

## **CREDIT APPRAISAL PROCESS OF KARNATAKA STATE FINANCIAL CORPORATION FOR WOMEN ENTREPRENEURS**

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### ***Abstract***

Entrepreneurship activities are also enhancing steadily and the contribution by the women entrepreneurs is remarkable. Being an entrepreneur, utilizing skills, presenting knowledge in a particular field, building organization, providing employment facilities are at the optimal level.

Entrepreneurs are the key drivers to the economy; in these background women entrepreneurs are more versatile, many developments have taken place. Women have dual responsibility either to their family or to the business. Women have shown tremendous power either in the allocation of family resources or childbearing decisions or increasing their self-esteem and confidence. In this research paper process involved in availing loan facility for women entrepreneurs is analysed. Generally the financial corporations go through a systematic and comprehensive analysis with reference to Technical, Financial, Commercial, Economical and environmental analysis for the given proposal before the loan being sanctioned by the corporations. A study is being made to comprehend, appreciate and understand the nature of credit appraisal process, the components of appraisal of a given proposal for a women entrepreneur and the process in the way the amount is being disbursed by the Karnataka State financial Corporation is being analysed. The proposal given by women entrepreneur from the MSME sector is evaluated as a part of the research paper.

***Keywords: Financial appraisal, economic, Tax clearance, Legal status***

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## **1.0 Introduction to the topic:**

Entrepreneurs are the key drivers to the economy; in these background women entrepreneurs are more versatile, many developments have taken place. Women have dual responsibility either to their family or to the business. Hence there is lots of opportunity and prospects for women to become entrepreneurs and avail assistance from various financial organizations which are set up for the development and empowerment of women. According to the study made by India's Financial corporation which studied the Micro, Small and Medium Enterprises (MSME) that were set up in India made an exclusive report on 'improving access to finance for women-owned MSMEs'. As per this study it is seen that approximately 78 per cent of all women enterprises belong to the services sector. It is also seen that the GDP of India though services Industries is about 56% of the total GDP. Coming to Karnataka state a new change was brought in in favour of women entrepreneurs. One of the highlights of Chief Minister Siddaramaiah's 2017-18 budgets was that an announcement was made for women who could avail loans up to Rs 2 crore at a nominal interest rate of 4%, which would be implemented through the Karnataka State Finance Corporation. As seen there is huge group of women entrepreneur growing as well as institutions which are supporting the initiative and funding loans to these entrepreneurs.

## **1.1 Objectives of the Study**

- a) To comprehend on the credit appraisal process followed by the Karnataka State Financial Corporation
- b) To analyse, evaluate and synthesize the components of credit appraisal system for a given proposal submitted by the women entrepreneur.
- c) To provide suggestions to the study which will benefit women who are opting for loan facility from KSFC.

## 1.2 Credit Appraisal

Credit appraisal is nothing but the assessment of credit-worthiness of the project which is applied for the sanction of loan in any financial institution. Credit appraisal for the entrepreneurial projects is usually done by various institutions like government, financial institutions and it differs from that of financial institutions but the methods used will be similar. The process is initiated by the financial corporations before taking a decision to lend loans in order to avoid the risk of defaults in repayment of those loans.

Technical Appraisal for a project focuses on analyzing the data with respect to physical inputs and ensuring required inputs will be available to the project. It includes selected manufacturing process, success rate, technical know-how, plant size, availability of raw materials, changing technology, production and its cost-effectiveness, procurement of plant and machinery, personnel to operate, possibility of product mix of existing plant, project location nearing to village or town or city, land requirements and feasibility, nearness to raw materials, power facilities, availability of water and transportation facilities.

