"A Case Study on Credit Appraisal for Working Capital Finance to Small and Medium Enterprises in Bank of India"

*** Prof TrilokNath Shukla**
****AbhijeetSatpathy**

* Associate professor and vice principal, BCCM, BhartiyaVidya Bhavan, Bhubneswar
** Student, PGP (II), BCCM, Bhartiya Vidya Bhavan, Bhubneswar.

Executive Summary

Also the findings are open for further survey & research by scholars in academia.

Introduction

Micro, Small and Medium Enterprises (M.S.M.E) sector has emerged as a highly vibrant and dynamic sector of the Indian economy over the last five decades. M.S.M.Es not only play crucial role in providing large employment opportunities at comparatively lower capital cost than large industries but also help in industrialization of rural & backward areas, thereby, reducing regional imbalances, assuring more equitable distribution of national income and wealth. M.S.M.Es is complementary to large industries as ancillary units and this sector contributes enormously to the socio-economic development of the country.

The Small and Medium scale enterprises (S.M.Es) play a crucial role in the socio-economic growth story of India accounting for more than 45% of the manufacturing output and around 40% of the total export of India as of 2013-14, as per annual report of Ministry of M.S.M.E. This sector is also the leading provider for employment and business avenues in rural and urban India, thereby spurting equitable and inclusive growth across local economies. Yet, the potential of the Indian S.M.Es in creating jobs and livelihood generation opportunities remains untapped. Inadequate access to technology, technical and business skills and finance have been highlighted as some of the key constraints for the M.S.M.Es in the manufacturing sector. The M.S.M.Es primarily relies on bank finance for their operations and as such ensuring timely and adequate flow of credit to the sector has been an overriding public policy objective.

Credit Appraisal means an investigation/assessment done by the banks before providing any Loans & advances/project finance & also checks the commercial, financial & technical viability of the project proposed, its funding pattern & further checks the primary & collateral security cover available for recovery of such funds.

The Need for studying the Credit Appraisal for Working Capital Finance to Small and Medium Enterprises is to ascertain the risks associated with the extension of the credit facility. It is generally carried on by the financial institutions, which are involved in providing financial funding to its customers in order to meet the Financial Gap.Credit risk is a risk related to non-repayment of the credit obtained by the customer of a bank. Thus it is necessary to appraise the credibility of the customer in order to mitigate the credit risk. Proper evaluation of the customer is performed; this measures the financial condition and the ability of the customer to repay back the Loan in future. Generally the credits facilities are extended against the security known as Collateral Security. But even though the Loans are backed by the collateral, banks are normally interested in the actual Loan amount to be repaid along with the interest.

Thus, the customer's cash flows are ascertained to ensure the timely payment of principal and the interest.It is the process of appraising the credit worthiness of a Loan applicant. Factors like age, income, number of dependents, nature of employment, continuity of employment, repayment capacity, previous Loans, credit cards, etc. are taken into account while appraising the creditworthiness of a person. Every bank or lending institution has its own panel of officials for this purpose.

Statement of the Problem:-

To Study the Credit Appraisal for Working Capital Finance to Small and Medium Enterprises in Bank of India. The following steps that are to be analysed are as follows: -

1) To Study & Verify the Borrower's Papers, Documents& Necessary information required.
2) To Study the Financial Tools required for the Credit Appraisal of the Project :
   a) To Study & Verify the Project Report of the Company.
   b) To Study & Analyse the Financial Statements of the Company.
   c) To Verify the Statutory Approvals required for the Project.
3) To Study & Analyse the Working Capital Assessment of the Company.
4) To Study & Analyse the Credit Rating of the Account on the basis of which the Credit Rating Grade is to be provided to the respective Company.

Objectives of the Research:-

Credit appraisal of a term loan denotes evaluating the proposal of the loan to find out repayment capacity of the borrower. The primary objective is to ensure safety of the money of the bank and its customers. The process involves appraisal of market, management, technical, and financial. Getting a term loan from financial institution is not so easy. The corporate asking for the term loan has to go through several tests. The bank follows an extensive process of credit appraisal before sanctioning any loan. It analyses the loan proposal from all angles. The primary objective of credit appraisal is to ensure that the money is given in right hands and the capital and interest income of the bank is relatively secured. While appraising a term loan, a financial institution would focus on evaluating the credit worthiness of the company and future expected stream of cash flow with the amount of risk attached to them. Credit worthiness is assessed with parameters such as willingness of promoters to pay the money back and repayment capacity of the borrower.

Micro, Small and Medium Enterprises (M.S.M.E)

Holistic development of the M.S.M.E sector has been a priority of Government of India due to its significant contribution towards economic growth, employment generation, balanced regional development, overall poverty reduction & emergence as an important vehicle for attaining inclusive growth in the country.Government of India enacted M.S.M.E.D Act 2006 with an aim to enable M.S.M.E entrepreneurs for increasing their worth & efficiency so that they may sustain the competition, enlarge their scope of activity & enlist them among the top performers.

Bank loans above Rs. 5 Crore per borrower/unit to Micro & Small Enterprises engaged in providing or rendering of services, with investment in equipment as defined under M.S.M.E.D Act, 2006 shall not be reckoned while computing achievement under the overall priority sector targets. However, such loans would be reckoned for assessing the performance of the bank with regard to achievement of targets prescribed by the

Prime Minister's Task Force on M.S.M.Es for lending to M.S.E Sector.In terms of the recommendations of the Prime Minister's Task Force on M.S.M.Es, banks have to achieve a 20 percent Year-on-Year growth in credit to Micro & Small Enterprises & a 10 percent Year-on-Year growth in the number of Micro Enterprise accounts.

In order to ensure that sufficient credit is available to Micro Enterprise within the MSE Sector, branches should ensure that:-

a. 40 percent of the total advances to M.S.E sector should go to Micro (Manufacturing) enterprises having investment in plant & machinery up to Rs. 10 Lakhs & Micro (Service) enterprises having investment in equipment up to Rs. 4 Lakhs [say Micro-I].
b. 20 percent of the total advances to M.S.E sector should go to Micro (Manufacturing) enterprises with investment in plant & machinery above Rs. 10 Lakhs & up to Rs. 25 Lakhs, and Micro (Service) enterprises with investment in equipment above Rs. 4 Lakhs & up to Rs. 10 Lakhs [say Micro-II].Thus, 60 percent of M.S.E advances should go to the Micro Enterprises.
c. The target for lending to Micro Enterprises within the M.S.E Sector (i.e. 60% of total lending to MSE Sector should go to Micro enterprises) will be computed with reference to the outstanding credit to MSE Sector as on proceeding March 31st.

Credit Appraisal:-

Proper identification of the enterprises, verification of applicant(s) & his/her/their antecedent in accordance with KYC Norms/Guidelines, their experience in the proposed line of activity, educational & social background, technical/professional competence, integrity, initiatives, etc.

a. Checking out for Wilful Defaulter's List of R.B.I, Specific Approval List (S.A.L) of E.C.G.C, C.I.B.I.L reports individuals as well as commercial etc.
b. The acceptability of the product manufactured its market demand/supply position, market competition, marketing arrangement, etc.
c. Evaluation of State & Central Govt. Policies (enabling environment) with specific reference to the Enterprise in question, Environmental stipulations, availability of necessary infrastructure-roads, power, labour, raw material & markets.
d. Techno-economic Appraisal of units to be carried out as per guidelines circulated by our T.A.D department from time to time. At present it is HOBC 107/46 dated 06.06.2013.
e. Project Cost, the Proponent's own financial contribution, projections for following three years, & other important parameters which would include the Break-Even Point (B.E.P), Liquidity, Solvency & Profitability Ratios, etc.

Credit Tenure: -

The Term Loan exposure to MSME Sector would generally be for a term of 7-10 year maturity, while working capital will be on demand.

Banking Codes & Standard Board Of India (B.C.S.B.I): -

The Banking Codes & Standard Board of India (B.C.S.B.I) has formulated a Code of Bank's Commitment to Micro & Small Enterprises. This is a voluntary Code, which sets minimum standards of banking practices for banks to follow when they are dealing with Micro & Small Enterprises (M.S.Es) as defined in the Micro, Small & Medium Enterprises Development (M.S.M.E.D) Act, 2006. The Code does not replace or supersede regulatory or supervisory instructions issued by the Reserve Bank of India (R.B.I) & banks will comply with such instructions/directions issued by the R.B.I from time to time.

Salient Features Of The Revised Code That Enhance Services Offered To The M.S.M.E Sector: -

The Banks are Committed to: -

a. Display their policies on "Lending to the Micro & Small Enterprises" & "Rehabilitation" of Micro & Small Enterprises on their websites as also make them available at branches.
b. Explain the features of subsidy schemes & any requirement needed to be fulfilled where a loan is eligible to be covered under any such scheme in force.
c. Advise the M.S.E borrower about the functioning of the Central Registry & the fact of availability of their records for search by any lender or any other person desirous of dealing with the property.
d. Give the M.S.E customer the Most Important Terms & Conditions (M.I.T.C) governing the loan/credit facility approved by them & which may be availed by the M.S.E.
e. Dispose of the Loan Application of the M.S.E for a credit limit or enhancement in existing credit limit within the stipulated time frame reckoned from the date of receipt of application, provided the application is complete in all respects & is accompanied by documents as per 'Check List' provided.
f. Not insist on Collateral for credit limits up to Rs. 10 Lakhs or up to limits specified by R.B.I, from time to time.
g. Endeavour to send the M.S.E borrower a communication through letter/mail or S.M.S about the status of his/her account before it becomes a Non-Performing Asset (N.P.A).
h. Give the M.S.M.E borrower notice, sufficiently in advance, if the bank decides to recall/ accelerate payment or performance under the agreement or seek additional securities.

