth Economic Census conducted in 2005 the total number of establishments grew at an annual rate of about 4.8 per cent. The growth rate in rural areas was 5.5 per cent and in urban areas it was 3.7 per cent. Though the Economic Census is expected to list completely the establishments in the country irrespective of their size, location and industrial sector, in practice, it has not been possible to identify all the enterprises.[1]

Third All India Census of Small Scale Industries

2.11 The Third Census of Small Scale Industries (SSIs) was conducted by the Small Industries Development Organisation (SIDO) now known as MSMEDO during the year 2001–02. All the establishments permanently registered with the State Directorates of Industries till March 31, 2001 were surveyed on a complete enumeration basis in the Census. However, this Census suffers from a major limitation since the units under the purview of Khadi and Village Industries Commission (KVIC), Silk Board, All India Handloom Board, Handicrafts Board, Textile Commissioner, etc are outside its scope.

2.12 For the purpose of this Census, enterprises with investment in Plant and Machinery up to Rs. 100 lakhs as on March 31, 2001 was considered as small scale industrial units. Similarly, service and business related enterprises with investments in fixed assets, excluding building and land, up to Rs. 10 lakhs as on March 31, 2001 were considered as Small Scale Service and Business Enterprises (SSSBEs).

2.13 Based on the Census the registered (with District Industries Centres) and unregistered establishments in the small scale industries sector as on March 31, 2001 were estimated to be 10.52 million. They included 4.18

[1] Although the Economic Census means complete enumeration there is a possibility of under coverage especially of the micro enterprises

million manufacturing units, 1.72 million repair and maintenance units and 4.62 million service units. Among the small scale industries, about 97.78 per cent of the units were proprietary and partnership firms and within them 96.37 per cent of the units were employing less than ten workers. The percentage distribution of the units by type of ownership and employment size class is given in Table 2.1.

Table 2.1: Distribution of Small Scale Industries (per cent)

Employment Size (Nos)	Proprietary and Partnership	Others	All enterprises
1	39.45	0.66	40.11
2 - 5	54.07	1.18	55.25
6 - 9	2.85	0.14	2.99
Sub Total	**96.37**	**1.98**	**98.35**
10 -19	1.02	0.14	1.16
20+	0.38	0.11	0.49
Sub Total	**1.41**	**0.24**	**1.05**
All	**97.78**	**2.22**	**100.00**

Source: SSI, 2001, Third All India Census of Small Scale Industries.

NSS 55th Round Informal Non-Agricultural Enterprises Survey

2.14 The Informal Sector Survey conducted during July 1999 - June 2000 covered proprietary and partnership establishments both in manufacturing and service sectors without any size restriction. As per the survey, the estimated number of establishments in the informal sector was about 44.42 million and employed about 79.79 million persons. The number of units employing less than 10 workers was as high as 99.31 per cent but the share of these units in the number of workers and gross value added was only 94.4 per cent and 89.29 per cent, respectively.

2.15 The percentage distribution of these establishments by employment size class along with the percentage share of employment, and gross value added is given in Table 2.2.

NSS 56th Round, Unorganised Manufacturing Sector Survey

2.16 The unorganised manufacturing enterprises (units not covered under Annual Survey of Industries) were surveyed in the NSS 56th Round during July 2000 and June 2001. As per the survey, there were about 17.02 million unorganised manufacturing units in the country. Of these, about 99.90 per cent of the units were proprietary and partnership establishments and only 0.10 per cent were in the other categories of companies, cooperatives, etc. The establishments employing less than ten workers amongst proprietary and partnership firms were about 98.77 per cent. The percentage distribution of unorganised manufacturing units by employment size and type of ownership is given in Table 2.3.

Table 2.2: Distribution of Non- Farm Unorganised Enterprises (per cent)

Employment Size (Nos)	No. of Units	No. of Workers	Gross Value Added
1	57.10	31.80	29.08
2 - 5	40.29	54.74	46.94
6 - 9	1.92	7.5	13.27
1 - 9	**99.31**	**94.40**	**89.29**
10 - 19	0.58	4.08	7.78
20 +	0.11	1.88	2.93
10 +	**0.69**	**5.96**	**10.71**
All	**100.00**	**100.00.**	**100.00**

Source: NSS 55th Round 1999-00, Informal Non-agricultural Enterprises, Computed

Table 2.3: Distribution of Unorganised Manufacturing Enterprises (per cent)

Employment Size (Nos)	Proprietary and Partnership	Others	All Enterprises
1	42.43	0.01	42.44
2 - 5	53.35	0.03	53.38
6 - 9	2.99	0.01	3.00
Sub - total	**98.77**	**0.05**	**98.82**
10 - 19	0.94	0.03	0.97
20 +	0.19	0.02	0.21
Sub - total	**1.13**	**0.05**	**1.18**
All	**99.90**	**0.10**	**100.00**

Source: NSS 56th Round 2000-01, Unorganised Manufacture Sector in India, Computed.

The NSS 57th Round Unorganised Service Sector Survey

2.17 The unorganised services sector enterprises (units not run by Government or those in the public sector) were surveyed in the NSS 57th Round during July 2001 to June 2002. This Survey however, excluded an important sub-sector namely trade and financial intermediation which is the largest sector providing employment to those engaged in non-farm unorganised economic activities. As per the survey, the estimated service sector enterprises excluding the units engaged in Trade and Financial

Intermediation were 14.47 million. About 98.67 per cent of these enterprises were proprietary and partnership and of these about 97.81 per cent were employing less than ten workers each. In fact, 64.14 per cent units did not have any worker except the entrepreneur (known as Own Account Workers) shown in Table 2.4.

Table 2.4: Distribution of Unorganised Service Sector Enterprises (per cent)

Employment Size (Nos)	Proprietary and Partnership	Others	All Enterprises
1	64.14	0.19	64.33
2 - 5	31.87	0.40	32.27
6 - 9	1.79	0.34	2.13
Sub - total	**97.81**	**0.92**	**98.73**
10 - 19	0.71	0.21	0.92
20 +	0.15	0.20	0.35
Sub - total	**0.86**	**0.41**	**1.27**
All	**98.67**	**1.33**	**100.00**

Source: NSS 57th Round 2001-02, Unorganised Service Sector in India, Computed.

Characteristics of Non-farm Unorganised Enterprises

Enterprises by Employment Size

2.18 Table 2.5 reveals that the share of own account enterprises (OAEs) in the total unorganised sector enterprises is very high. The preponderance of Own Account Workers in the total non-farm unorganised enterprises is also confirmed by the results of all the surveys. According to the 55th NSS Round, 57 per cent of enterprises operated with only one worker, which means that they were Own Account Enterprises. This was found to be 42 per cent in the case of manufacturing unorganised enterprises (56th Round) and 64 per cent in the case of service-related unorganised enterprises. In the case of the SSI sector, 40 per cent of the units were Own Account Workers. It is confirmed from all the surveys and also the Census that more than 95 per cent of the enterprises did not have more than 5 workers and almost 99 per cent of enterprises had less than 10 workers.

Other Characteristics

2.19 Estimates based on the NSS 55th Round, 1999-2000, Employment and Unemployment Survey, show that 32 per cent of the unorganised sector workforce is engaged in non-farm activities. According to the Informal Non-agricultural Enterprise Survey, 1999-2000, of the non-farm unorganised sector enterprises, 56 per cent are in rural areas and 44 per cent are in urban areas. Table 2.6 gives a brief on the characteristics of the unorganised enterprises by industry. The number of unorganised sector enterprises is estimated to be 44 million in 1999-2000. Trade has the largest share of enterprises,

Table 2.5: Estimated Number of Enterprises by Employment Size (million)

Employment Size (nos)	55th Round		56th Round		57th Round		Third Census of SSI	
	1999 - 2000		2000 - 2001		2001 - 2002		2001 - 02	
	Number	Percentage	Number	Percentage	Number	Percentage	Number	Percentage
1	25.36	57.09	7.23	42.57	9.31	64.29	4.22	40.11
2 - 5	17.90	40.29	9.09	53.40	4.67	32.27	5.81	55.23
6 - 9	0.85	1.91	0.50	2.93	0.31	2.14	0.31	2.94
Sub - total	**44.11**	**99.30**	**16.82**	**98.80**	**14.29**	**98.70**	**10.35**	**98.28**
10 - 19	0.26	0.58	0.17	1.00	0.13	0.90	0.12	1.14
20 +	0.05	0.12	0.04	0.20	0.05	0.40	0.05	0.58
Sub - total	**0.31**	**0.70**	**0.21**	**1.20**	**0.18**	**1.30**	**0.17**	**1.72**
All	**44.42**	**100.00**	**17.02**	**100.00**	**14.47**	**100.00**	**10.52**	**100.00**

Note: - NSS 55th Round, Informal Sector covered all non-agricultural establishments.
NSS 56th Round Survey covering unorganised manufacturing enterprises.
NSS 57th Round Survey covered unorganised services engaged in hotels, restaurants, transport, storage and communication, real estate, resulting business activities, education, health, social work and other community, social and personal service activities
Third Census of SSI covered both manufacturing and selected services.

Source: NSS 55th Round 1999-00, Informal Non-agricultural Enterprises; NSS 56th Round 2000-01, Unorganised Manufacture Sector in India; NSS 57th Round 2001-02, Unorganised Service Sector in India; SSI 2001, Third All India Census of Small Scale Industries 2001. Computed

Table 2.6: Characteristics of Non-Farm Unorganised Sector Enterprises 1999-2000

Broad Industry Group	Enterprises	Employment	Gross Value Added	Plant and Machinery	GVA Per Enterprise	GVA Per Worker	Plant & Machinery Per Enterprise (Rs)
	(Millions)	Percentage Distribution			(Rs)		
Manufacturing	14.0	36.16	25.13	57.99	30,921	15,995	17,759
Construction	1.8	3.19	3.67	1.49	34,513	26,515	34,301
Trade & Repair Services	17.4	37.12	46.79	8.79	46,525	29,013	10,364
Hotels & Restaurants	1.8	5.18	5.03	0.95	49,521	22,384	4,994
Transport, Storage, Communication	3.9	6.72	8.08	6.22	35,813	27,687	36,314
Other Services	5.2	11.63	11.3	24.56	37,429	22,356	58,359
Total	44.1	100	100	100	39,157	23,019	20,245

Source: NSS 55th Round 1999-00, Informal Non-agricultural Enterprises. Computed

is also the largest in employment, in total value added and also per enterprise value added. The share of Plant and Machinery to total plant and machinery is highest in manufacturing 58 per cent and 25 per cent in other services while the per enterprise investment in Plant and Machinery was highest in Other services which is a heterogeneous group, Construction and Transport has plant and machinery investment of over Rs 30,000 per enterprise. The number of units employing less than 10 workers is 99.31 per cent of the total number of units contributing 89 per cent of the GVA.

2.20 Table 2.7 presents the rural-urban differentials in the characteristics of the unorganised sector enterprises. It is evident that the unorganised sector enterprises are predominantly urban oriented though the share of number of enterprises in rural areas is higher while the employment share is quite even. The contribution of the value added is much higher in the urban enterprises. All other productivity ratios like GVA per worker or enterprise are higher in the urban enterprises as compared to the rural counterparts. The value of Plant and Machinery is also very high in urban enterprises.

2.21 The contribution of unorganised sector as defined by NCEUS to total value added in 2004-05 (at 1999-2000 prices) is estimated to be 50.6 per cent as revealed in Table 2.8. The methodology of estimation followed is based on the recommendations of the sub-group of the Task Force on Definitional and Statistical Issues to estimate the contribution of unorganised sector to GDP. The contribution of non-farm sector in total unorganised sector GDP is 62 per cent, which is far lower than the aggregate GDP, around 80 per cent.

2.22 Table 2.9 presents the percentage distribution of number of units, employment, plant and machinery and gross output classified by investment in plant and machinery, obtained from the reporting units of the

Table 2.7 : Characteristics of Non-Farm Unorganised Sector Enterprises (NCEUS Definition), 1999-2000

Sector	Enterprises	Employment	GVA	Value of Assets	Value of Assets - Plant and Machinery	GVA Per Enterprise	GVA Per Worker	Plant and Machinery Per Enterprise
	(Millions)		Percentage			(Rs)		
Rural	25.0	38.4	32.6	20.6	30.7	22,525	14,638	11,604
Urban	19.1	36.6	67.4	79.4	69.3	60,875	31,823	30,240
Total	44.1	75.0	100.0	100.0	100.0	39,157	23,019	20,245

Source: NSS 55th Round 1999-00, Informal Non-agricultural Enterprises. Computed.

Table 2.8: Estimated Share of Unorganised Sector in GDP in 2004-05 (Per cent)

Industry Group	Unorganised	Organised	Total	Industry-wise Share of the unorganised sector
Agriculture	94.5	5.52	100.00	37.7
Industry	28.9	71.15	100.00	15.0
Services	44.7	55.26	100.00	47.2
Total	50.6	49.39	100.00	100.0

NCEUS 2007. "Report of the Sub- Committee on Contribution of the Unorganised Sector GDP", Mimeo.

Informal Sector Survey of NSSO 1999-2000. Almost 100 per cent of the enterprises have investment in plant and machinery below Rs. 25 lakhs. More than 99.5 per cent have investment in plant and machinery up to Rs. 5 lakhs and generate 90 per cent of the gross output.

Table 2.9: Percentage Distribution of Plant and Machinery (P & M) Value Slabs (Per cent)

Value of P & M slabs (Rs. Lakhs)	Units	Employment	Share in Value of P & M	Gross Output
Upto 1	96.36	89.19	44.30	76.69
1-2	2.12	4.84	13.28	7.42
2-5	0.98	3.32	12.75	5.68
sub total	99.45	97.35	70.32	89.79
5-10	0.29	1.25	8.79	2.92
10-100	0.26	1.40	20.76	7.29
More than 100	0.00	0.00	0.13	0.00
Total	100.00	100.00	100.00	100.00

Source: NSS 55th Round 1999-00, Informal Non-agricultural Enterprises. Computed.

Employment across Sectors

2.23 Table 2.10 presents the distribution of all workers including agricultural workers by formal and informal both in organised and unorganised sectors. The estimates of unorganised/informal and organised employment both in organised and unorganised sectors were worked out for the years 1999-2000 and 2004-05. As per these estimates, about 45.7 per cent of the employees in the organised sector were unorganised/informal workers during 1999-2000 and it went up to 46.6 per cent by

Table 2.10: Distribution of Workers by Type of Employment and Sector (Million)

Sector	1999-2000			2004-2005		
	Informal	Formal	Total	Informal	Formal	Total
Unorganised Sector	341.28(99.60)	1.36(0.40)	342.64(100)	393.47(99.64)	1.43(0.36)	394.90(100)
Organised Sector	20.46(37.80)	33.67(62.20)	54.12(100)	29.14(46.58)	33.42(53.42)	62.57(100)
Total:	361.74(91.17)	35.02(8.83)	396.76(100)	422.61(92.38)	34.85(7.46)	457.46(100)

Note: 1. Figures in brackets indicate percentages.

2. Un-organized/Informal workers consist of those working in the un-organized sector or households, excluding regular workers with social security benefits provided by the employers and the workers in the formal sector without any employment and social security benefits provided by the employers.

Source: NSSO 55th Round 1999-00, Employment and Unemployment; NSSO 61st Round 2004-05, Employment and Unemployment. Computed

2004-05. There was also organised/formal employment in the unorganised sector to the extent of about 0.4 per cent of the unorganised sector workers both in 1999-2000 and in 2004-05. Out of the total work force, 91.2 per cent were unorganised/informal workers in 1999-2000, which increased to 92.4 per cent in 2004-05. The distribution of non-farm workers by formal and informal categories is given in Table 2.11. The share of unorganised/informal non-farm workers has gone up from 80 percent in 1999-2000 to 84 percent in 2004-05.

2.24 The Approach Paper to the 11th Five Year Plan recognized the dualistic nature of the economy, with large differences in productivity between agriculture and non-agriculture on the one hand and within the non-agriculture sector, between the organised and unorganised sectors on the other. The trends show that while employment in the unorganised non-agricultural sector has expanded it is generally low quality employment constrained by low productivity. Further the increase is largely in the self-employment category suggesting a relative shrinkage in wage employment opportunities of a decent kind, especially those with some job protection and social security. The strategy proposed for improving the quality of employment in the unorganised sector is to achieve a 4 per cent annual growth in the capital-labour ratio of non-farm unorganised employment with proper intermediation of savings available so that income per worker could increase at roughly the same rate as that in agriculture.

2.25 Since finance is required by the enterprises to meet various needs, particularly fixed capital and working capital, it is essential to estimate the present size of the non-farm unorganised enterprises in the country as well as their likely size by the end of Eleventh Five Year Plan so that an assessment of the credit needs could be made.

Target Group: Size of Non-Farm Unorganised Enterprises by the End of 2011-12

2.26 The rate of growth of the number of enterprises was 4.8 per cent per annum according to the provisional results of the Fifth Economic Census i.e. between the years 1998 and 2005.[2] However, given the doubts about the possible under-coverage of units in the base year, the number of enterprises was taken from the Informal Sector Survey of the NSS conducted for the year in 1999-2000. In addition to this, such an under coverage in the First Economic Census might have led to an overestimation of the rate of growth i.e. 4.8 per cent growth. In order to moderate the possible over estimation of the growth rate, we have taken a constant annual growth rate of 4 per cent to project the number of units for the period upto 2011-2012. This is similar to the growth rate as observed in the registration of units at DICs and reported by the office of DCSSI.

2.27 Based on this assumption, it is estimated that the number of non-farm enterprises might have increased from 44 million in 1999-2000 (NSSO 2001b) to 54 million in 2004-05. Adopting the same growth rate the number of non- farm enterprises would be 58.4 million by 2006-07 and 71 million by 2011-12 (Table 2.12).

Table 2.12: Estimated Number of Non-farm Unorganised Enterprises 1999-2012

Year	Number of enterprises (Million)
1999-2000	44.11
2004-05	54.0
2006-07	58
2011-12	70.6

Note: Based on 1999-2000 figures and 4 percent rate of growth

2.28 Thus, in so far as this report is concerned, the target group of non-farm unorganised enterprises works out to 70.6 million in 2011-12, employing less than 10 workers and capital investment of less than Rs. 25 lakhs. Based on the average of 1.8 persons per enterprise, as per the survey, the overall additional employment during the Eleventh Plan (2007-12) would be 22 million.

2.29 The rest of this report deals with the credit requirement of this universe of enterprises and proposals for meeting the same.

Table 2.11: Distribution of Non-Farm Workers by Type of Employment and Sector

	1999-2000			2004-2005		
	Informal	Formal	Total	Informal	Formal	Total
Unorganised Sector	109.37 (99.04)	1.06 (0.96)	110.43 (100)	140.65 (99.00)	1.42 (1.00)	142.07 (100)
Organised Sector	17.58 (36.13)	31.08 (63.87)	48.66 (100)	25.89 (45.85)	30.58 (54.15)	56.47 (100)
Total workers	126.95 (79.80)	32.13 (20.20)	159.09 (100)	166.54 (83.89)	31.99 (16.11)	198.54 (100)

Note: Figures in brackets indicate percentages
Source: same as in Table 2.10

2 The rate of growth of enterprises according to the Office of Development Commissioner, Small Scale Industries was 6.3 per cent per annum and mostly covered manufacturing enterprises.

3 Institutional Arrangement for Credit to Enterprises in the Unorganised Sector

Banking in Post Independence Years

3.1 Following Independence, the development of rural India was accorded a high priority. To cater to the needs of the rural areas, an official committee (All India Rural Credit Survey Committee) was created which recommended that the Imperial Bank which was the prime functioning bank in India, should be taken over by a state-partnered and state-sponsored bank. By an act of Parliament, the State Bank of India (SBI) was constituted on 1 July, 1955. With its creation, more than a quarter of the resources of the Indian banking system thus passed on to the direct control of the state. Subsequently in 1959, the State Bank of India (Subsidiary Bank) Act was passed, enabling the SBI to take over eight former state-associate banks as its subsidiaries (later named associated). This marked a significant step in the launch of a state-controlled banking system in India, that was expanded further in 1969 by the nationalization of the major private Scheduled Commercial Banks leading to the spread of banking in to hitherto relatively non-catered areas especially in the rural parts.

3.2 In addition, the Agricultural Refinance Act of 1955 allowed the setting up of a specialised bank for agriculture. Such a bank was set up in 1982 and named as the National Bank for Agriculture and Rural Development (NABARD), which catered exclusively to agriculture. Subsequent to these developments, the state felt the need for a wider diffusion of banking facilities including bank lending. The problem was apparent with the proportion of credit for industry and trade moving up, from 83 per cent to 90 per cent between 1951 and 1968. The rise was clearly at the expense of crucial segments of the economy like agriculture and the small-scale industry. More critically, bank failures and mergers were rather rampant, with the number of banks dropping from 648 (including 97 Scheduled Commercial Banks or SCBs and 551 non-SCBs) in 1947 to 89 in 1969 (comprising 73 SCBs and 16 non-SCBs).

3.3 Some of the important features of the development of banking in India are highlighted below:

Nationalisation of Banks

3.4 'Social control' of bank credit flows, with priority sector lending as a major aspect, was an important objective of bank nationalisation. It introduced restrictions on advances by banking companies in order to ensure that bank advances were confined not only to large-scale industries and big business houses, but were also directed, in due proportion, to important sectors such as agriculture, small-scale industries and exports. Since 1969, there has been a significant spread of the banking habit in the economy with banks able to mobilise a large amount of savings. However, by the 1980s there was a general perception that the operational efficiency of banks in India was on the downturn with low profitability, growing non-performing assets (NPAs), which were already high, and a low capital base. Poor internal controls and the lack of proper disclosure norms led to many problems, which were kept undercover. The quality of customer service did not keep pace with the increasing expectations. All these factors led to the next phase of nationalisation in 1980 which raised the public sector banks' share of deposit from 86 per cent (1969) to 92 per cent (1980). Around this (1979) time Regional Rural Banks came into being to specifically address the credit needs of rural areas and weaker sections of the society. However, a reversal of the process started with the introduction of large-scale banking de-regulation and reforms in the banking sector as part of the overall economic liberalisation in India in 1991.

Changing Composition of Banks

3.5 Since the mid-1990s, the competitive nature of the banking sector has witnessed significant changes, largely due to the presence of the new domestic private sector (NPBs) and foreign banks. The Public Sector Banks (PSBs) have gradually lost their market share to new private sector banks with their share in aggregate deposits falling from 92 per cent in 1991 to 78 per cent in 2004 and the share of domestic private sector banks going up from 4 per cent to 17 per cent. In terms of advances, while the share of PSBs share has declined from 92 per cent in 1991 to 73 per cent in 2004, that of the domestic private sector banks has increased from 3 per cent to 19 per cent.

Priority Sector Lending

3.6 At a meeting of the National Credit Council held in July 1968, it was emphasized that commercial banks should increase their involvement in financing the priority sectors, viz., agriculture and small scale industries. The description of the priority sectors was later formalized in 1972 on the basis of the report submitted by the Informal Study Group on Statistics relating to advances to the priority sectors constituted by the Reserve Bank in May 1971. On the basis of this report, the Reserve Bank prescribed a modified return for reporting priority sector advances and certain guidelines were issued indicating the scope of the items to be included under the various priority sector categories. Although initially there was no specific target fixed in respect of priority sector lending, in November 1974 the banks were advised to raise the share of these sectors in their aggregate advances to the level of 33 1/3 per cent by March 1979. Subsequently, on the basis of the recommendations of the Working Group on the Modalities of Implementation of Priority Sector Lending and the Twenty Point Economic Programme by Banks, all commercial banks were advised to achieve the target of priority sector lending at 40 per cent of aggregate bank advances by 1985. Sub-targets were also specified for lending to agriculture and the weaker sections within the priority sector. Since then, there have been several changes in the scope of priority sector lending and the targets and sub-targets applicable to various bank groups. Beginning in the 1990s, the 40 per cent priority sector lending requirement for net bank credit (NBC) as applicable to PSBs as well as private sector banks continued, but its burden on banks was eased by freeing the rates on loans above Rs. 2 lakhs, raising the rates on small loans and making additional types of credit available. The requirement was increased to 32 per cent for foreign banks been liberalized in terms of the interest rates and also the additional types of priority credit as have been made eligible

Role of Reserve Bank of India in Credit Policy

Reserve Bank of India

3.7 The overall regulation of the monetary policy, which includes credit to SSI and other non-farm enterprises is in the hands of the Reserve Bank of India (RBI). The RBI regulates the operation of the entire banking system in India and draws its powers from Section 21 of the Banking Regulation Act 1949 which reads as under:

> "Power of Reserve Bank to control advances by banking companies:
>
> (i) Where the Reserve Bank is satisfied that it is necessary or expedient in the public interest, (ii) or in the interests of depositors, (iii) or banking policy so to do, it may determined the policy in relation to advances to be followed by banking companies generally or by any banking company in particular, and when the policy has been so determined, all banking companies or the banking company concerned, as the case may be, shall be bound to follow the policy as so determined.
>
> Without prejudice to the generality of the power vested in the Reserve Bank under sub-section (1) the Reserve Bank may give directions to banking companies, either generally or to any banking company or group of banking companies in particular as to:

i) The purposes for which advances may or may not be made,

ii) The margins to be maintained in respect of secured advances,

iii) The maximum amount of advances

iv) The maximum amount up to which guarantees may be given

v) The rate of interest and other terms and conditions on which advances or financial accommodation may be made or guarantees may be given.

Every banking company shall be bound to comply with any directions given to it under this section".

3.8 While taking any policy decision, the Reserve Bank is governed by the requirement of the monetary policy to fit in within the overall framework of the economic policy of the country. With regard to credit to small scale industries a standing committee on SSI credit under the chairmanship of a Deputy Governor has been constituted which monitors the flow of credit on a quarterly basis. Regular guidelines are issued to the banks for promoting credit to small enterprises. RBI guidelines to banks with regard to the target on SSI credit are as under:

- The Scheduled Commercial Banks are expected to enlarge credit to the priority sector which includes the SSI sector, which is 40 per cent of the net bank credit.
- While there is no sub-target for lending to the SSI sector, banks may fix a self-set target for growth in advances to this sector.
- Of the credit going to the SSI sector 40 per cent should go to cottage industries, KVIs, artisans and tiny industries with investment in plant and machinery upto Rs.5 lakhs, 20 per cent to SSI with investment in plant and machinery between Rs. 5 lakhs and Rs. 25 lakhs and the remaining 40 per cent to other SSIs.

3.9 RBI is invited to all credit-related meetings of the Ministry of MSME and also in the meetings of the Standing Committee of the Parliament.

Multi-Level Institutional Structure for Non-Farm Sector

3.10 A large number of institutions are engaged in the task of credit dispensation to the farm and non-farm enterprises. Major national/state-level institutions operating in the country are:

Commercial Banks

3.11 These banks have been playing a pivotal role in financing the working capital requirements of agriculture and small scale enterprise sector. Besides providing short-term assistance, these institutions have also extended support to small enterprises by way of providing term-loans (in the form of composite loans) and funding of the government sponsored self-employment schemes under which small enterprises are set up by first-generation entrepreneurs. Apart from SSI loans, commercial banks also support non-farm unorganised enterprises, through loans for (i) industrial estates, (ii) small road and water transport operators, (iii) retail trade, (iv) small business, (v) housing loans, (vi) advances to self- help groups, etc. under their priority sector lending programme. Currently, about 80 per cent of the commercial bank's credit to the SSI sector is in the form of working capital and the balance is as term loans. Under the RBI guidelines banks have started composite loaning to the SSIs. The current limit for such loans is Rs. 1 crore.

State Financial Corporations (SFCs)

3.12 The SFCs are mandated to serve as regional/ state level financing agencies for promoting regional growth in the country through the development of small and medium enterprises by grant of loans and participation in their equity. The main objectives of SFCs are to provide financial assistance to industries, catalyse investment, generate employment and widen the industry base. The eighteen SFCs across the country provide financial assistance by way of term loans. The operations of the SFC's have declined over the years, thereby adversely affecting the credit flow to the small enterprises sector. The lending is in the format of loans and debentures and they also operate schemes of IDBI/SIDBI in addition to extending working capital loans under the composite loan scheme. Most of them have a huge portfolio of non- performing assets due to improper project appraisals and lack of follow-up and supervision of the assets financed by them.

Regional Rural Banks

3.13 Regional Rural Banks (RRB) have been created to promote agriculture, trade, commerce and industry in rural areas and thereby to improve the rural economy. RRBs also support micro/tiny and artisan-based units and village industries located in the rural areas. Most of the NABARD's schemes for non-farm unorganised enterprise are operated through RRBs. For quite sometime, the RRBs had been facing problems in their operation as a result of which a large number of branches became unviable. Government of India has recently restructured the working of 139 RRBs (out of total of 196) and linked them with the founder bank.

Cooperative Banks

3.14 The cooperative banks mostly finance those enterprises, which are formed on a cooperative basis either for production or marketing. Mostly handlooms, powerlooms, coir and some village industries work on a cooperative basis and avail of cooperative loans. NABARD uses this channel for extending credit to farm and non-farm enterprises. Cooperatives provide working capital funds to traditional industries. More than one lakh Primary Agriculture Cooperatives (PACs) finance the agriculture and agriculture-related industries. The Urban Cooperative Banks (UCBs) has 1853 branches which play a vital role in meeting the working capital needs of the cottage and tiny industries.

Small Industries Development Bank of India (SIDBI)

3.15 SIDBI was established in April 1990 as the apex refinance bank and the principal development financial institution for the promotion, finance and development of the small industries sector and to coordinate the functions of other institutions engaged in similar activities. It has 4 regional offices and 65 branches for the channeling of the direct and indirect credit. SIDBI is engaged in both refinance and in direct credit, however it does not have a full complement of reach and services such as flexibility to offer working capital, fund-based and non-fund based guarantees, value added services, etc to its clients due to which it is not able to capitalize on its competitive advantages in the market.

Indirect Assistance

- SIDBI's financial assistance to the small sector is primarily channeled through the existing credit delivery system, which consists of state level institutions, rural and commercial banks.
- SIDBI provides refinance to and discounts bills of primary lending Institutions (PLI).
  - The assistance is available for:
  - Marketing of SSI products;
  - Setting up of new ventures;
  - Availability of working capital;
  - Expansion;
  - Modernisation;
  - Human resource development;
  - Diversification of existing units for all activities.

Direct Assistance:

- The loans are available for new ventures, diversification technology upgradation, industrialization and expansion of well-run small and medium scale enterprises.
- Foreign currency loans for import of equipment are also available to export oriented small and medium scale enterprise.
- Micro credit to Micro Financing Institutions.

3.16 SIDBI also provides venture capital assistance to the entrepreneurs for their innovative ventures if they have a sound management team, long term competitive advantage and a potential for above average profitability leading to an attractive return on investment,.

National Bank for Agriculture and Rural Development (NABARD)

3.17 National Bank for Agriculture and Rural Development (NABARD) was created in 1982 with the main objective to provide assistance to agriculture and agriculture-related activities. It also carries out promotional programmes for rural development such as a Rural Entrepreneurship Development Programme (REDP), training-cum-production programmes and action plan for rural industrialization. A part of its activities are also addressed to the non-farm sector, though its prime responsibility is the farm sector. It plays a significant role in the promotion of micro credit under SHG-Bank Linkage Programme. Assistance is also provided to State Governments for the development of infrastructure through Rural Infrastructure Development Fund.

SSIs under Priority Sector Lending of Banks

3.18 The subject of providing credit to people engaged in SSIs and other unorganised enterprises particularly in the rural areas has received the attention of the government since the beginning of the planning era. Finding the disinclination of the banking system to assist this sector, the government has brought this sector under the Priority Sector Lending Programme of the banks, wherein commercial banks have been asked to advance 40 per cent of the net bank credit to the priority sector. In the case of cooperative banks, the priority sector ceiling was fixed at 60 per cent. Initially, the priority sector consisted of agriculture, small scale Industries, small and marginal farmers and artisans and exports. However, subsequently housing, education, consumption, profession, I.T. Sector, food processing not falling under SSI, etc. were also included under the priority sector based on the recommendations of the Narasimham Committee (1992). This has, in our view, diluted the real intent of the priority sector lending in terms of credit flow to weaker sections of the population that would include the non-farm unorganised sector, dealt with in this report. Since the desired credit was not going to agriculture, a quota at 18 per cent of the net bank credit was fixed. There is no such quota for the SSI sector. However, another quota of 10 per cent exists for small and marginal farmers and artisans termed as the weaker section. There is no quota for small scale industries; however, quota of 60 per cent of SSI credit exists for micro enterprises with investment in plant and machinery upto Rs. 25 lakhs.

3.19 Indian credit system, as it has emerged, is a product of evolution as well as intervention. The broad objectives of the policy intervention have been:

- To institutionalise credit;
- To enlarge its coverage, and
- To ensure the provision of timely and adequate credit at a reasonable rate of interest to as large a segment of the population as possible.

3.20 Institutional innovations have been a continuous process with changes occurring depending on the experience. In providing credit to unorganised enterprises, a multi-agency approach has been adopted so as to take advantage of the strengths of different institutional forms.

Sources of Credit Support to Non-Farm Sector-Overall Arrangement

3.21 Institutional financial assistance to unorganised enterprises consists of (i) direct credit (ii) indirect credit (iii) micro credit (iv) subsidy under government schemes to encourage the flow of credit. The government has devised schemes to enhance the confidence of banks in favour of SSI lending such as the Credit Guarantee Scheme.

Direct Credit

3.22 The major portion of credit (about 95 per cent) is in the form of direct credit from the banks wherein they are in direct touch with the entrepreneurs and loans are advanced by them after appraisal of the project proposals, ascertaining their viability, assessing the creditworthiness of the customers and after the entrepreneurs fulfill all the conditions of the banks including margin money, collateral, third party guarantee and payment of service charges, etc. Banks undertake this task through their branches, which are spread to rural and urban areas depending upon the need of the area. Important banking institutions engaged in this task are listed below:

- Scheduled Commercial Banks consisting of public sector banks, private sector banks and foreign banks- about 59,000 branches
- Regional Rural Banks- about 14,500 branches
- Cooperative banks- about 13,500 branches
- Small Industries Development Bank of India (SIDBI)- 65 branches
- State Financial Corporations (SFC)- in 18 states
- Small Industries Development Corporations (SIDC) in all the states.

Indirect Credit

3.23 A very small segment of the loan goes to the small and unorganised enterprises in the form of indirect credit to entrepreneurs by the banks in the form of micro credit. It is indirect, since entrepreneurs are not in direct contact with the banks. There are intermediaries in between in the form of Self-help Groups (SHGs), NGOs, voluntary agencies and micro-financing institutions. Refinance from NABARD and SIDBI though is seemingly indirect in reality generates direct credit by the banks. The institutions engaged in indirect credit and refinancing are as under:

- Micro Credit under Self Help Group (SHG) – Bank Linkage Programme
- Refinance from:
  - National Bank for Agriculture and Rural Development (NABARD)
  - Small Industries Development Bank of India (SIDBI)
- Credit through Micro Financing Institutions (MFIs).

Subsidy under Government Schemes to Encourage Flow of Credit (General) – Major Schemes

3.24 The Central Government has been implementing a large number of schemes to encourage the poor people particularly those who find it difficult to meet the banks' conditionalities directly to go for self employment by raising loans from the banks. The Government helps the poor through a subsidy on the loan or through margin/ equity money. This helps them to approach banks for a term loan and a working capital loan. Some of the major schemes being implemented by the government are listed below:

- Prime Minister's Rojgar Yojana (PMRY) (Ministry of MSME)
- Rural Employment Generation Programme (REGP) for Village Industries by KVIC (Ministry of MSME)
- Interest Subsidy Eligibility Certification (ISEC) Scheme for Khadi by KVIC (Ministry of MSME)
- Swarnjayanti Gram Swarozgar Yojana (SGSY) (Ministry of Rural Development)
- Swarnjayanti Shahari Swarozgar Yojana (SSSY), (Ministry of Urban Employment & Poverty Alleviation.).

Subsidy for Technology Upgradation

3.25 Modernisation and technology up-gradation is one of the principal requirements for enhancing competitiveness. Competition has further intensified in the wake of liberalisation and globalisation. Modernisation, however is a costly proposition. In order to encourage small entrepreneurs to modernize, the Government of India has been implementing a few schemes of interest subsidy and capital subsidy. Some of these schemes are:

- Interest and / or Capital Subsidy for Technology Upgradation of Textile Units (Ministry of Textiles)
- Credit-Linked Capital Subsidy Scheme for Technology Up-gradation of SSI (Ministry of SSI).

Schemes to Enhance the Comfort Level of the Banks to Finance Small Scale and Micro/Tiny Enterprises

3.26 Banks being commercial enterprises do not prefer lending to small enterprises and other non-farm informal enterprises because of the high risk, high transaction costs, higher NPAs and lower and erratic repayments by the enterprises. Many entrepreneurs, even though in great need of credit, are not able to obtain bank loans because of their inability to arrange collaterals. In order to enhance the confidence level of banks in small lending, the Government has launched a few schemes for example:

- Credit Guarantee Scheme (Ministry of SSI)
- Credit Rating Scheme for SSIs (Ministry of SSI).

Role of Micro Finance Institutions (MFI)

3.27 The Micro Finance Institutions (MFI) model is currently catching up in India as institutions for extending micro credit to the poor. Although their share is less than 10 per cent in total micro credit, it is becoming popular because of good portfolio quality and efficient system of operation; although the interest rates charged by them are higher than the alternate sources. The MFI model in India is characterized by the diversity of institutional and legal forms. The first well known MFI, SEWA was incorporated as an urban cooperative bank in 1974, and paved the way for micro finance in India by showing that the poor were bankable. In 1980, the Working Womens' Forum started its activites dealing with Micro-Finance. In 1980s, a number of registered societies and trusts commenced group-based savings and credit activities on the basis of grant funds from donors. Towards the end of the decade others began replicating the Grameen Model of Bangladesh, based initially on donor funding but increasingly on funding from domestic apex financial institutions such as SIDBI, FWWB (Friends of Women's World Banking) and RMK (Rashtriya Mahila Kosh).

3.28 The Micro Financial Sector (Development and Regulation) Bill 2007 introduced in Parliament has defined MFIs as an organisation or association of individuals including the following if it is established for the purpose of carrying on the business of extending micro finance services-

i) A society registered under Societies Registration Act, 1860.

ii) A trust created under the Indian Trust Act, 1880 or public trust registered under any state enactment governing Trust for public religious or charitable purposes.

iii) A cooperative society or mutual benefits society or mutually aided society registered under any state enactment relating to such societies or any multi state cooperative society registered under the Multi-State Cooperative Societies Act, 2002 but not including (A) a cooperative bank as defined in clause (cci) of Section 5 of the Banking Regulation Act, 1949 or (B) a cooperative society engaged in agricultural operations or industrial activity or purchase or sale of any goods and services.

3.29 Under this Bill, it has been proposed that the micro finance sector will be placed under regulatory authority of NABARD. It may be mentioned that NABARD under SHG-Bank Linkage scheme provides nearly 70 per cent of micro credit available in the country.

Informal Credit – Role of Moneylenders

3.30 Historically, moneylenders, in different guises, have played a significant role in meeting, the credit needs of the rural producers covering both farm and non-farm activities. With stringent laws against money lending and the phenomenal growth of the formal credit delivery system, it was thought that money lenders would soon be out of business. Instead they have been in the business of lending in several disguises. The All India Debt and Investment Survey revealed that the share of moneylenders in the total dues of rural households rose from 17.5 per cent in 1991 to 29.6 per cent in 2002. This is also confirmed by the statement of the Finance Minister while presenting 2006-07 Union Budget:

"*The findings of the NSS 59th Round (2003) reveal that out of the total number of cultivator households, only 27 per cent receive credit from formal sources and 22 per cent from informal sources. The remaining households, of mainly small and marginal farmers, have virtually no access to credit. With a view to bring more cultivator households within the banking fold, I propose to appoint a Committee on Financial Inclusion. The Committee will be asked to identify the reasons for exclusion, and suggest a plan for designing and delivering credit to every household that seeks credit from lending institutions*"

3.31 As promised, the Committee has been constituted in June 2006, under the Chairmanship of Dr. C. Rangarajan.

3.32 The Household Indebtedness and Investment Survey, conducted by the National Sample Survey Organization (59th Round) in 2003, brings out the important role of moneylenders in the credit system. In all, the indebtedness was of the order of Rs. 1,76,795 crores as of June 2003. Rural households, which form 73 per cent of the total number of households, hold 63 per cent of the debt while urban household constitutes 27 per cent; owe the other 37 per cent. The Incidence of Indebtedness (IOI), or the percentage of indebted households, is nearly 27 per cent for the rural areas and 18 per cent in the urban areas. It is 24 per cent for the country as a whole. Every fourth household is, thus, indebted, with an average debt of nearly Rs. 9,000. The level of indebtedness by the households is incurred both from institutional and non-institutional sources. The former constitute mainly cooperative societies/banks and commercial banks and the latter moneylenders and to some extent, friends and relatives. The share of the non-institutional category (mainly moneylenders) has actually risen in the rural areas between 1981 and 2002. Nearly 45 per cent of lending in the rural areas is by moneylenders and 25 per cent of urban indebtedness is due to moneylenders in the rural areas. The dependence of non-cultivators on moneylenders was nearly 54 per cent in 2002 and of the self- employed in the urban areas 33 per cent. The survey also suggests that interest rates are on the higher in non-institutional lending than in institutional lending. Around 40 per cent of the lending by moneylenders was at interest rates above 30 per cent in the rural areas in 2002.

3.33 The issue under examination for the present is: what makes the moneylenders survive in the rural and non-farm sector. The reasons are clear. The information problem is serious in rural credit markets. Banks cannot match moneylenders in getting information on the credit worthiness of borrowers, and their utilisation and repayment capacity. The rates charged by moneylenders are high but these can be explained. They incur costs in collecting information on borrowers, monitoring their actions and ensuring repayment. For borrowers, timely credit is more important than the associated costs. So moneylenders are able to reach the needy – the borrowers – better than the banks. However, the exploitative nature of moneylenders cannot be denied. The need for regulating them cannot be denied. The gap to be created by their withdrawal will have to be bridged by the institutional sources. In fact in order to reduce the role of the moneylenders, it is essential that banking sector should incorporate factors such as flexibility, easy accessibility, better information and monitoring etc. into the banking system. RBI is considering to give a legal status to moneylenders and to make better use of the institution in a formal way.

4 Flow of Institutional Credit to Non-Farm Unorganised Enterprises (NFUEs)

Current Status of Unorganised Enterprises- Based on Surveys and Studies

4.1 According to the Third Census of SSIs (2001-02), of the total number of 10.5 million small enterprises in 2001-02, about 87 per cent units were unregistered (not registered with DICs), while 1.04 lakh units were factory units with power (employing more than 10 workers and registered under the Factories Act). Of the manufacturing SSI units 99.5 per cent were tiny units now called micro units (having an investment in plant and machinery less than Rs. 25 lakhs) about 94 per cent of the units were having investment in Plant and Machinery up to Rs 5 lakhs. We may call this segment as special sub-group of Micro Enterprises (SSME). While a registered unit employed on an average 4.48 persons, unregistered units had only 2.05 persons per unit. Per unit investment in plant and machinery was found to be Rs. 2.21 lakhs in the case of registered units and Rs. 0.27 lakhs in the case of unregistered units. Per unit fixed investment was Rs. 6.68 lakhs in registered units and Rs.0.68 lakhs in unregistered units. The average for the SSI sector as a whole was Rs. 1.47 lakhs. Average per unit output of the registered units was Rs.14.78 lakhs. It was Rs. 0.86 lakhs in the case of unregistered units. The average for SSI sector was Rs. 2.68 lakhs. Most of the non-farm unorganised enterprises could be said to fall in the category of unregistered small scale enterprises.

4.2 The Third Census of SSI (2001-02) found that only 14.26 per cent of the registered units (registered with District Industries centres of the State Governments) availed of bank finance, while only 3.09 per cent of the unregistered units had access to bank finance. This means that about 97 per cent of the smaller among the small enterprises or the non-farm unorganised enterprises (NFUEs) were deprived of the institutional credit. In other words, most of the non-farm unorganised enterprises existing in the form of tiny and micro enterprises use self-finance (savings) or borrowed funds from friends, relatives and moneylenders. Moneylenders continue to play an important role after self-finance. The recent All India Debt and Investment Survey has revealed that the share of moneylenders in the total dues of rural households rose from 17.5 per cent in 1991 to 29.6 per cent in 2002.

4.3 According to the NSS 55th Round (1999-2000) only 7.98 per cent of the unorganised sector enterprises have any outstanding loans and thus have any access to external finance. Of the total number of enterprises in the unorganised sector almost an equal share of enterprises obtain such a loan from institutional and non-institutional sources (4.13 per cent and 4.10 per cent respectively). Since this survey is exclusively for non-farm unorganised enterprises, it would be appropriate to examine its findings in some detail.

4.4 An analysis of the NSS 55th Round data reveals the following trends:

- The average institutional loan per reporting enterprise was Rs. 45,356 for enterprises and Rs. 71,229 for enterprises with value of assets upto Rs. 5 Lakhs and upto Rs. 25 lakhs respectively.
- Total amount of outstanding loans in the informal sector units in 1999-2000 amounted to Rs. 23,098 crores. Institutional loans amounted to Rs. 12,257 crores and those from non-institutional sources came to Rs. 10,842 crores.
- The share of institutional loans is higher than the non-institutional loans and comprises nearly three-fourths of the total loans taken in rural areas and a little less than half (46 per cent) in the urban areas.
- Majority of the loans were from banks (28 per cent) followed by those from relatives (20 per cent).
- The maximum volume of loans per enterprise was from other sources, followed by agencies, relatives, and partners. Banks, which form the most prominent source of loans, have Rs. 63 thousand loans per enterprise and moneylenders, Rs. 51 thousand.
- The least amount of loans per enterprise was from contractors.
- 45 per cent of the enterprises had outstanding loans ranging from Rs. 10,000 to –Rs.99,999 and 34 per cent have outstanding loans between Rs. 1,000 and Rs.9,999.
- In the institutional category, majority of the enterprises had outstanding loans ranging between Rs. 10,000 and Rs.99,999.
- The total amount of outstanding loans is higher in the case of urban enterprises than in the rural unorganised sector enterprises.
- In rural areas, around 41 per cent of the enterprises have outstanding loans between Rs. 1000 and Rs.9999. 42 per cent of them have outstanding loans between Rs. 10,000 and Rs. 99,999 each. In urban areas, almost 50 per cent of enterprises have outstanding loans between Rs. 10,000 and Rs. 99,999.
- The amount of outstanding loans is the largest in the employment size 2-5 persons and then for 6-9 employees.
- In rural areas, the share of institutional sources increases with an increase in the employment size; the opposite is true in urban areas.
- In rural areas, the share of interest payable to moneylenders and relatives is considerably higher in construction while in hotels and restaurants it is higher for the moneylenders. In urban areas, the share of interest payable to other non-institutional sources is considerably higher.
- The outstanding loans of the non-agricultural unorganised sector comprised only 1.41 per cent of the total outstanding credit of the banks while outstanding loans of banks and cooperatives comprised of about 2.15 per cent of the total outstanding credit of this sector in 1999-2000.
- The proportion of enterprises availing loans is higher in urban than in rural areas (urban 8.80 per cent and rural 5.59 per cent).
- Within the institutional sources, banks followed by cooperative agencies are more important sources of loans (56 and 26 per cent respectively).
- Among the non-institutional sources moneylenders still form the main source of outstanding loans followed by relatives and contractors and suppliers.
- The share of enterprises with institutional and non-institutional loans is higher in the urban areas indicating that in rural areas each enterprise tends to avail a loan primarily from one source while in urban areas each enterprise seek loans from multiple agencies.

4.5 A recent research study (World Bank, 2006) on the status of flow of credit to the SME sector, (study of 213 firms in Gurgaon and Hyderabad by a World Bank Team), has revealed that in the start up phase, family constitutes an extremely important source of funds for the overwhelming majority (over 85 per cent) of the respondents and 'trade credits' came next in importance (representing an extremely important source of funds for 27 per cent of the respondents). In comparison, bank loans from state-owned banks make up an extremely important source for 15 per cent and very important source for about 17 per cent of the firms surveyed. It may be mentioned that the firms studied are mostly the larger ones among the SSIs and include medium enterprises as well.

4.6 In subsequent paragraphs an attempt has been made to examine the status of bank credit to on-farm unorganised enterprises with the help of credit flow data as emerging from various RBI reports and statistical statements.

4.7 Direct credit is extended by banks to SSIs as also for other non-farm activities such as the setting up of industrial estates to carry out small businesses, retail trade, road and water transport, etc. Banks also assist Self-Help Groups. In Table 4.1 an attempt has been made to bring together at one place, all the possible credit which flows from various banking channels to the non-farm unorganised sector for two years, 2002-03 and 2003-04.

4.8 Major portion of institutional credit to the non-farm unorganised enterprises comes from the scheduled commercial banks. The share of these banks was 66.7 per cent in 2002-03, 73.7 per cent in 2003-04 and 76.7 per cent in 2004-05. Cooperative banks happen to be the second largest contributor to institutional credit but their share declined drastically from 17.9 per cent in 2002-03 to 10.6 per cent. It is estimated to be 13.7 per cent of the total in 2004-05. The loss in cooperative banks' share was a gain for commercial banks and regional rural banks. Regional rural banks' share moved up from 8.4 per cent in 2002-03 to 10.1 per cent in 2003-04. But it declined to 8.9 per cent in 2004-05. Apart from providing refinance to banks and SFCs, SIDBI makes direct advances to SSIs and medium enterprises but its share in the total is less than 2 per cent and thus is not significant. A matter of major concern, however, is the

Table 4.1: Institutional Credit to Non-Farm Unorganised Enterprises (NFUEs) including the SSIs (Rs. crores)

S.No.	Institutional Sources *	March 2003	March 2004	March 2005
1	Scheduled Commercial Banks			
	(i) SSI and Allied activities	64,707	71,209	93,498
		(46.0)	(49.8)	45.8
	(ii) Other NFUEs@	29,593	34,313	46,287
		(19.7)	(24.0)	(30.9)
	(iii) (i +ii)	94,300	1,05,522	129,785
		(66.7)	(73.0)	(76.7)
2	Regional Rural Banks	11,897	14,393	16,161
		(8.4)	(10.1)	(8.9)
3	Cooperative Banks	25,317	15,117	24,912*
	(Urban Cooperative PCBs)	(17.9)	(10.6)	(13.7)
4	SIDBI (Direct Finance)	1,917	2,695	3,494
		(1.3)	(1.9)	(1.9)
5	State Financial Corporations	1,856	1,134	1,495**
		(1.3)	(0.6)	(0.8)
6	Small Industries Development	6,789	4,414	6188
	Corporations including NSIC	(4.8)	(3.01)	(3.4)
	Total	1,42,076	1,43,005	1,82,035
		(100.0)	(100.0)	(100.0)

Note: Figures in bracket are the shares in total.
* Since data for 2005 is not available, it is the average of 2004 and 2006.
** Since data for 2005 is not available it is average of 2003 and 2004.
@ Credit for Small business-retail trade, road and water transport - operation, industrial estate, SHGs etc.
Source: Compiled from various sources (RBI, Progress of Banking in India, 2004-2005; RBI, Statistical Tables Relating to Banks in India, 2004-05; Economic Survey 2005 - 06; Other banking statistics)

declining flow of credit from the State Financial Corporations. These Corporations were created to provide mainly term finance but over the years, out of 18 SFCs in the country, 14 are running into losses or have become almost defunct. Small Industries Corporations set up in various states also help the small and tiny enterprises through equity support, margin money support, and assistance for procuring raw materials. Their contribution to the total has been in the range of 3 to 5 per cent during 2003-05. The National Small Industries Corporation has also been extending some finance for hire-purchase of machinery and marketing, however, separate data is not available.

Credit Flow to SSI Sector Including Non-farm Unorganised Enterprises (NFUE) – through Commercial Banks

4.9 Non-farm unorganised enterprises have been contributing significantly to the country's industrial production, employment and exports. Small scale industries and traditional industries covering Khadi and Village Industries, Handlooms, Powerlooms, Sericulture, Coir and Handicrafts account for about 49.5 per cent of industrial production (2006), and 55 per cent of national exports and generate employment opportunities for about 70 million persons (both full-time and part time). However, within the non-farm unorganised sector, the Small Scale Industries (SSIs) including tiny industries have been playing a very important role; since it is a relatively modern segment of small enterprises and provides full-time employment as against mostly part-time employment by the traditional industries.

4.10 SSIs accounted for 39 per cent of industrial production and 35 per cent of national export and provided full time employment to over 29 million persons by the end of March 2006. The contribution made by the SSI sector in absolute terms could be seen in the Table 4.2

4.11 During the 5 year period 2000-01 to 2005-06 number of small scale industries have increased from 101.1 lakhs to 123.42 lakhs and employment from 239 lakhs persons to 295 lakhs persons The sector recorded an annual growth of 4.4 per cent in units, 8.2 per cent in output and 5.2 per cent in employment during the same period..

4.12 In view of the important role played by SSIs in the non-farm unorganised sector, it is essential to look into the status of flow of credit to the SSIs from the prime source of credit to the sector viz. Scheduled Commercial Banks

4.13 Despite the potential of and the demand on the unorganised sector for employment generation and poverty reduction, this sector has not received a focused, singular and national mission type attention as far as adequate credit at affordable rates and developmental support are concerned. Moreover there is clear indication that there is a decline in credit to 'Small Scale Industries' to which micro enterprises form an important constituent.

4.14 There is a continuous decline in SSI credit as percentage to Gross Bank Credit of the scheduled

Table 4.2: Status and Contribution of SSIs in India
(Units and Employment in lakhs, Production and Exports in Rs. crores)

Year	No. of Registered Units (Lakhs)	No. of Unregistered Units (Lakhs)	TotalUnits (Lakhs)	Production (Rs. Crore)		Employ-ment (Lakhs)	Export (Rs. Crores)
				Constant prices) (Base 1993)	Current Prices		
2000-01	13.10	88.00	101.10	1,84,428	2,61,297	239.09	69,797
2001-02	13.75	91.46	105.21	1,95,613	2,82,270	249.09	71,244
2002-03	15.91	93.58	109.49	2,10,636	3,11,993	260.13	86,013
2003-04	16.97	96.98	113.95	2,28,730	3,57,733	271.36	97,644
2004-05	17.53	101.05	118.59	2,51,511	4,18,263	282.57	124,417
2005-06	18.71	104.71	123.42	2,77,668	4,76,,201	294.91	NA

Source : Ministry of MSME, Office of DCMSME, Annual Report 2006-07.

