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PROGRESS AND PROBLEMS IN IMPLEMENTING  
PROGRAMMES OF FINANCIAL ASSISTANCE 1/

by

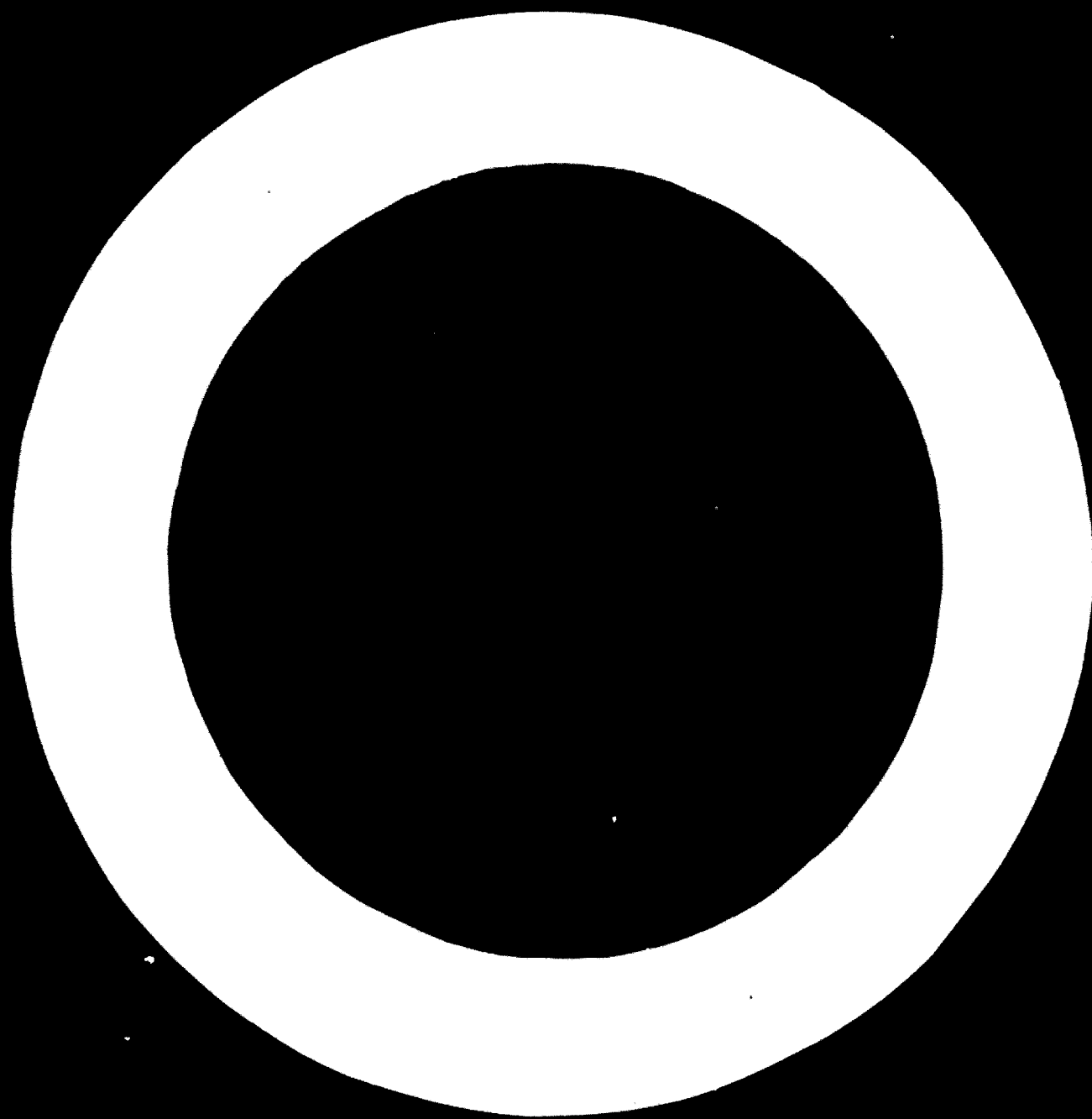
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## INTRODUCTION

