## Chapter - 2

## EVOLUTION AND MAIN FEATURES OF THE NEW BANK LENDING SYSTEM

Commercial Banks are primarily engaged in providing working capital to industries. Partially, they provide medium term finance also. Provision of long term finance is essentially a function of the term lending institutions. The present system of commercial bank lending in India is partly governed by the historical goals of commercial banking and partly by the cumulative efforts of the regulatory authorities, viz., the Reserve Bank of India and the Govt. of India[1].

Before we try to examine the impact of the New Bank Lending System (NBLS) on the working capital management efficiency of beneficiary industrial firms, it is necessary to examine the different forms of advances and the system of bank lending in India, that prevailed prior to the genesis and implementation of the New Bank Lending System (NBLS). The different forms of the bank advances, their peculiar characteristics, strengths and weaknesses are discussed at the outset followed by a review of the emergence and main features of the New Bank Lending System.

### Forms of Bank Advances

Commercial banks provide credit facilities to industrial firms in different forms, viz., the cash credit, loans, discounting

of bills etc. Each one of these forms have distinct features and relevance in meeting the financial needs of the borrowers as discussed below.

**Cash Credit System**

Under the cash credit system a cash credit account of the borrower firm is maintained by the bank and the credit limits are fixed. The customer is allowed to draw any amount within the credit limit sanctioned by the bank. The cash credit limits are ordinarily sanctioned against the pledge or hypothecation of goods and/or against personal security of the borrowers.[2]

In the initial stages, when the banks were mainly financing trade and seasonal industries, their emphasis was mainly on security of the loan rather than on the purpose for which the facility was used and thus they found the cash credit system more convenient not only to them but also to the beneficiary customers.[3]

The main advantage of this system is its flexibility. It enables the borrowers to recycle the funds efficiently as they may operate the account within the stipulated credit limit as and when required and thereby minimise interest cost by reducing the debit balances. The anxiety to minimise interest cost prompts the borrower to route all his cash accruals through the account and keep the drawings at the minimum required level. This ensures lesser cost

to the borrowers and better turnover of funds to the Bank. The flexibility of the system prevents undue delay, by not repeating documentation and changing securities.[4] Because of this, the banks and their customers, in India have been traditionally accustomed to this system.

However, there are certain weaknesses in this, from the view point of banks and society. For instance, the system does not ensure efficient management of funds by both parties. The traditioal practice of fixing borrowing limits to meet the peak level needs, under the cash credit system, has usually resulted in the fixation of larger limits than required for most part of the year. This system enables the borrowers to draw funds from the account even during the periods of credit restraint as the limits once sanctioned are not curtailed during credit squeeze. Also because of the importance attached to the nature and value of the security under the system, it accentuates, to some extent atleast, the inflationary pressures and also adversely affects the efficacy of banks in their credit planning efforts and the effective regulation of credit by the central banking authority.[5]

The cash credit system is also not conducive to working capital management efficiency in the borrowing firms. An efficient manufacturer gets less finance because his inventory and receivables level will be lower than that of an inefficient producer. Similarly,

a producer who withholds his output, holding larger stocks of raw materials to take advantage of the rising prices in the market is more favoured under the system than the one who sells out his output and maintains his inventory at the minimum required levels.

The limits under the cash credit system are normally reviewed. This is a long period for review looking to the short term nature of the advances. Often even the annual reviews are delayed.

**Loan System**

Under the loan system, the entire amount is sanctioned and paid to the borrower, either in cash or by transfer to his current account. No subsequent debit is ordinarily allowed except by way of interest, incidental charges, insurance premium, expenses for security protection etc. Usually the repayment is made through mutually agreed instalments.