Table 4.3: Flow of Credit from Scheduled Commercial Banks (SCBs) to SSI and Allied Sectors (Rs. Crores)

Year	Gross Bank Credit (GBC)	Credit to SSIs	SSI credit as per cent of GBC
1990-91	116,301	17,938	15.42
1991-92	125,592	18,939	15.07
1992-93	151,982	20,975	13.80
1993-94	164,418	23,978	14.58
1994-95	211,560	29,175	13.79
1995-96	254,015	34,246	13.48
1996-97	301,698	38,196	12.60
1997-98	352,696	45,771	13.00
1998-99	399,436	51,679	12.90
1999-00	475,113	57,035	12.00
2000-01	558,766	60,141	10.76
2001-02	680,958	67,107	9.85
2002-03	778,043	64,707	8.31
2003-04	902,026	71,209	7.89
2004-05	1045,954	83,498	7.98
2005-06	1443,920	101,385	7.02
2006-07	1841,978	116,908	6.34

Source: RBI, Handbook of Statistics on Indian Economy 2005-06; RBI, Annual Report, 2006-07.

commercial banks from 15.42 per cent in 1990-91 to 6.4 per cent in 2006-07 (Table 4.3). Further, during the last 6 years itself the credit to SSI sector has declined from 10.76 per cent of Gross Bank Credit in 2000-01 to 6.34 per cent in 2006-07. The status of credit to Micro Enterprises also tells the same story as could be seen from the Table 4.4

4.15 Micro enterprises have received about 3 per cent of Gross Bank Credit (GBC) during 2002-03 to 2004-05. Further, against the stipulation that micro enterprises should get 60 per cent of the total credit to SSI, in reality they have been getting just about 40 per cent. In fact, during the year 2004-05 it was much lower at 34 per cent. Within this unorganised non-farm sector, the most vulnerable segment is the smaller sized micro enterprises with investment up to Rs. 5 lakhs. This sector received just about 2.2 per cent of GBC from SCBs and 3 per cent of the GBC from three major sources namely Scheduled Commercial Banks (SCBs), Regional Rural Banks (RRBs) and Urban Co-operative Banks (UCBs) as given in Table 4.5.

4.16 However, as per the Commission's definition, unorganised sector enterprises include those enterprises, which are engaged in manufacturing, business and trade, etc. The Commission has made an independent estimate of the credit flow in to this growth segment with the help of credit data from SCBs, RRBs and UCBs which constitute over 95 per cent of institutional credit of this sector. Estimates for the year 2004-05 to 2006-07 are given in the Table 4.5.

Table 4.4: SCB's Credit to Micro Enterprises (Rs. Crore)

Sl.No	Segment of Credit	2002-03	2003-04	2004-05
1	Gross Bank Credit	7,78,043	9,02,026	10,45,954
2	Credit to SSI	64,707	71,209	83,498
3	Credit to Micro Enterprises with investment in P&M upto Rs. 5 lakh	15,080	13,677	14,482
4	3 as percentage of SSI credit	23.3	19.20	17.34
5	Credit to Micro Enterprises with investment in P&M between Rs. 5 lakh and Rs. 25 lakh	13,896	14,870	14,048
6	5 as percentage of SSI credit	21.4	20.9	16.82
7	Credit to Micro Enterprises with investment in P&M upto Rs. 25 lakh (3+5)	28,976	28,547	28,530
8	7 as percentage of SSI credit	44.8	40.1	34.16
9	7 as percentage of GBC	3.7	3.1	2.7

Source: RBI, Statistical Tables Relating to Banks in India, 2004-05; 2005-06

Table 4.5: Estimated Institutional Credit to Non-farm Unorganised Enterprises

Segments of Credit	Credit Advanced (Rs. Crore)				Share in total credit (per cent)			
	As on March 2005							
	SCBs	RRBs	UCBs	Total	SCBs	RRBs	UCBs	Total
Total Credit Advanced	1,045,954	31,803	66,874	11,44,631	100	100	100	100
Below 5 lakh	22,982	5,657	8,238	3,6877	2.2	17.8	12.3	3.3
5 to 25 lakh	22,302	0	4,119	26,421	2.1	0	6.2	2.3
Total up to 25 lakh	45,284	5,657	12,357	63,298	4.3	17.8	18.5	5.6
	As on March 2006							
	SCBs	RRBs	UCBs	Total	SCBs	RRBs	UCBs	Total
Total Credit Advanced	14,43,920	36,050	70,379	15,50,349	100	100	100	100
Below 5 lakh	31,726	5,451	9,772	46,949	2.2	15.1	13.9	3.1
5 to 25 lakh	30,787	0	4,886	35,673	2.1	0	6.9	2.3
Total up to 25 lakh	62,514	5,451	14,658	82,623	4.3	15.1	20.8	5.4
	As on March 2007							
	SCBs	RRBs	UCBs	Total	SCBs	RRBs	UCBs	Total
Total Credit Advanced	18,41,978	48,043	73,898	19,63,919	100	100	100	100
Below 5 lakh	40,472	8,546	10,261	59,279	2.2	17.8	13.9	3
5 to 25 lakh	39,275	0	5,130	44,405	2.1	0	6.9	2.3
Total up to 25 lakh	79,747	8,546	15,391	1,03,684	4.3	17.8	20.8	5.3

Note: Since separate data on credit to NFUE are not being maintained by the RBI and the Banks these have been estimated on the basis of available data and following assumptions:

(i) NFUEs are assumed to consist of micro enterprises engaged in manufacturing (up to investment of Rs. 25 lakhs in P&M), cottage and village industries, artisan units and units engaged in services, small business, retail trade, road and water transport, professional self-employed persons and industrial estates up to a stipulated investment ceiling of Rs. 25 lakhs.

(ii) It is estimated that SCBs, RRBs, UCBs taken together account for 95 per cent of the total institutional credit to unorganised sector enterprises. The contribution of other agencies like SIDBI, SFCs and SIDCs are insignificant and more over they cater to the upper segment of the small and medium enterprises.

(iii) SCBs maintain separate data for credit to micro enterprises up to Rs. 5 lakhs and up to Rs. 25 lakh in P&M engaged in manufacturing. However they do not maintain separate data in these categories for credit to service, business and trade. As such, this has been worked out on the basis of micro enterprises engaged in manufacturing share to SSI credit.

(iv) In the case of RRBs entire credit to artisans, small industries and small business has been taken as micro enterprise credit below Rs. 5 lakh of investment since these are small sized rural units.

(v) In the case of UCBs credit to this segment has been apportioned on the basis of RBI guidelines to co-operatives that 60 per cent of the total advances should go to priority sector and 40 per cent to units with investment up to Rs. 5 lakhs and 20 per cent to units with investment up to Rs. 25 lakhs.

(vi) Since detailed data in the case of SCBs are available only for 2004-05, the same share has been maintained for the subsequent years.

(vii) The share of RRBs and UCBs for the year 2006-07 has been taken out of the better shares between 2004-05 and 2005-06.

Sources: RBI, Report on Trend and Progress of Banking in India 2005-06; Statistical Tables Relating to Banks in India 2005-06; SIDBI, Annual Report, various years; RBI Hand Book of Statistics on The Indian Economy, various years.

4.17 It is further disconcerting to note that this paltry 2.2 per cent credit had gone to only 4.2 per cent (or 2.4 million) of such small unorganised sector enterprises, out of the total 58 million units in 2007, despite a banking network of more than 75,000 branches of Scheduled Commercial Banks including RRBs in the country. Even for the SSI sector as a whole, the overall credit from scheduled commercial banks has declined from 15.4 per cent of gross bank credit in 1990-911 to 6.3 per cent in 2006-07. Another disturbing feature is the substantial piggy backing of the loans at the lower segment of the unorganised sector enterprises with investment of less than Rs. 5 lakhs on to credit-cum-subsidy linked self-employment schemes such as, PMRY, REGP, SGSY, USEP etc. implemented by the Government, where banks are confident of a part of the loan advanced coming back to them in the form of subsidy for margin money. A portion of such loans is also those, which have been advanced under SHG-Bank Linkage Programme. It is estimated that total credit under the Government sponsored programme was about Rs. 6000 crores and under SHG-Bank Linkage Rs. 18000 crores in 2006-2007.

4.18 It is pertinent to mention that the culture of micro finance is gaining pace in India. The volume of micro finance increased from about Rs. 200 crores five years back to Rs. 18,000 crores at present. But this is significantly below the present requirement of more than Rs. 50, 000 crores. This shows that, on the whole, there exists a large gap in the demand for and supply of credit to these unorganised small size enterprises. It may be mentioned here that even though credit is made available to the poor through micro credit, it is by and large, limited to consumption and production loans without asset creation, and hence, unsustainable.

4.19 It is thus obvious that banks were not able to meet adequately the credit requirements of the unorganised sector. The reluctance of the banks is primarily reflective of their high-risk perception of the sector, high transaction cost for small loans and non-stipulation of any priority sector target for the sector. The reluctance of the bankers is further vindicated by the fact that despite the availability of credit guarantee facility by CGTME up to Rs. 25 lakhs loan (raised to Rs. 50 lakhs from February 2007), the coverage is very limited. As on March 31st 2007, only about 0.07 million units were found covered under credit guarantee. It was also found that, in spite of the RBI guidelines that loans up to Rs. 5 lakhs should be given without collaterals, available data reveals that only 26 per cent of such loans were advanced without collaterals. In other words, a major productive sector of our economy, which is located in rural and semi urban areas, is still deprived of financial inclusion in letter and spirit.

4.20 Since micro enterprises constitute just one of the components of the non-farm unorganised sector, it would be appropriate to look into the flow of credit to all the components of the non-farm unorganised sector. These consist of: (i) Cottage; Village and Tiny Industries; (ii) Small Road and Water Transport; (iii) Retail Trade; (iv) Small Business; (v) Professional Self- employed; and (vi) Advances to SHGs. The flow of credit to this segment is given in Table 4.6.

Table 4.6: Flow of Scheduled Commercial Bank's Credit to Unorganised Sector 2004-05

	Rs Crore
Net Bank Credit	971,809
Priority Sector Credit	4,00,775
Unorganised Sector Credit	71,311
Cottage, Village, Tiny Industries	20,403
Small road & water transport	9,810
Retail trade	22,364
Small Business	11,038
Professional self employed	5,621
Advances to SHGs	2,075

Source: RBI, Statistical Tables Relating to Banks in India 2005-06.

4.21 Schemes of commercial banks' credit to the unorganised sector constituted 7.3 per cent of the total Gross Bank Credit and 17.8 per cent of the total advances to the priority sector flowing to various regions. Table 4.7 gives their regional distribution.

4.22 It emerges from the table that the North Eastern Region received the lowest amount of credit i.e. 1.07 per cent of the total priority sector and 2.41 per cent of the total unorganised sector credit. The best performance came from the Southern Region, which received 31.68 per cent of the total priority sector credit and 31.38 per cent of the total unorganised sector credit.

4.23 In the sixties and seventies, the small scale industries were the preferred route of financing for the commercial banks. However, since 1992, (after implementation of the Narasimham Committee recommendations) there has been a steady and drastic fall in the share of bank credit to the small scale industries.

Table 4.7: Scheduled Commercial Banks
Region-wise Flow of Credit for Unorganised Sector 2004-05

Rs. Crores

	Total Advances under Priority Sector		Total unorganised sector Advances	
	No. of A/cs	**Amt**	**No. of A/cs**	**Amt**
Northern Region (7 States)	**42,18,281**	**88,574**	**10,12,097**	**12,679**
Percentage Share to total	12.31	22.10	12.42	17.78
North-Eastern Region (7 States)	**5,54,184**	**4,283**	**2,54,466**	**1,718**
Percentage Share to total	1.62	1.07	3.12	2.41
Eastern Region (6 States)	**45,83,390**	**37,107**	**17,52,510**	**9,918**
Percentage Share to total	13.38	9.26	21.50	13.91
Central Region (4 States)	**58,44,645**	**49,327**	**13,75,904**	**10,384**
Percentage Share to total	17.06	12.31	16.88	14.56
Western Region (5 States)	**38,17,328**	**94,512**	**10,66,453**	**14,236**
Percentage Share to total	11.14	23.58	13.08	19.96
Southern Region (6 States)	**1,52,40,298**	**1,26,972**	**26,89,078**	**22,376**
Percentage Share to total	44.49	31.68	32.99	31.38
Total	**3,42,58,126**	**4,00,775**	**81,50,508**	**71,311**

Source- RBI, Statistical Tables Relating to Banks in India, 2005-06

Table 4.3 brings out the extent of decline in SSI lending by the scheduled commercial banks, from 15.4 per cent in 1990-91 to 6.3 per cent in 2006-07.. The decline in credit to SSI is mainly on account of a dilution of the priority sector lending programme of the banks. This becomes evident from a close look at the Scheduled Commercial Banks credit data for the year 2005-06 (Table 4.8).

4.24 From the Table 4.8 it appears that large industries which account for 50 per cent of the industrial production received 31.06 per cent of the bank credit, and the small enterprises which account for the remaining 50 per cent of industrial production received only 7.02 per cent of the bank credit from the scheduled commercial banks.

4.25 Secondly, it emerges that priority sector credit constituted only 35.31 per cent of the total bank credit against the stipulated 40 per cent.

Table 4.8: Scheduled Commercial Banks' Credit 2005-06 (Rs. Crores)

	AmountTotal	Percentage
Total Bank Credit	14,43,920	100.00
Credit to large industries (which account for 50 per cent of industrial production)	4,48,555	31.06
Credit to small scale industries and allied activities (which account for the remaining 50 per cent of industrial production)	1,01,385	7.02
Priority Sector		
Total Priority Sector	5,09,910	35.31
Agriculture	172,292	11.93
SSIs (including allied activities)	101,385	7.02
Housing	133,360	9.23
Transport Operators	11,951	0.8

Source- RBI, Statistical Tables Relating to Banks in India, 2005-06.

Further, it is apparent that the agriculture sector received only 11.92 per cent of the bank credit against the stipulated 18 per cent. It can also be seen that a major chunk of the priority sector lending went to the housing sector, 9.23 per cent of the bank credit. This credit is at the cost of agriculture and the SSI sector. Thus, these sectors are the major sufferers due to a dilution of the priority sector lending.

4.26 The status of credit flow from scheduled commercial banks to unorganised enterprises is still dismal even if we consider the entire loans given to retail trade small business, small road and water transport, industrial estate and loans to professionals and self-employed as loans to unorganised sector along with that separately given to micro enterprises engaged in manufacturing, as can be seen from Table 4.9.

of the credit to units below Rs. 5 lakhs of loan are mostly through government sponsored programmes like PMRY, SGSY, etc. and the credit under SHG-Banking Linkage.. Thus, it appears that on their own initiative commercial banks virtually neglected the non-farm unorganised enterprises. This segment of unorganised enterprises accounting for about 30 per cent of industrial production and providing employment to about 70 million persons received just 2.3 per cent of the commercial banks' credit in 2004-05. This is despite the existence of over 69,000 branches of scheduled commercial banks, including 14,500 of RRBs, in addition to the cooperative banks' branches and network of 1,09,924 rural and 1853 urban banks/ institutions, 22 lakh SHGs, 800 MFIs, 56 branches of SIDBI and 18 SFCs. Various studies and surveys reveal that of the major problems faced by the non-farm unorganised enterprises is the extremely inadequate access to institutional credit. In our view, had the sector received adequate credit, it would have created much larger employment, output and exports given its untapped immense potential.

Table 4.9: Scheduled Commercial Banks' Credit 2004-05 to the Non-farm Unorganised Sector (Rs. Crores)

Total Bank Credit	9,71,809
Credit to Tiny Units (with investment in P& M below Rs. 5 lakhs)	14,482
Credit to Tiny Units (with investment in P & M between Rs. 5 lakhs and Rs. 25 Lakhs*	14,048
Credit for retail trade, small business small transporters, industrial estate, etc.*	49,133

*Entire credit advanced to retail trade, small business, small road and water transporters, industrial estates and professional self-employed.
Source: RBI, Statistical Tables Relating to Banks in India- 2004-05 and 2005-06.

4.27 Thus, unorganised enterprises received a total credit of Rs.77,663 crores from the commercial banks. This was 8.0 per cent of the gross bank credit. However, if we take just advances to units up to Rs. 5 lakhs in plant and machinery (micro enterprises) engaged in manufacturing it was as low as 1.5 per cent of the gross bank credit of the scheduled commercial banks and 17.3 per cent of SSI credit. Taking the same share for micro service/business units, the total credit to units with investment up to Rs. 5 lakhs comes to Rs. 22982 crores (Rs. 14,482 crores plus Rs. 8500 crores) Thus the lower segment of non-farm sector received less than 2.3 per cent of the net bank credit in 2004-05. A significant part

Neglect of the Weakest among NFUEs

4.28 Artisans and village industries form the weakest segment of NFUEs. This segment deserves special attention from the point of view of protecting and sustaining their sources of livelihood. However, they have been experiencing persistent neglect from the commercial banks despite many policy guidelines. Table 4.10 shows that not even one per cent of the credit has gone to the

Table 4.10: SCBs' Outstanding Credit to Artisans and Village Industries (Rs. Crores).

Year	No. of Accounts	per cent to All India	Amount	per cent to All India
March 1990	21,51,263	4.0	926	0.9
March 1995	24,15,484	4.2	1,129	0.5
March 2000	20,13,171	3.7	2,677	0.6
March 2005	12,88,321	1.7	6,149	0.6

Source: RBI, Statistical Returns of Scheduled Commercial Banks, various years.

weakest segment among the NFUEs.

Other Credit Related Problems

4.29 Other disturbing trends noticed with regard to credit to small enterprises are: (i) Inadequate working capital which currently ranges between 10 per cent and 13 per cent against the RBI norm of 20 per cent of the projected turnover to be given as working capital. (ii) Insistence on collaterals even on a loan up to Rs. 5 lakhs, in spite of the RBI guidelines (loans to the SSIs without collaterals, out of the total loans below Rs. 5 lakhs, to SSI was 25.9 per cent in 2004-05). (iii) Neglect of the small loan segment, since the share of loans below Rs. 25,000 has declined from 21 per cent of the total outstanding of scheduled commercial banks' loans in June 1985, to 3.7 per cent in March 2005. (iv) Banks' disinterest in advancing loans under the Credit Guarantee Scheme which is available for loans up to Rs 50 lakhs. During the last 6 years of this scheme, the quantum of loans advanced under guarantee cover does not exceed to Rs. 1705 crores as per data for March, 2007)

Credit to Weaker Sections

4.30 Credit to weaker sections comes under the priority sector lending policy of the banks for which a quota of 10 per cent of the net bank credit is fixed. Weaker sections consist of various categories of beneficiaries such as small and marginal farmers, artisans, village and cottage industries up to Rs. 50,000 per borrower, beneficiaries under SJSY, SJSRY advances to SC, ST and SHGs etc. The status of credit to weaker sections is given in the Table 4.11.

4.31 It emerges from Table 4.11 that the target of 10 per cent of net bank credit to the weaker sections has never been achieved either as banking through public sector banks or combined loaning of the scheduled commercial banks. Even for the public and private sector banks it has always been less than 10 per cent and shows a declining trend, from 9.5 per cent of net bank credit in 1990-91 to 6.5 per cent in 2005-06.

4.32 From the foregoing paragraphs in this chapter, it could be seen that credit to micro and small enterprises and weaker sections has suffered particularly after 1990-91.

Opportunity Lost

4.33 Had the SSI sector received the same percentage of gross bank credit as it got between 1994-95 and 1999-2000 i.e. 15 per cent of the net bank credit, the actual credit to this sector would have been Rs 203,190 crores instead of Rs. 101385 crores in 2006. The addition of about Rs. 1,02,000 crores would have doubled the employment, output and export. On the basis of current statistics of production, employment and exports, we find that the nation lost about 30 million of mandays employment, about Rs. 5,00,000 crores of production and about Rs. 1,50,000 crores of exports . A sector which has the potential to grow at a much higher rate than 9 to 10 per cent and create large employment was denied this opportunity due to the short supply of credit.

Table 4.11: Commercial Banks Credit to Weaker Sections during 1991-2006 (Rs. Crores)

Year	Public Sector Banks	Per cent of Net Bank Credit	Total Public and Private Sector Banks	Per cent of Net Bank Credit
1991	10,260	9.7	10,506	9.5
1992	10,881	9.7	11,150	9.4
1993	11,865	8.9	12,148	8.7
1994	12,779	9.1	13,079	8.7
1995	13,918	8.2	14,257	7.8
1996	15579	8.4	15,960	7.8
2001	24,899	7.2	25,858	6.4
2002	28,970	7.3	30,116	6.5
2003	32,303	6.7	33,526	5.9
2004	41,589	7.4	43,084	6.4
2005	63,492	8.8	65,405	7.4
2006	78,373	7.7	82,282	6.5

Note: Data between 1997 and 2000 are not available
Source: RBI,Report on Trend and Progress of banking in India, various issues.

5 Status of Micro Finance in India

Introduction

5.1 Microfinance has come to mean the 'provision of thrift, credit and other financial services and products of very small amounts to the poor in rural, semi-urban and urban areas for enabling them to raise their income levels and improve living standards' (NABARD, 1998) . It is, however, understood that the Micro Finance Institutions (MFIs) provide other non-credit services as well such as capacity building, training, marketing of the products of the SHGs, micro-insurance etc.

5.2 Microfinance has the potential to become an important component of successful and sustainable poverty alleviation programme. It is gaining popularity in several developing countries. The Commission does not consider microfinance as a substitute for increasing the access to credit for the poor from the banking system but as a component to serve the needs of the poorer sections requiring small amounts of loans. It is in this perspective that we examine the status and potential of micro finance in India to meet the credit gap being faced by the NFUEs. By the end of 2003, about 80 million clients across the world were serviced by approximately 2900 microfinance institutions. India's share in the total was 20 million or 25 per cent of the world total. Latest statistics show that this number has increased to 40 million.

Types of Microfinance Models in Various Countries

5.3 Broadly, the microfinance methodologies could be classified into the following five models:

Grameen Model

5.4 People form groups of three to eight persons on the condition that each of them would be assuming responsibility for the lending and other financial operations for the other members of the group. Lending as well as repayment is directly to and from the individuals but with the guarantee of the other group members. Grameen Bank in Bangladesh has perfected this technique and it has been adopted in many countries with modifications to suit the local conditions and cultures. The programmes of Banco Sol in Bolivia and most of the solidarity group models in Latin America follow this methodology.

The Group Approach

5.5 The group approach delegates the entire financial process to the group rather than the financial institutions. Savings, loans and loan repayments are taken care of at the group level. These groups are in turn linked to a financial or a microfinance institution for sourcing of additional funds as well as depositing their savings. Best examples of this type of arrangement are the Self-Help Groups- Bank Linkage Programme in India, the PHBK project in Indonesia and the Chikola groups of K-REP in Kenya.

Individual Credit

5.6 Credit given directly to the individuals also forms a part of the microfinance technology. Many institutions have adopted the individual credit route for microfinance where loan appraisal, loan disbursements and loan repayments as well as saving collections are all done on an individual basis. These technologies are predominant in the

BRI-Unit Desa in Indonesia as well as priority sector lending by banks in India especially the regional rural banks and cooperative banks.

Community Banking

5.7 This model is, to an extent, an expansion of the group approach where the basic financial necessities of the poor especially the women are met through the community banking system. The community or village banks are organised with 30-50 members. These banks in turn borrow from the programme implementing institution and on-lend to the members. A prominent example of this type of microfinance institution is the Village Bank of FINCA in Latin America, which had been replicated in Africa and central Asia.

Credit Unions and Cooperatives

5.8 Credit unions and cooperatives are member-owned organizations providing credit and other financial services to their members. The apex bodies provide technical and financial support to the federating units. SANASA of Sri Lanka is a successful example of rural credit cooperatives as microfinance service provider.

Beginnings of Microfinance in India

5.9 The first official interest in informal group lending in India took shape during 1986-87 on the initiative of NABARD, which initiated certain research projects in the late 1980s on Self-Help Groups (SHGs) as a channel for delivery of microfinance. Amongst these the Mysore Resettlement and Development Agency (MYRADA) sponsored action research project on "Savings and Credit Management of SHGs" was partially funded by NABARD in 1986-87., In collaboration with some of the member institutions of the Asia- Pacific Rural and Agricultural Credit Association (APRACA), NABARD undertook a survey of 43 NGOs in 11 states in India in 1988-89, to study the functioning of microfinance SHGs and their collaboration possibilities with the formal banking system. Both these research projects threw up encouraging possibilities and NABARD initiated a pilot project called the SHG Linkage Project (NABARD 1991).

5.10 By then micro financing by 'non-formal' financial organisations had already started. Self-Employed Women's Association (SEWA) of women of petty trade groups was established in 1974 in Gujarat on cooperative principles. The earliest steps in microfinance in India can be traced to this initiative undertaken for providing banking services to the poor women employed in the unorganised sector in Ahmedabad. In 1980 SEWA set up a bank by registering it as an urban cooperative bank. Since then the bank has been providing banking services to the poor and the self-employed, working as hawkers, vendors, domestic servants, etc. Another association of working women in unorganised sector, Working Women's Forum (WWF), started promoting working women's cooperative societies in Tamil Nadu since 1980. In Kerala another model called Kutumbashri has been working since early nineties on a federated organizational model by forming Self-Help Groups of poor women and linking them up with banks for accessing micro finance. This is being actively promoted by a Government Sponsored Mission and currently has a membership of over 3 million. A similar Government supported programme called Velugu in Andhra Pradesh has been organizing similar women SHGs. At the national level, while the SHG movement has had a longer history through NGOs' work at the community level, the linking of SHGs to microfinance is of a more recent origin. It is only in the late 1980s that a few NGOs initiated experimentation in channelling microfinance through SHGs mobilised by them. MYRADA mobilised multi-purpose SHGs around group savings and introduced credit. Professional Assistance for Development Action (PRADAN) in its Madurai project, formed women's SHGs with the explicit objective of mobilising savings and rotating this as credit to group members, eventually towards the goal of forming a community banking system. There are several smaller groups and organizations now engaged in micro-finance sector in different parts of the country.

5.11 Pilot Project of NABARD: Before the commencement of its pilot project NABARD held extensive consultations with the Reserve Bank of India. This resulted in the RBI's policy circular in 1991 to all commercial banks to participate and extend finance to SHGs (RBI 1991). NABARD also issued a broad set of flexible guidelines in February 1992, to the formal rural banking system, explaining the project's modalities. The project was extended to the regional rural banks and cooperative banks, in addition to the commercial banks in 1993. The main objectives of this project were: to evolve supplementary credit strategies for meeting the credit needs of the poor by combining flexibility, sensitivity and responsiveness of the informal credit system.

Progress of SHG-Bank Linkage Programme

5.12 No doubt, micro-credit movement has shown significant potential in India, and with intensive official support, the coverage has rapidly expanded in recent years. The evolution of SHG Bank-Linkage Programme could be viewed in terms of three distinct phases, viz. (i) pilot testing during 1992 -1995, (ii) mainstreaming during 1996 - 1998 and (iii) expansion from 1998 onwards. The number of SHGs which was 255 in 1992 – 93, has increased to 2.24 million by the end of March, 2006 and the volume of credit have increased from Rs. 29 lakhs to Rs. 11398 crores during the same period. Almost all scheduled commercial banks and regional rural banks (RRBs) have embraced it as an important banking programme. Available information shows that over 22.38 lakhs SHGs have obtained bank loans aggregating Rs 11,398 crores for about 330 lakhs poor households with the refinance support of Rs 4,157 crores from NABARD at the end of March 2006. Likewise, the cumulative assistance under the SIDBI scheme has aggregated Rs 422 crores for 15 lakhs poor households at the end of March 2005.

5.13 However, inspite of the impressive growth there exists a vast gap in demand and supply of credit. As per a study by SADHAN, the micro credit requirement was assessed at Rs. 50,000 crore for the year 1999 – 2000. By adding other requirements such as housing loans, education loans and micro-enterprise loans, the upper ceiling of loan requirements was assessed at Rs. 2 lakh crores of micro credit. At the present rate of cost escalation and taking the base as Rs.50,000 crores, it is estimated that the current minimum requirements of micro credit may be Rs. 70,000 crores. As against this, the supply is not more than Rs. 11,000 crores (March 2006).

5.14 SHGs comprising only women members constituted 90 per cent of the total; with of course timely loan repayment (95 per cent).

5.15 There has been substantial regional concentration of SHGs, with the southern states occupying a pride of place – accounting for 54 per cent of the total SHGs credit and 75 per cent of the bank loans disbursed as at the end of March 2006. Andhra Pradesh alone accounted for 26 per cent of the SHGs credit and 38 per cent of the cumulative bank loans as at the end of March 2006. This situation was more acutely concentrated until the recent period. It is claimed to be undergoing a change as may be seen in the latest data provided by NABARD (Table 5.1). It emerges that 13 northern, western and eastern states share in SHG growth has increased from 30.7 per cent of total in 2002 to 44.9 per cent in 2006. However, it is important to note that for the BIMARU states, the proportion of SHGs in the all-India total has remained at about 15-16 per cent even at the end of March 2006.

5.16 SHGs directly formed and financed by banks still constitute only 20 per cent of the total as at end-March 2006; an overwhelming 74 per cent are formed by NGO organisations but directly financed by banks and another 6 per cent are financed by banks using financial intermediaries.

5.17 Southern States which commanded over 64 per cent of SHGs in 2002, had to their share more than 54 per cent of SHGs even in 2006 (Table 5.1). The share of 13 financially excluded states has also increased in recent years from 30.7 per cent in 2002 to about 45 per cent in 2006.

Microfinance outside SHG-bank Linkage

5.18 The SHG- Bank Linkage Programme has expanded at a fast pace in India to evolve into the largest microfinance programme in the world. By far it is the major microfinance programme in India. However, there are also MFIs operating in the country following a variety of saving and credit technologies. As indicated earlier, even before the SHG method was perfected, many NGOs were using a variety of delivery mechanisms for providing credit services to the poor with financial support from external donors and later by apex institutions including the Rashtriya Mahila Kosh set up by the government, the SIDBI Foundation for Micro Credit and NABARD. Since 2000, commercial banks including regional rural banks are providing funds to MFIs for on-lending to poor clients.

5.19 While there is no published data on MFIs in India, their number is estimated to be around 800 according to reliable sources. But not more than 10 MFIs are reported to have an outreach of more than 1,00,000 microfinance clients. An overwhelming majority of the MFIs are operating on a smaller scale with clients ranging between 100 and 1,500 per MFI. The geographical distribution of MFIs is lopsided with concentration in the southern states. It is estimated that the share of MFIs in the total microfinance business in the country is about 8 per cent (Satish, 2005). While most are registered under Societies Registration Act, some are functioning as non-bank financial companies.

Table 5.1: Cumulative Growth in SHG-Bank Linkage by States (As on March 31st) (Number of SHGs)

State	2002	2003	2004	2005	2006
Assam	1,024	3,477	10,706	31,234	56,449
Bihar	3,957	8,161	16,246	28,015	46,221
Chhattisgarh	3,763	6,763	9,796	18,569	31,291
Gujarat	9,496	13,875	15,974	24,712	34,160
Himachal Pradesh	5,069	8,875	13,228	17,798	22,920
Jharkhand	4,198	7,765	12,647	21,531	30,819
Maharashtra	19,619	28,065	38,535	71,146	1,31,470
Madhya Pradesh	7,981	15,271	27,095	45,105	57,125
Orissa	20,553	42,272	77,588	1,23,256	1,80,896
Rajasthan	12,564	22,742	33,846	60,006	98,171
Uttar Pradesh	33,114	53,696	79,210	1,19,648	1,61,911
Uttaranchal	3,323	5,853	10,908	14,043	17,588
West Bengal	17,143	32,647	51,685	92,698	1,36,251
Total for 13 states	1,41,804	2,49,462	3,97,464	6,67,761	10,05,272
	(30.7)	(34.7)	(36.8)	(41.2)	(44.9)
Southern States	3,17,276	4,63,712	6,74,356	9,38,941	12,14,431
	(68.8)	(64.7)	(62.5)	(58.0)	(54.3)
BIMARU States	57,616	99,870	1,56,397	2,52,774	3,63,428
	(12.5)	(13.9)	(14.5)	(15.6)	(16.2)
All-India Total	4,61,478	7,17,360	1,079,091	1,618,456	22,38,565

Note: Figures in brackets are the percentages to All-India totals
Source: NABARD, Progress of SHG - Bank Linkage in India, Various Issues.

5.20 Currently there are five organisational forms of the MFIs, viz., Trusts; Societies; Cooperative Societies; Not-for-Profit Companies and Non-Banking Finance Companies. There are also instances of large corporates undertaking micro-credit activity as a part of their operations. Table 5.2 describes the various legal forms under which MFIs operate in India.

Table 5.2: Legal Forms of MFIs in India

Type of MFIs	Estimated Number*	Legal Acts under which Registered
Not- for- Profit MFIs		
(a) NGO-MFIs	400 to 500	Societies Registration Act, 1860 or similar Provincial Acts Indian Trust Act, 1882
(b) Non- Profit Companies	10	Section 25 of the Companies Act, 1956
Mutual Benefit MFIs		
Mutually Aided Cooperative Societies (MACS) and Similarly Set up I Institutions	200 to 250	Mutually Aided Cooperative Societies Act enacted by State Governments
For- Profit MFIs		
Non-Banking Financial Companies (NBFCs)	6	Indian Companies Act, 1956 Reserve Bank of India Act, 1934
Total	**700-800**	

Note: * The estimated number includes only those MFIs, which are actually undertaking lending activity.
Source: Adapted from the Report of the Task Force on Supportive Policy and Regulatory Framework for Microfinance (NABARD 1999) and updated in (Satish, 2005)

NGO-MFIs

5.21 A large number of NGOs undertook the task of financial intermediation. Majority of them are registered as a trust or a society. Many NGOs have also helped SHGs organise themselves into federations which are also registered as trusts or societies. Many of them are performing non-financial functions like social and capacity building activities, facilitate training of SHGs, undertake internal audit and promote new groups while some of them act as apex level financial service providers. The NGO-MFIs vary significantly in their size, philosophy and approach. While these institutions are strong on social and community capacity building, they are inexperienced as far as financial management issues are concerned. Therefore, it has been argued by some that these NGOs are structurally not the right type of institutions for undertaking financial intermediation activities, as by-laws of these institutions are generally restrictive in allowing any commercial operations. These organisations by their charter are non-profit organisations and as a result face several problems in borrowing funds from higher financial institutions. The NGO-MFIs, which are large in number, are still outside the purview of any financial regulation. It is contended by many that these are the institutions for which policy and regulatory framework would need to be established.

Non-Profit Companies as MFIs

5.22 Many NGOs feel that combining financial intermediation with their core competency activity of social intermediation is not the right path. It is felt that a financial institution or a company may be set up for this purpose. Further, MFIs are to demonstrate that banking with the poor is indeed profitable and sustainable; it has to function as a distinct institution so that cross subsidisation can be avoided. On account of these factors, NGO-MFIs are of late setting up separate non-profit companies for their microfinance operations. Such an MFI is prohibited from paying any dividend to its members.

Mutual Benefit MFIs

5.23 The state cooperative acts did not provide for an enabling framework for the emergence of business enterprises owned, managed and controlled by the members for their own development. Several state governments therefore enacted the Mutually Aided Cooperative Societies (MACS) Act to enable promotion of self-reliant and vibrant cooperative societies based on thrift and self-help. MACS enjoy the advantages of operational freedom and virtually no governmental interference because of the provision that societies under the Act cannot accept share capital or loan from the state government. Many of the SHG federations, promoted by NGOs and development agencies of the state government have been registered as MACS. The RBI does not regulate MACS, even though they may be providing financial services to their members.

For Profit MFIs

5.24 Non Banking Financial Companies (NBFCs) are those companies registered under the Companies Act, 1956 and regulated by the RBI which introduced a new regulatory framework for the NBFCs who want to accept public deposits. All the NBFCs accepting public deposits are subjected to capital adequacy requirements and prudential norms. There are only a few MFIs in the country that are registered as NBFCs. Many MFIs view NBFCs as a preferred legal form and are aspiring to become NBFCs but they are finding it difficult to meet the requirements stipulated by RBI. The number of NBFCs having exclusive focus on microfinance is negligible.

Agency Model – Greater Involvement of Bank

5.25 Based on the recommendations of the Internal Group of RBI to examine Issues relating to Rural Credit and Micro Finance (July 2005), the RBI has issued guidelines on the adoption of agency banking based on two distinct models.

Model A- Business Facilitator Model

5.26 Model A would involve the use by banks of Civil Society Organizations (CSOs) and others for support. These organizations would provide support services for effective delivery of such financial services as (i) borrowers' identification (ii) collection, processing and submission of applications, (iii) preliminary appraisal, (iv) maintenance of the financial products including saving, (v) post sanction monitoring (vi) promotion and nurturing of SHGs and (vii) follow up of recovery. The organizations may include NGOs, farmers clubs, functional cooperatives, IT enabled rural outlets of corporate, postal agents, insurance agents, well functioning panchayats, rural multi purpose/ village knowledge centers, agri clinics / business centers financed by banks, Krishi Vigyan Kendras, KVIC/ KVIB units etc.

Model B- Business Correspondent Model

5.27 Model B would go a step further and allow institutional agents and other external entities to act as business correspondents and support the banks for extending financial services. The business correspondents would function as "pass through" agencies to provide credit related services like disbursal of small value credit and recovery of principal/ collection of interest, sale of micro insurance, mutual fund products, pension products, etc. in addition to functions prescribed in Model A. Based on their performance, they may also be allowed to provide other important financial services like collection of small deposits receipt and delivery of remittances, etc.

5.28 RBI has issued general permission to the banks to engage and pay remuneration to Business Facilitators besides permission to Business Correspondents to undertake banking activities like collection of savings (under section 23 of the Banking Regulation Act) subject to certain terms and conditions. This will help in increasing the outreach of banks for micro finance. RRBs are also to be strengthened as purveyor of rural credit. Sponsor banks have been encouraged to merge the RRBs sponsored by them in order to strengthen them.

Gaps and Weaknesses in Micro Financing in India

5.29 While micro financing is growing at a rapid pace in India, particularly since 2000, there are a few gaps and weaknesses in micro financing in India. Broadly, these are as under:-

- As we have shown in Table 5.1, the micro credit programme is yet to take deep roots in majority of states in the country. Given the limited outreach of NGOs, despite their large number, there is a case for the State Governments to intervene proactively by promoting and supporting the SHGs. The experience of southern states in this regard would provide useful lessons.
- Micro financing, as it is now practiced, consists of small loans (in the range of Rs. 2000-3000), which are nothing more than assistance for consumption smoothening. Given the demonstrated enthusiasm and capacity of the SHGs, there is a case for increasing the loan amount so as to help them to set up / sustain micro enterprises, which could in turn provide regular employment and income to poorer households. The micro financing is in nascent stage and the higher repayment rates are confined to small loans only (say below Rs. 2000-3000).

5.30 The most serious criticism against micro financing is the high rate of interest charged, ranging from 20 per cent to 36 per cent, significantly higher than the highest interest rate charged by the banks from small enterprises, about 15 - 16 per cent. This high interest rate, considered highly unviable even to the strong corporate sector enterprises, deserves to be examined by the government seriously. If the poor have to generate rates of return of more than 34-36 per cent from such small loans, it would not be surprising, if they are forced to fall back on the same source for further loans, this will only create a situation of perpetual indebtedness - defeating the very objective of micro credit.

Livelihood Finance - An approach to Micro Enterprise Financing

5.31 While micro credit serves as a useful complement to the survival strategies of the poor households, it is not for sustainable employment generation and growth and hence is not an ideal instrument of micro enterprise financing. The average loan per unit in micro credit is between Rs. 2,500 and Rs. 3,000 whereas the average requirement of credit for setting up a micro enterprise is not less than Rs. one lakh. Moreover, credit alone is not sufficient for the successful operation of a micro enterprise. The entrepreneur must have the ability to run the business. Moreover, micro credit does not lead to creation of assets which is a basic requirement of the micro enterprise. Many studies show that the impact of micro credit is limited.

5.32 There are some micro credit organizations which have revised their strategies and now offer micro credit along with a whole suite of insurance products covering life, health, crop and livestock. For enhancing productivity, a whole range of agricultural and business development services are being offered to borrowers. For ensuring better prices, alternate market linkages are being facilitated both on the input and output side.

5.33 Estimates show that it will take an investment of Rs. 1 lakh per household to provide the infrastructure, financial and technical support services needed to raise every household above the poverty line. Thus there is need of Rs. 400,000 crores for 40 million poor households.

Recent Initiatives

Committee on Financial Inclusion

5.34 Government of India has constituted a Committee to look into the issues of Financial Inclusion by various credit providers under the Chairmanship of Dr. C. Rangarajan. Based on the Interim Report of the Committee, Finance Minister, in his budget speech 2007-08, has proposed the constitution of two Funds viz. (i) Financial Inclusion Fund and (ii) Financial Inclusion Technology Fund.

Micro Finance Bill

5.35 As promised by the Finance Minister, the Micro Financial Sector (Development and Regulation) Bill has been introduced in the Lok Sabha in the Budget Session (March 2007). The goal of the bill is to provide for the development and orderly growth of micro finance sector in the rural and urban areas under the regulatory ambit of NABARD, which will ensure its management and governance. NABARD would also specify the form and manner in the accounting of business operations of micro finance organisations, other than those accepting thrift services. The limit of loan for individual and small entrepreneurs will be Rs.50,000 and for housing projects, the limit will be Rs.1.5 lakhs. The Bill also provides for the constitution of a corpus called the Micro Finance Development and Equity Fund for the development of the sector.

Commission's Recommendations

- Increased involvement of commercial banks in micro financing is absolutely essential for a sustainable micro financing programme in the country. In order to reduce the transaction cost, the group approach to credit could be adopted by linking the programme with organizations of SHGs
- Constraints which inhibit micro finance to graduate to micro enterprise financing should be removed through: (a) support for building assets to run the enterprises, (b) increasing product mix by adding insurance and money transfer, along with credit and thrift: (c) provision of livelihood finance to meet the essential infrastructure requirements, and (d) capacity building of SHGs, MFIs, NGOs etc so that the beneficiaries take up projects involving value additions as against more production and consumption loans.
- It is necessary to recognise that the focus has to be on extending financial services in both the rural and urban areas for ensuring financial inclusion of all segments of the population. At the same time, the temptation of creating one set of banking and financial institutions to cater to the poor or the unorganised, and another for the rest will have to be restrained. The growth of micro finance has to necessarily be accompanied by the overall growth in mainstream rural finance. The medium to long-term objective should be to ensure inclusion of all the segments in the mainstream institutions while taking advantage of the flexibility of multiplicity of models of delivering a wide range of financial services.
- Public policies ought not to consider micro-finance as a substitute for the series of other public programmes that have significant impacts on the growth processes and reduction of poverty and unemployment. In this light, a comprehensive framework to revive the cooperative credit system, revitalise the Regional Rural Banks, reorient commercial banking system, and remove the hurdles in the working of micro financing initiatives and non-banking financing companies (within the framework of overall financial discipline) need to get a high priority while simultaneously encouraging and enabling the growth of micro-finance movement in India, which has been very successful.

6 Need for Innovative Financing

6.1 The Commission feels that there is a need for innovative financing of non-farm unorganised enterprises for a variety of reasons. The main reasons as we see them are given:

To Bridge the Existing Credit Gap of Debt Financing

6.2 Existing credit flows to small enterprises and other non-farm unorganised enterprises from institutional sources in the form of traditional term loans and working capital are inadequate. There exists a vast credit gap between the demand for and the supply of credit. Hence, innovative finance, other than the traditional bank finance, is required to bridge the credit gap.

Financing through Innovative Instruments

6.3 Non-traditional instruments like venture capital, factory service, bill discount, lease financing, equity finance, etc not only would go a long way in covering some of the critical risks being faced by NFUEs but would also enhance their confidence in functioning in a competitive environment.

Credit to Clusters

6.4 In clusters, small enterprises work in groups and need credit both to meet the individual and collective needs of the firms. An innovative financial instrument is needed since clusters are fast emerging as the strategy for small enterprises development in a large number of emerging economies including India.

6.5 The innovative instruments mentioned above, for financing NFUEs which have emerged in recent years in different part of the world including India are discussed in the paragraphs below. It may, however, be mentioned that these instruments are not popular at the lower end of the micro enterprises for various reasons such as absence of modern managerial and information practices. Financial institutions are required to be more helpful to the lower end of the micro enterprises and should encourage innovative instruments. This calls for extra effort on their part.

Bill Discounting

6.6 For small enterprises that are vendors to large and financially strong organisations, MNCs etc. with a reputation for timely payments can obtain cheap finance under bill discounting at reasonable rates, say lower than Prime Lending Rates. This rate depends on the strength of the buyer and the volume of supplies by the vendor. Such finances are available for short-term periods of 90-120 days. This system does not involve demand for security or collaterals.

6.7 Under the scheme, bills of exchange/promissory notes, arising out of sale/purchase of machinery by industrial concerns in the SSI sector are discounted. Short-term Bill Discounting facility is also provided against inland supply to bills of SSIs to enable them to sell on credit and to encourage the bill culture in the country. The system of Bill Discounting is done by SIDBI, public sector banks, foreign banks, and private banks in India. However, it is not popular because of the high risk involved and the absence of counter-guarantee. High stamp duty also discourages the popularization of this instrument. Mostly, the strong corporate bodies, which accept bills of exchange, are eligible for this facility.

Lease Financing

6.8 Although the business of renting equipment and other items has been in existence for long, the modern concept of equipment leasing has been around only for the last 50-55 years. In a typical lease agreement, a machinery or equipment owner grants the users (the lessees) the right to use equipment for an agreed period of time in exchange for specified payments. Since its modest inception in the United States in the 1950s, it has grown to be a US$ 500 billion industry on a world-wide basis. Approximately one third of the developed and developing countries of the world have some form of cognizable leasing activity. There is, however, a major difference between the traditional and modern leasing systems. This is the emergence of the third party financial element in the modern system.

6.9 Most of the leasing companies exist in Asia, prominent among them being in Japan, Korea, Peoples' Republic of China, Hong Kong, Taiwan, Indonesia, India, Pakistan, Malaysia, Singapore, Thailand, the Philippines and Sri Lanka which have a significant and sophisticated leasing industry for some time. The combined leasing volume in these countries account for almost 20 per cent of the world's total leasing activity.

6.10 In India, the National Small Industries Corporation (NSIC) and State Small Industries Development Corporations (SSIDCs) have been providing leasing facilities to small enterprises in the country. The real challenge in our country is to popularize this instrument among smaller enterprises, especially the NFUEs. The possibility of such an extension should be examined by the Ministry of MSME with a view to help developing the sector.

Factoring Services

6.11 Factoring in financial parlance means purchase of receivables. The basic principle of factoring is the same as Bill Discounting. The only difference is that in this case there will be no bill of exchange. Finance is made available on the basis of invoice. This eliminates the need for drawing up a bill of exchange and its stamping. Factoring entails the use of accounts receivable as banking for a loan and is based on their valuation independent of the risk profile of the borrower. Factoring service involves a contract concluded between one party (the supplier–client) and another party (factor), pursuant to which the supplier will assign contracts of selling of goods made between the supplier and its customers. This facilitates finance for the client (loans and advance payments) and helps in maintenance of accounts (ledgering) relating to receivables. Factoring helps in the collection of receivables, and provides protection against default in payment by debtors. In India it is considered as a solution to the problem of delayed payment on sales by the small and unorganised units.

6.12 As against domestic factoring, international factoring is a product, which is applicable to exporters. An exporter can expect up to 90 per cent of the finance and 100 per cent risk protection. The factoring company will set up limits for each importer or the exporter and buy exports made within this limit. This facility is available for tenure of up to 180 days. Financing is in foreign exchange. Otherwise, the principles of export factoring are the same as domestic factoring.

6.13 SBI and Canara Bank were the first to set up factoring subsidiaries in 1991. SIDBI participated 20 per cent in their equity. SIDBI has been providing lines of credit to both these factoring companies on concessional terms against SSI debts factored by them. Banks are allowed to undertake factoring departmentally as well. But there was lack of response. There is the need for a separate legislation on factoring. Currently, factoring services have to operate within the existing legislation on contracts, sale of goods, transfer of property, etc. These enactments do not comprehensively deal with the various aspects involved in the factoring business and are not found adequate to provide the requisite protection to a Factor. The existing law does not require the assignee (Factor) to give notice to the debtor that it has taken assignment of the debt. However, in order to prevent the debtor from paying the debt to the client or to a subsequent assignee, and also to enable the Factor to claim the payment of debt in his own right, giving notice of the assignment becomes necessary. There are, however, certain problems that come in the way of the enactment of an effective legislation on factoring. Important among them is the payment of stamp duty and registration of assignment. MSMED Act has come out with some provisions of legal recourse on delayed payment. But legal recourse works negatively for weaker enterprises. Hence an appropriate Factoring Policy needs to be formulated for unorganised enterprises, since it is aimed at addressing the problem of delayed payments, which leads to the sickness of the small and for NFUEs.

Equity Financing

6.14 The most essential requirement for equity financing is the existence of a well developed capital market along with sound small enterprises with brands. One of the major problems faced by the developing economies in financing small enterprises is the inadequacy of capital markets to bridge the credit gaps of such units. Capital markets take a long time to develop and deepen and do not necessarily work in ways predicated. Often the lack of financial instruments and the smaller number of participants restrict the capacity for financial deepening. In low income countries many family based indigenous enterprises are reluctant to change their status. The development of capital markets helps in introducing efficient and effective mechanisms of regulation and supervision to avoid malpractices. If these are not in place then markets will fail to assess the intermediate risks appropriately. Despite many attempts by SIDBI, it could not succeed to take some of the large SSIs to capital market, We understand that the Government has been advising SIDBI to promote group based equity financing by participation in the capital market. In addition, the Commission is also aware that the Government is considering in terms of promoting SME stock exchanges in this country. These initiatives need to be speeded up with a view to bringing in at least those segments of enterprises in the unorganised sector, which are dynamic.

Venture Capital

6.15 Venture capital financing is one of the forms of equity financing. While credit is usually a primary financial resource for small enterprises to operate and invest, equity capital is also an indispensable element in SME financing. Equity capital is important, in particular, in start-up phases and rapid growth periods. In most cases, small enterprises obtain equity capital from the founders and their relatives and friends. However, in some advanced market countries like the UK and US, the venture capital industry has developed as an important source of equity capital for small enterprises. Venture Capital funds bridge the gaps in the institutional financing mechanism of the SME sector in respect of units, which due to the inherent characteristics of their projects in terms of the proposed products/technology involved may not qualify for assistance through the conventional route of term financing. Normally, it serves those ventures which have latent innovative potential in industries like Information Technology (IT), Bio Technology, Food Products (processing to enhance shelf-life and new foods qualifying in terms of emerging requirements of health and hygiene), electronics, new chemicals, drugs and pharmaceuticals, etc.

6.16 Government has taken various steps to promote venture capital investment for small enterprises in India. Small Industries Development Bank of India (SIDBI) launched the Venture Capital Scheme in October, 1992, and created a separate Venture Capital Fund with an initial corpus of Rs. 100 million. The corpus of the Fund has continuously been enhanced since then. Some developmental and financial institutions have started financing of enterprises through venture capital in recent years.

6.17 Venture capital is ideal for knowledge and technology-based industries. The IT sector, software industry and related business such as e-commerce, networking, multimedia, data communication and value added communicating services is a growing sector and SME units venturing into these areas need to be assisted. However, player enterprises will have to move up to the value chain from providing low-end finance and accounting or customer interaction services to e - learning, engineering design, etc. Small enterprises with strong managerial teams and excellent executing capability trying to obtain VC funds should not only be provided with fund support but assistance like information and market access, technological net-working and hand holding to manage business more effectively and achieve rapid growth in the internationally competitive environment. In the first instance it may appear as if there is not much scope for venture capital finance in the unorganised sector since venture capital involves moving to untried risky ventures and new product lines. However, with the constant innovations going on and with the development of clusters, venture funds could find a useful role even in this sector. Hence it would be appropriate to create and encourage venture capital funds for this sector. Venture capital as an innovative instrument for small enterprise financing is gaining prominence in many countries both developing and developed in recent years.

Cluster Financing

6.18 Among the innovative instruments of financing, cluster financing assumes the most important place. Clusters are emerging as the strategy for sustainable development of unorganised enterprises. International experience suggests that small enterprises flourish in situations where they can be clustered together in areas where it is easier to develop common infrastructure facilities of high quality. Many such clusters have already emerged. According to UNIDO, there are 388 clusters in the country of which, 34 have turnover exceeding Rs. 1000 crores. A few have a gross turnover exceeding Rs.10,000 crores. The SSI Census identified over 1200 clusters in the country. Besides, there are well known KVIC, handlooms, handicrafts, sericulture, coir, jute and wool clusters. It is estimated that there are over 2000 artisan-based clusters in the country. However, at present there is no clear policy for financing of the clusters leading to their up-gradation and development so that they become part of the global chain. The Expert Committee on Small Enterprises, popularly known as the Abid Hussain Committee (1997) had recommended that the states should identify the existing clusters and promote joint ventures between the state government or local authority and business associations in these clusters. Recently, the Ministry of MSME (formerly SSI), Ministry of Textiles (Handloom and Handicraft Boards) and Ministry of Food Processing have launched a large number of cluster development programmes. It is high time that all these separate programmes are coordinated for the purpose of policy, credit, technology and marketing. While presenting the 2006 –07, Union Budget Finance Minister observed that currently there are nine ministries/departments engaged in the task of cluster development and these needs to be coordinated. It is learnt that the Ministry of SSI (now called Ministry of MSME) has been asked to undertake the task of coordination.

