LEASE FINANCING IN INDIA

Thesis submitted to the
Cochin University of Science and Technology
for the Award of the Degree of
Doctor of Philosophy
under the faculty of
Social Sciences

By

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MAY 1994

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CERTIFICATE

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DECLARATION

I hereby declare that this thesis entitled "Lease Financing in India", is the record of bonafide research work carried out by me under the supervision of Dr. K. George Varghese, Reader, School of Management Studies, Cochin University of Science and Technology, Kochi - 22. I further declare that this thesis has not previously formed the basis for the award of any degree, diploma, associateship, fellowship or other similar title of recognition.

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ACKNOWLEDGEMENT

This thesis is the result of long years of hardwork. The list of kind persons who have helped me along the way is pretty long.

I owe incalculable gratitude to Dr. K. George Varghese, my guide, Reader, School of Management Studies. He has been highly optimistic, pleasant and helpful through out this endeavour. It was he who taught me to think and to write. The freedom he gave me to discuss any matter was invaluable.

To Dr. K.K. George, Professor, School of Management Studies, I owe much for his moral encouragement and help.

I am grately indebted to Prof. P. Rajendra Prasad, retired Professor of the same school for his valuable suggestions and advice.

I remember with a great sense of gratitude Dr. Mary Joseph, Mrs. Annies Vincent and Dr. Rajasenan, Faculty members, for their constant help and wise directions at every stage of my work.

Gratefully I acknowledge my heartfelt thanks to Prof. P. Ramachandra Poduval, present Director, Prof. N. Ranganathan and Prof. N. Parameswaran Nair, former Directors of the School of Management Studies, who were gracious enough to provide me with the necessary insight.

I am most fortunate to have the use of the extensive facilities of the Management Library in gathering pertinent materials. I remember with gratitude the librarians Smt. Celine Rose, Sri. Scaria, Sri. C.K. Al-Aassankutty, Sri. Gopinathan as also Smt. Elizabeth, Librarian, Department of Applied Economics.

I am indebted to the office staff particularly to Sri. Murali and Sri. Sukumaran Nair for all their assistance.

Words cannot express my deep sense of gratitude to Fr. Paul Alappat, my former Principal, Prof. O.K. George, former Head of the Department of Commerce, Prof. Mathew K. Koola, present Head of the Department and to my numerous friends and colleagues of St. Thomas College, Trichur for all their kindness and good will.

Dr. K.J. Antony, Dr. V.L. Abraham, Prof. L.D. George, Prof. Maliekkal and Prof. A.M. Francis, among other friends, deserve my thanks for invigorating my spirit during stages of depression.

My sincere thanks to Messrs. 'Classix' especially to Miss. Ajitha for the prompt services rendered in typing this thesis.

In every phase of this work, my wife, Mrs. Thankamma has been indispensable. But for her single hearted devotion and dogged persistance this work would never have seen the light of day. My debt to her is irredeemable.

My sons, Vijay Francis (11), and Vivek Francis (6), by their trust in God, by their supplication and intercession in their humble and simple way have captured my mind and often spurred me to action. They have made me a proud father.

There are many others from whom I have drawn directly or indirectly during this long period of gestation. To them all I say thanks, deeply and sincerely.

C.K. FRANCIS

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CHAPTER 1

INTRODUCTION

1.1 Leasing is a simple but unique, innovative source of medium term/long term finance. It is a method of acquiring the use of an asset without buying it. Leasing provides cent percent finance to a business which requires new plant and machinery, other office equipments, miscellaneous industrial, construction and commercial equipments. Hence it is an alternative to borrowing funds for the purchase of fixed assets.

1.2 This method of acquiring fixed assets gained ground in western countries by the middle of this century. In India, it got momentum only in the eighties. The growth in the volume of leasing activity in the recent past shows that the business community in India has widely accepted this mode of financing. It is estimated that there are nearly 1400 leasing companies (including private limited companies) in India at present and many are in the offing. Banks both in the public as well as in the private sector have managed to enter this field by starting subsidiaries. Of late, almost all manufacturing groups have formed captive leasing units. Quite recently Reserve Bank of India has issued orders allowing commercial Banks to indulge into the field of leasing directly.

1.3 Leasing refers to a contract between the lessor who owns the equipment and the lessee (user), for the lease of specifically approved items of equipment, on payment of a periodical amount (lease rental) for a definite period of lease. The lease rental paid by the lessee to the lessor incorporates the components of interest charges and the actual cost of an asset.

1.4 **Leasing Transaction:**

A lessee chooses an asset and locates the lessor who will acquire it for him. The period of lease may spread over the entire economic life of the asset. The ownership in legal terms will always be with the lessor. The lessor may or may not be the manufacturer of the equipment. If he is the manufacturer (which is not the case usually) he capitalises the cost of the equipment in his books, funding it as a capital asset, and then gives it out on lease to the lessee. If he is not a manufacturer, he will purchase the equipment from the manufacturer paying the cost (including duties and taxes). He becomes the owner and will capitalise it in his books and then leases it out. Basically there are two major forms of leases - Financial lease and operational lease.

1.5 Financial lease, also known as capital lease or full pay out lease, is generally a long term lease. Here the lessee selects the equipment, settles the price and terms of sale and arranges with a lessor to buy it. He takes the asset on lease by entering into an irrevocable, noncancellable contractual agreement with the lessor for a fixed term period. The lessee uses the equipment exclusively, maintains it, insures it and avails of the after sales service and the warranty backing it. In other words, all the risks and rewards incident to ownership is availed by the lessee, while the lessor retains the legal ownership.

1.6 Financial lease period may be primary lease period and secondary lease period. Primary lease is usually for five years which is followed by a 'secondary lease' of another three or four years depending on the type of equipment. During the primary lease period, the rentals are generally higher, to cover the cost. Rent for the subsequent period is normally lower and during this period, the lessor is getting the maximum profit, as the cost of equipment might have been covered in the initial period.

In finanacial lease there can be various options the lessor and lessee may exercise during or at the end of the lease term.

a. Lease with purchase option - The lessee will have the option to buy the equipment. Acquisition may be at a pre-determined price or at a price fixed at the time of transfer, (Interview with lessors shows that ownership is transferred to the nominee of the lessee. Otherwise leasing transaction may be interpreted as Hire Purchase)

b. Lease with lessee enjoying residual benefit. The lessee will have the right to share a portion of the terminal sale proceeds and/or to review the lease agreement at a bargain rental.

1.7 There are various types of financial leases like sale and lease back, leveraged lease, consortium lease etc.

Sale and Lease Back - This is an arrangement by which an entity that owns a given asset may sell it to a lessor and then lease it back. This enables the lessee to immediately defreeze the money that it has locked up in the said asset, and makes it available for utilising in more profitable ventures. According to Earnest W. Walker, the net effect of the sale and lease back transaction is for the firm to 'trade' a fixed asset for a current asset[1]. Lalitha Narayanan opines that sale and lease back

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1. Earnest W.Walker, Essentials of financial Management, Prentice Hall of India Pvt. Ltd., New Delhi, 1974 Page 146.

arrangement is very tricky both from the point of view of equipment finance and from the point of view of income tax. Some companies sell the assets and invest the sale proceeds in U T I Units to get income tax benefits[2]. Because of the unique advantage of this scheme many lease arrangements are under sale and lease back. Mangalore Chemicals and Fertilisers has entered into a Rs. 25 crores sale and lease back arrangement on its ageing Di-ammonium Phosphate (DAP) Plant[3].

Leverage Lease - Leveraged lease involves the inclusion of a third party. The third party may be a financier for a particular asset to be leased or owner of the asset. The lessor manages to get loan from the third party at a rate lower than the return from leasing (rate agreed between lessor and lessee). The difference in the rates can be enjoyed by the lessor.

Consortium Leasing - Under this arrangement, two or more lessors may jointly acquire the asset and lease it out to the lessee. In the case of assets which require

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2. Lalitha Narayanan 'leasing' - Industrial Economist, The Journal of Industry & Finance, Madras, Vol. XVIII No.108.

3. "Sale and Lease-DAP" - Business India, Bombay, Oct 3-16, 1988, Page 9

huge funds, a single lessor may not be capable of acquiring it or may not be willing to shoulder the entire risk associated with it. In such cases two lessors jointly own the asset and share the rentals.

1.8 Operating Lease: This type of lease is also known as maintenance lease or service lease. Under this, the lessor has to maintain and service the leased equipment and the cost of maintenance is built into the lease payments. Because of the inclusion of service charges in the lease rentals, operating lease rentals will be comparatively higher than other leases. Operating lease may contain a cancellation clause which can be exercised either by the lessor or lessee. The lessor can take away the equipment on circumstances like misbehaviour of the lessee, non payment of the rental in time, misuse of the equipment for a use not shown in the contract etc. The lessee can return the equipment at any time, on any ground which may be technological developments which make the equipment obsolete, non-requirement of the services, the unsatisfactory performance of the lessor etc. Operational leases are common in telephones, computers, aircrafts and so on.

1.9 Among the different forms of leases, Indian leasing companies offer financial leases. Most leases have a primary period of five years, followed by a secondary period. Lease can be front loaded (more rentals charged in the earlier years) or back loaded (less rentals charged in the initial years). There is also equated lease which is equated in terms of payment over the period of lease. Lease rentals are paid on definite intervals of time as agreed upon. In short, the flexibility of dates, timing and arrangement of financial lease, depends upon both the lessor and lessee.

1.10 Lease Versus Hire Purchase and Instalment Selling:

A leasing transaction can be distinguished from a 'Hire purchase' transaction or that of payment by instalments. In the case of payment by instalments, the user actually becomes the owner on payment of first instalment. The balance is to be paid in periodic instalments. But in a hire purchase transaction, some down payment is made, the balance being payable over a specified period. Eventhough ownership is passed on only on the payment of last instalment, he is deemed to be the owner at the very beginning.

Thus in both these transactions, the user acquires the ownership during the validity of the agreement, while under lease transaction the user (lessee) gets only the custody/usage of the equipment. He will not get the ownership at any time during the period of the contract.

1.11 In accounting treatment also there is a substantial difference between the two. Under leasing the entire lease rentals represent a 'hire charge' for the lessee (user). They are treated as expenses and are deductable under tax laws. But under hire purchase, part of the instalment represents capital payment and is not an expense. Only that part of the instalment which is termed as interest on the loan is considered as a revenue expenditure and is tax deductable. Lease rentals represent income to the lessor and is credited to Profit & Loss Account.

1.12 In the case of leasing, the leased asset is not shown in the balance sheet of the lessee. But the lease rentals are debited to Profit and Loss Account. Further, as the lessee is not the owner, he cannot claim depreciation on the leased assets. As against this, the hire purchase capitalises the asset brought under hire purchase contract although ownership is not acquired by him until the end of the contract. He can claim depreciation as he is the deemed owner.

Thus, advocates of leasing vociferously claim that this is a covenient mode of financing assets due to the off balance sheet reporting and entitlement of 100 percent tax deduction inspite of losing depreciation benefits.

1.13 **Significance of Leasing:**

In India, leasing business was confined to just two companies till 1982 and the total assets leased out amounted to Rs. 50 crores. The various policy announcements like freeing of a number of items of import from the licensing list, measures to reduce bureaucratic delays in clearance of industrial projects, commendable changes in MRTP Act, etc. during the middle of 1980s ushered in a congenial climate for faster economic growth. Large number of manufacturing companies came into existence intensifying competition in the wake of technology upgradation and modernisation. The number of letters of intent issued during 1985 was 1456 - an all time record and was 37 percent more than those issued in 1984[4]. Enormous funds were required for financing the activities of these concerns. But conventional sources of financing like bank loans and financial institution loans failed to meet the potential requirements of the corporate sector.

1.14 During the middle of 1980s Government reduced the budgetory support to public sector companies and halted the liberal financial institution advances to these undertakings. Government made it known that as regards financial accomodation, both public sector and private sector will be treated at par. Public sector companies

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4. Economic Diary, May 7-13, 1986.

too were allowed to tap the capital market for raising required funds. Consequently fund availability of private sector companies was expected to shrink. The seventh five year plan (1985-90) envisaged an investment of Rs. 64,000 crores at the 1984-85 prices in the private sector. A growth of investment intentions is reflected in the spurt of consents granted by Controller of Capital Issues (CCI) aggregating to Rs. 5278 crores and Rs. 8029 crores during the years 1987-88 and 1988-89[5]. The actual investment by the Private corporate sector during the 7th plan period has been below the average annual investment of Rs. 12,800 crores postulated in the Plan[6]. The gap was inferred to be bridged by other sources. Financial Institutions cannot cater to the increased needs of the corporate sector due to the fund constraints faced by them. Accordingly, the Seventh Five Year Plan projected an investment saving gap of Rs. 12,000 crores to be met from alternative sources.

1.15 The traditional passion for ownership, among the Indian Industrialists, began to wear off due to the paucity of funds, increasing the scope for lease financing. The outstanding performance of the pioneer companies in the field, accelerated the pace of leasing activity. First Leasing Company of India Limited increased its profits from Rs. 2.35 lakhs as on 30th November

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5. Kothari Industrial Directory of India,1990

6. Ibid....

1974 to Rs. 2.8 crores as on 30th November 1987[7]. Forecast of shortage of funds tempted shrewd entrepreneurs to form leasing companies. Anticipating the prospects for leasing activities, well known industrialists, commercial magnates, top executives and taxation experts have been lured towards lease financing.

1.16 There was mushroom growth of leasing companies during 1985-86 period, the first year of the Seventh five year plan. There was large scale acceptance from the investing public and the issues of leasing companies were heavily oversubscribed. Unlike manufacturing companies, leasing companies do not have gestation period and they distributed handsome dividends from the initial year itself. In the early 1980s the share prices of leasing companies were very buoyant. Share prices of some of the leasing companies appreciated even upto 570 percent[8].

1.17 It can be seen that Government also was concerned about the healthy development of lease financing in India. The policy decision of the Government during the initial stages of the leasing boom period to enable the leasing companies to raise more funds equating it with the hire purchase companies is worth noting. Since August 22, 1984 leasing companies have been brought within the purview of

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7. Business India, Bombay, November 14-27, 1988. Page 41.

8. The Economic Times, Bombay, Vol XXV, May 10, 1985.

the Non Banking Financial Companies Directions 1977 and thereby leasing companies were permitted to raise deposits upto ten times their net owned funds. Till that date, leasing companies were governed by the Companies (Acceptance and deposit) Rules of 1976. This rule lays a ceiling of 25 per cent of paid up capital and free reserves for accepting deposits. Another positive sign of promoting this industry can be traced to the permission given to nationalised banks and financial institutions like IDBI, ICICI, IRCI, etc. to enter the field of leasing. Further the permission extended to International Finance Corporation (IFC), an affiliate of the World Bank, to enter the leasing arena of the country, also pronounce the fact that the Government is much eager to promote the leasing industry. The Dahotre Committee's report on norms of bank lending to leasing companies encouraged this line of activity. Thus, leasing which picked up momentum in our country in the beginning of 1980s, flourished to its peak level within the next three or four years.

1.18 But the subsequent happenings indicated that this was only a short lived phenomenon. Leasing experts view some governmental measures as anti leasing. For gathering more funds to the exchequer, Government took a decision to tax this fast developing line of activity. The 46th Amendment Act empowers the State Government to impose tax on the right to use goods. Further the State Governments denied the privilage of using 'C' form by leasing companies. Otherwise the equipments could be purchased at a reduced cost. Introduction of Section 115 J which will lead to charging of minimum tax on book profits was seen as a blow to leasing companies. Accounting guidelines framed by Institute of Chartered Accountants of India for leasing transactions really scared the leasing companies.