Documentations Required For the Credit Appraisal of A Company: -

For the Purpose of Lending Loans to the Micro, Small and Medium Enterprises (M.S.M.Es) the Bank demands for certain pivotal Papers, Documents and other necessary vital information's which has to be duly submitted by the respective Company, that have applied for both the Term Loan and Working Capital Loan. All these Papers and Documents are to be properlyscrutinized by the bank before allowing the Loan to the respective Company. This is the Initial Step after which the Credit Appraisal Process of the Company Starts.

Check Lists of the Borrower's Papers, Documents & Necessary Information required: -

a. M.S.M.E Application completed in all respects duly signed by all the Directors under Company's seal along with the photographs.
b. CBD-23s in respect of all the Directors and other proposed Guarantors (with all the required enclosures mentioned therein) along with Net Worth certificate by a Chartered Accountant (C.A).
c. Copy of Memorandum of Association (M.O.A) & Article of Association (A.O.A) along with copy of Certificate of Incorporation.

d. Copies of Audited Balance Sheets of the company with (i) 3CA & 3CD (ii) Auditor's Report, as on 31.03.2013, 31.03.2014 & 31.03.2015.
e. Copies of Income Tax Returns of the Company for Financial Years 2011-12, 2012-13 & 20113-14.
f. Copies of Statement of all Accounts of the Company with other Banks/Financial Institutions from 01/04/2014 till date along with copies of Sanction Letters.
g. Profile of the Company, activity being undertaken, address of all offices & plants (along with copies of telephone/electricity bill), manufacturing process, capacity of plant, details about raw material used & their suppliers, details about buyers, details about major competitors & companies, details of present work orders in hand, if any.
h. Bio data of the Directors & key Management Personnel in the company including age, qualification, experience in present activity.
i. Succession Planning, SWOT Analysis, Risks &Mitigants.
j. Detailed Project Report (D.P.R) containing Cost of the Project (C.O.P), Means of Finance (M.O.F), Assets to be acquired along with the details & quotations of Machineries to be acquired (with mention of Schedule of Supply/Erection & Terms of Payment), Calculation of D.S.C.R & Break Even till the last year of repayment of Term Loan, Assumptions & details of Calculation of Sales & Expenses till the last year of repayment of loan to match with the figures in calculation of D.S.C.R & Break Even, Drawdown Schedule, Implementation Schedule, Repayment Schedule of Term Loan.
k. Details about requirement, source & arrangement of power & water.
l. Copy of Approved Site Plan/Factory Plan. Approvals for construction of factory/office building from Municipal Corporation/Local Body etc.
m. Architect's Estimate regarding the proposed building cost (to be vetted by Bank's approved engineer/architect).
n. Details of Technical & Financial Consultants & copies of agreements with the consultants along with the copy of agreement with construction contractor.
o. Details of Group concerns, if any, then copies of their Audited Balance Sheet as on 31.03.2014/31.03.15 along with A.O.A/M.O.A.
p. Copies of P.A.N Card & address proof of all Directors, Proposed Guarantors & Company.
q. C.M.A Data duly signed by the Directors under Company's Seal.
r. Copies of V.A.T & C.S.T registration, M.S.M.E.D registration/Industrial License, N.O.C form Pollution Control Board, Power & Water Sanction Letter.
s. Copies of all relevant licenses, approvals, No Objection Certificate (N.O.C) required for the activity.
t. Details of the Securities offered (Primary & Collateral) along with copies of all the papers pertaining to the properties proposed to be mortgaged along with Location Map Copies.
u. Detailed search from Registrar of Companies evidencing (i) Existing Charges (ii) Authorised Capital (iii) Paid-Up Capital (iv) Share Holding Pattern (v) Details of Directors since Inception-Bank.
v. K.Y.C, Due Diligence in respect of the Company, Directors & Proposed Guarantors to be submitted separately along with the documents listed therein-Bank.
w. Pre-Sanction Inspection Report containing all the information required for the processing of the request-Bank.

x. In case of submission of photocopies of any of the papers & documents, each page of the same is to be verified from the original by the competent official of the branch.

Financial Tools Required For the Credit Appraisal of a Company: -

A. Project Report Of The Company:-

The Project Report of the Company comprises of the following:-

a)Cost of Project (C.O.P) b)Means of Finance (M.O.F),

c)Utility Details of the Project d)Capacity Utilisation of the Project,

e)Project's Implementation & Drawdown Schedule, &f)Repayment Schedule.

B. Financial Statements Of The Company: -

In the Financial Statements, the Bank goes for the following: - Estimation of Sales, Estimation of Profit, Calculation of various types of Ratios (i.e. Ratio Analysis) such as: - the Current Ratio, the Debt-Equity Ratio (D.E.R), the Debt Service Coverage Ratio (D.S.C.R), the Interest Service Coverage Ratio (I.S.C.R) & finally the Calculation of the Break-Even Point (B.E.P).

C. List Of Statutory Approvals Required: -

The following are the list of Statutory Approvals required for the process of Document Scrutinization: - D.I.C (District Industries Centre) Registration Approval, Obtain various necessary N.O.Cs (No Objection Certificates) and clearances from regulatory bodies such as Pollution Control Board (P.C.B), Labour Regulations, Obtain facilities for accommodation & land, B.D.A/C.D.A/Gram Panchayat N.O.Cs, V.A.T Registration No., P.A.N Card, Power Supply Approval, Other approvals, etc.

Note: - After the Document Scrutinization of the above Financial Tools, the bank goes for the Working Capital Assessment of the Company followed by the Credit Rating of the Account.

Working Capital Assessment: -

The "Working Capital Assessment" refers to the day-to-day expenses required for the proper functioning of an organisation. Here, the Bank goes for the assessment of Working Capital of the Company in order to know whether the Loan amount proposed by the respective Company is Acceptable or not.

The following tools required for the Assessment of the Working Capital are: -"the Holding Period" (otherwise known as "the Operating Cycle Time-period") & the various methods of Working Capital Assessment are: "Turnover Method"&"Second Method of Lending" (otherwise known as "the Maximum Permissible Bank Finance Method" (M.P.B.F)).

Holding Period: - It refers to the time between an Assets Purchase & its Sales. It is otherwise known as "Operating Cycle Time-period".

Credit Rating of the Account: -

In case of the "Credit Rating of the Account", the Bank takes the following Scores into consideration: -

(a)Financial Risk Scores (b)Management Risk Scores,(c)Business/Industry Risk Scores.

And after adding all these above scores i.e. the "Final Risk Score" is taken into consideration on the basis of which the "Credit Rating Grade" is given to the respective Company.

Note: -The following formulae are to be taken care of while calculating the Financial Risk Scores: -

- $\mathbf{SALESGROWTH} = \left[\frac{\mathbf{NETSALESINCURRENTYEAR}}{\mathbf{NETSALESINPREVIOUSYEAR}} - \mathbf{1}\right] \times \mathbf{100}$
- $\mathbf{PROFITABILITY} = \left[\frac{\mathbf{P.B.I.D.T.A}}{\mathbf{NETSALES}}\right] \times \mathbf{100}$
- $\mathbf{PROFITABILITY} = \frac{\mathbf{OPERATINGPROFITBEFOREINTEREST+DEPRECIATION+AMORTIZATION+TAXATION}}{\mathbf{NETSALES}} \times \mathbf{100}$
- $\mathbf{LEVERAGE\ (or, Debt - EquityRatio)} = \frac{\mathbf{TOTALOUTSIDELIABILITIES\ (T.O.L)}}{\mathbf{TANGIBLENETWORTH\ (T.N.W)}}$
- $\mathbf{D.S.C.R} = \frac{\mathbf{(NETPROFIT+INTEREST+DEPRECIATION+AMORTIZATION)}}{\mathbf{(CURRENTPORTIONOFLONGTERMDEBT+INTEREST)}}$
- $\mathbf{LIQUIDITY(or, CurrentRatio)} = \frac{\mathbf{CURRENTASSETS}}{\mathbf{CURRENTLIABILITIES}}$
- $\mathbf{I.S.C.R} = \frac{\mathbf{PROFITBEFORETAX+INTEREST+DEPRECIATION+AMORTIZATION}}{\mathbf{INTERESTCOST}}$