6.19 Currently, common facility needs of the clusters are provided by the government through budgetary allocations. Since, clusters are going to gain momentum and finally emerge as the strategy of small enterprises and unorganised enterprise development, it would be appropriate to link the financing of common facility and infrastructural needs of the clusters through institutional sources. For balanced and coordinated development of clusters and to workout modalities for attracting bank finance for cluster development, it would be appropriate to evolve a mechanism for bank financing of the clusters. RBI has already issued intimation to the banks to prepare cluster credit plans and include them in the Annual District Credit Plans.

7 Policy Initiatives and Measures to Improve the Flow of Credit

Policy Initiatives

7.1 To analyse the impact of policy initiatives to improve the flow of funds to the small enterprise sector, including complexities of the system and procedure relating thereto, the RBI has constituted various committees since the decade of the nineties. Prominent among these are the Nayak Committee, S.L. Kapur Committee, Ganguly Committee and H.R. Khan Committee. These committees have given a number of recommendations covering various aspects relating to flow of credit to the SSI sector. A number of recommendations of these committees have been translated into policy prescription by the RBI and the Government of India for players in the financial system and support service institutions engaged in the development of the SSI sector. Some of the important recommendations pertaining to the credit dispensation of these committees and action taken there on are summarised below.

7.2 Among all the committees the report of the Nayak committee still forms the main basis of the guidelines governing credit to the small scale sector because this committee, for the first time in Independent India, estimated the quantum of credit going to small scale (non-agriculture) sector and found that this sector was getting 8.1 per cent of its annual turnover by way of working capital advances from the banks. Of this, the tiny units, the village industries and artisan units were receiving 2.7 per cent of the annual turnover by way of working capital advances from the banks. This committee, for the first time, also made a normative assessment of the credit and turnover relationship and recommended that a minimum of 20 per cent of projected annual turnover should be provided by way of working capital loans by the banks. Subsequently, another committee viz., Kapur Committee, was set up to look into non-implementation of the Nayak Committee recommendations. Even this was found deficient, therefore RBI set up the Ganguly Committee in 2003-04. As a result of the recommendations of the committees the Government came out with a credit package for SME sector in 2005. These are also reflected in MSMED Act of 2006. In the light of the sharp drop in the share of credit to the SME sector, the RBI constituted an Internal Group (headed by Shri C S Murthy) to examine the issue. Further, another Internal Group was set up by the RBI to examine the issue of rural credit and micro finance (Khan Committee). This group recommended adoption of agency model for comprehensive financial services as well as extending the reach to large areas. As the Commission observed in Chapter 4 of this Report, the situation continues to be bleak in so far as access to credit in general and NFUEs in particular. A summary of recommendations of the various committees and internal groups is given in Table 7.1.

Table 7.1: Summary of Recommendations of Various Committees on SSI Sector

Name of the Committee and Objectives	Findings/Recommendations
Nayak Committee (1992)- Adequacy of Institutional Credit to the SSI Sector and Related Issues	(i) (a) Banks have insufficiently serviced the working capital needs of the SSI sector and in particular, village and tiny enterprises. The SSI sector has been getting 8.1 per cent of its annual turnover by way of working capital advances from the banks. Of this, the tiny units, village industries and artisan units were receiving only 2.7 per cent of their annual turnover by way of working capital advances from the banks. (b) The need for specialised bank branches for SSIs, the absence of which, in the past, has led to serious bottlenecks, namely., (a) arbitrary reductions in credit limits applied for, (b) inordinate delays and irregularity in the sanction of working capital, and (c) scarce availability of the assistance for start-ups, expansions and diversifications. (c) The system of providing term credit and working capital by two kinds of institutions viz., banks and SFCs has given rise to a problem of co-ordination between them. (ii) The entire SSI sector is entitled to the priority sector lending of the banks. Village Industries and smaller tiny units with credit limits upto Rs. 1 lakh should have the first claim on the priority sector credit to the SSI. (iii) Bank branches should give priority to those Village Industries and smaller tiny industries, which can use working capital efficiently. (iv) The working capital loans to the existing and new SSI units should correspond to a minimum of 20 per cent of the projected annual turnover but not exceeding Rs. 100 lakhs of their Fund-based needs. (v) Commercial banks to open specialised or dedicated branches in areas with a high density of small industry ranging between 1,000 and 2,000 registered SSI units. (vi) An SSI unit may be classified as sick, when: [i] any of its borrowal accounts has become a doubtful advance i.e. principal or interest in respect of any of its borrowal accounts has remained overdue for periods exceeding 2 1/2years, and [ii] there is erosion in net worth due to accumulated cash losses to the extent of 50 per cent or more of its peak net worth during the preceding two accounting years. (vii) Further, it is necessary that rehabilitation packages for alleviating sickness of potentially viable small units are made more effective.
Kapur Committee (1998)-To find out reasons for non-implementation of Nayak Committee Recommendations	a) Banks should open more specialised SSI branches or shift/restructure some of the existing branches and convert them into specialised branches for financing the small scale sector. b) With regard to simplification of application forms, it was recommended that the application form prescribed for facilities up to Rs. 2 lakhs could straight away be permitted to be used for facilities up to Rs. 10 lakhs. c) Loan applications should be sanctioned promptly and normally within one month.

Table 7.1 Cont.......

Name of the Committee and Objectives	Findings/Recommendations
	d) The SFCs and other state-level institutions should be restructured as per the recommendations made by the Khan Working Group. e) The existing Credit Guarantee Scheme being operated by Deposit Insurance and Credit Guarantee Corporation (DICGC) should be scrapped and be replaced by a more objective and suitable scheme to be operated by a new Guarantee Corporation. f) The Reserve Bank of India might consider, in consultation with the Government of India, the need to set up a Small Industries Infrastructure Development Fund, for the development of industrial areas in/around metropolitan cities, urban and semi-urban areas which were not covered by RIDF of NABARD. g) Credit rating for SSI units could help in augmenting the flow of credit to SSIs.
Ganguly Working Group (2003-04)-To find out reasons of slow down in SME credit	The Committee observed "The present slow down in lending to the SME sector is principally due to the risk aversion arising out of a high proportion of the lending becoming nonperforming".The Committee suggested changes in the lending strategy, these are: - (a) Lending should be directed to those units which have linkages with large corporate undertakings as vendors or suppliers. For them credit could be tied up with large undertakings, through technology transfer and greater attention to the quality of products, (b) Second strategy consists in developing a set up of products for units belonging to the same cluster of industries, (c) The third strategy is to develop local financial intermediaries specifically aimed at financing units in the tiny and small sectors. These would be in the nature of NBFCs but without permission to accept deposits from public. The Committee recommended adoption of a cluster-based approach for financing the SME sector, setting up of Technology Bank by SIDBI and proactive role by Credit Guarantee Scheme for SSIs. The SME Credit Package 2005 and Micro, Small and Medium Enterprises Act 2006, reflect action on various recommendations of the Ganguly Committee.
Murthy Committee (2005)-RBI Internal Group on SME sector	The Internal Group has inter-alia recommended: (i) Constitution of empowered committees at the regional office of Reserve Bank to periodically review the progress in SSI and Medium Enterprises financing and also to coordinate with other banks/financial institutions and the state governments in removing bottlenecks, if any, in ensuring a smooth flow of credit to the sector. (ii) Opening of specialized SME branches in identified clusters/centres that have a preponderance of SSI and ME units to enable easy access by entrepreneurs to bank credit and to equip bank personnel to develop the requisite expertise.
Khan Committee (2005)-RBI Internal Group on Rural Credit and Micro Finance	The observation made by this group is relevant with regard to institutional development of rural banking in India. It observes *"The outreach of Indian Banking System has seen rapid growth in rural areas. In so far as all the Scheduled Commercial Banks (SCBs) including RRBs are concerned, 48 per*

Table 7.1 Cont.......

Name of the Committee and Objectives	Findings/Recommendations
	cent of their branches (32,303 branches which translate to a population of about 23,000 per branch), 31 per cent (13.67 crores) of their deposit accounts and 43 per cent (2.55 crores) of their borrowal accounts are in the rural areas. Such an unprecedented expansion of the formal financial infrastructure has reduced dependence of the rural populace on the informal money lending sector from 68.3 per cent in 1971 to 36 per cent in 1991. (All India Debt and Investment Survey 1991)." According to the Report, on the supply side, the factors which are responsible for poor flow of credit to rural areas are :- • Persons are un-bankable in the evaluation/perception of bankers. • The loan amount is too small to invite attention of the bankers. • The person is bankable on a credit appraisal approach but distances are too long for serving and supporting the accounts and expanding branch network is not feasible and viable. • High transaction costs particularly in dealing with a large number of small accounts. • Lack of collateral security. • Inability to evaluate and monitor cash flow cycles and repayment capacities due to information asymmetry, lack of data base and absence of credit history of people with small means. • Human resources related constraints both in terms of inadequacy of manpower and lack of proper orientation/expertise. • Adverse security situation prevailing in some parts of rural India. ; • Lack of banking habits and credit culture. • Information - shadow geographical areas. • Inadequacy of extension services crucial to improve the production efficiency of the farmers leading to better loan repayment. On the demand side, according to the Khan Internal Group, the factors responsible for poor flow of credit to rural areas and the rural poor remaining excluded from the formal banking sector are : - • High transaction costs at the client level due to expenses such as travel costs, wage losses, incidental expenses; - Documentation; - Lack of awareness; - Lack of social capital; - Non - availability of ideal products; - Very small volume/size of transactions which are not encouraged by formal institutions; - Hassles related to documentation and procedures in the formal system; - Easy availability of timely and doorstep services from money lenders/ informal sources, and - Prior experiences of rejection by/indifference of the formal banking system. • For providing comprehensive financial services encompassing savings, credit and remittance, insurance and pension products in rural areas, and also for extending the reach to larger areas, the Group recommended two models, viz., the Business Facilitator Model and the Business Correspondent Model as proactive response.

Table 7.1 Cont.......

Name of the Committee and Objectives	Findings/Recommendations
	• Under the Business Facilitator Model, it was envisaged that banks could use a wide array of civil society organisations (CSOs) and others for supporting them by undertaking non-financial services. The Facilitators would provide support services for effective delivery of financial services such as: (i) borrowers' identification (ii) collection, processing and submission of applications; (iii) preliminary appraisal; (iv) marketing of the financial products including savings; (v) post - sanction monitoring; (vi) promotion and nurturing SHFs/ Joint Liability Groups (JLGs); and (vii) follow-up for recovery. • Under the Business Correspondent Model, institutional agencies/other external entities may support the banks for extending financial services. The Business Correspondents would function as 'pass through' agencies to provide credit-related services such as disbursal of small value credit, recovery of principal/collection of interest and sale of micro insurance/ mutual fund products/pension products besides other functions of the Business Facilitator Model. • The civil society organisations consists of the following components - NGOs, farmers clubs, functional cooperatives, IT-enabled rural outlets of corporates, postal agents, insurance agents, well-functioning panchayats, rural multi-purpose kiosks/village knowledge centres, agri-clinics/business centres financed by banks, Krishi Vigyan Kendras, Khadi and Village Industry Commission (KVIC)./Khadi and Village Industries Board (KVIB). Such units may function as the Business Facilitators. • Registered NBFCs with a significant rural presence, NGO-micro-finance institutions (MFIs) set up under the Societies/Trust Acts, Mutually Aided Cooperative Societies (MACS) with a charter to undertake appropriate contractual agreements with the principal; well running primary agricultural credit societies (PACSs) and post offices may function as the Business Correspondents.

Narasimham Committee (1991) on Banking Sector Reform

7.3 The Narasimham Committee's (1991) recommendations charted a road map for reforms in the financial sector in the context of a major shift in India's macro economic policies. Several major recommendations were made to liberalise the banking sector by making them function within the framework of market demand and competition. Banks were given more freedom to choose the loan taking into account the client's creditworthiness. Against fixed ceiling rate of 16.5 per cent on advance, a minimum rate of lending was fixed. As a result, the less creditworthy SSIs, micro enterprises and Village Industries suffered which is evident from the declining share of credit to them in percentage terms.

7.4 The Narasimham Committee (1991) observed that the system of 40 per cent directed credit should be phased out. But because of the compelling ground realities supported by political considerations, the 40 per cent target for the priority sector could not be dispensed with. Instead, the authorities have attempted to nullify, through the back door, the operational relevance of the priority sector target. This was done by including a vast number of items, which cannot be conceived of as belonging to the weaker section's small loan requirements. The impact of the implementation of these recommendations has been in the form of a declining share of farm and non-farm credit under priority sector lending.

Rangarajan Committee on Financial Inclusion (2006-07)

7.5 The Commission feels that the reforms undertaken in the banking sector has indeed enhanced the competitiveness of Indian banking system as well as enabled it to expand rapidly in the context of high growth performance of the Indian economy. However, it has come with a price in the form of a relative neglect of both the

SSI sector and within that unorganised sector as well as agriculture sector. The 2003 Farmers Survey revealed the distressing development viz. increasing reliance of the farmers on money lenders for their credit needs. Debt induced agrarian distress posed a challenge to the political leadership. Organisations of small scale industries continue to express their anguish with regard to their declining share of credit. It was in this context that the UPA government appointed a Committee on Financial Inclusion in 2006 under the chairmanship of Dr C Rangarajan. The Committee has submitted its Interim Report with main observations and recommendations as under:

a) About 51.4 per cent of farmers households do not access credit from either the institutional or non-institutional sources; 27 per cent of them are indebted; 68 per cent of the financially excluded households are in North-Eastern, Eastern and Central Region; marginal farmer's households constitute 66 per cent of all excluded farm households; exclusion is around 80 per cent among non-farm households.

b) Based on a detailed examination of the role of conventional delivery channels such as commercial banks, RRBs, cooperative etc. the Committee agreed with the conclusions of the earlier committees that rural credit suffered from the problems of inadequacy, constraints on timely availability, high cost, neglect of small and marginal farmers, low C-D ratio in many states and presence of informal markets. While tracing the evolution of other conventional delivery channels and reform of these institutions over a period of time, the Committee recommended the formulation of the National Financial Inclusion Plan based on targets, fully utilizing the capacity of bank branches, branch expansion, bringing attitudinal changes in bank staff; procedural changes; and promotional measures consisting of farmers' training, entrepreneurship training of selected borrowers and linking Self-Help Groups with formal sector.

c) The Committee also recommended the need to recognise a separate category of MF-NBFCs with equity support from NABARD, to reduce foreign equity limit for MF-NBFCs, and to introduce a code of conduct for MFIs. It emphasised the need for the MFIs to act as banking correspondents and render promotional support to MFIs in financially excluded regions.

Government Schemes to Facilitate Flow of Credit

7.6 As the Commission observed in Chapter 4 of the present Report what ever credit is now being made available to the micro enterprises in the NFUEs sector especially to those with an investment in Plant and Machinery up to Rs 5 lakh is largely through government sponsored schemes and programmes but for these schemes it would have been extremely difficult to obtain any credit from the commercial banking system to these enterprises. We therefore briefly deal with the existing schemes in the following paras.

Prime Minister's Rojgar Yojana (PMRY)

7.7 PMRY was started in 1993 with the objective of making available institutional finance to the educated unemployed youth for setting up self-employment ventures for all economically viable activities covering manufacturing, service, business and trade and creating new employment opportunities in both Rural and Urban Areas of the country. Bank Finance is made available without collateral for projects up to Rs.1 lakh for business sector, Rs.2 lakhs for manufacturing and other activities. If 10 or more eligible persons join together in a partnership, projects up to Rs.10 lakhs would be eligible for funding. Under the scheme subsidy up to 15 per cent of the project cost subject to a ceiling of Rs.7,500/- per entrepreneur is extended by the Government. Banks are allowed to take margin money from entrepreneurs varying from 5 per cent to 16.25 per cent of the project cost so as to make the total of the subsidy and margin money equal to 20 per cent of the project cost. The rate of subsidy for North Eastern Region is 15 per cent of the project cost subject to a ceiling of Rs.15,000/- per entrepreneur. Normal rate of interest is charged by the banks. The scheme envisages 22.5 per cent reservation for SC/ST and 27 per cent for OBCs. The educational qualification prescribed for the entrepreneurs is VIII passed with preference to trained persons in any trade. The scheme is implemented through the State Governments at the level of District Industries Centres (DICs). Under the PMRY, loans have been disbursed to 24.5 lakhs self-employed ventures since inception in 1993 till 31st March 2006. On an average about 2 lakhs new enterprises are set up every year under this scheme.

7.8 Table 7.2 gives the subsidy relesed by the Government for improving the flow of bank credit under PMRY

Table 7.2: Subsidy and Credit under PMRY (Rs Crores)

Year	No. of Units	Subsidy	Bank Loan	Employment (Nos)
1993-94	23,035	30	137	34,553
1994-95	158,863	100	872	238,295
1995-96	241,843	120	1,378	362,765
1996-97	228,495	98	1,352	342,743
1997-98	209,103	79	1,218	313,655
1998-99	191,351	120	1,093	287,027
1999-00	203,454	174	1,269	305,181
2000-01	184,890	183	1,168	277,335
2001-02	189,860	179	1,185	284,790
2002-03	190,521	152	1,198	285,782
2003-04	219,444	148	1,368	329,166
2004-05	244,884	190	1,502	367,326
2005-06*	173,713	251	1,021	260,570
Total	**2,459,456**	**1,823**	**14,761**	**3,689,189**

* Provisional
Source: Ministry of A&RI, Annual Reports.

7.9 Subsidy Credit Ratio under PMRY is 1:8, which is very high in terms of credit generated by per unit of subsidy. Under the scheme 24 lakhs enterprises have been set up providing employment to 36 lakhs persons. In terms of impact, it is considered as one of the successful programmes of the Government. The scheme is being monitored constantly by the Central Government, RBI and the State Governments at levels of Directorate of Industries and also the DICs. Studies have revealed that the scheme provides per unit employment to 1.5 persons and assets have been created in 89.7 per cent of the cases disbursed. Per unit loan in the case of PMRY units has been found at Rs.64,000/- in 2000 – 01. Some disturbing trends, however, are :

- Employment generation per unit has declined from 2.5 persons in the initial stage of the scheme (1995) to 1.5 person in 2004 – 05.
- The proportion of rural beneficiaries has come down from 49.9 in 1995 to 39.1
- Only 36.4 per cent of the beneficiaries are paying loan installments in time.
- Average rate of recovery is 38 per cent.
- Most beneficiaries prefer to go for servicing business and trade related activities since they find manufacturing as difficult, time consuming and cumbersome activity
- In the initial stages there were also reports of banks asking for collaterals and indulging in some malpractices.
- The programme could be improved by proper selection of projects and through skill and entrepreneurial based training. Trained persons should get preference in loan sanctions by the banks. A proper scrutiny of the project proposals in terms of their viability should receive high priority in the implementation of this programme.

Rural Employment Generation Programme for Village Industries (REGP)

7.10 REGP is implemented by the Khadi and Village Industries Commission since 1st April 1995. Under the scheme, rural industries projects having maximum investment limit of Rs.25 lakhs are promoted with the margin money subsidy. This scheme is dovetailed with bank credit. The margin money is provided for setting up labour – intensive village industries in rural areas and small towns with a population up to 20,000. KVIC provides margin money in advance to the public sector banks, empowering them to assess projects and take their own credit decisions. The objective of the programme is to provide productive employment to the people, in these areas and also help reduce migration from the rural to urban areas. Initially it was aimed at to create 2 million jobs under the programme. Subsequently the target was scaled down to 1.5 million jobs by the end of 9^{th} Plan. For 10^{th} Plan, the target was 25 lakhs jobs.

7.11 The objectives of this programme are:

- To generate employment in rural areas.
- To develop entrepreneurial skill among rural unemployed youth.
- To facilitate participation of banks in mobilisation of credit to rural industries
- To achieve the goal of rural industrialization.

This programme is implemented by Khadi Village Industries Commission.

7.12 A three day EDP training is mandatory for all entrepreneurs who desire to set up a REGP project. First installment of credit is released in ten working days of the bank after successful completion of training. Under REGP, 2,09,705 units have been set up and 28.06 lakh additional job opportunities have been created since inception in 1995 up to March 2005. Of these, approximately 12.4 per cent of the projects have benefited persons from the Scheduled Casts, 5.7 per cent from the Scheduled Tribes and 23.8 per cent from the OBC. The proportion of women entrepreneurs securing gainful employment under the programme is about 25.7 per cent. Table 7.3 shows the targets and achievements of social categories under the programme in the Tenth plan.

Table 7.3: Tenth Plan Social Categories Under REGP Progrmme (Per cent)

	Target	Achievement
SC	15	9.53
ST	7.5	7.043
OBC	27	19.87
Women	30	24.09

Source: Ministry of MSME, 2006-07, Annual Report.

7.13 The subsidy for general category on projects up to Rs. 10 lakhs is 25 per cent of the project cost. It is Rs. 2.5 lakhs plus 10 per cent of the balance project cost on projects above Rs.10 lakhs and up to Rs. 25 lakhs. In the case of SCs/STs/OBCs/Womens/ Physically Handicapped/Ex-Servicemen/North-East Region/Hill Areas, rate of subsidy is 30 per cent of the project cost up to Rs.10 lakhs and Rs.3 lakhs plus 10 per cent of balance the project cost for projects above Rs. 10 lakhs and up to 25 lakhs. The borrower is required to invest his own contribution of 10 per cent of the project cost if he is from general category and 5 per cent of the project cost in the case of beneficiaries from SCs/STs and other Weaker Sections. 65 per cent of the project is provided as loan by the banks.

7.14 Achievement of the REGP during 10th Plan Period is given in Table 7.4. The scheme has been performing well. Therefore the target per year has been raised to 5.5 lakhs persons every year.

7.15 Subsidy credit ratio is 1:2. Most of the enterprises are working as cooperatives or under groups and receive constant support from the KVIC in the form of technology, skill development and marketing which help in improving the viability of the enterprises. Coverage of Credit Guarantee Fund Trust for small industries has been ensured to mitigate the problems of the rural entrepreneurs who are otherwise required to furnish collateral security for projects under REGP. Marketing support coming from KVIC, KVI Boards, registered institutions and cooperatives is a major positive

Table 7.4: REGP - Progress during the Tenth Plan

Year Tenth Plan	Target for Employment Generation (Lakhs Persons)	Employment Generated (Lakh Persons)	Number of Projects set up	Margin Money Released (Rs. Crores)	Estimated Credit Flow (Rs. Crores)
2002-03	4.00	3.61	21,024	194	484
2003-04	5.00	4.71	24,747	266	605
2004-05	5.25	5.30	23,454	292	665
2005-06	5.56	5.67	26,650	321	730
2006 - 07	5.90	N.A.	31,760 (Target)	372 (Target)	NA

Source: Ministry of A &RI, Annual Report 2005 -06 and KVIC, Mumbai.

point behind the success of this scheme. Cumulative achievement since 1995 to March 2006 is shown in Table 7.5.

Table 7.5: Cumulative Performance of REGP

No. of Projects	2.36 lakhs
Employment Generated	33.73 lakh persons
Margin Money Utilisation	Rs.1,712.38 crores
Bank Credit	Rs.4,395.00 crores
Investment	Rs.6,761.00 crores

Source - Ministry of A &RI, Annual Report, 2005 -06 and KVIC, Mumbai.

7.16 Best performing REGP states according to KVIC are Arunachal Pradesh, Himachal Pradesh, .Jammu & Kashmir, Assam, Mizoram, Kerala, Tamil Nadu, Gujarat, Chhattisgarh, and Uttaranchal (Uttarakhand). Though the progress of availing credit from banks under REGP is encouraging, inaccessibility of bank branches in the rural and remote areas, particularly in North Eastern Region, is a problem being faced by the artisans and entrepreneurs. Similar situation exists in Lakshadweep Islands. KVIC is considering to restructure this scheme by linking it with PMRY. The additional attraction of PMRY is that it is for the educated unemployed youth and the project cost is very high in REGP i.e. up to Rs.25 lakhs. It may be worthwhile to upgrade PMRY scheme to REGP level by enhancing the limit of project cost and the quantum of subsidy.

Interest Subsidy Eligibility Certification (ISEC) Scheme for Khadi.

7.17 The Interest Subsidy Eligibility Certificate (ISEC) Scheme is a major credit linked programme for the Khadi Sector implemented by Khadi and Village Industries Commission (KVIC). It was introduced in May 1977 to mobilise funds from the banking institutions to fill the gap in the actual fund requirements and the availability from budgetary sources. Under the ISEC Scheme, credit at concessional rate of interest of 4 per cent per annum for capital expenditure as well as working capital is given as per the requirement of the institutions. The difference between the actual lending rate and 4 per cent is paid by the Central Government through the KVIC to the lending banks. Institutions registered with the KVIC/State Khadi and Village Industries Boards (KVIBs) can avail finances under this scheme. Initially, the entire KVI Sector including the village industries was covered under the Scheme but with the introduction of separate scheme for Village Industries called Rural Employment Generation Programme for Village Industries, the ISEC Scheme now supports only the Khadi and Polyvastra Sector. However, all the existing village industries as on 31st March, 1995 and falling within the purview of the KVIC, have been allowed to avail this facility for the amount of bank finance availed as on that date on actual basis.

Swarnjayanti Gram Swarozgar Yojana (SGSY)

7.18 Swarnjayanti Gram Swarozgar Yojana is a major on-going programme for self-employment of rural poor operated by the Union Ministry of Rural Development. The programme was started in April 1999 after restructuring the erstwhile Integrated Rural Development Programme and other allied programmes. The basic objective of the SGSY is to bring the assisted poor families above the poverty line by providing them income generating assets through a mix of bank credit and government subsidy. The programme aims at establishing a large number of micro - enterprises in rural areas based on the ability of the poor and potential of each area. The emphasis is on the development of activity clusters to ensure proper forward and backward linkages. NGOs play active role in formation and capacity building of Self-Help Groups (SHGs). Vulnerable sections of the society namely SCs, STs, women and the disabled get special attention.

7.19 Table 7.6 gives the overall performance of the scheme since inception up to December 2005.

Table 7.6: Overall Progress under SGSY up to December 2005

No. of SHGs Formed	24.13 lakhs
No. of Swarozgaries Assisted of the Swarozgaries	74.03 lakhs
Subsidy Disbursed	Rs.5,402 crores
Credit Disbursed by Banks	Rs.10,705 crores
Per capita Investment	Rs.21,818
Percentage of Women Beneficiaries	53.32 per cent (2004-05)

Source: Ministry of Rural Development, Annual Report, 2005-06; 2006-07.

7.20 SGSY is one of the highly successful programmes of self-employment in rural areas and for people below the poverty line. The successful implementation of SGSY, to a great extent, depends on the adequate flow of credit from the banks to swarozgaries. The credit mobilization targets are being fixed every year by a committee, which has representative of RBI, NABARD, Banking Division (Ministry of Finance) and Ministry of Rural Development. During the year 2004-05, the credit mobilisation target under SGSY was Rs.2,507 crores but actual achievement was only Rs.1657 crores, which was 66 per cent of the credit target. Though the percentage of credit mobilization has increased from 32.96 per cent in 1999-2000 to 66.09 per cent in 2004-05, the rate of increase is far below the expected rate of credit mobilization. Adequate mobilization of bank credit is possible with timely sponsoring of loan applications, simplification of the bank procedures and better monitoring of the progress of credit mobilization at regular intervals.

Urban Self-Employment Programme (USEP)

7.21 Urban Self Employment Programme is a component of Swarnjayanti Shahri Rojgar Yojana (SSRY), being implemented by the Ministry of Urban Employment and Poverty Alleviation since December 1997 after subsuming some earlier self-employment and wage employment programmes meant for urban areas. SSRY is funded on a 75: 25 basis between the centre and the states. This programme is applicable to all towns in India with special emphasis on Urban Poor Clusters.

7.22 This is also a credit linked subsidy based programme for setting up micro-enterprises. The salient features of the programme are given in Table 7.7.

Table 7.7: Salient Features of USEP

Maximum Unit Cost	Rs.50,000/-
Subsidy	15 per cent of the project costsubject to a maximum of Rs.7,500/-
Margin money to be contributed by the beneficiaries	5 per cent of the project cost.
Special Attention	SCs/STs, women and disabled persons.
Women Beneficiaries	Not less than 30 per cent in each town

Source: Ministry of Housing & Urban Poverty Alleviation, Annual Report, 2006-07.

7.23 Since the inception of the programme in December 1997 and till December 2006, 7.3 lakhs beneficiaries have been assisted to set up micro - enterprises. A sum of Rs.979 crores has been released to states. Of the total beneficiaries under this programme 1.7 lakhs were women. Central funds for the implementation of the scheme is released to the State Governments/state Nodal Agencies who is turn disburse the money to the District Urban Development Agencies/ Urban Local Bodies. Subsidy pattern in this scheme is just like PMRY and hence subsidy - credit is also expected to be like PMRY i.e. in the range of 1:5 to 1:8.

7.24 SSRY has one more component based on subsidy for bank loan exclusively for women called Development of Women and Children in Urban Areas for taking up self - employment ventures. This is a group-based programme. A group may consist of at least 10 women. Ceiling on subsidy is Rs.1.25 lakhs or 50 per cent of the cost of the project which ever is less., Since its inception till March 2005, 1.6 lakhs women have been assisted under this programme and a sum of Rs.85.22 crores has been released as subsidy.

Credit Linked Capital Subsidy Scheme (CLCSS)

7.25 Aimed at technology up-gradation of the small scale enterprises, the Government (M/MSME formerly SSI) has been operating a Credit Linked Capital Subsidy Scheme (CLCSS) since the year 2000. The scheme aims at facilitating technology up-gradation of the SSI units for improvement in productivity, by providing them 15 per cent (initially it was 12 per cent) upfront subsidy. This scheme is available to all types of SSI units including agro and rural industry units, on institutional finance (credit) availed by them for the modernization of their production equipment (plant and machinery) and technology. Existing SSI units registered with the State Directorates of Industries, and which upgrade with the state-of-the-art technology, with or without expansion as well as new SSI units which are registered with the State Directorate of Industries and which set up their facilities only with appropriate eligible and proven technology are eligible for subsidy under this scheme. The scheme was launched on 1st October, 2000 for a period of 5 years or till the sanction of the capital subsidy reached Rs.600 crore, which ever was earlier. The scheme has now been extended upto March 2007. SIDBI, NABARD and other select commercial banks implement this scheme, while credit is extended by eligible Primary Lending Institutions (PLIs) such as Scheduled Commercial Banks, eligible cooperative banks (other than Urban Cooperative Banks), eligible Regional Rural

Banks, National Small Industries Corporation, State Financial Corporations (SFCs) and North Eastern Development Financial Institution (NEDFi).

7.26 The guidelines of the scheme have been revised from time to time by the Governing and Technology Approval Board of CLCSS to include more sub-sectors/ products and approved technologies under the scheme. The scheme currently covers 45 sub-sectors important among them are food processing, poultry, leather and leather products, electronic equipment, auto parts, bicycle parts, general engineering works, bio-tech industries, foundries, toys, sports goods, wooden furniture, khadi, and village industries, coir and coir products, agricultural equipment, plastics, rubber, glass and ceramics, etc.
To accelerate the pace of implementation of the scheme and also on the basis of the experiences gathered in implementing the scheme, the scheme has been revised recently in 2005.

Technology Up-gradation Fund Scheme for Textile

7.27 The Technology Up-gradation Fund Scheme (TUS), the flag ship scheme of the Ministry of Textiles was launched in April, 1999 with the objective of making funds available to the domestic textile industry for up-grading technology of existing units and also to set up new units with state-of-the-art technology for enhancing their viability in the domestic and international markets. The scheme is valid till March 2007 and provides for a 5 per cent reimbursement of the normal interest charged by the lending institutions on rupee term loan. Though the scheme covers both large mills and small units such as handlooms, it has mostly been utilised by the large units. As per the Annual Report 2005-2006 of the Ministry of Textiles 4,514 applications with the total project cost of Rs.37,026 crores have received subsidy worth Rs.9,161 crores up to 31st December, 2005. The decentralized segment the scheme also covers handlooms, which account for 13 per cent of total cloth production in the country, and also the powerloom sector. In lieu of interest subsidy, an additional option of credit linked capital subsidy has been offered for the decentralized textile sector. Under TUFs, a powerloom owner can reduce cost of borrowing capital either by (i) availing 20 per cent upfront credit linked capital subsidy from the enlarged credit network that include cooperative banks and other genuine NBFCs recognized by the RBI, or (ii) by obtaining a 5 per cent interest subsidy on loan. By December 2005, subsidy amounting to Rs.18.00 crores was released in respect of 347 powerloom units. Separate figure for Handlooms is not available. It appears that the decentralized sector is not a significant beneficiary of this scheme. A review of the scheme carried out for powerloom sector, which is equally applicable for the handloom sector, is relevant in this regard.

7.28 Although the scheme is launched to help the handloom sector, the Commission understands that much of the benefits is cornered by the larger units. Part of the problem could be due to the powerloom units' inability to maintain modern accounting practices such as books of accounts and other documents necessary for bank loans. Banks also consider what is economically viable venture that often leave out units with less than 10 shuttless looms. In the light of these drawbacks there is a case for re-examining the scheme to suit the requirements of the smaller powerloom and handloom units.

Schemes to Enhance Confidence of Banks in SSI Lending

Credit Guarantee Scheme for Small Enterprises

7.29 Obtaining bank loan without collateral has been one of the main problems of small entrepreneurs. Besides, the banks find lending to small enterprises a risky proposition. As a solution to this problem, the Credit Guarantee Fund Trust Scheme for Small Industries was introduced by the Government (Ministry of Small Scale Industries) in May 2000 with the objective of making available credit to small scale industrial units, particularly the tiny units (with investment in plant and machinery less than Rs.25 lakhs) for loans up to Rs.10 lakhs without collateral/ third party guarantees. The scheme is being operated through the Credit Guarantee Fund Trust for Small Industries (CGTSI) now called Credit Guarantee Fund Trust for Micro and Small Enterprises (CGTMSE) set up jointly by the Government of India and the Small Industries Development Bank of India (SIDBI). The loan limit under the scheme, which was Rs.10 lakhs per borrower, has been enhanced to Rs.25 lakhs per borrower in accordance with the Comprehensive Policy Package for SSIs announced on 30th August 2000 when the Scheme was formally launched. The scheme covers collateral free loan (term loan and/or working capital including non Fund based working capital) extended by eligible lending institutions to new and existing SSI units as well as Small Scale Service and Business (industry related), Entities (SSSBEs) including Information Technology and Software Industry up to Rs.25 lakhs per borrowing units.

7.30 The guarantee cover under the scheme is up to 75 per cent of the credit subject to a maximum guarantee limit of Rs.18.75 lakh. However, the member lending institutions (MLIs) are allowed to extend additional credit facilities against collateral security and/or third party guarantee to the borrowers already covered under the scheme in those cases where the credit facility already covered under the scheme has already reached the ceiling of Rs.25 lakhs. The lending institutions are made available guarantee fees of 2.5 per cent and service fees of 0.75 per cent per annum of the credit facility sanctioned by the lending institution to the borrower. As announced in the "Policy Package for Stepping up Credit to Small and Medium Enterprises 2005" and also in the Union Budget 2006-07, the guarantee fee has been reduced from 2.5 per cent to 1.5 per cent. Government has also decided to raise the size of the Fund to Rs.2,500 crores as initially proposed at the time of the formulation of the scheme. Apart from the Small Scale Industries falling within the purview of the Office of the Development Commissions (SSI), it has also been decided to bring Khadi and Village Industries, Coir and Handicraft Units within the fold of the scheme if they intend to avail guarantee cover on bank loan. Though the scheme has been in operation for the last 5 years now, the coverage of loans at around Rs 800 crores by the end of August, 2005 is very low. It emerges that most of the major banks including the State Bank of India took lot of time in taking a decision to join the scheme. Most of the banks feel that loans with collateral gives them added comfort and as such are not inclined to sanction loans under guarantee scheme. Further, there is lack of awareness about this scheme at the banks' branch level.

7.31 The Credit Guarantee Scheme was initially approved for one year with a corpus of Rs. 125 crores, contributed by the Government of India and SIDBI in the ratio of 4:1. Subsequently the Government decided to continue the scheme beyond one year. By the end of July 2006, the corpus of CGTMSE stood at Rs.1,336 crores with the contribution of Rs.1,069 crore from the Government and Rs. 267 crore from SIDBI. By the end of July, 2006, 52 eligible institutions comprising 28 Public Sector Banks, 11 Regional Rural Banks (RRBs), National Small Industries Corporation (NSIC), North Eastern Development Finance Corporation (NEDFi) and Small Industries Development Bank of India (SIDBI) have become Member Lending Institutions (MLIs) of CGTMSE for participating in this Scheme. By December, 2006, 61,312 proposals were approved for guarantee cover for an aggregate credit of Rs.1,544 crores. Even if the scheme has started taking off smoothly in recent years, the progress of the scheme has been still very low, when compared with the vast requirements of credit coverage of micro and unorganised enterprises in the country. Many banks do not find guarantee schemes preferable to collaterals.

7.32 It is essential to extend the coverage of the scheme to the entire unorganised sector enterprises including handlooms, sericulture and micro enterprises. It is, however, suggested that in the case of loans to micro enterprises with investment in plant and machinery less than Rs.5 lakhs, (SSMEs) guarantee cover should be raised to 90 per cent of the loan as against 75 per cent at present. Further to reduce the cost of borrowing, the guarantee fee should be met by the Government in the case of loans to SSMEs. Sound Micro Financing Institutions (MFIs) from RRBs, cooperative banks, SFCs could also be considered for inclusion as Member Lending Institution. This will help MFIs to extend credit to micro enterprises. The CGTSI should also evolve a mechanism to provide guarantee cover to loans raised for providing common services/facilities in clusters.

Credit Rating Scheme for SSIs

7.33 Another scheme to facilitate the flow of credit i.e. the Credit Rating Scheme has been launched recently i.e. in January 2005. This scheme is being implemented by the National Small Industries Corporation (NSIC). The basic objective of this scheme is to sensitise the SSI sector to the need for obtaining credit rating and encourage them to maintain a good financial track record, which would earn them a higher rating whenever they approach the financial institutions for their working capital and investment requirements. The Indian Banks' Association has accorded its consent to support the scheme. NSIC has empanelled six rating agencies namely CARE, CRISIL, D&B, FITCH, ICRA and ONICRA to carry out the rating of the interested SSI units under the scheme. The scheme is available to only those units, which are registered with DICs. Government of India reimburses 75 per cent of the fee charged for rating subject to a maximum of Rs. 40,000.

7.34 Micro and Small Enterprise (MSE) sector has been perceived as a high risk funding proposition mainly because such units are heterogeneous and the evaluation and assessment of such units are regarded as complex in the absence of transparent information about their functioning. This information asymmetry largely in the form of lack of properly structured financial information with limited availability of audited financial statements acts as a major deterrent to the smooth flow of credit from banking channels to MSEs. Perceived higher risk also leads to higher product pricing for this segment. In order to address this problem SIDBI in association with Credit Information Bureau (India) Ltd. (CIBIL), Dun & Bradstreet India (D&B) and some of the public sector and private sector banks established SME Rating Agency of India Ltd. (SMERA) in September 2005.

7.35 SMERA, with the help of NSIC's Performance and credit rating scheme, has been offering eligible SSI units rating services at an all-inclusive price of Rs. 5,612/-. In order to upscale the rating operations and incentivise the MSEs to go for rating, the following suggestions are made:

- One way to rationalise credit pricing is to efficiently measure their credit risk. SIDBI, with its long experience of term financing, has developed an advanced but simplistic, technology-based rating model for MSMEs called Credit Appraisal and Rating Tool (CART)
- Credit rating may be seen in the long-term perspective. Accordingly, subsidy for rating may be provided both for the first time rating as well as on an ongoing basis for rating renewal. This may be available and applicable for the rating from all the empanelled rating agencies for the MSEs. Moreover, the rating system may be widely published in all MSE clusters.

7.36 Since the scheme has been launched only recently, it is too early to evaluate its performance. However, the scheme covers large SSIs or medium enterprises, which have corporate entities and not the tiny or micro enterprises. To start with, the scheme should be liberalized to cover all small and micro enterprises whether registered or unorganised. Arrangement for the credit rating of SHGs, MIFs and others engaged in micro financing, at cheaper costs, also needs to be made.

7.37 In addition to the above, a good part of a number of measures, taken by the Government of India to cover non-farm sector could as well be applicable to the unorganised sector. These are:

- Banks have been advised to fix self-set targets for growth in advances to SSI sector over the previous year's achievements and overall trends in the growth of net bank credit.
- Ministry of SSI has identified 78 clusters for focused development of SSIs and sent the list to the RBI for incorporation of the credit requirements of these clusters in the State Credit Plans of the Banks. RBI has written to all State Level Bankers' Committee (SLBC) Convener Banks to incorporate the credit requirements of these clusters in the State Credit Plans and initiate necessary action for enhancing the credit flow to the SSI sector, particularly in these clusters.
- Publicity by the banks to various schemes/facilities like availability of collateral-free/composite loans and schemes under Technology Up-gradation Fund Scheme (TUFS) /National Equity Fund (NEF)/ Credit Guarantee Fund Trust for Small Industries (CGTSI), etc. is being given. To increase awareness about the schemes/facilities to SSI sector, State Bank of India came out with a 'Charter for SSI, ' which was advertised in all the leading newspapers. Indian Banks' Association (IBA) has issued a circular to all member banks to come out with similar charters for the SSI sector. All 27 public sector banks have issued 'Charter for SSI'.
- Exemption limit of borrower accounts for obtaining/requiring collateral securities has been raised to Rs. 5 lakhs for both tiny and SSI units. Further, the RBI has advised the banks that they may, on the basis of good track record and financial position of the units, increase the limit, of dispensing with collateral requirements for loans from the existing Rs.5 lakhs to Rs. 25 lakhs.
- The existing Composite Loan Scheme of banks helps small borrowers by providing working capital and term loans through a single window. To promote credit flow to small borrowers, the composite loan limit was increased from Rs. 50 lakhs to Rs. 1 crores in October, 2004. The composite loan (outstanding) of the public sector banks up to December 2004 was Rs. 1,796.34 crores (constituting 2.85 per cent of the total loan outstanding) for 1.89 lakhs SSI accounts.
- Banks have been advised to open at least one specialized SSI branch in each district. Further, banks have been permitted to categorize their general banking branches having 60 per cent or more of their advances to SSI sector as specialised SSI branches in order to provide better service to this sector as a whole. As at the end of March, 2005, it is reported that 537 specialized SSI

branches have been operationalised in 175 districts out of 598 districts in the country.

- As per the announcement made by the Finance Minister in the Budget Speech of 2003-04, Indian Banks' Association (IBA) has advised the banks to adopt the interest rate band of 2 per cent above and below their Prime Lending Rates (PLR) for secured advances. This is not being adhered to strictly, as reported by small entrepreneurs. Non-SSI units (large and medium) are financed at a rate of interest even below 2 per cent of PLR.
- Banks have been advised to examine having at least three slabs of rate of interest for loans up to Rs. 50,000, between Rs. 50,000 and Rs. 2 lakhs, and above Rs. 2 lakhs. As reported by the RBI to the Ministry of SSI, majority of the public sector banks have fixed three slabs in interest rate for advances to the SSI sector.
- To make available timely credit to the sector, a time frame has been fixed for disposal of loan applications, i.e., loans up to Rs. 25,000 within 2 weeks and loans up to Rs. 5 lakhs within 4 weeks, provided that the loan applications are complete in all respects and accompanied by the 'check list'. The SSI associations often complain that it takes far longer time to get loans sanctioned than the time limit fixed by the RBI.

Policy Package (2005) for Stepping Up Credit to SMEs

7.38 Following the UPA Government's promise to help the flow of credit to SSI sector, the Government announced a policy package for stepping up of credit to Small and Medium Enterprises in the Parliament on August 10, 2005. The important elements of the package are as under:

- Public Sector Banks will be advised to fix their own targets for funding SMEs in order to achieve a minimum 20 per cent year-on-year growth in credit to the SME sector. The objective is to double the flow of credit to the SME sector from Rs. 67,600 crores in 2004-05 to Rs. 1,35,000 crores in 2009-10, i.e., within a period of five years.
- Public Sector Banks will be advised to follow a transparent rating system with cost of credit being linked to the credit rating of the enterprise.
- The commercial banks (including regional rural banks) with over 67,000 branches will make concerted efforts to provide credit cover on an average to at least 5 new tiny, small and medium enterprises at each of their semi urban/urban branches per year.
- RBI will issue detailed guidelines relating to debt restructuring mechanism so as to ensure restructuring of debt of all eligible small and medium enterprises at terms which are not less favourable than the Corporate Debt Restructuring (CDR) mechanism in the banking sector.
- A one-time settlement scheme to apply to small scale NPA accounts in the books of the banks as on March 31,2006.
- In order to reduce the cost of guarantee to the weaker segments of the borrowers, particularly the tiny units, the CGTSI will be advised to reduce the one-time guarantee fee from 2.5 per cent to 1.5 per cent for (i) loans up to Rs. 2 lakhs (ii) eligible women entrepreneurs, and (iii) eligible borrowers located in the North Eastern region (including Sikkim) and Jammu and Kashmir. Further, public sector banks will be encouraged to absorb the annual service fee in excess of 0.25 per cent in respect of guarantee for all (i) loans up to Rs. 2 lakhs (ii) eligible women entrepreneurs, and (iii) eligible borrowers located in the North Eastern region (including Sikkim) and Jammu and Kashmir.
- To broaden the financing options for infrastructure development in clusters through public private partnership, SIDBI will formulate a scheme in consultation with the stakeholders. SIDBI has already initiated the process of establishing Small Enterprises Financial Centres in select clusters. Risk profile of each cluster would be studied by a professional credit rating agency and such risk profile reports would be made available to the commercial banks. Each lead bank of a district will consider absorption of at least one cluster.
- At the Regional Offices, the RBI will constitute empowered committees with the its Regional Director as Chairman to review the progress in SME financing and rehabilitation of sick small (SSI) and medium units to coordinate with other banks/financial institutions and the State Governments in removing bottlenecks, if any, to

ensure smooth flow of credit to the sector. The regional level empowered committees may decide on the need to have similar committees at the cluster/district levels.

- Banks will ensure specialized SME branches in the identified clusters/centres with the preponderance of small enterprises to enable the entrepreneurs to have easy access to bank credit and to equip bank personnel to develop the requisite expertise. The existing specialized SSI branches will be re-designated as SME branches.
- Boards of banks will be advised to 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 is given to this sector.
- For wider dissemination and easy accessibility, the policy guidelines formulated by boards of banks as well as instructions / guidelines issued by the RBI will be displayed on the respective websites of the Public Sector Banks as well as the website of SIDBI. The banks would also be advised to prominently display all the facilities/schemes offered by them to the small entrepreneurs at each of their branches.

Package for Promotion of Micro and Small Enterprises, 2007

7.39 The Ministry of SSI announced a package for promotion of Micro and Small Enterprises in February 2007. The provisions relating to credit support to this sector are as under:

- In line with the policy package for stepping up credit to Small and Medium enterprises (SME), announced in August 2005 the RBI has already issued the guidelines to public sector banks to ensure 20 per cent year-on-year growth in credit to the SMEs. Action has also been initiated to operationalise other elements of the policy package. Implementation of these measures will be closely monitored by the RBI and the Government.
- SIDBI will scale up and strengthen its credit operations for micro enterprises and cover 50 lakhs additional beneficiaries over the five years beginning 2006-07. Government will provide grant to SIDBI to augment its Portfolio Risk Fund for this purpose.
- Government will also provide grant to SIDBI to enable it to create a Risk Capital Fund (as a pilot scheme in 2006-07) so as to provide, directly, or through intermediaries, demand-based small loans to micro enterprises.
- SIDBI's direct lending operations will be expanded by increasing the number of branches from 56 to 100 in two years beginning 2006-07, with a view to catering to the credit needs of more clusters of micro and small enterprises (MSEs).
- The eligible loan limit under the Credit Guarantee Fund Scheme will be raised to Rs.50 lakhs. The credit guarantee cover will be raised from 75 per cent to 80 per cent for micro enterprises for loans up to Rs.5 lakhs. Accordingly, to strengthen the Credit Guarantee Fund, the corpus of the Fund will be raised from Rs.1,189 crores as on 1 April 2006 to Rs.2,500 crores over a period of five years (with contribution by the Government and SIDBI in the existing ratio of 4:1).
- Moreover, to encourage public sector banks and public financial institutions to contribute to the corpus of the Fund, the feasibility of allowing deduction of their contributions for income tax purposes would be examined.
- The Fund will continue to be maintained with and managed by the Credit Guarantee Fund Trust for Small Industries (CGTSI). The Trust will be renamed as 'Credit Guarantee Fund Trust for Micro and Small Enterprises'(CGTMSE)

An Assessment

7.40 Despite the many committees and interventions by the Government, this Commission feels that no perceptible improvement has taken place with regard to the credit flow to the SSI sector in general and NFUEs in particular. As we have shown in our earlier Chapters of the report, decline in the credit flow to these segments continues unabated. Such a situation that alienates an important segment of the economy, which provides livelihood opportunities to nearly half of the workforce in the non- agriculture sectors should not be allowed to continue. This calls for a major institutional intervention that exclusively addresses the credit and other related problems of NFUEs. This has been dealt in a separate report by the Commission, which recommended the creation of a National Fund for the Non- farm Unorganised Sector.

8 Policies and Institutional Arrangements for Financing Unorganised Enterprises: International Experience

Introduction

8.1 Small business units are globally known as Small and Medium Enterprises (SME). These include micro/tiny and unorganised enterprises. In India, however, the small enterprises are known as Micro, Small and Medium Enterprises (MSME) and each segment has been clearly defined under two broad categories of manufacturing and services. In India, micro enterprises which include a large segment of the unorganised enterprises are included as identified segment of the small enterprises, since over 99 per cent of them exist as micro enterprises. Considering the important role played by SMEs in employment generation, export promotion and income redistribution, this sector receives policy support in all countries of world, whether developing or developed. Special schemes and institutions exist almost every where for the financing of SMEs.

Definitions

8.2 Before the issue of financing of such enterprises is considered, it may be relevant to look into the definition of Small enterprises as it exists in various countries as shown in Table 8.1.

Developmental Financing Agencies and Programmes in Various Countries

USA

8.3 US Small Business Administration Act is considered the most effective and comprehensive measure taken by any country for the promotion of small business in the country. Hence it is essential to go in to the details of the working of this Act.

8.4 Through the US Small Business Act of July 30, 1953, Congress created the Small Business Administration, whose function was to "aid, counsel, assist and protect, in so far as is possible, the interests of small business concerns". The charter also stipulated that the SBA would ensure small businesses a "fair proportion" of government contracts and sales of surplus property. By 1954, SBA already was making direct business loans and guaranteeing bank loans to small businesses, as well as making loans to victims of natural disasters, working to get government procurement contracts for small businesses and helping business owners with management and technical assistance and business training. The Investment Company Act of 1958 established the Small Business Investment

Table 8.1: Definition of Small Enterprises in Asia and Other Countries

Country	Category of Industry	Criteria/ Country's Official definition	Measure
North America			
USA	Very small enterprise Small Enterprise Medium Enterprise	< 20 employees 20-29 employees 100-499 employees	Employment
Canada	Manufacturing	Independent firms having <200 employees	Employment
Latin America			
Mexico	MicroSmallMedium	<15 employees and gross income/sales<US$ 175,000 15-99 employees and gross income/sales <US $175,000 100-249 employees and gross income/sales<US$3,500,000	Employment and gross income/ sales
Europe			
Belgium	SME	Annual staff average of 50 employees, annual turnover (VAT excluded ECU - 4.2 million, balance sheet total of ECU 2.1 million	Employment and annual turnover
Denmark	Manufacturing	<500 employees, Production units with more than 5 employees	Employment
France	SME	10-499 employees	Employment
Germany	SME	<500 employees	Employment
Greece	Small Enterprise Medium Enterprise	<50 employees 50-500 employees	Employment
Ireland	SME	<500 employee	Employment
Italy	Small Enterprise	<200 employees	Employment
Netherlands	Small Enterprise Medium Enterprise	<10 employees 10-100 employees	Employment
Portugall	SME	<500 employees <Esc 2400 million in sales (value for 1993) is not controlled more than 50 per cent of any company (nor does it hold more than 50 per cent of any other company)	Employment and sales value
Spain	Small Enterprise Medium Enterprise	<200 employees <500 employees	Employment Employment
Sweden	SME	Autonomous firms with < 200 employees	
Switzerland	SME	No fixed definition	
United Kingdom	SME	No fixed definition	
Asia			
China	SME	Depends on product group. Usually <100 employees. Investment ceiling 30 million Yuan (US$ 8 million)	Employment & investment
Indonesia	SME	<100 employees	Employment
Japan	Manufacturing Wholesale TradeRetail Trade and Services	<300 employees or asset capitalization <100 million yen <50 employees or asset capitalization <30 million Yen <50 employees or asset capitalization <10 million Yen	Employment and assets
Korea	Manufacturing services	<300 employees <20 employees	Employment

Table 8.1 Cont.....

Country	Category of Industry	Criteria/ Country's Official definition	Measure
Malaysia	SMIs	<75 full time workers or with a shareholder fund of <RM 2.5 million (US$ 1 million)	Employment and share holder fund
	Sis	Manufacturing establishments employing between 5 and 50 employees with a shareholder fund upto RM 5000,000	
	Mis	Manufacturing establishments employing between 50 and 75 full time employees or with shareholders fund between RM 5000,000 to RM 2..5 million	
Singapore	Manufacturing Services	<S$ 12 million fixed assets <100 employees	Fixed assets Employment
Taiwan	Small enterprise	In manufacturing, mining and construction-invested capital is <NT$40 million or regular employees to <200	Employment or invest capital
	Small enterprise	In manufacturing and construction-sales turnover <NT$120 million or regular 20	Employment or sales turnover
Thailand	Labour intensive sectors Capital intensive sectors	<200 employee <100 employee	Employment
Vietnam	SME	No fixed definition, generally <200 employees	Employment
Brunei	SME	0-100 employee	Employment
Hong Kong	SME	Manufacturing enterprises with fewer than 100 employee and non manufacturing enterprises with fewer than 50 employee	Employment
Australia	Manufacturing Service	Small enterprise <100 employee Medium enterprise<20 employee	Employment

Note : In most part of the globe, SMEs are defined in terms of employment. In some countries this is also backed by the criterion of turn over or sales.

