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### FINANCIAL INSTITUTIONS PROBLEMS, PROSPECTS AND CHALLENGES - AN ANALYSIS OF HIMACHAL PRADESH FINANCIAL CORPORATION

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#### ABSTRACT

*Finance is an essential and important input for breaking the vicious circle of poverty. Finance refers to the entire flexible structure and processes by which financial services and loans facility is provided to the entrepreneurs. The aim of finance is not only to extend credits to the entrepreneurs but to promote and boost financial markets that will provide sustainable access to financial services by creating a relationship between those with financial resources and those who need them. For any business to grow credit is essential, lack of credit is a barrier to investment and the growth of income particularly of entrepreneurs and nation as a whole. To boost the economy in the state of Himachal Pradesh. Himachal Pradesh Financial Corporation has come a big way to provide institutional credit to the small and medium scale enterprises. It has been found that due to topography of the state and reluctance on the part of government and some entrepreneurs this institutions is not working up to the mark. It has also been observed that due to sickness in industries H.P. Financial Corporation is also suffering huge losses and facing various financial challenges.*

**KEYWORDS:** Industrial health and its impact on financial institutions.

#### INTRODUCTION

Industrialization is one of the accepted tools for the economic development of any nation. In developing countries like India, industrial growth may be carried out by establishing the large, medium, small and tiny/cottage industries by creating employment opportunities. But even after sixty two years of Independence, poverty and unemployment continue to be the major problem plaguing the country, demanding complete attention of planners and policy makers. Different approaches were spelt out in different plans. But the basic objective of ensuring growth with equity and social justice, self reliance, improved efficiency and productivity

ultimately resulting in full employment has remained unfilled. The focus has always been on the problems of poverty alleviation and increasing employment opportunities.

At this stage industrialization is the only hope of the developing country .Industrialization is a multidimensional process. It is the creation of large scale machine based production in all sectors of national economy especially manufacturing. Industrialization assures the predominance of production of manufactured goods in a country's economy and makes possible the transformation of an agrarian or mostly agrarian country into a predominantly industrial country. The production relations prevailing in a country determine the nature, rate, sources of capital, purposes and social consequences of industrialization. Definitely the nature and pattern of industrialization will be different under the different social economic systems.

Therefore, the importance of industrialization does not pertain merely to an economic sphere only but it has political, social, and strategic values also. As the U. N. Committee for development and planning stated:" Industrialization should be viewed primarily as a means of improving the condition of work and living of standards of poverty stricken masses the world over and not merely as means of producing a wider variety of products by application of modern technology. If this is not kept in mind efforts to industrialize may leave the lives of majority of people untouched"

Due to topography of the Himachal Pradesh Medium and Small Scale Industries play a significant role in economic development of the Pradesh .These industries by and large represent a stage of economic transaction from traditional to modern high-tech industries. The variation in transitional nature of this process is reflected in the diversity of these industrial units. These units provide employment in large scale on the one hand and suitable to tap the natural resources where difficult to establish large scale industries.

## **INDUSTRIALISATION IN HIMACHAL**

During the last few years, the industrialization in Himachal Pradesh has made significant progress. Due to topography of the state emphasis was given on small scale sector in the state. During 50s and 60s it was thought that Himachal Pradesh is not suitable for industries. But during planning period Government gave impetus in this direction. The main industrially advanced areas are in district Sirmour, Solan, Parwanoo, Baddi and Baritiwala Sansarpur-terrace, Mehatpur and Damtal.

The details s of the registered unit is shown in Table-1.

**TABLE-1**

### **DISTRICT WISE DETAILS OF THE REGISTERED INDUSTRIAL UNITS (MICRO, SMALL, MEDIUM& LARGE)**

Sr.No	District	No. of Units	Investment ( Rs in lacs)	Employment
1	Bilaspur	2239	52760	9771

2	Chamba	1733	2850.13	6015
3	Hamirpur	2718	6102.	9832
4	Kangra	8761	29615.18	39372
5	Kullu	2438	7066.55	12822
6	Kinnaur	562	490.23	1762
7	Lahaul& Spiti	572	318.77	1575
8	Mandi	3727	9904.81	15386
9	Shimla	3317	23597.42	12819
10	Solan	4574	694118.75	88610
11	Sirmour	3065	136676.99	25695
12	Una	3139	77339.35	18004
	<b>Total</b>	<b>36845</b>	<b>10413.53</b>	<b>241663</b>

Source: Directorate of Industries Himachal Pradesh.