A. **Financial Risk Score:-**

Parameters	Measures	Score	Assigned Score (a)	Weight (b)	Total Score (a × b)
1. Sales Growth	15% & above increase over previous year	1		4	
	5% & above but below 15% increase over previous year	2			
	0% & above but below 5% increase over previous year	3			
	Negative over previous year	4			
2. Profitability	25% & above increase over previous year	1		4	
	15% & above but below 25% increase over previous year	2			
	0% & above but below 15% increase over previous year	3			
	Negative over previous year	4			
3. Liquidity	1.50 & above	1		4	
	1.33 & above but below 1.50	2			
	1.00 & above but below 1.33	3			
	Below 1.00	4			
4. Leverage	0.00 above but below 1.00	1		4	
	1.00 & above but below 3.00	2			
	3.00 & above but below 4.00	3			
	4.00 & above	4			
5. Coverage					
a. Debt Service Coverage Ratio (D.S.C.R)	2.00 & above	1			
	1.50 & above but below 2.00	2			
	1.00 & above but below 1.50	3			
	-1.00 & above but below 1.00	4		4	
b. Interest Service Coverage Ratio (I.S.C.R)	2.00 & above	1		4	
	1.50 & above but below 2.00	2			
	1.00 & above but below 1.50	3			
	-1.00 & above but below 1.00	4			
SUB-TOTAL OF FINANCIAL RISK SCORE (1 to 5)			**xxxxxxx**	**xxxxxxx**	

B. **Management risk Score: -**

1. **Management character Score: -**

Parameters	Measures	Score	Assigned Score (a)	Weight (b)	Total Score (a × b)
1. Diversion of Funds	There is no possibility of diversion of funds & there are no group companies.	1		4	
	Diversion of funds is unlikely, though there are group entities marginal amounts may be diverted for personal use.	2			
	Diversion of funds is likely on a regular basis to group entities & for personal use.	3			
	The borrowing entity is only a front for diversion.	4			
2. Integrity	Well-established member of the community whose integrity is unquestionable.	1		4	
	Generally respected by peers & by the community.	2			
	Does not always act in an upright & honest manner.	3			
	Should repayment capacity be impaired, management may not co-operate with lender or no information could be obtained about management's integrity.	4			
3. Business Commitment	Promoter is highly involved in this business, has long standing.	1		4	
	Promoter is fairly committed to this business.	2			
	This business occupies only a small portion of his time & investment & his most significant business interest lies elsewhere.	3			
	No involvement by the promoter; business merely a legacy or promoter diversifying into other areas where his involvement will increase in future or unable to gauge commitment.	4			
SUB-TOTAL OF MANAGEMENT CHARACTER SCORE (1 to 3)			**xxxxxxx**	**xxxxxxx**	

2. Management Capacity Score:-

Parameters	Measures	Score	Assigned Score (a)	Weight (b)	Total Score (a × b)
1. Financial Strength	Financially very strong; high net worth & flourishing group entities.	1		4	
	Good Financial strength; minor group entity may not be doing well.	2			
	Financial strength is OK; however poor group entity could have an impact.	3			
	Very poor financials or financial strength could not be ascertained.	4			
2. Competence	Management is very good. Person is well organised & knowledgeable about the company & the industry in which he operates.	1		2	
	Person has reasonable management skills but weakness in one or two areas is evident. Tasks are performed satisfactorily.	2			
	Person exhibits limited managerial skills. Individual does not have a complete understanding of the business.	3			
	Person exhibits a total lack of skill. Decisions are illogical & loan repayment could be at risk.	4			
3. Business Experience	Several years of sound business experience in the same line & extremely successful.	1		2	
	Fairly long experience in the same line of business with limited success.	2			
	Fair experience but in related line of business.	3			
	Very short or no experience in any business.	4			
4. Internal Controls	Internal control is fairly good & is dependent on the owner's long standing relationship with his employees.	1		2	
	Internal control is not very tight & employees have too much discretion.	2			
	Internal control is totally dependent on the owner's presence in the business location & his personal supervision.	3			

	No internal control at all – the owner does not have a clue to what is happening.	4			
5. Employee Quality	Motivated & loyal employees who have a sound understanding of the business.	1		2	
	Employees are loyal but do not have much experience.	2			
	Employees are not motivated & do not contribute their best.	3			
	Employees are neither motivated nor competent.	4			
SUB-TOTAL OF MANAGEMENT CAPACITY SCORE (1 to 5)			**xxxxxxx**	**xxxxxxx**	

3. Management succession score: -

Parameters	Measures	Score	Assigned Score (a)	Weight (b)	Total Score (a × b)
1. Successor Identification	Well-defined succession plan in place; business not dependent on one person.	1		4	
	Business dependent on one person at present, but in the event of incapacitation of that person a good succession plan in place.	2			
	Succession is not addressed adequately & hence dealing with a change in the management team could adversely affect the company's performance; however the damages can be contained.	3			
	Succession has not been addressed & in the event of incapacitation of the key person, the business would suffer financial setbacks.	4			
2. Successor Preparedness	Successors have far more than the necessary skills, experience & knowledge about the business.	1		4	
	Successors have adequate skills, experience & knowledge about the business even though there would be some learning & adjustment needed to be fully capable of replacing current management.	2			
	Successors have some skills & knowledge about the business but a lot of learning & adjustment needed to be fully capable of replacing current management.	3			
	Successors are poorly prepared for assuming the role of current management & are not currently, nor could they be made capable of replacing current management.	4			
SUB-TOTAL OF MANAGEMENT SUCCESSION SCORE (1 to 2)			xxxxxxx	xxxxxxx	

1. Management Reputation Score: -

Parameters	Measures	Score	Assigned Score (a)	Weight (b)	Total Score ($a \times b$)
1. Business Loan History	Obligations to creditors are met before or within agreed terms.	1		4	
	Payments have extended beyond agreed upon terms on an infrequent basis.	2			
	Often borrower allows bills to extend 60-90 days beyond payment date.	3			
	Credit checks indicate the borrower is consistently late, without cause, in paying its suppliers or information could not be obtained on how the borrower handles its payment responsibilities.	4			
2. Credit Track Record	Company has never violated any term & condition of its loan agreement.	1		4	
	Company rarely does not meet all terms & conditions of its loan agreement.	2			
	Now & then the Company breaches a significant term or condition of the credit agreement.	3			
	Company consistently violates loan agreement covenants.	4			
3. Firm's Age	Firm in existence for more than 10 years.	1		8	
	Firm in existence for more than 5 years.	2			
	Firm in existence for more than 2 years.	3			
	Firm in existence for less than 2 years.	4			
4. Reputation with Customer &	Excellent relationship with suppliers with no supplies. Excellent reputation with customers resulting in growth & timely payments.	1		4	

suppliers	Good relationship with suppliers with some disruption of supplies. Good reputation with customers resulting in growth & generally timely payments.	2			
	Fair relationship with suppliers with frequent disruption of supplies. Fair reputation with customers but increase in credit period & some defaults.	3			
	Poor relationship with suppliers. Poor reputation with customers with substantial increase in credit period & high defaults.	4			
SUB-TOTAL OF MANAGEMENT REPUTATION SCORE (1 to 4)			**xxxxxxx**	**xxxxxxx**	
SUB-TOTAL OF MANAGEMENT RISK SCORE (B1 to B4)			**xxxxxxx**	**xxxxxxx**	

C. **Business/Industry Risk Score: -**

Parameters	Measures	Score	Assigned Score (a)	Weight (b)	Total Score ($a \times b$)
1. Customer Quality & Concentration	Diversified customer base having reasonable size, stable purchase pattern from the firm & likely to pay outstanding invoices on a timely basis.	1		4	
	Generally diversified customer base who may not have either a reasonable size or a stable purchase pattern from the firm but is likely to pay outstanding invoices on a timely basis. There may be a few large customers.	2			
	Customer has neither reasonable size nor a stable purchase pattern from the firm but is likely to pay outstanding invoices on a timely basis. The firm may have only a few customers with little product diversification.	3			
	Customers are not expected to pay on time. The firm may have only 1-2 customers.	4			
2. Supplier Quality & Concentration	Firm has a choice of suppliers supplying quality goods & services.	1		4	
	Firm has a choice of suppliers supplying average quality goods & services.	2			
	Firm has very few suppliers supplying goods & services. Quality of goods & services is not very good.	3			
	Monopsonistic situation with no control over quality.	4			
3. Impact of Competition on G.P. Margins	Current industry structure not expected to lead to decline in G.P. Margin.	1		4	
	Industry competition may result in marginal decline in margins.	2			

	Industry competition has resulted/may result in significant decline in margins.	3			
	G.P. Margins have declined significantly due to competition & expected to decline further.	4			
4. Sales Trend (Product)	Product has no substitutes, regulatory threats demand will remain stable or grow.	1		4	
	Product has limited substitutes (other brands or other products) & regulatory threats; however, this will not pose a threat to the borrower.	2			
	Demand for product may be affected by lower-price substitutes & regulation; however the threat is unlikely.	3			
	Demand faces serious threat due to substitutes & regulation.	4			
5. Technology Dependence (Product)	Technology is tested & not expected to change in the long run.	1		2	
	Technology is tested & unlikely to change in the medium term.	2			
	Technology is tested but likely to change in the medium term.	3			
	Obsolete technology or technology subject to very fast obsolescence or technology as yet untried/untested.	4			
6. Regulatory/Fiscal risk impact of duties	There are no foreseen changes in the direct/indirect tax structure or import/export restrictions which could impact the industry profitability.	1		4	
	While some changes in the direct/indirect tax structure or import/export restrictions which impact the industry are foreseen, these may have some impact on industry profitability.	2			
	Some changes are foreseen in the direct/indirect tax structure or import/export restrictions which	3			

	impact the industry. These may have a major impact on industry profitability & affect viability of marginal players.				
	Significant changes are foreseen in the direct/indirect tax structure and/or import/export restrictions which impact the industry. These may have a significant impact on industry profitability & viability of players.	4			
7. Environmental Impact (Product)	Unlikely to face pollution related problems in future.	1		2	
	Limited likelihood of facing pollution related problems in future.	2			
	Polluting industry but companies with current norms which are subject to change.	3			
	Polluting industry & does not comply current norms.	4			
SUB-TOTAL OF BUSINESS/INDUSTRY RISK SCORE (1 to 7)			**xxxxxxx**	**xxxxxxx**	