Sources: SIDBI's Report on Small Scale Industries Sector 2001.

Company (SBIC) Program, under which SBA licensed, regulated and helped to provide funds for privately owned and operated venture capital investment firms. They specialized in providing long-term debt and equity investments to high-risk small businesses. Its creation was the result of a Federal Reserve study that discovered in the simplest terms that small businesses could not get the credit they needed to keep pace with technological advancement. In 1964, SBA began to attack poverty through the Equal Opportunity Loan (EQL) program and relaxed the credit and collateral requirements for applicants living below the poverty level in an effort to encourage new businesses that had been unable to attract financial backing, but was nevertheless sound commercial initiatives.

8.5 Over the past 10 years, (FY 1991-2000), the SBA helped almost 435,000 small businesses to get more than $94.6 billion in loans, the highest in the entire history of the agency before 1991. No other lender in the country - perhaps no other lender in the world - has been responsible for as much small business financing as the SBA has during that time. Since 1958, SBA's venture capital program has put more than $30 billion into the hands of small business owners to finance their growth.

8.6 The United States offers a very attractive environment for the venture capital industry with a number of factors which make it much more market-oriented, including flexible labour laws which makes it easier to enter and exit the jobs, low taxation, and less regulation.

8.7 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.

China

8.8 Since China's reform and opening up, SMEs have gradually enjoyed a healthy external environment for development. By reforming the system of a planned economy, the nation relaxed its limitations on the development of SMEs so that urban collective enterprises, township and village enterprises, individual businesses, private enterprises, foreign-funded enterprises and joint ventures could rapidly develop. Regarding the various forms of SME ownership, different development policies were adopted. For state-owned SMEs, from its efforts to "decentralize authority to release benefits" (fangquan rangli) in 1978 to "grasp the large and let go of the small" (zhuada fangxiao) adopted at the Third Plenary Session of the 14th Central Committee in 1995, the Government's policy has focused on reforming the old system which did not adapt to the demand of a market economy. In the mid-1990s, China adopted the policy of "deregulation to render agile" (fangkai gaohuo) and privatization policy for small-sized state owned enterprises. Many state-owned and collective SMEs reinforced their competitive activities through reform and "privatization", which transformed the system of property rights and managements. As for non-state-owned SMEs, China mainly adopted policies of relaxing policy restrictions, granting political acceptance and financial support, and gradually established a market environment of fair competition and legal protection. As the main body of SMEs, township and village enterprises, individual and private enterprises that rapidly developed in the mid-to late-1990s, gradually improved their status and function in the national economy.

8.9 Since the mid 1990s, developing SMEs has been an important strategy in China. The Asian financial crisis of 1997 made the Chinese Government and academic circles completely rethink the shortcomings of the strategy that relied on large enterprises. The Government and its institutions came to recognise the need to the development of SMEs. From 1999, the Ministry of Finance and other departments started to actively establish a SMEs loan guarantee system. By 2001, they published some laws and regulations, such as the Provisional Regulation of SME Credit Guarantee System and Management Methods of Credit Guarantees for SMEs. By the end of 2000, 30 provinces, municipalities and autonomous regions in China had opened pilot sites for the SME credit-guarantee system, established more than 200 credit-guarantee institutions, raised a guarantee fund of 10 billion Yuan, and put forth an important effort to improve the credit environment for SME development. The Ministry of Science and Technology provides 10 billion Yuan per year to build venture capital funds for hi-tech enterprises. Shanghai established the Shanghai SMEs Service Center, which released 13.9 million Yuan in credit to 11 SMEs from June to September 1998 (Wang, Y, 2004). The Shanghai Branch of the China Industrial and Commercial Bank set up SME credit departments and took 10 measures to support SMEs. By April, 1999, it had shelled out about 300 million Yuan in credit to SMEs.

8.10 Throughout the reform process and especially in recent years, China has begun placing emphasis on the issue of supporting SME development. But there are still many problems in the relevant policies. First, China lacks a long-term, systematic, unified and relatively independent SME development strategy and policy system. Second, the SME management system and relevant policies are inconsistent, and basic management is weak. Furthermore, since the design of the social service system is severely behind the times, the burden of taxation and quotas is heavy. Finally, without sufficient financial support for SMEs, difficulties in obtaining loans and raising funds will block SME development. Banks are structurally weak and have not yet specialized in SME financing.

Canada

8.11 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 complementary source of SME financing. The Canada Small Business Financing Act (CBFSA) programme has been in existence in the form of a five-year pilot project for capital leases called the Capital Leasing Pilot Project, which gives the small enterprises an additional financing option, thereby serving the needs of smaller and younger firms, which were earlier, underserved.

Japan

8.12 The Japan Finance Corporation for Small Business supplies the long-term capital to develop SME businesses and offers small enterprises long-term, fixed-interest, low-interest capital. 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 small enterprises. The two institutions playing important role in financing are:

- The **Shoko Chukin Bank** is a full-service financial institution with funds not only from the government but also from SME cooperatives and other organisations that serve the co-operatives, their members, and other clients.

- The **National Life Finance Corporation** offers primarily small, unsecured loans for very small companies.

Korea

8.13 To facilitate SME's access to bank loans, Korea established the Industrial Bank, which awards the bulk of its lending to small enterprises. The SME Promotion Fund provides funds for restructuring projects to business start-ups and to small enterprises less than three years old. The Korean Government is focusing on the improvement of direct financing for small enterprises. Salient features of SME financing are as under:-

- Where venture capital was provided by way of loans in the past, now small enterprises receive financing in the form of investment. The investment-to-loan ratio of venture capital has surged from KRW 1.1 Trillion in 1997 to 35.4 Trillion 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 Small and Medium Business Administration (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.

Philippines

8.14 The Development Bank of the Philippines (DBP) provides wholesale credit through the Industrial Support Services Expansion Programme (ISSEP). Through the Industrial Guarantee and Loan Fund (IGLF), it provides credit supplementation support by the extension of guarantee schemes to stimulate the flow of credit to small enterprises. **Small Business Guarantee Fund Corporation** (SBGFC) has the following financing programmes:

- ***SME Force*** - (Financing for organisationally 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 small enterprises in the domestic economy.
- *First Light* is a financing programme 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 programme, which immediately addresses the credit needs of small enterprises, particularly in the export sector.
- *Window III* - is the centerpiece of DBP's retail lending operations. It finances innovative and socially desirable projects with high developmental impacts. Funds are made available to non-government organisations (NGOs) for re-lending to eligible micro enterprises. The Export Assistance Network (EXPONET) serves as a trade facilitation office that provides real and immediate assistance to the existing and potential exporters.

Spain

8.15 The ICO-PYME (Official Credit Institute-SME) facility is meant to provide financing under preferential conditions, for investment projects undertaken by the small enterprises in Spain. As part of the search for new financing instruments for small enterprises, ENISA (Empress National 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. In the light of the difficulties faced by small enterprises in finding finance, suited to their needs in terms of cost and time, the government's policy has been geared, firstly, to easing access to existing sources of financing (by reducing costs, extending terms and providing guarantees) and second, to promoting new finance facilities and instruments. Loans are granted through banks and savings banks and they are available to small enterprises for investment in fixed assets, whether tangible or intangible, with a financing ceiling of 70 per cent 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.

Thailand

8.16 Financial and advisory supports are provided through the newly-established SME Development Bank. It provides various services to the small enterprises in the economy, including debt financing, equity financing, SME counseling, or diversification of loan products and other financial services. The establishment of the Thailand Recovery Fund and the Fund for Venture Capital Investment in small enterprises, 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.

Germany

8.17 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 small enterprises. 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 per cent release from liability, has proved to be particularly helpful for start-up entrepreneurs. To help start-up entrepreneurs and small enterprises gain access to bank credit, loan guarantees have also been made available as the security normally required by banks.

UK

8.18 The UK High Technology Fund (UKHTF) was developed to encourage institutional investment in the 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 the early stage technology investments. The UK Government is working to improve the relationship between banks and small businesses and to enhance access to financing through the setting up of 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 Steerling for small enterprises, but not all the 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 at the necessary minimum to stimulate private sector investors to provide small-scale risk finance for small enterprises with a growth potential. The Government has been working with the main banks and others since 1998 to see that the informal investment market is fully operational in order that business angels can become a mainstream source of finance for small enterprises. Together, they jointly support the National Business Angels Network (NBAN) in England, launched in 1999, which is 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.

Similarity with India

8.19 To sum up, the international experience of SME lending reveals more or less the same features of assistance as are India's development packages and policies. Eligibility is largely dictated by the characteristics of enterprises in the respective countries. Though the eligible enterprises are larger than our standards, the assistance includes relaxed collateral requirements, loan guarantees, counseling sessions (USA); fixed interest, low interest capital (Japan); Industrial Bank in Korea which awards bulk of its lending to small enterprises; financing under preferential conditions (Spain); grants for certification (Czech). Many countries have set up Special Funds to supplement their financial system's resources. Venture capital as source of financing is gaining prominence in many countries in recent years.

9 Problems and Constraints

Disturbing Symptoms

High Non-Performing Assets

9.1 One of the major reasons for discrimination against the SSI sector in India as compared to large industries is the high non-performing assets (NPA). As against an NPA of 8 per cent in respect of large industries, it is as high as 15 per cent in the case of SSI units. However, in absolute terms the amount of non-performing assets is larger in the case of the non-priority sector than the priority sector as can be seen in Table 9.1.

9.2 In 2004-05, out of the total advance of Rs. 11,52,684 crores, the NPA was Rs. 56,496 crores. Whereas as out of the total advance of Rs. 15,51,378 crores the NPA was Rs. 49,208 crore in 2005-06. As percentage of total advances the NPAs of SCBs, have declined from 4.9 per cent in 2004-05 to 3.2 per cent in 2005-06. Within the priority sector out of the total loan of Rs. 1,25,250 crores and Rs. 1,72,292 crores in 2004-05 and 2005-06 respectively to agriculture, the NPAs account for 6.2 per cent and 3.9 per cent respectively. In the case of SSI out of an advance of Rs. 74,588 crores and Rs. 90,239 crores in 2004-05 and 2005-06 NPAs account for 11.8 per cent and 8.6 per cent respectively. This was higher than in the case of agriculture sector.

9.3 To find out the real incidence of NPAs, it would be appropriate to compare the same with the credit extended to that sector as is examined in Table 9.2.

9.4 From Table 9.2 it emerges that NPA in the SSI sector is among the highest. In 2000-01, it was as high as 22.4 per cent in the SSI sector, while it was only 16.9 per cent in the case of agriculture and other priority sectors and 15.3 per cent in the case of large industries and the non-priority sectors. Even in 2003-04, when there has been a decline in NPA for the entire banking sector, it was 15.1 per cent in the case of SSIs, 8 per cent in the case of agriculture and other priority sectors and 8.3 per cent for large industries and non-priority sectors. Thus as compared to large industries, the NPA in SSI is almost the double. This deters banks from advancing credit to the SSI sector even though it happens to be one of the priority sectors of the economy. Banks prefer to extend loans to transport, retail trade and small business since these are less risky than manufacturing and the recovery rate is high.

Table 9.1: Sector-wise NPAs of SCBs (Rs. Crores)

	2004-2005			2005-2006		
	Total Credit	NPA	Per cent to total Credit	Total Credit	NPA	Per cent to total Credit
SCB Credit	11,52,684	56496	4.9	15,51,378	49208	3.2
Agriculture	1,25,250	7719	6.2	1,72,292	6718	3.9
SSI	74,588	8799	11.8	90,239	7725	8.6
Other Priority Sector	1,81,638	9067	5.0	2,47,379	10215	4.1

Source : RBI, Report on Trend and Progress of Banks in India, 2005-06

Table 9.2: Public Sector Banks - NPAs (Rs. crore)

Year	Total Credit	SSI Sector		Agriculture and Other Priority Sectors		Large Industries and Non-Priority Sectors	
		Credit	NPA	Credit	NPA	Credit	NPA
2000-01	3,16,427	46,045	10,339 (22.4)	81,433	13,817 (16.9)	1,88,949	29,018 (15.3)
2001-02	3,41,291	48,400	10,584 (21.9)	1,00,716	14,555 (14.4)	1,92,175	31,367 (16.3)
2002-03	3,94,064	54,268	10,161 (18.7)	1,17,217	14,777 (12.6)	2,22,579	27,869 (12.5)
2003-04	5,60,819	58,311	8,838 (15.1)	1,86,145	15,001 (8.0)	3,15,363	26,308 (8.3)

Note: Figures in parentheses denote NPA as percentage to total credit to that sector.
Source: Compiled on the basis of data from Economic Survey 2005-06, and RBI data supplied to Ministry of SSI.

Decaying State Financial Corporations (SFCs)

9.5 The SFCs are mandated to serve as regional/ state level financing agencies for the promotion of regional growth in the country through the development of small scale and medium enterprises. The SFCs are currently in a bad shape and their contribution to the unorganised sector loans is almost negligible. The asset base of SFCs has been shrinking. The SFCs have themselves been borrowing capital to meet their day-to-day and other expenses. The SFCs suffered a combined net loss of Rs. 427 crores in 2004. The details of the sanctions and disbursements by the SFCs during the last three years are given in Table 9.3.

Table 9.3: SFC Credit to SSIs

	SSI Sector (Rs. Crores)		Total (Rs. Crores)	
	Sanctions	Disbursements	Sanctions	Disbursements
2001-02	1,171	1,254	1,838	1,722
2002-03	1,158	1,077	1,398	1,289
2003-04	1,016	864	1,256	1,005
Cumulative*	27,711	23,670	37,540	31,284

Note: * Up to 31st March, 2004 since inception.
Source: RBI, Report of Trends and Progress of Banks in India ,2004-05.

High Incidence of Sickness in the SSI Sector

9.6 The data compiled by the Reserve Bank of India from the scheduled commercial banks, indicates the status of sick SSI units, potentially viable units and units under nursing as given below in Table 9.4.

Table 9.4: Status of Sickness in SSI Sector

As at the end of March	Number of sick units	Amount Outstanding (Rs. Crores)	Potentially viable units	Units under nursing
2000	3,04,235	4,608	14,373	663
2001	2,49,630	4,505	13,076	753
2002	1,77,336	4,819	4,493	621
2003	1,67,980	5,706	3,626	993
2004	1,38,811	5,285	2,385	NA
2005	1,38,811	5,380	NA	NA

Source: RBI, Handbook of Statistics on Indian Economy, 2005-06.

9.7 The number of sick units appears to have declined. In reality, however, this is not so. The decline is on account of a revision in the bank's policy to show sick units separately from the books of account and pursue the issue of recovery and demand notices. Inspite of the change in mode of showing sick units, there is a steady increase in the amount under default. In fact, per unit default has increased from Rs. 1.60 lakhs in 2000 to Rs. 3.90 lakhs in 2005. However, the major problem is the lack of revival plans of the sick units or an exit route. Table 9.4 shows that as on March 2003, out of 1.67 lakh sick units, only 3,626 units were identified as potentially viable by the banks (i.e. 2.16 per cent of the total sick units). Of these, only 993 units were put under nursing by the banks, which is indicative of the slow pace of the rehabilitation process. Further, as per the guidelines of RBI on the rehabilitation of sick SSI units, only those sick units, which are considered potentially viable /viable are to be taken up for rehabilitation. Thus, there is no mechanism for addressing the problems of a large number of units, which are in the 'non-viable' category. There is, therefore, a need to put in place a debt restructuring mechanism to address the concern of units under the 'non-viable' category as well as those at the incipient stage of sickness. A convenient 'exit' route needs to be created for non-viable sick units so that the amount blocked in sick units could be released to productive use.

Recent Changes in Banking Policy

9.8 Indian economy entered a new phase of economic reforms in 1991-92. The recommendations of the Narasimham Committee (1991) charted a road map for reforms in the financial sector. Statutory measures like the Cash Reserve Ratio (CRR), Statutory Liquidity Ratio (SLR) and the Bank Rate (BR) underwent a series of changes through the relaxation of the controls hitherto imposed on the banking sector. The CRR, SLR and BR were ruling high at the beginning of the 1990s at around 15 per cent, 31.5 per cent and 12 per cent respectively. In addition, the banking sector was also subject to a sector-specific credit ceiling. These factors restricted the availability of funds with the banking system for credit disbursement. With the advent of reforms and the implementation of the Narasimham Committee recommendations, these ratios and the bank rate were gradually lowered and more funds were made available to the banks for credit delivery purposes. In addition, the economy also witnessed a significant change in the interest rate structure, in the deposit and lending rates as well as in the credit delivery system. Banks were given more freedom to choose the loan, taking into account the client's creditworthiness. Against a fixed ceiling rate of 16.5 per cent on advance, a minimum rate of lending was fixed. As a result, the less creditworthy SSIs, Tiny Units and Village Industries suffered which is evident from the declining credit to them in percentage terms.

Dilution of Priority Sector Lending

9.9 The present position of the priority sector lending and the targets and sub-targets in operation for domestic and foreign banks are given in Table 9.5.

The problem in composition

9.10 It all began with the banking sector reform agenda as recommended by the Narasimham Committee Report-I (1993) and, to an extent, even somewhat earlier when dealers in agricultural machinery, short-term advances to plantations (tea, coffee, rubber and spices) regardless of the size of landholding and transport operators owning ten vehicles instead of six, were included under the priority sector. The Committee had observed that the system of 40 per cent directed credit should be phased out. But because of the society's imperative needs supported by political compulsions, the 40 per cent target for the priority sector could not be dispensed with. Instead, what the authorities have done has been to nullify, through the back door, the operational relevance of the priority sector target by including a vast number of items which, by no stretch of imagination, can be conceived of as belonging to the weaker sections, who would not possess other bankable projects and who would otherwise face difficulty in getting bank credit. The following extensive extract from the latest RBI Report on Trend and Progress of Banking in India 2004-05 speaks volumes for the extent to which the coverage under priority sector lending has increasingly moved away from the original intensions of the programme:

> *"In order to align bank credit to the changing needs of the society, the scope and definition of priority sector have been fine tuned over time by including new items as also by enhancing credit limit of the constituent sub-sectors. As part of this process, some more measures were initiated in 2004-05. First, the ceiling on credit limit to farmers against pledge/hypothecation of agricultural produce (including warehouse receipts) was increased from Rs. 5 lakh to Rs. 10 lakh under the priority sector. Second, the limit on advances under the priority sector for dealers in agricultural machinery, including drip/sprinkler irrigation systems*

Table 9.5: Targets of Priority Sector Lending

	Domestic Banks	Foreign Banks
Total Priority Sector advances	40 per cent of Net Bank Credit (NBC) (60 per cent for RRBs and primary urban cooperative banks)	32 per cent of NBC
Total agricultural advances	18 per cent of NBC However, advances under indirect lending to agriculture in excess of 4.5 per cent of NBC not to be reckoned in computing performance under the sub-target of 18 per cent.	No target
SSI advances	No target	10 per cent of NBC
Tiny sector within SSI	40 per cent of SSI advances to units having investment in plant and machinery up to Rs. 5 lakhs, 20 per cent to units with investment between Rs. 5 lakhs and Rs. 25 lakhs (Thus, 60 per cent of SSI advances to go to the tiny sector)	Same a for domestic banks
Export credit	Export credit not to form part of priority sector	12 per cent of NBC
Advances to weaker sections	10 per cent of NBC (15 per cent for RRBs and 25 per cent for primary (urban) cooperative banks.	No target
DRI advances	1 per cent of previous year's total advances	No target
Contribution to RIDF/ SIDBI	Shortfall subject to a maximum of 1.5 per cent of NBC, contributed to NABARD's RIDF at 8 per cent rate of interest. No such penalty provision for RRBs.	Shortfall to be contributed to SIDBI'S corpus at a rate of interest ranging from the Bank Rate and the Bank Rate minus 3 per cent determined as inversely proportional to the shortfall.

Source: RBI's Internal Working Group on Priority Sector Lending (Chairman C.S. Murthy, September 2005)

was increased from Rs. 20 lakh to Rs. 30 lakh and for distribution of inputs for allied activities from Rs. 25 lakh to Rs. 40 lakh. Third, banks were permitted to extend direct finance to the housing sector up to Rs. 15 lakh, irrespective of location, as part of their priority sector lending. Fourth, investments by banks in the mortgage backed securities (MBS) have been classified as direct lending to housing within the priority sector lending subject to certain conditions. Fifth, loans advanced to distressed urban poor to prepay their debt to non- institutional lenders, against appropriate collateral or group security, have been classified as advances to weaker sections within the priority sector. Sixth, the investment limit in plant and machinery for seven items belonging to sports goods, which figure in the list of items reserved for manufacture in the small scale industries (SSI) sector, was enhanced from Re. 1 crore to Rs. 5 crore for the purpose of classification under priority sector advances. Seventh, banks were urged to make efforts to increase their disbursements to small and marginal farmers to 40 per cent of their direct advances under Special Agricultural Credit Plans (SACP) by March 2007. All private sector banks were also asked to formulate SACP targets from 2005-06 with an annual growth rate of at least 20-25 per cent of credit disbursements to agriculture. Eight, investment by banks in securities assets has been classified as their direct lending to the SSI sector under priority sector lending, subject to certain conditions". (RBI 2005)

Loss of Momentum in Bank Credit to Small Borrowers

9.11 There has been a drastic fall in the number of bank accounts of small borrowers. Between 1972 and 1983, there were 21.2 million additional bank loan accounts in the aggregate nursed by the Scheduled Commercial Banks, of which 19.8 million or 93.1 per cent were accounts with Rs.10,000 or less of credit limits. This trend of focusing on small borrowal accounts continued for another decade. Between 1982 and 1992, there were 38.1 million additional bank accounts, of which 36 million were the redefined small borrowal accounts with a credit limit of Rs.25,000 and less. Between March 1992 and March 2001, there has been an absolute decline of about 13.5 million in the aggregate bank loan accounts and this has happened entirely because of a much larger decline of 25.3 million accounts for the redefined small borrowal accounts of Rs.25,000 or less as could be seen in Table 9.6.

Table 9.6: Trends in the Number of Small and Large Borrowal Accounts (million)

Period end	Total Bank Borrowal Accounts	Small Borrowal Accounts (Rs.25000 & below)	Other Bigger Accounts
December 1983	27.75	26.52	1.23
March 1992	65.86	62.55	3.31
March 2001	52.37	37.25	15.11
March 2005	77.15	38.73	38.42

Source: RBI, Bank Statistical Returns, various issues

Non-Adherence to RBI Guidelines

9.12 The Commission would like to record some other disturbing trends noticed with regard to credit to small enterprises. These are: (i) Inadequate coverage of working capital which is currently ranging between 10 and 13 per cent against the RBI norm of 20 per cent of projected turnover to be given as working capital. (ii) Insistence on collaterals even on a loan of up to Rs. 5 lakhs, in spite of RBI guidelines to this effect (loans without collateral out of a total loan below Rs. 5 lakh to SSI was 25.9 per cent in 2004-05). (iii) Neglect of small loans since the share of loans below Rs. 25,000 has declined from 21 per cent of total outstanding of Scheduled Commercial Banks' outstanding in June 1985, to 3.7 per cent in March 2005. (iv) Disinterest of banks in advancing loans under Credit Guarantee Scheme, available for loans up to Rs 25 lakhs (since during the last 5 years of existence of this scheme, the quantum of loans advanced under guarantee cover does not exceed Rs. 1,400 crores as per data for December, 2006). These figures clearly indicate the extent to which RBI guidelines are being ignored by the banks.

9.13 The Commission finds that the credit to enterprises below Rs. 5 lakhs of investment has largely been based on piggy backing on government programmes such as PMRY, REGP and SGSY, which have a component of subsidy on bank loan either as interest subsidy or margin money support. Further, for the comfort of banks, there are number of schemes such as the Credit Guarantee Fund, Technology Upgradation Fund, and Credit Linked Capital Subsidy Scheme for Technology Upgradation. However, in spite of these schemes aimed at enhancing the confidence of banks in small loans they have, by and large, not taken steps to extend credit through these schemes. Many bank branches do not display these schemes. Even though banks have entered into MOU with Guarantee Fund Trust, many of their branches express their lack of awareness about the existence of credit guarantee schemes.

9.14 There are also problems of inadequate institutional infrastructure at field level. In recent years the number of commercial bank branches in rural areas declined from 35,134 in March, 1991 to 30,572 in March, 2006. This looks like the reversal of the trend in extending banking facilities that began in the early seventies after the nationalization of major private commercial banks. It has also been reported that a large number of vacancies remain unfilled for quite sometime. Recruitment of professionally qualified persons for evaluating project proposals is also on the decline. It has been reported that a number of new generation private generation banks resort to hiring employees through contract agencies resulting in a disconnect between banking institutions goals and responsibilities on the one hand and commitment of employees on the other. These unhealthy practices permitted in the name of competition and profitability could prove to be counterproductive to the long term credibility of banking institutions.

9.15 It was also revealed that the first generation entrepreneurs suffer also due to lack of technical guidance in the selection of suitable projects particularly at the level of rural bank branches. This is also reflected in bank's apathy in propagating and adopting the agency models of business facilitators and correspondents in extending the coverage of credit to the neglected areas and segments of society which is further hampered by severe shortage of staff in rural area branches. Normally, people blame lower level functionaries and branch managers for the apathy to small borrowers. A close look at the RBI guidelines/directives to banks particularly the one on 30th April, 2007 regarding the priority sector guidelines(Appendix 1) , and instructions relating to adherence of Basel norms, reveal that apathy either deliberately or by mistake also exists at the top and policy planning levels.

9.16 As against the supply side constraints mentioned above, there are also certain demand side constraints arising out of the inherently 'weak' position of the small enterprises in general and the NFUEs in particular. Some of them, seen as important enough to merit the attention of the Government as well as the RBI, are dealt with below.

9.17 One of the major constraints is the inability of the NFUEs to meet collateral requirements: Banks demand collaterals, which poor unorganised sector borrowers lack in spite of RBI guidelines that loans up to Rs. 5 lakhs should be given without collaterals. This is also one of the reasons for not encouraging borrowing under the credit guarantee scheme. However, the problems with the poor and assetless borrowers is that they do not have property to place as collateral in the absence of which banks are not interested in making advances to unorganised sector borrowers. According to Rural Finance Access Survey of the World Bank and NCAER (2003) 89 per cent of the households surveyed who borrowed from RRBs and 87 per cent of households who borrowed from commercial banks, reporting that they had to provide collaterals.

9.18 As the Credit System operates under the existing guidelines of the RBI, it emerges that the small borrowers are competing with large and strong borrowers. It can be noted from the Priority Sector Lending Guidelines of 30th April 2007 issued by the RBI (Appendix 1) that, in the agricultural sector, there is a mention of short term loans for raising crops; loans to small and marginal farmers; distress farmers without any stipulation on the minimum or maximum amount. There is a mention of advances up to Rs. 10 lakhs for hypothecation of agricultural produce, loans for food and agro-based processing units with investment in plant and machinery upto Rs.10 crores, loans for construction and running of storage facilities and finance extended to dealers in drip irrigation/agricultural machinery with ceiling up to Rs. 30 lakhs. From the existing priority sector guidelines the corporates can borrow direct crop loans for agriculture up to Rs. 1 crores and indirect loans for agriculture and allied activities (dairy, fishery, piggery, poultry, bee-keeping etc) of up to two thirds of any amount of loans under the priority sector lending policy of the banks. This clearly shows that the small or the poor farmers have to compete with large and strong borrowers such as corporates, traders and institutions. Similarly, even for education, the guidelines provide for loans up to Rs. 10 lakhs and Rs.20 lakhs and for housing, the loans go up to Rs. 20 lakhs, although there is a provision for repairs of dwelling units up to Rs. 1 lakh in rural and Rs. 2 lakhs in urban and metropolitan areas. The housing loan is also available to governmental agencies and NGOs subject to a ceiling of Rs.5 lakhs per dwelling unit. Here again, it is evident that due to dilution of priority sector lending policy, the poor are competing with the comparatively stronger claimants. Such a guideline of priority sector lending, has, in our view, made a mockery of the concept of 'weaker sections'.

9.19 Unorganised enterprises have to pay interest at 2 per cent less than the PLR i.e. at 9.5 per cent on a loan of up to Rs. 2 lakhs. And above the PLR on higher loans i.e. at 13.5 per cent. PLR varies from bank to bank. Currently average PLR is 11.5 to 12 per cent. In addition they are required to pay various service charges which raise the cost of credit by another 2 - 3 per cent. Thus, the total cost of credit is 16 per cent. As against the above, the rate of interest for large industries is often lower than the PLR on the ground of better credit worthiness. The rate of interest on agriculture credit on a loan of up to Rs. 3 lakhs is 7 per cent. Thus, while the large enterprises pay a rate of interest lower than the PLR, micro enterprises pay an interest between 13 and 16 per cent. In addition to the higher cost of credit, banks levy heavy service charges in the name of processing fee, renewal fee, bankers cheque charges, statement charges, payments to chartered accountants for obtaining records and so on. These add up to another 2 per cent of the cost. All these charges raise the cost to prohibitively high levels. The higher cost of credit makes the small enterprises especially the NFUEs uncompetitive, a sector which has the potential of generating large-scale employment opportunities at a lower capital cost.

9.20 Apart from the cost of credit, the small borrowers have to incur many other expenses. Firstly, there are factors like distance of the bank branches from their residences/ places of work, time taken in processing loan applications and number of visits required to get the loans sanctioned. According to Rural Finance Access Survey by World Bank and NCAER (2003) in Andhra Pradesh and UP, in 2003, the median distance to the nearest bank branch was 5 km. Keeping in view the average time taken for a loan decision (28.5 weeks and 33 weeks for commercial banks and RRBs respectively) it may result in at least 6 to 7 visits to the branch as observed by the National Commission on Farmers (2006, Fourth Report p.383). These factors discourage the small borrowers in approaching the banks for credit. Small borrowers find the informal channels (money lenders etc.) preferable since they take on the spot decisions. Moreover, distance, delay and number of visits mean additional cost to the borrowers. Sometimes, these costs become so high that in spite of the comparatively lower rates charged by the formal institutions, it works out more or less equal to the rate of interest charged by informal agencies. Unorganised enterprises being mostly one man shows, a visit to bank means disruption/closure of the enterprise for the day resulting in loss of production and earning. An additional factor is the compliance of large number of formalities including filling of various forms, submission of several documents (which more often than not require payment for services to someone who can fill the forms for the illiterate or semi-literate entrepreneur) etc. This also adds to the cost and then the institutional interest is often higher or, at best equal to the rate of interest charged by the informal sources.

9.21 Services provided by the banks do not meet the total credit needs of the unorganised sector borrowers. Banks particularly in rural areas do not provide flexible products and services to meet the income and expenditure patterns of the small unorganised sector borrowers. Such borrowers have irregular/volatile income streams and expenditure needs (social functions-births-marriage, sickness) and repay in small installments but most banks do not offer such products.

9.22 RBI has revised the NPA norms for default in the repayment from 180 days to 90 days. This means even failure in repayment of loan for one quarter would attract the provisions under the Banking Securitisation Act (2002) that confers powers to banks to auction the property of the defaulting unit if the loan amount is above Rs. 1 lakh. While large units take recourse of BIFR and save themselves from the harassment by banks, it is often the small entrepreneurs who face the music and find their factories getting auctioned.

9.23 Unorganised entrepreneurs' inability to meet all documentation requirements for availing bank credit creates a wide gap between the lender and loanee. Weaker sections' entrepreneurs face difficulty in meeting the documentation requirements because of various factors particularly due to their weak financial base, difficulty in establishing right over property (which are often joint property), difficulty in finding guarantors and last but not least difficulty in understanding the exact requirements due to their low educational levels and lack of guidance. Banks find it difficult to advance loans in the absence of proper documents.

9.24 Unorgansied sector entrepreneurs prefer raising loans from money lenders since it is available at their door-step and that too hassle free, even though the rate of interest is high. The All India Debt and Investment Survey (2002) reveals that the share of moneylenders in total dues of the rural households rose from 17.5 per cent in 1991 to 29.6 per cent in 2002. What makes the moneylenders service grow in rural and non-farm sector? The reasons seem to be clear. The information problem is serious in rural credit markets. Banks cannot match money lenders in getting information on the credit worthiness of borrowers and their utilisation and repayment capacity. The high rates of interest charged by money lenders is partly on account of collecting information on the credit worthiness of the borrowers, monitoring their actions and ensuring repayments. For unorganised borrowers, timely credit is more important than the associated costs.

10 Recommendations

10.1 The Commission's findings that the non-farm unorganised sector enterprises receive only 5 - 6 per cent of total institutional credit despite contributing 30 per cent to GDP should be viewed as a matter of serious concern in an economy consisting mostly of large number of small enterprises. From the point of the objective of inclusive growth, such a finding poses formidable challenges to the banking system in the country. The Commission's additional finding that enterprises with up to Rs. 5 lakhs investment dominate the non-farm unorganised sector receive only between 2.3 and 3.6 per cent of the total credit, mostly by piggy backing on the government schemes, points to the reality of exclusion of this vast segment from institutional credit.

10.2 In the light of these findings, the Commission recommends the following to improve access to finances for the unorganised sector. These may be grouped into (a) supply side issues, (b) demand side issues and (c) development support.

Supply side Intervention

1. Revise Priority Sector Guidelines

10.3 In order, to ensure increased access to credit, the first task is to revise the priority sector guidelines to focus on lending to the needy sectors. Table 10.1 gives the main features of the RBI guidelines and also the modifications suggested by the Commission. Although the Report deals with only non-farm unorganised enterprises we have also given our suggestions for modifying the priority sector lending policy for agriculture in line with our recommendations given in an earlier Report on Conditions of Work and Promotion of Livelihood. The Commission also feels that even the guidelines pertaining to weaker sections needs to be tailored in favour of the most vulnerable sections of the society.

Table 10.1: Priority Sector Lending Policy (PSLP)

Existing Provisions	Proposed by the Commission (NCEUS)
Agriculture and Allied Activities (Dairy, Piggery, Poultry etc.)	
• 18 per cent of Adjusted Net Bank Credit (ANBC) reserved for agriculture • Of this not more than 4.5 per cent to be reckoned as indirect credit. **Direct Loan** **To individual farmers and SHGs etc. (No limit)** • Short-term loan for raising crops • Up to Rs. 10 lakhs against hypothecation of agricultural produce • Working capital and term loans • To small and marginal farmers for purchase of land • For pre-harvest activities	• Loan for agriculture and related activities (no distinction of Direct and Indirect loans) to individual farmers and SHGs either directly or through NGOs, MFIs. • Continue with reservation of 18 per cent for agriculture. Of this, reserve 10 per cent of ANBC for marginal farmers (land holding less than 2.5 acres of land) and for landless agricultural labourers, tenants farmers, share croppers) under the above limit. • 8 per cent of ANBC to be fixed for small farmers with land holding between 2.5 and 5 acres and share croppers under the above limit.

Table 10.1 Cont.........

Existing Provisions	Proposed by the Commission (NCEUS)
To others (corporates, institutions etc.) • Loans up to Rs. 1 crore for purposes as available to individual farmers • One third of loan in excess of Rs. 1 crore to above categories. **Indirect Loan** • For others - two third of loan in excess of Rs. 1 crore • To food and agro based processing units upto Rs. 10 crores. • For purchase and distribution of fertilizers, pesticides, seeds etc. • Upto Rs. 40 lakhs for purchase and distribution of inputs • For setting up agriculture clinics • For H/P of agriculture machinery • To PACS, FSS, LAMPS·To NCDC, State Electricity Boards, power distributors·To cooperative societies • For construction and running of storage facilities • To dealers of drip irrigation up to Rs. 30 lakhs per dealer • To commission agents • To NGOs/MFIs	
Weaker Sections	

• 10 per cent of ANBC reserved for this
• 1 per cent of ANBC under DRI scheme at 4 per cent up to Rs. 6000/- Of this 40 per cent for SCs/STs
 	
Eligible categories
• Small and marginal farmers (upto 5acres) landless labourers, tenant farmers, share croppers)
• Artisans, village and cottage industries up to Rs. 50,000/- per individual
• SGSY beneficiaries·SJSRY beneficiaries
• SHGs
• Distressed poor to prepay debt
• Minorities
• SCs/STs
• DRI beneficiaries
• Scavengers' liberation schemes
	- Continue with reservation of 10 per cent of ANBCs for weaker sections
	- upper ceiling of loan be fixed at Rs. 5 lakhs
	
	Eligible categories
	• Loans upto Rs. 5 lakhs to following categories/purposes:
	  - Education
	  - Housing
	  - Retail Trade
	  - SHGs
	  - Distressed poor
	  - Minorities
	  - SCs/STs
	  - DRI beneficiaries
	  - Scavenger liberation schemes

Small Enterprises and Others	
• Small enterprises-10 per cent in the case of foreign banks • Direct finance to small enterprises • Small manufacturing enterprises with investment in P&M up to Rs. 5 crores • Small service enterprises with investment up to Rs. 2 crores • Micro manufacturing enterprises with investment in P&M up to Rs. 25 lakhs • Micro service enterprises up to Rs. 10 lakhs • 40 per cent of Small Scale Enterprises credit reserved for Micro Enterprises up to Rs. 5 lakhs of investment in P&M • 20 per cent of SSE credit reserved for Micro Enterprises between Rs. 5 lakhs and Rs. 25 lakhs of investment in P&M • KVI to be treated as Micro Enterprises	Reserve 12 per cent of ANBC for micro enterprises and others ***Eligible categories*** • Micro enterprises (MEs) up to Rs. 25 lakhs • This will include manufacture, service business, KVI and traditional industries, transport operators and professionals. • Out of which reserve 5 per cent for MEs with investment up to 5 lakhs. Reserve an additional 3 per cent for MEs between Rs. 5 and Rs. 25 lakhs of investment. Remaining 4 per cent for others such as micro credit up to Rs. 50,000 per individual, • Artisans, village and cottage industries up to Rs. 50,000 per individual, • SGSY and • SJSRY beneficiaries

Table 10.1 Cont.........

Existing Provisions	Proposed by the Commission (NCEUS)
Indirect Finance to Small Enterprises • For supply of inputs and marketing • Advance to cooperatives of artisans, cottage and village industries • Loans to NBFCs for MSEs • Retail Trade (fair price shop) consumers cooperatives up to Rs. 20 lakhs) • Micro credit up to Rs. 50,000 • Poor/ indebted in the informal sector • State sponsored organisations for SCs/STs • Education loans up to Rs. 10 lakhs (internal), up to Rs. 20 lakhs (foreign education) • Housing loans up to Rs. 20 lakhs	

10.4 From the aforesaid revision it could be noted that: (a) in so far as agriculture sector is concerned our proposal is that, within the 18 per cent, a reservation of 10 per cent and 8 per cent for marginal and small farmers respectively, (b) for the weaker sections we have fixed an upper loan ceiling of Rs. 5 lakhs for each of the categories along with proposed rationalization of categories, and (c) the segment of small enterprises and others will take up another 12 per cent with micro enterprises up to Rs. 5 lakhs getting 5 per cent and between Rs. 5 lakhs and Rs. 25 lakhs additional 3 per cent along with revision in the eligible categories. Justification for change in the Priority Sector Guidelines is given in Appendix 2.

10.5 It is recommended that the Priority Sector Guidelines be revised as mentioned above and be monitored at District, State, Region and all India levels and appropriate policy interventions be made in case of shortfall, if any.

2. Providing Adequate Safety Nets to the Banks

10.6 The Commission recommends that the guarantee cover under Credit Guarantee Scheme be raised to 90 per cent (from the existing 80 per cent) for loans up to Rs. 5 lakhs. Guarantee fee be reduced to 1 per cent of the loan (as against the current 1.5 per cent) for loan up to Rs. 5 lakhs. The hindrances/road blocks existing in the Credit Guarantee Scheme, which deter the banks to make use of this scheme should be expeditiously removed. The scheme should be made user friendly keeping the interest of both the entrepreneurs and the bankers. 80 per cent of the default sum (as against the existing 75 per cent of default) should be paid to banks on their first reporting of defaults and the balance within the stipulated date by which recovery proceedings are to be completed. More financial institutions such as SFCs, cooperative banks etc., should be included as Member Lending Institutions (MLIs) of the CGTMSE.

10.7 An appropriate credit rating mechanism be introduced, keeping in view the constraints of micro enterprises at affordable cost. Unorganised enterprises due to their inherent weakness cannot fulfill the credit rating requirements, which are easily satisfied by the large enterprises. Moreover, the efficiencies of the micro enterprises cannot be measured through the same yard stick. Hence, a liberal approach should be adopted and a simple system of risk analysis of the borrowers in the non-farm informal sector needs to be evolved and adopted for advancing credit to these enterprises.

10.8 To change the mindset of all those who work for the financing of the unorganised sector, it is necessary to impart suitable training to the personnel so that they appreciate the weaknesses and strengths of the small entrepreneurs. This also calls for the formulation of appropriate personnel policy with regard to training, posting in the rural and semi-urban branches and granting them special incentives along with appropriate rules and regulations to achieve the goal. A proper framework of monitoring the above targets needs to be worked out by all the banks.

3. Penalty to Banks Not Adhering to Priority Sector Guidelines

10.9 As the banking policy exists at present, there is no compulsion that the stipulated targets be achieved. Recent figures indicate that despite reservation of 18 per cent of NBC (Net Bank Credit), credit to agriculture is not more than 12 per cent. Similarly, despite reservation of 10 per cent for the weaker sections actual credit is not more than 6.5 per cent. Due to the existence of attractive alternatives for parking the money with NABARD and SIDBI, banks are not inclined to lend under priority sector. Hence, the Commission proposes that RBI should devise a mechanism to disincentivise depositing money with financial institutions. Further, 50 per cent of the shortfall in the priority sector lending either by domestic or foreign banks should be deposited with the proposed National Fund for Unorganised Sector (NAFUS).

4. Strengthening Delivery Points

10.10 To extend credit to the unorganised enterprises which are currently outside the reach of the banking system (over 95 per cent of enterprises are outside the reach of institutional credit) and also that segment which will get added during the Eleventh Five Year Plan, it is essential to prescribe targets for reaching the unreached. Banks are required to offer loan facilities to the existing and new unorganised enterprises. To achieve this, it is recommended that each bank branch (commercial, RRBs, cooperatives) may consider fixing annual targets of new accounts of non-farm unorganised sector enterprises with the approval of District Level Credit Committees.

10.11 In order to achieve the goal of improving the access to institutional credit of unorganised enterprises, there is a need to further spread the branch network by Scheduled Commercial Banks and RRBs. It is recommended that the Government and RBI policies should consider spreading the institutional network in rural and other financially excluded areas as this vast, regionally spread out non-farm unorganised sector alone has the potential to expand employment opportunities in the country.

10.12 The Government should seriously consider strengthening the existing RRBs and expanding their number to hitherto under-banked areas. The current ownership structure of RRBs should be reviewed with a view to enable them to function independently and catering to the credit and other banking requirements of their respective regions.

10.13 The system of ‘agency banking’ could also be strengthened and used to supplement the operations of bank branches in rural and semi-urban areas. Broad structure of this model has already been outlined by RBI’s Khan Committee and accepted by the RBI.

10.14 Considering the reluctance of commercial banks to operate in non-profitable or less profitable areas and regions, it is necessary to modify the system of measuring profitability at the branch level. It is improper to perceive, even as a business consideration, that every rural branch should achieve a break-even point and reach the stage of profit in three years or so. The expectation should rather be to achieve positive profits in a cluster of bank branches, say within a taluk or even a district. Hence, it is recommended that the profitability should be judged for a cluster of bank branches and not for every branch independently.

10.15 The credit delivery objectives for the informal sectors would be better achieved if there is close coordination between district planning authorities and banking institutions operating in a district.

10.16 The lead bank of the district should identify the nodal bank branch at the taluka/block level. An Annual Action Plan for the non-farm unorganised sector should be prepared both at block and district levels and their implementation be properly monitored at district and state levels, to be reviewed by the banks and the RBI.

10.17 The reach of the commercial banks could be increased through adoption of some of the positive points of micro credit and money lender services. These may consist of : (i) introducing flexible products (like those offered by micro-finance) (ii) composite financial services (like insurance for life, health and crop) (iii) doorstep services (like money lenders) (iv) quick decisions (like money lenders) (v) simplification of procedure to open a bank account by reducing clients transaction cost, (vi) better staffing policies (recruiting staff from local areas who understand clients needs), and (viii) use of technology such as computers, smart cards to cut paper work which will help to reduce the transaction cost of the banks.

10.18 It is recommended that the rural and semi-urban bank branches should be strengthened with technically qualified graduates who can guide the entrepreneurs in the selection and implementation of projects. Banks will, however, have the option either to hire each technical staff on regular basis, or hire them on a short-term basis from the market. The main objective is to provide services and guidance from experts to the farmers as well as unorganised sector enterprises.

5. Strengthen Micro Financing

10.19 Increased involvement of commercial banks in micro financing is absolutely essential for a sustainable micro financing programme in the country. A directive from the government may be helpful for meeting minimum percentages of NBC by way of micro credit in addition to the liberal refinancing facility by NABARD, SIDBI and proposed NAFUS.

10.20 Constraints which inhibit micro finance to graduate to micro enterprise financing should be removed through; (a) support for building assets to run the enterprise (b) increasing product mix by adding insurance, money transfer, along with credit and thrift (c) provision of livelihood finance to take care of essential infrastructural requirements (d) capacity building of SHGs, MFIs, NGOs etc so that the beneficiaries take up projects involving value additions as against mere consumption loans.

10.21 Public policies ought not to consider microfinance as a substitute for the series of other public programmes that have significant impacts on the growth processes and reduction of poverty and unemployment. In this light, a comprehensive framework to revive the cooperative credit system, revitalise the Regional Rural Banks and reorient commercial banking system and removal of hurdles in the working of micro financing initiatives and non-banking financing companies (within the framework of overall financial discipline) need to be given high priority while simultaneously encouraging and enabling the growth of micro-finance movement in India, which has been very successful.

6. Innovative Instruments

10.22 A large number of untried product lines are getting added continuously in India due to emerging ventures like bio-tech, food processing, IT, pharmaceutical sectors etc. . There is a need for the creation of Venture Capital Funds to meet the equity requirements of these units in the initial phase of their working. SIDBI can take a lead in creating a venture capital fund for financing newly emerging product lines. It is recommended that venture capital funds for emerging product lines be set up by the commercial and development banks. The proposed NAFUS should also play a role along with SIDBI in this regard.

10.23 Banks should also be encouraged to go for factoring services for NFUEs in order to address the chronic problem of delayed payments.

Demand side Interventions

1. Rationalising the Cost of Lending

10.24 The rate of interest should be governed by the overall cost and not the specific high cost of lending of small loans alone. The rate of interest on loans up to Rs.5 lakhs to non–farm unorganised enterprises should be same as in the case of agriculture. Employment intensive farm and non – farm unorganised enterprises deserve the same treatment.

10.25 Clusters have emerged as an accepted strategy for small and micro-enterprise development because of their various advantages including the economies of scale. The cluster development programmes are being implemented by various ministries and organisations both at the Central and state government levels. The programme needs support of various service providers such as banks, financial institutions, market development agencies, training institutions, etc. The products need improvement in quality, design etc. If all the service providers fix the price of their services based on their transaction cost and commercial yardsticks, the price of services will become so high that it will be beyond the reach of the clusters. As a result the whole programme will suffer. It is learnt that national level institutions like NIFT, NID etc. charge exorbitantly for rendering their services on quality and design improvement. It is recommended that the Government consider extending financial assistance for procuring the services of specialized institutions at reasonable cost for development of micro enterprises and clusters.

2. Empowering Entrepreneurs

10.26 Various agencies have formulated different types of credit cards catering to the needs of some selected segments to the unorganised sector. These exist in the form of Laghu Udyami Credit Card, Artisan Credit Card and Swarojgar Credit Card. These cards do not cover the entire unorganised sector. Further the multiplicity of cards creates problem for the implementing agencies. All these cards need to be clubbed into one multi-purpose Swarojgar Credit Card for self-employed persons in the unorganised sector. On the pattern of the Kisan Credit Card, a single multi-purpose non-farm informal enterprises credit card can be issued up to an amount of Rs. 10 lakhs as in the case of Laghu Udyami Credit Card. The number of enterprises to be covered by the credit card may be fixed by the Indian Banks' Association in a phased manner so that by the end of the Eleventh Five Year Plan all non-farm unorganised enterprises are issued credit cards. This will enable better access to finance to meet short-term financial needs of the enterprises. No frill accounts are already being promoted and issue of credit cards to all will lead to extension of institutional credit cover in a meaningful way and will reduce dependency on moneylenders.

10.27 This is an age of public private partnership. While the Government may continue as a facilitator, major tasks of guiding the entrepreneurs, arranging their training and skill development, development of infrastructure, marketing, etc. can be done by associations and federations of non-farm unorganised enterprises. However, they are very weak financially, technically and man – power wise. They need to be strengthened. The necessary financial support needs to be given for development of their infrastructure and for their capacity building. Developed associations and federations could provide a link between enterprises and service providing agencies and would play a catalytic role to cluster development and in providing supportive facilities to entrepreneurs.

10.28 The lower segment of micro enterprises with investment in P&M up to Rs 5 lakhs i.e. SSMEs currently facing harassment under the Bank Securitization Act where the limit for action on default is currently at Rs one lakh. This affects the psychological efficiency of the SSMEs as for them there is no recourse such as BIFR, available to the large units. Hence it is recommended that the limit for action on default may be raised to Rs 5 lakhs through an amendment in the Act.

10.29 Apart from the rate of interest which itself is very high for micro enterprises, the banks charge additional 2-3 per cent in the form of servicing charge, processing fee etc. These charges raise the rate of interest further making this sector uncompetitive. It is recommended that these charges be rationalised.

10.30 To address the problems faced by unorganised/informal enterprises in obtaining bank loans it is recommended that at least 2 representatives of NFUEs sector should be included in the Board of Directors of each Public Sector Bank. The membership could be rotated after every 2 years. This will help the unorganised enterprises to place their demands before the policy makers in the banking sector and also to remove supply related constraints.

Developmental Support

1. Ensuring Better Coordination among Development Agencies

10.31 A large number of government departments and agencies are engaged in the task of promotion and development of the unorganised sector including the cluster development. At the Government of India itself, there is large number of ministries engaged in this task and these are Ministries of MSME, Textiles, Food Processing, Rural Development etc. Similarly, there are various all-India boards and Commissions such as Handloom Board, Handicraft Boards, KVIC, Coir Board etc. Then there are a few development banks like NABARD and SIDBI. There is a need to bring about proper coordination so that a holistic view on this subject could be taken. There is a need for convergence of efforts of various development agencies like NABARD, SIDBI, KVIC and Ministries of the Government of India in the implementation of various schemes for the benefit of the unorganised sector. It is recommended that a suitable consultative mechanism be created to bring out the needed coordination and convergence of efforts.

2. Improving Productivity

10.32 Apart from credit, some of the other areas in which the unorganised enterprises face major problems are those of quality and design, and also those arising out of environmental conditions and pollution, difficulties in accessing infrastructure and critical raw materials. Not the least is the problem of marketing. All these constraints affect productivity. There is an urgent need for technology upgradation to improve the quality and productivity and also to meet environmental regulations. There are a few requirements, which cannot be met by individual units but through groups such as clusters. Some other requirements would be better served, if there are proper linkages among large, medium, small and micro enterprises through ancillaries. Each of these tasks whether it is technology up-gradation or marketing, are costly propositions. To induce the enterprises to go for technology up-gradation, adopt pollution control measures, there is the need for inducements through appropriate fiscal support. Similar fiscal inducements are required to encourage a greater linkage among the large, medium, small and micro enterprises.

10.33 Two basic infrastructure problems, which affect productivity relate to poor roads and communication facility in rural and remote areas and inadequate power supply. Along with augmentation of the existing programme, a part of RIDF money needs to be utilized for creating necessary infrastructure for non-farm enterprises.

3. Extending Credit plus Services and Providing Livelihood Finance

10.34 So far, micro credit has confined itself to meeting production and consumption needs of the poor. It has not yet graduated to financing of micro enterprises. Micro credit is not a long- term instrument of financing. It is required till the time the poor is poor. Once the economy assumes a high rate of growth resulting into increased income, increased employment, micro credit may not be required. Micro enterprises need substantial credit say between Rs. 50,000 and Rs. 1 lakh and not the meager sum of Rs 3000, which is currently flowing as micro credit. For this, it is essential that a shift takes place from Micro Credit to Livelihood Finance which is a comprehensive approach for promoting sustainable livelihoods for the micro entrepreneurs. To implement the above recommendations, it would be necessary to strengthen and enlarge the banking structure. The purpose would be served by the adoption of 'Agency Model' of Business Facilitation and Business Correspondents.

4. Strengthening Self-employment Schemes

10.35 There are a large number of government schemes to enhance the flow of credit to this needy sector such as Credit Guarantee Scheme, National Equity Fund Scheme, Rural Employment Generation Programme, Prime Minister's Rozgar Yojana etc. but these are not properly displayed at bank branches resulting into lack of awareness about these programmes. Banks should enhance awareness on government schemes and should give the customers an opportunity to avail these schemes. It is suggested that the loan application should contain a list of all government and other schemes as annexure and should ask the customers if they would like to avail any of these schemes. RBI may issue appropriate guidelines to the banks for the same.

10.36 Since major part of the credit for the lower segment of micro enterprises with investment in P&M up to RS 5 lakh i.e SSMEs flows through the government sponsored schemes in order to expand the employment opportunities in the non farm unorganised sector. There is a case for enhancing their targets substantially. Similarly, the rate of margin money support which varies from scheme to scheme should be made uniform for all the self- employment schemes and be kept at 25 per cent of the project cost as in the case of REGP.

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Appendices

Appendix - 1

RBI/2006-2007/358
RPCD. No. Plan. BC. 84 /04.09.01/ 2006-07

April 30, 2007

The Chairman/ Managing Director/
Chief Executive Officer

[All scheduled commercial banks
(excluding Regional Rural Banks)]

Dear Sir,

GUIDELINES ON LENDING TO PRIORITY SECTOR – Revised

As announced in the Reserve Bank's Annual Policy Statement for the year 2005-06, the prescriptions relating to priority sector lending have been modified and several new areas included from time to time. There is a view that enlargement of areas has resulted in loss of focus. There have also been suggestions for a further review of the eligibility criteria and other related aspects. Further, it is argued that only those sectors that impact large sections of the population, the weaker sections and the sectors which are employment-intensive such as agriculture, and tiny and small enterprises should be eligible for inclusion under the priority sector.

