Quadrant II - Notes

Course Code: COD 112

Module Name: Industrial Finance and New Challenges , Refinance

What is Industrial Finance?

Finance has been aptly described as the life blood of industry. It is a pre-requisite for the mobilization of real resources to organise production and marketing. The provision of adequate finance is of basic importance for the smooth working of the industries and for their expansion.

Meaning of Industrial Finance

The industrial finance pertains to the financial system that provides financial resources for the conduct of industrial activities. The need is for different types of finance and an efficient financial system that adequately finances production and enhances industrial capacity.

The industrial finance refers to the provision of finance for the conduct of activities connected with the production of industrial goods. Production activities involve such diverse activities as construction of building, manufacture of machines, supply/procurement of raw materials, engagement of labourers etc. These activities are undertaken to produce investment-goods and consumption-goods. All these activities imply the use of real/physical resources for production.

Functions of Industrial Finance

Industrial finance is a very complicated problem. Its management is of vital importance because the development of any country depends largely on the industrial development of that country's economy. The term industrial finance is used to denote the organisation of various types of finance needed by industries for carrying on their activities connected with the production of goods and services. The activities in relation to production include construction of buildings, purchase of machines, their repairs, buying raw materials, payment of wages etc. In the case of large-scale industries, the provision of the entire capital required for an industry by an individual or a few individuals is out of question. Therefore, the provision of finance for industries is done through institutions such as banks, money market and capital market. **There are various important functions of industrial finance these functions are as follows:**

1) To provide Financial help or support:

For the improvement of each business there is need of finance. To fulfil the general and salient/ basic needs of the industry or business the financial support or help is must. Industrial finance provides financial support to business.

2) Help for Standing the new Industries :

To build up a strong economy of any country, there must be a need of standing new industry or business that economic area with present industry or business. Industrial finance plays vital important role in helping for standing the new industries.

3) Renovation and Modernization of the present business or industry:

21st century is considered as science and technology and also the information technology. Due to the evolution in the science and technology the continuous changes in the business technology and concept takes place. So, if there is impact or effect of these changes takes place on the total product then there is need of renovation and modernization in the business. To fulfil this technology and modernization need the industrial finance plays an important role.

4) To fulfil the procedures before and after production:
When any industry is established, it has to go through the various procedures during start of the exact production. There should be the fulfilment of the procedures likes, building, machinery, raw materials, market, distribution and marketing before production and after production. For the purpose of fulfil these needs industrial finance plays vital role.

5) To promote Research and Development:
According to the world change there must be modernization in the industrial technology, management system, economic and budget control system for this the research and development is so important. To promote this there is need of finance. Through the medium of industrial finance, the research and development is promoted in brief it is said that the various needs of the industrial procedures are fulfil by the industrial finance very well.

6) Provide Direct Assistance:
It provides direct assistance to industries in the form of Term Loans and this is one of the important functions of industrial finance.

7) Encourages to Corporate:
It encourages the New as well as the existing corporate to raise capital through different types of securities.
8) Project Financing:
It finances the projects of self-employed, handicapped and blind people. It provides refinancing facilities to State Financial Corporations.

Challenges/Problems Faced by Industrial Finance :

The following are some of the important challenges/problems faced by industrial finance in India:

1. Backward Financial System:

One of the important drawback of industrial finance in India is that it is not yet developed fully, the extent of capital market which is a source of long term finance including equity and debt is quite small. It also fails to provide risk capital in adequate quantity. The development of non-bank financial intermediaries is also very poor.

Very little arrangement is made about venture capital which usually makes risky investment for high returns. The system is very much inadequate in respect of financial deepening which can be measured as a ratio of liquid liabilities to GNP. All these indicators reflect about the undeveloped financial system prevailing in our country.

2. Paucity of Funds:

Another shortcoming of industrial finance is that it is grossly inadequate for the continuously growing and large requirements, especially to meet the needs of large industries. Moreover, the small industries are also facing shortage of finance in a acute manner. Besides, the securing and servicing of foreign funds are becoming difficult and expensive. Thus as a result of paucity of fund the expansion of industries is becoming very difficult.

3. Unsatisfactory Interest Structure:

The interest rate structure for different types loans like short term, medium term and long term are more or less unsatisfactory. These rates are not appropriate and are not properly aligned with one another and these rates are largely distorted and does not attain demand – supply equality for capital. Indigenous money lenders also charges high rate of interest from small and village industries distorting the market interest rate structure.

4. Lack of Adequate Capital Formation:

Industrial finance usually suffers from lack of adequate capital formation. There are inherent difficulties of mobilizing the quantum of incremental rural incomes which could have been utilized for financing rural industries.

5. Difficulties of Small Industries:

Small industries located both in urban and rural areas are facing serious problem in realizing adequate finance. The problems faced by SSIs are varied.

i. Lack of institutional finance available to SSI units. Even till to day financial corporations exclusively meant for SSI units have not yet been set up in all the states of the country.
ii. in meeting the short term needs of SSI Units, banks and other financial institution demand adequate security acceptable to them showing least, regard to potentials and other qualities of SSI units reducing the credit worthiness of these units.

iii. in respect long term capital also, i.e., in raising share capital, SSI units are getting less favour as compared to that of large industries. Finally, whatever financial support are available informal and indigenous sources of industrial finance to SSI units are considered to be small and costly considering the high rate of interest changed by these lenders.

Thus the industrial finance as a system in India has been suffering from several drawbacks. Accordingly, it is found to be inadequate, undeveloped following unsatisfactory interest structure and less friendly to small reach and tiny industrial units.

Meaning of Refinance

- ✓ A refinance, or "refi" for short, refers to the process of revising and replacing the terms of an existing credit agreement usually as it relates to a loan or mortgage.

- ✓ When a business or an individual decides to refinance a credit obligation, they effectively seek to make favorable changes to their interest rate, payment schedule, and/or other terms outlined in their contract.

- ✓ If approved, the borrower gets a new contract that takes the place of the original agreement.

- ✓ Borrowers often choose to refinance when the interest-rate environment changes substantially, causing potential savings on debt payments from a new agreement.