Customer Rating Score:-

SL.NO.	ITEMS	SCORES
A	Financial Risk Score	
B	Management Risk Score	
C	Business/Industry Risk Score	
FINAL RISK SCORE (A+B+C)		
CREDIT RATING GRADE BASED ON FINAL RISK SCORE		

Note: - "For Credit limits from Rs. 10 lakhs to Rs. 5 Crores", the Credit Rating of the Account is done through "Small Business Segment (S.B.S) Model" where the "Rate of Interest" will be applicable (to Small & Medium Enterprises) as per the following table:

TABLE-1 : Limits From Rs. 10 Lakhs to <Rs. 1 Crore		
Credit Rating	**Existing**	**Proposed**
SBS-1	12.80	12.65
SBS-2	12.80	12.65
SBS-3	12.85	12.75
SBS-4	12.85	12.75
SBS-5	13.10	13.00
SBS-6	13.40	13.35
SBS-7	13.90	13.85
SBS-8	15.45	15.45
SBS-9	15.45	15.45
SBS-10	15.45	15.45

TABLE-2 : Limits From Rs. 1 Crore to <Rs. 5 Crores		
Credit Rating	**Existing**	**Proposed**
SBS-1 to 2	13.30	13.15
SBS-3	13.35	13.25
SBS-4	13.85	13.75
SBS-5	14.35	14.25
SBS-6	14.40	14.35
SBS-7	14.40	14.35
SBS-8 to 10	15.45	15.45

Note: -"For Credit limits less than Rs. 10 lakhs", the Credit Rating of the Account is done through "Web Based Model" where the "Rate of Interest" will be applicable (to Small & Medium Enterprises) as per the following table: -

TABLE : Limits <Rs. 10 Lakhs (Small Enterprise)		
Sanctioned Limit	**Existing**	**Proposed**
< 50000	10.70	10.45
50000 to < 2 Lakhs	11.70	11.45
2 Lakhs to < 10 Lakhs	12.70	12.45

Overall Credit Rating Grade – "Through S.B.S Model": -

FINANCIAL RISK		MANAGEMENT RISK		BUSINESS/ INDUSTRY RISK		CUSTOMER RATING (Based on Final Risk Score)	
Financial Risk Score (A)	**Financial Rating**	**Mgmt. Risk Score (B)**	**Mgmt. Rating**	**Business or Industry Risk Score (C)**	**Business or Industry Rating**	**Final Risk Score (A+B+C)**	**Credit Rating Grade**
0 to 28	1	0 to 51	1	0	1	0	**SBS-1**
29 to 33	2	52 to 77	2	24	2	120	**SBS-2**
34 to 37	3	78 to 103	3	36	3	140	**SBS-3**
38 to 42	4	104 to 120	4	48	4	160	**SBS-4**
43 to 50	5	121 to 138	5	56	5	180	**SBS-5**
51 to 58	6	139 to 155	6	64	6	213	**SBS-6**
59 to 63	7	156 to 172	7	72	7	247	**SBS-7**
64 to 68	8	173 to 190	8	80	8	268	**SBS-8**
69 to 95	9	191 to 207	9	88	9	287	**SBS-9**
96	10	208	10	96	10	400	**SBS-10**

Note: -"S.B.S – 5 Rating" is otherwise known as "the Entry Level Rating".

Data Analysis

Type of Research: -

Here, the Type of Research is both Descriptive and Analytical.

It is Descriptive as the Project deals with various theories regarding the Bank of India's (B.O.I's) Credit Policy (which includes both the Credit Lending and Credit Rating Policies) while providing the Term Loan to the Micro, Small and Medium Enterprises (M.S.M.E) and also regarding the various ways of assessing the Working Capital Finance to the Micro, Small and Medium Enterprises (M.S.M.E).And it is Analytical as the Project deals with the Study and Analysis of the Sales Estimation, the Ratio Analysis, the Break-Even Point Calculation, the Working Capital Assessment and finally, the Credit Rating of the Account on the basis of which the Credit will be appraised by the bank for providing the Working Capital Finance to Micro, Small and Medium Enterprises (M.S.M.E).

Data Collection: -

Here, the data collected is both from the Primary Source as well as from the Secondary Source, so the Data Collection is both Primary and Secondary Data. Primary Data as the information's are collected directly from the Banker and Secondary Data as the Project is referred from various Books, Bank of India's (B.O.I's) Website and Customer files at B.O.I.

Software Used For Data Analysis: -

Here, the Software Used for Data Analysis is: - Microsoft Excel (M.S. EXCEL) Version-2013.

Data Presentation: -

Here, the Presentation of Data's includes: Brief Introduction regarding the ABC Limited Cashew Processing Unit, the Company's C.M.A Data and Financial Projections in the form of Excel Sheet. It also includes the Calculation of Sales Estimation, Calculation of various Ratios (Current Ratio, Debt-Equity Ratio and Debt Service Coverage Ratio), Calculation of BreakEven Point, Calculation of Working Capital Assessment and finally the Calculation of Credit Rating of the Account.

Brief Introduction of the Firm: -

The Firm is a sister concern of M/s. A.B.C Pvt. Ltd. M/s A.B.C Industries is a Proprietorship concern owned by Mr. XYZ who is also a Promoter Director in A.B.C Pvt. Ltd. The Main Objective of the Firm is Processing of Cashew Nut to produce Quality Cashew. The Main Aim of the Govt. Policy is to increase the flow of investments across the supply chain from farm to market, increase the value addition and reduce wastage of farm production and increase the income of farmers. There are very few local competitors to face in the eastern region. So, the Company can get good exposure over the Eastern Zone Market.

The Company has requested for Credit Facilities of Rs. 99.50 Lakhs for Division-1 (Cashew Processing Unit) which consists of Term Loan of Rs. 57 Lakhs and Working Capital Loan of Rs. 42.50 Lakhs.

The Company has submitted herewith the Complete Project Report along with the Projected C.M.A Data and other requisite information/documents. The Company expects a maximum Rate of Interest on above Credit Facilities to be availed to them as follows: -

a. Credit Limit – 12.50% (If needed, the bank will allow interest concession of 1% as applicable).

b. Term Loan – 12.50% (rate, being an Agro-Based Manufacturing Unit).

Coverage under C.G.T.M.S.E Scheme: - Adequate Principal Security will be created after availment of proposed bank loan. However, since presently the Firm is not in a position to offer any Collateral Security, the Firm requests the Bank to cover their proposed Credit Facility under C.G.T.M.S.E Scheme. The Firm agrees to abide by the terms and conditions of above scheme.

Products and Services: - The Firm has the following Products and Services: - Whole Cashew Nuts, Broken Cashew Nuts, Small Bits and Letting out Godown.

Availability of Raw Material: - The only Raw Material required will be Cashew Fruits.

Capacity and Production: - Here, the Installed Capacity is 750 Kg per Day, No. of Working Days is 300 and Working Hour per Day is 8 hours.

Here, the Repayment Period is in 28 Quarterly Instalments, Loan Duration is 96 Months and Total No. of Instalments is 84 Nos.

The Input-Output Ratio is 4:1. The Firm has presently considered the Selling Price of Rs. 450 per kg, Rs. 250 per kg and Rs. 175 per kg of Whole Cashew Kernels, Broken Cashews and Small Bits respectively.

Note: - The Firm has Projected to start its operations from the month of July, 2015, hence, Firm will be operating for 9 months during next F.Y. 2016-17 and F.Y. 2017-18 will be Firm's first full year of operations.

Calculation of Financial Tools: -

A. Calculation Of Sales Estimation: -

We know that, from the D.I.C. Registration Report;

Installed Capacity (In KG's Per Day) ---------750 kg/day

No. of Days of Working-------------------------300.00

No. of Working Hours---------------------------8.00

Total Installed Capacity per Annum----------- (750×300) = 225000 kg p.a.

Now, for 2016, the Bank has proposed an Utilisation Capacity of 60%.

I.e. 60% of 225000 kg p.a. = 135000 kg p.a.

Since the No. of Working Months for 2016 is 9 Months, thus for 9 Months the Annual Production in Kg's becomes = 135000× (9/12) = 101250 kg p.a.

Now, the Industry says;

No. of Days for Work in Progress is 4.

No. of Months of Finished Goods is 0.5.

Calculation of Closing Stock of Work-in-Progress (in 2016): -

$$\textbf{Closing Stock of Work} - \textbf{in} - \textbf{Progress} = \frac{\textbf{Annual Production} \times \textbf{No.of days for W.i.p}}{\textbf{No.of days worked}}$$

That implies, C.S. of W.I.P $=\frac{101250 \times 4}{300}=$ 1,350 kg.