2. In this context, an Internal Working Group was set up in Reserve Bank (Chairman: Shri C. S. Murthy) to examine the need for continuance of priority sector lending prescriptions; review the existing policy on priority sector lending including the segments constituting the priority sector, targets and sub-targets, etc.; and to recommend changes, if any, required in this regard. The recommendations of the Group have been examined in the light of the comments/suggestions received from the banks, financial institutions, Non-Banking Financial Companies, Associations of industries, media, public and Indian Banks' Association, and accordingly the guidelines on priority sector lending have been revised. The detailed revised guidelines are enclosed.

3. These guidelines take into account the revised definition of small and micro enterprises as per the Micro, Small and Medium Enterprises Development Act, 2006.

4. The revised guidelines will be effective **with immediate effect**. In case, any bank has any difficulty in complying with the revised priority sector guidelines, they may approach Reserve Bank of India with appropriate reasons and time frame for compliance.

5. We are separately forwarding the revised formats of half-yearly and yearly returns for reporting data on priority sector advances.

6. Please acknowledge receipt.

Yours faithfully,

(C. S. Murthy)
Chief General Manager-in-Charge

LENDING TO PRIORITY SECTOR

At a meeting of the National Credit Council held in July 1968, it was emphasised that commercial banks should increase their involvement in the financing of priority sectors, viz., agriculture and small scale industries. The description of the priority sectors was later formalised in 1972 on the basis of the report submitted by the Informal Study Group on Statistics relating to advances to the Priority Sectors constituted by the Reserve Bank in May 1971. On the basis of this report, the Reserve Bank prescribed a modified return for reporting priority sector advances and certain guidelines were issued in this connection indicating the scope of the items to be included under the various categories of priority sector. Although initially there was no specific target fixed in respect of priority sector lending, in November 1974 the banks were advised to raise the share of these sectors in their aggregate advances to the level of 33 1/3 per cent by March 1979. At a meeting of the Union Finance Minister with the Chief Executive Officers of public sector banks held in March 1980, it was agreed that banks should aim at raising the proportion of their advances to priority sector to 40 per cent by March 1985. Subsequently, on the basis of the recommendations of the Working Group on the Modalities of Implementation of Priority Sector Lending and the Twenty Point Economic Programme by Banks (Chairman: Dr. K. S. Krishnaswamy), all commercial banks were advised to achieve the target of priority sector lending at 40 per cent of aggregate bank advances by 1985. Sub-targets were also specified for lending to agriculture and the weaker sections within the priority sector. Since then, there have been several changes in the scope of priority sector lending and the targets and sub-targets applicable to various bank groups.

On the basis of the recommendations made in September 2005 by the Internal Working Group (Chairman: Shri C. S. Murthy), set up in Reserve Bank to examine, review and recommend changes, if any, in the existing policy on priority sector lending including the segments constituting the priority sector, targets and sub-targets, etc. and the comments/suggestions received thereon from banks, financial institutions, public and the Indian Banks' Association (IBA), it has been decided to include only those sectors as part of the priority sector, that impact large sections of the population, the weaker sections and the sectors which are employment-intensive such as agriculture, and tiny and small enterprises.

Accordingly, the broad categories of priority sector for all scheduled commercial banks will be as under:

I. CATEGORIES OF PRIORITY SECTOR

(i) **Agriculture (Direct and Indirect finance):** Direct finance to agriculture shall include short, medium and long term loans given for agriculture and allied activities (dairy, fishery, piggery, poultry, bee-keeping, etc.) directly to individual farmers, Self-Help Groups (SHGs) or Joint Liability Groups (JLGs) of individual farmers without limit and to others (such as corporates, partnership firms and institutions) up to the limits indicated in Section I, for taking up agriculture/allied activities. Indirect finance to agriculture shall include loans given for agriculture and allied activities as specified in Section I, appended.

(ii) **Small Enterprises (Direct and Indirect Finance):** Direct finance to small enterprises shall include all loans given to micro and small (manufacturing) enterprises engaged in manufacture/ production, processing or preservation of goods, and micro and small (service) enterprises engaged in providing or rendering of services, and whose investment in plant and machinery and equipment (original cost excluding land and building and such items as mentioned therein) respectively, does not exceed the amounts specified in Section I, appended. The micro and small (service) enterprises shall include small road & water transport operators, small business, professional & self-employed persons, and all other service enterprises, as per the definition given in Section I appended. Indirect finance to small enterprises shall include finance to any person providing inputs to or marketing the output of artisans, village and cottage industries, handlooms and to cooperatives of producers in this sector.

(iii) **Retail Trade** shall include retail traders/private retail traders dealing in essential commodities (fair price shops), and consumer co-operative stores, as per the definition given in Section I appended.

(iv) **Micro Credit:** Provision of credit and other financial services and products of very small amounts not exceeding Rs. 50,000 per borrower, either directly or indirectly through a SHG/JLG mechanism or to NBFC/

MFI for on-lending up to Rs. 50,000 per borrower, will constitute micro credit.

(v) **Education loans:** Education loans include loans and advances granted to only individuals for educational purposes up to Rs. 10 lakh for studies in India and Rs. 20 lakh for studies abroad, and do not include those granted to institutions;

(vi) **Housing loans:** Loans up to Rs. 20 lakh to individuals for purchase/construction of dwelling unit per family, (excluding loans granted by banks to their own employees)and loans given for repairs to the damaged dwelling units of families up to Rs. 1 lakh in rural and semi-urban areas and up to Rs. 2 lakh in urban and metropolitan areas.

II. OTHER IMPORTANT FEATURES OF THE GUIDELINES

(i) Investments by banks in securitised assets, representing loans to various categories of priority sector, shall be eligible for classification under respective categories of priority sector (direct or indirect) depending on the underlying assets, provided the securitised assets are originated by banks and financial institutions and fulfill the Reserve Bank of India guidelines on securitisation. This would mean that the banks' investments in the above categories of securitised assets shall be eligible for classification under the respective categories of priority sector only if the securitised advances were eligible to be classified as priority sector advances before their securitisation.

(ii) Outright purchases of any loan asset eligible to be categorised under priority sector, shall be eligible for classification under the respective categories of priority sector (direct or indirect), provided the loans purchased are eligible to be categorized under priority sector; the loan assets are purchased (after due diligence and at fair value) from banks and financial institutions, without any recourse to the seller; and the eligible loan assets are not disposed of, other than by way of repayment, within a period of six months from the date of purchase.

(iii) Investments by banks in Inter Bank Participation Certificates (IBPCs), on a risk sharing basis, shall be eligible for classification under respective categories of priority sector, provided the underlying assets are eligible to be categorised under the respective categories of priority sector and are held for at least 180 days from the date of investment.

(iv) The targets and sub-targets under priority sector lending would be linked to Adjusted Net Bank Credit (ANBC) (Net Bank Credit plus investments made by banks in non-SLR bonds held in HTM category) or Credit Equivalent amount of Off-Balance Sheet Exposures (OBE), whichever is higher, as on March 31 of the previous year. The outstanding FCNR (B) and NRNR deposits balances will no longer be deducted for computation of ANBC for priority sector lending purposes. Investments made by banks in the Recapitalization Bonds floated by Government of India will not be taken into account for the purpose. Existing investments, as on the date of this circular, made by banks in non-SLR bonds held in HTM category will not be taken into account for calculation of ANBC, up to March 31, 2010. However, fresh investments by banks in non-SLR bonds held in HTM category will be taken into account for the purpose. Deposits placed by banks with NABARD/SIDBI, as the case may be, in lieu of non-achievement of priority sector lending targets/sub-targets, though shown under Schedule 8 – 'Investments' in the Balance Sheet at item I (vi) – 'Others', will not be treated as investment in non-SLR bonds held under HTM category. For the purpose of calculation of credit equivalent of off-balance sheet exposures, banks may use current exposure method. Inter-bank exposures will not be taken into account for the purpose of priority sector lending targets/sub-targets.

(v) Fresh deposits placed by banks' on or after the date of this circular with NABARD/SIDBI on account of non-achievement of priority sector lending targets/sub-targets would not be eligible for classification as indirect finance to agriculture/Small Enterprises Sector, as the case may be. However, the deposits placed with NABARD/SIDBI by banks on the above account and outstanding as on the date of this circular would be eligible for classification as indirect finance to agriculture/Small Enterprises sector, as the case may be, till the date of maturity of such deposits or March 31, 2010, whichever is earlier.

III. TARGETS/SUB-TARGETS

The targets and sub-targets set under priority sector lending for domestic and foreign banks operating in India are furnished in Table A1.1.

Table A1.1: Targets under Priority Sector Lending

	Domestic commercial banks	Foreign banks
Total Priority Sector advances	40 per cent of Adjusted Net Bank Credit (ANBC) or credit equivalent amount of Off-Balance Sheet Exposure, whichever is higher.	32 per cent of ANBC or credit equivalent amount of Off-Balance Sheet Exposure, whichever is higher.
Total agricultural advances	18 per cent of ANBC or credit equivalent amount of Off-Balance Sheet Exposure, whichever is higher. Of this, indirect lending in excess of 4.5per cent of ANBC or credit equivalent amount of Off-Balance Sheet Exposure, whichever is higher, will not be reckoned for computing performance under 18 per cent target. However, all agricultural advances under the categories 'direct' and 'indirect' will be reckoned in computing performance under the overall priority sector target of 40 per cent of ANBC or credit equivalent amount of Off-Balance Sheet Exposure, whichever is higher.	No target.
Small Enterprise advances	Advances to small enterprises sector will be reckoned in computing performance under the overall priority sector target of 40 per cent of ANBC or credit equivalent amount of Off-Balance Sheet Exposure, whichever is higher.	10 per cent of ANBC or credit equivalent amount of Off-Balance Sheet Exposure, whichever is higher.
Micro enterprises within Small Enterprises sector	(i) 40 per cent of total advances to small enterprises sector should go to micro (manufacturing) enterprises having investment in plant and machinery up to Rs 5 lakh and micro (service) enterprises having investment in equipment up to Rs. 2 lakh;ii) 20 per cent of total advances to small enterprises sector should go to micro (manufacturing) enterprises with investment in plant and machinery above Rs 5 lakh and up to Rs. 25 lakh, and micro (service) enterprises with investment in equipment above Rs. 2 lakh and up to Rs. 10 lakh. (Thus, 60 per cent of small enterprises advances should go to the micro enterprises).	Same as for domestic banks.
Export credit	Export credit is not a part of priority sector for domestic commercial banks.	12 per cent of ANBC or credit equivalent amount of Off-Balance Sheet Exposure, whichever is higher.
Advances to weaker sections	10 per cent of ANBC or credit equivalent amount of Off-Balance Sheet Exposure, whichever is higher.	No target.
Differential Rate of Interest Scheme	1 per cent of total advances outstanding as at the end of the previous year. It should be ensured that not less than 40 per cent of the total advances granted under DRI scheme go to scheduled caste/scheduled tribes. At least two third of DRI advances should be granted through rural and semi-urban branches.	No target.

Note : ANBC or credit equivalent of Off-Balance Sheet Exposures (as defined by Department of Banking Operations and Development of Reserve Bank of India from time to time) will be computed with reference to the outstanding as on March 31 of the previous year. For this purpose, outstanding FCNR (B) and NRNR deposits balances will no longer be deducted for computation of ANBC for priority sector lending purposes. For the purpose of priority sector lending, ANBC denotes NBC plus investments made by banks in non-SLR bonds held in HTM category. Investments made by banks in the Recapitalization Bonds floated by Government of India will not be taken into account for the purpose of calculation of ANBC. Existing investments, as on the date of this circular, made by banks in non-SLR bonds held in HTM category will not be taken into account for calculation of ANBC, up to March 31, 2010. However, fresh investments by banks in non-SLR bonds held in HTM category will be taken into account for the purpose. Deposits placed by banks with NABARD/SIDBI, as the case may be, in lieu of non-achievement of priority sector lending targets/sub-targets, though shown under Schedule 8 - 'Investments' in the Balance Sheet at item I (vi) - 'Others', will not be treated as investment in non-SLR bonds held under HTM category. For the purpose of calculation of credit equivalent of off-balance sheet exposures, banks may use current exposure method. Inter-bank exposures will not be taken into account for the purpose of priority sector lending targets/sub-targets.

The detailed guidelines in this regard are given hereunder.

SECTION I

1. AGRICULTURE

DIRECT FINANCE

1.1 Finance to individual farmers [including Self Help Groups (SHGs) or Joint Liability Groups (JLGs), i.e. groups of individual farmers, provided banks maintain disaggregated data on such finance] for Agriculture and Allied Activities (dairy, fishery, piggery, poultry, bee-keeping, etc.)

1.1.1 Short-term loans for raising crops, i.e. for crop loans. This will include traditional/non-traditional plantations and horticulture.

1.1.2 Advances up to Rs. 10 lakh against pledge/hypothecation of agricultural produce (including warehouse receipts) for a period not exceeding 12 months, irrespective of whether the farmers were given crop loans for raising the produce or not.

1.1.3 Working capital and term loans for financing production and investment requirements for agriculture and allied activities.

1.1.4 Loans to small and marginal farmers for purchase of land for agricultural purposes.

1.1.5 Loans to distressed farmers indebted to non-institutional lenders, against appropriate collateral or group security.

1.1.6 Loans granted for pre-harvest and post-harvest activities such as spraying, weeding, harvesting, grading, sorting, processing and transporting undertaken by individuals, SHGs and cooperatives in rural areas.

1.2 Finance to others [such as corporates, partnership firms and institutions] for Agriculture and Allied Activities (dairy, fishery, piggery, poultry, bee-keeping, etc.)

1.2.1 Loans granted for pre-harvest and post harvest activities such as spraying, weeding, harvesting, grading, sorting and transporting.

1.2.2 Finance up to an aggregate amount of Rs. one crore per borrower for the purposes listed at 1.1.1, 1.1.2, 1.1.3 and 1.2.1 above.

1.2.3 One-third of loans in excess of Rs. one crore in aggregate per borrower for agriculture and allied activities.

INDIRECT FINANCE

1.3 Finance for Agriculture and Allied Activities

1.3.1 Two-third of loans to entities covered under 1.2 above in excess of Rs. one crore in aggregate per borrower for agriculture and allied activities.

1.3.2 Loans to food and agro-based processing units with investments in plant and machinery up to Rs. 10 crore, undertaken by those other than 1.1.6 above.

1.3.3 (i) Credit for purchase and distribution of fertilizers, pesticides, seeds, etc.

(ii) Loans up to Rs. 40 lakh granted for purchase and distribution of inputs for the allied activities such as cattle feed, poultry feed, etc.

1.3.4 Finance for setting up of Agriclinics and Agribusiness Centres.

1.3.5 Finance for hire-purchase schemes for distribution of agricultural machinery and implements.

1.3.6 Loans to farmers through Primary Agricultural Credit Societies (PACS), Farmers' Service Societies (FSS) and Large-sized Adivasi Multi Purpose Societies (LAMPS).

1.3.7 Loans to cooperative societies of farmers for disposing of the produce of members.

1.3.8 Financing the farmers indirectly through the co-operative system (otherwise than by subscription to bonds and debenture issues).

1.3.9 Existing investments as on March 31, 2007, made by banks in special bonds issued by NABARD with the objective of financing exclusively agriculture/allied activities may be classified as indirect finance to agriculture till the date of maturity of such bonds or March 31, 2010, whichever is earlier. Fresh investments in such special bonds made subsequent to March 31, 2007 will, however, not be eligible for such classification.

1.3.10 Loans for construction and running of storage facilities (warehouse, market yards, godowns, and silos), including cold storage units designed to store agriculture produce/products, irrespective of their location.

If the storage unit is registered as SSI unit/micro or small enterprise, the loans granted to such units may be classified under advances to Small Enterprises sector.

1.3.11 Advances to Custom Service Units managed by individuals, institutions or organisations who maintain a fleet of tractors, bulldozers, well-boring equipment, threshers, combines, etc., and undertake work for farmers on contract basis.

1.3.12 Finance extended to dealers in drip irrigation/ sprinkler irrigation system/agricultural machinery, irrespective of their location, subject to the following conditions:

(a) The dealer should be dealing exclusively in such items or if dealing in other products, should be maintaining separate and distinct records in respect of such items.

(b) A ceiling of up to Rs. 30 lakh per dealer should be observed.

1.3.13 Loans to Arthias (commission agents in rural/ semi-urban areas functioning in markets/mandies) for extending credit to farmers, for supply of inputs as also for buying the output from the individual farmers/ SHGs/ JLGs.

1.3.14 Fifty per cent of the credit outstanding under loans for general purposes under General Credit Cards (GCC).

1.3.15 The deposits placed in RIDF with NABARD by banks on account of non-achievement of priority sector lending targets/sub-targets and outstanding as on the date of this circular would be eligible for classification as indirect finance to agriculture sector till the date of maturity of such deposits or March 31, 2010, whichever is earlier.

1.3.16 Loans already disbursed and outstanding as on the date of this circular to State Electricity Boards (SEBs) and power distribution corporations/ companies, emerging out of bifurcation/ restructuring of SEBs, for reimbursing the expenditure already incurred by them for providing low tension connection from step-down point to individual farmers for energising their wells and for Systems Improvement Scheme under Special Project Agriculture (SI-SPA), are eligible for classification as indirect finance till the dates of their maturity/repayment or March 31, 2010, whichever is earlier. Fresh advances will, however, not be eligible for classification as indirect finance to agriculture.

1.3.17 Loans to National Co-operative Development Corporation (NCDC) for on-lending to the co-operative sector for purposes coming under the priority sector will be treated as indirect finance to agriculture till March 31, 2010.

1.3.18 Loans to Non-Banking Financial Companies (NBFCs) for on lending to individual farmers or their SHGs/JLGs.

1.3.19 Loans granted to NGOs/MFIs for on-lending to individual farmers or their SHGs/JLGs.

2 SMALL ENTERPRISES

DIRECT FINANCE

2.1 Direct Finance in the small enterprises sector will include credit to:

2.1.1 Manufacturing Enterprises

(a) Small(manufacturing) Enterprises

Enterprises engaged in the manufacture/ production, processing or preservation of goods and whose investment in plant and machinery [original cost excluding land and building and the items specified by the Ministry of Small Scale Industries vide its notification no. S.O. 1722 (E) dated October 5, 2006] does not exceed Rs. 5 crore.

(b) Micro (manufacturing) Enterprises

Enterprises engaged in the manufacture/ production, processing or preservation of goods and whose investment in plant and machinery [original cost excluding land and building and such items as in 2.1.1 (a)] does not exceed Rs. 25 lakh, irrespective of the location of the unit.

2.1.2 Service Enterprises

(a) Small (service) Enterprises

Enterprises engaged in providing/rendering of services and whose investment in equipment (original cost excluding land and building and furniture, fittings and other items not directly related to the service rendered or as may be notified under the MSMED Act, 2006) does not exceed Rs. 2 crore.

(b) Micro (service) Enterprises

Enterprises engaged in providing/rendering of services and whose investment in equipment [original cost excluding land and building and furniture, fittings and such items as in 2.1.2 (a)] does not exceed Rs. 10 lakh.

(c) The small and micro (service) enterprises shall include small road & water transport operators, small business, professional & self-employed persons, and all other service enterprises.

2.1.3 Khadi and Village Industries Sector (KVI)

All advances granted to units in the KVI sector, irrespective of their size of operations, location and amount of original investment in plant and machinery. Such advances will be eligible for consideration under the sub-target (60 per cent) of the small enterprises segment within the priority sector.

INDIRECT FINANCE

2.2 Indirect finance to the small (manufacturing as well as service) enterprises sector will include credit to:

2.2.1 Persons involved in assisting the decentralised sector in the supply of inputs to and marketing of outputs of artisans, village and cottage industries.

2.2.2 Advances to cooperatives of producers in the decentralised sector viz. artisans village and cottage industries.

2.2.3 Existing investments as on March 31, 2007, made by banks in special bonds issued by NABARD with the objective of financing exclusively non-farm sector may be classified as indirect finance to Small Enterprises sector till the date of maturity of such bonds or March 31, 2010, whichever is earlier. Investments in such special bonds made subsequent to March 31, 2007 will, however, not be eligible for such classification.

2.2.4 The deposits placed with SIDBI by foreign banks, having offices in India, on account of non-achievement of priority sector lending targets/sub-targets and outstanding as on the date of this circular would be eligible for classification as indirect finance to Small Enterprises sector till the date of maturity of such deposits or March 31, 2010, whichever is earlier.

2.2.5 Loans granted by banks to NBFCs for on-lending to small and micro enterprises (manufacturing as well as service).

3. RETAIL TRADE

3.1 Advances granted to retail traders dealing in essential commodities (fair price shops), consumer co-operative stores, and;

3.2 Advances granted to private retail traders with credit limits not exceeding Rs. 20 lakh.

4. MICRO CREDIT

4.1 Loans of very small amount not exceeding Rs. 50,000 per borrower provided by banks either directly or indirectly through a SHG/JLG mechanism or to NBFC/MFI for on-lending up to Rs. 50,000 per borrower.

4.2 Loans to poor indebted to informal sector

Loans to distressed persons (other than farmers) to prepay their debt to non-institutional lenders, against appropriate collateral or group security, would be eligible for classification under priority sector.

5. STATE SPONSORED ORGANIZATIONS FOR SCHEDULED CASTES/ SCHEDULED TRIBES

Advances sanctioned to State Sponsored Organisations for Scheduled Castes/ Scheduled Tribes for the specific purpose of purchase and supply of inputs to and/or the marketing of the outputs of the beneficiaries of these organisations.

6. EDUCATION

6.1 Educational loans granted to individuals for educational purposes up to Rs. 10 lakh for studies in India and Rs. 20 lakh for studies abroad. Loans granted to institutions will not be eligible to be classified as priority sector advances.

6.2 Loans granted by banks to NBFCs for on-lending to individuals for educational purposes up to Rs. 10 lakh for studies in India and Rs. 20 lakh for studies abroad.

7. HOUSING

7.1 Loans up to Rs. 20 lakh, irrespective of location, to individuals for purchase/construction of a dwelling unit per family, excluding loans granted by banks to their own employees.

7.2 Loans given for repairs to the damaged dwelling units of families up to Rs. 1 lakh in rural and semi-urban areas and up to Rs. 2 lakh in urban and metropolitan areas.

7.3 Assistance given to any governmental agency for construction of dwelling units or for slum clearance and rehabilitation of slum dwellers, subject to a ceiling of Rs. 5 lakh of loan amount per dwelling unit.

7.4 Assistance given to a non-governmental agency approved by the NHB for the purpose of refinance for construction/reconstruction of dwelling units or for slum clearance and rehabilitation of slum dwellers, subject to a ceiling of loan component of Rs. 5 lakh per dwelling unit.

8. WEAKER SECTIONS

The weaker sections under priority sector shall include the following:

(a) Small and marginal farmers with land holding of 5 acres and less, and landless labourers, tenant farmers and share croppers;

(b) Artisans, village and cottage industries where individual credit limits do not exceed Rs. 50,000;

(c) Beneficiaries of Swarnjayanti Gram Swarozgar Yojana (SGSY);

(d) Scheduled Castes and Scheduled Tribes;

(e) Beneficiaries of Differential Rate of Interest (DRI) scheme;

(f) Beneficiaries under Swarna Jayanti Shahari Rozgar Yojana (SJSRY);

(g) Beneficiaries under the Scheme for Liberation and Rehabilitation of Scavengers (SLRS);

(h) Advances to Self Help Groups;

(i) Loans to distressed poor to prepay their debt to informal sector, against appropriate collateral or group security.

9. Export Credit

This category will form part of priority sector for foreign banks only.

SECTION II

PENALTIES for NON-ACHIEVEMENT OF PRIORITY SECTOR LENDING TARGET / SUB-TARGETS

1. Domestic scheduled commercial banks – Contribution by banks to Rural Infrastructure Development Fund (RIDF):

1.1 Domestic scheduled commercial banks having shortfall in lending to priority sector target (40 per cent of ANBC or credit equivalent amount of Off-Balance Sheet Exposure, whichever is higher) and / or agriculture target (18 per cent of ANBC or credit equivalent amount of Off-Balance Sheet Exposure, whichever is higher) shall be allocated amounts for contribution to the Rural Infrastructure Development Fund (RIDF) established with NABARD. For the purpose of allocation of RIDF tranche, the achievement level of priority sector lending as on the last reporting Friday of March of the immediately preceding financial year will be taken into account. The concerned banks will be called upon by NABARD, on receiving demands from various State Governments, to contribute to RIDF.

1.2 The corpus of a particular tranche of RIDF is decided by Government of India every year. Fifty per cent of the corpus shall be allocated among the domestic commercial banks having shortfall in lending to priority sector target of 40 per cent of ANBC or credit equivalent amount of Off-Balance Sheet Exposure, whichever is higher, on a pro-rata basis. The balance fifty per cent of the corpus shall be allocated among the banks having shortfall in lending to agriculture target of 18 per cent of ANBC or credit equivalent amount of Off-Balance Sheet Exposure, whichever is higher, on a pro-rata basis. The amount of contribution by banks to a particular tranche of RIDF will be decided in the beginning of the financial year.

1.3 The interest rates on banks' contribution to RIDF shall be fixed by Reserve Bank of India from time to time.

1.4 Details regarding operationalisation of the RIDF such as the amounts to be deposited by banks, interest rates on deposits, period of deposits, etc., will be communicated to the concerned banks separately by August of each year to enable them to plan their deployment of funds.

2. Foreign Banks – Deposit by Foreign Banks with SIDBI

2.1 The foreign banks having shortfall in lending to stipulated priority sector target/sub-targets will be required to contribute to Small Enterprises Development Fund (SEDF) to be set up by Small Industries Development Bank of India (SIDBI), or for such other purpose as may be stipulated by Reserve Bank of India from time to time.

2.2 For the purpose of such allocation, the achievement level of priority sector lending as on the last reporting Friday of March of the immediately preceding financial year will be taken into account.

2.3 The corpus of SEDF shall be decided by Reserve Bank of India on a year-to-year basis. The tenor of the deposits shall be for a period of three years or as decided by Reserve Bank from time to time. Fifty per cent of the corpus shall be contributed by foreign banks having shortfall in lending to priority sector target of 32 per cent of ANBC or credit equivalent amount of Off-Balance Sheet Exposure, whichever is higher, on a pro-rata basis. The balance fifty per cent of the corpus shall be contributed by foreign banks having aggregate shortfall in lending to Small Enterprises sector and export sector of 10 per cent and 12 per cent respectively, of ANBC or credit equivalent amount of Off-Balance Sheet Exposure, whichever is higher, on a pro-rata basis. The contribution required to be made by foreign banks would, however, not be more than the amount of shortfall in priority sector lending target/sub-targets of the foreign banks.

2.4 The concerned foreign banks will be called upon by SIDBI/or such other institution as may be decided by Reserve Bank, as and when funds are required by them, after giving one month's notice.

2.5 The interest rates on foreign banks' contribution, period of deposits, etc. shall be fixed by Reserve Bank of India from time to time.

3. Non-achievement of priority sector targets and sub-targets will be taken into account while granting regulatory clearances/approvals for various purposes.

Appendix - 2

Justification for Suggested changes in Priority Sector Guidelines

The justification for the changes proposed by the Commission in the RBI's Priority Sector Guidelines are briefly discussed below:

i) *Credit for Agriculture*

The Commission review of credit has found that in 2003-04, small and marginal farmers received 30 per cent of credit to agriculture from commercial banks. They comprised of 83.9 per cent of the total farmers households in the country operating in 43 per cent of agricultural land. Marginal farmers alone accounted for 65.9 per cent of farmers household while small farmers 18 per cent of the farmers household (NSS 59th Round).

Further, in 2003-04 the SCB advanced approximately Rs.96,000 crores to the agriculture sector. Of this marginal farmers received approximately Rs.15,000 crores (15.6 per cent) and small farmers received approximately Rs.14,000 (14.6 per cent). The balance approximately 70 per cent went to farmers at the higher end and to other Agricultural purposes. These figures have remained more and less the same since 2000-01 (28-30 per cent).

Commission therefore suggests restricting agricultural credit under priority sector only to small and marginal farmers since they are not able to benefit both from state interventions as well as market based mechanisms to an appropriate extent.

ii) *Credit for Weaker sections*

- The Commission found that, inspite of the RBI guidelines that loans up to Rs. 5 lakh should be given without collaterals, available data reveal that only 26 per cent of such loans were advanced without collaterals.
- Separate data on credit to various constituents of weaker sections are not available. However, as against the fixed quota of 10 per cent of ANBC of the scheduled commercial banks for the weaker section, the actual has been just around 5 to 6 per cent.
- The credit to weaker sections has been declining over the years in percentage terms. In 1990-91 as against total net bank credit (outstanding) of Rs. 1,24,203 crore from the scheduled commercial banks. Weaker section received Rs. 10,506 crore which was 8.5 per cent of the net bank credit. In 2005-06, weaker sections received Rs. 82,282 crore out of total of Rs. 1,445,837 crore of credit from the scheduled commercial banks, which was 5.7 per cent of the total. Thus as percentage of net bank credit of scheduled commercial banks, it has declined from 8.5 per cent in 1990-91 to 5.7 per cent in 2005-06.

The Commission therefore suggests that:

(a) *Loan demands of Rs. 10 lakh and Rs. 20 lakh which would be with collateral can easily be taken out from this priority sector segment.*

(b) *Since small and marginal farmers are important constituents of farm sector there is no justification for keeping them both under farm sector and under weaker section. Since the Commission is recommending entire farm credit for small and marginal farmers, this segment should form part of farm loan only.*

(c) *It is necessary to fix a limit of loan under weaker section, so that upper end loaning is avoided. Restrict loan limit under weaker sections for a sum not exceeding Rs. 5 lakh.*

(d) *Since all segments of priority sector will receive targeted credit, it is necessary to bring untargeted segments like housing, education, retail trade etc. under weaker sections with an upper limit of Rs. 5 lakh only.*

iii) Credit for Non Farm Unorganised Enterprises

- It is found that as per the present definition of small enterprises, which is enterprises with investment in plant and machinery upto Rs. 5 crore, over 99 per cent of enterprises which are micro enterprises (upto Rs 25 Lakh investment in P&M)as per MSMED Act definition. Keeping enterprises upto Rs. 5 crore of investment in the priority sector, will encourage the banks to go for higher end lending.
- Currently there is no quota for small enterprises within priority sector unlike agriculture and weaker section.
- Currently, there is a quota of 60 per cent for micro enterprises out of credit to small enterprises (for which there is no quota), and that credit to small

enterprises has been declining, as a result credit to micro enterprise has also been declining.

- Large enterprises which account for 50 per cent of industrial production and 20 per cent of export receive over 31 per cent of bank credit.
- Credit to small enterprises was Rs. 45,771 crore out of net bank credit of Rs. 2,97,265 crore of scheduled commercial banks in 1997-98. Credit to SEs was 15.4 per cent of the total. In 2005-06, small enterprises received Rs. 1,01,385 crore out of total credit of Rs. 14,45,837 crore which was 7.0 per cent of the total. Thus credit to small enterprises has declined from 15.4 per cent in 1997-98 to 7 per cent in 2005-06.
- Credit to micro enterprises was Rs. 24,742 crore in 1999-2000 which was 54 per cent of SSI credit (Rs. 46045 crore) from Public Sector Banks whereas credit to micro enterprises was Rs. 33,314 crore out of total net bank credit of Rs. 82,275 crore to SSI from the public sector banks which was 40.5 per cent of the total in 2005-06.
- Micro enterprises with investment in plant and machinery below Rs. 5 lakh are about 94 per cent of small enterprises. Hence of the two constituents of micro enterprises i.e. upto 5 lakh and those below Rs. 5 lakh to 25 lakh, the first category is more needy both in terms of size and weakness.

The Commission recommends that

(a) *Only Micro Enterprises upto investment of Rs. 25 lakh in plant and machinery (engaged in manufacturing) and upto Rs. 10 lakh of investment if engaged in business or trade as per MSMED Act 2006, engaged in service or business should be eligible for priority sector lending.*

(b) *quota of credit should also be fixed for micro enterprises since they receive not more than 5 per cent of net bank credit, whereas they account for over 30 per cent of industrial production and 30 per cent of export.*

(c) *reservation of 4 per cent of ANBC for micro enterprises upto Rs. 5 lakh of investment and another 4 per cent for those between Rs. 5 lakh to Rs. 25 lakh of investment as per current definition of micro enterprises given in MSMED Act, 2006.*

(d) *to bring all non-farm enterprises under the category of Micro enterprises under the category of micro enterprises and shift loans to SJSY, SJSRY, Micro credit from weaker section to Mirco enterprise category and total quota of loan for this category be fixed at 12 per cent of ANBC.*

Report on

CREATION OF A NATIONAL FUND FOR THE UNORGANISED SECTOR (NAFUS)

1 Background and Rationale of the National Fund

A. Mandate

1.1 As a part of its terms of reference, the National Commission for Enterprises in the Unorganised Sector (NCEUS), has reviewed the overall gaps in credit, skill, technology, marketing, raw materials and infrastructure for the unorganised sector and feels that the attention given over time to meet the requirements of the sector is grossly inadequate and also lacks focus. The lack of focus has been due to the practice of subsuming this vast sector of tiny / micro enterprises numbering more than 42 million or 98 per cent of total enterprises (as per the Economic Census of 2005) under the official definition of micro and small enterprises in terms of capital investment. This has enabled the bigger ones among the small to secure the benefits arising out of various policy and programme interventions. To address this issue, the Commission has prepared reports on the overall requirements of credit and the various livelihood promotion measures essential for this sector to contribute consistently to the enhanced productivity and increased employment. Recognising the weaknesses in the delivery system, the Common Minimum Programme (CMP) of the UPA Government desired that the Commission should "make appropriate recommendations to provide technical, marketing and credit support to these enterprises." The CMP has proposed the creation of a National Fund for this purpose. Accordingly, NCEUS had deliberated on the constraints faced by the unorganised sector enterprises in regard to the credit and developmental support, and suggested creation of a statutory body under an Act of Parliament to utilise the proposed national fund in a manner as detailed subsequently.

1.2 This Report on the Creation of a National Fund for Unorganised Sector (hereinafter called NAFUS) is the outcome of deliberations of the Commission on issues relating to financing the unorganised sector enterprises. This was done through a Task Force headed by an eminent economist, Professor V.S. Vyas as well as interactions with the RBI, Indian Banks Association, selected representatives of banks, associations of tiny/ micro and small enterprises, and experts on the subject. The outcome of these deliberations is given in a separate, but accompanying Report on Financing the Unorganised Sector Enterprises.

B. Background

1.3 According to the Approach Paper of the 11th Plan, there would be an estimated additional workforce of 65 million during the Plan period, for whom employment opportunities will have to be generated mainly in the unorganised non-farm sector. This is because: first, as per the Approach Paper, there is limited scope of further employment in the agricultural sector, which according to the Planning Commission, needs to shed employment so that, at the projected rates of growth, income differentials between agriculture and non-agriculture can at least be maintained if not narrowed. Second, the employment growth rate has been almost negligible in the organised sector. Third, the vast unorganised sector still has the potential to generate gainful employment if only they are enabled to overcome such critical constraints as access to credit, power, marketing and technology.

1.4 The unorganised non-farm sector is defined by NCEUS as

"those unincorporated private enterprises owned by individuals or households engaged in the sale and production of goods and services, operated on a proprietary or partnership basis and with less than 10 workers".

1.5 According to the Commission's estimates, about 86.3 per cent of the workforce is directly engaged in the unorganised sector covering both farm and non-farm activities as per the estimates derived from the Employment-Unemployment Survey of NSSO in 2004-05. Estimates based on this survey also show that 32 per cent or 126 million of the unorganised sector workforce is engaged in non-farm activities.

1.6 In this Report, the Commission has confined itself to non-farm (including off-farm) enterprises, thus, excluding cultivation related activities. According to the Informal Non- Agricultural Enterprise Survey, 1999-2000, of the total non-farm unorganised sector enterprises, 56 per cent are in rural areas and 44 per cent are in urban areas. Table 1.1 gives a brief on the characteristics of the unorganised enterprises by industry. The number of unorganised sector enterprises is estimated at 44 million in 1999-2000. Trade has the largest share of enterprises, is the largest employer and has also the highest share in total value added. It also has the largest per capita and per enterprise value added. As could be expected Manufacturing has the highest share of plant and machinery (58 per cent), followed by Other Services (25 per cent). A heterogeneous group, Other Services, has the highest per enterprise investment in plant and machinery (Rs. 58359) and Construction and Transport has investment in plant and machinery of over Rs 30,000 per enterprise. In the above survey, units employing less than 10 workers, which are non-agricultural unorganised sector enterprises as per the NCEUS definition, account for 99.31 per cent of the total number of units covered and contribute 89 per cent of the GVA.[1]

1.7 Table 1.2 presents the rural urban differentials in the characteristics of the unorganised sector enterprises. It is evident that these are predominantly urban oriented enterprises though their share in rural areas is higher while the employment share is almost even. The contribution to the value added is much higher by the urban enterprises. All productivity ratios like GVA per worker or per enterprise too are higher in the urban enterprises as compared to those in rural areas. The use of plant and machinery is also comparatively high in urban enterprises.

1.8 The contribution of the total unorganised sector as defined by NCEUS to the total value added in 2004-05 (at 1999-2000 prices) is estimated at 50.6 per cent (Table1.3). Non-agricultural unorganised sector

Table 1.1: Characteristics of Non-Farm Unorganised Sector Enterprises 1999-2000

Broad Industry Group	Enterprises	Employment	Gross Value Added	Plant & Machinery	GVA Per Enterprise	GVA Per Worker	P& M Per Enterprise
	(Millions)	Percentage Distribution			(Rs)		
Manufacturing	14.0	36.16	25.13	57.99	30921	15995	17759
Construction	1.8	3.19	3.67	1.49	34513	26515	34301
Trade & Repair Services	17.4	37.12	46.79	8.79	46525	29013	10364
Hotels & Restaurants	1.8	5.18	5.03	0.95	49521	22384	4994
Transport, Storage, Communication	3.9	6.72	8.08	6.22	35813	27687	36314
Other Services	5.2	11.63	11.3	24.56	37429	22356	58359
Total	**44.1**	**100**	**100**	**100**	**39157**	**23019**	**20245**

Source: NSS 55th Round 1999-2000, Informal Sector, Estimated

[1] The Informal Non- Agricultural Enterprise Survey, 1999-2000, covered all non-agricultural proprietary and partnership based enterprises, whereas, as per the NCEUS definition, only that sub-set of such enterprises which employed less than 10 workers were non-agricultural unorganised/informal sector enterprises.

Table 1.2: Characteristics of Non-Farm Unorganised Sector Enterprises (NCEUS Definition) 1999-2000

Sector	Enterprises	Employment	GVA	Value of Assets	Value of - Plant & Machinery	GVA Per Enterprise	GVA Per Worker	Plant & Machinery Per Enterprise
	Millions		Percentage			(Rs.)		
Rural	25.0	38.4	32.6	20.6	30.7	22525	14638	11604
Urban	19.1	36.6	67.4	79.4	69.3	60875	31823	30240
Total	44.1	75.0	100.0	100.0	100.0	39157	23019	20245

Source: Same as in Table 1.1

enterprises contribute as much as 62 per cent to total unorganised sector GDP and 31.5 per cent to total GDP.

Table 1.3: Estimated Share in GDP in 2004-05 (per cent)

Industry Group	Unorganised	Organised	Industry-wise Share of the Unorganised Sector
Agriculture	94.5	5.52	37.7
Industry	28.9	71.1	15.0
Services	44.7	55.3	47.2
Total	50.6	49.4	100.0

Source: NCEUS 2007

1.9 For operational purposes, the Government of India defines the smallest segment of industries, as Micro enterprises (earlier Tiny enterprises) covering the manufacturing sector and selected services. Till October 2, 2006, tiny units (now called micro enterprises) were defined as a segment of small-scale units, with investment in plant and machinery up to Rs. 25 lakhs. The Micro, Small and Medium Enterprises Act 2006, which has come into operation on October 2, 2006, has now defined micro enterprises as a separate segment of small industries which in the case of manufacturing enterprises has an investment in plant and machinery up to Rs. 25 lakhs and in the case of services, an investment limit of Rs. 10 lakh.

1.10 The Reserve Bank of India, which extends and monitors credit to small scale industries under its priority sector guidelines has specified that 60 per cent of this credit should go to micro enterprises with investment in P&M up to Rs. 25 lakhs and within this segment, 40 per cent of the total SSI credit should go to the micro enterprises with investment in P&M up to Rs. 5 lakhs. However, there are some differences in the way the RBI defines and monitors credit to micro enterprises and changes in the definition after the issuance of the new guidelines in April 2007. Under RBI's earlier policy guidelines, activities like small business, loans to professionals etc were not part of SSI credit, but credit to Khadi & Village Industries and artisans in excess of Rs. 50,000 were included. However, as per the revised Priority Sector Guidelines of the RBI issued on 30th April 2007, Small and Micro (Services) Enterprises shall include small road and water transport operations, small businesses, professionals and self-employed persons and all other service enterprises.

1.11 These definitions of micro-enterprise, especially of the lower segment of micro-enterprises (investment in P&M of less than Rs. 5 lakhs in the case of manufacturing and of less than Rs. 2 lakhs in the case of services) overlap very significantly with the NCEUS definition of unorganised sector enterprises. This is brought out both by the Third Census of Small Scale Industries and the Informal Sector Survey. According to the Third Census of SSI (2001-02), while over 99 per cent of small manufacturing enterprises exist in the form of micro enterprises (with investment in plant and machinery below Rs. 25 lakhs), as many as 95.6 per cent of all such units are partnership and proprietary, employ less than 9 workers (i.e. they are unorganised enterprises as per the NCEUS definition) and also have less than Rs. 5 lakhs investment in P & M.. As per the estimates of the Informal Sector Survey, 1999-2000, which covers the lower segment of the micro enterprises more comprehensively, more than 99.8 per cent of the enterprises, employ less than 10 workers and have less than Rs. 5 lakhs investment in Plant and Machinery. But it should be noted that the scope of the NCEUS definition is wider than the MSME definition in terms of sectoral coverage. This Report deals with all non-farm enterprises and leaves out of its purview all activities related to crop cultivation.

1.12 Based on the projections using the NSS and Economic Census data, the Commission has estimated the number of unorganised non-farm enterprises at 58 million in 2007. Considering the vast size and high growth potential of the unorganised sector, these unorganised sector enterprises need to be strengthened and raised to a higher growth level, so that the additional employment opportunities in the sector can create more income, which can add directly more than one per cent to GDP growth. In other words, the Commission is of the view that if properly nurtured and strengthened, the unorganised non-farm sector will emerge as a potent tool for employment creation, poverty reduction and faster inclusive growth during the 11th Plan.

C. Rationale

Present Status of Financing of Unorganised Sector Enterprises

1.13 Despite the potential of, and the demand on, the unorganised sector for employment generation and poverty reduction, this sector has not received the focused, singular and national mission type attention as far as norms of adequate credit at affordable rates and developmental support are concerned. On the contrary, RBI statistics clearly brings out the fact that credit to Small Scale Industries, of which micro enterprises form an important constituent, has declined significantly over the last several years as a percentage of total credit disbursed.

1.14 Table 1.4 reveals the steady decline in SSI credit as percentage of Gross Bank Credit from the Scheduled Commercial Banks, from 15.42 in 1990-91 to 6.4 in 2006-07. Further, during the last 6 years itself the credit to SSI sector has declined from 10.76 per cent of the Gross Bank Credit in 2000-01 to 6.34 per cent in 2006-07.

Table 1.4: Flow of Credit from Scheduled Commercial Banks to SSI and Allied Sectors (Rs. Crores)

Year	Gross Bank Credit (GBC)	Credit to SSI	SSI Credit as Per cent of GBC
1990-91	1,16,301	17,938	15.42
1991-92	1,25,592	18,939	15.07
1992-93	1,51,982	20,975	13.80
1993-94	1,64,418	23,978	14.58
1994-95	2,11,560	29,175	13.79
1995-96	2,54,015	34,246	13.48
1996-97	3,01,698	38,196	12.60
1997-98	3,52,696	45,771	13.00
1998-99	3,99,436	51,679	12.90
1999-00	4,75,113	57,035	12.00
2000-01	5,58,766	60,141	10.76
2001-02	6,80,958	67,107	9.85
2002-03	7,78,043	64,707	8.31
2003-04	9,02,026	71,209	7.89
2004-05	10,45,954	83,498	7.98
2005-06	14,43,920	1,01,385	7.02
2006-07	18,41,978	1,16,908	6.34

Source: RBI (2006-07a, b)

1.15 The status of credit to Micro Enterprises also tells the same story. This can be seen from the Table 1.5.

Table 1.5: SCB's Credit to Micro Enterprises (Rs. Crores)

Sl.No	Segment of Credit	2002-03	2003-04	2004-05
1	Gross Bank Credit	778043	902026	1045954
2	Credit to SSI	64707	71209	83498
3	Credit to Micro Enterprises with Investment in P&M up to Rs. 5 lakhs	15080	13677	14482
4	3 as Percentage of SSI Credit	23.3	19.20	17.34
5	Credit to Micro Enterprises with Investment in P&M between Rs. 5 lakhs and Rs. 25 lakhs	13896	14870	14048
6	5 as Percentage of SSI Credit	21.4	20.9	16.82
7	Credit to Micro Enterprises with Investment in P&M up to Rs. 25 lakhs	28976	28547	28530
8	7 as percentage of SSI Credit	44.8	40.1	34.16
9	7 as percentage of GBC	3.7	3.1	2.7

Source: RBI (2004-05, 2005-06)

1.16 Micro enterprises have received about 3 per cent of Gross Bank Credit during 2002/03 - 2004/05. Further, against the RBI priority sector stipulation that micro enterprises should get 60 per cent of the total credit to SSI, in reality they have been getting just about 40 per cent. In fact, in the year 2004-05, this share was much lower at 34 per cent.

1.17 As per the Commission's definition, the Non-Farm Unorganised Sector includes those enterprises, which are engaged in manufacturing, business and trade, etc. As shown earlier, the government uses the investment limit criterion in manufacturing and selected services to delineate the micro-enterprise sector. The Commission has made an independent estimate of the credit flow, extending the micro-enterprise investment limit criterion to the entire non-farm enterprise sector, with the help of credit data from the Scheduled Commercial Banks (SCBs), Regional Rural Banks (RRBs) and Urban Cooperative Banks (UCBs) which, in its estimate, account for over 95 per cent of the institutional credit flow to this sector. Within the non-farm unorganised sector, the most vulnerable segment is the smaller size micro enterprises with investment up to Rs. 5 lakhs. This sector by this segment of unorganised enterprises is just about 2.2 per cent of GBC from SCBs and 3 per cent of GBC from three major sources namely Scheduled Commercial Banks (SCBs), Regional Rural Banks (RRBs) and Urban Co-operative Banks (UCBs). Estimates for the years 2004-05 to 2006-07 are given in Table 1.6 separately for enterprises with investment up to Rs. 5 lakhs and between Rs. 5 lakhs and Rs. 25 lakhs. Such a finding, in our view, should indeed be viewed as an eye-opener.

1.18 It is disconcerting to note that a paltry 2.2 per cent of credit has gone to the unorganised sector enterprises in the lower segment in 2007. Moreover, as per the Informal Sector Survey of 1999-00, only 4.2 per cent of such units (or an estimated 2.4 millions of the 58 million in 2006-07) availed of the institutional credit. This is despite a banking network of more than 75,000 branches of Scheduled Commercial Banks in the country. Another disturbing feature, as shown in the Commission's accompanying Report on Financing of the Unorganised Sector, is the substantial piggy backing of the loans at the lower segment of the unorganised sector enterprises with investment of less than Rs. 5 lakhs on to the credit-cum-subsidy linked self-employment schemes such as, Prime Minister Rozgar Yojana (PMRY), Rural Employment Gurantee Program (REGP), Swaranjyanti Grameen Swarozgar Yojana (SGSY) and Urban Self-employment Program (USEP) implemented by the Government, where banks are confident of a part of the loans advanced coming back to them in the form of subsidy for margin money. A portion of such loans is also those, which has been advanced under the SHG-Bank linkage programme.

1.19 It is pertinent to mention that the culture of micro finance is gaining pace in India. The volume of micro finance increased from about Rs. 200 crores five years back to Rs. 18,000 crores at present. This flow is largely included in the credit disbursement data discussed above. The flow of microfinance, though impressive, is still much lower than the estimated present requirements which are in the range of Rs. 50,000 - Rs. 200,000 crores. Thus, while microfinance has helped to bridge the gap to some extent, there still continues to exist a large gap in the demand for, and supply of, credit to the unorganised small size enterprises. It may be mentioned here that the Commission, in its accompanying Report on Financing has advocated the graduation of microfinance to livelihood finance and has pointed out that the present average size of loans available to the poor through micro credit is quite small, and is by and large, limited to smoothing of consumption and provision of very small production loans without due emphasis on enterprise asset creation which would require larger per unit quantum of assistance.

1.20 It is, thus, obvious that banks have not been able to meet adequately the credit requirements of the unorganised sector. The reluctance of the banks primarily reflects the bankers' high-risk perception of the sector (certainly not borne out by the exceptionally high rate of recovery in the case of micro credit), high transaction cost for small loans and also the non- stipulation of any priority sector target for the sector. The reluctance of the bankers is further corroborated by the fact that despite the availability of credit guarantee facility by Credit Guarantee Fund Trust for Micro and Small Enterprises (CGFTMSE) for loans up to Rs. 25 lakhs (raised to Rs. 50 lakhs from February 2007). As on March 31st 2007, only about 0.07 million units were found covered under credit guarantee. It was also found that, in spite of the RBI guidelines that loans up to Rs. 5 lakhs should be given without collaterals, available data reveal that only 26 per cent of such loans were advanced without collaterals. In other words, a vast productive sector of the economy populated by numerous micro enterprises continues to be deprived of financial inclusion in letter and spirit.

Table 1.6: Estimated Institutional Credit to Non-Farm Unorganised Sector Enterprises

Segments of Credit	Credit Advanced (Rs. Crores)				Share in Total Credit (per cent)			
	SCBs	RRBs	UCBs	Total	SCBs	RRBs	UCBs	Total
	As on March 2005							
Total Credit Advanced	1045954	31803	66874	1144631	100	100	100	100
Below Rs. 5 lakhs	22982	5657	8238	36877	2.2	17.8	12.3	3.3
Rs. 5 - 25 lakhs	22302	0	4119	26421	2.1	0	6.2	2.3
Total up to Rs.25 lakhs	45284	5657	12357	63298	4.3	17.8	18.5	5.6
	As on March 2006							
Total Credit Advanced	1443920	36050	70379	1550349	100	100	100	100
Below Rs. 5 lakhs	31726	5451	9772	46949	2.2	15.1	13.9	3.1
Rs. 5- 25 lakhs	30787	0	4886	35673	2.1	0	6.9	2.3
Total up to Rs. 25 lakhs	62514	5451	14658	82623	4.3	15.1	20.8	5.4
	As on March 2007							
Total Credit Advanced	1841978	48043	73898	1963919	100	100	100	100
Below Rs. 5 lakhs	40472	8546	10261	59279	2.2	17.8	13.9	3
Rs. 5- 25 lakhs	39275	0	5130	44405	2.1	0	6.9	2.3
Total up to Rs. 25 lakhs	79747	8546	15391	103684	4.3	17.8	20.8	5.3

Sources: RBI (2005-06a, b)

Note: Since separate data on credit to unorganised sector enterprises are not being maintained by the RBI and the Banks these have been estimated on the basis of available data and are based on the following assumptions:

(i) Unorganised sector enterprises consist of micro enterprises engaged in manufacturing (up to investment of Rs. 25 lakhs in P&M), cottage and village industries, artisan units and units engaged in services, small business, retail trade, road and water transport, professional self-employed persons and industrial estates up to a stipulated investment ceiling of Rs. 25 lakhs.

(ii) It is estimated that SCBs, RRBs, UCBs taken together account for 95 per cent of the total institutional credit to the unorganised sector enterprises. The contribution of other agencies like SIDBI, SFCs and SIDCs are insignificant since they cater mostly to the upper segment of the small and medium enterprises.

(iii) SCBs maintain separate data for credit to micro enterprises up to Rs. 5 lakhs - Rs. 25 lakhs in P&M, engaged in manufacturing. However they do not maintain separate data in these categories for credit to service, business and trade. Therefore, this has been worked out on the basis of the share of micro enterprises engaged in manufacturing in SSI credit.

(iv) In the case of RRBs the entire credit to artisans, small industries and small business has been taken as credit to micro enterprises with below Rs. 5 lakhs of investment since these are small sized rural units.

(v) In the case of UCBs credit to this segment has been apportioned on the basis of RBI guidelines to co-operatives that 60 per cent of the total advances should go to priority sector and 40 per cent to units with investment up to Rs. 5 lakhs and 20 per cent to units with investment up to Rs. 25 lakhs.

(vi) Since detailed data in the case of SCBs are available only for the year 2004-05, the same share has been maintained for the subsequent years.

(vii) The shares of RRBs and UCBs for the year 2006-07 have been computed on the basis of their shares in credit disbursed in 2004-05 and 2005-06.

Role of Developmental Financial Institutions

1.21 Besides commercial banks, Regional Rural Banks (RRBs) and cooperative banks, there are two other leading developmental financial institutions, viz, the Small Industries Development Bank of India (SIDBI) and National Bank for Agriculture and Rural Development (NABARD), which were set up to cater to the credit needs, among others, of the unorganised sector including the SSI sector. But despite a number of important initiatives, the efforts by these institutions still falls far short of meeting the credit and other developmental requirements of the non-farm unorganised sector.

[4] For non-manufacturing units the investment thresholds are as follows: Micro (Rs. 10 lakhs), Small (Rs. 10 lakhs - Rs. 2 crores), Medium (Rs. 2 - Rs. 5 crores).