1.19 Annual reports of leasing companies showed that they were not able to perform as expected. Leasing companies reduced or skipped the dividends in the wake of meagre bottomlines. Some leasing companies diversified into manufacturing activities, many added hire purchase as an activity, while several others became defunct. After 1986, the leasing scenario totally changed and in many cases the share prices nosedived to the brim point or even less. Most of the leasing company shares were striving hard to trade it at the par value. The leasing industry is apparantly caught amidst a tangle of confused mix of policies and regulations, indicating that all is not well and growing in the industry. The reasons for this state of affairs has not so far been analysed systematically.

1.20 However some publications have already come out, but they are mostly in the nature of text books.

P.K. Ghosh and G.S. Gupta in their book Fundamentals of Leasing and Lease Financing[9] explain the concept of leasing and evaluates the economic rationale of leasing. Various types of leases and the organisation and management of leasing companies are discussed in a general way.

Rajas Parchure and N. Ashok Kumar in their book, Introduction to Lease Financing[10] elucidates the scientific evaluation of lease rent. It also exposes other aspects of financial leases like taxation, investment allowance, interest rate etc.

Dr. Prem Lal Joshi in his publication, Leasing Comes of Age, Indian Scene[11] provides a comprehensive exposition of lease financing. History and development of leasing, accounting for leases, buy V/S lease evaluation etc. are some of the points it projects.

J.C. Verma in his book Lease Financing[12] - concept, Law and Procedure, elucidates, the prospects for lease

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9 Ghosh, P.K. & Gupta, G.S., Fundamentals of Leasing and Lease Financing - Vision Books Pvt. Ltd., New Delhi - 1985.

10 Rajas Parchure and Ashok Kumar N. - Introduction to Lease Financing - The Times Research Foundation, Pune 1985.

11 Dr. Prem Lal Joshi, Leasing comes of Age, Indian Scene, Amrita Prakashan, Bombay, 1986.

12 Verma, J.C., Lease Financing - Concept, Law and Procedure with Hire Purchase Act 1972, Bharat Law House, New Delhi - 1986.

finance in India, Laws applicable to lease transactions like Indian Contract Act 1872, Indian Sale of Goods Act 1930, Transfer of Property Act 1882, Indian Registration Act 1908, Companies Act 1956, Monopolies and Restrictive Trade Practices Act (MRTP) 1969 are discussed therein.

Vinod Kothari in his book Lease Financing & Hire Purchase including Consumer Credit[13] gives an analysis of legal aspects, direct taxes and sales tax implications on leasing, besides familiarising businessmen with the concept of leasing. It also highlights accounting for leasing transactions.

1.21 Several related articles have appeared in journals and dailies, covering mainly the advantages and disadvantages of leasing. Some have focussed on the leasing scenario in India while others projected the prospects of leasing. However, there are some research articles worth mentioning. An exploratory study done by R. Narayana Swamy[14] expresses the views of leasing

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Kothari vinod, Lease Financing & Hire Purchase including consumer Credit, Wadhwa & Co. Pvt. Ltd. Nagpur - 1985.

14

Narayana Swamy, R., "Views of leasing Cos on Lease Accounting Issues in India - An exploratory study" - Chartered Financial Analyst, Nov/Dec. 1989 - P.9.

companies on lease accounting issues in India. It deals only with several aspects of accounting regulation, accounting standard setting, accounting proposals and implications and economic consequences of the proposals for leasing companies and for lessees and users of financial statements. Another article dealing with the growth and performance of leasing industry by Rita Vasan[15] gives just a peripheral view of the performance of leasing companies. Hence an indepth study is attempted to analyse the leasing industry in India, in all its manifestations.

1.22 Objectives :

The study has the following objectives.

Primary Objective:

To examine the present state of leasing industry and to assess the prospects of leasing in India.

Secondary Objectives:

1) To evaluate the financial performance of leasing companies.
2) To examine the impact of Government regulations on leasing industry.

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15 Vasan Rita - Leasing : "Some dross behind the gloss", Business Std. A business Std. supplement, 1986 - p.49.

1.23 Data and Methodology :

The study is an exploratory one. The required information is obtained from both primary and secondary data. Primary data is collected from company annual reports, discussions with executives of lessor and lessee companies as well as experts in the leasing field and secondary data from the publications of the Reserve Bank of India, Stock Exchanges, various magazines and dailies.

For a detailed analysis, from a universe of 75 leasing companies who are members of Equipment Leasing Association (ELA) as in 1988, a sample of 15 companies has been drawn by random sampling. The study period covers 5 balance sheet periods from 1986 to 1990-91. In order to ensure uniformity in accounting periods, balance sheet periods are equated to 12 months wherever required.

Only simple statistical tools like compound growth rates, percentages, averages and trend analysis are used besides financial management techniques like ratios, cash flow statements and common size statements.

1.24 Limitations :

The financial data obtained for the study is based on annual reports prepared as on a particular date. In order to show a realistic picture of figures in annual reports, averaging is resorted to, if found necessary.

Certain companies in the sample are in the [illegible] stage and hence an abnormal growth is observed in [illegible] of these companies. It is noticed that there [illegible] uniformity in reporting lease and hire purchase income. Certain companies are not segregating income into lease income and hirepurchase income. In the absence of such details, income is apportioned to lease and hire purchase income in proportion to the funds blocked in these areas. Operation results may not be strictly comparable due to varied practices followed with regard to depreciation and income accounting.

1.25 **Plan of Study :**

The report proposes to have the following chapters - The introductory chapter familiarises the reader with the concept of leasing, parties involved in a lease, types of leasing found in India and the difference between leasing, hire purchase and instalment. Significance of the study, review of literature, objectives, hypothesis, data and methodology and limitations are also covered.

The second chapter, Leasing Industry in India, deals with the emergence of leasing, structure of leasing, growth and expansion of leasing, competition, diversification, other catalysts etc.

The economies of leasing are evaluated in the third chapter.

The fourth chapter deals with various regulations imposed by Government, RBI, ICAI etc. on leasing. The impact of these regulations on the industry is evaluated.

The fifth chapter fund management, elaborates the various sources and deployment pattern. Adequacy of funds for financing the main activity (leasing and hire purchase activity) is explored. In the sixth chapter profitability analysis, the effect of lease rentals, cost of borrowings and the volume of activity are examined. Possibilities of shifting to non fund activities are also looked into.

The prospects of leasing, considering the eighth five year plan capital expenditure projections, insufficiency of funds from capital market, financial institutions and banks are highlighted in the seventh chapter.

Findings, conclusions and suggestions are incorporated in the last chapter.

CHAPTER II

LEASING INDUSTRY IN INDIA

2.1 India witnessed the emergence of leasing as a formal instrument of industrial finance during the late 1970s only, eventhough this form of financing was prevalant in other advanced countries during the 1960s. The 1980s saw a dramatic rise in the number of leasing companies. Aggressive marketing efforts of the promoters supported by professionals, helped to have overwhelming support of the public in contributing to the share capital of these companies. Besides pure leasing companies, hire purchase companies also started doing leasing in a big way. The recession in hire purchase business during the early eighties forced them for the diversion. (It is reported that almost 85 percent of hire purchase activity was for commercial vehicle industry). There was steep increase in cost of vehicles and other running costs not matched by a corresponding hike in freight rates. As a result HP companies in general found it difficult to get prompt repayments. The reduction in hire purchase volume forced prominent HP companies to add leasing as an additional activity[1]. This caused a sudden upsurge in the number of leasing companies.

2.2 An important feature of the early phase of the

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1. Kothari H.C., Chairman's Statement, The Investment Trust of India Limited Annual Report, 1982.

industry was the ability of leasing companies to raise resources easily from the capital market. This can be attributed to the equity boom of 1986. During the boom conditions, the capital issues of leasing companies were particularly successful due to the projection of nil gestation period which will enable the leasing companies to declare dividends in the very first year itself. Moreover, accounting practices enabled many to under-provide depreciation and to boost the reported profits of leasing companies. The spectacular results of the existing pioneer companies prompted the investors to support the new issues of leasing companies. During the early 1980s, the industry was characterised by the excessive availability of leasing funds for the better known corporate clientele. This resulted in the undue crowding of lessors. By 31st March 1986, there were 470 companies in the fray[2]. Along with the crowding of lessors, the volume of assets acquired by the industry grew from about Rs. 50 crores in 1983 to around Rs. 450 crores in 1985[3]. The mushroom growth of leasing companies resulted in unhealthy competition, fall in rates and a compromise on the quality of the leasing portfolio. The lease rentals nosedived from Rs. 33 per month per thousand to Rs. 26 per month per thousand by 1985.[4]

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2. Ojha, P.D., "Some Aspects of Lease Financing", RBI Bulletin, Bombay, March 1988, Page 209.

3. Modern Management, Journal of the International Institute for Management Science - Calcutta, May-July 1986 Vol. 2.

4. The new Boom in Leasing, Business Update, Bombay, March 7-20, 1986

2.3 Then came the entry of institutional lessors to the leasing scenario. The Industrial Credit and Investment Corporation of India Limited (ICICI) was the first all India financial institution to offer leasing. Even though it commenced the leasing operations in 1983, it was done on a big scale only from 1986 onwards. Leasing constituted a major arm of ICICI's consistent and well planned diversification effort. ICICI gets practically all its funds at 12%, which gives it an after tax discount rate of 6%[5]. Resorting to leasing at the prevailing rentals will strengthen the profit objectives of ICICI. The Industrial Reconstruction Bank of India (IRBI) entered the field around the same time, but after ICICI. A large number of State level financial institutions also, took interest in leasing, particularly in Gujarat and Maharashtra. Gujarat Industrial Investment Corporation started Gujarat Lease Financing Ltd. for undertaking leasing and related activities for assisting Small Scale Industries. The National Small Industries Corporation (NSIC) entered the leasing scene to cater exclusively to the needs of established small units. It is now possible for small units to acquire machinery and equipment on lease basis with NSIC doing leasing business. The existing leasing companies generally take care of the needs of larger units.

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5. Raghunathan V, "Lease Rentals, The unholy dip," The Economic Times, Bombay, July 10, 1986 Vol XXVI, No. 126, Page 9.

2.4 A new dimension to the Indian leasing industry was brought in by the entry of Scheduled Banks, albeit through their subsidiaries, into the field of leasing. This was possible by the lifting of the statutory bar on banks, not to do equipment leasing. Hitherto, Indian leasing industry has been rather peculiar in that, unlike in the west, where most leasing companies are directly or indirectly associated with banks, none of the Indian leasing companies so far were in any way connected with banking operations. The first commercial bank to set up a leasing subsidiary was the State Bank of India (SBI), whose SBI capital Markets Limited was formed in October 1986[6]. Besides leasing, the subsidiary took over the existing merchant banking division of the bank. Following the SBI model, Canara Bank set up Canbank Financial Services Limited and Punjab National Bank has set up PNB Financial Services Limited. A number of other Indian banks have commissioned working groups to examine the feasibility of offering leasing. Many proposals are in the pipe line now.

2.5 Infrastructure Leasing and Financial Services Ltd. (ILFS), promoted by the Central Bank of India, the Unit Trust of India and the Housing Development and Finance Corporation, is set up to serve areas like highways, power

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6. 'The Leasing Industry - A new lease of life?', PTI Corporate Trends, New Delhi, Aug. 25, 1990 page 29 Vol.IV, No.12

and telecom.[7] It arranged to get Rs.800 crores in finance from serveral domestic financial institutions and international institutions like the World Bank, the Common Wealth Development Corporation and the Asian Development Bank.[8] One among the projects so undertaken was the Rs.700 crore Delhi Kanpur Highway.[9]

2.6 The financial institutions and commercial banks would be able to escape the interest rate guidelines set by the Reserve Bank of India by entering the leasing business. Besides, commercial banks can find out an outlet for deploying their funds by way of leasing. The bank subsidiaries can also keep a closer watch on its leasing clientele through its large net work of branches.

2.7 Meanwhile, financial institutions like IDBI, IFCI etc. started doing leasing business. IFCI's leasing activities commenced in June 1988. Besides the scheme of equipment leasing, IDBI and IFCI have funding schemes for term financing of leasing companies. Under the resources support to financial intermediaries, IDBI sanctioned Rs.86.5 crores to leasing companies during 1991-92.[10] For this, necessary amendments were made in the Act to widen the scope of IDBI and IFCI to cover leasing industry also.

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7 Business Update, Bomby, July 2-15, 1988, page 35, Column 1

8 Ibid. . . .

9 Ibid. . . .

10 IDBI Annual Report, 1991-92.

2.8 With the objective of imparting foreign technical expertise to the nascent leasing industry, RBI has worked out a policy guideline to allow foreign banks to enter leasing business in India, if they tie up with an Indian Bank/leasing company. Accordingly the standard Chartered Bank was the first foreign bank to be granted permission to invest in Cholamandalam Investment and Finance Company, a leasing company based in Madras[11]. Subsequently, American Express Bank has been allowed to join hands with Tata Industrial Finance Company Limited promoted by the Tatas[12]. Of late SAFE (South Asian Financial Exchange) promoted by 18 top industrialists in the south has reached a Memorandum of Understanding (MOU) with Barclays Bank of U.K. for co-operation in certain key areas of financial service business[13].

2.9 International Finance Corporation (IFC), an affiliate of World Bank has assumed the responsibility of strengthening leasing business in developing countries like Sri Lanka, Thailand, India, etc[14]. They propose to do this by co-ordinating local financial institutions and banks and participating in their activities. By this arrangement, leasing companies are able to do import leasing. They pay the foreign supplier either through banking channels or directly from credits obtained from

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11. The Economic Times, Bombay, October 10, 1986
12. 'The leasing Industry-A new lease of life?' PTI Corporate Trends, Vol IV No:2, August 25, 1990, Page 30
13. The Economic Times, Bombay August 11, 1992
14. The Economic Times, Bombay, June 14, 1985 Vol.XXV, No:101

IFC. IFC will extend a loan of five million dollars besides equity participation of 15 percent in the proposed joint venture leasing company. The loan granted by IFC is repayable over a period of 10 years with an initial two year moratorium. The rate of interest is a fixed rate at 13.5 percent per annum. The management of the leasing company will be with participating finance group, since the Chairman and the majority of directors will be from the finance company. IFC initiated the formation of joint ventures in four regions of the country and these ventures have reported very good business.

2.10 Some manufacturing groups, especially the recession hit industries began to make use of leasing as a 'sales aid'. Ashok Leyland, a popular vehicle manufacturing company formed Ashok Leyland Finance. A few have agreements with leasing companies to finance the sale of their products.

2.11 Among the leasing companies, the presence of 'inhouse' leasing is noticeable by the middle of 1980s. An inhouse leasing company could lease out assets exclusively to the parent company, so that the latter indirectly enjoyed a debt to equity ratio close to 10:1, instead of the meagre leverage allowed by the Controller of Capital Issues. (A leasing company is eligible to borrow upto 10 times the net worth whereas a manufacturing company can borrow only 25 percent of the net worth in the form of public deposits).

2.12 At present Indian leasing industry has become peculiar, with the presence of the following different classes of players.

1. Old leasing companies and finance companies.
2. Financial Institutions with leasing operation.
3. New leasing companies including inhouse lessors.
4. Leasing subsidiaries of banks.

2.13 The entrance of financial institutions and banks to the leasing scene, which is over crowded even otherwise, resulted in cut throat competition. These instituional lessors and bank sponsored leasing companies were able to quote a lower rate than the prevailing Rs.26 per month per thousand, since the funds at the disposal of these lessors are of comparatively cheaper rates - Most of the private leasing companies were depending on bank loans and their cost of funds are exorbitant. Mobilising public deposits to reduce cost was not easy as Indian investors were reluctant to support new companies without good track record. As a result, many companies were unable to make any headway. Several leasing companies became defunct and the number of companies active in the field was reduced to about 200 by the close of 1980s.[15] Some were forced to

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15 Business India Bombay, February 18 - March 3, 1991

diversify to new activities like trading, manufacturing, education etc. Certain companies changed even their names partially/fully to do diversified activities.