Calculation of Closing Stock of Finished Goods (in 2016): -

$$\textbf{Closing Stock of Finished Goods} = \frac{\textbf{Annual Production} \times \textbf{No.of months for Finished goods}}{\textbf{12}}$$

That implies, C.S. of F.G. $=\frac{101250 \times 0.5}{12}=$ 4,219 kg.

Thus, Annual Sales Production for 2016 = (101250 – 1350 - 4219) = 95,681 Kg P.a.

Calculation of Total Sales (in 2016): -

The Ideal Industrial Production is in the Ratio of 4:1.

(I.e. If 100 pieces of Input items are given then the Output items obtained will be only of 25 pieces, which is in the Ratio of 4:1).

Now,

Selling Price/Kg and % of Total Production of: -

Whole Cashew Kernels (Qty in KGs) ------- 450.00 70.00%

Broken Cashews (Qty in KGs) ----------------250.00 20.00%

Small Bits (Qty in KGs) ------------------------175.00 10.00%, respectively.

Then,

Amount of Whole Cashew Kernels Produced = (70% of 95,681) = 66,977 kg p.a.

Amount of Broken Cashews Produced = (20% of 95,681) = 19,136 kg p.a.

Amount of Small Bits Produced = (10% of 95,681) = 9,568 kg p.a.

We know that,

Selling Price of 1 kg of Whole Cashew Kernels = Rs. 450/-

Then, Selling Price of 66,977 kg of Whole Cashew Kernels = Rs. (450×66,977) = Rs. 301.3965 Lakhs. -------Equn. (1)

Similarly,

S.P. of 1 kg of Broken Cashews = Rs. 250/-

Then, S.P. of 19,136 kg of Broken Cashews = Rs. (250×19,136) = Rs. 47.84 Lakhs--Equn. (2)

Lastly,

S.P. of 1 kg of Small Bits = Rs. 175/-

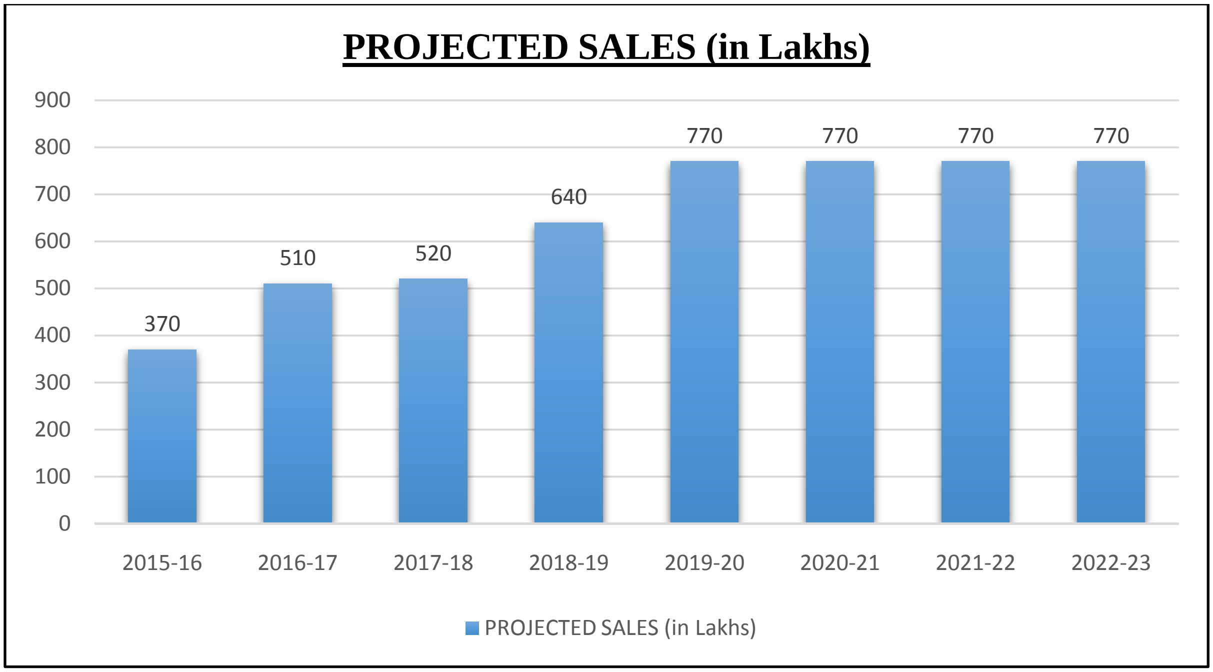
Then, S.P. of 9,568 kg of Small Bits = Rs. (175×9,568) = Rs. 16.744 Lakhs. ---Equn. (3)

Thus, Adding Equn. (1) + (2) + (3), we get: -

Total Sales = Rs. (301.3965+47.84+16.744) Lakhs = Rs. 365.98 Lakhs = **Rs. 370 Lakhs** (Rounded off).

Similarly in this way, the Projected Sales figures for 2017, 2018, 2019, 2020, 2021, 2022, and 2023 are found out to be: **Rs. 510 Lakhs**, **Rs. 520 Lakhs**, **Rs. 640 Lakhs**, **Rs. 770 Lakhs**, **Rs. 770 Lakhs**, **Rs. 770 Lakhs** and **Rs. 770 Lakhs** respectively.

Note: - Similarly, the Sales Estimation for the Simultaneous (Projected) Years are calculated in the same manner.



B. CALCULATION OF CURRENT RATIO: -

We know,

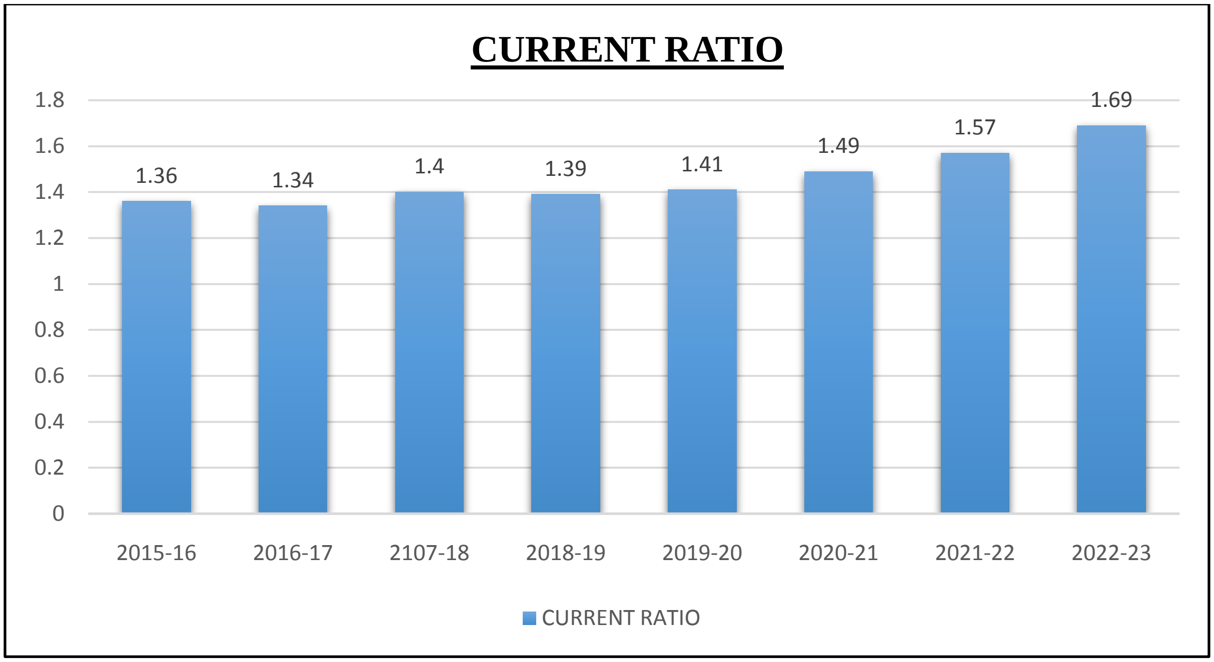
$$\textbf{Current Ratio} = \frac{\textbf{Current Assets}}{\textbf{Current Liabilities}}$$

Particulars	2015-16	2016-17	2017-18	2018-19	2019-20	2020-21	2021-22	2022-23
Total Current Assets (A)	137.38	186.33	197.52	239.33	274.33	280.89	292.26	306.02
Total Current Liabilities (B)	100.74	139.42	141.04	172.02	194.30	188.90	186.20	180.86
Current Ratio $(\frac{A}{B})$	**1.36**	**1.34**	**1.40**	**1.39**	**1.41**	**1.49**	**1.57**	**1.69**

Note: -Here, According to the C.M.A. Report, the respective Company's: -

a. Total Current Assets = (Inventory + Cash & Bank Balances + Receivables + Other Current Assets).

b. Total Current Liabilities = (Bank Borrowings + Creditors + Provisions + Other Statutory Liabilities + Other Current Liabilities).