1.22 SIDBI was created in 1990 for meeting the credit and developmental needs of the small-scale sector, which was then defined as enterprises with investment in plant & machinery up to Rs. one crore. Although SIDBI's mandate did not explicitly mention tiny/micro enterprises, the then definition of 'small' subsumed the micro/tiny sector. While SIDBI has played an important role in the development of the small enterprise sector, its contribution to the micro-enterprise sector has been comparatively modest. SIDBI has no regulatory power over the banks and has to work only through the limited number of its own branches. Its direct financing has been limited to term loans of Rs. 10 lakhs and above which can be availed of mainly by the larger among the small enterprises. SIDBI supports the entire small sector, including the micro-sector through credit refinance. The total refinance extended by SIDBI in 2006-07 was Rs.5,189 crores while direct credit was extended for projects worth Rs. 5,036 crores. As per the Commission's estimate, SIDBI's support to the micro enterprises, covering both refinance and direct finance, has not been more than 18 per cent of its total disbursements in 2006-07. SIDBI has also been operating a Micro Credit Foundation since 1995 and it has advanced a cumulative total of Rs.948 crores to Micro Finance Institutions (MFIs) up to 2007. During 2006-07, out of a total financial disbursement of Rs. 10,225 crores, SIDBI's support to the MFIs was to the tune of Rs. 376 crores.

1.23 With the enactment of Micro, Small and Medium Enterprise Development (MSMED) Act 2006, the small enterprise sector has been expanded to include what was earlier considered to be bigger units. As such, the small scale sector now embraces bigger units than before. The revised definition, as earlier, is based on investment without any reference to employment, that is to say, capital-labour ratio. Small enterprises in manufacturing are those with investment in plant and machinery above Rs. 25 lakhs and up to Rs. 5 crores. A new category of Medium enterprises in manufacturing has also been added, those with an investment of above Rs. 5 crores but below Rs. 10 crores. The micro-enterprises (with investment up to Rs. 25 lakhs) *now constitute a separate segment not subsumed under the small enterprises.*[4] *As such, these units may fall outside the scope of SIDBI.* On the other hand, the institution's scope of financing now extends to enterprises up to investment of Rs. 10 crores in plant and machinery.

1.24 Similarly, NABARD, created in 1982 by an Act of Parliament is also not in a position to cater to the huge credit demand of the unorganised sector in an adequate manner. NABARD has been set up for providing and regulating credit and other facilities for the promotion and development of agriculture, small-scale industries, cottage and village industries, handicrafts and other rural crafts and other allied economic activities in rural areas with a view to promoting integrated rural development and securing prosperity of rural areas. By the end of 2006-07, it had a resource base of Rs. 81,220 crores, a major part of which has been utilized for medium and long term loans for agriculture projects. In addition, the Rural Infrastructure Development Fund (RIDF) and the Bharat Nirman Fund are routed to states through NABARD. In the current year, i.e. 2007-08, the budget provision under these two funds is Rs. 16,000 crores.

1.25 NABARD is primarily a refinancing institution for the farm sector and operates mainly via cooperative banks and RRBs through the refinancing route. It is the supervising authority for RRBs. NABARD has also focused on the diversification and strengthening of the non-farm sector in rural areas through a number of initiatives and has been the principal source of expansion of micro credit through SHG-Bank linkage. According to the estimate made by the Commission, NABARD has been financing non-farm enterprises to the extent of 22-25 per cent of its total financial operations.

1.26 A brief note on the functioning of SIDBI and NABARD in relation to unorganised sector enterprises is given in Appendix 1. The Commission notes and acknowledges the important role played by these Development Banks for the unorganised sector. However, for SIDBI and NABARD, the non-farm unorganised sector is only one of the many functions. Moreover, NABARD's activities are restricted to rural areas, and SIDBI's role is confined to small-scale units. As with the banking operations in general, the lowest segment of the economy does not get adequate priority. The Commission has also separately noted (see below) that most of the existing funds operated by SIDBI and NABARD are special purpose funds (such as for venture capital to large companies, or for dairy and poultry sector). The quantum of these funds is either very low or is met out of the year-to-year budgetary allocation. The principal conclusion drawn by this Commission is that although both these institutions have played an important role with respect to the unorganised sector, there is still a huge gap which is needed to be filled through a more focused initiative.

Status of Existing Funds

1.27 There are a number of funds being maintained by SIDBI and NABARD for the promotion and development of the small and medium enterprises and for the farm and non-farm sectors. Among the funds maintained by SIDBI out of its own budget are the National Equity Fund, National Venture Fund for Software and IT Industry (NFSIT), Capital Fund, SME Growth Fund, Marketing Development Fund, Portfolio Risk Fund, Mahila Udhyam Nidhi, and the Mahila Vikas Nidhi. Firstly, the provisions made under these funds are so small (such as Rs. 15 crores for Portfolio Risk Fund and Rs. 9 crores for Mahila Vikas Nidhi) as to make any perceptible impact. Secondly, most of its funds have become non-functional. The only two funds that are functional at present are the Venture Capital Fund and SME Growth Fund to meet venture capital needs of large SSIs and medium enterprises, which exist in the form of companies.

1.28 Similarly NABARD is also maintaining several funds but most of them are for the agriculture sector such as Watershed Development, Farm Innovation, and Cattle Development. The only fund that exists for non-farm sector is the Rural Innovation Fund, the size of which is very small i.e less than Rs. 70 crores. The most important fund maintained by NABARD is the Rural Infrastructure Development Fund from which assistance is given to state governments to develop agricultural infrastructure such as irrigation, soil conservation, watershed development, rural bridges, roads etc.

1.29 In addition to the existing funds, there are three national level funds under creation, which have some relevance to the unorganised sector enterprises. These are: the Financial Inclusion Fund and the Financial Inclusion Technology Fund being created with NABARD as per the recommendations made in the interim report of the Rangarajan Committee on Financial Inclusion and announced by the Finance Minister in 2007-08 Budget proposals. The size of both these funds would be Rs 500 crores each. In addition, the RBI has proposed creation of the Small Enterprises Development Fund in its priority sector guidelines announced on 30th April, 2007. This fund will be created with SIDBI out of the short fall in priority sector lending to small enterprises sector by the foreign banks. A brief write up on the working of the existing funds having relevance to the unorganised sector enterprises and those proposed to be created is given in Appendix 2.

1.30 The main features of the existing funds are that they are budgeted, targeted and special purpose funds and none of them is available entirely for the unorganised sector.

1.31 This clearly shows that the existing institutions such as SIDBI and NABARD, and the various Funds which are in existence today are not in a position to meet the vast credit demand of the micro units. This non-availability of institutional credit in adequate and timely manner, coupled with the high interest rate, has resulted in financial distress, bankruptcy and suicide in a number of cases in the unorganised sector (e.g. handloom weavers). Thus, for varying reasons, the impact of these funds and overall credit by various institutions is still woefully small so far as the unorganised sector enterprises are concerned. This implies that a different approach is needed to meet the financial and developmental needs of the unorganised sector enterprises.

Non-Credit Needs of Unorganised Sector Enterprises

1.32 Moreover, inadequate and costly credit is just one of the numerous problems faced by the unorganised enterprises. Several other problems also exist, such as, obsolete technology, difficulties in procuring raw material and in the marketing of products, and those associated with the lack of skill development and entrepreneurship opportunities and inadequate infrastructure, particularly, that of power availability and transport facility. The sector is also beleaguered with information inefficiency, as information of well-intentioned government schemes has not percolated to the grass-root level of the economy. In other words, besides credit, promotional and developmental support is the crying need of the unorganised sector. Also, there is no national level institution to meet the credit requirements, to provide promotional and developmental support and above all, to advocate policy formulation for this unorganised sector.

The Necessity of a National Fund

1.33 Considering the urgency and necessity of providing adequate credit and developmental support to the unorganised sector enterprises for a faster and inclusive growth on the one hand and the inability and limitations of the present institutions like banks, SIDBI or NABARD to meet their growing credit demand on the other, there is a felt need for an exclusive and national level development financial institution which would ensure not only adequate finance by way of supplementing hitherto inadequate efforts of the existing financial institutions, but also provide financial and other assistance for promotional and developmental services to the unorganised sector.

2 Structure, Functions and Operation of the National Fund

A. Proposed Name

2.1 The National level Development Financial Institution for the Unorganised Sector will be called the National Fund for Unorganised Sector (NAFUS).

B. Legal Entity of the Organization

2.2 The Commission examined various forms of organisation, such as Government companies u/s 619 of Companies Act, Statutory Body under an Act of Parliament, Joint Venture, Trust and Societies to decide upon the suitable constitution of the Fund. Considering the various features of these forms of organisation as given in Appendix 3, and the relative merits and demerits of these organisational forms along with the nature of the working and functioning of the proposed Fund, the Commission recommends that it be created as a Statutory Body under an Act of Parliament.

2.3 A statutory body will have certain advantages such as:

- A statutory body will be guided by the provisions contained in the specific Act created for the specific purposes.
- The Fund will be set up with a larger socio-economic objective in mind but, given professional management, it could function as an economically viable entity as in the case of other public development finance institutions.
- A statutory body will be free from constraints faced by a government company.
- Also, as the Fund will have close collaboration and coordination with other national level institutions like SIDBI and NABARD, international level multilateral financial and development institutions and state level institutions like State Financial Corporations (SFCs) and State Industrial Development Corporations (SIDCs), It is suggested that NAFUS should have a high and national level stature as an apex development financial institution for the unorganised sector.

C. Capital Structure

2.4 Considering the vast resource requirements to provide increased credit support to the unorganised sector, NCEUS proposes an authorized capital of Rs. 1000 crores for the proposed institution. The initial paid-up capital is proposed at Rs. 500 crores in 2008 which would be gradually enhanced to Rs. 600 crores in 2009, Rs. 700 crores in 2010, Rs. 800 crores in 2011 and Rs. 1000 crores by 2011-12. The paid-up capital may be funded by the Central Government, public sector banks, financial institutions and others in such a way that the control of the Government of India directly or indirectly shall not be less than 51 per cent.

2.5 It may be noted that similar institutions like SIDBI, NABARD and India Infrastructure Financial Co. Ltd. (IIFCL) have the authorized capital of Rs. 1000 crores, Rs. 5000 crores and Rs. 1000 crores and paid-up capital of Rs. 450 crores, Rs. 2000 crores and Rs. 100 crores, respectively. In deciding the amount of paid up capital for the Fund, the Commission has been guided by two considerations. First, the Fund's volume of business will be larger than that of SIDBI and smaller than that of NABARD. Second, with this amount of paid up capital, the Fund will be able to leverage a much larger amount of capital as, like SIDBI, it will be controlled by government and will have sovereign guarantee.

D. Management

2.6 The management of the proposed Fund will consist of the following:

- A Board of Directors, comprising representatives of the Ministry of MSME, Ministry of Finance (MoF) and other concerned ministries, state governments, major shareholders, independent experts in the MSME sector, etc and representatives of regional/ national level associations of tiny/ micro enterprises.
- The Board shall be assisted by the following executives who shall be persons with proper professional competence and experience:
  - One Chairman cum Managing Director who shall be the Chief Executive.
  - Two Executive Directors (EDs), who shall be members of the proposed Board.
  - Such staff and other supporting professionals and executives as may be decided by the Board from time to time.

E. Target Group

2.7 The target group of NAFUS shall be all enterprises in the unorganised sector covering non-farm activities employing less than 10 workers, primarily those with investment in plant and machinery not exceeding Rs. 5 lakhs (excluding land and buildings) at 2004-05 prices, if engaged in manufacturing, and not exceeding Rs. 2 lakhs investment in plant and machinery, if engaged in non-manufacturing. However the upper limit of financing by the Fund will be enterprises with investment in plant and machinery not exceeding Rs. 25 lakhs, if engaged in manufacturing and investment in equipment not exceeding Rs. 10 lakhs, if engaged in non-manufacturing activities. It may be mentioned that 98 per cent of all the manufacturing non-agricultural small enterprises employ less than 10 workers with an average capital investment of Rs. 1.47 lakhs, as per the Third Census of SSI (2001-02). A large number of these enterprises are also engaged in service, business and trade. These enterprises account for 30 per cent of industrial production and provide employment to about 70 million persons.

F. Main Objectives

2.8 The NAFUS will be an apex development financial institution meant exclusively for the promotion, financing and development of the non-farm unorganised sector enterprises. The sector includes all enterprises in the primary sector (excluding cultivation), manufacturing, trade and services, which employ less than ten persons.

2.9 The main aim of NAFUS will be to bring about increased employment and higher incomes for people engaged in the unorganised sector by promoting and catalyzing the growth of the sector. Given the contribution of this sector to employment and the national economy, these objectives will promote inclusive national economic growth and reduce poverty and deprivation.

2.10 NAFUS will cater to the developmental needs of the unorganised sector through assistance to a range of promotional and developmental activities in the areas of credit, marketing, skill development, technology up-gradation, refinance, factoring services and common infrastructure development.

2.11 In order to fulfill its mandate, NAFUS will work in partnership with the existing financial institutions, national and state level agencies, micro-finance organisations, private and corporate bodies, R &D laboratories, marketing agencies and such other institutions and organisations as are concerned with the development of micro enterprises in the country.

G. Proposed Functions of the National Fund

Credit Assistance

2.12 The Fund will provide credit assistance to unorganised sector through:

(i) Refinance to banks and other financial intermediaries as in the case of agriculture refinance, to supplement their efforts to provide credit to unorganised sector enterprises with investment in plant and machinery up to Rs. 25 lakhs with special focus on enterprises with investment in plant and machinery up to Rs. 5 lakhs.

(ii) Provide micro finance support through NGOs/ SHGs/ Micro Finance Institutions (MFIs) as well as the formal banking system.

(iii) Provide seed capital and such other start up capital requirements for the new entrepreneurs in the unorganised sector.

Developmental Support

2.13 To provide grant support to institutions engaged in the promotion and development of unorganised sector enterprises with the twin objectives of: (a) creation of new unorganised sector enterprises, and (b) strengthening the existing unorganised sector enterprises to withstand the competition.

a) Creation of Unorganised Sector Enterprises

2.14 *Entrepreneurship Development:* The objective of the Programme of Entrepreneurship Development (PED) is to promote entrepreneurship and create avenues for self-employed ventures capable of generating additional employment. This can be done by supporting the existing institutions engaged in this task. It is important that the focus of this effort should be towards practical and functional training. It should cover areas such as production scheduling, book keeping, profit monitoring, basic legal compliance, market assessment, trouble shooting and logistics.

2.15 *Vocational Training:* A number of entrepreneurs are self-employed and as the economy becomes more sophisticated, learning in an informal manner will not be adequate. Electricians, caterers, taxi operators, motor mechanics etc. are examples of businesses that will increasingly need formal training. There are institutions both in the public and private domains that provide training and certification. The Fund will support the capabilities of the training institutions in order to impart skills that are contemporary and based on market needs. The initiative of the Fund will also supplement the existing programmes for vocational training.

2.16 *Capacity Building and Hand Holding:* The programme of creation and development of unorganised enterprises may be implemented by the NGOs, Technical Consultancy Organisations (TCOs), Entrepreneurship Development Institutes, development professionals, and similar agencies. These agencies could provide various professional services necessary for setting up of micro enterprises. Such services would inter-alia, include identifying and motivating rural entrepreneurs, project identification, training, appropriate technology/ finance tie-up and development market linkages. The strength lies in gainful utilisation of a vast quantum of local resources in rural areas by harnessing locally available skills, thereby addressing the national problems such as rural unemployment and urban migration. It is, thus, essential to strengthen the agencies, which provide linkages through their capacity building.

b) Strengthening of Unorganised Sector Enterprises

2.17 *Strengthening of Unorganised Sector Enterprise Clusters:* Cluster Development Programme (CDP) would be oriented to meet the diverse needs of a cluster, particularly, the provision of common facilities, infrastructure, testing facilities, effluent treatment, strengthening marketing network, improvement of quality etc. There are various agencies like Development Commissioner for Small Scale Industries (DCSSI), Khadi and Village Industries Commission (KVIC) and the All India Boards engaged in this task. These need to be coordinated and integrated to achieve larger goals. The NAFUS will try to bring about integrated development of clusters working in the unorganised sector.

2.18 *Marketing Support:* This is the area where the unorganised sector needs maximum assistance. Past efforts have failed due to inadequate understanding of the market or poor delivery capabilities. Market understanding includes assessing the size of market, competitive environment, international implications, future threats, consumer understanding and so on. Often delivery is poor due to improper trade channels, high cost logistics, inventory build up and so on. Unorganised sector cannot compete with large players as they do not have the resource back up. Often the organised sector is able to dominate in areas that were traditionally unorganised. Snack foods is an example where large players are now increasing their presence. If small players were provided support in the areas listed above, they will be able to effectively compete as they have lower overhead costs. The Fund will support specialized institutions that can help in aggregating both small producers and mainstream markets, and effectively link both ends.

2.19 *Support for Raw Material Procurement:* The Fund will facilitate the availability of raw materials to the unorganised enterprises by way of deferred payments through the current banking channels and strengthen the existing agencies like SIDC, NSIC and KVIC engaged in the task. It may be mentioned that the KVIC has introduced the common facility service in the form of rural industrial service centres through which the group/ clusters can organise raw material godowns for common purpose to solve raw material crisis. Area-wise requirement of critical raw materials needs to be assessed and their supplies need to be integrated through the existing agencies. The Fund is envisaged to bring this coordination.

2.20 *Technology Upgradation:* This is again an important area as very often a change in technology can lead to businesses becoming obsolete. Some prominent examples are: (a) With the universal presence of mobile telephones, the PCO sector is under threat, (b) Availability of paper and plastic plates can make the pottery and the leaf plate business obsolete. Addressing these challenges is necessary so that either alternative activities are identified or technology is upgraded to meet the challenges. This should be done in a proactive way for all the major businesses that normally fall within the unorganised sector, so that the damage on account of technology changes is minimized. There are several institutions such as the Technology Centre at the Indian Institute of Technology (IIT), Delhi and Application of Science and Technology for Rural Areas (ASTRA) set up by the Indian Institute of Science (IISc), Bangalore that can play this role and the Fund should support such institutions. For example, KVIC has developed interface with the 7 IITs. Mahatma Gandhi Institute for Rural Industrialisation has been set up at Wardha with the assistance of IIT, Delhi for providing inputs in the area of Technology Up-gradation, Research and Development, Quality Control and Training. There are several other, perhaps lesser known, institutions of similar kind who could play a crucial role in strengthening the technical capacity of the micro enterprises. The programme of various agencies engaged in this task need to be coordinated in the light of the emerging technology requirements of the unorganised sector.

c) Information Dissemination

2.21 The Fund will work as the resource centre for information on unorganised sector.

d) Policy Advocacy:

2.22 The National Fund will advocate policy initiations with central and state governments, Planning Commission, RBI and others. To realize the objectives, the Fund will establish linkages with the existing institutions/agencies working for the development and financing of the unorganised sector.

H. Mode of Operation of the National Fund for Unorganised Sector

2.23 The Fund, after being set up as a legal entity, will channelize the financial resources by leveraging the infrastructure of the banks and various other financial organizations in the country. In order to bring synergy, it will enter into MoUs with the banks, various national and state level Direct Financial Institutions (DFIs) like NABARD, SIDBI, NSIC, SFCs, SIDCs and such other institutions as engaged in similar activities. It will also enter into MoUs with the Credit Guarantee Fund Trust for Micro & Small Enterprises (CGTMSE) for providing additional credit guarantee coverage; with SME Rating Agency of India Ltd. (SMERA) for credit rating of micro enterprises; with MFIs for supporting the micro financing and also with venture financing institutions. Thus, the operational and functional activities of the new entity shall be based on a business-to-business (B to B) model.

I. Operating Targets

2.24 The operating targets for credit would be: (a) to raise the bank credit availability for the unorganised sector enterprises with investment in plant and machinery up to Rs. 5 lakhs, from the current level of 2.2 per cent to 5 per cent by 2011-12; (b) to raise the bank credit availability for the unorganised sector enterprises with investment in plant and machinery up to Rs. 25 lakhs from the current level of 5 per cent to 8 per cent by 2011-12; and (c) to cover 500 districts for promotional and developmental support during the 11th Plan.

J. Projected Operations of the Fund

2.25 As per the operational targets, the projected operations of the Fund have been estimated for two segments for unorganised sector enterprises: (i) with investment in plant and machinery up to Rs. 5 lakhs, and (ii) with investment in plant and machinery up to Rs. 25 lakhs.

Projections for Unorganised Sector Enterprises with Investment up to Rs. 5 lakhs

Uses of Fund

2.26 The main uses of funds are (i) refinance, (ii) developmental support, (iii) interest payments on borrowed money, and (iv) administrative expenses.

Refinance

2.27 As per the main objective and operating targets, the Fund will be mainly used to provide refinance support to banks and financial institutions so as to calibrate the present share of bank finance to unorganised sector enterprises from 2.2 per cent to 5 per cent by 2012. The estimation of the refinance requirements during the 11th Plan is based on the following assumptions:

(i) The main sources of credit to the unorganised sector are Scheduled Commercial Banks (SCBs), RRBs and Urban Cooperative Banks (UCBs). These three sources constitute almost 95 per cent of the total credit to the unorganised sector.

(ii) The non- food gross bank credit is expected to grow at 20 per cent p.a. during the 11th Plan. Although the growth rate during 2006-07 is estimated at 28 per cent, it is expected to moderate during the 11th Plan.

(iii) Even though NCEUS recommends a mandatory 5 per cent bank credit to the unorganised sector, it is assumed that the Scheduled Commercial Banks (SCBs) would commit 2.2 per cent of their credit disbursement to the unorganised sector on a business-as-usual scenario and the balance 2.8 per cent would be made available by the Fund by way of refinance support to banks.

(iv) It is assumed that while the RRBs would continue to record 20 per cent annual growth rate in their gross credit in tandem with the SCBs, the share of the unorganised sector enterprises with investment up to Rs. 5 lakhs would remain constant at 17.8 per cent.

(v) Similarly, Urban Cooperative Banks (UCBs) are expected to show a 5 per cent annual credit growth, while the share of the unorganised sector enterprises up to investment of Rs. 5 lakhs would remain constant at 13.9 per cent.

2.28 Based on the above assumptions, the estimation of the total credit gap for the whole of the unorganised sector and refinance requirements for enhancing bank credit share of the unorganised sector enterprises with investment up to Rs 5 lakhs from 2.2 per cent to 5 per cent is given in Table 2.1.

Table 2.1: Estimation of the Refinance Requirements (Outstanding) for Units with Investment in Plant and Machinery up to Rs. 5 lakhs

Item	2006-07	2007-08	2008-09	2009-10	2010-11	2011-12	Variation during 11th Plan (2011-12 over 2006-07)
1. Total number of units in the unorganised sector (based on 4 per cent growth rate) (lakhs)	580	603	627	652	678	706	126
2. Average Credit Off take by an Unorganised Sector Enterprise (with an expected 4 per cent inflation) (Rs. Lakhs)@	0.64	0.67	0.69	0.72	0.75	0.78	--
3. Total Credit Requirements [(1) x (2)] (Rs. 000 crores)	371	401	434	469	508	550	179
4. Estimated Credit from SCBs at Constant 2.2 per cent, for RRBs at 17.8 per cent and UCBs at 13.9 per cent (Rs. 000 crores) (rounded)	59	70	82	97	114	135	76

Table 2.1 Cont......

Item	2006-07	2007-08	2008-09	2009-10	2010-11	2011-12	Variation during 11th Plan (2011-12 over 2006-07)
5. Credit Gap at Constant 5 per cent Share [(3) - (4)] (Rs. 000 crores)	312	331	352	372	394	415	n.a.
Credit Gap (as per cent of (3))	84	82	81	79	78	75	_
6. Expected Credit to Unorganised Sector Enterprises from SCBs (Increasing Share from 2.2 per cent to 5 per cent) (Rs. 000 crores, rounded)	59	83	114	154	202	264	205
7. Credit Gap with Increased Share of Bank Credit [(3) - (6)] (Rs. 000 crores)	312	318	320	315	306	286	--
	84	79	74	67	60	52	n.a.
8. Additional Credit Flow for the increased share of 5 per cent (Rs. 000 crore) (Increase over previous year)	N.A	24	31	40	48	62	204
Of which:							
(a) By Banks at Constant 2.2 per cent) (Increase over previous year)	--	11	12	15	17	21	76
(b) Finance Gap to be filled up by the National Fund (8-(a))		13	19	25	31	40	128
Memo Items: i) Non-food Gross Bank Credit of SCBs (at 20 per cent Growth Rate) (Rs. 000 crore)	1964	2346	2803	3351	4009	4797	2833
ii) Proposed increase in per cent Share of SCBs	2.2	2.8	3.4	4.0	4.5	5.0	

Note: @ estimated from NSSO 55th Round Informal sector Survey, 1999-2000
Source: Computed based on RBI (2006-07b; 2005-06a), NSSO (2001)

2.29 It may be observed from the Table 2.1 that if the past trend of 4 per cent growth is taken as the base, the total number of unorganised sector enterprises would increase from an estimated 58 million in 2006-07 to almost 71 million in the terminal year of the 11th Plan, i.e. 2011-12, resulting in additional 12.6 million unorganised sector enterprises during the Plan period. The credit requirement would increase from Rs. 371 thousand crores in 2006-07 to Rs. 550 thousand crores in 2011-12; thus requiring an additional credit of Rs. 179 thousand crores for the unorganised sector. This is by any means a huge amount, which would be very difficult for the formal financial institutions (FFIs) like banks to meet under the current scenario, given that the past share of bank's outstanding credit to this sector has been very nominal, at around 2.2 per cent only. If this trend is maintained, the outstanding bank credit by 2012 would be Rs. 135 thousand crores which means banks would be able to meet only 25 per cent of the outstanding credit requirements (Rs. 550 thousand crores) of the unorganised sector enterprises as against about 16 per cent in 2007. On an incremental basis, the banks' credit (Rs. 76 thousand crores) during the 11th Plan would meet only 42 per cent of the additional credit requirements.

2.30 It is thus clear that if the normal trend in bank finance to unorganised sector is maintained, almost 75 per cent of the credit requirements would remain outside the financial institutions. Hence, special thrust is needed to meet at least 50 per cent of the outstanding credit requirements from the banks, which would be possible only when the banks and others are in a position to meet more than the additional credit requirements of these unorganised sector enterprises. Hence, in order to widen the financial inclusion growth process, the Commission has recommended that bank credit to the unorganised sector enterprises with investment up to Rs. 5 lakhs should be calibrated from the current 2.2 per cent to 5 per cent by the end of the 11^{th} Plan. With this increased bank finance, banks would be able to meet almost 48 per cent of the outstanding credit requirements by the end of 2011-12 and about 114 per cent of the additional credit requirements of the sector for the Plan.

2.31 It may also be observed from the Table 2.1 that in order to calibrate the share of bank finance to unorganised sector enterprises from the present level of 2.2 per cent to 5 per cent by 2012, the additional credit flow of Rs. 128 thousand crores during the 11th Plan, corresponding to the increase of 2.8 per cent of the outstanding credit, needs to be provided by way of refinance support to banks and other financial institutions from the proposed National Fund. For this, the banks need to be sufficiently incentivised to increase their financing support to unorganised sector enterprises to the estimated level, for which an 8 point action plan, based on the Commission's Report on Financing Requirement of the Unorganised Sector is suggested in Appendix 4 of this Report.

Grant Support for Developmental Activities

2.32 Besides refinance support, the proposed Fund is also to be used for providing promotional and developmental support in term of entrepreneurship development, management oriented training, vocational training, capacity building and hand-holding marketing support, skill up gradation, etc. as outlined under broad developmental functions elsewhere in this Report. The detailed estimation of grant support is based on the following assumptions

(i) The programme of Capacity Building and Hand-holding (CBH) to promote rural industrialisation, which generally spans over a period of 5 years, is expected to generate 100 units in the first year and additional 50 units in the subsequent year.

(ii) Each CBH is assumed to cost Rs. 10 lakhs.

(iii) Employment per unit created under CBH is assumed as 2.

(iv) Each Programme of Entrepreneurship Development (PED) would comprise 25-30 participants. Assuming a success rate of 40-50 per cent, the number of units to be set up after every PED is estimated at 12.

(v) Employment per unit created under PED is kept constant at 2.

(vi) Grant support to each PED is assumed at Rs. 75000/- @ Rs. 3000/-per candidate. This is comparable with the grant support of Rs.3500/- given under PMRY training.

(vii) Each Management Programme (MP) would comprise 25 candidates.

(viii) The success rate of each MP in employment engagement is assumed at 100 per cent.

(ix) Each Vocational Training (VT) would comprise 36 candidates.

(x) The success rate of finding jobs for candidates trained under VT is assumed at 100 per cent.

2.33 Based on the above assumptions, the estimation of funds requirements for supporting developmental activities are given in the Table 2.2.

Table 2.2: Estimation of Grant Support for Developmental Activities (Rs. Crores) (Units with Investment in Plant and Machinery up to Rs. 5 lakhs)

Sl. No.	Items	2007-08	2008-09	2009-10	2010-11	2011-12
1	Capacity Building and Hand-holding (CBH) (As per Appendix Table A5.1)	12	13	14	15	16
2	Programmes Entrepreneurship Development (PEDs) (As per Appendix Table A5.2)	40	59	79	99	119
3	Management Programmes (MPs) (As per Appendix Table A5.3)	3	5	7	8	10
4	Vocational Trainings (VTs) (As per Appendix Table A5.4)	10	20	30	40	50
5	Cluster Development Programme	10	20	30	40	50
6	Others (Marketing, Skill Up-gradation, Information Disseminations, Pollution Control, Raw Material Support)	17	35	51	70	87
	Total	**92**	**142**	**192**	**242**	**292**

Source: Estimated.

2.34 A breakup of the various components of P&D expenditure is given in Appendix 5. It would be noticed from Table 2.2 and the Appendix, that the P&D grant support has been projected at a very modest level. However, as the Fund's capacity to undertake such expenditures increases, there is a vary strong case for expanding P & D support, both in view of the vastness of the sector and the benefit-cost ratio of such expenditure, as has emerged from experience of other Development Financial Institutions such as SIDBI.

Interest Payments and Administrative Expenses

2.35 Besides the funding requirements of refinance to banks and developmental grant support to the sector, the other uses of the National Fund are for payment of interest on borrowed funds which is assumed to be at a weighted average rate of 7 per cent of the outlays for both domestic and international borrowings, and administrative and related expenses. The consolidated uses of funds are given in Table 2.3.

Table 2.3: Uses of Funds (Rs. Crores) for Units with Investment in Plant and Machinery up to Rs. 5 lakhs

Year	Refinance Support	Interest payments (@ 7 per cent)	P & D Break-up Expenses	Adm. Exp.	Total
2007-08	13262	464	92	13	13831
2008-09	18567	1578	142	18	20305
2009-10	25464	3119	192	23	28798
2010-11	30556	5080	242	28	35906
2011-12	40487	7566	292	33	48378
Total	**128336**	**17807**	**960**	**115**	**147218**

Source: Estimated

2.36 It is observed from the Table 2.3 that the total funding requirements of the National Fund are estimated to be Rs. 1,47,218 crores which will increase from Rs. 13,831 crores during 2008 to Rs. 48378 crores during the terminal year of the 11th Plan, i.e. 2012.

Sources of Funds

Interest Income

2.37 Interest income has 2 components. First is the interest income on refinance support @ 7 per cent per annum. The second component is interest income on the investment of paid-up capital @ 7 per cent per annum.

Government's Budgetary Support

2.38 Budgetary support from the Government is proposed to meet 3 types of expenditure. First, it is required to meet the grant based developmental support to the unorganised sector enterprise sector. Second, it is required for meeting the regular administrative expenses. The third requirement is the interest subsidy. Based on the recommendation separately made by the Commission that the cost of borrowing for this sector should be the same as for agriculture, it is assumed that while the Fund would provide refinance to banks and others at 7 per cent by borrowing resources at higher market related rates, it needs to be suitably compensated by way of an interest subsidy of 2 per cent from Government of India as in case of agriculture loans.

Market Borrowing

2.39 FUS shall be largely met from domestic market borrowings through SLR bonds, tax free bonds, borrowing from the international market with Government bearing the exchange risk. The major sources are given in the Table 2.4.

Table 2.4: Sources of Funds (Rs. Crores)

(For Loans for Unorganised Sector Enterprises with Investments up to 5 lakhs in Plant and Machinery

Sl.No	Item/Year	2007-08	2008-09	2009-10	2010-11	2011-12	Total during the 11th Plan
1	Interest Income @ 7 per cent (both on Refinance and Paid-up Capital)	482	1620	3168	5136	7636	18042
	Per cent Share of the Total	3.48	7.98	11.00	14.30	15.78	12.26
2	GoI Total	237	611	1106	1721	2487	6162
	P&D Expenditure	92	142	192	242	292	960
	Administrative Expenditure	13	18	23	28	33	115
	Interest Subsidy at 2 per cent	132	451	891	1451	2162	5087
	per cent Share of the total	1.71	3.01	3.84	4.79	5.14	4.19
3	International Borrowing	3458	5076	7200	8977	12095	36805
	Per cent Share of the Total	25	25	25	25	25	25
4	Market Borrowing (as SLR, Tax Free Bonds)	9654	12998	17325	20073	26161	86210
	Per cent Share of the Total	69.80	64.01	60.16	55.90	54.08	58.56
	Total	**13831**	**20305**	**28798**	**35906**	**48378**	**147218**

Note: Interest income is calculated @ 7 per cent refinance. For every annual refinance volume, the interest rate is calculated on half the amount for the initial year only as it is assumed that refinance will be spread over the whole year. For the subsequent years, refinance rate of 7 per cent is applied on the full refinance volume.

Source: Estimated

Projections for Unorganised Sector Enterprises with Investment up to Rs. 25 lakhs

Uses of Funds

2.40 The main uses of the funds are again for (i) refinance, (ii) developmental support, (iii) interest payments on borrowed money and (iv) administrative expenses.

Refinance

2.41 As per the main objective and operating targets, the Fund will be mainly used to provide refinance support to banks so as to calibrate the present share of bank finance to unorganised sector enterprises with investment in plant and machinery up to Rs. 25 lakhs from the present level of 5 per cent to 8 per cent by 2012. The estimation of the refinance requirements during the 11th Plan is based on the following assumptions:

- The main sources of credit to the unorganised sector are Scheduled Commercial Banks (SCBs), RRBs and Urban Cooperative Banks (UCBs). These three sources constitute almost 95 per cent of the total credit to unorganised sector.
- The Non- Food Gross Bank Credit is expected to grow at 20 per cent per annum during the 11th Plan. Though the growth rate during the last year was 28 per cent, it is expected to moderate during the 11th Plan.
- Even though NCEUS recommends a mandatory 8 per cent bank credit to the unorganised sector, it is assumed that the Scheduled Commercial Banks (SCBs) would commit only 4.3 per cent of their credit disbursement to the unorganised sector as observed in the present scenario and the balance 3.7 per cent would be made available by the Fund by way of refinance support to banks.
- It is assumed that while the RRBs would continue to record 20 per cent annual growth rate in their gross credit in tandem with the SCBs, their share to the unorganised sector enterprises with investment up to Rs. 25 lakhs would remain constant at 17.8 per cent.
- Similarly, Urban Cooperative Banks (UCBs) are expected to show 5 per cent annual credit growth, while their share of the credit to the unorganised sector enterprises up to investment in plant and machinery of Rs. 25 lakhs would remain constant at 20.8 per cent.

2.42 Based on the above assumptions, the estimated requirements of additional finance for enhanced bank credit share from 4.3 per cent to 8 per cent are given in Table 2.5.

Table 2.5: Estimation of Refinance Requirements (Outstanding) for Units with Investment in Plant and Machinery up to Rs. 25 lakhs

Item	2006-07	2007-08	2008-09	2009-10	2010-11	2011-12	Total variation during the 11th Plan (2011-12 over 2006-07)
1. Total Number of Units in the Unorganised Sector (based on 4 per cent Growth Rate) (lakhs)	581	604	628	653	679	707	126
2. Average Credit Requirement per SME (with an Expected 4 per cent I Inflation) (Rs. Lakhs) @	1.01	1.05	1.09	1.14	1.18	1.23	
3. Total Credit Requirements [(1) x (2)] (Rs. 000 crores) (rounded)	587	634	686	742	802	869	282
4. Estimated Credit from SCBs at Constant 4.3 per cent, r RRBs at 17.8 per cent and UCBs at 13.9 per cent (Rs. 000 crores)	104	121	143	169	201	238	134

Table 2.5 Cont.....

Item	2006-07	2007-08	2008-09	2009-10	2010-11	2011-12	Total variation during the 11th Plan (2011-12 over 2006-07)
5. Credit Gap at Constant 4.3 per cent Share [(3) - (4)] (Rs. 000 crores)	483	513	543	573	601	631	n.a.
Credit Gap (per cent)	82	81	79	77	75	73	n.a.
6. Expected Credit to Unorganised Sector Enterprises from SCBs, RRBs & UCBs (with Increased Share from 4.3 per cent to 8 per cent of SCB credit) (Rs 000 crore)	104	137	180	236	315	408	304
7. Credit Gap at increased Share of Bank Credit [(3) - (6)] (Rs. 000 crores)	483	497	506	506	487	469	n.a.
Credit Gap (per cent)	72	78	74	68	61	54	n.a.
8. Additional Credit Flow to increase to 8 per cent of Credit (Rs. 000 crores) (Increase over previous year)	N.A	33	43	56	79	92	304
Of which							
(a) By banks at Constant 4.3 per cent) (Increase over previous year)	--	18	22	26	31	37	134
(b) Finance Gap to increase to 8 per cent to be Filled by the National Fund (8-(a))		15	21	30	48	55	170
Memo Items: i) Non - Food Gross Bank Credit of SCBs (Outstanding) (at 20 per cent Growth Rate) (Rs. 000 crores)	1964	2346	2803	3351	4009	4797	2833
ii) Proposed Increase in per cent Share of SCBs	4.3	5.0	5.7	6.4	7.3	8.0	

Source: Same as in Table 2.1

2.43 It may be observed from Table 2.5 that if the present trend of 4.3 per cent total bank credit to this segment is maintained, the outstanding bank credit by the end of 2012 would be Rs. 238 thousand crores, which would be meeting almost 27 per cent of the total outstanding credit requirements. On an incremental basis, the additional bank finance at Rs. 134 thousand crores would be meeting almost 48 per cent of the additional credit requirements. However, with the proposed increase in bank credit from 4.3 per cent to 8 per cent, the outstanding bank credit would be equivalent to almost 46 per cent of the total outstanding credit requirements. This would be possible only when the additional credit availability from the banks and others at 8 per cent of the total bank credit meet more than 100 per cent of the additional credit requirements for all the units with investment up to Rs 25 lakhs. In the present estimate the additional credit flow would be 108 per cent of the additional credit requirements. In fact, if one wants to meet at least 50 per cent of the outstanding credit by 2012, the additional credit flow should be Rs 331 thousand crores or 117 per cent of the additional credit requirements of all the units with investment up to Rs 25 lakhs. In other words, for meeting 50 per cent of the outstanding credit requirements, banks may be required to give more than 8 per cent of the total credit to these units. However, on a reasonable basis, NCEUS recommends only 8 per cent of bank credit to go to units with investment up to 25 lakhs by 2012.

2.44 It may be observed from Table 2.5 that if the banks maintain 4.3 per cent constant share, there would be a credit gap of almost Rs.170 thousand crores for increasing the share to 8 per cent. This gap needs to be bridged by the NAFUS by way of refinance support to the banks.

Grant Support for Developmental Activities

2.45 The grant support for developmental activities would remain the same as indicated under the operations of unorganised sector enterprises with investment in plant and machinery up to Rs. 5 lakhs.

Interest Payments and Administrative Expenses

2.46 Besides the funding requirements of refinance to banks and developmental grant support to the sector, the other uses of the National Fund are for payment of interest on borrowed funds which is assumed to be at a weighted average rate of 7 per cent for both domestic and international borrowings, and administrative and related expenses. The consolidated uses of funds are given in Table 2.6.

Table 2.6: Uses of Funds (Rs. Crores)
(For Unorganised Sector Enterprises with Investments in Plant and Machinery upto 25 lakhs

Year	Refinance Support	Interest Payments (7 per cent rate)	P & D Expenses	Adm. Exp.	Total
2007-08	15473	542	92	13	16120
2008-09	21662	1841	142	18	23663
2009-10	29707	3639	192	23	33561
2010-11	47744	6350	242	28	54364
2011-12	55001	9946	292	33	65272
Total	**169587**	**22318**	**960**	**115**	**192980**

Source: Estimated

2.47 It is observed from the Table 2.6 that the total funding requirements of the National Fund during the 11th Plan would be Rs. 192980 crores, an increase from Rs. 16120 crores during F.Y. 2008 to Rs. 65272 crores during the terminal year of the 11th Plan, i.e. F.Y. 2012.

Sources of Funds

Interest Income

2.48 Interest income has 2 components. First is the interest income on refinance support @ 7 per cent p.a. The second is the interest income on the investment of paid-up capital @ 7 per cent p.a.

Government's Budgetary Support

2.49 The Government's budgetary support is proposed to meet 3 types of expenditure. First, is the grant based developmental support to the unorganised sector enterprise sector. Second, the regular administrative expenses and third the cost of the interest subsidy. As stated earlier, the Commission has recommended that the interest borne by the unorganised sector enterprises should be the same as in the case of agriculture. It is therefore assumed that while the Fund would provide refinance to banks and others at 7 per cent by borrowing resources at higher market related rates, it needs to be suitably compensated by way of interest subsidy of 2 per cent from Government as in case of agriculture loans.

Market Borrowing

2.50 The funds for the financial operations of the NAFUS shall be largely met from the domestic market borrowings through SLR bonds, tax free bonds, borrowing from international market with the Government bearing the exchange risk. The major sources are given in the Table 2.7.

Table 2.7: Sources of Funds (Rs. Crores)
(For Unorganised Sector Enterprises with Investments in Plant and Machinery up to 25 lakhs)

Item	2007-08	2008-09	2009-10	2010-11	2011-12	During 11th Plan
1. Interest Income @ 7 per cent	560	1883	3688	6406	10016	22553
Per cent Share of the Total	3.47	7.96	10.99	11.78	15.35	11.69
2. GoI (Budgetary Provision for P & D, Admn. and 2 per cent Interest Subsidy),	260	686	1255	2088	3167	7456
Of which Interest Subsidy	155	526	1040	1814	2842	6377
P & D Exp	92	142	192	242	292	960
Admn. Exp	13	18	23	28	33	115
Per cent Share of the Total	1.61	2.90	3.74	3.84	4.85	3.86
3. International Borrowing	4030	5916	8390	13591	16318	48245
Per cent Share of the Total	25	25	25	25	25	25
4. Market Borrowing (as SLR, Tax free Bonds)	11270	15178	20228	32279	35771	114726
Per cent Share the Total	69.91	64.14	60.27	59.38	54.80	59.45
Total	**16120**	**23663**	**33561**	**54364**	**65272**	**192980**

Note: Interest income is calculated @ 7 per cent refinance for every annual refinance volume. The interest rate is calculated on half the amount for the initial year only as it is assumed that refinance will be spread over the whole year. For the subsequent years, refinance rate of 7 per cent is applied on the full refinance volume.

Source: Estimated

K. Impact of Increased Credit Support

2.51 The increased credit support to the unorganised sector would bring a vast section of the population under the fold of financially inclusive growth process. Moreover, in the changing scenario of increasing liberalisation and intensified competition, the survival of the unorganised enterprises on a sustainable basis may be at stake. Hence, substantial growth of unorganised sector enterprises and employment during the 11th Plan would be possible only through the increased institutional credit and promotional and developmental support. The specific impacts on employment and income are given in Table 2.8.

Impact on Employment creation

Enterprises with investment upto Rs. 5 lakh

2.52 With a constant 2.2 per cent bank credit share during the Plan, the normal growth in bank financed unorganised sector enterprises would be 10.41 million and employment generation would be 18.74 million during the Plan (Table 2.8). However, with the proposed intervention of higher credit flow from the banks to the unorganised sector from 2.2 per cent to 5 per cent share, there will be the creation of additional 17.5 million unorganised sector enterprises and 31.5 million additional employment opportunities during the 11th Plan.

Table 2.8: Impact of Additional Bank Credit
(For Unorganised Sector Enterprises with Investments in Plant and Machinery up to Rs. 5 lakhs)

Item	2007-08	2008-09	2009-10	2010-11	2011-12	Total Variation during the 11th Plan
Scenario 1 : Bank Credit to the Unorganised Sector at Constant 2.2 per cent Share of the Total Bank Credit						
Additional Credit Availability (Rs. crores)	10397	12317	14700	17555	20977	75,946
Additional no. of Units to be Created (lakhs)	15.5	17.9	20.4	23.4	26.9	104.1
Additional Employment creation (@1.8 persons per unit) (lakhs)	27.9	32.2	36.7	42.1	48.4	187.4
Scenario 2: Bank Credit to the Unorganised Sector Increasing from 2.2 per cent to 5 per cent						
Additional Credit Availability (Rs. crores)	13262	18567	25464	30556	40487	128336
Additional no. of Units to be created (lakhs)	19.8	26.9	35.4	40.7	51.9	174.7
Additional Employment creation (@1.8 Persons per unit) (lakhs)	35.6	48.4	63.7	73.3	93.4	314.5

Source: Estimated

Enterprises with investment upto Rs. 25 lakh

2.53 With the proposed intervention of higher credit flow from the banks to the unorganised sector at 8 per cent share, an additional 15 million unorganised sector enterprises will be created along with 26 million additional employment opportunities during the 11th Plan (Table 2.9). However, it may be noted that the increase in number of enterprises were projected at 12.6 million as explained in Chapter 2 of the Financing of Unorganised Enterprises report. It can also be termed as business as usual scenario. It can be seen that the additional number of enterprises created with investment upto Rs 25 lakhs would be lower than projected.

Impact on National Income

2.54 According to the Commission's estimate, the proposed refinance intervention will lead to an addition of 1.23 per cent and 1.68 per cent of GDP for units with investment in P&M upto Rs 5 lakh and for units upto Rs 25 lakh respectively for the year 2011-12. This was estimated with the assumption that GDP would grow at 9 per cent per annum with a 4 per cent inflation over the previous year 2011-12. It was also assumed that the value added would be 40 per cent of the total value of production determined by taking 4 times (implying 4 cycles of production) the refinance support in 2011-12.

Table 2.9: Impact of Additional Bank Credit (For Unorganised Sector Enterprises with Investments in Plant and Machinery up to Rs. 25 lakhs)

Item	2007-08	2008-09	2009-10	2010-11	2011-12	Total Variation during the 11th Plan
Scenario 1 : Bank Credit to the Unorganised Sector at Constant 4.3 per cent Share of the Total Bank Credit						
Additional Credit Availability (Rs. crores)	17763	21869	26121	31218	37329	134,300
Additional no. of Units to be Created (million)	1.69	2.01	2.29	2.65	3.03	11.67
Additional Employment Creation (@1.8 Persons per unit) (million)	3.04	3.62	4.12	4.77	5.45	21.01
Scenario 2: Bank Credit to Unorganised Sector I Increasing from 5 per cent to 8 per cent						
Additional Credit Availability (Rs. crores)	15473	21662	29707	47744	55001	169587
Additional no. of Units to be Created (million)	1.47	1.99	2.61	4.05	4.47	14.59
Additional Employment Creation (@1.8 Persons per unit) (million)	2.65	3.58	4.70	7.29	8.05	26.26

Source: Estimated.

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Appendices

Appendix - 1
Institutional Support for the Unorganised Sector and Role of NABARD and SIDBI

A1.1 The scheduled commercial banks and RRBs have been the primary source of credit to the small scale, micro and village industries sector. However, in order to supplement the credit flow to the small sector in a focused manner, Government of India created the National Bank for Agriculture and Rural Development (NABARD) in 1982 to cater primarily to the needs of the farm sector and rural development. Later in 1990 the Small Industries Development Bank of India (SIDBI) was also created for the non-farm sector.

National Bank for Agriculture and Rural Development (NABARD)

A1.2 The National Bank for Agriculture and Rural Development (NABARD) was set up in July, 1982 under an Act of Parliament by merging the Agriculture Credit Department and Rural Planning and Credit Cell of the Reserve Bank of India and the entire undertaking of Agriculture Refinance and Development Corporation (ARDC). NABARD is an apex development bank for supporting and promoting agriculture and rural development in the country. The specific objective of setting up of NABARD was for "promoting sustainable and equitable agriculture and rural development through effective credit support, related services, institution building and other innovative initiatives." In terms of the preamble to NABARD Act (1981), the institution has been mandated to facilitate credit flow for the promotion and development of agriculture, small scale industries, cottage and village industries, handicrafts and rural crafts. NABARD was also mandated to support all other allied economic activities in rural areas, promote integrated and sustainable rural development and secure prosperity of rural areas, as also matters connected there with and incidental there to. With a paid up capital of Rs.2000 crores (authorized capital Rs. 5000 crores) contributed by Government of India and the Reserve Bank of India, it operates through its Head Office in Mumbai, 25 regional offices situated in the state capitals, a sub-office in Port Blair and 281 district offices. While NABARD primarily addresses the needs of the farm sector, it also extends services to non-farm sector. In the non-farm sector the developmental initiative consists of rural entrepreneurship development, skill development, orientation meets, women empowerment, environmental promotion, setting up rural marketing outlets, strengthening of rural haats, capacity building of PLIs / NGOs, and special schemes of District Industries Projects and cluster development.

Sources of Funds for NABARD

A1.3 Apart from paid up capital of Rs. 2,000 crores (authorized capital of Rs. 5,000 crore), NABARD had access to approximately Rs. 15,000 crores at the time of inception, available with ARDC and other funds, which were merged to crate NABARD. It also received an annual grant ranging between Rs. 200 and 400 crores from the RBI till 1990-91. Over a period of time it has also developed access to market borrowing including from the international market . A break up of its sources of funds by the end of March 2007 is as in Table A1.1

Table A1.1: Sources of Funds of NABARD as on March 2007 (Rs. Crores)

Capital	2000
Reserve and surplus	7802
National Rural Credit (long term operation) Fund	13214
National Rural credit (stabilization) Fund	1533
Other funds	2007
RIDF deposits	20155
Deposits	82
Bonds and debentures	28892
Borrowings (GOI, RBI, SCBs, Foreign loan)	3171
Other liabilities	2364
Total	81220

Source: NABARD (2006-07)

A1.4 Thus, it had access to Rs. 81220 crores of funds by the end of 2006-07.

Table A.1.2: Advances by NABARD by the End of March 2007 (Rs. Crores)

Refinance	
Production and Marketing Credit	14758
Investment Credit (Medium and Long Term Project Loan)	32017
Liquidity Support	2492
Others	852
Direct Loan	
RIDF	20005
Other Loans	24
Total	**70148**

Source: NABARD (2006-07)

NABARD's Functioning vis-à-vis Non-farm Sector

A1.5 Data from NABARD's Annual Report 2006-07 reveals that out of the total refinance of Rs. 8795 crores, the refinance extended to the non-farm sector was of the order of Rs. 2265 crores or 25.8 per cent of the total. NABARD's refinancing of the non-farm sector has been steadily declining over the years, from 31.1 per cent in 2003-04, to 29.6 per cent in 2004-05, 26.5 per cent in 2005-06 and further to 25.8 per cent in 2006-07. The report further reveals that, of the total refinance to non-farm sector, Rs. 1088 crores was for housing alone. This leaves a sum of over Rs. 1177 crores which was spent on schemes such as margin money for artisans, consumption credit, loans to entrepreneurs for working capital and on purchase of second hand vehicles for road and transport operations. Under micro finance (SHG financing), refinance to the tune of Rs. 1292.86 crores was disbursed during the year 2006-07. In addition to the above, Rs. 13 crores on micro credit operations and Rs. 355 crores on SC/ST Action Plan were spent under SGSY etc. Thus after taking in to account the refinance to the non-farm sector, micro credit, under District Industries Project and direct assistance to the non-farm sector, the non-farm sector received about 25-26 per cent of the total operations of NABARD during the year. This calculation does not include loans under RIDF.

Table A.1.3 NABARD's Assistance through Development Schemes During 2006-07

I	**Farm Sector**	**(Rs. Crores)**
1.	Watershed Development	13.60
2	Tribal Development	21.16
3	Farm Innovation and Promotion Fund	0.99
4	Kutch Drought Project	1.23
5	Cattle Development Project	8.96 (cumulative)
6	On-going Projects (External)	15.86
II	**Non-Farm Sector**	
1.	NABARD-SDC Rural Innovation Fund	15.16
2	District Rural Industries Project	223.61 (Re-finance)*
3	Rural Haats	0.28
4	Rural Entrepreneurship	0.01
5	Cluster Development	0.05
6	Swarojagar Credit Card	0.12
7	Women Empowerment	0.25
8	Marketing and Other Initiatives	0.68
9	Rural Habitat Scheme	2.10
III	**Micro Credit**	
	Micro- Credit to SHG	1292.86 (Re-finance)
2.	Revolving Fund Assistance	1 .00
3	Capital/Equity Support	3 00
4.	Micro-finance Development and Equity Fund	11.18

* Ground level credit for RNFS stood at Rs. 2525.36 crores in 106 districts
Source: NABARD (2006-07)

A1.6 Data on developmental effort reveals that in 2006-07, NABARD spent about Rs. 18.59 crores on the non-farm sector covering activities like innovative financing, marketing, entrepreneurship development etc.

A1.7 From the above analysis, it is apparent that the unorganised sector in rural areas has been one of the components of NABARD's financing and attention through several schemes and funds. The funds that directly cater to the development needs of some sections of the unorganised sector (such as Tribal and Adivasi Development Fund, Soft Loan Assistance Fund, Micro Finance Development Fund etc.) have a comparatively small corpus of only Rs. 415 crores. NABARD has done excellent work in the micro finance sector of promoting SHG-Bank Linkage Programme and cluster interventions. On the whole, however, NABARD's credit interventions in favour of the unorganised sector in rural areas have had a limited impact on the sector and there exists a vast gap between availability of credit and its overall requirement.