"Small Sector" as a distinct component of the Industrial Sector was recognised by the Government of Pakistan in 1955 when the National Small Industries Corporation came into being. The recognition of the role of Small Sector in the over-all industrial policy was the first giant stride taken in the direction of development of this Sector and the first positive attempt to take effective steps in meeting the demands of the small entrepreneur. The West Pakistan Small Industries Corporation was established in 1960. The Small Industries Corporation was, however, subsequently merged with the West Pakistan Industrial Development Corporation in 1962 wherein it became to be known as Small Industries Division of that Corporation. The credit operations started after the merger of the Small Industries Corporation with the West Pakistan Industrial Development Corporation. The policy of the Government to decentralize various developmental agencies of the country also resulted in the bifurcation of functions of the Small Industries Division of the West Pakistan Industrial Development Corporation and the establishment of West Pakistan Small Industries Corporation in 1965.

"Small Industry" is defined as an industry engaged in the handicrafts or manufacture of consumer or producer goods, the value of the total fixed assets whereof (including land) does not exceed ten lacs of rupees.

Scarcity of capital has been primarily responsible in the slow development of the Industrial Sector in all the developing countries. The Small Sector has been no exception to this general rule. The traditional sources & institutions of finance are shy to invest in small ventures and advance

loans to smaller units. The Small Sector is deprived of its due share of whatever little capital is available because:

- i) It is considered that smaller units cannot compete economically with the bigger units;
- ii) In the developing countries having mixed economies the banks and Insurance Companies are by and large controlled by the big business. Therefore, the big business has more influence upon them. Consequently the financial needs of the small entrepreneur are neglected by them;
- iii) The small industrialist does not have sufficient leverage with the Government to get the Import Policy framed so as to suit their industrial raw material requirements;
- iv) Most of the small units are not registered on Stock Exchange.

Public Corporations in the form of Small Industries Corporations have, therefore, been established to promote the development of small industries and to supplement capital in cases where it is not forth-coming.

The financial assistance thus provided, is of three types:

- I. Equity Participation by the Government;
- II. Under-writing of shares; and
- III. Credits.

#### Equity Participation Fund

The Government of Pakistan established an Equity Participation Fund in 1973 to provide equity support and to promote and generate investment in the Private Sector in East Pakistan and less-developed areas of West Pakistan. Initially a sum of Rs.5.00 crores is placed at the disposal

of the Equity Participation Fund. This is contributed as follows:

Government of Pakistan:	Rs.2.00 crores.
Government of East Pakistan:	Rs.50.00 lacs.
Government of West Pakistan:	Rs.50.00 lacs.
State Bank of Pakistan:	Rs.1.00 crores.
Institutional Investors:	<u>Rs.1.00 crores.</u>
Total:	<u>Rs.5.00 crores.</u>

Since its inception in mid 1970, the Fund has disbursed over Rs.2.00 crores mainly to entrepreneurs of moderate means in East Pakistan. Since the operation of the Fund is confined to Companies and is not extended to sole proprietorships the scope of the Fund is limited. Sole proprietorships have been primarily excluded due to lack of liquidity of their shares.

The under-writing operations of the Fund give further support though not directly yet when public issue is not fully subscribed due to inadequate public response the eventual take-up of shares by the Fund also amounts to financial assistance. Moreover, since Fund is an independent Government sponsored organisation properly staffed with technical personnel, under-writing of shares by it infuses enormous confidence in the general public to take up such shares.

#### Credits

One of the primary functions of the West Pakistan Small Industries Corporation is to provide financial assistance in the form of loans to small entrepreneur. There are two types of loans: Loans in foreign currency and loans in local currency. Local currency loans are

further categorised as long term and short term loans.