C. CALCULATION OF DEBT-EQUITY RATIO (D.E.R): -

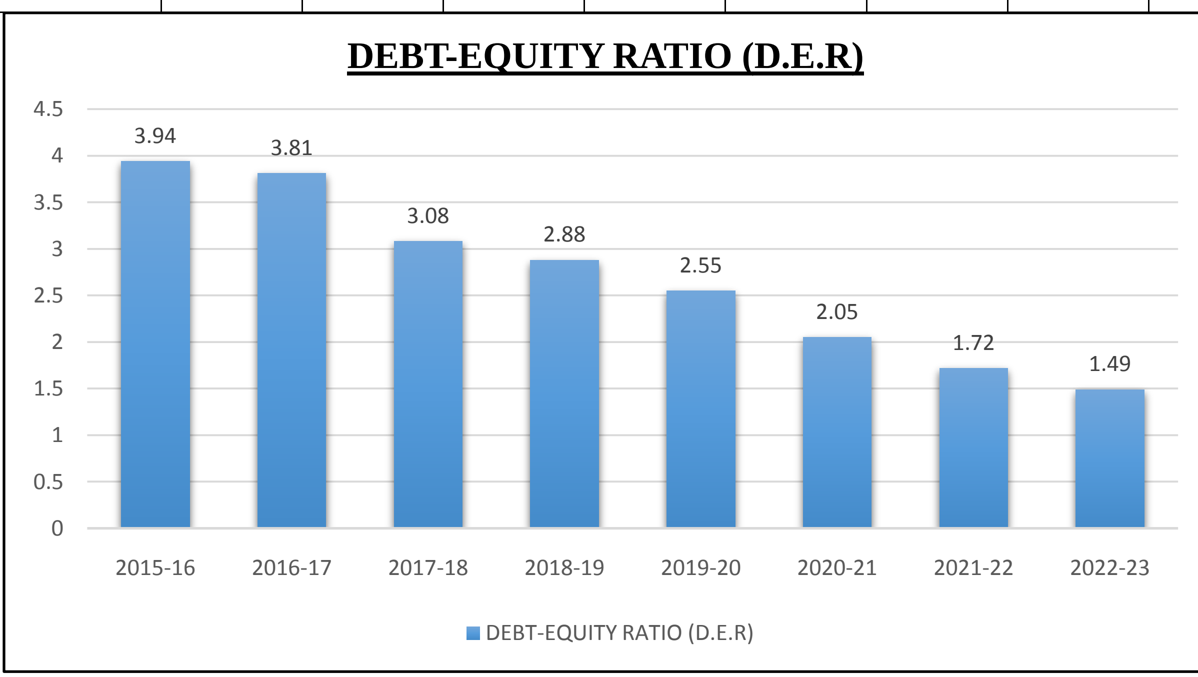
We know,

$$\text{DEBT} - \text{EQUITY RATIO} = \frac{\text{TOTAL OUTSIDER'S LIABILITIES (T.O.L)}}{\text{TANGIBLE NET WORTH (T.N.W)}}$$

Or, $$\text{D.E.R} = \frac{\text{TOTAL CURRENT LIABILITIES+TOTAL TERM LIABILITIES}}{\text{TANGIBLE NET WORTH}}$$

Note: -Here, "Total Term Liabilities" is otherwise known as: - "the Total Loans".

Particulars	2015-16	2016-17	2017-18	2018-19	2019-20	2020-21	2021-22	2022-23
Total Loans (1)	66.14	58.00	49.86	41.71	33.57	25.43	20.00	20.00
Total Current Liabilities (2)	100.74	139.42	141.04	172.02	194.30	188.90	186.20	180.86
Total Outsider's Liabilities (T.O.L) (1+2)= (A)	166.88	197.42	190.9	213.73	227.87	214.33	206.2	200.86
Tangible Net Worth (T.N.W) (B)	42.31	51.88	61.94	74.29	89.40	104.51	119.67	135.01
Debt-Equity Ratio ($\frac{A}{B}$)	**3.94**	**3.81**	**3.08**	**2.88**	**2.55**	**2.05**	**1.72**	**1.49**

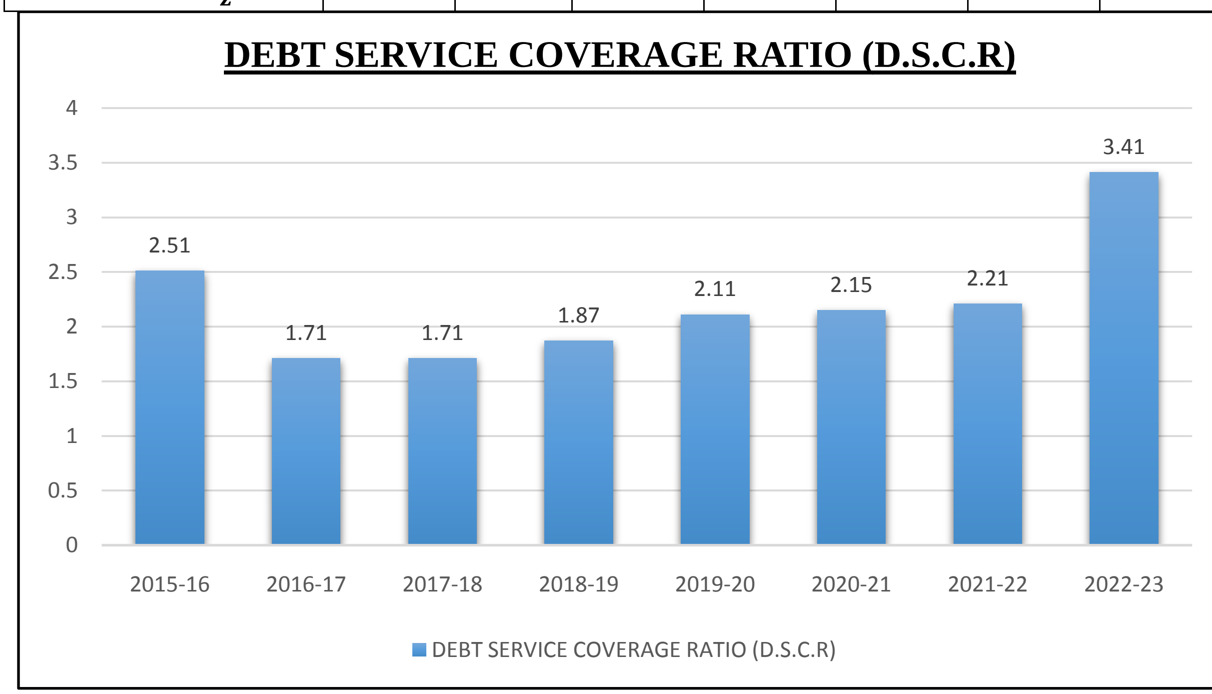


D. CALCULATION OF DEBT SERVICE COVERAGE RATIO (D.S.C.R): -

We know,

$$\text{D.S.C.R} = \frac{\text{Profit After Tax} + \text{Depreciation} + \text{Interest for the Current year}}{\text{Instalment} + \text{Interest}}$$

Particulars	2015-16	2016-17	2017-18	2018-19	2019-20	2020-21	2021-22	2022-23
Profit After Tax (A)	6.92	9.57	10.06	12.35	15.11	15.11	15.15	15.34
Depreciation (B)	10.21	8.84	7.65	6.63	5.75	4.99	4.33	3.77
Interest (on Term Loan) (C)	6.82	6.32	5.30	4.28	3.27	2.25	1.23	0.25
Total (A+B+C) = (D)	23.96	24.73	23.01	23.27	24.13	22.35	20.72	19.36
Interest (on Term Loan) (X)	6.82	6.32	5.30	4.28	3.27	2.25	1.23	0.25
Instalment (of Term Loan) (Y)	2.71	8.14	8.14	8.14	8.14	8.14	8.14	5.43
Total (X+Y) = (Z)	9.54	14.46	13.44	12.43	11.41	10.39	9.37	5.68
D.S.C.R ($\frac{D}{Z}$)	**2.51**	**1.71**	**1.71**	**1.87**	**2.11**	**2.15**	**2.21**	**3.41**



E. CALCULATION OF BREAK-EVEN POINT (B.E.P): -

We know,

- $\mathbf{CONTRIBUTION = TOTAL\ REVENUE - VARIABLE\ COST = FIXED\ COST + PROFIT}$
- $\mathbf{\frac{PROFIT}{VOLUME} RATIO = \frac{TOTAL\ REVENUE - VARIABLE\ COST}{TOTAL\ REVENUE} \times 100}$
- $\mathbf{BREAK-EVEN\ SALES\ (in\ Rs.) = \frac{FIXED\ COST}{SALES - VARIABLE\ COST} \times SALES}$
- $\mathbf{BREAK-EVEN\ POINT\ (in\ \%ge) = \frac{FIXED\ COST}{TOTAL\ CONTRIBUTION} \times 100}$
- $\mathbf{BREAK-EVEN\ POINT\ (in\ \%ge) = \frac{BREAK-EVEN\ SALES\ (in\ Rs.)}{100\%\ CAPACITY\ SALES} \times 100}$