Small Industries Development Bank of India (SIDBI)

A1.8 The Small Industries Development Bank of India was established in April 1990 by an Act of Parliament as the principal financial institution for the promotion, financing and development of the small scale industry sector and to coordinate the functions of other institutions engaged in similar activities. It has 4 zonal offices and 65 branches for the channeling of direct and indirect credit. SIDBI's authorized capital is Rs. 1000 crores and paid up capital is Rs. 450 crores. SIDBI is engaged in both refinance and direct credit. However, it does not have a full complement of reach and services such as a country-wide branch network, flexibility to offer working capital etc.. The broad features of SIDBI's financing activities and scope are as under:

- SIDBI's financial assistance to the small sector is channeled through the existing credit delivery system, which consists of state level institutions, rural and commercial banks and SIDBI's own branches.
- SIDBI provides refinance to and discounts bills of primary lending institutions (PLI).
- The assistance is available for setting up of new ventures, modernization, expansion, diversification, working capital and market promotion for small and medium enterprises.
- Venture capital assistance to the entrepreneurs for their innovative ventures if they have a sound management team, long term competitive advantage and potential for above average profitability leading to attractive return on investment.
- SIDBI Foundation for Micro Credit has been set up to provide financial assistance to the poor and to meet the emerging needs of the micro finance sector especially in rural areas.
- SIDBI's direct finance (project loan) is for relatively larger projects of the SME sector where minimum loan requirement is not less than Rs. 50 lakhs for setting up new units.

SIDBI's Sources of Funds

A1.9 Apart from the paid up capital of Rs. 450 crores, SIDBI has been depending primarily on the following sources of funding (Table A1.4) as could be seen from its operation in 2006-07.

Table A.1.4 SIDBI's Sources of Funds as on March 2007 (Rs. Crores)

Reserve Fund and Surplus	4691
National Equity Fund	144
Venture Capital Fund	178
Marketing Development Fund	58
Bonds and Debentures	6463
Deposits	1690
Borrowings	
Internal	755
External (Germany, Japan, Italy, World Bank)	2020

Source: SIDBI Annual Report, 2006-07.

Extent of Financing of Unorganised Sector by SIDBI

A1.10 Separate data on SIDBI's credit, both direct and indirect/refinance to micro and unorganised enterprises are not available. Further, SIDBI's direct finance is primarily for those units whose credit requirements are not less than Rs. 10 lakhs. Similarly, its Venture Capital Fund is meant for the small and medium enterprises. For meeting the venture capital / equity support to MFIs to enable them to increase their micro finance activities, SIDBI has set up a SIDBI Growth Fund of Rs. 50 crores. Going by the performance in 2006-07, the identified funds for the unorganised enterprises are as in Table A1.5.

Table A.1.5 SIDBI's Financing-2006-07

	Total	Micro Enterprises (Estimated) (Rs. Crores)
Refinance	5189	1482
Equity Assistance	29	29
Bill Financing	2263	-
Resource Support to SFCs, SIDCs etc.	548	-
Project Financing	1717	-
Micro Finance and Other Developmental	379	379
Total	**10225**	**1890**

Note: The calculations for refinancing assume that micro enterprises receive the same share of small enterprise credit (2 out of 7 per cent) as is the case with Scheduled Commercial Banks.
Source: SIDBI (2006-07).

A1.11 Thus, about 18 per cent of SIDBI's financial support could be attributed to micro and smaller segments of the unorganised enterprises.

Review of SIDBI's Functioning vis-à-vis Micro Enterprises Development

A1.12 SIDBI is not able to meet the financial needs of the enterprises in the non-farm unorganised sector. Its charter mentions the development of small scale industries as its main function with no separate mention of tiny or micro enterprises. Small scale industries as defined till October 2006 were those with investment in plant and machinery up to Rs. 1 crores. For later years, it is changed to units with investment in plant and machinery above Rs. 25 lakhs and up to Rs. 5 crores. Being a "for profit" (income tax paying) institution, it is natural that the institution has been paying attention for the upper end of the small enterprises and not the micro enterprises. After the enactment of MSMED Act, 2006, now its function stretches and covers even medium enterprises i.e. with investment in plant and machinery above Rs. 5 crores and up to Rs. 10 crores. Hence, the micro enterprises' chance to receive SIDBI's attention gets further diminished.

A1.13 SIDBI does not maintain even separate data on its financial assistance to micro enterprises.

A1.14 A review of the present functioning reveals that SIDBI is paying attention more to direct financing and less to refinancing. In 1990-91 direct financing was just 5 per cent of its operations and refinancing 95 per cent. In 2006-07, direct financing accounts for 51 per cent of its operations while refinancing came down to 49 per cent. It is also evident from the SIDBI's schemes that 90 per cent of direct finance is for the larger segment of the SSIs and also the medium enterprises. Thus, of the total, not more than 28 per cent of SIDBI's financing could be accruing to micro enterprises. Therefore, since the inception of SIDBI, the unorganised sector has hardly benefited from the creation of this institution.

A1.15 SIDBI has been operating funds as shown in Table A.1.6.

Table A1.6: List of SIDBI's Funds (Rs. Crores)

	Size	Utilisation	Remarks
National Equity Fund	144.54	34.41	Discontinued from 2007-08
Venture Capital Fund	178.35	39.17	Used by larger SSIs
SME Growth Fund	500.00	156.00	Used by medium and large SSIs
Marketing Development Fund	58.25	1.50	Meager utilisation
Portfolio Risk Fund	15.00	4.00	Government has decided to augment the fund
Mahila Udyan Nidhi	17.49	Nil	Zero utilisation
Mahila Vikas Nidhi	9.86	Nil	Zero utilisation
Technology Development and Modernisation Fund	No fund earmarked	Nil	Zero utilisation
Micro Credit Foundation Scheme		376.00	In the total micro credit of Rs. 18000 crores, this is insignificant

Source: ibid.

A1.16 Keeping the above in mind, Government of India announced a policy package for micro and small enterprises in February 2007, according to which, among other things, SIDBI has been mandated to scale up and strengthen credit operations for micro enterprises and cover 50 lakhs additional beneficiaries over the five years beginning 2006-07. Government will provide grant to SIDBI to augment its Portfolio Risk Fund. The Government's grant to SIDBI under the Portfolio Risk Fund has been only around Rs. 4 crores annually. Of the total advances made by way of micro credit of over Rs. 18000 cores by 2006-07, SIDBI's advance to MFIs from 1995 till date has been around Rs. 1000 crores, which is just about 5 per cent. Therefore, its contribution to the development of unorganised sector enterprises is almost inconsequential.

A1.17 So far as the grant based promotional and development activities are concerned, SIDBI has been engaged in activities like Rural Industries Programme wherein small units are being encouraged through entrepreneurship development programmes, strengthening SMEs through skill _cum-technology up-gradation, diagnostic studies for cluster development, trade fairs and exhibitions, and market development etc. From SIDBI's 2006-07 Annual Report it is clear that a sum of Rs. 379.02 crores was disbursed on micro finance and other promotional and development activities. Of this, assistance through micro finance alone was Rs. 376 crores. It means only a meager Rs. 3 crores was spent on promotion and development activities by SIDBI, thereby, further reflecting the inadequacy of attention to the unorganised sector. This is understandable since SIDBI does not get any grant from the Government of India for its grant-based promotional and developmental activities, which are carried out from its own resources.

Appendix - 2

A Review of Existing National Level Funds

A2.1 Currently, there are 32 major national level funds engaged in the task of economic development and /or relief work. A list of these funds is given below:

National Funds Relating to Economic Development

SIDBI

1 National Equity Fund.

2 Technology Development and Modernisation Fund.

3 Mahila Vikas Nidhi.

4 Mahila Udyam Nidhi.

5 SME Fund - 2004.

6 SME Growth Fund.

7 Credit Guarantee Fund.

NABARD

8 Rural Innovation Fund (RIF).

9 Micro Finance Development and Equity Fund.

10 Agriculture and Rural Enterprise Incubation Fund.

11 Tribal Development Fund.

12 Soft Loan Assistance Fund for Margin Money.

13 Watershed Development Fund.

14 KFW- NABARD Adivasi Development Fund.

15 Farm Innovation and Promotion Fund.

16 Foreign Currency Risk Fund.

17 National Rural Credit (LTO) Fund.

18 Cooperative Development Fund.

19 National Rural Credit (Stabilisation) Fund.

20 Research and Development Fund.

Implemented through NABARD

21 Venture Capital Fund for Dairy and Poultry Sectors.

22 Rural Infrastructure Development Fund.

Others

23 Rashtriya Mahila Kosh (Ministry of Women and Child Development).

24 Technology Upgradation Fund (Ministry of Textile)

25 Backward Regions Grant Fund.

26. Prarambhik Siksha Kosh.

27. Price Stabilisation Fund for Plantation Sector.

28. Sugar Development Fund.

29. USO Fund for Rural Household Telephone.

30. Special Purpose Vehicle Fund for Infrastructure Development.

31. India Development and Relief Fund.

32. World Wild Life Fund - India Chapter.

Being Set Up

33 National Fund for Strategic Agricultural Research.

34 National Employment Guarantee Fund.

35 Special Purpose Tea Fund.

36 Small Enterprises Development Fund (SIDBI).

37 Risk Capital Fund (SIDBI).

A2.2 While presenting the Union Budget for 2007-08, Finance Minister has proposed the creation of two funds of Rs. 500 crores each called: (a) Financial Inclusion Fund, and (b) Financial Inclusion Technology Fund both with NABARD. The first is for meeting the cost of developmental and promotional interventions for financial inclusion of the vulnerable groups and the second is to meet specifically the costs of technology up-gradation. The corpus of the Funds would be contributed by the Central Government, RBI and NABARD.

A2.3 Out of the existing 32 Funds, 13 are maintained by NABARD, 2 are implemented through NABARD and 7 by SIDBI. However, only 13 Funds relate to the SME sector, non- farm unorganised sector or Micro Enterprise sector. The Funds, which relate to the above mentioned sectors are listed at Sl. Nos 1 to 9 and 21 and 23 above. Fund no. 22, i.e. Rural Infrastructure

Development Fund indirectly relates to the unorganised sector since it promotes infrastructure such as roads and communication in rural areas. Among the funds being set up, the two listed at Nos. 36 and 37 are also related to the SME Sector.

A2.4 Before examining the specific purpose and the size of the proposed National Fund, it would be appropriate to evaluate the experience in the workings of the existing funds that have been set up for the development of the non-farm unorganised and small scale enterprises. Many of these funds are being managed by NABARD and SIDBI.

National Equity Fund (NEF) Scheme

A2.5 The NEF scheme was introduced in 1990 by the Ministry of Finance, Government of India to provide support to entrepreneurs to set up new projects in the tiny/small scale sector. Existing tiny, SSI units and service enterprises could undertake expansion, modernization, technology up-gradation and diversification. They also made provision for rehabilitation of potentially viable sick units irrespective of location. Assistance under NEF helps the small-scale units to strengthen their equity base. It helps the entrepreneurs to meet the gap in prescribed promoter's minimum contribution and/or in equity. The scheme is being operated by SIDBI since the year 2000 through SFCs/ twin function SIDCs, Scheduled Commercial Banks and select Urban Cooperative Banks.

NEF Scheme Parameters

A2.6 As per the existing guidelines under the scheme, the project cost should not exceed Rs. 50 lakhs in the case of new projects. In the case of existing units and service enterprises, the total outlay, including the proposed outlay on expansion/modernization should not exceed Rs. 50 lakhs. The entire project cost to be covered under NEF is required to be funded in the following manner:

Promoter's Contribution	-	10 per cent (minimum)
Equity (by way of soft loan)	-	25 per cent of the cost of project (subject to max. of Rs. 10 lakhs) per project
Term Loan	-	65 per cent
Debt Equity Ratio	-	1.857:1
Service Charges	-	5 per cent p.a. on soft loan
Condition	-	Institutions availing this scheme must obtain refinance from SIDBI

Performance under the Scheme

A2.7 The size of the fund is Rs. 152 crores. The overall sanctions and disbursements under the scheme stood at Rs. 377.19 crores and Rs. 272.44 crores respectively as on March 31, 2005. The operations under the scheme for the last 5 years are given in the Table A2.1

Table A2.1: Operations under National Equity Fund Scheme during the last 5 Years (Rs. crores)

Year	No. of Units	Sanction	Disbursement
2001-02	1073	19.55	16.22
2002-03	1648	53.17	35.18
2003-04	1238	54.35	41.18
2004-05	676	42.33	37.52
2005-06	807	42.1	38.47
2006-07*	NA	34.4	29.00

Note : *In-the year no disbursements made by SIDBI under all equity based schemes i.e National Equity Fund, Mahila Udyam Nidhi, and Self- Employment for Ex-servicemen.

Source:- SIDBI, 2006-07, Annual Report

A2.8 Outstanding under NEF scheme as on March 31, 2005, stood at Rs. 215.06 crores, against which, the overdue aggregated to Rs. 71.44 crores including overdue service charges of Rs. 3.98 crores. Among the defaulting PLIs are the following: Karnataka State Finance Corporation (Rs. 24.60 crores), Maharashtra State Financial Corporation (Rs. 9.53 crores), Punjab Financial Corporation (Rs. 3.18 crores), Orissa State Financial Corporation (Rs. 4.97 crores), Himachal Pradesh Financial Corporation (Rs. 2.54 crores), Kerala Finance Corporation (Rs. 5.32 crores), Bank of Maharshtra (Rs. 2.98 crores), Bank of India (Rs. 2.48 crores), United Western Bank (Rs. 1.80 crores), and Canara Bank (Rs. 1.81 crore). Together they accounted for 83 per cent of the total overdue.

A2.9 The overdue under NEF accounted for 33 per cent of the total outstanding under the scheme. The low recovery rate under the scheme, particularly the soft loan component, could be attributed to the following factors:

- The soft loan portion is funded by SIDBI / GOI and the risk there of is also borne by them. The PLIs function only as agents for channeling the soft loan assistance under NEF and therefore do not feel any compulsion to recover this amount.
- While the PLIs are required to ensure a proper monitoring of the projects for recovery of both

term loan and soft loan, proper awareness is lacking at the PLIs branches and also among the beneficiaries concerned that assistance under the soft loan scheme is to be repaid to SIDBI. Though SIDBI has conducted many awareness programmes to educate the PLIs in this aspect, yet their recovery efforts are found to be slack in the soft loan portion on account of the absence of charge on assets, etc. as compared to the term loans. The beneficiaries too tend to repay the high cost term loan installments and default in making payment of dues under the soft loan component.

- A return of 1 per cent, allowed to the PLIs on the service charge of 5 per cent for the soft loan, also does not offer much incentive to the PLIs.
- In the recent past, banks are not inclined, it is found, to cover eligible projects under the NEF as refinance on the term loan portion is compulsory under the scheme to avail of the soft loan portion. In view of their comfortable liquidity position, banks are not interested to avail the refinance against the term loan component from SIDBI. The aggregate under the soft loan component of NEF during the last 15 years stood at Rs. 87.85 crores compared to Rs. 190.83 crores availed by SFCs/ SIDCs during the same period.

Action taken by SIDBI

A2.10 Till date, GOI has contributed Rs. 143.74 crores on the total disbursement of Rs. 278.68 crores. Though, at present, the default ratio under the NEF scheme is about 33 per cent, this should be seen from the perspective that the assistance under NEF is being canalised to eligible entrepreneurs in the small scale sector who are prone to high failure rates.

A2.11 With a view to improving the recovery, PLIs have been advised to step up their recovery efforts under the scheme and share the recovered amount in respect of suit filed/ DRT / OTS cases on a pro-rata basis with SIDBI. Zonal offices/ branch offices of the Bank have also been advised to make concerted efforts to enhance the recovery of soft loan dues by undertaking visits to the beneficiary units and offices of the PLIs. These efforts have resulted in an overall recovery of Rs. 19.88 crores in FY 2005 as compared to Rs. 13.19 crores in FY 2004. Efforts to improve recovery would continue during FY 2006 as well, as the concerted efforts to collect dues under the soft loan component of NEF seem to be showing positive results. SIDBI has decided to discontinue this scheme with effect from 2007-08.

Technology Development and Modernisation Fund (TDMF)

A2.12 SIDBI has been implementing the TDMF Scheme since its inception in 1990. The Fund covers the existing SSI units, which opt for modernisation or technology up-gradation provided that the unit has been in operation for at least three years and is not in default to any institution or banks. The units graduating out of SSIs, i.e. medium and large industries, are also eligible for assistance under the scheme.

A2.13 The assistance is available for following purposes:

- For purchase of capital equipment, need-based civil works and acquisition of additional land and need-based additional margin money for working capital.
- Acquisitions of technical know how, designs, drawings and fashion forecast.
- Up-gradation of process technology and products with a thrust on quality improvement, comparable with acceptable domestic and international standards.
- Improvement in packaging.
- Cost of TQM and acquisition of ISO 9000 series certification.

A2.14 The minimum amount of assistance is Rs.10 lakhs per unit, which, including the initial moratorium, is repayable in 5 years.

A2.15 There is no Fund earmarked specially for these purposes and thus it forms part of the annual budget of SIDBI. Ministry of Finance stopped making contributions to the Fund. The scheme has lost its importance and has virtually been abandoned recently as is apparent from the utilisation data for last the 3 years. For the years 2003-04, 2004-05, 2005-06, the disbursement has been Rs.22.91 crores, Rs.27.95 crores and Rs.3.39 crores respectively. During the FY 2006-07, the disbursement under this Fund further declined to Rs. 0.77 crores.

A2.16 This scheme has lost it popularity due to the emergence of subsidy-based schemes such as:

- Credit Linked Capital Subsidy Scheme for small scale industries (15 per cent capital subsidy)
- Technology Up-gradation Fund for textiles sector (5 per cent interest subsidy or 20 per cent capital subsidy).

A2.17 The condition of a minimum loan of Rs. 10 lakhs, indicates that it is not meant for micro enterprises whose average investment in plant and machinery is less than Rs. 2 lakhs. Moreover, this scheme is not available for other service enterprises and segments or unorganised enterprises.

Mahila Vikas Nidhi

A2.18 Mahila Vikas Nidhi is SIDBI's fund specially designed for the economic development of women, particularly from the rural poor, providing them with avenues for training and employment opportunities. A judicious mix of loan and grant to accredited NGOs is extended to ensure that women are provided training and employment opportunities. The basic activity involves the setting up of training-cum-production centres by the assisted NGOs. Activities like vocational training, arrangements for supply of improved inputs, production and technology improvements are also covered under this scheme. Assistance is mainly in the form of a loan repayable in 5 years.

A2.19 The size of the Fund is Rs. 17.49 crores. Data on expenditure under this Fund for various years is not separately available. But it is not a significant Fund and the total may not be more than Rs. 30 crores, though the scheme has been in operation for the last 15 years. The scheme is virtually stagnant.

Mahila Udyam Nidhi

A2.20 SIDBI is also maintaining a Mahila Udyam Nidhi of Rs. 10 crores. Figures of expenditure under this Fund are also not available. Basically, the scheme aims at providing equity type support to women entrepreneurs for setting up new projects in the tiny/small scale sector and for rehabilitation of viable sick SSI units. The scheme operates through SFCs / twin function SIDCs / Scheduled Commercial Banks and Scheduled Urban Cooperative Banks. The cost of the project should not exceed Rs. 10 lakhs. The quantum of equity support is limited to 25 per cent of the project cost while not exceeding Rs. 2.5 lakhs per project. Service charge levied is 1 per cent p.a. on soft loans. Separate information on the progress and performance of the Fund is not available. But, like the Mahila Vikas Nidhi, its over all operation is low.

SIDBIs' SME Fund-2004

A2.21 The SME Fund was created in SIDBI in 2004 following the announcement made by the Government of India on January 09, 2004 regarding the desired creation of an SME Fund of Rs.10,000 crores to make available adequate and timely credit to SMEs. SIDBI was appointed as the Nodal Agency. The Fund became operational with effect from 1 April, 2004 and was to be utilised in two years i.e. FY 2005 and FY 2006. Under the Fund, assistance was extended to SMEs by SIDBI directly through its own resources and by way of refinance to primary lending institutions (PLIs). In order to provide loans at competitive rates, direct assistance under the Fund have been extended at an interest rate of 2 per cent below the Bank's PLR i.e. at 9.5 per cent. To SFCs, refinance was available in the interest rate band of 7.5 - 8 per cent. Based on the financials of the banks, their quality of assets and the Capital Adequacy Ratio, refinance was also available in the interest rate band of 6.25-7.25 per cent per annum. For the smooth operation of the Fund, Government of India had approved the limit of investment in plant and machinery above Rs 1 crores and up to Rs. 10 crores for defining a unit as a Medium Enterprise. It was done, since by that time, there was no official definition of 'SME' sector in India. As per SIDBI's Annual Report 2005-06, an assistance of Rs.2,825 crores was sanctioned and an amount of Rs.1833 crores was disbursed benefiting 3,908 enterprises during 2004-2005. During the second year of operation, i.e. FY, 2006, the assistance sanctioned and disbursed was Rs. 4157 crores and Rs. 3878 crores, respectively. Separate figures on the number of enterprises under the SSI and tiny categories, which received credit from the Fund are not available. In the two years, the total expenditure from this Fund was Rs.5715 crores. With the completion of the designated two years, this Fund is no longer in operation.

SIDBI's SME Growth Fund

A2.22 The Working Group set up by the Reserve Bank of India on Flow of Credit to SSI Sector (2004), headed by Dr. A.S.Ganguly, had recommended the setting up of a national level SME Fund for the export-oriented, high technology SMEs which could play a catalytic role in the advancement of the SME sector. To meet the need of risk capital, a fund for SMEs named the SME Growth Fund with a corpus of Rs. 500 crores was set up in October, 2004. The corpus of the Fund was reaffirmed by the Finance Minister in the Union Budget 2006 - 07. The Fund is intended to be utilised as investment in equity and equity-linked instruments in the growth sectors including life sciences, retailing, light engineering, food processing, information technology, infrastructure related to services like health care, logistics, and distribution , etc. The SME Growth Fund is an 8-year, close ended Venture Capital Fund. The Fund has received commitments for the entire amount of Rs.500 crores from various banks that include State Bank of India, Punjab National Bank, Bank of Baroda, Oriental Bank of Commerce, Bank of India, Union Bank of India, Corporation Bank and Central Bank of India, in addition to SIDBI's own commitment of Rs. 100 crores. The Fund has started its operations and approved of 3 investments aggregating Rs.26 crores and has disbursed a sum of Rs.5.70 crores to companies during 2004-05. During 2005-06, the Fund committed venture capital investments to the extent of Rs. 98.82 crores spread over 7 proposals. During the last two years, the total sanction under this Fund was Rs.124 crores and a total disbursement of Rs. 50 crores was given to 10 projects. This amounts to a per unit sanction of Rs. 12.4 crores covering the varied activities of Engineering, IT Communication Technology, Manufacturing, Pharmaceuticals, Retailing and Services. The disbursement under this Fund was very encouraging in FY 2006-07. In fact, SIDBI is maintaining two Venture Capital Funds. Besides, the above listed Fund it has the National Venture Capital Fund for Software and Information Technology (NFSIT). The total disbursement under the two funds during 2006-07 was Rs. 125.46 crores and this raised the total cumulative disbursements to Rs. 238.54 crores by the end of March, 2007. The individual disbursement under NFSIT has been Rs. 50.79 crores, thus, the total disbursement under SME Growth Fund has been Rs. 187.75 crores so far.

A2.23 The purpose of this Fund is undoubtedly innovative but it caters to small and medium enterprises only because the micro-enterprises do not offer viable exit options in the foreseeable future. One of the conditions for availing assistance is that the concern should have a sound management team, long-term competitive advantage, potential for above average profitability leading to attractive return on investment. Micro enterprises also need venture capital support in bio-technology, food processing etc. but with terms and conditions which are in tune with their scale of operation as they cannot afford a sound management team or a company type of organisation.

Credit Guarantee Fund

A2.24 The Credit Guarantee Fund for Small Industries was set up by the Government of India and SIDBI in August 2000 who have contributed funds in the ratio of 4:1 respectively. The corpus of the Fund is Rs. 1339 cores (March 2007). In the 2006-07 Union Budget, Finance Minister indicated that the size of the Fund would be raised to Rs. 2,500 crores in the next 5 years. The Fund is operated by the Credit Guarantee Fund Trust for Micro & Small Enterprises (CGTMSE) with headquarters in Mumbai. It helps the small scale and tiny units in accessing institutional credit for viable projects without arranging for collateral security and /or third party guarantee. CGTMSE extends guarantee cover for mitigating credit risk up to 75 per cent of the collateral free credits extended by the eligible Member Lending Institutions (60 MLIs by March, 2007 consisting of 28 public sector banks, 12 private sector banks, 17 RRBs, National Small Industries Corporation, North Eastern Development Finance Corporation Limited and SIDBI) subject to maximum credit of Rs. 25 lakhs (raised to Rs. 50 lakhs from February 27,2007). Consequent to the announcement of the SME Credit Policy Package in August 2005, several changes had been introduced to make the scheme attractive for tiny and rural enterprises. The guarantee fee was reduced from 2.5 per cent to 1.5 per cent. Though, initially the response to this scheme was not encouraging, gradually it is picking up. Through the Micro and Small Enterprise Package of February 2007, the collateral free loan limit has been raised to Rs. 50 lakhs and guarantee cover has been raised to 80 per cent for loans up to Rs. 5 lakhs and for women enterprises.

A2.25 Some of the salient features of the scheme are as under:

- Guarantee cover can be extended to any collateral free credit facility (both term loan and working capital) up to Rs. 25 lakhs provided by MLIs to new as well as existing manufacturing SSI units and small scale service and business enterprises, including Information Technology and Software industries.
- The lending institutions availing guarantee from the Trust have to pay a one-time guarantee fee of 1.5 per cent and service charges of 0.75 per cent per annum on the credit facility sanctioned.
- This scheme also provides life insurance cover of Rs. 2 lakhs, irrespective of the loan amount for the chief promoter of the unit covered under the CGTSI guarantee.
- There is a lock-in period of 24 months for preferring any claim by the MLIs. While 75 per cent of the guaranteed portion in default is paid

by the Trust immediately, the balance 25 per cent of the defaults or guaranteed cap amount is paid on conclusion of the recovery proceedings. The Trust has included this clause to obtain the banks' commitment to the scheme and to ensure efforts by the banks in recovering defaults. Table A2.2 gives the progress of the scheme: -

Table A2.2: Progress of Credit Guarantee Fund Scheme

Year	Number of Proposals Approved	Amount of Credit Guaranteed (Rs. Crores)	Average Loan (Rs. Lakhs)
2000 - 01	951	6.06	0.64
2001 - 02	2296	29.52	1.28
2002 - 03	4955	58.67	1.18
2003 - 04	6603	117.60	1.78
2004 - 05	9516	326.77	3.43
2005 - 06	12727	461.90	3.63
2006 - 07	27457	705.54	2.90
Table	**68062**	**1705.00**	**2.57**

Source - Ministry of MSME, SIDBI, 2006-07 Annual Reports.

A2.26 The average size of the loan at Rs. 2.6 lakhs indicates that the scheme has covered the smaller among the small enterprises. However, in the stakeholders meeting a view was expressed that under this scheme banks have included PMRY loans which are already collateral free as per the government instructions.

A2.27 In terms of the importance of enhancing the confidence of banks in small enterprises' lending, this Fund is very important. Various handicaps in the successful operation of this scheme need to be removed. Loans to khadi and village industries, coir and handicrafts have also been recently included within the purview of this Fund. However, it is suggested that the entire unorganised non-farm sector needs to be covered by CGTMSE.

NABARD-SDC Rural Innovation Fund (RIF)

A2.28 Effective from 1 October 2005, the Rural Promotion Corpus Fund (RPCF) and the Credit and Financial Services Fund (CFSF) were merged to form a new Fund, the NABARD - SDC Rural Innovation Fund (RIF), to support/promote all the existing activities covered under the RPCF and CFSF to promote livelihood opportunities, reduce drudgery as also other innovative, unconventional experiments in farm, non-farm and micro-finance sectors to create employment opportunities in rural areas. The RIF would be administered by a Steering Committee headed by the Chairman, NABARD with prominent economists and social activists as members. State-wise workshops were organised for sensitization of the NGOs, academic and research organisations. Consultations with National Innovation Foundation, Department of Science and Technology, Government of India etc. were held in 2006-07 on future collaboration. The scheme operated through this Fund was remodeled in February 2007. The main objective of the remodeled scheme is to promote linkages between banks and MFIs so that the poor can have better access to financial services by MFIs. The specific objective of the scheme is to provide capital/ equity support to MFIs so as to enable them to leverage capital/equity for accessing funds from banks, to promote financial services at an affordable cost to the poor and to enable MFIs to achieve sustainability in their credit operations over a period of 3-5 years. Current rate of interest charged on soft loan is 3.5 per cent. Equity support is restricted up to 10 per cent of the total paid up capital of the equity with a ceiling of Rs. 2 crores. During 2006-07, three agencies were sanctioned total capital support of Rs. 3 crores. During 2005-06, an amount of Rs. 19.11 crores and during 2006-07 an amount of Rs. 15.16 crores were disbursed taking the cumulative disbursement to Rs. 87.96 crores as on 31 March 2007.

NABARD'S Micro Finance Development and Equity Fund

A2.29 The Micro-Finance Development Fund (MFDF), set up in NABARD with a start up contribution of Rs.40 crores each from NABARD and RBI and Rs.20 crores each from 11 commercial banks identified by the RBI, became fully operational on 7 March 2003. The Fund is being utilised for scaling up various micro finance initiatives with a special focus on capacity building under the SHG - Bank Linkage Programme. The various components of the Funds' activities cover support to partner agencies, support to micro finance institutions, capacity building of partner institutions, special scaling up efforts, etc.

A2.30 During the year 2004-05, a sum of Rs.6.39 crores was utilised from the Fund. In 2004-05, GOI decided to re-designate the existing MFDF as the Micro Finance Development and Equity Fund. It has also been decided to enhance the corpus from Rs. 100 crores to Rs. 200 crores. The Fund would be managed by an Advisory Board consisting of representatives from the RBI, NABARD and commercial banks, i.e. the contributors to this Fund.

NABARD's Venture Capital Fund for Dairy and Poultry Sectors

A2.31 Ministry of Agriculture, GOI has announced a scheme for the creation of a Fund for providing venture capital for the dairy and poultry sectors in 2004-05. The scheme is being implemented in the Tenth Five Year Plan and involves a total revolving fund assistance of Rs. 25 crores to be made available to NGOs, public and private sector undertakings, cooperatives, etc. Under the dairy sector, eligible activities include the setting up of modern dairy farms, bringing about structural changes in the processing and marketing of pasteurised milk at the village level, and up-gradation of quality on a commercial scale. Under the poultry sector, assistance would be provided to boost the unorganised poultry sector in states where development of this sector is at an elementary stage. Further, the Fund will provide incentives and create infrastructure facilities for the export of poultry products by the organised sector in advanced states. It will help in establishing poultry and breeding farms with low input technology, and in the setting up of poultry feed plants, egg grading, packing and sorting facility for export and marketing of poultry products. Of the total project outlay, half the cost would be met as interest free loans from the Fund, 40 per cent from bank loans and the balance would be the entrepreneur's contribution. Commercial banks, RRBs and cooperative banks would implement the scheme. During 2006-07, loans were sanctioned to 1877 units, involving total financing of Rs. 32.34 crores including bank loans of Rs. 12.94 crores and interest free loans of Rs. 16.02 crores. As on 31st March 2007, total financing of Rs. 56 crores was made through the Fund which included Rs. 22.40 crores bank loans and Rs. 28 crores interest free loans sanctioned to 2940 units.

Rural Infrastructure Development Fund (RIDF)

A2.32 Government of India, in 1995, announced a scheme for the setting up of a Rural Infrastructure Development Fund (RIDF), to be sourced from the commercial banks to the extent of the shortfall in their agricultural lending. RIDF has continued from year to year with the corpus being announced annually during the budget. So far, twelve trenches have been completed and the thirteenth trench is underway during the current financial year (2007-08). Allocation has been increasing in each trench . The allocation in the IX trench was Rs. 5,500 crores. In the Xth and XIth it was Rs. 8,000 crores and in tranche XII it was Rs. 10,000 crores. Out of a total allocation of Rs. 60,000 crores to this Fund by 2006-07, the cumulative disbursement was Rs. 37560 crores by the end of March, 2007.

A2.33 The activities being financed out of the Fund include rural roads and bridges, micro, minor-medium-major irrigation, community irrigation wells, micro-hydel projects, drinking water, soil conservation, watershed development, drainage, flood protection, forest development, market yard, godowns, apna mandi, rural haats, other marketing infrastructure, cold storages, plantation and horticulture, fishing harbour, animal husbandry, modern abattoirs, etc. Though the Fund is primarily for the farm sector and, only to some extent, meant for non-farm enterprises, the infrastructure facilities created in rural areas are bound to help the non-farm activities, both directly or indirectly. The assistance provided under this Fund till 2006-07 is expected to facilitate the expansion of the production base in rural areas and in the creation of additional employment opportunities to the extent of 64.16 lakhs recurring jobs.

Rashtriya Mahila Kosh (RMK)

A2.34 The Rashtriya Mahila Kosh (National Credit Fund for Women) was set up in the year 1993 under the Ministry of Women and Child Development. It started with an initial corpus of Rs. 31 crores. The corpus has grown four times and now stands at Rs. 178 crores. The main objective of RMK is to facilitate credit support or micro credit support to the poor women for income generating production, skill development and housing activities in order to make them economically independent. The RMK canalises its support through NGOs, Women Development Corporations, Cooperative Societies, SHGs, etc. The main activities of the RMK consist of: (a) Loan promotion (b) Revolving Fund to MFIs with a satisfactory track record up to Rs. 5 crores, (c) Franchise scheme, (d) Gold Credit Pass Book - hassle free finance to medium and large NGOs - up to Rs. 5 crores, (e) Housing Loan Scheme up to Rs. 50,000 per beneficiary, (f) Family Loan Scheme, (g) Refinance to Women Urban Cooperative Banks. etc.

A2.35 The RMK has a unique successful credit delivery model, the 'RMK-NGO-SHG-beneficiary model' Margin money requirement for availing of a loan from the RMK is only 10 per cent. Loans are without collaterals. The interest rate charged is 8 per cent p.a.

(5 per cent p.a. in the case of franchise scheme) on a reducing balance from the borrowing agency. The borrowing organisations are required to repay the loan within 36 months in 11 quarterly installments with an initial grace period of 6 months for income generation activities.

A2.36 The RMK also undertakes and organises training programmes and awareness-cum-business development workshops. The RMK has succeeded in creating a niche position as an apex micro-credit institution for meeting the micro-credit requirements of poor women. It has succeeded in introducing an innovative customer friendly credit delivery mechanism and in developing entrepreneurial skills amongst the poor women.

Technology Up-gradation Fund

A2.37 The Technology Up-gradation Fund Scheme (TUFS), the 'flagship' scheme of the Ministry of Textiles was launched on 1 April, 1999 with the objective of making funds available for the domestic textile industry including power looms, and handlooms, for upgrading the technology of the existing units, and also to set up new units with state-of-the-art technology for enhancing their viability and competitiveness in the domestic and international markets. Initially, the scheme was in effect up to March 2004, but subsequently was extended up to March 2007. While presenting the Union Budget 2007-08, Finance Minister has proposed the extension of this fund till the end of the Eleventh Five Year Plan in 2012. During the Tenth Five Year Plan, an allocation of Rs. 1270 crores has been made to this Fund which provides for grants of 5 per cent interest subsidy on a bank loan or 20 per cent credit linked capital subsidy, whichever is favourable to the unit. SIDBI, which operates this scheme on behalf of Ministry of Textiles, disbursed a sum of Rs. 130.90 crores in 2006-07.

A2.38 The major beneficiaries of this fund have been the large textile mills engaged in ginning, spinning, weaving and garmenting. In the first 5 years since TUFS was introduced as much as Rs. 4,50,000 crores in investment has been made in this industry. The handloom and power loom sectors have not been able to utilise more than Rs. 25 crores from this fund. A large number of small units in the decentralised sector are not able to access TUFS due to the absence of books of accounts as they work on a job basis. Where as the minimum per unit requirement of loan in the handloom and power loom sectors is not more than Rs. 2-3 lakhs, the minimum loan limit under this scheme being operated by SIDBI is Rs. 10 lakhs. The poor capital base of the units, whose credit requirements for technology up-gradation falls below the prescribed norms of the banks, is a major constraint. Further, the banks do not consider existing small units viable enough.

Small Enterprises Development Fund (Proposed)

A2.39 The RBI in its new Priority Sector Lending Policy Guidelines, announced on 30th April 2007, has proposed the creation of a new fund called the Small Enterprises Development Fund (SEDF) to be implemented through SIDBI. Those foreign banks that have a shortfall in their lending to the stipulated priority sector target (32 per cent) and sub-targets (SSI sector 10 per cent) will be required to contribute to Small Enterprises Development Fund to be set up by SIDBI. Thus, the financing of SEDF will be on the pattern of RIDF, which receives Funds from commercial banks on their shortfall in the priority sector target (40 per cent) and agriculture sector target (18 per cent of NBC).

A2.40 The corpus of SEDF shall be decided upon by the RBI on a year-to-year basis. It is estimated that the shortfall in foreign banks' lending ranges between Rs.1000 crores and Rs.1500 crores annually. The tenure of the deposits shall be for a period of three years or as decided upon by the RBI from time to time. Fifty per cent of the corpus shall be contributed by foreign banks that have a shortfall in lending to the priority sector target of 32 per cent of ANBC (Adjusted Net Bank Credit, which is Net Bank Credit Plus investments made by banks in non-SLR bonds held in HTM category) or credit equivalent amount of Off Balance Sheet exposure, whichever is higher, on a pro-rata basis. The remaining 50 per cent of the corpus shall be contributed by the foreign banks that have an aggregate shortfall in lending to the SSI sector and the export sector to the extent of 10 per cent and 12 per cent respectively of ANBC or a credit equivalent amount of Off Balance sheet exposure, whichever is higher, on a pro rata basis. The concerned foreign banks will be called upon by SIDBI as and when required to contribute to SEDF, after giving one month's notice. The interest rates on foreign banks' contribution to SEDF shall be fixed by the RBI from time to time.

A2.41 RBI's Priority Sector Guidelines do not indicate the functions of this Fund. In the absence of this, it may, as in the case of the SME Fund 2004, be utilised by SIDBI to carry out its day-to-day functions of refinancing, bills discounting and for making direct loans to relatively large size projects catering to larger SSIs or even medium enterprises and it may not be utilized to undertake any special development work. Further, going by the investment size, it may not cover micro enterprises and also the non-farm unorganised enterprises.

Risk Capital Fund

A2.42 The policy package finalised by the Ministry of SSI has proposed the creation of this Fund under SIDBI for micro enterprises on a pilot basis in 2006 - 07. Details of the Fund is under finalization.

Equity Base of Various Funds

A2.43 An idea of the equity base of various Funds could be obtained from Table A2.3.

Table A2.3: Equity Base of Funds

FUNDS	Rs. crores
SIDBI	
National Equity Fund	144 (budgetary allocation) It is to be discontinued
Technology Development and Modernisation Fund	Discontinued
Mahila Vikas Nidhi	17 (budgetary allocation)-no progress
Mahila Udyam Nidhi	10 (budgetary allocation)-no progress
SME Fund - 2004	Discontinued
GSME Growth Fund	500 (meant for public and private companies)- good progress
Credit Guarantee Fund	1339 (to be raised to Rs.2500 crores in the next 5 years). It is a special purpose fund managed by a separate Trust of Ministry of MSME
NABARD	
Rural Innovation Fund	62
Micro Finance Development and Equity Fund	200
Venture Capital Fund for Dairy and Poultry	25
Rural Infrastructure Development Fund	Mainly for farm sector in rural areas. Budgetary allocation - Rs. 66,000 crores (up to 2006-07), Rs. 12,000 crores (Proposed for 2007-08)
Rashtriya Mahila Kosh	178
Technology Up-gradation Fund	No separate allocation for unorganised sector. Large units - main beneficiary.
Small Enterprise Development Fund (proposed by RBI)	No allocation indicated
Financial Inclusion Fund	500 (Proposed in 2007-08 Budget)-Not yet operational (September 2007)
Financial Inclusion Technology Fund	500 (Proposed in 2007-08 Budget))-Not yet operational (September 2007)

Source : Complied for various reports

A2.44 For most of the Funds, there is no earmarked provision/corpus. Most of these are being financed out of the budgetary allocations to the various organisations. Thus, they are, by and large, in the nature of on going schemes.

Review of the Existing Funds: A Summary

A2.45 A review of the working of all the existing and proposed Funds being operated by SIDBI reveals the following:

- They are losing importance e.g. National Equity Fund, Technology Development and Modernization Fund.
- Some Funds have ceased operations e.g. the SME Fund 2004 or have become inconsequential due to their extremely low size such as the Mahila Vikas Nidhi and Mahila Udyam Nidhi.
- A few Funds are not meant for micro enterprises, for example, the SME Growth Fund (Venture

Capital Fund) which is available to public or private companies with a minimum loan requirement of Rs. 10 lakhs,

- Some funds are in the nature of a special purpose Funds such as the Credit Guarantee Fund to guarantee collateral free loans.
- None of the Funds covers the entire gamut of the non-farm unorganised enterprises, which include besides manufacturing, services and transport activities like retail trade, construction, vendors, tourism, etc. Moreover, SIDBI's existing branch network is limited (56) and operates mostly in cities and big towns.

A2.46 Though the Funds in operation under NABARD cover non-farm unorganised enterprises such as the Rural Promotion Corpus Fund (now Rural Innovation Fund) these suffer from the low size (Rs. 62 crores). NABARD's Micro Finance and Equity Fund is meant for micro credit (not exceeding Rs.2500-3000 per family) but not micro enterprises credit. Venture Capital Fund for Poultry and Dairy are for specific purposes. It is well known that NABARD is primarily meant for the farm sector and its support to the non-farm sector is not among its main objectives. Moreover, its activities are confined to rural areas only. NABARD is basically a refinancing institution.

A2.47 Rashtriya Mahila Kosh is confined to micro credit (very small size of loan) to poor women. It does not provide credit to micro enterprises where the average credit requirement per unit is in the range of Rs. 50,000-Rs.1 lakh. The proposed Small Enterprises Development Fund under SIDBI is still at the consideration stage. It is not clear whether SIDBI will extend the assistance under this Fund to micro and other non-farm unorganised enterprises.

A2.48 The package for promotion of micro and small enterprises announced by the Ministry of MSME (February, 2007) suggested the creation of the Risk Capital Fund as a pilot scheme in 2006-07. Under this scheme it is proposed to support the MFIs in strengthening their equity for which Government of India will be contributing 12 per cent, SIDBI 6 per cent and the MFIs 2 per cent.

A2.49 The two Funds to be created for financial inclusion with NABARD may not serve the purpose since the focus of NABARD is on the farm sector in rural areas whereas unorganised enterprises are spread in all parts of the country covering both rural and urban areas and include both farm and non-farm sectors of the economy. Moreover, the National Fund must cover not only financial but also other promotional and developmental issues relating to unorganised enterprises.

Appendix - 3

Comparative Features of Different Forms of Organization

S.No.	Points Of Difference	Government Company Under Section 619	Statutory Body Under the Act of Parliament	Trust	Society
01	Purpose	Carry on business activities as per Objects in its Memorandum of Association.	Objects for which Parliament will pass the Act and for which Statutory Body will be established	For discharge of the charitable and/ or religious sentiments of the author or settler of the Trust, in a way that ensures public benefit.	Established for charitable literary, scientific purposes etc.
02	Enactment	Companies Act, 1956	Relevant Act of the Parliament	Governed by Indian Trust Act, 1882	Governed by Societies Registration Act, 1860.
03	Charter	Memorandum & Articles of Association	Relevant Act of the Parliament and regulation there of.	Trust Deed	- Memorandum of Association - Bye Laws
04	Formation	Formation is to be strictly in accordance with the provisions of the Companies Act, 1956.	Relevant Act will provide for the formation of the Statutory Body.	Formation procedure is simple and easy, only Trust Deed has to be registered.	Formation procedure is simple and easy, only MOA & Bye Laws has to be registered.
05	Management	Day to day management by the Board of Directors of the Company and exceptional matters requires approval of shareholders.	Board as will be established by the Act of Parliament will be the sole authority for management of affairs of the Statutory Body	Management of trust is easy and simple and not many restrictions have been imposed under the Act.	Management of Society is easy and simple and not many restrictions have been imposed under the Act.
06	Registration Fees	In accordance with the provisions of the Companies Act, 1956.	No registration fees will have to be paid.	No registration fee is required, only Trust Deed is required to be registered.	Registration fee for Registration of Society is Rs. 50/-.
07	Minimum no of members	Minimum 2 in the case of a private and 7 members in the case of a public company.	As per the requirements of constituting Act.	Three parties essential to form a trust.	These should be at least 7 members of any Governing Body.
08	Capital Contribution	At least 51 per cent of the capital has to be contributed by the Government.	Capital of the Body will depend on the relevant Act.	No capital requirements	No capital requirements
09	Issue of Bonds	It can issue bonds or debentures or other financial instruments	It can issue bonds, debentures or other financial instruments	Can not issue bonds or debentures	Can not issue bonds or debentures

Appendix - 3 Cont.......

S.No.	Points Of Difference	Government Company Under Section 619	Statutory Body Under the Act of Parliament	Trust	Society
10	Registration with RBI	Company with the financial objects can not commence business under Section 149 of Companies Act, 1956 unless the Company is registered with the RBI under Section 45I of the Reserve Bank of India Act, 1934.	No registration with RBI will be required for commencing financial business.	Since it cannot accept public deposit, no such registration is required.	Since it cannot accept public deposit, no such registration is required.
11	Amendment of Charter	Fast, Amendment of Memorandum of Association (for alteration of Main Objects or Articles of Association (for changing rules and regulations governing day to day affairs) is easy and can be done by a shareholders' resolution.	Slow, Objects or Rules or Regulation of Statutory Body can only be done if Parliament so resolves or in the manner as the Parliament may provide.	Fast, Trust deed cannot be amended without the specific order of Civil Court.	Fast, Memorandum of Association/ Bye laws can be amended in accordance with the provisions of the Societies Registration Act, 1860.
12	Objective	Profit	Social	Charitable	Charitable
13	Examples of Financial Institutions	1. The Industrial Credit and Investment Corporation of India Limited 2. Infrastructure Development Finance Company Limited. 3. All public sector banks.	1. Industrial Finance Corporation of India established under Section 3 of the Industrial Finance Corporation Act, 1948. 2. Industrial Development Bank of India, established under Section 3 of the Industrial Development Bank of India Act, 1964. 3. Unit Trust of India, established under Section 3 of the Unit Trust of India Act, 1963.4. SIDBINABARD		Rashtriya Mahila Kosh

Appendix - 4

An Action Plan to Improve the Flow of Institutional Credit

A4.1 The Guidelines for Priority Sector Lending by banks need to be revised. While the extant Priority Sector Lending Guidelines for the private and foreign banks may be maintained due to their limited branch network, the said guidelines for the nationalized banks may be revised as follows:

A4.2 The shortfall in the priority sector lending targets of nationalized banks for agriculture sector (18 per cent) may be made good by depositing equal amount with NABARD, which is the apex financial institution for agricultural sector. Similarly, the shortfall in priority sector lending to weaker sections (10 per cent), micro enterprises sector and other non-farm sector of nationalized, private and foreign banks (12 per cent) may be mad good by depositing equivalent money with SIDBI, which is the apex financial institution for financing, promotion and development of micro, small and medium enterprises in the country. The rate of interest on such deposits shall continue to be the same as prescribed by Reserve Bank of India.

A4.3 The banks need to be encouraged and incentivised to accelerate flow of credit to the unorganised sector by way of:

- Loans up to Rs. 5 lakhs to the unorganised sector may be treated as non-performing assets (NPA) only after 180 days of the non-payment from the due date.
- The Credit Guarantee Fund Trust for Micro & Small Enterprises (CGTMSE) may cover SHGs/ NGOs/MFIs/Co-operative Banks. Furthermore, in case, such loans up to Rs. 5 lakhs to the unorganised sector, covered under the Credit Guarantee Fund for Micro & Small Enterprises (CGFMSE), turn NPA, the CGTMSE may promptly transfer the amounts to the Member Lending Institution (MLI). In case of subsequent recovery, the respective MLI may first keep the balance 20 per cent of loan amount and return the surplus money to CGTMSE.
- RBI, in consultation with IBA, may decide a suitable mechanism to compensate the banks the increased transaction cost incurred by them due to annual incremental lending to the unorganised sector. The amount may be drawn from the proposed NAFUS.
- An Equity Risk Fund may be set up under the proposed National Fund with an initial corpus of Rs. 500 cores to provide equity support to unorganised sector for i) borrowing up to Rs.5 lakhs, ii) NGOs/SHGs/MFIs and iii) also rehabilitation of viable sick units in the unorganised sector. The exact mechanism of the Fund utilisation may be decided in consultation with SIDBI.
- All kinds of monetary subsidies provided by either Central Government or state governments may necessarily be treated as promoters' contribution, irrespective of the timing of the release of such subsidy amount by the respective governments. Such subsidies may be released within 1 month of the claim by the bank, subject to adherence to the prescribed norms. In case of delay beyond one month, the lending rate may be charged on the subsidy amount after one month and the complaint may be lodged with the Nodal Agency which will liaise with Government of India to get the money released directly from the Central Government and in the case of state governments, get the money released against the plan allocation to the state.
- In the case of delayed payments from state government depts./ PSUs/municipal and other local bodies to the micro enterprises in the unorganised sector, it is recommended that SIDBI/ SBI/PSBs may be identified as the nodal agencies for effecting these delayed payments of, at least 75 per cent of the total dues, to SMEs from the state government depts./PSUs/ municipal and other local bodies. In case the respective state agencies do not repay the same to SIDBI/SBI/PSBs within the prescribed time frame, the amount may be deducted directly from their Plan allocations and be paid to SIDBI/SBI/PSBs by the Central Government/Planning Commission. This would solve working capital problems of such micro enterprises, to some extent.
- Once a loan to the unorganised sector becomes NPA, the banks may initiate expeditious measures to restructure /rehabilitate, enter into OTS with

such accounts /units within 6 months. After such restructuring /rehabilitation /OTS, the account shall cease to become NPA. In the case of non-feasibility of the above, the measure of recovery may be resorted to, as the last step and the whole process shall be completed within one year of the asset turning into NPA. RBI may develop a suitable mechanism/ suggest suitable measures in this regard.

A4.4 The enactment of Micro Finance Bill may be expedited. The said Act would provide a legal status to SHGs/NGOs, thereby increasing the comfort level of the banks for lending to the sector.

A4.5 A capital and / or interest rate subsidy scheme may be introduced for the micro enterprises with investment up to Rs. 5 lakhs.

A4.6 Banking education /financial literacy/ credit counseling / banking facilitations. Due to the growing complexity of financial products and plethora of banking rules and regulations in the country, it has become imperative to impart financial education to the micro enterprises in the unorganised sector. This financial literacy may be given through credit counseling which would ultimately help the micro entrepreneur and thus reduce sickness attributable to information lacuna and asymmetry. Accordingly, it is proposed to set up a credit counseling and debt management agency for the unorganised sector.

A4.7 Timely disposal of credit. Timely availability of credit through faster sanction and disbursement may be strictly followed and monitored by the Reserve Bank of India.

A4.8 Other recommendations of the Commission are discussed in the Report on Financing of the Unorganised Sector.

Appendix - 5

Promotion and Development Expenditure

Table A5.1: Programme of Capacity Building and Hand-holding (CBH)

Year	No. of CBHs	No. of Enterprises in the 1st Year	Additional. Enterprises in Subsequent Years	Total Enterprises [Col(3) + Col(4)]	Employment (@4 per Unit)	Total Cost (Rs. Cr)	Incentive (Rs. Cr)	Total Cost (Rs. Cr)
(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)
2007-08	100	10000	-	10000	40000	10	2	12
2008-09	100	10000	5000	15000	60000	10	3	13
2009-10	100	10000	10000	20000	80000	10	4	14
2010-11	100	10000	15000	25000	100000	10	5	15
2011-12	100	10000	20000	30000	120000	10	6	16
Total	**500**	**50000**	**50000**	**100000**	**400000**	**50**	**20**	**70**

Source: Estimated

Notes: 1. Each CBH is to be conducted in one district and is assumed to enable setting up of 100 units in the 1st year and 50 units in the subsequent yrs.

2. Each CBH is expected to cost Rs. 10 lakh.

3. Incentive is given for setting up of units.

Table A5.2: Programmes of Entrepreneurship Development (PED)

Year	PEDs	Enterprises (@12 per EDP)	Employment (@4 per Unit)	Cost (Rs. Cr)	Incentive (Rs. Cr)	TotalCost (Rs. Cr)
2007-08	4000	48000	192000	30	9.6	39.6
2008-09	6000	72000	288000	45	14.4	59.4
2009-10	8000	96000	384000	60	19.2	79.2
2010-11	10000	120000	480000	75	24	99.0
2011-12	12000	144000	576000	90	28.8	118.8
Total	**40000**	**480000**	**1920000**	**300**	**96**	**396.0**

Source: Estimated

Note: 1. Each PED is assumed for 25-30 persons, with a success rate of 40-50 per cent.