2.14 The composition of the leasing industry's portfolio has seen a shift from small peripheral items to critical items. Now almost all equipments closely aligned with the manufacturing process are leased. The change in the pattern of assets leased shows the growing role of leasing.

2.15 Indian industry continues to import a large proportion of its requirement of capital goods for upgradation, modernisation and expansion of existing facilities. The funding of imported equipment, until 1985, was through foreign currency loans from term lending institutions or purchase of foreign exchange through a permit from the Reserve Bank of India.[16] In such purchases the user was the legal owner and was entitled to the capital allowance on the asset. The government now allows the funding of imported equipment through leases. The ICICI was one of the first leasing companies to offer this facility and a large number of the major leases for imported equipment are from ICICI. As a result of dialogue between I F C and the Government authorities, changes in the 1983-84 import-export policy now permit

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16 PTI Corporate Trends, Opcit, page 34

selected leasing companies to make imported equipment available to actual users.[17] Import of equipment into India can be either under the open General Licence (OGL) or against a licence issued by the Chief Controller of Imports and Exports (C C I & E), normally issued to actual users. Licences may be issued against free foreign exchange, government to government bilateral trade credits or against foreign currency borrowing. Lease financing is posible for O G L items and for items imported against free foreign exchange licences.

2.16 Most lessors offer leasing of imported equipment with payments denoted in rupees. The option of using external foreign currency borrowing to fund the lease is also available, although on a selective basis. The lessor would pay for the CIF cost of the equipment from the foreign currency borrowing or deferred credit. The payment for items like duties would be in Indian rupees. The possible advantage of a currency lease is cheaper interest rate, compared with the domestic interest rate. It is also possible that the choosen currency could provide better terms of moratorium, repayment and so on, imparting an additional level of flexibility. The advantage of a lower interest cost would, however, need to be weighted against the risk, of an adverse exchange rate

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17 Ibid . . . .

movement. The benefit of lower interest rate may well be offset by the devaluation of the rupees.

To guard against an adverse exchange rate movement, a lessor could seek exchange cover. However, the forward exchange market in India is not yet adequately developed to provide a long term solution.

2.17 Another inhibiting factor for currency leases is the tax treatment of the exchange fluctation in the lessor's books. Under Section 43 A of the Income Tax Act, the exchange fluctuation on repayment of foreign currency borrowing cannot be written off as expense but must be capitalised and depreciated. Even if the lessee compensates for the exchange fluctation through higher rental, the lessor is not fully covered on a post-tax basis, as the additional rental would be taxed immediately as income. The Indian Government follows a cautious policy in its external borrowing programme. If permission were accorded to all leasing companies to offer currency leases, many would prefer access to the foreign markets. This could pose problems in monitoring the credit worthiness of lessors and if a lessor were to default, the credit rating of the country would be affected. A possible solution is to permit leasing companies to borrow foreign currency funds from financial institutions/banks and allow these institutions to raise their own foreign currency funds for import leases.

2.18 In the meantime, Government announced that only leasing companies which are listed on the Stock Exchanges can do import leasing.[18] Import leasing holds good prospects, considering the fact that the total imports of equipments during the 7th plan period was around Rs.95000 crores of which capital goods import will alone be about Rs.20,000 crores, i.e. Rs.4000 crores per annum.[19] Even if a small percentage of such capital assets are acquired under lease finance, all the listed leasing companies in India may not be able to attain the target. Allowing only listed leasing companies to do import lesing will be detrimental to the bank sponsored leasing companies. Bank subsidiary leasing companies cannot be listed since they are closely held companies. This restriction will not be in the interest of the booming leasing industry.

2.19 Although,no cross border leasing has taken place in India, cross border operating leases are quite common in oil industry. Cross border leasing is a transaction where lessor and lessee are located in different countries. Assets generally chosen for cross border leasing are those that are internationally mobile, have adequate residual value and enjoy undisputed title (international registration) - ships, aircraft, drilling rigs etc. are

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18 Ramesh Gelli, "Leasing-some Issues," The Banker, New Delhi, June 1991, page 45.

19 "Leasing Industry, Bid to evolve norms for healthy operations" - The Economic Times, Dec. 25, 1986, Page 4.

typical assets. A beginning of typical cross border lease has been made by the Government approving the lease of an aircraft by Air India.

2.20 With the arrival of bank subsidiaries and institutions, Indian leasing industry witnessed consortium leasing for undertaking big ticket leases. The Mahanagar Telephone Nigam Ltd. (MTNL), made arrangements with State Bank of India Capital Market Ltd., Canbank Financial Services Ltd., and the Punjab National Bank Capital Services Ltd., for leasing of telecom equipment worth Rs.114 crores.[20] MTNL made another consortium leasing arrangements for its massive expansion programme to the tune of Rs.1600 crores.[21]

2.21 Recently big ticket leases are also done in India. Financial institutions and bank sponsored leasing companies are eyeing on big deals. It is reported that Financial institutions extended Rs.100 crores lease finance to Reliance Petrochemicals.[22] Total leases worth Rs.500 crore by 470 companies during 1986 substantiates that the leasing companies, majority being private ones, are doing small ticket leases. The visible segmentation among these companies, ie. public sector lessors confining to big

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20 The Economic Times, Bombay, April 11, 1989.

21 Ibid. . . .

22 "News Events" Business India, Bombay, November 12-25 1990.

ticket leases, while private lessors concentrating on small corporate requirements, shows that the Indian leasing industry is poised for healthy growth and development.

2.22 Eventhough after 1990, rentals have firmed up from Rs.23/50 per month per thousand (PMPT) to around Rs.26 P M P T, there are problems in recovery arising from the unsatisfactory financial performance of many lessees. The number of payment defaulters increased since the private leasing companies were forced to compromise on the quality of lessees with the entrance of public sector leasing companies. To tide over the situation, leasing companies came to meet together and exchange opinion about lessees under the forum of lessors called Equipment Leasing Association. If the desired results are not forthcoming, the cash flow problem will be aggravated.

2.23 Leasing and hirepurchase companies are passing through a major transition period. The companies operating in the high risk areas are seeking diversification in fund-based and non-fund-based activities. Most of the private leasing companies have chalked out programmes for diversification - the choice areas being bill discounting, merchant banking, portfolio management etc. In view of the higher returns of the companies having diverse activities in fund-based and non-fund based segments than those confined to mostly leasing and hire purchase operations there is no option for companies but to go in for diversification.

2.24 Bill discounting is a lucrative area for leasing companies to diversify. According to Reserve Bank of India guidelines after the Stock Scam, rediscounting facility was denied to leasing/finance companies. However, these companies still have discount facilities from its own funds.

2.25 Other diversification outlets include money changing, acquisition, mergers etc. Due to liberalisation, leasing/ finance companies are in an advantageous position to offer services on acquisition and mergers. During 1991-92, Alpic Finance earned an income of Rs.1.10 crores under negotiation charges.[23]

2.26 With free pricing of issues, coupled with increasing trend toward equity financing by companies, more and more companies are entering the capital market for funds, resulting in greater scope for merchant banking services. This development may prompt some leasing companies to approach SEBI to act as merchant bankers. Thus in the merchant banking sector, the domination of SBI Capital markets, PNB Capital Services and other subsidiaries of public sector banks and foreign banks are being reduced due to the entry of n· ··ivate sector units.

23 The Economic T· ··ombay, November 26, 1992, Page 9

2.27 The growing awareness about the capital market and shift of investments of the household sector from physical assets to shares have resulted in growth in the volume of turnover of the capital market both in primary and secondary markets. Realising this potential, many leasing/finance companies have set up portfolio management divisions. This requires research and analysis, use of econometric models, ratio analysis for identification of low priced scrips with good fundamentals etc. Some leasing companies have reaped bonanza from profit on sale of investments.

2.28 Inspite of the diversification to non-fund activities for enhancing the bottom line, the volume of lease business written by the industry has shown a spectacular increase over the years. Till 1990 the total lease business written which was approximately Rs.2000 crores shot up to Rs.7500 crores by 1993 and is expected to touch Rs.10,000 crores by 1995.[23] The spurt in the volume of leasing business can be attributed to the benefits obtained from this innovative mode of financing.

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23 (a) Thakkar Mahesh, "Winds of change in leasing", The Banker, New Delhi, December 1991, page 49.

(b) Views expressed by Ramabhadran, T., ELA Chairman, Financial Express, July 25, 1993.

CHAPTER - III

MERITS OF LEASE FINANCING

The merits of lease financing are merits inherent in leasing as a finance function, merits associated with leasing companies being in the private sector and practical advantages of leasing.

3.1 Merits inherent in leasing:

Cent percent financing:- Leasing an equipment is equivalent to a cent percent loan. The lessee can use the equipment without paying anything towards the cost but for the payment of rent. No other mode of institutional finance offers such a facility. Hence, firms which are short of cash (less liquid) can always prefer this mode of finance for acquiring assets.

Tax benefit:- Lease rent is an operating expense and can be charged to the revenue account. To that extent, profit can be reduced and this gives an ultimate tax savings to the lessee. The entire lease payments comprising both principal and interest amounts are operating expenses and allowable for tax deduction. Besides, the lessor company can also show depreciation as a charge on profits which further reduces the tax burden.

Leaves the borrowing capacity of the lessee unaffected: The debt equity ratio remains the same inspite of leasing. The leased asset does not appear in the Balance Sheet. Lessee can raise loans as leasing does not in any way limit the borrowing capacity of the lessee.

Sale and lease back technique:- Once the lessee gets exhausted of his financial outlets, sale and lease back technique comes in handy for further raising of funds. The existing assets are sold to a leasing company and they are leased back. There is no physical movement of assets but simply a book entry for recording the transaction. The lessee company enjoys the benefit of taking existing capital assets off the balance sheet without disrupting its activities.

Piece - meal financing device:- If a firm is expanding by adding relatively smaller amounts of fixed assets at regular intervals, it will have to locate the funds also at regular intervals for financing its activities. Raising loans or issuing bonds at frequent intervals will be expensive and time consuming. Under such situations, lease financing is a convenient and cheap mode of financing.

As much finance as required:- In case of bank borrowings or loans from financial institutions there exist a limit upto which credit can be extended to a company, keeping in view the debt equity ratio, nature of the industry, the purpose of the loan etc. Similarly, there exists a limit on levels of fixed deposits/debentures which can be raised by a company from the public. There is no such limit or constraint in the case of lease finance. For efficiently managed, growing and expanding companies, as much finance as required can be raised through lease financing.

An insurance against out of date technology:- When technology is rapidly changing, leasing provides a cushion for the lessee by shifting the risk of obsolescence to the lessor. The operating lease contains a revocable clause and provides a leverage to the lessee to cancel the lease when the equipment becomes obsolete.

Elimination of equipment disposal problem:- On the expiry of the lease term, the lessor takes away the leased property. The lessee need not bother about the disposal of the obsolete and worn out asset.

Avoidance of bankruptcy risk:- The leased amount is not regarded as a debt and hence there are no risks of bankruptcy. The lessor can at the maximum take away his assets after due serving of notices.

No dilution of present management:- On buying an asset on lease, the need for raising further equity is done away with and changes in shareholding pattern is prevented. It is a plus point for the existing management as there is no dilution of control.

Convenient administration:- While assets are acquired on lease basis, the documentation formalities are negligible. There is no need for maintaining detailed depreciation tables and this makes the book keeping methods very simple.

Possibility of clubbing other costs:- Additional charges in acquiring equipments, such as delivery and installation charges, inspection costs, consultants' fees, interest charges tied up in advance payments, and other incidental or ancilliary costs, may be added to the capital cost of an asset and amortised over the lease period.

3.1 Merits associated with leasing Companies being in the private sector:

Leasing companies, which number about 1400, are mostly in the private sector. Existence in the private sector has provided certain benefits to leasing companies, which other financial institutions do not enjoy. The prominent financial institutions are IDBI, IFCI, NIDC, ICICI, NSIC, LIC, SFC, SIDC, IRCI, etc. They grant loans for acquiring assets. But the legal formalities, restrictions and procedural delays inherent in these institutions make them less attractive to the borrowers.

Flexibility in payment of lease rentals:- Leasing arrangements are very flexible. Leasing companies have proved more adaptable than banks and financing institutions with regard to contract structures - Rental payments may be varied according to the revenue expectations of lessees, and arrangements such as "balloon payments" at the front end or back end of leases, "stepped rentals" and so on may be made to suit a lessee's book.

Adjustment in the duration of the lease period:- The duration of the lease period is always adjusted according to the convenience of the lessee. The primary period may range from 4 to 8 years and secondary from 5 to 10 years. The rental payment period may also be adjusted to suit the needs of the lessee - monthly, quarterly, half yearly or even yearly - Banks and financial institutions may not be that much liberal to the lessee.

Immediate availability of funds:- For obtaining lease finance the procedural difficulties are less and documentation is very simple. Quick disbursement of money by cutting down cumbersome procedure is possible. Loans from banks and other financial institutions require elaborate formalities and lengthy procedures. In the case of debt raising, there are problems related to creation of mortgage on assets, appointment of trustees for debentureholders and payment of stamp duty.

No government control:- Lease finance is the only source of finance available without any government control either on the amount of loan or on the rate of interest. The RBI controls the capacity of banks and financial institutions to create credit through various measures especially in times of inflation. The expansion programmes and even the current working of probable lessees get paralysed under such conditions.

Leasing companies are liberal:- Leasing companies are not particular about the purpose for which the leased assets are put to. They accomodate activities which are given less priority or even denied by banks and other financial institutions.

No interference by the lender:- The lessee is free to use the asset without the lessor's interference thus avoiding any encounter between the two. Financial institutions may attach strips like convertibility clause or inclusion of their nominee in the director board restricting the freedom of the lessee.

Escape from asset based restrictions:- In India, MRTP and FERA companies are closely monitored by the Government and are not allowed to expand beyond certain limits. MRTP Act defines big companies as those whose total assets are in excess of Rs. 20 crores. Since a leased asset is not an asset owned by the lessee (it is an asset of the lessor company), leasing some assets can help big companies to escape the asset based restrictions. Leasing comes as a blessing in disguise to such companies for acquiring unavoidable assets.

Budget preparation made easier:- As lease rentals are definite and certain, the budget preparation can be made easier.

3.3 Practical Advantages:

Citing some practical advantages in going for lease financing will certainly benefit shrewd businessmen.

Corporate bodies which are financially sound, but have tax liabilities, find it more economic to lease unproductive assets, ie. assets which do not directly participate in the production process of the company and which do not generally qualify for multiple shift depreciation. These are assets like vehicles, refrigerators, air conditioners etc, which may be taken on lease for a five year period. At the end of the lease period, the asset remains the property of the lessor and can be made available to the lessee for a nominal value (generally not more than 2 percent of the original acquisition cost). The lessee company instead of acquiring the asset, can direct the lessor to sell the asset to one of its employees who is to be rewarded.

2. In the private sector today, only top management personnel are provided with company vehicels. Other levels of management are generally provided loans (at concessional rates of interest) to purchase vehicles - cars, scooters or mopeds. The differential in interest, till recently, was considered a perquisite and was taxable. Apart from interest, the repayment of the loan is a burden for the employee and, however well paid he is, finds it difficult to leave sufficient saving after meeting his other personal commitments. In such a situation, the company offering the loan may not be sure of boosting the morale of the beneficiary. Besides, the company

has to raise sufficient funds to give loans. In such cases, profit making corporate bodies can work out a scheme whereby the company acquires vehicles on lease basis and then arranges with the lessor (leasing company) for an outright sale of the leased asset to the employee at a nominal price, when the company wants to give the benefit. This is totally outside the tax orbit of the company.