Particulars	2015-16	2016-17	2017-18	2018-19	2019-20	2020-21	2021-22
Capacity Utilisation (in %)	60%	60%	60%	75%	90%	90%	90%
Total Revenue (or, Sales) (A)	370	510	520	640	770	770	770
Variable Cost (B)	327.54	370.42	352.93	464.50	556.54	531.10	531.94
Contribution (A-B)	42.46	139.58	167.07	175.50	213.46	238.90	238.06
Fixed Cost (C)	32.44	125.73	152.51	157.63	191.59	217.03	216.13
P/V Ratio $(\frac{A-B}{A} \times 100)$	11.48	27.37	32.13	27.42	27.72	31.03	30.92
Break-Even Point (in Rs. Lakhs) $(\frac{C}{A-B} \times A)$ **(or, Break-Even Sales)**	**282.68**	**459.38**	**474.68**	**574.82**	**691.12**	**699.51**	**699.07**
Break-Even Point (in %) $(\frac{Break-Even\ Sales}{100\ \%\ Capacity\ Sales}) \times 100$	**46%**	**54%**	**55%**	**67%**	**81%**	**82%**	**82%**

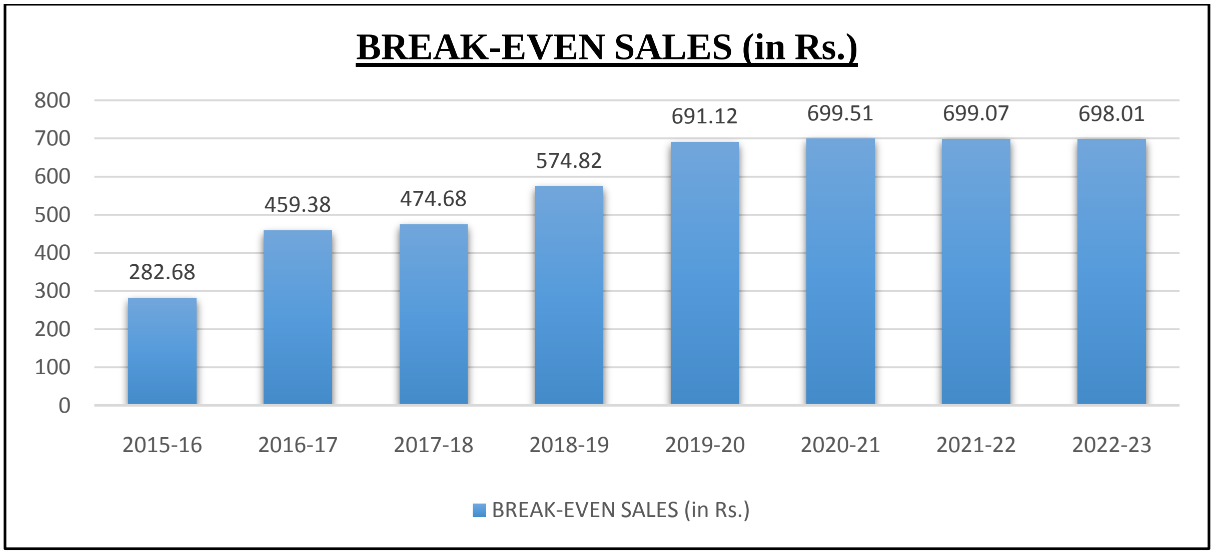
Note: -For 2016, 60% Capacity Sales = Rs. 370 Lakhs.

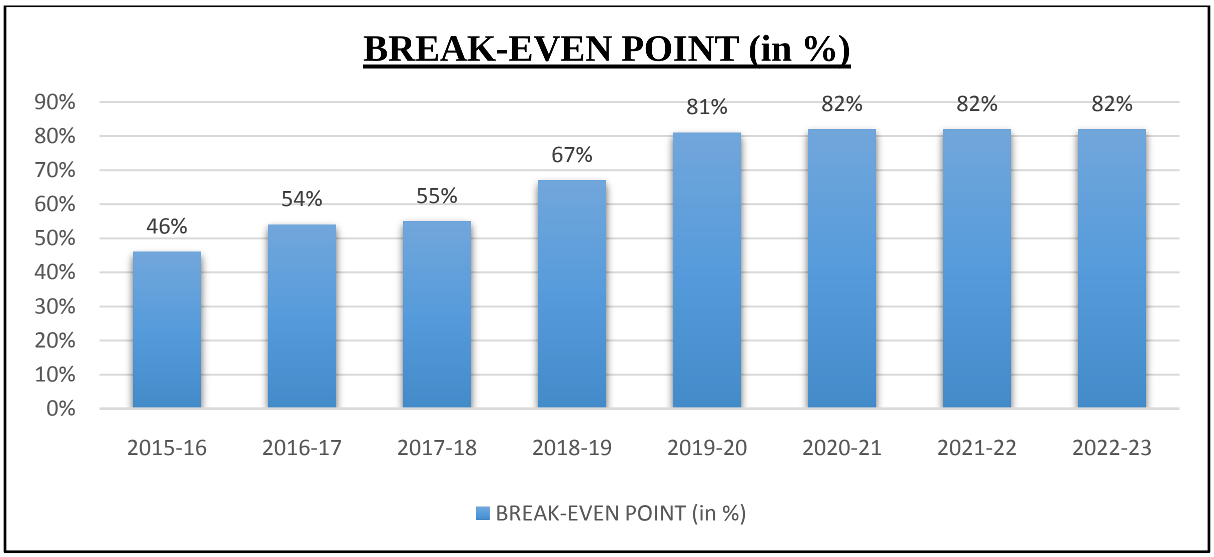
Then For 100% Capacity Sales = [(Rs. 370 Lakhs)/60] ×100 = Rs. 616.66 Lakhs.

Thus, the **Break-Even Point (in %)** = [(Rs. 282.68 Lakhs)/ (Rs. 616.66 Lakhs)] ×100

= 45.84 % = **46 %** (Rounded-off).

Similarly, the Break-Even Point (in %) has been calculated for the rest of the Projected Years. For 2017, 2018, 2019, 2020, 2021, 2022 and 2023 the Break-Even Point (in %) are: **54 %**, **55 %**, **67 %**, **81 %**, **82 %**, **82 %** and **82 %** respectively.





F. Calculation Of Working Capital Assessment: -

In order to meet its Working Capital requirements & day-to-day expenses, the firm has requested for fund based working capital (cash credit) limit of Rs. 42.50 Lakhs for Fiscal Year 2015-16 (9 months working) & Fiscal Year 2016-17 (first full year of operations) based on estimated & projected sales of Rs. 370 Lakhs &Rs. 510 Lakhs, which appears to be reasonable as per the bank.

Accordingly, the bank has carried out the Fund-Based Working Capital (F.B.W.C) Assessment based on the estimated & projected inventory, receivables & creditors levels (on the basis of C.M.A data submitted by the firm) as under: -

CURRENT ASSETS	Projection 31.03.2016 (**) (in Lakhs)	Projection 31.03.2017 (in Lakhs)
Raw Materials including stores, spares, consumables & other items included in the process of manufacturing (Rs. in Lakhs)	89.00	118.00
Raw Material Consumed (Rs. in Lakhs)	301.00	401.00
Raw Material Holding Period (in months)	**2.66**	**3.53**
Stock in Process (Rs. in Lakhs)	5.00	6.00
Cost of Production (Rs. in Lakhs)	340.46	454.54
Stock in Process Holding Period (in months)	**0.13**	**0.16**
Finished Goods (Rs. in Lakhs)	15.00	19.00
Cost of Sales (Rs. in Lakhs)	325.46	450.54
Finished Goods Holding Period (in months)	**0.41**	**0.51**
Receivables other than export & deferred receivables (Rs. in Lakhs)	25.00	34.00
Domestic Sales: excluding Deferred Payment Sales (Rs. in Lakhs)	370.00	510.00
Receivables Holding Period (in months)	**0.61**	**0.80**
CURRENT LIABILITIES		
Creditors for purchase of raw materials, stores & consumable spares (Rs. in Lakhs)	39.00	64.50
Purchase of Raw Materials, Stores & Consumable Spares	390.00	430.00
Creditor's Holding Period (in months)	**0.90**	**1.80**
Operating Cycle in months	**2.92**	**3.20**
(**) for 9 months of operations		

The various formulae used for the "Calculation of Operating Cycle or Holding Period in months" are as follows: -

- $\mathbf{R.M.H.P(in\ months) = \frac{COST\ OF\ RAW\ MATERIALS}{COST\ OF\ RAW\ MATERIALS\ CONSUMED} \times 12}$
- $\mathbf{Work-in-Progress = \frac{Annual\ Production \times No.of\ days\ for\ W.i.p}{No.of\ days\ worked} \times 12}$
- $\mathbf{F.G.H.P(in\ months) = \frac{FINISHED\ GOODS}{TOTAL\ COST\ OF\ SALES} \times 12}$
- $\mathbf{R.H.P(in\ months) = \frac{RECEIVABLES}{TOTAL\ SALES} \times 12}$
- $\mathbf{C.H.P(in\ months) = \frac{CREDITORS}{TOTAL\ PURCHASE\ AMOUNT} \times 12}$
- $\mathbf{HOLDING\ PERIOD = (R.M.H.P + W.I.P.H.P + F.G.H.P + R.H.P - C.H.P)}$

Now, as the Total Working Capital Requirement of the Firm from the Banking Sector is "less than Rs. 5 Crores", the bank, hereunder, have assessed the Firm's Fund Based Working Capital Limit (F.B.W.C.L) under "the Turnover Method": -