The essential advantage of the loan system is that it is for a fixed period. So the borrowers have to negotiate every time with the banker for renewing the loan. Under the system, the banker is in a decisive position to renew it or not, depending upon his own resource position and credit policy. At the other end, the borrower also has to plan his credit requirements, otherwise he may be saddled with surplus funds or may find it difficult

to meet his requirements of funds during that time. This system, therefore, ensures a better financial discipline, both among the borrowers and the bankers.[6]

As pointed out earlier, there is a built-in system of reviewing the loan proposal when the earlier loan is settled. There are a few other advantages also, mainly to the bankers, such as book-keeping convenience, avoidance of leakage of income, etc. and the simplicity of the system as compared to the cash credit system of determining limits and sub-limits.[7]

The main weakness of the loan system is its inflexibility. Each time it has to be negotiated. This leads to the tendency among the borrowers to borrow more than what they need in order to avoid the formalities of documentation, repeatedly.

Although a loan is always given for specified purposes, banks usually have no control over the end use of the loaned funds. The individual transaction loans have to be usually combined with the revolving credit agreement and informal lines of credit which are virtually commitments to give loans, arranged in advance, as and when required by the borrower. The loans are also more often renewed than repaid. Thus, it is argued that the loan system also would in effect be a 'roll over' credit. The loan system, while simpler than cash credit system in general, has certain

operational difficulties in India due to legal, traditional and infra-structural factors. For instance, the loan documentation is more comprehensive in India than under the cash credit system and has many in-built complications under the existing legal provisions relating to registration charges, etc. Further, in U.S.A. and other developed countries, there is a well-developed secondary level financial market to supplement bank finance. It could not so far develop in India. As a result, industrial borrowers have to entirely depend on the bank loans and credits. While single transaction loans are a form of finance in India its extensive use with large industrial borrowers has not developed as it does not confer any particular advantage over the cash credit system.

**Bill System**

Under this system Bills are purchased and discounted by banks, mainly of approved customers in whose favour regular cash credit limits are sanctioned. In case of documentary bills, the drafts are accompanied by railway receipts or bills of lading etc. For determining the bills' limit, bankers verify the credit-worthiness of borrowers and the genuineness of the bills.

The bills discounted by banks lead to the commitment of the bank funds for the period between the date of discounting the bill

and the date of maturity. The usual maturity time of bills is 90 days or so. The use of bills in meeting the working capital needs of industries in India was not popular due to legal factors, cost factor and the in-built discipline factor. However, due to the genuineness of transactions and the financial discipline facilitating credit and funds planning in banks as well as in industries, several Committees/Study Groups recommended time and again that the bill system be made more popular in India as the use of bills of exchange, as an instrument of credit, would enable the banks and others with surplus funds, to buy bills of various maturity and those who are in deficit, to discount such bills in the market to suit their requirements.[8] Also due to a definite date of repayment in the case of bill finance, credit planning in banks becomes relatively easy. However inspite of many merits of bill finance, it cannot totally replace the other forms of bank lending especially the cash credit system. The process of evaluation of the genuineness of bills is time consuming and the provision of stamp duty and other administrative costs, both at the banks and the beneficiaries' levels, make it a relatively high cost source of finance. Inspite of all these weaknesses it is still felt desirable to encourage the bill system of financing in India.

The existing system of bank lending in the country is a combination of cash credit, loans and bills. Loan system is used where the

borrower needs money in a lump-sum for a definite purpose, viz., purchase of fixed assets or durable goods. These loans are repayable in time-bound instalments. The cash credit system is used for financing working capital requirements of manufacturing and trading firms and the bill system is used to supplement the cash credit system to finance sales and receivables.

However, a review of the lending pattern by commercial banks and their portfolio analysis shows that of all the forms of bank advances, the cash credit system still occupies the most important place in terms of its share in the total bank credit. For example in 1968 the share of cash credit, was 70 per cent in the total credits sanctioned by the banks[9]. The reasons for this situation may be found in the greater emphasis of banks on deployment of their funds in short-term and medium-term avenues, under-developed state of the capital and the bill markets, and greater preference of borrowers for the cash credit form of advance over loans and bills system.