Inspite of the numerous merits associated with leasing,the functioning of the industry is handicapped due to a series of regulations which prevent it from blossoming and flourishing.

CHAPTER - IV

REGULATIONS ON LEASING

4.1. Leasing business as stated earlier is of recent origin in India. Eventhough it is in active operation for about one and a half decades, an exclusive enactment for the leasing industry is yet to emerge. In the absence of such an exclusive enactment, its working is governed by the various laws of the country and directions from the government as well as semi government organisations. These include taxation laws, Companies Act, Reserve Bank of India directives, Export Import Policy and other directives consist of financial institution directives, bank instructions, Accountancy and Finance body regulations and the like. These regulations and directives influence the flow of funds to and from the industry, its operations and in turn, the profitability of leasing companies.

4.2. Regulations on Sourcesof Funds:-

Equity capital is one of the major sources of funds. The promoters of a company are expected to bring in a certain minimum percentage of this fund and the rest can be by means of public issue. In the absence of a minimum stake on the part of promoters, the public is generally taken for a ride. Till recently, the promoters were expected to bring in 20 percent as in the case of any other industry. Guidelines for capital issues of leasing companies insist on promoter's stake to the tune of 40 percent of the share capital whereas for other industries it is 20-25 percent. Such shareholding shall not be transferred or disposed of for a period of five years from the date of allotment of shares. Even where the shares are transferred after the stipulated lock in period, the promoters should notify the concerned stock exchange to keep the investors informed about the reduced stake of the promoters in the company. Moreover, the promoter's contribution should be brought in before the public issue opens for subscription.

4.3. These guidelines are intended for ensuring the healthiness of the industry. Enhanced interest of promoters prompts them to strive for the wellbeing of the company. The entry of 'fly by night' operators to the leasing scene can be curbed. But this is applicable only for the new companies and not for the existing companies. However, this caused a reduction in the entry of new companies. The mushroom growth of leasing companies as seen in the middle of 1980s is not likely to be repeated.

4.4. The finance ministry further decided that no finance or leasing company will be given consent to raise capital from the public unless it has been working for at least three years.[1] This measure was meant to check the public issues of new leasing companies. Following this decision it was reported that at least 20 finance companies have been stuck for permission to raise equity.[2] As a relaxation, the ministry subsequently permitted leasing companies to raise public equity on seeking institutional appraisal for their issues. Now, public issues of leasing companies will be allowed, provided they report good working results. All finance companies, whether in public or private sector, must obtain compulsorily a credit and risk rating before they come to the market.[3] This exercise will pave the way for the entry of only good finance companies, promoted by established and experienced persons.

4.5. The stock exchanges also joined in regulating leasing industry. The general trebling of the stock exchange listing floor from Rs.1 crores to Rs.3 crores was made applicable to leasing companies also. Besides, guidelines for the listing of companies on the Over The Counter Exchange of India (OTCEI) was detrimental to leasing companies. The objective of OTCEI is to create a stock exchange which will help companies raise finance from the

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1 The Business World, Bombay, 24th Oct - 6 Nov.,1990, Page 17.

2 News Scan, The Chartered Accountant, New Delhi, Feb.1991.

3 Ibid ... News Scan, Jan. 1992, Vol.XL,No.7,Page 573.

capital market in a cost-effective manner and provide a convenient and efficient avenue of capital market investment for investors.[4] Finance, leasing, and hire purchase companies are not eligible for listing whereas other companies with a minimum equity capital of Rs.30 lakhs and maximum of Rs. 10 crores are allowed to be listed.[5]

4.6 The Reserve Bank of India also tried to restrict the new issues of leasing companies. The Reserve Bank of India barred capital services subsidiaries of scheduled commercial banks from undertaking issue management functions of other leasing and hire purchase companies in the private sector.[6] In the absence of underwriting from the banking system, leasing companies proposing to raise capital would have to depend on financial institutions and private brokers for the underwriting obligations. Financial experts predicted that the financial institutions would not be available for relatively smaller companies and underwriting by private brokers would be highly unreliable and ultimately cause the demise of many proposed issues by new entrants.

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4. Ravimohan R., Chief Executive of OTCEI, paper presented at All India Conference on Corporate Finance and Financial Services, Background material for seminars on Financial services, 1992, ICAI, New Delhi.

5. Business India, Bombay, May 27 - June 9, 1991, page 20

6. The Economic Times, Ist July, 1991, page 1.

4.7 Contrary to the above predictions, as per the information obtained from Prime Public Issue Monitor, the tempo of leasing company issues is maintained. The number of leasing/finance issues which stood at 8 (out of 140 total issues) during 1990-91 increased to 24 (out of 441 total issues) in 1992-93.[7] Realising the loss of business of bank subsidiaries, the Reserve Bank of India has recently allowed the bank subsidiaries to resume the issue management functions of other leasing and hire purchase finance companies.[8]

4.8 Though the governmental efforts were to restrict public issues, the Reserve Bank of India was liberal in allowing borrowings to leasing companies. They are permitted to borrow upto 10 times their net owned funds. The borrwings can be in the form of bank borrowings, public deposits and institutional accommodations.

4.9 In the initial periods, bank borrowings were in the form of term loans as well as cash credits. By 1986, bank borrowings as a percentage of total funds was around 19 percent. In 1987 this increased to approximately 23 percent. This steady growth has been restricted by the Reserve Bank of India, by issuing a directive that bank

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7 Prime Public Issue Monitor, 1990-91, 1991-92 and 1992-93, collected from Cochin Stock Exchange Ltd.

8 The Economic Times, 22nd Feb., 1994, page 1

loans to leasing companies shall not exceed three times the net owned funds.[9] This, infact, was based on the recommendation of the Dahotre Committee. The Reserve Bank of India also prohibited commercial banks from extending term loans to leasing companies from 1988 onwards. This restricted the leasing companies to avail only cash credits, which can be upto three times the net owned funds.

4.10 This infact increased the financial burden of leasing companies as cash credit is costlier than term loans. Leasing companies opted going for this source only if other sources are not adequate and available. The utilisation of eligible bank loan is only 40 percent as on 1990-91 by the industry. Moreover, the frequent interest rate revisions have made this source unattrative to leasing companies. The interest rates were pushed to 22.5 percent as on October 1, 1991[10] from around 17.5 percent in 1988. Consequently, leasing companies have reduced the dependence on bank loans. Bank loans as a percentage of total funds declined from 23 in 1987 to 22 in 1988 and 19 in 1990-91, as observed in Table no. 4.1

4.11 The State Bank of India, on its own, introduced a novel scheme for financing leasing companies. As per

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9 Reserve Bank of India, Circular No.IECD (CAD) 201/C446 (LF) 87-88 dated 12th April 1988.

10 Collected from Credit Department, Catholic Syrian Bank Ltd., Trichur.

Table No. 4.1.

BANK LOAN OUT OF TOTAL FUND

YEAR	TOTAL FUND (Rs. in Lakhs)	BANK LOAN (Rs. in lakhs)	PERCENTAGE OF BANK LOAN TO TOTAL FUND
1986	33036	6171	18.68
1987	42459	9790	23.06
1988	55435	11997	21.64
1989	72376	16345	22.58
1990-91	92267	17473	18.94

Source: Computed from Company Annual Reports

(Total Fund = Net Worth + All Borrowings) this, all leasing companies intending to borrow more than Rs. 50 lakhs from the State Bank of India have to acquire a rating from CRISIL. The interest rate also will vary and the companies which acquire higher ratings would stand to benefit in that they will be extended loans at finer rates of interest.[11]

4.12 In India there are three credit rating agencies viz., CRISIL, IICRA and CARE functioning at present. The rating methodology adopted by these various credit raters may not be uniform. Subjective judgements may involve controversies in ratings. Hence leasing companies, inspite of strong fundamentals, may be denied State Bank of India loans at reduced rate of interest.

4.13 Leasing companies turned to co-operative banks for financial accommodation when Reserve Bank of India tightened the grip on commercial banks from funding these companies. Finance from co-operative banks can be at a reasonably favourable rate of interest and for longer period of time. Eyeing on this, certain leasing companies took equity shares of co-operative banks. First leasing company, 20th Century Finance, Nagarjuna Finance, Midwest Leasing, New Century Leasing etc. report equity participation in local co-operative banks. But, later in June 1990, Reserve Bank of India restricted co-operative banks from funding leasing and hire purchase companies. Thus, another source of fund for leasing/hire purchase companies was closed.

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11 The Economic Times, Nov. 21, 1989, Page 1

4.14 Public deposits, the major source, is an unsecured loan received from the public as deposits. Leasing companies are allowed to raise deposits upto ten times the net owned funds from 1984. Till 22.8.1984, deposits received by leasing companies were governed by the companies (Acceptance and Deposits) Rules of 1975. This rule lays a ceiling of 25 percent of paid up capital and free reserves.

4.15 Dependence on deposits by leasing companies assumed greater importance with the increase in leasing activity as well as the number of players. The following table makes it clear.

Table No.4.2

NUMBER OF LEASING COMPANIES AND DEPOSITS - TOTAL AND PER COMPANY

YEAR	DEPOSITS (Crores)	NO. OF EQUIPMENT LEASING COMPANIES	DEPOSITS/COMPANY (Crores)
1986	25.6	29	0.88
1987	45.6	49	0.93
1988	115.7	76	1.52

Source - Reserve Bank of India Bulletin, July 1991

Deposits per company increased from 0.88 crores in 1986 to 1.52 crores in 1988. According to the report of the Reserve Bank of India working group on financial companies, among non-banking finance companies, equipment leasing companies have strengthened their position in a short period as far as deposit mobilisation is concerned, accounting for 16 percent of the total in 1990.[12]

4.16 During 1986, leasing companies were permitted to accept deposits for a minimum period of six months and a maximum period of 36 months. The maximum interest on these deposits was fixed at 15 percent. It was reported that finance companies were having an edge over the manufacturing companies in deposit mobilisation by offering an interest rate of 14 percent even on short term deposits of six months. Banking section too had started feeling the pinch from the severe competition posed by finance companies. Investors obtained a very high rate of interest for six months than they got from the longer term deposits with the banks. Eventhough, the security of deposits is comapratively less in a finance company than in a bank, huge amounts of household savings were diverted from scheduled banks to the finance companies.

4.17 In April 1987, the ceiling rate of interest on deposits was reduced by one percentage point each from the prevailing level and the ceiling rate of interest was 14

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12 The Hindu, Business Page, Sept. 28, 1992.

percent.[13] Eventhough the interest rate was reduced by one percent, leasing companies still attracted the patronage of investors by offering reasonably higher interest rate for short duration. During 1988, the deposits collected by the companies under study increased to 44 percent from 41 percent of the total funds.

4.18 Later, Reserve Bank of India plugged this added advantage of finance companies. Under the new directions to the non-banking financial companies, effective from April 1, 1989, a hire purchase finance or an equipment leasing company cannot accept deposits for a period less than two years. At the same time the maximum period of deposit was increased to 5 years. The maximum rate of interest payable on deposits was maintained unchanged at 14 percent per annum. Leasing/hire purchase companies were told not to pay interest on premature withdrawal of deposits before the minimum maturity period of 24 months. With the introduction of this directive, deposits of leasing/finance companies under study showed a declining percentage. From 44 percent in 1988, the percentage of deposits to total funds declined to 42 percent and 41 percent respectively during 1989 and 1990-91.

4.19 Accepting partially the representations of leasing/ finance companies, on 26th July 1991 the Reserve Bank of India announced that the maximum rate of interest a

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13 "Capital Market", Report on Currency and Finance, 1986-87, Page 323.

finance company could pay on deposits has been raised from 14 percent to 15 percent per annum. The new rates were applicable to fresh deposits and renewals of existing deposits. The rate will be applied at quarterly rests. The Reserve Bank of India declined to allow finance companies to pay interest if the deposit was closed before the minimum period of 24 months (preclosure of deposits). This gesture of Reserve Bank of India was not at all helpful to leasing companies in deposit mobilisation.

4.20 Later, in order to mitigate the problems of leasing companies with regard to deposit canvassing, Reserve Bank of India allowed them to pay interest on premature withdrawal. As per the directive on June 19, 1992, non-banking financial companies should pay interest at the rate not exceeding 11 percent per annum on premature withdrawal of deposits after 12 months but before 24 months of the date of deposit. For premature withdrawal after 24 months, the then existing directive (payment of interest at one percent less than the contracted rate of interest) will continue. Moreover, non-banking finance companies can pay interest or compound interest at rests which shall not be shorter than monthly rests.[14] This concession allowed in respect of withdrawal enabled leasing companies to have massive deposit mobilisation

14 Indian Express, June 19, 1992.

once again. During 1992, four companies (Sundaram Finance, Sakthi Finance, ICDS and Shri Ram Investments) crossed Rs.100 crores mark in fixed deposit moblisation.[15]

4.21 The Reserve Bank of India accepting the suggestions of the Shah Committee, in April 1993, brought down the period of deposits for all finance companies to 'over 12 months' instead of 'over 24 months'. The existing maximum period remains unchanged at 60 months. At the same time, finance companies can offer only a lower interest rate of 14 percent to its fixed deposit holders for a period of one year, as against 15 percent which can be offered by manufacturing companies. Manufacturing companies are given a special treatment and they have an edge over finance/leasing companies in that they can accept deposits for a shorter duration of six months. This reduction in the interest rate by one percent from April 1993 will hit the deposit mobilistion of leasing companies. The investor will get one percent higher return if he puts his money in a manufacturing company.

4.22 The Reserve Bank of India having due concern for the interest and safety of the depositors imposes certain restrictions on the use of deposits. Every equipment leasing/hire purchase finance company is required to maintain liquid assets by way of deposits in an account

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15 The Economic Times, August 25, 1992, page 15.

with a scheduled bank (free from charge or lien) or in unencumbered approved securities, a sum which is not, at the close of business on any day, less than ten percent of the deposits outstanding in the books of the company on that day.

4.23 An analysis for discerning whether leasing companies adhere to the liquidity norm as insisted by Reserve Bank of India shows that the requirement is not strictly followed by the industry as a whole. Well established and longstanding companies like First leasing company and Sundaram Finance are seen to keep the required liquid assets for the years under review. 20th Century Finance failed to keep the same during the periods 1986 and 1987. New Companies are found unable to keep the required portion of deposits by way of liquid assets. Among the liquid assets, leasing companies prefer bank fixed deposits since it is more rewarding from the point of view of the companies.

4.24 On 26th July 1991, Reserve Bank of India directed leasing/hire Purchase companies to enhance their liquidity by increasing their statutory deposit liabilities with banks/or in unencumbered approved securities, from 10 percent to 15 percent by Nov. 1, 1991. In this 15 percent, 5 percent must be in gilt edged securities. Now Reserve Bank of India norm with liquidity percentage increased from 10 percent to 15 percent and the insistance that 5 percent of deposit liability is to be invested in gilt edged securities, will force leasing companies to invest more in government as well as trust securities. It is seen that certain leasing companies especially well established ones prefer investment in trust securities like IDBI bonds, NTPC bonds, UTI units etc. Income from intercorporate investments are exempted under section 80MM of the Income Tax Act. Deposit liability for considering the liquidity norm was defined as total deposits less unregulated deposits.[16]

4.25 Shah committee report has redefined the deposit liability and the percentage of liquid assets to be maintained has been reduced from 15 percent to 10 percent. Now, deposit liability means total deposits inclusive of debentures, bonds, intercorporate loans, deposits from directors, shareholders etc. Eventhough the percentage of liquid assets has been reduced from 15 percent of deposits to 10 percent, the revised definition of deposits will be a severe blow to leasing companies. Besides the stipulation of keeping 5 percent of revised deposit liability in government securities will pose problem for many leasing comapnies. The relief given to the leasing companies by reducing the liquidity percentage is offset by the redefinition of deposit liability.