Financial Appraisal is finding out the financial viability of a project. It takes into account capital cost of the project, and pattern of funding. Also financial charges of depreciation, interest and the dividends are taken into account. Funds are also procured with a combination of equity capital and debt capital from the promoters of the firm. Profitability and cash flow statements are estimated and the projected balance sheet is prepared. Financial tool especially ratio analysis is an important tool to analyse the financial performance of the project. Important ratio includes Debt-Equity Ratio, Current Ratio, Debt Service Coverage Ratio, Margin on security, Break-even point, Fixed cost, Variable cost, Selling price, Contribution and Internal Rate of Return,

Management Appraisal looks into the promoter's knowledge about product, process, technicalities, and decision making ability and leadership skills. Promoter's background is verified, with institutions connected with business.

Commercial Appraisal includes the verification and analysis for the demand of the goods in the market. Economic Appraisal is a study to assess social and economic benefits and costs (including direct and indirect) of the proposed project.

Legal Appraisal means studying and analyzing the documents provided by the entrepreneur related to the unit. Documents are scrutinized for the collateral security that is given by the entrepreneur which may include land, buildings, residential houses, etc. Environmental Appraisal is a study relating to factors like air, water, land, and location and the pollutant aspects of the project.

### 1.3 Karnataka State Financial Corporation

Karnataka State Financial Corporation is a financial institution established at the state level by the government of Karnataka with a view to provide term loans to the micro, small and medium enterprises. It has been set up in 1959 based on State Finance Corporation Act 1951. When established, this institution was known with the name Mysore State Financial Corporation. After 14 years of the establishment, the government changed MSFC in to KSFC by issuing a notification regarding the same. KSFC is contributing to a greater extent for the development of the economy of the state. KSFC being responsive for the development and growth in the SME sector assisting the industries in this sector by financing for their inception.

### 1.4 Analysis of the proposal provided by a Woman Entrepreneur to KSFC:

Recent projects approved and loans sanctioned by Karnataka State Financial Corporation are taken to understand the Credit Appraisal Procedure in KSFC in the year 2018 (Information is re-stated)

**A. Details of the firm:** The proprietor Mrs. Shanthi Ramdas applies for loan in KSFC of Rs. 50 Lakhs and the institution reduced the amount to Rs. 48 Lakhs. The loan is sanctioned under General Loan Interest Subsidy Scheme for Women Entrepreneurs of Karnataka. The rate of interest is 14 percent on the provided loan.

### B. Project at a glance

1.	Unit Name	Shanthi Ramdas Manufacturers
2.	Constitution	Proprietor
3.	a) Type of Industry	Manufacturing Foot Wear, Other Textiles

	b) Size of Industry	Industry Sector – Small Enterprises
4.	Line of Activity	Woven Cloth Articles
5.	Capacity: (a) Installed (b) Maximum Operating Capacity Envisaged	Rs. 105 Lakhs 80%
7.	Main Raw Material	Color Polyester Yarns/Threads
8..	End Use Of Finished Product	As Labels In Readymade Garments
9.	Sales Turnover In Normal Year	Rs. 84 Lakhs

**C. Project cost:**

SI No	Project details	Amount (Rs in lakhs)
1	Plant & Machinery Indigenous (New)	73.50
2	Miscellaneous Fixed Assets	0.50
3	Deposits	4.00
4	Preliminary. & Pre-Operating Expenses	1.00
5	Interest During Implementation	0.50
6	Start Up Expenses	0.50
<b>Total cost of project</b>		<b>80.00</b>

**D. Means of finance:**

SI no	Means of finance details	Amount (Rs in lakhs)		
Debt	Term Loan From KSFC	48.00	Rs. 53.00 lakhs	<b>Total Rs. 80 lakhs</b>
	Unsecured Loans	5.00		
Equity	Proprietor's Capital	26.00	Rs. 27.00 lakhs	
	Interest Free U.S. Loans from Promoters	1.00		

The proposal is securitized by the employees in KSFC and the proposals which are feasible will be taken for assessment. Generally women entrepreneurs can borrow upto Rs.2 crores from the Karnataka Financial Corporation. Initial Rs 50 lakh is approved at the interest rate will be at 4%. Subsequently if the amount is risen up to Rs 1 crore, then generally the first 50 lakhs will be given at 4% and the rest of the amount will be at higher rate of interest. So, if some women entrepreneur is looking for a loan amount of Rs 2 crore, they can get at 8% annual interest which is lesser than that of Commercial bank interest rate.