**Emergence of NBLS**

In order to understand the founding ground of the NBLS, it is necessary to recapitulate the findings and recommendations of three main committees/study groups, viz., the Dahejia Committee, the Tandon Study Group and the Chore Committee which dealt with the problem. The Dahejia Committee initiated the process of identification

of the weaknesses of the prevailing system of bank lending. The Tandon Study Group came out more specifically, taking a multi-dimensional view and suggested measures for ensuring improvement in the system to ensure a better utilisation of resources, monitoring of the end use of bank credit and financial discipline, at the beneficiary level. The Chore Committee was more or less a follow up of the Tandon Study Group which mainly concerned itself with the gap filling task and offered many suggestions to streamline the procedures in the New Bank Lending System. The issues relevant to this study, brought out by the above committees/study groups are briefly discussed below.

**Dahejia Committee**

This Study Group constituted by NCC under the chairmanship of V.T.Dahejia examined 'the extent to which credit needs of industry and trade were likely to be inflated and how such trends could be checked'. The Group highlighted that a large part of the cash credit was getting diverted for other purposes. A significant portion of funds was siphoned off for purposes other than the specified ones; and that the cash credit system was mainly security-based which failed to ensure the proper end-use of bank credit. The 'self cheque' drawings were also questionable as in many cases and the actual withdrawals were not always based on stock levels.[10] Cash receipts through sales processes were not always channeled through the cash credit account leading to many weaknesses in the monitoring system.

The group further observed that the bank credit during the period 1960-61 to 1966-67 expanded at a higher rate than the expansion in industrial production. Between 1961 and 1967 the value of inventories increased in Industry by 80 per cent while short-term bank credit increased by 130 per cent. The ratio of short-term bank credit to inventories went up from 40 per cent to 52 per cent during this period.

A study of 255 companies over the period 1961-62 to 1966-67 showed a deterioration in their current ratio due to increase in the short term liabilities. Bank credit was partly utilised to bridge the gap between long term assets and long term liabilities as one-fifth of the gross fixed assets of these companies were financed by expansion in short-term liabilities, including bank loans. As a result, short-term bank credit no longer remained a circulating fund. Such a situation, according to the committee, was the result of the cash credit system of lending which accounted for about 70 per cent of total bank credit.[11]

In view of the above, the Committee suggested that the cash credit requirements should be estimated realistically and scientifically. The core part of the working capital requirements and the fluctuating components of such requirements should be separated. For the core part, banks should have a committed response to the borrowers. But in the case of fluctuating components adequate attention should be given to the assessment of needs realistically and to the

follow-up for preventing diversion of funds.

The Committee, thus, for the first time highlighted the weaknesses of the then prevailing cash credit system of bank finance to meet the working capital needs of industries, especially with regard to inventory finance.

**Tandon Study Group**

The imbalance between demand for, and the supply of, bank credit and the felt need for reform in the lending system of banks led to the appointment of the Study Group in July 1974 to frame guidelines for the follow-up of Bank Credit. The Study Group headed by P.L.Tandon submitted its Interim Report in November, 1974, in which it suggestd norms for holding current assets in respect of 10 major industries. The Reserve Bank of India accepted the interim recommendations and directed the banks to implement the recommendations with immediate effect. The final report was submitted in mid 1975 which was, by and large, accepted by the R.B.I. for implementation with effect from August 1975. The present system called NBLS is essentially based on the recommendations of the Group, with some procedural changes introduced over a period of time.

The Study Group basically had two philosophical bases in their endeavour. Firstly, it felt that inventory and receivables comprise

the major portion of current assets in industrial firms and it should be the responsibility of banks to supplement the borrower's resources and not substitute, them, to help him carry a 'responsible level' of current assets. Secondly, it felt the need for ensuring financial discipline amongst the borrowers by laying down norms in such a way that the whole gamut of the suggested New System of Bank Lending, should enable the Banks also to plan and allocate credit more rationally and realistically, and to help in the reducing of regional and sectoral imbalances in the deployment of bank funds.