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16 Intercorporate deposits, borrowings and monies received from directors/shareholders of private comapnies are treated as unregulated deposits.

4.26 In the changed situation, companies depending solely on public deposits gain, while companies with mixed portfolio of intercorporate deposits, debentures, deposits of directors etc. stand to lose due to the necessity of keeping more funds as liquid assets. Companies like Sundaram Finance and Sakthi Finance are the biggest beneficiaries. First leasing company and 20th Century Finance have other secured loans like debentrues, bonds etc. besides the unsecured loan of fixed deposits. The profitability of these companies are going to be affected adversely. Funds used for financing prime income generating assets (lease, hire purchase etc.) will have to be utilised for satisfying the liquidity requirement and got deployed in other less rewarding assets (NSC, Indira Vikas Patra etc.)

4.27 Reserve Bank of India directive of 26th July 1991, enables a depositor to avail loans from hire purchase and leasing companies six months after placing his deposit and upto an amount not exceeding 75 percent of the deposited sum at an interest rate which is two percent above the rate payable on the deposits. Another stipulation is that in the event of death of a depositor, his deposit may be repaid prematurely to the surviving depositor/s, in the case of joint holding with survivor clause, or his legal heir/s with interest at the contracted rate upto the date of repayment.

4.28 These new instructions are not at all alarming as far as the leasing industry is concerned. Analysis of current assets of leasing companies shows that a major portion of current assets is bank balance. Even if ten percent of the total deposits come for loan facility or has to be repaid due to death of the investor, there will be sufficient bank deposits in the form of savings account and current account balance. Among the companies studied, Sundaram Finance and Sakthi Finance are the companies with maximum fixed deposits (Public deposits) and they are having sufficiently large bank balances included in their current assets. This is depicted in the following table.

Table No.4.3

THE AMOUNT AND PERCENTAGE OF BANK BALANCE INCLUDED IN THE CURRENT ASSETS

(Rs. in Lakhs)

YEAR	TOTAL FIXED DEPOSITS	BANK BALANCE INCLUDED IN C. ASSETS	TOTAL CURRENT ASSETS	PERCENTAGE OF BANK BALANCE IN TOTAL CURRENT ASSETS
1986	14298	3806	7538	50
1987	17392	2730	7182	38
1988	24069	4485	10857	41
1989	30107	5074	15270	33
1990-91	37758	6171	18794	33

Source: Computed from company Annual Reports

4.29 Besides bank loans and public deposits, leasing companies go for term loans also for financing their activities. Term loans, also referred to as term finance, represent a secured loan which is repayable in more than one year but less than 10 years. Leasing and hire purchase companies could avail term loans upto a maximum of Rs. 5 crores. Later this maximum ceiling was removed. The loan bears a reasonable interest rate of 14 percent and the repayment is to be made over a period of 5 years in 60 monthly instalments.

4.30 Realising the need for strengthening the leasing industry by extending term loans, necessary amendments were made by the government to widen the scope of lending by IDBI and IFCI. IDBI is the principal supplier of term loans as far as leasing industry is concerned. For obtaining term loans from IDBI, leasing companies must fulfill the following conditions.

1) The leasing company should be in existence for a minimum period of 3 years.
2) The business of leasing should be at least Rs.3 crores in the preceeding year.
3) Net worth of the company should be atleast Rs. 100 lakhs.
4) The debt equity ratio should not exceed 6:1 (after taking into account the proposed loan)

5) The debt service coverage ratio should not be less than 1:8:1.

6) The company should get good rating from CRISIL.

4.31 It is noticed that all the above conditions are not strictly followed by institutions while assisting the companies. The interest coverage ratio of majority of companies are seen to be less than the standard of 1.8:1. Similarly, the debt equity ratio of certain companies are higher than 6:1 (Sundaram Finance, Sakthi Finance etc.). CRISIL rating is yet to become popular among the companies, since the first rating agency CRISIL was launched only in 1988.

4.32 From the quantum of sanctions given so far, it can be seen that financial institutions are liberal in extending term loans to leasing companies. Inspite of the reported fund constraints faced by financial institutions, total term loans enjoyed by the companies under study went up to Rs.14486.77 lakhs in 1990-91 from Rs.106.44 lakhs in 1986. i.e. a compound growth rate of 167 percent over a period of five yers. Similarly term loans out of total funds of the leasing companies showed a remarkable uptrend. From 5.96 percent in 1988, it went up to 15.70 percent in 1990-91, the term loan component becoming a significant source of funding like bank borrowings (19 percent in 1990-91).

Table No. 4.4

TERM LOAN AND TOTAL SOURCES

(Rs. in Lakhs)

YEAR	TOTAL SOURCES	TOTAL TERM LOAN	PERCENTAGE OF TERM LOAN OUT OF TOTAL FUNDS
1986	33036	106.44	0.32
1987	43459	545.00	1.28
1988	55435	3302.75	5.96
1989	72376	7862.07	10.86
1990-91	92267	14486.77	15.70

Source: Computed from company annual Reports

4.33 It is observed from table No.4.4 that from 1988 onwards term loans recorded almost 100 percent increase over the previous years. In his recent budget speech, the finance minister announced reduction of interest on term loans by one percent for new loans. Leasing companies will be benefited most since new loans are pumped into the industry in large volumes. Among the companies under study, well established companies like 20th Century Finance, First Leasing, Ashok Leyland Finance etc. are having substantial term loans in their total borrowings.

4.34 **Impact on working**

Leasing companies like other organisations are obliged to comply with numerous statutory requirements. Pertinent Corporate laws, accounting guidelines, government polices etc. are likely to intervene in the working of leasing companies.

Occasionally Leasing companies may have to invest profitably surplus funds, left after financing the prime income generating activities, leasing and hire purchase. Granting of loans to other companies/purchase of shares of other companies are governed by section 370 and 372 of the companies Act 1956 and leasing companies do face hardship because of these provisions.

4.35 No company shall make any loan to any body corporate unless the granting of such loan has been previously authorised by a special resolution of the lending company. Intercorporate deposits shall also be deemed to be loans. If loans and investments cross 10 percent of the aggregate subscribed capital and free reserves of the lending company, then the lending company must obtain prior approval of the Central Government. Approval of the Central Government should follow the sanctioning of the loan by the lending company by means of a special resolution. However these sections are not applicable to any loan made

1) by a holding company to its subsidiary or
2) by a banking company or an insurance company in the ordinary course of its business.
3) by a company established with the object of financing industrial enterprises.

By the very nature of objectives of a leasing company, they are not exempted from the applicability of section 370 and 372 and hence find it difficult to deploy sizeable amounts in times of low lease business volumes.

4.36 In order to overcome section 370 of the companies Act, leasing companies, mostly in the private sector, added 'financing industrial enterprises', as an object in the Memorandum of Association. They argue that the main object of leasing companies is to provide finance to industrial enterprises through the mode of leasing.

4.37 Very recently, the company Law Board has ruled that the private sector companies cannot claim exemption from section 370 and 372. The Board specifically made known that the exemption is applicable only for state level industrial Development corporations or financial institutions like ICICI, which are the prime movers in financing industrial enterprises. By this ruling of company law Board, leasing companies mostly in the private sector cannot deploy large amounts as loans when they find it difficult to do leasing at remunerative rates or when leasing/hire purchase business are low. But an examination of the fund management of sample leasing companies shows that they have made loans and advances at times when lease/hire purchase business volumes are low.

4.38 The introduction of sales tax on lease rentals is another inhibiting factor. With the transfer of the right to use goods, brought under the definition of sale, in the 46th Constitutional Amendment in 1981, the Central Government empowered the state government to levy sales tax on leasing transactions. The major objective of redefinining the sale is to enlarge the concept of tax on the sale of goods to enable the state governments to levy tax on transactions which are not sale or purchase as conventionally understood. Almost all the state governments in India (except Union Territories) started levying tax on leasing transactions by amending suitably the respective states Sales tax Acts. The rate of sales tax differ from State to State and it is around 5 percent on the lease rentals.

4.39 Leasing companies are exposed to two options-shoulder the tax themselves or pass on this expense to the lessee. If the leasing company treat it as their expense, then their profitability will be adversely affected. With too many players in the field lease rentals have already gone down to very low levels lowering their profits. If on the other hand, the leasing company charges the lessee, then the economies of leasing will be denied to the lessee. Then lessee may have a second thought to go for leasing or to go for outright purchase.

4.40 The levy of sales tax on lease rentals amounts to double taxation as the goods are already subjected to sale tax when purchased by the lessor. Andhra Pradesh government observing strictly the logic and rationale of the leasing transactions, has notified that where any equipment under lease transaction has suffered first point tax under APGST, then no further tax on lease rentals of such equipments should be levied[17] The stand of Andra Pradesh Government stands to reason and it is high time

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17 Ramesh Gelli op cit p.48

that other states emulated Andhra Pradesh and avoided double taxation.

4.41 Though State Governments are imposing Sales tax on lease transaction, treating it as a sale, Leasing industry is not permitted to issue C-forms (to avail concessional rate of Sales tax, on inter-state transaction) as the Central Sales Tax Act is not yet amended suitably. Hence, leasng companies are bound to pay 10% or applicable rate in that state whichever is higher on the assets procured from other states. Recently, the Honourable Supreme Court has ruled in the case of 'Builders Association of India' that when a transaction is deemed to be a sale it will have to be treated so, for all purposes [18] (including eligibility of issuing C-forms). It is hoped that Central Sales Tax Act will be amended suitably at the earliest so as to facilitate availment of 'C' form benefits to the leasing industry.

4.42 The income from lease financing is to be taxed under the head 'Profit and gains of Business or Profession' of the Income Tax Act, 1961. The Act governs the grant of depreciation, investment allowance and investment deposit. Leasing Companies, as owners of the equipment, claim investment allowance. The fiscal policy changes have abolished investment allowance with effect from April 1, 1987. This was a severe blow for leasing companies. It

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18 Ibid. . .

was reported that leasing companies were chasing as much business as possible before the deadline set for the withdrawal of investment allowance.

4.43 Government of India now allows the funding of imported equipment through leases and follows a cautious policy in its external borrowing programme. So leasing of imported goods is allowed to those companies which fulfill the following conditions. Such companies are eligible for grant of a joint import licence (jointly with the actual user) after normal capital goods scrutiny.

1) The Articles of the company should specifically provide leasing as one of the objectives.
2) The company should have a paid up capital of not less than Rs.100 lakhs.
3) The company's shares are to be listed on the stock exchanges.

These conditions are not at all detrimental to the leasing industry as almost all leasing companies satisfy these requirements. But bank subsidiary leasing companies which are closely held companies of banks are not listed in the stock exchanges and hence they are unable to do import leasing.

4.44 Government introduced Section 115J in the finance Bill from the assessment year 1988-89 onwards a tax imposed on a company's book profits where it has no taxable income. The profitability of leasing companies were seriously affected by the introduction of section 115J.

Most of the leasing companies which were reporting no tax till date had to transfer around 15-16 percent of their profit beore tax as provision for tax, complying with section 115J. In the finance Bill of 1990, the provision contained in Section 115J, imposing minimum profits tax has been dropped and leasing companies are benefitted to a very good extent. Among the companies studied, certain companies like Ashok Leyland Finance, Integrated Finance, etc. report a very low percent of profit before tax as provision for tax for the period 1991.

4.45 Accounting for leases has been a contraversial subject among the accountants, financial community and accounting standard setters since the rise of the global popularity of leasing. A variety of accounting practices have been adopted by leasing companies in India. The council of Institute of chartered Accountants of India has issued draft guidance notes governing accounting standards for leasing companies in Dec. 1988. A major issue that has been attracting attention is the provision of depreciation on leased assets by the leasing companies. The main thrust of the guidance note has been provision of depreciation matching with lease periods.

4.46 A majority of leasing companies inflate the profits by underproviding depreciation. At the same time well managed companies like 20th Century Finance, First leasing company etc. follow a very prudent and conservative policy of providing depreciation on its leased assets as per details set out in the note. The intention of these companies is providing depreciation, in the Books of Accounts, which will match the lease period for which lease are written.

Recently, the honourable High Court of Tamil Nadu has issued a stay order restraining ICAI and its officers from directing and/or compelling any of the chartered accountants to follow the directions in the Guidance Note.[19]

4.47 To sum up, the regulations, business practices, accounting procedures etc. are not standardised for the leasing industy. The industry which is still in its infancy needs the liberal assistance of Government, banks and financial institutions so as to contribute to economic growth and efficiency. So far, the industry has contributed around five percent of capital formation in the private secor. In comparison with the corresponding percentage figures of 20-25 percent in most developed countries and even in undeveloped countries like South Korea, Indian leasing industry's contribution is

CHAPTER - V

FUND MANAGEMENT

5.1 The asset requirements of firms depend on the size of the organisation, type of products and the method of production proposed. Estimation of asset requirements preceeds the determination of the amount and type of funds to finance it. In the case of manufacturing companies, probable investment in assets can be predicted before hand with reasonable accuracy. The asset pattern of such companies consist of fixed assets and current assets. Fixed assets include land and buildings, plant and machinery, furniture and fixtures, vehicles etc. Current assets consist of cash and bank balance, stock of raw materials, work in process, finished goods, debtors, bills receivable etc.

5.2 Long term funds are required to finance fixed assets as well as that part of current assets which is always invested in the business, while short term funds finance the rest of the current assets. Unlike manufacturing concerns, asset requirement and fund estimation in advance is not possible for leasing/finance companies. They make a rough estimate of the volume of business and obtain the required type of funds.

5.3 **Structure of Assets :**

In a leasing company, on an average 86 percent of assets are of fixed nature, indicating the enormous volume of permanent fund requirement. The broad categories of fixed assets and current assets for the industry appear as follows over the years;

Table No. 5.1.

STRUCTURE OF ASSETS

(Figures in brackets denote the percentage to total assets)

(Rs. in lakhs)

	1986	1987	1988	1989	1990-91
Fixed Assets	39451 (84%)	53958 (88%)	70411 (87%)	94249 (86%)	121230 (87%)
Current Assets	7538 (16%)	7182 (12%)	10857 (13%)	15270 (14%)	18794 (13%)

Source : Computed from Annual Reports of Companies

5.4 Fixed assets of leasing companies consist of leased assets, stock on hire, owned assets and investments. Leased assets represent the lease business written and includes various items on lease such as plant and machinery, vehicles/automobiles, office equipments, air conditioners etc. Stock on hire consist of road transport equipments and consumer durables hired out. The amount invested in leased assets and stock on hire are rotated in the business unlike the investment in fixed assets of other companies. Indian leases are generally for a primary period of five years. The cost of the asset will be recouped within this period. Certain lease agreements are for eight year duration too. Thus, leasing and hire purchase activities block the funds for a minimum period of three to five years. But such funds are required permanently, since fresh leases and hire purchases are written as business expands. Owned assets and investments, like fixed assets of other concerns, too require funds on a permanent basis.

5.5 Structure of Fixed Assets

An analysis of the structure of the fixed assets of the industry reveals that leased assets and stock on hire dominate the fixed assets. Owned assets and investments form only a meagre part of fixed assets. The following table makes the picture clear.

Table No. 5.2

STRUCTURE OF FIXED ASSETS

(Figures in brackets indicate the percentage to fixed assets)

(Rs. in lakhs)

	1986	1987	1988	1989	1990-91
Fixed Assets	39452	53958	70411	94250	121230
Leased Assets	17240 (44%)	23450 (43%)	30069 (42%)	36817 (39%)	44487 (37%)
Stock on hire	20509 (52%)	28465 (53%)	37650 (53%)	52939 (56%)	71491 (59%)
Owned Assets	1229 (3%)	1498 (3%)	1995 (3%)	2158 (2%)	2882 (2%)
Investments	474 (1%)	545 (1%)	697 (1%)	2336 (2%)	2370 (2%)

Source : Computed from Company Annual Reports

The table also indicates the declining proportion of leased assets from 44 percent to 37 percent and the increasing proportion of stock on hire from 52 percent to 59 percent in the fixed assets. The same is also presented through diagram No. 5.1. It is desired to examine whether the same tendency is shown by individual companies as well. The proportion of leased and hire purchase assets of companies during 1986 to 1990-91 is represented in table no. 5.3.