## 1.5 Credit Appraisal Procedure

### A. Financial appraisal- Showing financial and profitability indicators

Ratios	Minimum prescribed	Actually provided
Promoter's Contribution	25%	32.50%
Debt-Equity Ratio-Project	2:1	1.96:1
Debt Service Coverage Ratio	1.5:1	1.8:1
Security Margin Retained	25%	34.69%
Overall Security Margin Retained	25%	60.75%
Return on Capital after Taxation in Normal Year of Maximum Operating Capacity	24.85%	
Margin of Profit on Sales before Taxation in Normal Year Of Maximum Operating Capacity	21.21%	
Internal Rate of Return	29.52%	
Break Even Point: (i) As a Percentage of Installed Capacity	56.16%	
(ii) In Terms of Sales	Rs.58.97 Lakhs	

### Details of repayment

Repayment Period	Repayable in 6 Years Excluding a Moratorium Period of 12 Months
Implementation Period	6 Months

Employment Potential Proposed	8 Persons
Capital Investment Per Person Employed	10 Lakhs
Power Requirement Proposed	40.00 KVA
Requirement of Power Per Person	5.00 KVA
Scheme under which the loan is sanctioned	General Loan Scheme
Loan Amount Applied	Rs. 50,00,000
Loan Amount Recommended for Sanction	Rs. 48,00,000
Income tax Returns Filed	Required but not Obtained
Date of Receipt of Application	18- Jan-2018
Time taken for Processing the Loan	13 Days
Name of the Bankers	Axis Bank, Bengaluru

### Net worth details

Assets		Amount
1	Cash in hand	50,000.00
2	Cash at bank	5,000.00
3	Jewelry	11,00,000.00
4	Deposits- Lease Deposit of Rented Premises	4,00,000.00
5	Investment in the proposed project	10,75,000.00
<b>Total assets</b>		26,30,000.00
<b>Total liability</b>		0.00
<b>Total net worth</b>		26,30,000.00

### **A. Technical appraisals-Location and Building**

The unit proposed will be located at a shed in Industrial Estate, KamakshipalyaPalya, Bengaluru. This shed is taken for a lease by the proprietor. The location is in the industrial estate and there are many readymade garment manufacturing units

**Plant and Machinery-** The proprietor proposed to acquire 2 highly sophisticated and technologically advanced “SOMET THEMA” Super Excel Label Weaving Machine made in Italy fitted with IBJ Bonus Jacquard 250 Series made in England. The estimated cost of each unit is 30 Lakhs.

**Raw Material-** Raw material used by the unit for the production of labels is Polyester Yarn/ Silk Yarn/ Cotton Yarn/ Viscose Yarn/ Blended Yarn of different counts and colors, which comes on cones.

**Manufacturing Process-**From the raw material received in cones, wrap is made using wrapping machine. The designs of the labels will be provided by the customers in the form of software stored in drives.

**Power-**The power required by the unit is 40 HP, which is already available at the factory premises and moreover, the lessor also has agreed to use the available power for the working of the unit. Therefore, the unit does not face any problem relating to power.

**Man power-** The man power required for the unit are 8 people including operators, helpers and office staff. There is no problem analyzed in getting the required man power.

**Transport-**As the unit is situated in industrial area, there is no problem of transportation. The area is well connected with roads and good transport facilities.

**Water-** The unit requires water facilities for human consumption. There is no issue related to water as it is supplied by local suppliers.

**B. Management appraisals:**

The unit for which the loan sanctioned is a proprietary concern which will be managed by its promoter. The knowledge, aptitude, skills, and capabilities of the women entrepreneur are assessed by the firm.