The Corporation is authorised to stand guarantee for loans of the following aggregate limits:

- a) In the case of Industries located outside  
Small Industries Estates:
  - i) When made to an individual Rs.50,000.00
  - ii) When made to any borrower other than individual: Rs.2,00,000.00
- b) In the case of Industries located inside  
Small Industries Estates:
  - i) When made to an individual Rs.1,00,000.00
  - ii) When made to any borrower other than individual: Rs.5,00,000.00

Aggregate limit of the loan can, however, be increased with the approval of the Government.

Foreign Credits. Loans in foreign currency are dependant upon the availability of foreign credits with the Government. No cash foreign exchange is made available to the Corporation for disbursement of loans to the small entrepreneur.

Foreign credits are meant for the import of machinery and equipment for establishing new units or for balancing and modernisation of the existing units. Beside World Bank Loans all foreign credits are tied loans and, therefore, by their very nature are unable to meet the diverse requirements of this Sector. This is obviously so because no single country is producing machinery and equipment economical and competitive enough to cater to the needs of various lines of manufacture undertaken in the



entire Small Sector. Since International Bank for Reconstruction & Development loans are scarce, it is, therefore, imperative that credits from various countries are made available simultaneously to the Small Industries Corporation for disbursement to promote the development of this area of industry as a whole. Foreign credits sanctioned upto 31st December, 1970 to small entrepreneurs through the Small Industries Corporation are equivalent to Rs.521.47 lacs.

In addition to the out-right credits, occasionally an allocation is also made to the Small Industries Corporations out of Barter Agreements. The list of the machinery is given with every such agreement and, therefore, allocation is to be utilised for that particular machinery only. The Socialist countries and Barter agreements pertain to them, are traditionally the suppliers of heavy machinery and barring very few exceptions, they do not provide machinery which could be useful for setting up of small industries. Moreover, the prices of such machinery are not competitive with those prevailing in the world market and, therefore, does not attract the small entrepreneurs. Although theoretically this source of assistance in foreign exchange is also made available to Small Sector but in most of the cases it remains un-utilised.

#### Rupay Financing.

Long-term credits. Long term rupee credits are primarily meant for financing the purchase of

machinery manufactured in Pakistan. Such loans are advanced by the Industrial Development Bank of Pakistan. The Corporation shares the risk of bad debts in the ratio of 75 : 25. The Corporation has disbursed long-term rupee credits to the tune of Rs.120.00 lacs upto 31st of December, 1970. The repayment schedule is mutually agreed to between the parties and the Industrial Development Bank of Pakistan. It may extend to even ten years. The interest charged on these advances is :

- |                                      |                             |
|--------------------------------------|-----------------------------|
| i) For loans upto Rs.1.00 lac:       | 3% above the Bank-rate.     |
| ii) For loans more than Rs.1.00 lac: | 3 1/2% above the Bank-rate. |

Short-term credits. The West Pakistan Small Industries Corporation have executed agreements with various scheduled commercial banks by virtue of which these banks provide short-term loans to meet the working-capital requirements of the small entrepreneurs. The loan is for a period of 3-5 years and is repayable in six-monthly instalments. The West Pakistan Small Industries Corporation shares the bad-debt risk in the ratio of 75 : 25.

Short-term credits disbursed upto 31st December, 1970 are to the tune of Rs.51.52 lacs.

The credit operations explained in the fore-going paragraphs have generated a total investment of Rs.1604.00

lacs out of which sponsors' own contribution amounts to Rs.966.00 lacs. A total number of 854 units have been established in various provinces of West Pakistan. Total production capacity created by these industrial units is Rs.4143.50 lacs thus creating 12904 new jobs in the process.

The picture of the financial assistance will not be complete if it is not mentioned that the Corporation has also ventured into operations in areas where the private sector is shy and have invested an amount of Rs.751.32 lacs upto 31st December, 1970. These industries constitute primarily service facilities, Service Centres, Technical Centres and industries catering to the needs of small entrepreneurs, in order to facilitate their growth. It may also be mentioned that the public sector projects are not intended to compete with the private sector but only to supplement and provide assistance in the form of training of personnel, provision of special tools & equipment etc.