It is clear from above table that as on 31.3.2010 there were 36845 registered units in the Pradesh. And Rs 104113.53 lac investment has been made .These industries are providing employment to 241663 people in different sectors of the industries. To start the industrial activity entrepreneurs take money from banks and mainly from Himachal Pradesh Financial Corporation as term loan and working capital from the banks. Due to many constraints after establishment some of these industries are working well where as others are not performing as per expectorations and either sick or at the verge of sickness.

### HIMACHAL PRADESH FINANCIAL CORPORATION

Himachal Pradesh Financial Corporation (H.P.F.C) was established in the State under the State Financial Corporation Act to provide medium/long term loans to the entrepreneurs for acquisition of fixed assets (land, building, plant& machinery and misc. fixed assets) Term loans is given for setting up new industrial units/ projects and expansion, diversification, modernization/quality up gradation of existing units. Where as working capital is given by the banks. In some cases under composite loan scheme both term loan and working capital is provided by the state financial corporation. Some of the activities of the corporation are explained as:

Activities eligible for financial assistance

- Industrial involved in manufacturing, preservation or processing of goods in small and medium sector.

- Tourism related activities including Hotels, Restaurants, Tourist Resorts, and Amusement Parks etc.
- Construction activities like commercial /housing complexes including community centers, conference halls.
- Medical health, hospitals and other allied services.
- Information technology, telecommunication/electronic software and hardware services.
- Mini/Micro hydro Power project up to 5 MW.
- Educational institutions (land & building component only).
- Small Transport operators(up to 20 vehicles)
- Other eligible activities.

To establish industrial culture and activities in the state H.P.F.C since inception to 31.3.2010, the corporation has made total loan disbursements to the tune of Rs 535.67 crores. During the year 2009-10, the H.P. Financial Corporation sanctioned total loans of Rs 30.22 crores and disbursed total loan of Rs 20.26 cores. And corporation made total recoveries of Rs 38.77 crores against recoveries of Rs 37.83 crores during the previous year. But at the close of the financial year an amount of Rs 132.60 crores remained in default including default in respect of cases where suits have been filled by the Corporation amounting to a total of Rs 101.07 crores. In the financial year 2009-10, the corporation earned the revenues of Rs 17.76 crores against Rs 16.64 crores in the previous year and incurred an expenditure of Rs 23.80 crores against Rs 20.80 crores during the previous year respectively. And in 2009-10 Corporation suffered loss to the tune of Rs 0.80 crore against a loss of Rs 4.16 crores during the previous year. It has been observed that year by year Corporation is bearing losses. At present there are many accounts those have been converted in to NPA's. It has been observed that there is a lack of coordination between the various financial institutions.

## **REVIEW OF RELATED STUDIES**

To advance the industries all over the world financial institutions have to play an important role. In some of the counties these industries are playing a vital role whereas in some countries these industries are not working properly and advance given by the banks are not recoverable. Some of the studies conducted by scholars are explained as:

Mohammad Ghos Iktiyaruddin Bagsiraj, in his study "Islamic Financial Institutions of India Progress, Problems and Prospects" stated that presently over two hundred Islamic banks and financial institutions all over the globe with total transactions valued at over 120 billion US dollars. And there does not seem to be much of correlation between the numbers of Islamic financial institutions established in a given region with the size of the market that these institutions can potentially serve.

K.M.Zahidul Islam, in his study, “The Revisiting SME Financing in Bangladesh” opined that although lot of potentials of SME’s but these industries are disappearing, abandoning developing countries. He stressed that SME’s create low cost employment opportunities, use locally available inputs and technologies, mobilize small and scattered private savings and correct the regional imbalance in development that exists in developing countries.

Hans Gersbach, in his study, “The workout of Banking Crises: A Macroeconomics perspective” analysed that Banking crises occurs when a large number of banks fail to meet capital requirements or are insolvent.