**C. Commercial appraisal- Demand and Supply-**

Woven labels are made out of silk, cotton and nylon yarns and they are used in all the garments. They give the manufacturer's identity and the specific material used by him. Demand for these labels has been increasing because of the awareness of the customers regarding the quality of products and brand. The exports of garments to other countries also have increased.

**D. Legal appraisals**

**Tax Clearance-**The proprietor's Income Tax Returns must be obtained subject to the conditions included in the Lending Policy of KSFC.

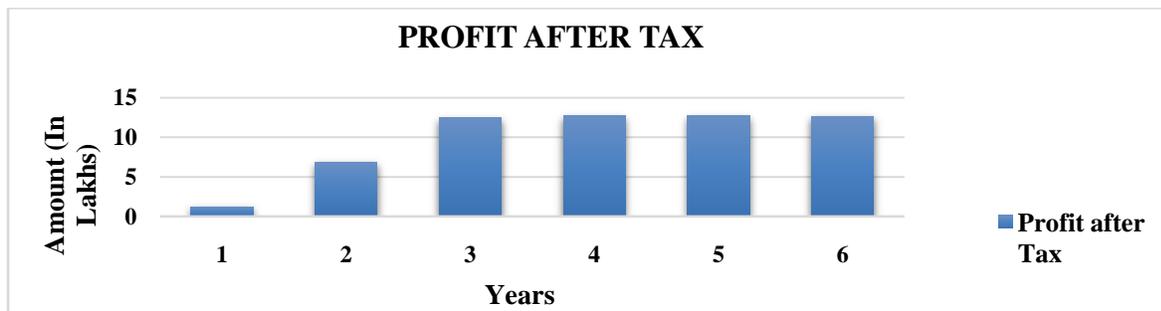
**Status of Government Consents-** Income Tax Returns filed by the borrower should be obtained. In this case there is no such information obtained since the promoter is not an IT assessee.

**1.6 Analysis of Financial performance, Calculation of important ratios based on the previous 5 years of Data****Profitability statement (Rs. In lakhs)**

Years	1	2	3	4	5	6
Capital Utilization %	60	70	80	80	80	80
Sales	63.00	73.50	84.00	84.00	84.00	84.00
Consumables	9.45	11.03	12.60	12.60	12.60	12.60
Power, Fuel	7.17	8.28	9.40	9.40	9.40	9.40
Salary and Wages	15.00	16.13	17.34	18.64	20.04	21.54
Administration and Miscellaneous expenses	7.50	8.06	8.66	9.31	10.01	10.76
Depreciation	11.10	9.44	8.02	6.82	5.79	4.93

Repairs	1.50	1.60	1.70	1.80	1.90	2.00
Interest on T.L.	6.72	6.05	5.04	3.86	2.69	1.34
Selling expenses	1.58	1.84	2.10	2.10	2.10	2.10
Interest on WC	0.47	0.52	0.57	0.57	0.57	0.57
Interest on U S L	0.75	0.75	0.75	0.75	0.75	0.75
Other Fixed Cost	0.00	0.00	0.00	0.00	0.00	0.00
Other Variable Cost	0.00	0.00	0.00	0.00	0.00	0.00
Cost of Production	61.24	63.70	66.18	65.85	65.85	65.99
Profit Before Tax	1.76	9.80	17.82	18.15	18.15	18.01
Tax	0.53	2.94	5.35	5.45	5.45	5.40
Profit after Tax	1.23	6.86	12.47	12.71	12.71	12.61

### Profit after tax



### Debt service coverage ratio

(Rs. In lakhs)