5.6 It is observed that the proportion of leased assets in fixed assets of 50 percent of the companies in the sample show a decline. The decline is more pronounced in the case of First Leasing and 20th Century Finance, the lone players in leasing, till 1982. Similarly, though there is an increase in the stock on hire of several companies, the hire purchase activities of First Leasing and 20th Century Finance show a substantial increase. The hire purchase base of these companies initially was negligible unlike other companies in the sample. Other companies had a wider hire purchase base in 1986 itself and hence a drastic change in business mix did not take place.

5.7 Significant variations are noticed in the business mix, i.e., lease and hire purchase activities of different companies. Hence it is desired to group the companies on the basis of their activities and the

Diagram No. 5.1

Structure of Fixed Assets for the Industry 1986 - 1990 -'91.

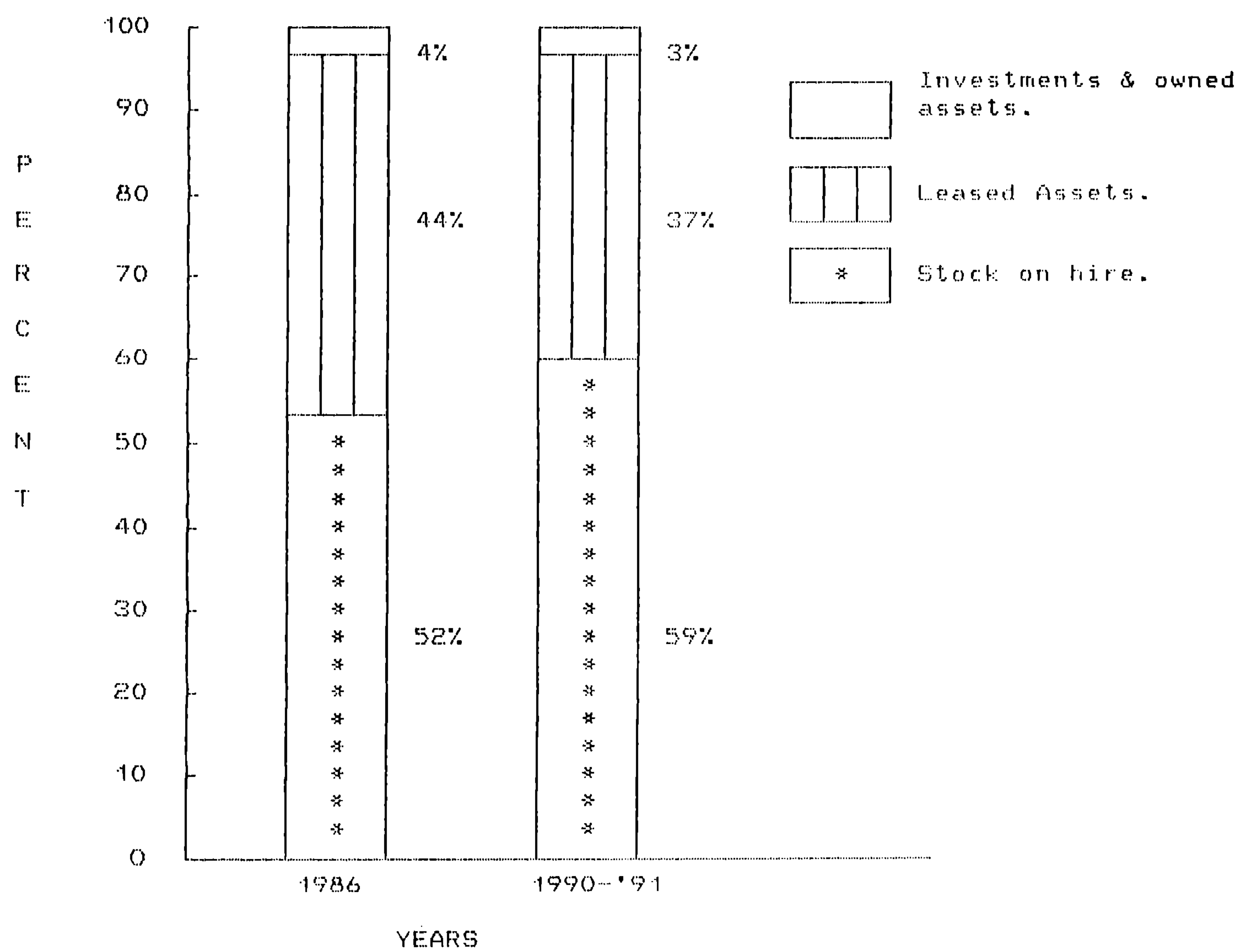


Table No. 5.3

PROPORTION OF LEASED ASSETS AND STOCK ON HIRE IN THE FIXED ASSETS DURING 1986 to 1990-91

(in Percentages)

	1986		1987		1988		1989		1990-91	
	LA	HP	LA	HP	LA	HP	LA	HP	LA	HP
First Leasing	95	3	88	10	81	18	61	37	58	41
20th Century Finance	86	5	80	13	72	22	63	27	64	28
Grover Leasing	64	32	65	29	63	30	73	21	69	26
P.L. Finance	74	23	72	24	69	28	67	30	74	21
United Leasing	71	29	55	44	61	38	63	35	67	32
World Link Finance	83	-	20	77	34	60	61	35	61	35
Midwest Leasing	38	59	29	69	26	73	31	68	38	61
DCL Finance	41	57	39	57	33	62	34	60	34	62
New Century Leasing	21	78	24	74	49	50	47	52	45	53
Sakthi Finance	35	58	34	59	36	56	41	49	38	48
Ashok Leyland Finance	17	81	19	81	15	84	15	84	15	83
Sundaram Finance	19	77	22	74	25	71	23	73	21	76
Integrated Finance	28	72	20	80	18	82	22	78	25	74
Kothari Orient Finance	19	79	27	70	24	73	23	74	28	70
Nagarjuna Finance	26	72	23	75	26	71	27	69	27	69
Grand Total	**44**	52	43	53	43	53	39	56	37	59

Sources : Computed from Company Annual Reports

LA = Leased Assets; HP = Hire purchase

following categories are formed. Companies concentrating on leasing (more than 70 percent of activity in leasing - average for five years) predominantly hire purchase companies (more than 70 percent activity in hire purchase - average for 5 years) Companies with significant volumes of both leasing and hire purchase (about 50 percent leasing and about 50 percent hire purchase - average for 5 years)

It is noticed that the business mix of predominantly hire purchase group remains more or less steady from the following table.

Table No.5.4

BUSINESS MIX OF PREDOMINANTLY HIRE PURCHASE GROUP

(PERCENTAGE TO TOTAL FIXED ASSETS)

	1986	1987	1988	1989	1990-91
Leased Assets	20	22	23	22	20
Hire Purchase Assets	76	74	74	75	77

Source: Computed from Company Annual Reports

Individual companies in the group also reveal the same tendency as observed from table No.5.5.

Table No. 5.5.

BUSINESS MIX OF PREDOMINANTLY HIRE PURCHASE COMPANIES
(PERCENTAGE TO TOTAL FIXED ASSETS)

	1986		1987		1988		1989		1990-91	
	LA	HP	LA	HP	LA	HP	LA	HP	LA	HP
Ashok Leyland Finance	17	81	19	81	15	84	15	84	15	83
Sundaram Finance	19	77	22	74	25	71	23	73	21	76
Integrated Finance	28	72	20	80	18	82	22	78	25	74
Kothari orient Finance	19	79	27	70	24	73	23	74	28	70
Nagarjuna Finance	26	72	23	75	26	71	27	69	27	69

LA = Leased Assets HP = Hire Purchase

Source : Computed from Annual Reports of Companies

The leasing activities of the mixture group reports a decline during 1987 and 1988 and thereafter an increase in the following years as shown in table No.5.6.

Table No. 5.6

BUSINESS MIX OF MIXTURE GROUP
(PERCENTAGE TO TOTAL FIXED ASSETS)

	1986	1987	1988	1989	1990-91
Leased Assets	39	34	37	42	42
Hire Purchase Assets	58	62	58	51	50

Source : Computed from Company Annual Reports.

Company wise analysis of the group in table No.5.7. shows that New Century Leasing registers a significant increase in their leasing business from 1988 onwards. Other companies in the group actually report a decline in their leased assets proportion in fixed assets. Stock on hire of New Century Leasing showed a noticeable reduction while other companies increased their stock on hire.

Table No. 5.7

BUSINESS MIX OF INDIVIDUAL COMPANIES IN THE MIXTURE GROUP

	1986		1987		1988		1989		1990-91	
	LA	HP	LA	HP	LA	HP	LA	HP	LA	HP
United Leasing	71	29	55	44	61	38	63	35	67	32
World Link Finance	83	-	20	77	34	60	61	35	61	35
Midwest leasing	38	59	29	69	26	73	31	68	38	61
DCL Finance	41	57	39	57	33	62	34	60	34	62
New Century Leasing	21	78	24	74	49	50	47	52	45	53
Sakthi Finance	35	58	34	59	36	56	41	49	38	48

LA = Leased Assets HP = Hire Purchase

Source : Computed from Annual Reports of Companies

The business mix of the predominantly leasing group reports a substantial change in mix as seen in table No.5.8.

Table No. 5.8.

BUSINESS MIX OF PREDOMINANTLY LEASING GROUP

(PERCENTGES TO TOTAL FIXED ASSETS)

	1986	1987	1988	1989	1990-91
Leased Assets	87	82	75	63	62
Hire Purchase	7	13	21	31	33

Source: Computed from Company Annual Reports

The group reported a steady decline in leasing and increase in hire purchase activities. But a company wise analysis in table No. 5.9. shows that the decline in leasing and increase in hire purchase is mainly due to change in the business mix of First Leasing and 20th Century Finance as stated earlier. The leasing and hire purchase mix of the other companies in the group records only minor variations.

Table No. 5.9.

BUSINESS MIX OF PREDOMINANTLY LEASING COMPANIES

	1986		1987		1988		1989		1990-91	
	LA	HP	LA	HP	LA	HP	LA	HP	LA	HP
First Leasing	95	3	88	10	81	18	61	37	58	41
20th Century Finance	86	5	80	13	72	22	63	27	65	28
Grover Leasing	64	32	65	29	63	30	73	21	69	26
P.L.Finance	74	23	72	24	69	28	67	30	74	21

Source : Computed from Annual Reports of Companies
LA = Leased Assets ; HP = Hire Purchase

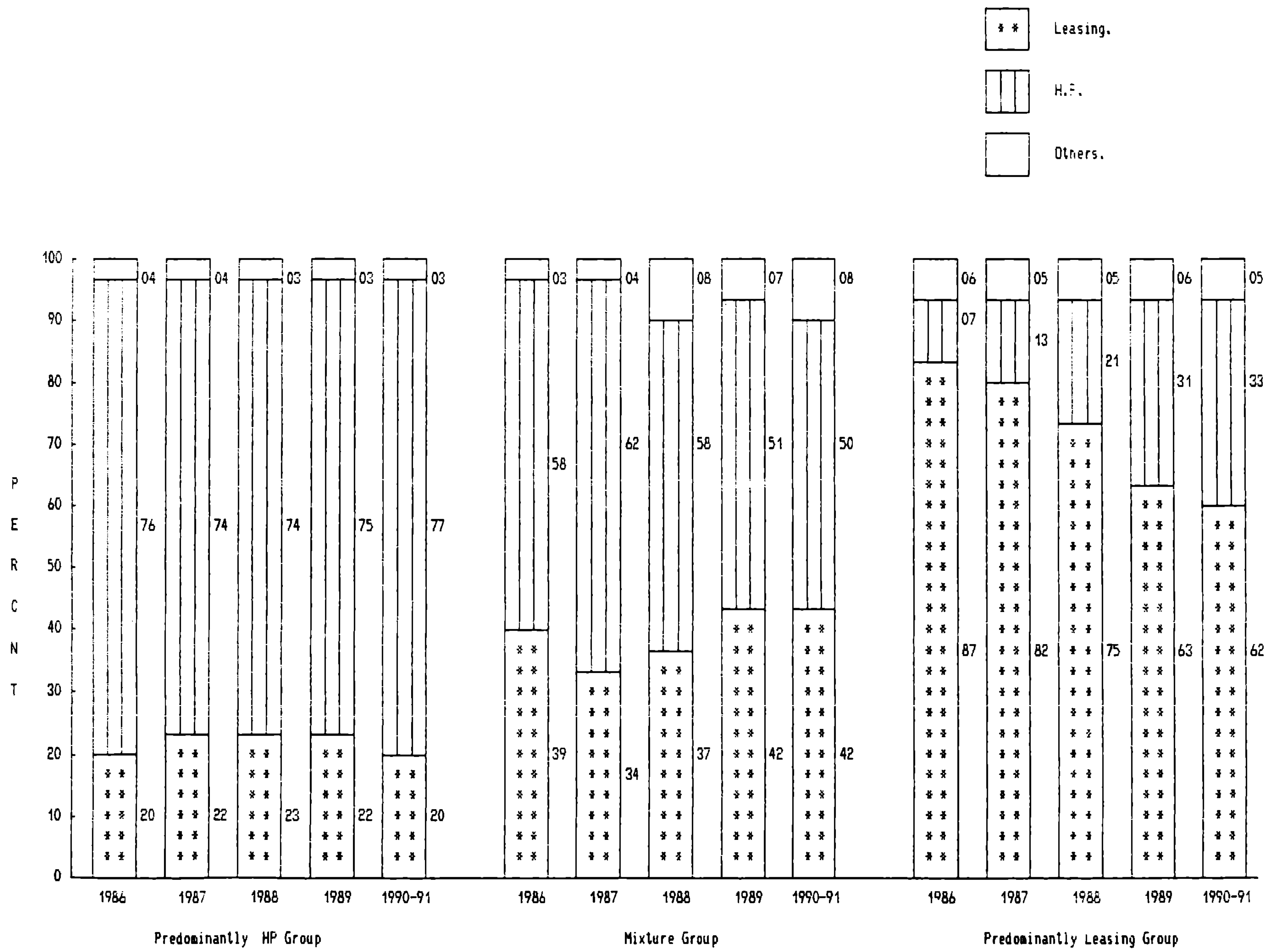
Diagram No. 5.2. presents the variations in the business mix of the three categories of leasing companies.

While the leasing business of the predominantly hire purchase group and mixture group remain more or less steady, the predominantly leasing group reports a steep decline in their leasing activities over the years.

The analysis of the proportion of leased assets and stock on hire in fixed assets thus leads to the conclusion that the proportion of leased assets has declined and stock on hire has increased. Companies with meagre leasing business are seen to maintain a steady business mix. Companies with larger volumes of leasing business

Diagram No. 5.2

DIAGRAM SHOWING THE CHANGES IN BUSINESS MIX OVER THE YEARS



had to reduce their leasing business and shift to *hire* purchase.

5.8 Structure of Leased Assets:

A scrutiny of the leased assets of the industry shows that plant and machinery dominates the leased out items. The pattern of leased assets of the industry is revealed in the following table.

Table No. 5.10

PATTERN OF LEASED ASSETS FOR THE INDUSTRY

(PERCENTAGE TO TOTAL LEASED ASSETS)

	1986	1987	1988	1989	1990-91
Plant and machinery	74	75	74	73	71
Consumer Durables	26	25	26	27	29

Source : Computed from company Annual Reports

It can be seen from the above table that though plant and machinery is the major item leased, consumer durables is gaining importance over the years. A similar pattern is followed by individual companies too vide table No.5.11. Among the consumer durable items, vehicle/ automobile leases is the dominant item for all companies.