#### Appreciation and Suggestions.

The rate of growth in the Small Sector had been slow and the investment has been sluggish in the past. The targets set-forth in the Plans could not be achieved. The problems faced in this connection are numerous. This paper is confined to problems of financial assistance and does not purport to deal with mobilisation of savings and modes of financing of investment in this Sector.

The mechanism of disbursement of loan has been briefly stated above. All the credits are disbursed by the institutions other than this Corporation. This is to say that the Corporation is not functioning as a bank. It also makes clear that the Corporation does not have funds of its own to make available in the form of credits to the small entrepreneurs. It solely relies upon other banks with whom it has entered into agreements for provision of such loans.

On the receipt of an application for loan the Corporation's staff examines the proposal both from technical as well as economic angle. If the project is considered feasible, the Corporation sanctions the loan and sponsors to the concerned bank. The bank again checks up the credit-worthiness and examines the entire proposal afresh. Although Corporation's liability in case of bad debts extends to 75% yet since the actual payment of money is to be done by the banks and they are in no way under the control or even the influence of this Corporation, they not only take their own time but are also averse to giving credits to clientele not coming to them direct but through the Corporation. It may be emphasised that the primary objective of banks is commercial and not promotion of industry. Banks are controlled by the big business. Their interest in the development of small sector is marginal

and, therefore, evidently they take much longer time in disbursing loans than is normally required for checking up the credit-worthiness and even putting forth the complete security arrangements. This is not accusing individual banks. The fault lies with the system. The problem would be there irrespective of the stage of economic development a country has reached. The dual control or entrustment of achievement of an objective to more than one organisation without any coordinating agency is bound to result in confusion. The slow disbursement is bound to be the natural consequence.

In cognisance of the widely-held opinion that Public Sector agencies are comparatively more inefficient than the private organisations, a proposal to form a consortium of commercial banks to deal with loaning operation of the Small Sector in West Pakistan is under the active consideration of the Government of Pakistan. Such a consortium exists in the case of East Pakistan. The performance in utilisation of foreign credits by the East Pakistan Small Industries Corporation is much better after this arrangement. The proposal aims at elimination of one of the Government agencies i.e. Industrial Development Bank

of Pakistan from this process of loan disbursement. The consortium will not be bound so rigidly by the rules and regulations followed by the Government Agencies and is expected to be more enterprising because of the profit motive. The applications for loans are likely to evoke a keener response from the banks because in most of the cases they would be dealing with the known clientele. Checking up of credit worthiness of parties would, therefore, not present a gigantic problem to them.

The proposal envisaging consortium of banks, in the writer's opinion is not the best solution although it would be a definite improvement over the present system. The problem can be solved only if the developmental corporations are converted, inter alia, into financial institutions, that is to say, they are also made banks. They would thus combine administrative as well as banking functions. The Government in collaboration with the financial institutions, if possible, can set up a revolving fund to be placed at the disposal of the Small Industries Corporation for disbursement to the Small Sector. The practice is already in vogue in the Equity Participation Fund. The details regarding terms and conditions of re-financing should not present an insurmountable

obstacle in the way of acceptance of this proposal. Industrial Development Bank of Pakistan, Pakistan Industrial Credit & Investment Corporation and Agricultural Development Bank of Pakistan are the precedents. The Small Industries Corporations, therefore, needs to be organized on those lines and should not be starved of funds. The dependence of these Corporations on other financial institutions tantamounts to this and it detracts from their effectiveness.

The acceptance of the above proposal would not only unify the various operations in a single organisation but would also make such an organisation directly responsible for success or failure in the achievement of the targets set-forth before it. The commercial banks should not be opposed to setting up of such a bank since it will not be competing with the commercial banks.

It is also necessary that the agreements which such a Corporation enters into with the potential industrialists have a clause to the effect that in case of failure to repay the dues, the Corporation shall have the right to take over the management or to dispose off the industrial unit in whatever manner it deems fit. This should secure the loans quite adequately.

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This applies to East Pakistan Small Industries Corporation. The limit for West Pakistan Small Industries Corporation is Rs.5.00 lacs. This, however, is likely to be revised and increased to Rs.10.00 lacs.





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