Years	1	2	3	4	5	6
Depreciation	11.10	9.44	8.02	6.82	5.79	4.93
Interest on TL	6.72	6.05	5.04	3.86	2.69	1.34
Profit After Tax	1.23	6.86	12.47	12.71	12.71	12.61
Total	19.05	22.35	25.53	23.39	21.19	18.88
<b>Loans repaid</b>						
Term Loan – Interest Subsidy Women Scheme	4.80	7.20	8.40	8.40	9.60	9.60
Interest on TL	6.72	6.05	5.04	3.86	2.69	1.34
Total	11.52	13.25	13.44	12.26	12.29	10.94
DSCR	1.65	1.69	1.90	1.91	1.72	1.73

**Combined DSCR 1.77****Working Capital Estimate****(Rs. In lakhs)**

<b>Years</b>		<b>1</b>	<b>2</b>	<b>3</b>
Raw Materials	0.50	0.39	0.46	0.53
Work in Progress	0.25	1.24	1.29	1.33
Working Expenses	1.00	2.73	2.99	3.27
Bills Receivables	0.25	1.31	1.53	1.75
Total Current Assets		5.67	6.27	6.88
Less: Creditors	0.00	0.00	0.00	0.00
Net Current Assets		5.67	6.27	6.88
Working Capital Margin		1.42	1.57	1.72
Working Capital Facility from Bank		4.25	4.71	5.16

Source: KSFC Project Proposal

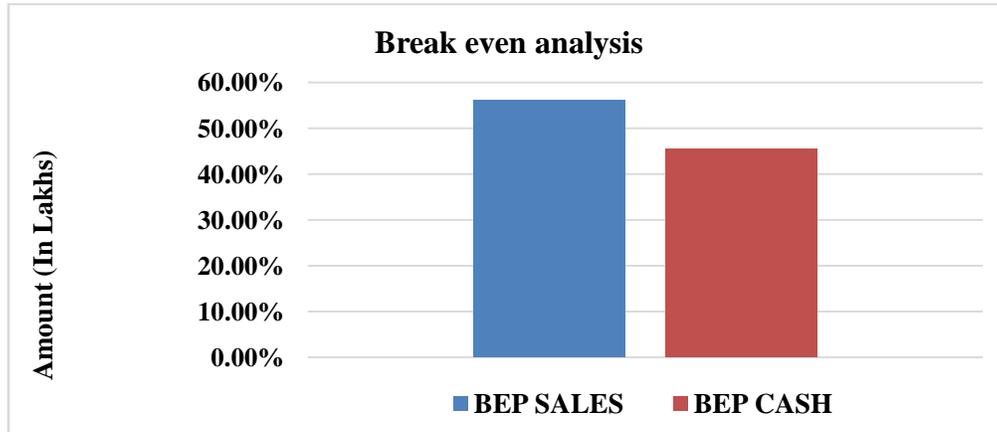
**Break even analysis****(Rs. In lakhs)**

<b>Fixed cost</b>		
<b>Item no</b>	<b>Description</b>	<b>Amount</b>
1	Power	0.45
2	Salary & Wages	17.34
3	Administration Expenses	8.66
4	Depreciation	8.02
5	Repairs & Maintenance	1.70
6	Interest on T L	5.04
7	Interest on U S L	0.75
Total		41.96
<b>Variable cost</b>		
<b>Item no</b>	<b>Description</b>	<b>Amount</b>
8	Consumables	12.60
9	Power - Variable	8.96
10	Selling Expenses	2.10
11	Interest on WC	0.57
Total		24.23
Sales		84.00
Contribution		59.77