**Main Feature of the NBLS**

The operative part of the New Bank Lending System (NBLS) may be understood under the following heads :

(i) Norms;
(ii) Rules for Lending;
(iii) Follow-up System

**Norms**

Norms are applicable to the industrial borrowers whose limits for working capital finance from the banking system exceed Rs.10 lacs. The Committee laid down norms only for 15 industries, as given below.[13]

## Suggested Norms for Inventory and Receivables

| | Industry | Raw materials | Stock in-process | Finished goods | receivables and bills purchased and discounted |
|---|---|---|---|---|---|
| | (1) | (2) | (3) | (4) | (5) |
| (i) | Cotton and Synthetic Textiles | Cotton 2(Bombay and Ahmedabad areas) | 3/4(Composite textile mills) | -----2¼ --------- | |
| | | | ½ (other mills)----do ------ | | |
| | | 3 (Eastern areas-- Bihar, Orissa, West Bengal, and Assam) | | | |
| | | 2½ (other than the above areas) | | ------do-------- | |
| | | 2 Other raw materials | | | |
| (ii) | Man-made Fabric | 1½ | ½ | -----1 3/4 | |
| (iii) | Jute Textiles | 2½ | ¼ | 1 (For domestic sales)and 1½ (for exports) | |
| (iv) | Rubber Products | 2 | ¼ | -------1 3/4---- | |

| (1) | (2) | (3) | (4) | (5) |
|---|---|---|---|---|
| (v) Fertilisers | | | | |
| (a) for nitrogenous plants | 3/4 (Units near refinery) | Negligible | 1(Where stocks are in plant site) | 1¼ |
| | 1½(Units away from refinery) | | 1½(Where stocks are also in up-country centres) | --do--- |
| (b) For phosphatic plants | 2 (Units in port areas) | Negligible | 1(Where stocks are in Plant site) | 1¼ |
| | 3 (Units away from port areas) | | 1½(Where stocks are also in upcountry centres) | --do-- |
| (vi) Pharmaceuticals | 2 3/4 | ½ | 2 | 1¼ |
| (vii) Dyes and dyestuff | 2¼ | 1 | 3/4 | 2¼ |
| (viii) Basic Industrial Chemicals | 2 3/4 | ¼ | 1 | 3/4 |
| (ix) Vegetable and Hydrogenated Oils | | Negligible | ------ 3/4 ------ | |

| (1) | | (2) | (3) | (4) | (5) |
|---|---|---|---|---|---|
| (x) | Paper | 2.6 Bamboo and wood (To be built up in stages from November to and thereafter to be brought down)<br>2¼ Chemicals | Negligible | 1(For controlled sales)<br>¼(For free sales) | 3/4 |
| (xi) | Cement | 2¼ Gypsum<br>1¼ Limestone<br>3/4 Coal<br>1½ Packing materials | ½ | --------1 | ------ |
| (xii) | Engineering Automobiles and Ancillaries | 2¼ | 3/4 | ------- 2 | ------ |
| (xiii) | Engineering Consumer Durables | 2 | 3/4 | ------- 2½ | ----- |
| (xiv) | Engineering Ancillaries (other than Automobile Ancillaries) and Component Suppliers | 2 | 3/4 | --------2½ | ------ |
| (xv) | Engineering Machinery Manufacturers and other Capital Equipment Suppliers (other than Heavy Engineering)** | 2 3/4 | 1¼ | ------ 3½ | ---------- |

**Notes.** (i) Raw materials are expressed as so many months' consumption. They include stores and other items used in the process of manufacture.

(ii) (a) Stocks-in-process are expressed as so many months' cost of production.

(b) In individual cases, the bank may deviate from the norm for stocks-in-process if it is satisfied that the actual process time involved in any particular unit, say, in view of the nature of production, past experience and technology employed, is more than the norm suggested.

(iii) (a) Finished goods and receivables are expressed as so many months, cost of sales and sales respectively. These figures represent only the average levels. Individual items of finished goods and receivables could be for different periods which could exceed the indicated norms so long as the overall average level of finished goods and receivables do not exceed the amounts as determined in terms of the norm.

(b) The norm prescribed for receivables relates only to inland bills on short term basis (i.e. excluding receivables arising out of deferred payment sales and exports).