TURNOVER METHOD		Projection 31.06.2016 (in Lakhs)	Projection 31.03.2017 (in Lakhs)
a.	Sales Projected	370.00	510.00
b.	Sales Accepted by Bank	370.00	510.00
c.	Working Capital Requirement (25% of "a")	92.50	127.50
d.	Minimum Margin Required (5% of "a")	18.50	25.50
e.	Actual Margin Available (C.A.-C.L.)	36.63	46.90
f.	Bank Finance (c-d)	74.00	102.00
g.	(c-e)	55.87	80.60
h.	**M.P.B.F (Lower of "f" & "g")**	**55.87**	**80.60**
i.	**Limit Proposed**	**42.00**	**42.00**

As the Firm's Operating Cycle (as on 31.03.2017- first full year of operation) projected to be "more than 3 months", the bank, hereunder, have also assessed the Firm's Fund Based Working Capital Limit (F.B.W.C.L) under "the Second Method of Lending": -

SECOND METHOD OF LENDING		Projection 31.03.2016 (in Lakhs)	Projection 31.03.2017 (in Lakhs)
a.	Total Current Assets (C.A.)	137.37	186.32
b.	Total Current Liabilities excluding Bank Borrowings (C.L.)	50.10	88.78
c.	Working Capital Gap (a-b)	87.27	97.54
d.	Minimum Stipulated Net Working Capital (25% of "a")	34.34	46.58
e.	Actual/Projected Net Working Capital	44.77	55.04
f.	Bank Finance (c-d)	52.93	50.96
g.	(c-e)	42.50	42.50
h.	**M.P.B.F (Lower of "f" & "g")**	**42.50**	**42.50**
i.	**Limit Proposed**	**42.00**	**42.00**

Note: - Considering the above calculations, the Firm is found to be eligible for the proposed Fund Based Working Capital Limit (F.B.W.C.L) of Rs. 42.50 Lakhs under both the Turnover as well as the Second Method of Lending.

G. Calculation Of Credit Rating Of The Account: -

Since, here the Proposed Credit limit lies between Rs. 10 lakhs to Rs. 5 Crores, so the Credit Rating of the Account is done through Small Business Segment (S.B.S) Model where the Rate of Interest will be applicable (to Small & Medium Enterprises) as per the following tables: -

TABLE-1 : Limits From Rs. 10 Lakhs to <Rs. 1 Crore		
Credit Rating	**Existing**	**Proposed**
SBS-1	12.80	12.65
SBS-2	12.80	12.65
SBS-3	12.85	12.75
SBS-4	12.85	12.75
SBS-5	13.10	13.00
SBS-6	13.40	13.35
SBS-7	13.90	13.85
SBS-8	15.45	15.45
SBS-9	15.45	15.45
SBS-10	15.45	15.45

TABLE-2 : Limits From Rs. 1 Crore to <Rs. 5 Crores		
Credit Rating	**Existing**	**Proposed**
SBS-1 to 2	13.30	13.15
SBS-3	13.35	13.25
SBS-4	13.85	13.75
SBS-5	14.35	14.25
SBS-6	14.40	14.35
SBS-7	14.40	14.35
SBS-8 to 10	15.45	15.45

Now, taking the following Scores into consideration and by adding them i.e. "Financial Risk Scores", "Management Risk Scores", "Business/Industry Risk Scores", "the Final Risk Score" is obtained on the basis of which the "Credit Rating Grade" is given to the respective Company. Here, the "Overall Credit Rating Grade" is given according to the "Small Business Segment (S.B.S) Model" which is based on the table mentioned below: -

FINANCIAL RISK		MANAGEMENT RISK		BUSINESS/ INDUSTRY RISK		CUSTOMER RATING (Based on Final Risk Score)	
Financial Risk Score (A)	**Financial Rating**	**Mgmt. Risk Score (B)**	**Mgmt. Rating**	**Business or Industry Risk Score (C)**	**Business or Industry Rating**	**Final Risk Score (A+B+C)**	**Credit Rating Grade**
0 to 28	1	0 to 51	1	0	1	0	**SBS-1**
29 to 33	2	52 to 77	2	24	2	120	**SBS-2**
34 to 37	3	78 to 103	3	36	3	140	**SBS-3**
38 to 42	4	104 to 120	4	48	4	160	**SBS-4**
43 to 50	5	121 to 138	5	56	5	180	**SBS-5**
51 to 58	6	139 to 155	6	64	6	213	**SBS-6**
59 to 63	7	156 to 172	7	72	7	247	**SBS-7**
64 to 68	8	173 to 190	8	80	8	268	**SBS-8**
69 to 95	9	191 to 207	9	88	9	287	**SBS-9**
96	10	208	10	96	10	400	**SBS-10**

Note: - For the Respective Cashew Processing Firm, the Final Risk Score is calculated by the bank and the Credit Rating obtained is "S.B.S-5 Rating" (i.e. otherwise known as the Entry Level Rating). Hence, the Proposed Rate of Interest applicable is "13% per annum".

Conclusion

Findings: -

1. **From the above Sales Estimation Analysis: -** It is very much clear that, the respective Company has the capacity to meet all its Estimated/Projected Sales.
2. **From the above Current Ratio Analysis: -** It is very much clear that, the respective Company is having a Sound Short-term Financial Position to meet all the requirements regarding its Current Liabilities.
3. **From the Debt-Equity Ratio Analysis: -**It is found that, the Debt-Equity Ratio (D.E.R) is decreasing year by year which shows the Company is doing well enough in all of its Business Operations.
4. **From the Debt Service Coverage Ratio Analysis: -** It is found that, the Debt Service Coverage Ratio (D.S.C.R) is increasing year by year in a positive manner. So, the Company is able to repay the debt including the interest to the bank within the respective time frame.
5. **From the Break-Even Point Analysis: -** It is found that, the Company is reaching the Break-Even Point in the first year i.e. in 2016 at Rs. 282.68. In the Subsequent two years i.e. in 2017 and 2018 there is no increase in the Capacity Utilisation by the Company so we can assume that, there will be no increase in fixed costs. The Company's Margin of Safety is increasing from Rs. 87.32 in the year 2016 to Rs. 227.32 in 2017 and Rs. 237.32 in 2018, which indicates that

the Company wants to stabilise and retain the earnings for further Capacity Utilisation which is reflected from the increase in the Capacity Utilisation to 75% in the year 2019 and so on.

6. **From the Credit Rating Analysis: -** The Final Risk Score for the respective Cashew Processing Firm/Unit is calculated by the bank and the corresponding Credit Rating obtained is "S.B.S-5 Rating" (i.e. otherwise known as "the Entry Level Rating"). Hence, the Proposed Rate of Interest applicable is "13% per annum".

Thus, Keeping in view the Bank's (i.e. Bank of India's) thrust on financing Micro, Small and Medium Enterprises (M.S.M.E) Units, the Scope of Activity, the Satisfactory Conduct of Group Account, the Projected Debt Service Coverage Ratio (D.S.C.R) Position, the Coverage under Credit Guarantee Fund Trust for Medium and Small Enterprises (C.G.T.M.S.E) Scheme, the bank then recommends for the sanction of the Term Loan and the Working Capital Loan. That is, finally the Authority (which includes the Finance Executive, the Credit Head and the Head – S.M.E. City Centre) has to sanction the Amount.

References

1. B. A. Fida, ***"The Importance of Small and Medium Enterprises (SMEs) in Economic Development"***, The Free Library. (2008). Retrieved November 23, 2011.

2. K. H. Chen and T. A. Shimerda, ***"An empirical analysis of useful financial ratios"***, Financial Management, 1981, Vol.10 (Issue 1), pp. 51-60.

3. D. E. Giacomino and D. E. Mielke, ***"Cash flows: another approach to ratio analysis"***, Journal of Accountancy, 1993, Vol. 175, pp. 55-8.

4. W. Hsiu-Kwang, ***"Bank Examiner Criticisms, Bank Loan Defaults, and Bank Loan Quality"*** The Journal of Finance, 1969, Vol. 24, pp. 697-705.

5. I.M.F (International Monetary Fund), ***"Banking Soundness and Monetary Policy in a World of Global Capital Flows"***, Proceedings of the Seventh Central Banking Seminar, Jan. 27-31, 1997, Washington D.C.Asian Research Journal of Business Management *Issue 1 (Vol.2)2014* Issn:2321-9246

6. N. Arora, A Gaur, Babita, ***"Credit Appraisal Process of SBI: A Case Study of Branch of SBI in Hisar"***, Arth Prabhand: A Journal of Economics and Management, 2013, Vol. 2 (Issue 1), pp.10-26.

7. D. H. Payle, ***"Bank Risk Management"***, Working Paper No.272, University of California., Berkeley Research Program in Finance Working Papers. No: RPF-272. July, 1997.

8. S. Varathan et al., ***"Credit policy and credit appraisal of Canara bank using ratio analysis"***, International Multidisciplinary Research Journal, 2012, Vol. 2 (Issue 7), pp.

19-28
9. D. N. Simson and G. H. Hempel, ***"Bank Management"***, text and Cases, Fifth edition,
John Wesley and Sons Inc., New York, 1999.
10. J. Sun and H. Li, ***"Data mining method for listed companies' financial distress prediction"***. Knowledge-Based Systems, 2008, Vol. 21 (Issue 1), pp. 1-5.
11. www. rbi.org.in
12. www.LVB.in
13. www.msmedi-chennai.gov.in
14. www.msmeonline.tn.gov.in
15. www. smallindustryindia.com