Table No. 5.11

PATTERN OF LEASED ASSETS FOR INDIVIDUAL COMPANIES

(PERCENTAGE TO TOTAL LEASED ASSETS)

	1986		1987		1988		1989		1990-91	
	P&M	CD	P&M	CD	P&M	CD	P&M	CD	P&M	CD
First Leasing	81	19	79	21	77	23	72	28	68	32
20th Century Finance	66	34	66	34	63	37	63	37	61	39
Grover Leasing	33	67	39	61	40	60	40	60	38	62
P.L. Finance	45	55	48	52	45	55	47	53	52	48
United Leasing	42	58	44	56	39	61	42	58	41	59
World Link Finance	100	-	36	64	16	84	5	95	9	91
Mid west Leasing	48	52	48	52	63	37	70	30	69	31
Nagarjuna Finance	85	15	83	17	85	15	83	17	79	21
DCL Finance	100	-	99	1	99	1	96	4	92	8
New Century Leasing	78	22	85	15	95	5	94	6	97	3
Sakthi Finance	74	26	85	15	93	7	96	4	97	3
Kothari Orient Finance	94	6	79	21	98	2	99	1	99	1
Ashok Layland Finance	69	31	66	34	54	46	64	36	62	38
Sundaram Finance	92	8	94	6	94	6	92	8	85	15
Integrated Finance	79	21	81	19	80	20	80	20	71	29

Source : Computed from Company Annual Reports

P & M = Plant and Machinery CD = Consumer Durables

Investments which form only around 2 percent of fixed assets, are either for complying with statutory requirements, or for parking the surplus funds for protecting the interests of associate companies. The statutory requirements are as directed by the R B I or Government and are meant to protect the interests of the industry. It is observed that only old companies like First Leasing, 20th Century Finance, and Sundaram Finance are keeping the legal requirement. The investments of the industry are more or less steadily maintained.

5.10 Leasing companies do not have much assets of their own as shown in their annual reports. Companies like First Leasing, United Leasing and Integrated Finance do not report owned assets at all. The fixed investments are kept at the minimum level by the industry.

Analysis of fixed assets thus makes it clear that more than 95 percent of the investments in fixed assets are in leasing and hire purchase. Plant and Machinery is the predominant leased out item, though recently consumer durables have emerged popular. Hire purchase business is larger than leasing for the industry as a whole throughout the period reviewed.

5.11 **Structure of Current Assets:**

The investment pattern in current assets also requires an analysis. During the course of business, leasing companies block certain amounts in debtors, as loans and advances, in bank and also as other miscellaneous items. Though, in real terms the current assets of the industry increased, the proportion in total assets registered a decline (from 16% to 13%).

5.12 It is noticed from table no. 5.12 that bank deposits dominate the current assets, though its share declined from 50 percent to 33 percent. The loans and advances have increased from 9 percent to 16 percent while the percentage of debtors stood reduced to 14 percent from 18 percent. Trade bills and other current assets too report an increase during this period.

Table No.5.12

STRUCTURE OF CURRENT ASSETS

(FIGURES IN BRACKETS DENOTE THE PERCENTAGE TO CURRENT ASSETS TOTAL)

(Rs. in Lakhs)

	1986	1987	1988	1989	1990-91
Debtors	1365 (18)	1537 (21)	1644 (15)	2345 (15)	2580 (14)
Loans & Advances	686 (9)	914 (13)	1483 (14)	2158 (14)	3022 (16)
Bank	3806 (50)	2730 (38)	4485 (41)	5074 (33)	6171 (33)
Trade Bills	286 (4)	313 (4)	743 (7)	1231 (8)	1755 (9)
Other CA	1413 (19)	1688 (24)	2502 (23)	4462 (29)	5265 (28)
Total CA	7538	7182	10857	15270	18794

Source : Computed from Company Annual Reports

There is no uniformity among the companies regarding the amount invested in these components. In order to have a clear picture of the pattern of current assets an examination component wise is attempted in table no.5.13.

5.13 **Debtors:**

The percentage of debtors in current assets vary widely between companies. Certain companies like Sundaram Finance and Integrated Finance do not report any debtors at all, while more than 50 percent of the current assets of Nagarjuna Finance constitute debtors through out the period of study. Debtors form more than 40 percent of current assets for PL Finance, and Midwest leasing. First leasing, New Century Leasing, Sakthi Finance and Ashok Leyland Finance show only less than 20 percent investment in debtors.

5.14 The quality of debtors determines to a large extent, the liquidity position of any company. The average age of debtors measures the quality of debt. A shorter collection period implies prompt payment by debtors and a longer collection period implies too liberal and inefficient credit collection performance.

Table No. 5.13

STRUCTURE OF CURRENT ASSETS OF INDIVIDUAL COMPANIES -1986

Predominantly Leasing Companies (Rs. in Lakhs)

	Debtors		L & AD		Bank Balance		T Bills		Other CA		Total CA		Total Assets
	Amt.	% to CA	Amt.	% to CA	Amt.	% to CA	Amt.	% to CA	Amt.	% to CA	Amt.	% to TA	
First Leasing	170	14	61	5	472	39	-	-	496	41	1199	22	5335
20th Century Finance	108	14	7	1	518	165	-	-	65	21	798	10	8052
Grover Leasing	1	-	9	20	18	41	-	-	16	36	44	7	651
PL Finance	42	25	76	45	33	20	-	-	17	10	168	18	955
TOTAL	321	15	153	7	1041	47	-	-	694	31	2209	15	14993
Mixture of Leasing and Hire Purchase Companies													
United Leasing	9	12	17	22	42	55	-	-	8	11	76	15	514
World Like Finance	15	8	39	22	18	10	-	-	105	59	177	94	189
Midwest Leasing	11	25	10	23	20	45	-	-	3	7	44	5	971
DCL Finance	7	16	5	11	15	33	-	-	18	40	45	8	559
New Century Leasing	6	14	-	-	15	36	-	-	21	50	42	7	638
Sakthi Finance	18	4	-	-	144	49	-	-	129	44	291	17	1727
TOTAL	66	10	71	11	254	38	-	-	284	42	675	15	4597
Predominantly Hire Purchase Companies													
Ashok Leyland Finance	4	11	-	-	24	67	-	-	8	22	36	3	1293
Sundharam Finance	-	-	158	6	2121	75	266	9	276	10	2821	14	20451
Integrated Finance	-	-	43	60	243	360	2	3	26	37	71	8	843
Kothari Orient Finance	5	17	-	-	15	50	-	-	10	33	30	6	467
Nagarjuna Finance	969	57	304	18	308	18	-	-	115	7	1696	39	4346
TOTAL	978	21	462	10	2511	54	268	6	435	9	4654	17	27399
Grand Total	1365	18	686	9	3806	50	268	4	1413	19	7538	16	46989

(Contd.....)

STRUCTURE OF CURRENT ASSETS OF INDIVIDUAL COMPANIES - 1987

Predominantly Leasing Companies (Rs. in lakhs)

	Debtors		L & AD		Bank Balance		T Bills		Other CA		Total CA		Total Assets
	Amt.	% to CA	Amt.	% to CA	Amt.	% to CA	Amt.	%to CA	Amt.	% of CA	Amt.	% to CA	
First Leasing	162	21	111	15	157	21	-	-	324	43	754	11	7067
20th Century Finance	223	28	123	16	157	20	-	-	285	36	788	7	10685
Grover Leasing	1	-	99	57	41	23	-	-	34	19	175	19	931
PL Finance	105	47	41	18	48	21	-	-	30	13	224	18	1226
TOTAL	491	25	374	19	403	21	-	-	673	35	1941	10	19909
Mixture of Leasing and Hire Purchase Companies													
United Leasing	19	24	16	21	32	41	-	-	11	14	78	9	832
World Like Finance	13	5	61	21	36	13	-	-	178	62	288	35	816
Midwest Leasing	26	23	44	38	38	33	-	-	7	6	115	26	445
DCL Finance	30	39	3	-	20	26	-	-	24	31	77	9	839
New Century Leasing	15	19	-	-	30	39	-	-	32	42	77	8	947
Sakthi Finance	60	8	45	6	309	42	-	-	323	44	737	19	3939
TOTAL	163	12	169	12	465	34	-	-	575	42	1372	16	8818
Predominantly Hire Purchase Companies													
Ashok Leyland Finance	7	10	-	-	33	47	-	-	30	43	70	3	2629
Sundharam Finance	-	-	188	8	1480	66	310	14	268	12	2246	10	21675
Integrated Finance	-	-	-	-	26	72	3	8	7	20	36	2	1736
Kothari Orient Finance	17	32	-	-	22	42	-	-	14	26	53	9	576
Nagarjuna Finance	859	59	183	13	301	21	-	-	121	8	1464	25	5805
TOTAL	883	23	371	10	1862	48	313	8	440	11	3869	12	32420
Grand Total	1537	21	914	13	2730	38	313	4	1688	24	7182	12	61147

(Contd......)

STRUCTURE OF CURRENT ASSETS OF INDIVIDUAL COMPANIES - 1988

Predominantly Leasing Companies (Rs. in lakhs)

	Debtors		L & AD		Bank Balance		T Bills		Other CA		Total CA		Total Assets
	Amt.	% to CA	Amt.	% to CA	Amt.	% to CA	Amt.	% to CA	Amt.	% to CA	Amt.	% to TA	
First Leasing	200	21	215	23	234	25	-	-	299	32	948	10	9628
20th Century Finance	345	38	84	9	143	16	-	-	335	37	907	7	13916
Grover Leasing	26	10	137	51	67	25	-	-	41	15	271	25	1105
PL Finance	74	38	31	16	54	27	-	-	38	19	197	15	1333
TOTAL	645	28	467	20	498	21	-	-	713	31	2323	9	25982
Mixtrure of Leasing and Hire purchase Companies													
United Leasing	17	4	16	4	87	19	-	-	327	73	447	36	1231
World Like Finance	13	5	89	35	49	20	-	-	100	40	251	24	1012
Midwest Leasing	78	20	208	53	79	20	-	-	31	8	396	15	2662
DCL Finance	39	26	3	2	49	33	-	-	57	39	148	11	1406
New Century Leasing	24	11	-	-	43	20	-	-	146	69	213	14	1542
Sakthi Finance	110	10	77	7	517	46	-	-	424	38	1128	17	6700
TOTAL	281	11	393	15	824	32	-	-	1085	42	2583	18	14553
Predominantly Hire Purchase Companies													
Ashok Leyland Finance	18	2	-	-	164	20	466	57	165	20	813	13	6171
Sundharam Finance	-	-	380	11	2637	74	275	8	293	8	3585	14	25075
Integrated Finance	-	-	-	-	35	32	2	2	74	67	111	5	2218
Kothari Orient Finance	-	-	17	25	33	49	-	-	17	25	67	9	727
Nagarjuna Finance	700	51	226	16	294	21	-	-	155	11	1375	21	6545
TOTAL	718	12	623	10	3163	53	743	12	704	12	5951	15	40736
Grand Total	**1644**	**15**	**1483**	**14**	**4485**	**41**	**743**	**7**	**2502**	**23**	**10857**	**14**	**81271**

(Contd...)

STRUCTURE OF CURRENT ASSETS OF INDIVIDUAL COMPANIES - 1989

Predominantly Leasing Companies (Rs. in lakhs)

	Debtors		L & AD		Bank Balance		T Bills		Other CA		Total CA		Total Assets
	Amt.	% to CA	Amt.	% to CA	Amt.	% to CA	Amt.	% to CA	Amt.	% to CA	Amt.	% to TA	
First Leasing	180	10	403	23	280	16	-	-	885	51	1748	13	13608
20th Century Finance	679	32	560	27	75	4	241	12	538	26	2093	11	19496
Grover Leasing	29	17	73	43	28	17	-	-	38	23	168	18	913
PL Finance	97	36	49	18	50	19	-	-	70	26	266	18	1520
TOTAL	985	23	1085	25	433	10	241	6	1531	36	4275	12	35537
Mixture of Leasing and Hire Purchase Companies													
United Leasing	21	4	18	3	99	19	-	-	389	74	527	34	1546
World Like Finance	52	25	30	15	10	5	-	-	113	55	205	15	1400
Midwest Leasing	107	31	52	15	120	35	-	-	63	18	342	11	3043
DCL Finance	34	17	8	4	78	40	-	-	77	39	197	11	1745
New Century Leasing	37	8	-	-	48	10	-	-	407	83	492	21	2341
Sakthi Finance	233	14	77	5	685	40	-	-	710	42	1705	16	10393
TOTAL	484	14	185	5	1040	30	-	-	1759	51	3468	17	20468
Predominantly Hire Purchase Companies													
Ashok Leyland Finance	18	1	-	-	479	31	636	41	400	26	1533	14	11262
Sundharam Finance	-	-	716	17	2620	63	354	8	482	12	4172	13	31488
Integrated Finance	-	-	6	4	59	44	-	-	70	52	135	5	2499
Kothari Orient Finance	-	-	-	-	41	61	-	-	26	39	67	8	800
Nagarjuna Finance	858	53	166	10	402	25	-	-	194	12	1620	22	7465
TOTAL	876	12	888	12	3601	48	990	13	1172	16	7527	14	53514
Grand Total	2345	15	2158	14	5074	33	1231	8	4462	29	15270	14	109519

(Contd.....)

STRUCTURE OF CURRENT ASSETS OF INDIVIDUAL COMPANIES - 1990-91

Predominantly Leasing Companies (Rs. inlakhs)

	Debtors		L & AD		Bank Balance		T Bills		Other CA		Total CA		Total Assets
	Amt.	% to CA	Amt.	% to CA	Amt.	% to CA	Amt.	% to CA	Amt.	% to CA	Amt.	% to TA	
First Leasing	176	12	622	43	255	18	-	-	378	26	1431	8	16993
20th Century Finance	607	32	475	25	244	13	118	6	474	25	1918	9	21369
Grover Leasing	35	23	51	33	36	23	-	-	33	21	155	14	1101
PL Finance	155	42	40	11	59	16	-	-	116	31	370	22	1705
TOTAL	973	25	1188	31	594	15	118	3	1001	26	3874	9	41168
Mixture of Leasing and Hire Purchase companies													
United Leasing	17	3	26	4	32	5	-	-	513	87	588	30	1932
World Like Finance	52	25	30	15	10	5	-	-	113	55	205	15	1400
Midwest Leasing	224	41	38	7	211	38	-	-	77	14	550	17	3224
DCL Finance	37	24	12	8	67	44	-	-	37	24	153	7	2062
New Century Leasing	84	17	1	-	34	7	-	-	373	76	492	18	2793
Sakthi Finance	432	17	201	8	859	35	-	-	980	40	2472	20	12550
TOTAL	846	19	308	7	1213	27	-	-	2093	47	4460	19	23961
Predominantly Hire Purchase Companies													
Ashok Leyland Finance	55	3	-	-	629	31	824	41	492	25	2001	11	18378
Sundharam Finance	-	-	1336	21	3102	48	808	13	1217	19	6463	15	43338
Integrated Finance	-	-	23	10	88	36	5	2	126	52	242	8	2982
Kothari Orient Finance	-	-	-	-	65	52	-	-	59	48	124	11	1151
Nagarjuna Finance	706	43	167	10	480	29	-	-	277	17	1630	18	9046
TOTAL	761	7	1526	15	4364	42	1637	16	2171	21	10460	14	74895
Grand Total	2580	14	3022	16	6171	33	1755	9	5265	28	18794	13	140024

Source : Computed from Company Annual Reports.