Break Even Point	56.16%
BEP In terms of Sales	58.97
Cash Break Even Point	45.43%

Source: KSFC Project Proposal

### Break Even Analysis



### 1.7 Findings of the Proposal

- KSFC is one of the lending financial institutions in the country with assistance to over 1,71,414 units amounting to nearly Rs 15,276 crore over the last 58 years in the State of Karnataka. KSFC is one of the robust and professionally managed State Financial Corporations seen. Accordingly, there is a steady growth of business units that are set up with the financial assistance, support and consultancy taken from the corporation. Through the research we are able to interpret that the proposed amount for request of credit may not be sanctioned. Generally, the amount sanctioned be lesser than the proposal as in case of the ShanthiRamdas Manufactures the approved loan was Rs. 48 lakhs.
- As per KSFC norms, the promoter has to bring the capital up to 25% of the total means of finance and it is satisfied by the promoter who contributed 32.50% that comes to 26 lakhs. The prescribed Debt-equity ratio by the KSFC is 2:1 while the actual ratio of the project is 1.96:1. The security margin retained specified by the KSFC is 25% and original ratio of the project is 34.69%. It is seen that Overall security margin retained of the project is 60.75% which is more than double of the prescribed percentage i.e.

25%. Return on capital after taxation in normal year of maximum operating Capacity is 24.85%. Margin of profit on Sales before taxation in normal year of maximum operating capacity is 21.21%.

- It is found that the unit has to repay the loan amount in 6 years excluding 12 months of moratorium period. The time for the implementation of the project which is given by the KSFC is 6 months. The unit proposed that 8 employees are required for the implementation of the project. It was found that 10 lakhs is the amount to be invested on each worker as per the unit's proposal. The project proposal shows that the total power requirement of the unit is 40.00 KVA. In the proposal, it is seen that the requirement of power per employee is 5.00 KVA.
- The scheme under which the loan is sanctioned comes under General Loan -Interest Subsidy Scheme for women entrepreneurs of Government of Karnataka. The corporation took 13 days to process the application after receiving the proposal from the unit. According to the project Proposal, the net worth of the proposed unit is found out to be Rs. 26, 30,000 which is in the form of assets and there are no liabilities.
- As per the profitability statement prepared by KSFC, it is found that the estimated profits of the unit are uniform in the last 4 years more than that of in the first 2 years. This shows the firm started growing and earning profits from the 3<sup>rd</sup> year. Debt Service Coverage Ratio specified by KSFC is 1.5:1. As per the estimations done by KSFC for the 6 years, it was found that Combined Debt Service Coverage Ratio of the project is 1.8:1 more than that of prescribed by the corporation. Even if it is seen separately also the DSCR in every year is more compared to the specification given by the KSFC.
- KSFC projected cash flows of the unit for the following six years. From these projections done by KSFC, it was found that the closing balance of cash of the unit in every year increased at a high growth rate. The working capital estimate of the unit prepared by the KSFC for 3 years, i.e. from 2018 to 2020 can be seen that the unit's requirement of working capital increased every year. It is proposed that the unit approaches the commercial bank for the loan amount required for working capital at a later stage after the stabilization of the unit. As per the calculations done by KSFC, it can be seen that the

break-even analysis of the unit as a percentage of installed capacity is 56.16%, in terms of Sales value it comes at 58.97 lakhs and cash break-even point is 45.43%.

- KSFC estimated internal rate of return of the project for the next 15 years which came to 29.52%.

### **1.8 Conclusion:**

Procuring funding has become modest for the women who rely extensively on finance funding. Process followed by KSFC is very transparent and adequate for women who are having less knowledge about the credit appraisal system of any Financial Institutions. The procedure followed in KSFC is very apparent and additionally versatile for women run organisations to make their proposal appropriate and pertinent to the requirement of their firm. Meanwhile, the evaluation and estimation of the proposal will automatically be synchronized with the appraising system followed by the firm. The firm will study all the modalities that include financial, legal, management, technical analysis, validate the outcome and decide to appropriate drives for funding the women entrepreneurs. The corporation should also focus on guiding the entrepreneurs in selecting the feasible projects which will satisfy all the required nomenclature. Guidance related to marketing and selling of the products, at the initial stage will help the women entrepreneurs to sustain and grow efficiently in the contemporary market. Overall it is observed that Financial Corporations are more profuse and transparent in their approach towards women entrepreneurs in Karnataka.

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