Norms relate to Chargeable Current Assets (CCA) comprising inventory and receivables as given below :

CCA = TCA - OCA, or

= I + R,

Where,

I = RM & CS + WIP + FG + Sp in which,

RM & CS = Raw Materials and Consumable Stores,

WIP = Work in Process

FG = Finished Goods Stock

Sp = Spares

R = Receivables of book debts arising out of credits given/credit sales.

In order to ensure that industrial units hold inventories and receivables only necessary for their operations, so that dead, slow moving, specultative and flabby inventories are eliminated, certain rules to calculate the acceptable levels of Chargeable Current Assets (CCA), which the borrower may be permitted to carry, have been framed, as given below : [14]

(1) The past practice of the borrower must be ascertained by calculating the holding of raw materials, work-in-process, finished goods and the level of receivables from the past, financial data in relation to consumption of raw materials, cost of production, cost of sales and gross sales, respectively.

(2) The past holdings must be compared to the norms to identify the lower of the two, as the norms were not suggested as entitlements but were the upper limits for the holding of inventory and receivables.

(3) The banker has to consider the past practice or norms, whichever is lower. This rule is meant for determining the maximum holding of inventory and level of receivables which is allowable for the next year.

While computing the norms for inventories and receivables, banks are expected to take note of the following facts :[15]

(1) So far as the norms for receivables are concerned, these are only for receivables arising out of inland, short-term sales and not for receivables relating to deferred sales and export sales.

(2) In individual cases, the bank may deviate from the norms for stocks-in-proces, if it is satisfied that

the actual process time involved in any particular unit is more than the norm suggested, especially in view of the nature of production, past practice and technology employed.

(3) In case of imported materials, comprising a major portion of raw material requirement, deviations may be allowed after considering factors such as volume, frequency of imports, past levels, etc. This deviation should be restricted only to raw materials imported directly by the borrower under his actual Users' Licence.

(4) The accepted level of stock of spares should be either the expected consumption of spares for the projected year or 5 per cent of the accepted level of inventory, whichever is lower. Any excess of spares over and above this level will have to be treated as non-current assets.

(5) Clubbed norms for more than one item of chargeable current assets in case of some industries have been presented.

**Deviations from Norms**

Norms for inventories and receivables cannot be changed for individual

borrowers. They can be changed for the entire industry; but only by the Committee of Directors of the Reserve Bank of India. This Committee can change the norms on the basis of representations made, by either the Bank or the Industry's representatives.

In the following six cases deviations are permitted for a short period of time : [16]

(1) Bunched receipts of raw materials including imports.

(2) Power-cuts, strikes and other unavoidable interruptions in the process of production which will affect raw material stock.

(3) Transport delays and bottlenecks which will affect finished stock.

(4) Accumulation of finished goods due to non-availability of shipping space for exports or other disruptions in sales, but not under circumstances where a sales stimulation is needed through reduction in prices.

(5) Built-up stocks of finished goods such as machinery, due to failure on the part of purchaser, for whom these were specifically made, to take delivery; and

(6) Need to cover full or substantial requirements of raw materials for specific import contract of short

duration provided there is no escalation clause in the contract.

The above deviations are permitted only for temporary periods. The units are expected to carry the normal levels of CCA as soon as these circumstances get over.

Thus, norms are prescribed separately for raw materials, stock-in-process, finished goods and receivables and all borrowed units must comply with each of the norms. Interchangeability of norms within the total sanctioned limit, in the sense of permitting holding of higher level of say, raw materials, because of lower levels of finished goods, etc. is not allowed.

**Rules for Lending**

The following two rules for lending are followed under the NBLS:

(i) Subject to certain listed exceptions, the maximum permissible levels of inventory and receivables should be equal to norms or the past practice, whichever is lower, and

(ii) Each borrowal unit must have a positive net working capital (NWC). It means, a part of the current assets must be financed by the borrower from his long-term funds.