2. Each PED is expected to cost Rs. 75,000/-

Table A5.3: Management Programmes (MP)

Year	No. of MPs	Employment (@4 per enterprise)	Total Cost (Rs. Cr)
2007-08	200	10000	3.34
2008-09	300	15000	5.01
2009-10	400	20000	6.68
2010-11	500	25000	8.35
2011-12	600	30000	10.02
Total	**2000**	**100000**	**33.4**

Source: Estimated

Table A5.4: Vocational Trainings (VT)

Year	No. of VTs	Employment	Total Cost (Rs. Cr)
2007-08	1000	30000	10
2008-09	2000	60000	20
2009-10	3000	90000	30
2010-11	4000	120000	40
2011-12	5000	150000	50
Total	**15000**	**450000**	**150**

Source: Estimated

Note: 1. Each VT is to be conducted for 30 persons

2. Success rate of getting employment is assumed to be 100 per cent

ABBREVIATIONS & ACRONYMS

Abbreviations & Acronyms

A&RI	Agro & Rural Industries
A/cs	Accounts
ADB	Asian Development Bank
AFI	Accredited Financial Institutions
Amt	Amount
ANBC	Adjusted Net Bank Credit
APRACA	Asia- Pacific Rural and Agricultural Credit Association
ARDC	Agriculture Refinance and Development Corporation
ASTRA	Application of Science and Technology for Rural Areas
ATM	Automatic Teller Machine
B - B	Business-to-Business
BDC	Business Development Bank of Canada
BIFR	Board for Industrial and Finance Reconstruction
BIMARU	Bihar, Madhya Pradesh, Rajasthan and UP
BR	Bank Rate
BRI-Unit Desa	Bank Rakyat Indonesia- Unit Desa
C.S.O	Central Statistical Organisation
CARE	Credit Analysis and Research Limited
CART	Credit Appraisal and Rating Tool
CBFSA	Canada Small Business Financing Act
CBH	Programme of Capacity Building and Hand-holding
CDC	Certified Development Company
CDP	Cluster Development Programme
CDR	Corporate Debt Restructuring
CFCF	Credit and Financial Services Fund
CGFTMSE	Credit Guarantee Fund Trust for Micro and Small Enterprises
CGTME	Credit Guarantee Fund Trust for Micro Enterprises
CGTMSE	Credit Guarantee Fund Trust for Micro and Small Enterprises
CGTSI	Credit Guarantee Fund Trust for Small Industries
CIBIL	Credit Information Bureau (India) Ltd.
CLCSS	Credit Linked Capital Subsidy Scheme
CMD	Chairman and Managing Director

CMP	Common Minimum Program
CRISIL	Credit Rating and Information Services of India Ltd.
CRR	Cash Reserve Ratio
CSO	Civil Society Organizations
D&B	Dun & Bradstreet India
DBP	Development Bank of the Philippines
DC	Development Commissioner
DCSSI	Development Commissioner for Small Scale Industries
DFI	Direct Financial Institutions
DIC	District Industries Centre
DICGC	Deposit Insurance and Credit Guarantee Corporation
DLCC	District Level Credit Committee
DRI	Differential Rate of Interest
DRT	Debt recovery Tribunal
ED	Executive Directors
EDP	Entrepreneurial Development Programme
ENISA	Empress National de Innovación, S.A
EPW	Economic and Political Weekly
EQL	Equal Opportunity Loan
EXPONET	Export Assistance Network
FCNR	Foreign Currency Non Resident Deposits
FFI	Formal Financial Institutions
FITCH	Credit Rating Agency
FSS F	armers' Service Societies
FTSSI	Federation of Tiny & Small Scale Industries of India
FWWB	Friends of Women's World Banking
GBC	Gross Bank Credit
GDP	Gross Domestic Product
GOI	Government of India
GUIDE	Guarantee Incubation for DTI Endorsed Enterprises
GVA	Gross Value Added
HTM	Held-to-Maturity
IBA	Indian Banks' Association
IBPC	Inter Bank Participation Certificates
ICMF	India Collective for Micro Finance

ICO-PYME	Official Credit Institute-SME
ICRA	Credit Rating Agency
ICSE	International Classification of Status in Employment
IDBI	Industrial Development Bank of India
IDS	Institute of Development Studies
IFC	Industrial Finance Corporation
IGIDR	Indira Gandhi Institute for Development and Research
IGLF	Industrial Guarantee and Loan Fund
IIFCL	India Infrastructure Financial Co. Ltd.
IISc	Indian Institute of Science
IIT	Indian Institute of Technology
ILO	International Labour Organisation
IOI	Incidence of Indebtedness
ISEC	Interest Subsidy Eligibility Certification
ISSP	Support Services Expansion Programme
IT	Information Technology
JLGs	Joint Liability Groups
KVIB	Khadi and Village Industries Board
KVIC	Khadi and Village Industries Commission
KVIs	Khadi and Village Industries
LAMPS	Large-sized Adivasi Multi Purpose Societies
MACS	Mutually Aided Cooperative Societies
MBS	mortgage backed securities
MFDF	Micro-Finance Development Fund
MFI	Micro Finance Institutions
MLI	Member Lending Institution
MNC	Multinational Corporation
MoF	Ministry of Finance
MP	Management Programmes
MSE	Micro and Small Enterprises Sector
MSME	Ministry of Small of Small and Medium Enterprises
MSMED	Micro, Small and Medium Enterprises Development
MSMEDO	Micro, Small and Medium Enterprises Development Office
MYRADA	Mysore Resettlement and Development Agency
NABARD	National Bank for Agriculture and Rural Development

NAFUS	National Fund for the Unorganised Sector
NBAN	National Business Angels Network
NBC	Net Bank Credit
NBFCs	Non-Banking Financial Companies
NCAER	National Council for Applied Economic Research
NCDC	National Co-operative Development Corporation
NCEUS	National Commission for Enterprises in the Unorganised Sector
NCF	National Commission on Farmers
NCMP	National Common Minimum Programme
NEDFi	North Eastern Development Finance Corporation (para 7.31)
NEF	National Equity Fund
NFSIT	National Venture Fund for Software and IT Industry
NFUEs	Non-Farm Unorganised Enterprises
NGO	Non-Governmental Organisation
NHB	National Housing Bank
NID	National Institute of Design
NIFT	National Institute of Fashion Technology
NPA	Non-Performing Assets
NPB	New Domestic Private Sector
NPC	National Productivity Council
NRNR	Non-Resident Non Repatriable
NSIC	National Small Industries Corporation
NSS/ NSSO	National Sample Survey (Organisation)
NT	Currency of Taiwan
OAE	Own Account Enterprises (without hired labour)
OBC	Other Backward Classes
OBE	Off-Balance Sheet Exposures
ONICRA	Credit rating Agency
OTS	On-time Settlement (to verify: refer to Appendix 2, Report 2, A2.11)
P&D	Promotion and Development Expenditure
P&M	Plant and Machinary
p.a.	Per Annum
PAC	Primary Agriculture Cooperatives
PCB	Primary Cooperative Banks
PED	Programmes of Entrepreneurship Development

PHBK Indonesia	Program Hubungan Bank dan KSM
PLI	Primary Lending Institutions
PLR	Prime Lending Rates
PMRY	Prime Minister's Rojgar Yojana
PRADAN	Professional Assistance for Development Action
PSBs	Public Sector Banks
PSLP	Priority Sector Lending Policy
R & D	Research & Development
RBI	Reserve Bank of India
REDP	Rural Entrepreneurship Development Programme
REGP	Rural Employment Generation Programme
RIDF	Rural Infrastructure Development Fund
RIF	Rural Innovation Fund
Rm	Malaysian Currency
RMK	Rashtriya Mahila Kosh
RNFS	Rural Non-Farm Sector
RPCF	Rural Promotion Corpus Fund
RRB	Regional Rural Banks
RUDSETI	Rural Development and Self-Employed Training Institute
SACP	Special Agricultural Credit Plans
SADHAN	Association of Community Development Finance Institutions
SANASA of Sri Lanka	Development Bank of Sri lanka
SBA	Small Business Administration
SBGFC	Small Business Guarantee and Finance Corporation
SBI	State Bank of India
SBIC	Small Business Investment Company
SC	Schedule Castes
SCBs	Scheduled Commercial Banks
SE	Small Enterprises
SEB	State Electricity Boards
SEDF	Small Enterprises Development Fund
SEFF	Small Enterprise Financing Facility
SEWA	Self Employment Women's Association
SEZ	Special Economic Zones
SFC	State Financial Corporation

SGSY	Swaranjaynati Gram Swarozgar Yojana
SHG	Self Help Group
SIDBI	Small Industries Development Bank of India
SIDC	State Industrial Development Corporations
SIDO	Small Industries Development Organisation
SISI	Small Industries Service Institute
SI-SPA	Systems Improvement Scheme under Special Project Agriculture
SJSRY	Urban Self Employment Programme under Swarna Jayanti Shahari Rozgar Yojana
SJSY	Swarnajayanti Gram Swarozgar Yojana
SLBC	State Level Bankers' Committee
SLR	Statutory Liquidity Ratio
SLRS	Scheme for Liberation and Rehabilitation of Scavengers
SMBA	Small and Medium Business Administration
SME	Small and Micro Enterprises
SMERA	SME Rating Agency of India Ltd.
SNA	System of National Accounts
SSI	Small Scale Industry
SSIDCs	State Small Industries Development Corporations
SSME	Special Sub-group of Micro Enterprises
SSSBE	Small Scale Service and Business Enterprises
SSSY	Swarnjayanti Shahari Swarozgar Yojana
ST	Scheduled Tribes
TCO	Technical Consultancy Organisations
TDMF	Technology Development and Modernisation Fund
TQM	Total Quality Management
TUS/ TUFS	Technology Up-gradation Fund Scheme
UCB	Urban Cooperative Banks
UKHTF	UK High Technology Fund
UN	United Nations
UNIDO	United Nations Industrial Development Organization
UNSC	United Nations Statistical Commission
UPA	United Progressive Alliance
US	United States
USEP	Urban Self-Employment Programme
USO	United Service Obligation

VAT	Value Added tax
VC	Venture Capital
Village Bank of FINCA	Micro finance Institution of Latin America
VT V	ocational Training
WWF	Working Women's Forum

ANNEXURES

Annexures

Annexure - 1

Terms of Reference of the Commission

The Government of India, constituted the National Commission for Enterprises in the Unorganised Sector (NCEUS) vide Ministry of Small Scale Industries Resolution No. 5(2)/2004-ICC dated 20th September, 2004, under the Chairmanship of Professor Arjun Sengupta. The Terms of Reference of the Commission are as follows:

i. Review the status of unorganised/informal sector in India including the nature of enterprises, their size, spread and scope, and magnitude of employment;

ii. Identify constraints faced by small enterprises with regard to freedom of carrying out the enterprise, access to raw materials, finance, skills, entrepreneurship development, infrastructure, technology and markets and suggest measures to provide institutional support and linkages to facilitate easy access to them;

iii. Suggest the legal and policy environment that should govern the informal/unorganised sector for growth, employment, exports and promotion;

iv. Examine the range of existing programmes that relate to employment generation in the informal/unorganised sector and suggest improvement for their redesign;

v. Identify innovative legal and financing instruments to promote the growth of the informal sector;

vi. Review the existing arrangements for estimating employment and unemployment in the informal sector, and examine why the rate of growth in employment has stagnated in the 1990s;

vii. Suggest elements of an employment strategy focussing on the informal sector;

viii. Review Indian labour laws, consistent with labour rights, and with the requirements of expanding growth of industry and services, particularly in the informal sector, and improving productivity and competitiveness; and

ix. Review the social security system available for labour in the informal sector, and make recommendations for expanding their coverage

Annexure - 2

Past and Present Composition of the Commission

The composition of the Commission is as follows:

Professor Arjun Sengupta Chairman, Centre for Development and Human Rights, New Delhi	**Chairman** [From 20.09.2004 to 01.07.2005 and from 17.11.2005 till date]
Professor K. Jayashankar Former Vice Chancellor, Kakatiya University, Warangal, Andhra Pradesh	**Full-time Member** [From 01.12.2004 to 9.03.2006]
Professor K. P. Kannan Fellow, Centre for Development Studies, Ulloor, Thiruvananthapuram 695011, Kerala	**Full-time Member** [From 01.11.2004 till date]
Professor Ravi S. Srivastava Professor, Centre for Studies in Regional Development, Jawaharlal Nehru University, New Delhi 110067	**Full-time Member** [From 01.05.2006 till date]
Shri B.N. Yugandhar Member, Planning Commission, New Delhi 110001	**Part-time Member** [From 05.11.2004 till date]
Shri Bibek Debroy, Director, Rajiv Gandhi Institute for Contemporary Studies, New Delhi 110001.	**Part-time Member** [From 27.10.2004 to 20.12.2005]
Professor T.S. Papola Director, Institute for Studies in Industrial Development, Vasant Kunj Institutional Area, New Delhi.110070	**Part-time Member** [From 06.04.2005 till date]
Shri K.K. Jaswal, IAS (Retd.)	**Member Secretary** [From 01.11.2004 to 18.02.2006]
Shri V.K. Malhotra, IAS (Retd.)	**Member Secretary** [From 01. 03.2006 till date]

Annexure - 3

Composition of the Advisory Board

1. **Professor Bhalchandra Mungekar,**
Member, Planning Commission,
Yojana Bhavan, New Delhi.

2. **Professor Amit Bhaduri,**
Council for Social Development,
53, Lodhi Estate, New Delhi - 110003.

3. **Swami Agnivesh,**
President, Bonded Labour Liberation Front,
13, South Avenue, New Delhi.

4. **Professor Sheila Bhalla,**
(Formerly Professsor of Economics,
Jawaharlal Nehru University, New Delhi)
Institute of Human Development,
Old IAMI Building (3rd Floor).
I.P.Estate, Mahatma Gandhi Marg,
New Delhi-110002.

5. **Professor Jean Dreze,**
Delhi School of Economics,
Department of Economics,
Delhi University, Delhi-110007.

6. **Professor Mahendra Dev,**
Director,
Centre for Economic and Social Studies,
Begumpet, Hyderabad.

7. **Ms. Madhu Kishwar,**
Editor, Manushi
C-1/3 Sangam Estate, 1, Underhill Road,
Civil Lines, Delhi-110054.

8. Ms. Mirai Chatterjee,
Self-Employed Women's Association (SEWA)
Opposite Victoria Garden, Bhadra,
Ahmedabad-380001.

9. **Shri Joginder Kumar**
President, Federation of Tiny &
Small Scale Industries of India (FTSSI),
General Metal Industries, B-189, Industrial Estate,
Ludhiana, Punjab.

10. **Shri Nachiket Mor,**
Executive Director, ICICI Bank Limited
ICICI Tower, Bandra Kurla Complex, Mumbai.

Annexure - 4

A-25022/ 26/2005-NCEUS

Government of India

National Commission for Enterprises in the Unorganised Sector

16th /19th Floor, Jawahar Vyapar Bhawan,

1 Tolstoy Marg, New Delhi 11001
Dated the 20TH April, 2006

ORDER

Subject: **Constitution of Task Force on Access to Finance, Raw Materials and Marketing relating to the Unorganised Sector.**

It has been decided that a Task Force on Access to Finance, Raw Materials, and Marketing relating to the Unorganised Sector be set up.

2. The composition of the Task Force shall be as follows:

1. Professor V.S.Vyas, Emeritus Professor, Institute of Development Studies, (IDS), Jaipur—Chairman
2. Mr. V,K.Malhotra, Member Secretary, National Commission for Enterprises in the Unorganised Sector, (NCEUS)-Member
2. Dr. Y.S. P. Thorat, Managing Director, National Bank for Agriculture and Rural Development, (NABARD) -Member
3. Shri N Balasubramaniam, MD, Small Industries Development Bank of India (SIDBI) -Member
4. Dr A. V. Sardesai, Ex. ED, Reserve Bank of India, (RBI), Pune - Member
5. Dr. S.L. Shetty, Economic and Political Weekly Research Foundation, (EPW) Mumbai -Member
6. Dr. Nachiket Mor, Advisory Board Member, National Commission for Enterprises in the Unorganised Sector, (NCEUS) - Member
7. Shri Kamal Taori, DG, National Productivity Council, (NPC)- Member
8. Shri Joginder Kumar, Advisory Board Member, National Commission for Enterprises in the Unorganised Sector, (NCEUS) -Member
9. Shri. C. Chandran, CEO, Khadi and Village Industries Commission, (KVIC) - Member
10. Representative from Textiles Ministry-Member
11. Ms. Achala, SADHAN – Member
12. Ms. Jayashree Vyas, MD Self Employed Women's Association (SEWA) Bank - Member
13. Shri Vipin Sharma, Program Director, CARE, Delhi—Member
14. Shri Mahesh Kumar, Director, National Commission for Enterprises in the Unorganised Sector, (NCEUS) - Convener

3 The Terms of Reference of the Task Force shall be as follows:

(i) Review of the existing arrangements for providing finance, raw material and marketing facilities to enterprises in the unorganised sector at the Central and State levels.

(ii) Review the policy environment and guidelines governing credit to the unorganised sector and suggest changes, if required.

(iii) Identify the constraints, and the declining trend, in enhancing access to finance, raw materials and marketing facilities for enterprises in the unorganised sector.

(iv) Review the innovative experiments, both emanating from public institutions as well as non-government organizations, for enhancing the access to finance, marketing and raw materials to enterprises in the unorganised sector.

(v) Suggest a strategy and measures to strengthen and enhance institutional support for accessing finance, raw materials and marketing facilities to enterprises in the unorganised sector.

(vi) Recommendations for the creation of a National Fund to provide technical, marketing and credit support to the unorganised enterprises.

Consider any matter related with, or incidental to, the above Terms of Reference.

4. Chairman will have the power to decide on field visits, commissioning of papers and/or co-opt experts to facilitate the writing of the report.

5. The Task Force shall submit its report within 6 months of its constitution.

6. The expenses towards TA/DA of the official members of the Task Force shall be met by the Government Departments/Institutions to which they belong. The TA/DA of non-official Members and invitees to meetings will be paid by NCEUS as admissible to Grade I Officers of the Government of India.

Sd/-
(SURESH KUMAR)
Under Secretary (NCEUS)

To

1. Prof. V.S. Vyas, Institute of Development Studies, 8-B, Jhalna Institutional Area, Jaipur-302004. Fax: 0141-2705348

Tel: Res. (0141) 2705601; Fax: (0141) 2709938;

Email: vsvyas@idsj.org vsvyas@datainfosys.net v

2. Dr K P Kannan, Member, National Commission for Enterprises in the Unorganised Sector, (NCEUS).

3. Dr. Y.S. P. Thorat, Managing Director, Managing Director, National Bank for Agriculture and Rural Development, (NABARD), Plot C-24, Bandra-Kurla Complex P.B. No. 8121, Bandra (E) Mumbai-400051 Fax: 022-26530114. nabmd@boom5.vsnl.net.in

4. Shri. N. Balasubramanian, Chairman & Managing Director, Small Industries Development Bank of India (SIDBI), SIDBI Tower, 15, Ashok Marg, Lucknow- 226001. Fax: 0522-2288494 bala@sidbi.com

5. Shri. A.V. Sardesai, C-16, Kumar Elixir, Banner Road, PUNE-411 045. e-mail: asarex1@yahoo.com

6. Dr.S.L. Shetty, Director, Economic and Political Weekly Research Foundation, (EPW), C-212, Akurli Industrial Estate, Kandivali (East), Mumbai-400 101. Fax: 022-28873038 epwf@vsnl.com

7. Shri Nachiket Mor, Advisory Board Member, National Commission for Enterprises in the Unorganised Sector, (NCEUS). - Exe. Director, ICICI Bank Ltd., ICICI Tower, Bandra Kurla Complex, Mumbai-400 051 Fax: 022-2653 1218.

8. Shri Kamal Taori, Director General, National Productivity Council, 5&6, Institutional area, Lodhi Road, New Delhi-110003. Fax:24615002,

9. Shri Joginder Kumar, President, Federation of Tiny & Small Industries of India, Mg. Partner, General Metal Industries, B-189, Industrial estate, LUDHIANA-141010. Tel: 2670800 (O) Mobile 3117002 Fax: 3945557/ 2539800.

10. Shri. C. Chandran, IAS, Chief Executive Officer and Commissioner, Khadi & Village Industries Commission, Irla Road, Vile Parle (W), Mumbai-400056. Fax 022-2671 8289

11. The Secretary, Ministry of Textiles, Government of India, New Delhi with the request to nominate a senior officer as representative for the Task force.

12. Ms. Achala, SADAN, 12&13, 2nd Floor, MPTCD Building, Special Institutional Area, Shaheed Jeet Sing Marg, New Delhi-110067, Fax: 26518276. emai;: policyteam@sa_dhan.org

13. Ms. Jayashree Vyas, MD, Self Employed Women's Association (SEWA) Bank, Ellis Bridge, Ahmedabad-380 006. Fax: 079-25506446

14. Sh. Vipin Sharma, Director, CARE India, 27, Hauz Khas Village, New Delhi-110016. Fax: 26564081/ 26564048. cbox@careindia.org

15. Mahesh Kumar, Director, National Commission for Enterprises in the Unorganised Sector, (NCEUS).

Copy to: PPS to Chairman, NCEUS.
Member (K)
Member Secretary
Director (Admn)

Annexure - 5

Prof. Vijay Shankar Vyas
Professor Emeritus, Institute of Development Studies

396, Vasundhara Extension, Gopalpura By-Pass, Tonk Road, Jaipur 302018, India
Ph: 91-141-2705601 • Fx: 91-141-2709938 • Em: vsvyas@idsj.org, vsvyas@mac.com

April 13, 2007
~~March 24, 2007~~

Letter of transmittal

Dear Dr. Sengupta,

I have pleasure in forwarding herewith Part I of the Report of Task Force on Credit, Marketing and Raw Material Supplies for Enterprises in Unorganised Sector set up by the National Commission on Enterprises in Unorganized Sector. This report contains our views and recommendations on credit related issues which we consider to be of paramount importance for enhancing income of and output from the unorganised sector.

In preparing this report we have benefited from the consultations we had among ourselves, but more importantly with the other stakeholders at different places in the country. Thus, report represents outcome of discussions with a large section of concerned publics.

In preparing this report all my colleagues on the Task Force, especially the non-officials members, made significant contribution. I would particularly like to mention the role played by Shri Joginder Kumar by attending practically all the meetings with stakeholders obviously at the cost of his time and convenience. Dr. S.L. Shetty, another distinguished member of the Task Force, prepared a very useful document as background paper for our consideration.

Among the staff of the National Commission we are particularly grateful to Dr. C.S. Prasad for preparing the draft of the report for our consideration. In doing so he brought to bear his in- depth knowledge and insights into the issues and problems we were engaged with. We will also like to acknowledge with thanks help provided by Shri Mahesh Kumar, convenor of the Task Force, in looking after all logistic arrangements in an efficient way. Above all, I have to thank you, Member-Secretary and the members of the National Commission for extremely valuable advice and guidance provided to us from time to time.

I do hope that the report will be of help to the Commission in fulfilling its mandate.

With kind regards,

Yours sincerely,

V. S. Vyas
[V.S. Vyas]

Dr. Arjun Sengupta
Chairman,
Commission For Enterprises in the Unorganised Sector
16th Floor. Jawahar Vyapar Bhawan,
1, Tolstoy Marg, New Delhi

Annexure - 6

Regional Consultations: Participants

Meeting of the Task Force on Access to Credit, Raw material and marketing held at SISI, Kanpur on 09.11.2006

SI.No.	Name & Address	Organisation
1.	Himani Shukla	Proprietor
2.	Rakesh Kr. Pandey	Micro Enterprise Federation
3.	D.H.BHUTA	Gramin Bank
4.	V.G.Pandit.	Gramin Bank
5.	Ram Krishna	Govt. of UP
6.	R.S.Verma	PNB
7.	T Das	KVIC
8.	Dr. M.T.Hamid	KVIB, Lucknow.
9.	Deep Mishra	Entrepreneur
10.	Jai Hemrjan	Entrepreneur
11.	Chandra Prakash Aggrwal	Entrepreneur
12.	Mickey Manchanda	State govt. UP
13.	Mauof Banka	ME Association
14.	Satish Gupta	Industry Association
15.	Ashish Manego	UPSIDC, Kanpur
16.	V.K .Malhotra	NCEUS
17.	Dr.C.S Prasad	NCEUS
18.	Joginder Kumar	NCEUS
19.	A.N. Singh	Govt. of UP
20.	U.C. Shukla	SISI
21.	A.R.Khan,	RBI
22.	S.K. Katiyar	Allahabad Bank
23.	V.K.Verma ,	Bank of Baroda
24.	Z.A.Khan	Bank of Baroda
25.	Praval Sinha	NABARD
26.	Toolika Pankaj	NABARD
27.	D.S. Deshpande	SIDBI
28.	R.Pandey	SBI
29.	SureshChandra	Indian Overseas Bank
30.	Joginder Paul	Indian Overseas Bank
31.	H.C.B. Sinha	Indian Overseas Bank
32.	R Vishwakarma	UCO Bank
33.	V.G.Choudharyr	UP Financial Corporation
34.	R.C.Grover	Bank of Baroda
35.	M. Venky Ipe	Shramik Bharti, NGO

SI.No.	Name & Address	Organisation
36.	A.K. Sharma	Credit Guarantee Corpn.
37.	Alok Diwan	Financial Reporter
38.	Naveen Sharma	Entrepreneur
39.	Tridip Soman	Entrepreneur
40.	P.N Singh	Central Bank of India
41.	Mrs. Annpurna Yadav	Entrepreneur
42.	Ladli Prasad	Laghu Udyog Bharti
43.	Amod Bajpai	SSI Association
44.	Tarun Chhetrapal	SMW Association
45.	G.S Mishra	Entrepreneur
46.	Paritosh Kant Manglik	Laghu Udyog Bharti
47.	Man Mohan Rajpal	ME Association
48.	Ajay Gupta	Industry Association
49.	S.K. Misra	Entrepreneur
50.	PS Bajpai	SISI
51.	H.P. Jaiswal	SISI
52.	Babal Lal Verma	SISI
53.	Gorakh Prasad	SISI
54.	M.S. Naqvi	Entrepreneur
55.	F.CS.Rahman	Entrepreneur
56.	Bijay Kumar Singh	Entrepreneur

Meeting of the Task Force on Access to Credit, Raw material and marketing held at SISI, Delhi on 13.11.2006

Sl. No.	Name (Mr./Mrs.)	Organisation
1	Suresh Yadav	SISI
2	V K Malhotra	NCEUS
3	Joginder Kumar	NCEUS
4	C S Prasad	NCEUS
5	M S Achala	Member Task Force
6	Mahesh Kumar	NCEUS
7	A K Vyas	SBI
8	R S Verma	PNB
9	Ravi Shanker	O/o Commissioner of Industries
10	A D Chowdhury	KVIC
11	U K Diwan	Delhi Financial Corporation
12	Garima Sharma	SHG Coordinator
13	A N Singh	NABARD
14	V N Sastry	FISME
15	General Manager	Central Bank of India

Sl. No.	Name (Mr./Mrs.)	Organisation
16	Chief Manager	Central Bank of India
17	S Chandrasekharan	Indian Overseas Bank
18	Bharat Gupta	Laghu udyog Bharti
19	Sudarshan Sareen	All India Confederation of Small & Micro Industries Association
20	Chandra shekhar Goel	FISME
21	G S Bhatia	SISI
22	Bishan Lal	SISI
23	Ranjit Bhattacharjee	SISI
24	Kamal Singh	SISI
25	G S Nangia	SISI
26	T N Sharma	Gramodyog Vikas Samiti
27	V K Malhotra	SISI
28	Gordhan Dass	SISI
29	Anil Kumar	UCO Bank
30	Kartar Chand Indoria	Deepshikha International
31	R K Das	SIDBI
32	Arvind Jain	Oriental Bank of Commerce
33	D R Sachdeva	Oriental Bank of Commerce
34	V L Tosharda	PNB
35	R C Nirmal	PNB
36	Kavindra Kumar	Liftwell Engineers
37	V A Kamble	SISI
38	Rajesh Kumar	State Bank of Hyderabad
39	Lalit Maurya	NABARD
40	Darshan Singh	NABARD
41	A K Bhatnagar	Delhi SC /ST /OBC /MND / HND Fin. & Devp. Corpn.
42	R P Sharma	Central Bank
43	Paramjeet Singh	NSIC
44	Harpal Singh	SISI
45	K C Bakshi	SISI
46	R P Singh	SISI
47	A K Vohra	SISI
48	V K Gupta	SISI
49	Lajwanti Chugh	SISI
50	C P Singh	SISI
51	C V Saraf	SISI
52	Praveen Mahto	DC(MSME)
53	P K Mukherjee	DC(MSME)
54	Laxmi Maheshwari	KVIC
55	Ashwani Gupta	KVIC

Sl. No.	Name (Mr./Mrs.)	Organisation
56	Bhagwan Dass	All India Confederation of Small and Micro Industries Association
57	Shyam Lal	Factory owner
58	S K Kapoor	SISI
59	S L Bagla	Bagla & Co.
60	Shashi Singh	CWEI
61	Chetan Dass	CWEI
62	Vikas Sakhija	KRIST Engineering

Meeting of the Task Force on Access to Credit, Raw material and marketing held at NIBM, Pune on 18.11.2006

Sl. No.	Name (Mr./Mrs.)	Organisation
1	Jagesh Sondule	Ujjawala Khadi & Gramodyog
2	Randolph Rowe	SIDBI
3	Nishikant Deshpande	SIDBI
4	Rajaram Gurav	Pune DCC Bank Ltd.
5	N Krishnamurthy	IBA
6	Mrs. Prabhuta Vyas	IBA
7	Mrs. Mangala Patil	Bank of Maharashtra
8	P T Gaade	Bank of Maharashtra
9	Dr. S B Gokhale	BAIF
10	Veena Chature	BAIF
11	Dr. S B Khadilkar	BAIF
12	Ratna Ganapathy	Gramin Mahila Vikas Mandal
13	R N Sharma	Central Bank of India
14	M K Patnekar	Canara Bank
15	T R Kamceujia	Bank of India
16	C B Gore	Bank of India
17	M B Joshi	PNB
18	R Hari Kumar	Bank of Maharashtra
19	Jigisha Thakar	NIBM
20	Shilpa Pasad	NIBM
21	R N More	DIC
22	Dr. Abdul Salam	HELPO Foundation
23	K S Bhasi	HELPO Foundation
24	Susheel Kumar	Dena Bank
25	Sai Prithvi Nath	Marathwada Gramin Bank
26	N Srinivasan	NABARD
27	H R Khan	College of Agricultural Banking, RBI
28	R N Dash	College of Agricultural Banking, RBI

Sl. No.	Name (Mr./Mrs.)	Organisation
29	P Praful Josh	NABARD
30	Arvin K Agrawal	SBI
31	Ratnesh	Credit Guarantee Fund Trust for Small Industries
32	Prof. Atul Bhatt	NIBM
33	Prof. P Subbarao	NIBM
34	Dr D P Khankhoje	NIBM
35	Dr. Gopal S Maadoo	Help Foundation
36	Ramesh Kulkarni	Omega Software Services, USA

Meeting of the Task Force on Access to Credit, Raw material and marketing held at Image Hall, R.A. Puram, Chennai on 25.11.2006

Sl. No.	Name(Shri/Smt/Mrs)	Organisation
1	L. Bhuvaneswari	NABARD
2	P. Muralidharan	SISI
3	M. Sankar	RBI
4	G. Namasivayam	SISI
5	B.V. Ramana	SISI
6	D. Zacharias	Indian Overseas Bank
7	D. Balasubramanian	Pallavan Grama Bank
8	S. Viswanathan	Indian Bank
9	S.K. Kaushal	Indian Bank
10	K.A. Umasankar	KVIC
11	TM Pandian	KVIC
12	Dr. L. Ravindran	FEDHHI
13	N. Bhaskaran	TANSIDC
14	Kalyani Kathiresan	Annai Egai Magalir Membattu Sangam
15	A. Savitha	-do-
16	K. Muthuswamy	SIDCO
17	Somohanesan	TANSIDCO
18	V. Umashankar	-do-
19	V. Venkatesan	-do-
20	H. Sundaresan	-do-
21	R.P. Pillai	Krysalis consultancy (P) Ltd.
22	E. Bhaskaran	Department of Industry & CommerceDIC, GOTN
23	K. Vivekanandan	Department of Industry& com;.
24	N. Elangovan	O/o. Commissioner & Industries and Commerce
25	N. Varadharajan	SISI
26	Paneerselvam. R.	SISI
27	M.S.S. Ravi	Directorate of Industries & Commerce
28	Madhavi Sharma	RBI

Sl. No.	Name(Shri/Smt/Mrs)	Organisation
29	A.R. Muralidharan	SIDBI
30	Arun P. Deo	NABARD
31	Lakshmi Narayanan	NABARD
32	M.S. Prakash	Indian Overseas Bank
33	Krishnamurthy Kota	Indian Bank
34	Vijayam Satish Kumar	KVIC
35	M. Narayanan	Madura Micro Finance Ltd.
36	K. Gurunathan	Tamil Nadu State Apex Co-op. Bank
37	V. Sukumar	Tharsan Industries Proprietor
38	Amman K. Karunanethi	Amma Industry
39	Bhavani. R.V.	M.S. Swaminathan Research Foundation
40	R. Sumathi	DHAN Foundation
41	Ms. Rameswari	WWF (India)
42	Ms. Nisha Moses	-do-
43	A.S. Kannan	Tact
44	Deramakrishanan	IFRGSTE & NACOSI
45	V.S. Narasimhan	SIMA
46	K. Gopalakrishanan	IEMA
47	A. Soumya Velayudhan	TANSTIA
48	C. Alagirismy	SISI
49	S. Subburaj	SISI
50	V. Arulnathan	NSIC
51	R. Rajaram	NSIC
52	Joginder Kumar	NCEUS
53	C.S. Prasad	NCEUS
54	Shivgnanam	SISI

Meeting of the Task Force on Access to Credit, Raw material and marketing held at SISI, Guwahati on 12.12.2006

Sl. No.	Name(Shri/Smt/Mrs)	Organisation
1	J.L. Gaudhari	KVIC
2	S.N.D. Bharati	RBI
3	M. Krupanandam	RBI
4	M. Raghunath	NABARD
5	T. Sonowal	Indian Overseas Bank
6	B. Datta	SBI
7	Indukalpa Nath	Rural Women Upliftment Association of Assam
8	G. Saikia	The Assam co-operative Apex Bank Ltd.
9	Biren Hazarika	District Industries & Commerce Centre
10	Rajendra Sormnh	Directorate of Industry & Commerce
11	Premnath Sarma	DICC

Sl. No.	Name(Shri/Smt/Mrs)	Organisation
12	NB Narjaree	SIDBI
13	N.T. Naidu	SSI
14	B.L. Agarwala	AASSIA
15	Atul Sarma	NCEUS
16	Joginder Kumar	NCEUS
17	K. Ahmed	IIE
18	M. Barghain	SISI
19	K. Bhowmik	Assam Gramin Vikas Bank
20	S.R. Pagars	SISI
21	H. Barman	SISI
22	P. Haldar	SISI
23	L.K. Lahkar	SISI
24	PC Das	SISI
25	S.S. Bama	SISI
26	A.K. Baruah	AASSIA
27	Lemli Loyi	NEDFI
28	C.S. Prasad	NCEUS
29	S. Divia	DD News
30	Nayan J Bhuyan	ASOMIYAPRATIPIN
31	P.K. Divia	LDM, Kamrup
32	R.L. Dhanal	MD Apex Bank
33	P. Sarma	View CEE, IIE

Meeting of the Task Force on Access to Credit, Raw material and marketing held at SISI, Kolkata on 12.01.2007

SI.No.	Name ,Designation	Organization
1.	K.S.Singhwan	SIDBI
2.	S. Daschaudhuri	Govt. of West Bengal
3.	B.L.Baheti	Micro Enterprise Federation
4.	R.D.Yadav	Gramin Bank, Bankura
5.	B.Mitra	NSIC
6.	K.K Sharma	NSIC
7.	Dipak Sanker	SME Association
8.	Protima Roy	SME Association
9.	Dr.G.C Baidy	Entrepreneur
10.	Damyanti Das	Entrepreneur
11.	Biswanath Haldar	SBI
12.	D.B. Dutta	State Government
13.	D Chakravorty	SISI
14.	S. Chakrobanty	SISI
15.	S V B Banerjee	SIDBI
16.	Saileshwar Panda	SME Association

SI.No.	Name ,Designation	Organization
17.	S.K Gupta	State Government
18.	L.N.Rautray	Gramin Bank Howrah
19.	K.K Sarkar	Micro enterprise Association
20.	B K Bakshi	Micro enterprise Association
21.	S.K. Patra	Allahabad Bank
22.	L.K.Pingle	NABARD
23.	B. Naik	NABARD
24.	S.Bandyopadhyay	State Govt.
25.	S.K. Patra	State Govt.
26.	S.K Dutt	KVIC
27.	D.M. Ghosh	KVIC.
28.	Alok Roy	SISI
29.	Jerab Malla	Entrepreneur
30.	J Biswal	RBI
31.	S Saha	Entrepreneur
32.	R. Maiti	State Cooperative Bank
33.	SANJAY Dalmia	MSE Association, Jharkhand
34.	G C Baisakh	State govt.
35.	Rinkoo Bandhpadhyay	SISI
36.	Sunita Das	KVIC
37.	Bipasha Biswas	KVI Organisation
38.	Ashoke kumar	KVI Association
39.	A. Karim	State govt.
40.	Kulidip Maity	MFI
41.	Chandra Shekhar Ghosh	MFI
42.	Sudipta Banerjee	MFI
43.	S.G Nadgonda	Central Bank of India
44.	R.K. Mohanty	United Bank of India
45.	A.N.Jha	Central Bank of India
46.	Gopal Biswas	Laghu Udyog Bharti
47.	U.S. Sharma	United Bank of India
48.	A.K Sanyal	UCO Bank
49.	Kalpana Basu	MSE Association
50.	Debdutta Banerjee	MSE Association
51.	S K Alimuzzaman	Entrepreneur
52.	Sheila Steel Furniture	Entrepreneur
53.	S K Hassanuzzaman	Entrepreneur
54.	Moyna Bibi	Entrepreneur
55.	Bibhas Dutta	KVI Board, WB
56.	Runu Ghosh	Entrepreneur

Meeting of the Task Force on Access to Credit, Raw material and marketing held at IGIDR, Mumbai on 04.05.2007

Sl. No.	Name (Mr./Mrs.)	Organisation
1	De Ramakrishnan	Industrial Finance Recons. Assn. For Small and Tiny Enterprises (IFRASTE),
2	Rajan Mehta	ICICI Bank
3	Dr. S L Shetty	EPW Research Foundation
4	Saurav Deshmuckh	Laghu Udyog Bharati
5	Prof. Manohar Kulkarni	Laghu Udyog Bharati
6	G M Ambhore	SISI
7	Anil D Patil	SISI
8	V K Srivastava	PNB
9	K Unnikrishnan	IBA
10	K P Vijay Kumar	ICICI Bank
11	Shilpa Padte	Entrepreneur
12	Rakshpal Abrol	Bombay Small Scale Industries Association
13	K R Khambatete	Chamber of Small Industry Associations
14	B B Kulkarni	Chamber of Small Industry Associations
15	C S Murthy	RBI
16	G P Borah	RBI
17	Y B Madhukar	All India Small Scale Cosmetics Manufacutring Association
18	Nirupam Mehrotra	NABARD
19	C S Prasad	NCEUS
20	Dr. K P Kannan	NCEUS
21	Dr. Ravi Srivastava	NCEUS
22	Dr. G S Bhalla	JNU
23	Dr. S Radha Krishna	IGIDR
24	Dr. Manoj Kumar Panda	IGIDR
25	Dr. Ganesh Kumar	IGIDR
26	Dr. Shovan Ray	IGIDR
27	Dr. M H Suryanarayana	IGIDR
28	Dr K V Ramaswamy	IGIDR
29	Dr. Vijaylakshmi Pande	IGIDR
30	Dr. Surajit Mishra	IGIDR
31	Srinivas Sajja	IGIDR

Annexure - 7

Regional Consultations: Issues, Observations and Suggestions

The Task Force on Finance, Raw Material and Marketing for the Unorganised Enterprises held regional consultations in various parts of the country. The list of participants and dates and locations of the meetings has been provided in Annexure 6. A summary of the issues discussed along with the suggestions received in these meetings under each broad item is given below.

1. Overall Financing of the Non-farm Unorganised Enterprises

Issues

- *Credit flow to Micro enterprises is dismal due to*
  - High risk factor
  - High administrative cost.
  - Attitudinal apathy of bank branch managers
  - Inability to arrange collaterals
  - Inability to assess market and changes
  - Entrepreneurs need guidance which is not available.
  - Lack of knowledge to manage money and enterprise
  - Lack of skill
- It is not the cost of credit but adequacy and timeliness of credit is the biggest problem
- There are 2 types of Risks:
  - for entrepreneurs – Risk adaptability.
  - for Banks – Risk mitigation.
- Charging lower rate of interest from corporates and higher rate from micro enterprises affects competitiveness.
- The rate of interest should not exceed 7 per cent.
- Banks not interested in government. schemes.

Bankers Response

- Bnks are giving credit at 2 per cent below PLR i.e. at 9.5 per cent on loan upto Rs. 2 lakhs.
- Ahering to RBI instructions on SME credit package – 2005.
- D not have separate data on loans below Rs.5 lakh but all of them mentioned that they maintain this data.
- D not go by Credit Rating Yard stick but by Credit Matrix based on 6 parameters which are not based on efficiency of enterprises.
- Hve achieved 21 per cent overall growth in credit last year but not certain about the rate of growth of credit extended to micro enterprise segment.
- Projects fail due to lack of skill but not due to credit
- Terms and conditions of Credit Guarantee Scheme did not suit the banks.
- 20-25 per cent staff shortage in rural areas.
- Principles of commercial viability and social obligation of employment generation cannot go together.
- Charging 7 per cent interest has to be a government. decision while their own cost of funds are around 9 per cent.
- Banks get 2 per cent subsidy from government. on Agriculture Loan. Hence government should provide similar subsidy for Micro enterprises if the they have to lend to the Micro enterprises at 7 per cent.

Views of Micro – entrepreneurs

- Banks do not advance even small loans upto Rs. 2 lakh without collaterals.
- Banks charge several extra fees over and above the rate of interest which in reality translates to a 2 to 3 per cent additional burden.
- Banks are not interested in advancing loans under Credit Guarantee Scheme or National Equity Fund. Most Bank branches do not publicize them.
- Rate of interest should not exceed 7 per cent. It can also be seen to be a social obligation of employment generation on the part of the bank. The enterprises mostly have poor capital base can be termed as akin to producing agricultural produce – and hence the need to attract only 7 per cent interest.

- Incentives are meaningless if the infrastructure conditions like road and power do not improve.
- SIDBI's focus is on larger SSEs and Medium enterprises. No direct lending to Micro enterprises below Rs. 50 lakh.
- Banks should also help the entrepreneurs in selection of viable projects.
- Credit card upto Rs. 10 lakh should be made available for meeting working capital requirements and should be ATM enabled. Currently only SBI provides such cards.
- Need to change the mindset of bankers and bureaucrats in respect of micro enterprises.
- Flow of credit to Micro enterprise be monitored separately and on a monthly basis at district level. Micro enterprises should not be treated as individual enterprise but as family enterprises.
- While banks expect the entrepreneurs to take risk, they themselves are not willing to take risk.

Suggestions

- Promote credit information bureaus in each bank.
- Set up credit counseling centres in each Taluka – with Handholding facilities – entrepreneurs need timely advice.
- Banks should give credit plus services support covering insurance and guidance.
- Promote Business Development Services to provide services of professionals at Taluka level
- Build a corpus of professionals to guide micro entrepreneurs.
- BMs have no flexibility, if there is one, it is in favour of credit worthy corporate sector.
- Staff accountability is killing the bankers.
- Subsidy should not be out of Budget but out of specially dedicated Fund such as Credit Guarantee Fund or Risk Fund.
- Skill sets needs to be enhanced to encourage risk adaptability
- It is necessary to enhance confidence of banks to address to risk mitigation.
- Micro enterprise financing should include insurance of persons and products. Scope of Credit Guarantee Fund be enhanced for this purpose.
- Focus of SIDBI and banks should shift to Micro enterprises by fixing credit targets and their monitoring.
- Remove refinancing condition from National Equity Fund Scheme
- Schemes like C.G. Scheme, National Equity Fund, etc should find mention in loan application and borrower should be asked to exercise his option.
- Encourage banks to advance more through Self Help Groups.
- NPAs on account of financing of small enterprises should be viewed leniently by the CVC.
- Train bank managers in SSE loaning.

2. Micro Credit

Issues

- Present Micro Credit scenario is no solution for Micro Enterprises.
- The Quantum of loan is very low (Rs. 2,500/-) while average requirement of micro enterprises is Rs. 50,000
- Products are limited.
- Has no link with Market.
- No repeat loan.
- Rate of interest very high.
- No encouragement to graduate to Micro Enterprise.

Suggestions

- Micro enterprises, need LIVELIHOOD FINANCE
- Convert SHGs, to Joint Liability Groups to enable viable linkage with banks.
- Agency model needs to be popularized with focus on handholding.
- Innovative products need to be included in Micro Financing.

3. Credit Guarantee Scheme

Issues

- Banks not interested in this Scheme as they are more comfortable in lending with collaterals.

- Find the terms and conditions unsuitable.
- Find it not modelled on DICGC pattern,
- Find 1.5 per cent guarantee fee and a 1 per cent service charge as burden to customers.

Suggestions

- Make loan upto Rs. 5 lakh under C.G. Scheme mandatory.
- Italian model of Mutual Guarantee by Associations be promoted to enhance the confidence of banks.

4. Priority Sector Lending

Issues

- Priority Sector lending got diluted with entry of new activities like housing, education, transport etc.
- No reservation for SSEs in Priority Sector lending unlike agriculture.

Suggestions

- Delete all subsequent additions to Priority Sector lending made after 1990.
- Size of Priority Sector financing be enhanced by including amount in excess of 25 per cent of SLR.
- Reserve 15 per cent of NBC for Micro and Small enterprises.
- Enhance reservation of micro enterprises in SSE lending from 60 per cent to 80 per cent with 60 per cent for enterprises below Rs. 5 lakhs.
- Restrict Priority Sector lending to quantum of loan say below Rs. 10 lakh

5. Innovative Financing

Suggestions

- For the new educated/ qualified entrepreneurs adopting new (risky) ventures, a separate credit routé needed
- Venture capital fund can be one such route
- Create and expand product specific funds
- Set up large number of incubation centres
- Banks should take up Factoring Services to address the problem of delayed payments.

6. Monitoring

Issues

- 21 per cent growth in credit includes large SSEs and medium enterprises.
- No separate figures available on credit to micro enterprises of 21 per cent growth.
- Micro enterprises credit declined to 40 per cent of SSI credit against a stipulation of 60 per cent.

Suggestions

- Fix overall target of 20 per cent on year to year credit increase in SME sector or doubling of credit flow in 5 years (credit package) will not work. Banks should ensure 20 per cent annual increase in each of the sectors separately including for the micro enterprises.
- Have separate monitoring for micro enterprises.
- Have regular monitoring at district level.

7. RBI Committee

Issues

- The standing committee meeting under RBI's Deputy Governor is not a regular one unlike that for agriculture
- Inadequate representation of Small and Micro enterprise (only 5 out of 30 members from MSE sector)

Suggestions

- The Committee meetings be made mandatory on the pattern of agriculture committee.
- Enhance representation of Micro and Small Enterprise Associations to 10.

8. Raw Material

Issues

- Small and Micro enterprise have been facing shortage / cost escalation in respect of following raw materials in recent years:
  - Steel
  - Coal
  - Nickel
  - Aluminum
  - Copper
  - Yarn
  - Non – edible oil for soap.

- Frequent price changes upsets calculation of Working Capital requirement. Banks fix the Working capital / limit once in a year and do not change them in between.
- Shortage of working capital leads to sickness of the units

Suggestions

- Fix the prices of critical raw materials for one year.
- Create price bands for critical raw materials.
- Set up Raw Materials depots of NSIC, SIDC, All India Boards and Corporation like Handloom Corporation, Handicraft Corporation, KVIC, KVIB, etc.

9. Technology

Issues

- Products suffer due to poor quality.
- Inclusion of new technology in the approved Credit Linked Capital Subsidy Scheme (CLCSS) of Ministry of MSME (formerly SSI) takes lot of time.

Suggestions

- Product specific and area specific design development centres be set up.
  - Promote Product Development/ product innovation
  - And Process Development
- Inclusion of Technology in CLCSS be made quicker.
- Rules and conditions of CLCSS be simplified. It should not debar the units from availing any other subsidy.

10. Skill Development

Issues

- By temperament – all the persons seeking livelihood are not entrepreneurs
- Projects fail more due to lack of skill than lack of credit.

Suggestions

- Make investment on skill development and entrepreneurship development.
- Promote micro-enterprises on RUDSETI model adopted by NABARD. Skill development preceding enterprise development - training based production.
- Set up technical training facilities in rural areas
- Hands-on training is needed to enhance technical capability.
- Training alone cannot make a person entrepreneur. They need integrated support for getting credit, procuring raw material and locating a market.
- Set up entrepreneurship guidance and counseling centres at District level, these centres be equipped with services of professionals.

11. Marketing

Issues

- The area of marketing in a Micro enterprise is the most neglected sector.
- Products lack competitiveness.
- Major problem is delayed payment for which MSMED Act 2006 is not solution as units are too small to take recourse to legal action against the buyers.

Suggestions

- Separate budget allocation of Rs.500 crores be made to DC(MSME) annually to promote marketing of micro enterprises.
- Promote on - line marketing to do away with middleman
- Promote brands
- Reserve 5 to 10 per cent space for micro enterprises in malls.
- Set up Rural Haats/Rural Marts.
- Set up Market Association consortia – Participation is exhibitions and trade fairs.
- Promote Factoring Services to solve the problem of delayed payments.
- Encourage Linkage between Micro / Small enterprises in industries and cluster with large enterprises through tax incentive and other measures.

12. Taxation

Issues

- Both large units and micro units pay same rate of excise duty on purchase of raw materials
- While large units avail cenvat since they make bulk purchases from factory depots but micro units cannot get tax benefit since they purchase from retail market without excisable bills
- The units have also to pay 12.24 per cent as service tax. It amounts to double taxation.
- Farm loan upto Rs. 5 lakh is without stamp duty but non-farm loanees have to pay stamp duty.
- The existing SSI Excise Exemption Scheme suffers from several anomalies. It is not universal for all products upto Rs. 1 crore
- Rs. 1 crore exemption unit fixed in 2000 has become redundant due to escalation in prices of raw materials.

Suggestions

- Rationalize tax structure in favour of micro enterprises allowing them a level playing ground.
- Exempt non- farm loan upto Rs. 5 lakh from stamp duty.
- Remove distortions of Excise Exemption Scheme.
- Enhance excise exemption ceiling to Rs. 2 crore due to escalation in prices of raw materials which have gone by 3 to 4 times since 2002.
- Stamp duty payable by SHGs on renewal of agreements with bank be waived off.
- Ensure only one point tax on raw materials.

13. Cluster Development

Suggestions

- Most appropriate strategy for Micro enterprises development is CLUSTER APPROACH.
- Bring clusters under Growth Pole or SEZ. Go for internationally accepted successful models.
- Thailand – one village one product model.
- Non-farm Enterprises Township on the pattern of China.
- Subsidy for development of common facilities and not for individual units.
- State Governments have to play lead role in infrastructure development of clusters particularly roads, power, sewage, water supply and communication net work.
- Collectivize some operations at cluster level such as raw material procurement, design, skill and marketing development.

14. Provision of Rural Connectivity – A Priority

Issues

- Most serious problem faced by Micro enterprises in rural area is poor rural connectivity of infrastructure, roads, power, communications etc.
- Development benefits have not percolated to rural areas due to inadequate infrastructure particularly, road and power.

Suggestions

- Investment on roads, and power should assume top priority.
- The grant under Integrated Infrastructure Development Scheme be raised to 80 per cent on the pattern of NE for relocation of polluting industries from residential areas.
- IID project cost limit be enhanced to Rs. 10 crore.

15. MSMED Act - 2006

Issues

- Newly enacted MSMED Act 2006 is unable to address to the problems of Micro enterprises since it includes 3 very diverse groups.
  - Micro enterprises (upto Rs. 25 lakh of P & M Investment)
  - SSE (upto Rs. 500 lakh of P & M Investment)
  - Medium Enterprises (upto Rs. 1000 lakh of P & M Investment)
- The Act does not address to the needs of Micro enterprise which constitute 99 per cent of total small enterprises and whose average investment is less than Rs. 2 lakh.

Suggestions

- Amend the Act.
- Create new Act for Micro enterprises.
- A separate Development Commissioner for Micro enterprises.

16. Institutional Arrangements

Issues

- Many of the existing institutions are defunct such as SFC, SIDC, DIC, unviable bank branches in rural areas, sub-contracting exchanges etc.
- There is absolute lack of Public-Private Partnership in the field on non-farm unorganised enterprise development. Further, there is no linkage between large, medium, small and micro units.

Suggestions

- Do not create new institutions but revamp the existing ones.
- Do not set up more rural bank branches, encourage linkage between banks and existing unorganised financial system.
- Do not abolish money lenders, but regulate their activities.
- Micro enterprises cannot succeed without family empowerment.

17. *Government Sponsored Self-employment Schemes*

Issues

- Micro credit programme under SGSY Scheme being Target based is adversely affecting Micro financing.
- Projects/ Schemes like PMRY suffer due to under financing by banks, long gap in release of funds, lack of skill and managerial ability and lack of post follow up and market tie up.

Observations

- Some of the successful micro enterprises schemes are:
  - KVIC run REGP Scheme.
  - NABARD run RUDSETI and District Rural Industries Project.
- These schemes provide integrated support with sufficient margin money support.
- REGP works through Individual Rural Volunteers.
- PMRY is lagging behind due to promotion of ill conceived project proposals and absence of integrated support particularly skill, entrepreneurship and marketing. However, inspite of handicaps, PMRY is the ideal scheme to promote micro enterprises
- SGSY Scheme does not promote enterprises, it simply supports the families those who are below poverty line with very small loans not exceeding Rs. 3,000/- under SHG – bank Linkage.

Suggestions

General

- Revamp the schemes
- Bring uniformity in the pattern and quantum of assistance
- Enhance targets to cover large number of non-farm unorganised entrepreneurs

PMRY

- Arrange compulsory 2 months training for prospective beneficiaries.
  - six weeks skill development.
  - two weeks Project Management.
- Persons undergone EDP training by SISIs and others should get preference.
- Raise project cost limit up to Rs. 5 lakh.
- Raise income eligibility limit to Rs. 1 lakh.
- Adequate finance be given by banks and quick disbursement after training.
- Involve, NGOs, service providers and market associations in PMRY units on the pattern of REGP.