S.Singh and Yogesh Singh in their studies, “ Risk Management in Banks Concepts and applications” stated that with introducing concept of income recognition, asset classification and provisioning during 1992-93 the impact of implementation of these prudential guidelines on commercial banks has been so strong that out of 20 nationalized banks, one had to be merged and out of 19 banks, except 6 ,all 13 were in red, showing net losses aggregating to a staggering level to Rs 3573.13 crores in March 1993 still a higher level of Rs 4705.01 crore in March 1994.They emphasized that if a bank want to survive and grow, it has no option but to actually recover the interest and principal in accordance with the terms of section. In case income is not received as per prudential norms, the loan will become a non-performing asset and NPA affect adversely the health of the bank.

## **OBJECTIVES**

1. To find out the financial accounts health position of HPFC
- 2 To suggest the remedial measure to recover the position

## **METHODOLOGY**

The present paper is an attempt to find out the impact of poor payments of industries and its impact on financial health of the Himachal Pradesh Financial Corporation in the state of Himachal Pradesh. Himachal Pradesh became a full fledged state on Jan, 1971.Now this state comprises 12 districts, spread in 55,673 Sq.kms and population is 60, 77,248 (2001 Census). Keeping in mind topography of the state emphasis was given on small scale sector in the state. But due to many constraints these are not working properly all over country and Himachal particular. In the present study the secondary data has been collected through from official records and annual reports of HPFC analyzed

The position of these steps has been shown in the following tables:

**TABLE -11**

**LOAN COMPOSITION OF HPFC AS PER HEALTH ASSETS COMPOSITION  
OF HPFC INDUSTRIAL UNITS (PERIOD 1993-2006)**

(RS. IN LACS)

Sr. N o.	Category	1993	1994	1995	1996	1997	1998	1999	2000	As on 31.3. 2006
1.	<b>Standard</b>	<b>5279.49</b> (30.27)	<b>5155.41</b> (26.99)	<b>5554.10</b> (27.54)	<b>5225.60</b> (24.49)	<b>5079.45</b> (22.12)	<b>5113.91</b> (22.12)	<b>5015.03</b> (19.68)	<b>4949</b> (17.12)	<b>9567.44</b> (76.00)
2.	<b>Sub- standard</b>	<b>2936.15</b> (16.83)	<b>3691.96</b> (19.33)	<b>3499.32</b> (17.35)	<b>2386.14</b> (11.09)	<b>2617.59</b> (11.92)	<b>2753.45</b> (11.91)	<b>2688.38</b> (10.55)	<b>1767</b> (6.11)	<b>1126.61</b> (8.07)
3.	<b>Doubtful</b>	<b>7903.90</b> (45.31)	<b>7406.02</b> (38.77)	<b>8220.84</b> (40.76)	<b>9212.25</b> (42.82)	<b>9148.10</b> (41.65)	<b>9336.56</b> (40.38)	<b>10907.37</b> (42.80)	<b>14860</b> (51.41)	<b>3555.23</b> (15.87)
4.	<b>Loss Assets</b>	<b>1322.51</b> (7.59)	<b>2849.47</b> (14.91)	<b>2895.20</b> (14.35)	<b>4691.03</b> (21.80)	<b>5121.16</b> (23.31)	<b>5121.16</b> (25.59)	<b>6873.81</b> (26.97)	<b>7327</b> (25.35)	<b>4155.16</b>
<b>Total</b>		<b>17441.24</b> (100.00)	<b>19102.86</b> (100.00)	<b>20169.46</b> (100.00)	<b>21515.02</b> (100.00)	<b>21966.30</b> (100.00)	<b>23121.60</b> (100.00)	<b>25484.59</b> (100.00)	<b>28903</b> (100.00)	<b>18504.44</b>
<b>NPA</b>		<b>12161.75</b> (69.73)	<b>13947.45</b> (73.01)	<b>14615.36</b> (72.46)	<b>16289.42</b> (75.71)	<b>16886.85</b> (76.88)	<b>18007.69</b> (77.88)	<b>20469.56</b> (80.32)	<b>23954</b> (82.87)	<b>8937.00</b> (24.00)