## Methods of Ascertaining PBF

There are two methods of calculating the Permissible Bank Finance under the new system which are explained below :

### First Method

Under the first method, banks should first calculate the Working Capital Gap (WCG), as given by

WCG = TCA - OCL

where,

WCG = Working Capital Gap,

TCA = Total Current Assets arrived at by

TCA = CCA + OCA,

Where,

CCA = RM + WIP + FG + Sp + R, each symbol means,

RM = Raw Materials + Consumable Stores,

WIP = Work in Process/Progress,

FG = Finished Goods Stock,

Sp = Spare parts kept in inventory,

R = Book Debts of receivables

OCA = Other Current Assets, such as cash, advances, etc. and

OCL = Other Current Liabilities, computed by

OCL = TCL - BB,

where,

TCL = Total Current Liabilities arrived at by TL - LTL,

where,

TL = Total Liabilities, and

LTL = Long Term Liabilities

BB = Borrowings from Bank

After calculating the WCG, the banks should calculate the Permissible Bank Finance by

PBF = .75 (CCA + OCA - OCL)

where,

PBF = Permissible Bank Finance and the other limits of credit

CCA = Chargeable Current Assets

OCA = Other Current Assets, and

OCL = Other Current Liabilities

Thus, under the first method, the borrower is supposed to finance 25 per cent of the WCG out of long term funds, called Matching Contribution (MC). Banks are expected to provide the balance of 75 per cent, in different forms, as per the needs of the borrowing firm.

**Second Method**

Under the Second Method, borrowers should provide 25 per cent of the total current assets (TCA) as matching contribution (MC) and from the 'remainder' so left, other current liabilities (OCL) should be deducted.

The balance would be the maximum permissible bank finance (PBF), as given by,

$$PBF = .75 (CCA + OCA) - OCL,$$

Thus, under the second method the matching contribution is higher than in case of the first method. It also, means that the current ratio of the firm will be higher in case of the second method, compared to the first. The implication of this method is that the ratio of Bank Credit to CCA will be lower in the case of the second method.

In the beginning the borrowers, who had weak financial position with credit limits of Rs. 10 lacs or more from the banking system, were required to be covered as early as possible, not exceeding a period of one year. The aim was to ensure that, the borrowers move from the first to the second method as early as possible, and those who are already in the second Category, not increase their dependence on bank borrowings.

The rationale behind these methods of lending is that there must

be a favourable relationship between current assets and current liabilities and that the borrower's contribution (Net Working Capital) for supporting the current assets must increase in due course, so that over a period of time the borrower's dependence on bank finance should come down.

At the time when the NBLS was introduced, it was felt that some time was needed by the borrowers to adjust themselves to the discipline of the new approach. The banks were supposed to work out the position of the existing customers and any excess of the finance was to be converted into working capital term loan (WCTL), which was to be paid by the borrowers in due course, depending upon their cash generating capacity, ability to raise additional equity, etc. It was felt that need for additional credit will arise with an increase in the level of production. For that, the borrower should bring a matching contribution required under the relevant method of lending. In case of excess borrowing representing the excess of inventory and receivables, credit facilities should not be given untill the current asset levels are brought down to the required levels.

Follow-up System

A comprehensive information system for proper financial follow-up of the bank credit is an integral part of the NBLS, mainly to ensure the safety of bank credit, and its proper end-use.

**The Suggested Information System**

From the angle of submission of periodical statements, borrowers are grouped under the following categories :[17]

(1) Borrowers enjoying a working capital limit of Rs.10 lacs and more.

(2) Big borrowers who enjoyed a working capital limit of Rs. 1 crore or more at the beginning of the NBLS.

Both the categories of borrowers are required to submit the following three statements :[18]

(1) Past and projected balance sheets and projected peak-level balance sheet (once a year)

(2) Past, present and projected operating statements (once a year), and

(3) Stock-statements in revised forms (once every month)

In addition to these, borrowers listed in the second category are required to submit the following Quarterly Statements :

(1) Statements of current assets and liabilities giving actuals of past quarter and projected for the current.

(2) Funds Flow Statement, giving actuals for the preceding quarter and projected for the current one;

(3) Operating statement on quarterly basis, giving actuals for the past quarter and projected for the current; and

(4) Half-yearly Pro-forma Balance Sheet and Profit & Loss A/c, within two months.