Note: Figures in brackets shows percentage

Source: Figures are based on annual reports of HPFC

Table no. 11. gives the picture of standard, substandard, doubtful accounts given by the HPFC, which is a main financier of the Industrial unit of Himachal Pradesh. It is clear that if unit did not improve his financial position, the unit will become sick. The doubtful and loss accounts reveal that units are sick. The table portrays that money invested by the HP .Financial Corporation in the state which was Rs. 17, 441,21 lac in the year 1993, which increased to Rs. 28903 lac in 2000 and 18504.44 lac in the year 2006. This shows a decline in accounts. It is also clear that in 1993 the composition of loan from HPFC in standard account was Rs.30.27 percent which decreased to 17.12 percent in the year 2000 and further increased to 76 percent during the year 2006, shows healthy sign. So far Substandard accounts are concerned it account to the tune of 16.83 percent in the year 1993 which registered a small

increase to 19.33 percent in the year 1994 but decreased to 17.35 percent in 1995 and 8.07 percent in the year 2006. As regards doubtful accounts are concerned it account to the tune of 45.31 percent in the year 1994 which decreased 40.38 percent in the year 1998 further increased to 51.41 percent in the year 2000 and decreased to 15.87 percent in the 2006 respectively. The loss assets which were Rs 1322.51 lac in the year 1993 increased to Rs.4155.16 lac in the year 2006.respectively.Therefore it is clear from the above that loss assets have shown more than three time increase, which is an alarming sign. . It has also been observed that there is a lack of coordination between the various financial institutions. Although the sick units are helped through the additional doses of credit, concessions and relief's so they revive their position. But this attempt deprived the financial institutions from recycling huge amount. In most of the cases the losses suffered by the financial institutions have been more than the losses suffered by the borrowers and the Government. In terms of new income accounting norms such as advances are categorized as non performing assets/advances (NPA's) interest. On the basis of this system, an advance is considered as performing assets only if interest in respect of that credit facility is paid by the borrower within stipulated time. If interest charged to borrower's account remain unpaid for more than two quarters, it has to be treated as non-performing asset (NPA).The Reserve Bank of India guidelines seek to classify the loan/assets in to four categories i.e. Standard, Substandard, Doubtful and Loss Assets. The Standard Assets means an asset which does not disclose any problem and which does not carry more than normal risk attached to the business. The Substandard assets refers to an asset which has been clarified as non performing asset for a period not exceeding two years.The doubtful asset is one which has remained as nonperforming asset for a period exceeding two years. The loss asset is an asset where the Reserve Bank of India has identified by the financial institutions or its internal and external auditors or loss, but the amount has not been written off wholly or partially. The non-performing assets (NPA's) mean a loan facility in respect of which principal and or interest remains overdue for a period more than two quarters. Thus the substandard, doubtful and the loss assets are considered as NPA's or sickness. In some countries such as Japan, banks have been encouraged to write-off bad loans with retained earnings or new capital or both. This ensures that cost of resolving NPAs is borne by the banks themselves. However this policy is not suitable for countries such as India where banks neither have adequate resources nor ability to raise new capital. And about 70 percent of gross NPAs are locked up in 'hard core' and loss assets accumulated over years. Most of these are backed by securities and therefore, recoverable. But these are pending either in courts or with the Board for Industrial and Financial Reconstruction (BIFR).

## SUGGESTIONS

1. It is suggested that proper monitoring is required before financing the units without any external pressure.
2. Some incentives should be given to those units those repay their installments regularly
3. Government should purchase their products on priority basis.

## CONCLUSION

Industrialization, sometimes also considers as a synonymous of economic growth. Because economic development of any region is mainly determined by the degree of industrialization acquired by it. In the present scenario of acute and increasing competition and thinning spreads, it is imperative for financial institutions to manage various risks arising from their activities, such as credit, market operational and liquidity on a standalone basis as well as an integrated risk basis. With increasing focus internationally on NPA's during 1990s affecting the risk taking behavior of financial institutions/ banks and central banks have typically reacted to the problem difficulty depending on the politico-economic system under which financial institutions operate. The risky projects are being promoted by the venture funds and financial institutions with the advent of era of liberalization, the small- scale entrepreneurs are facing an acute competition with the coming in force of the WTO agreement on 1.4.2001, and the SSI units will have to face the uphill task and the exchange from MNC and other large industries. RBI guidelines stipulate that interest on all NPAs should not be charged and considered in the income account and therefore a critical issue in presenting the clear picture on the profit/ loss account of the financial institutions. It has been observed that due to poor recovery position and the sick health of the industries the health of Himachal Pradesh Financial Corporation (HPFC) also affected a lot. The government should provide liberal assistance to the industries with condition that they will establish units in the state just not to avail incentives rather to settle the business permanently. It has been observed that there is a lack of coordination between the various financial institutions.

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