**Interpretation of Various Statements**

The information system had been so designed that it could be used in three ways to evaluate the operations of the borrower. Firstly, the past performance could be evaluated to asses the financial position and viability of the borrower. Secondly, the projections could be evaluated to check if the planned future operations were acceptable to the banker; and thirdly, the actual achievements could be compared with the plans to identify the variances of up to ± 10 per cent of the estimates which are permitted But variances beyond ± 10 per cent are to be enquired into by the banker.[19]

Other things to be seen in the stock statement as per the guidelines are that;

(1) The statement should show the entire stock of CCA belonging to the business, including stocks which might not have been pledged or hypothecated to the bank. Stocks shown in the statement are to be valued

consistently on the same basis on which they are valued for balance sheet purposes. The banker is permitted to charge 2 per cent penal rate of interest on excess borrowings on account of excess holding of CCA, if he felt that the party is not cooperating in bringing down the excess stock in accordance with the agreed programme.

(2) **Quarterly funds flow statement**

Quarterly funds flow statement shows the total sources and uses of funds for a given quarter. If during a particular quarter the sources side exceeds the uses side, the unit will be in surplus to that extent and the bank borrowings must come down accordingly. On the contrary, if sources side falls short of the uses side, the bank borrowings will go to the extent of this net deficit by the end of the quarter.[20] Thus, quarterly funds flow statement is meant for assessing the permissible quarterly levels of drawings.

(3) **Quarterly Statement of CA/CL (Form Ib)**

This statement which is a brief report of the current assets and liabilities at the end of the past quarter is also to be submitted, in the beginning of each quarter. Generally three points are being checked carefully from this statement :

(a) What is the net working capital (CA-CL) of the unit, as at the end of the past quarter and how does this compare with the NWC projected for the current quarter? If the projection shows any deterioration in the NWC, it should be examined.

(b) At the end of a quarter, the actual statement of CA/CL should be compared with the projected one submitted in the beginning of the quarter. Any significant variance should be noted and investigated.

(c) It should be ensured that the current assets shown in the projected statements (1b) are within the permitted levels. Similarly, the current assets at the end of the quarter should tally with the stock statement of that month, besides being within the permitted levels.

(4) <u>Quarterly operating Statement</u>

Big borrowers (working capital limit of Rs. 1 crore and more) are required to submit a quarterly operating statement - both actuals for the past quarter and projected for the current quarter. This is one of the most dependable sources of ascertaining the continued

viability of the borrowing unit.

Operating statement provides data on the following :

(1) Sales

(2) Cost of Production

(3) Cost of Sales

(4) Gross Profit

(5) Operating Profit

The banker is expected to study these figures and examine the statement from the following angles ;

(1) How projections for the next quarter, with reference to sales, cost of production, cost of sales, gross profit, operating profit, margin ratio, turnover ratio and return on investment, etc., compare with that of the previous quarter or the same quarter of the last year. It should also be seen that the quarterly statements are consistent with the annual projected, operating statement and the proposed business plan. Another important point is to ascertain whether projections are in conformity with the past or is there any sharp break- upward or downward ? If the projected figures are very different from the comparable ratios and figures of the past, the reasons must be ascertained.

(2) On receipt of the actual quarterly operating statement the banker is expected to look for any significance difference(s) between the projected and the actual figures. If such a comparison is unfavourable, preventive action may be taken by the banker.

(3) Quarterly operating statement (both projected and actual) is the basis of preparing (i) Quarterly funds flow statement, and (ii) the Quarterly statement of CA/CL. The banker must examine the consistency of these three statements and suggest corrective action wherever needed.

The main fatures of the New Bank Lending System, introduced in 1975, have got slightly modified, especially procedural matters on the recommendations of the Chore Committee, which was appointed by the R.B.I. to review the system of cash credit. Also, the inventory norms in respect of certain industries have been revised by the R.B.I. during the period of this study. Still, the main objects of the NBLS remain unchanged.


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