L & AD = Loans and Advances
CA = Current Assets
TA = Total Assets

Average age of debtors is determined by dividing the average debtors by average income (in the absence of sales). Average debtors is the average of opening and closing debtor balances. Average income is determined by dividing total income by the accounting period.

5.15 It is observed that the average age of debtors for the industry as a whole came down from 2.46 months to 1.76 months over the period reviewed as seen below.

Table No. 5.14

AVERAGE AGE OF DEBTORS (MONTHS)

1986	1987	1988	1989	1990-91
-	2.46	2.00	1.80	1.76

Source : Computed from Company Annual Reports

Company wise analysis in table No.5.15 reveals that Old companies like First Leasing and 20th Century Finance have lower collection periods (around 1 month). On the otherhand, companies like Nagarjuna, PL Finance, Midwest Leasing etc. report a longer collection period of 3 to 6 months. Ashok Leyland Finance, though a new company, report only a lower collection period of less than one month.

Table No. 5.15

AVERAGE AGE OF DEBTORS COMPANY WISE (MONTHS)

Name of companies	1987	1988	1989	1990-91
First Leasing	1.22	1.12	0.89	0.65
20th Century Finance	0.92	1.29	1.85	1.88
United Leasing	1.18	1.08	0.91	0.74
World Link Finance	1.03	0.71	1.34	2.13
Grover Leasing	0.03	0.60	1.30	1.56
PL Finance	3.37	4.16	3.37	5.65
Integrated Finance	-	-	-	-
Nagarjuna Finance	12.48	8.30	6.85	5.94
Midwest Leasing	0.88	1.58	2.04	3.25
DCL Finance	1.33	1.85	1.46	1.24
New Century Leasing	0.82	0.96	0.94	1.55
Kothari Orient Finance	1.25	-	-	-
Sakthi Finance	0.63	0.80	1.04	1.66
Sundaram Finance	-	-	-	-
Ashok Leyland Finance	0.16	0.19	0.12	0.15
TOTAL	2.46	2.00	1.80	1.76

Source : Computed from Company Annual Reports

5.16 This is inspite of increasing the problem accounts. Debtors with more than 6 months are treated as problem accounts. It is observed that problem accounts are consistently increasing over the years. In 1986 it was 5 percent of debtors, but increased to 26 percent during 1990-91 as revealed in the following table.

Table No.5.16

PROBLEM ACCOUNTS

(Rs. in lakhs)

	1986	1987	1988	1989	1990-91
Problem Accounts(1)	59	256	411	501	677
Debtors (2)	1320	1507	1643	2357	2653
½	5%	17%	25%	21%	26%

Source : Computed from Company Annual Reports

5.17 Companywise analysis in table no.5.17 shows that old companies like First Leasing, 20th Century Finance have sizeable problem accounts and it is increasing year by year, which is quite natural. But these companies are able to reduce the percentage of debtors in current assets as well as the debt collection period, over the years. It is achieved through the well acclaimed 'get together measure' adopted by leasing companies to tackle the problem accounts. Under the auspices of Equipment Leasing Association, lessor companies meet together to discuss the credit worthiness of the lessees.

Table No. 5.17 PROBLEM ACCOUNTS COMPANY WISE

(PERCENTAGE TO TOTAL DEBTORS)

Name of Companies	1986	1987	1988	1989	1990-91
First Leasing	25.67	66.48	108.16	65.47	84.63
20th Century Finance	6.47	81.15	110.83	174.50	187.17
United Leasing	1.41	0.58	3.82	6.45	4.85
World Link Finance	-	-	1.44	2.01	2.01
Grover Leasing	0.34	0.28	7.33	20.32	19.19
PL Finance	12.48	37.99	48.98	52.29	83.34
Integrated Finance	-	-	-	-	-
Nagarjuna Finance	7.53	17.34	51.85	75.48	61.21
Midwest Leasing	-	19.39	19.69	20.46	38.75
DCL Finance	-	14.08	24.67	20.81	30.67
New Century Leasing	0.25	2.27	6.09	16.58	28.59
Kothari Orient Finance	0.40	1.75	-	-	-
Sakthi Finance	4.66	14.34	27.76	46.20	130.59
Sundaram Finance	-	-	-	-	-
Ashok Leyland Finance	-	-	-	-	7.89
TOTAL	5.00	17.00	25.00	21.00	26.00

Source : Computed from Company Annual Reports

5.18 Analysis of debtors, thus reveals the efficient collection policies of Sundaram Finance and Integrated Finance, which enable them to report nil debtor balances. First Leasing, 20th Century Finance and Ashok Leyland Finance have lower debtor balances and shorter collection periods. Companies like Nagarjuna, PL Finance and Midwest Leasing have poor collection policies and have piled up debtors.

5.19 **Loans and Advances:**

Loans and advances have increased from 9 percent of current assets to 16 percent over the years. They consist of inter corporate deposits and advances to subsidiary companies for temporarily investing their surplus funds. The proportion of loans and advances of the predominantly leasing group and mixture group showed an increase during 1987 and 1988, while the loans and advances of hire purchase group remained steady.

5.20 The decrease in leasing business during 1987 and 1988 as observed earlier for the predominantly leasing group and mixture group, generated surplus funds which was temporarily invested as loans and advances until new leases were written. The hire purchase group, which maintained steady business mix, reported steady loans and advances till 1988. The following table provides a clear view of the same.

Table No. 5.18

LEASING BUSINESS, LOANS AND ADVANCES

(Percent to total usiness)

Name of the Group	1986		1987		1988		1989		1990-91	
	LB	L&AD	LB	L&AD	LB	L&AD	LB	L&AD	LB	L&AD
Predominantly Leasing Group	87	7	82	19	75	20	63	25	62	31
Mixture Group	39	11	34	12	37	15	42	5	42	7
Predominantly Hire Purchase Group	20	10	22	10	23	10	22	12	20	15

Source : Computed from Company Annual Reports

LB = Leasing Business
L & AD = Loans and Advances

5.21 The predominantly leasing group shows a steady decline in lease business and a corresponding increase in loans and advances. (87% to 62% decrease in leasing, 7% to 31 % increase in loans and advances).

Mixture group marginally declined leasing business from 39 percent in 1986 to 37 percent in 1988 and the loans and advances stood increased from 11 percent to 15 percent. Later in 1989 and 1990-91 while lease business increased to 42 percent the loans and advances decreased to 7 percent.

The hire purchase group which maintained a steady increase in lease business till 1988, reported constant loans and advances which later increased to 15 percent during 1990-91, while the percentage of lease business reported a slight decline from 23 percent to 20 percent.

5.22 It is also observed that contrary to the talk in the industry, leasing companies are not advancing large amounts to their subsidiaries. Only few companies have advanced loans to subsidiaries as is evident from table no. 5.19. Besides the percentage of such amounts to total funds is negligible and is getting reduced over the years indicating that syphoning of funds do not take place in the industry. Thus, it is understood that while leasing business volumes are low, companies invested their surplus funds as loans and advances until new business came along.

5.23 **Cash and bank balance:**

Cash and bank balances represent the largest component of current asset for the industry throughout the years as seen from the table No. 5.12. All companies in the predominantly hire purchase group are seen to maintain more cash/bank balances during the period reviewed (except Nagarjuna Finance with large amounts blocked in debtors). The cash balances of First Leasing and 20th Century Finance have been reduced in real terms and the percentage fell from 47 percent to 15 percent druing 1986-'90 period.

Table No. 5.19

LOANS AND ADVANCES OF LEASING COMPANIES TO SUBSIDIARY COMPANIES

(Rs. in Lakhs)

Name of Companies	1986 Advan-ces	1986 Funds Deployed	1986 %	1987 Advanced	1987 Funds Deployed	1987 %	1988 Advance	1988 Funds Deployed	1988 %	1989 Advances	1989 Funds Deployed	1989 %	1990-91 Advance	1990-91 Funds Deployed	1990-91 %
First Leasing	74	5529	1.33	14	7167	0.20	91	9738	0.94	79	13802	0.57	70	16993	0.41
20th Century Leasing*	-	-	-	14	11057	0.13	8	14754	0.06	13	20796	0.06	-	-	-
United Leasing	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
World Link Finance	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
Grover Leasing	-	-	-	60	947	6.4	64	1160	5.56	39	916	4.26	27	1114	2.46
PL Finance	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
Integrated Finance	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
Nagarjuna Finance*	5	4346	0.12	19	5804	0.32	41	6544	0.62	17	7465	0.23	20	9046	0.22
Midwest Leasing	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
DCL Finance	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
New Century Leasing	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
Kothari Orient Finance	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
Sakthi Finance	-	-	-	-	-	-	-	-	-	-	-	-	12	12615	0.69
Sundaram Finance	35	20451	0.17	50	21675	0.23	44	25075	0.18	-	-	-	25	43339	0.06

* Companies in which directors are interested and not purely subsidiary companies

Source : Computed from company Annual Reports

5.24 The cash balance of companies in the mixture group too register a decline and the proportion stand reduced from 38 to 27. Though, the predominantly hire purchase group shows the largest investment in bank, the share of this component in total current assets has declined due to the shifting to trade bills by Ashok Leyland Finance and to other Current Assets by Integrated Finance from 1988 onwards.

It is enough if a leasing company keeps only a low cash balance as speculation motive and precautionary motives do not influence the cash holdings of leasing companies in India. Even transaction motive is not having much influence due to the definite and regular cash flow patterns.

5.25 It is noticed that cash/bank balances of the industry has come down. The reduction in cash balance is significant for companies concentrating on leasing. However, since the cash balances as given on the last day of the accounting year, as reported in the Balance Sheet is being considered, a genuine picture of cash holdings of several companies may not be revealed.

5.26 **Other Assets:**

Items which do not belong to the earlier categories are grouped under other assets. Strict uniformity is not there regarding the items put under this head. The proportion of other Current Assets has gone up from 19 percent to 28 percent. Wide variations are noticed among companies regarding the amount blocked in other current assets. But a detailed analysis of the same is not attempted as the items included in the group are not strictly comparable.

5.27 A study of the current assets, thus brings out the efficient debt collection policies of some companies. It is understood that when leasing business is low, companies temporarily invest their surplus funds as loans and advances. An attempt is made by companies to reduce the share of bank balances in current assets. Trade bills have emerged popular recently. Inspite of all these, the percentage of current assets in total business is low and is getting reduced indicating the supremacy of fixed assets.

5.28 **Financial Policy:**

Since fixed assets are found to occupy a pivotal share of the assets of leasing companies (more than 86 percent) the long term fund requirement assumes more importance than the financing of the current assets. It is a prudent financial policy to finance the fixed assets and permanent current assets using long term funds, while only the fluctuating current assets are financed by short term funds. But the financing pattern of all concerns need not adhere strictly to this conservative policy. There are aggressive and highly aggressive financial policies practised by concerns. The following table indicates the financing pattern of the leasing industry.

Table No.5.20

FINANCING PATTERN

(Rs. in Lakhs)

	1986	1987	1988	1989	1990-91
Fixed Assets	39,451	53,958	70,411	94,249	1,21,230
Long Term Finance	33,041	42,421	55,079	72,302	92,155
(NW + all borrowing)					
Shortage	6,410	11,537	15,332	21,947	29,075
% of Fixed Assets	16%	21%	22%	23%	24%

Source : Computed from Company Annual Reports

5.29 The above table clearly shows that the long term funds of the industry are not sufficient to finance the fixed assets. The industry is following a highly aggressive policy of financing even fixed assets using short term funds. The percentage of fixed assets financed by short term fund goes on increasing from 16 percent in 1986 to 24 percent in 1990-91.

5.30 The groupwise financing pattern is given in table 5.21. It also reveals a similar policy. No group is having sufficient long term funds. Predominantly leasing group is seen to increase the percentage of fixed assets financed by short term funds from 14 percent to 30 percent while hire purchase group increased the percentage from 19 percent to 25 percent. The mixture group uses only a lower percentage of short term funds to finance their fixed assets and the percentage increased only to 8 percent from 7 percent.

Table No.5.21 FINANCING PATTERN - GROUP WISE

(Rs. in lakhs)

	1986	1984	1988	1989	1990-91
Predominantly leasing Companies					
Fixed assets	12,784	17,968	23,659	31,262	37,294
Long term Finance	10,962	13,808	17,125	22,902	25,932
Shortage	1,822	4,160	6,534	8,302	11,362
% to fixed assets	14%	23%	28%	27%	30%
Mixture of leasing and Hire purchase companies					
Fixed assets	3,922	7,446	11,970	17,000	19,501
Long term Finance	3,666	6,775	10,674	15,332	17,886
Shortage	256	671	1,296	1,668	1,615
% to fixed assets	7%	9%	11%	10%	8%
Predominantly Hire Purchase Companies					
Fixed assets	2,274	28,551	34,785	45,987	64,435
Long term Finance	18,413	21,838	27,280	34,068	48,336
Shortage	4,332	6,713	7,505	11,919	16,099
% to fixed assets	19%	24%	22%	26%	25%

Source : Computed from company Annual Report

5.31 Company wise analysis of financial pattern in table no.5.22 shows that the older companies in the leasing group are using more short term funds to finance their fixed assets than the new companies in the group as their leasing and hire purchase business is larger requiring more long term funds. In the Hire Purchase group all companies are using short term funds except Nagarjuna Finance in 1986. Ashok Leyland Finance is the most aggressive player in the group financing on an average 38 percent of fixed assets by short term funds.

In the mixture group also short term funds are increasingly used by companies except Sakthi Finance in 1989 and '90 and World Link in 1986 and 1987. Sakthi Finance, a company with a long track record amassed large volume of funds for financing its activities. World Link Finance started its operation only in 1986 and during the initial year the fund requirement was comparatively low.

The financial policy analysis makes clear that sufficient long term funds are not with concerns to finance their fixed assets. Either they are not going for long term funds or they are not getting it. A detailed analysis of the various components of long term funds are essential at this juncture.

Table No. 5.22

FINANCING PATTERN-COMPANY WISE

(Rs. in Lakhs)

	1986			1987			1988			1989			1990-91		
Name of Companies	FA	LTF	DEF %	FA	LTF	DEF %	FA	LTF	DEF %	FA	LTF	DEF %	FA	LTF	DEF %
First Leasing	4136	3613	13	6313	5208	18	8680	6425	26	11860	8892	25	15562	10225	34
20th Century Finance	7256	6014	17	9897	6941	30	13009	8754	33	17403	12199	43	19451	13700	30
Grover Leasing	607	575	5	756	811	+	834	1026	+	745	754	+	946	890	6
PL Finance	787	760	3	1002	848	15	1136	926	18	1256	1057	16	1335	1118	16
United Leasing	438	370	16	754	560	26	784	637	19	1019	834	18	1344	970	28
World Link Finance	12	203	+	528	682	+	761	725	5	1195	898	25	1195	898	25
Midwest Leasing	927	790	15	1330	1094	18	2266	2060	9	2701	2355	13	2674	2481	7
DCL Finance	514	448	13	762	658	14	1258	1065	15	1548	1311	15	1909	1547	19
New Century Leasing	596	465	22	870	698	20	1329	874	34	1849	1263	32	2301	1694	26
Sakthi Finance	1436	1390	3	3202	3083	4	5572	5313	5	8688	8671	<1	10078	10296	+
Ashok Leyland Finance	1257	826	34	2559	1480	42	5358	3381	37	9729	5618	42	16377	10615	35
Sundaram Finance	17630	13820	22	19429	14913	23	21490	17357	19	27316	21195	22	36875	28504	23
Integrated Finance	772	658	15	1700	1208	29	2107	1495	29	2364	1685	29	2740	1996	27
Kothari Orient Finance	437	349	20	523	447	15	660	549	17	733	621	15	1027	885	14
Nagarjuna Finance	2650	2760	+	4341	3790	13	5170	4498	13	5845	4949	15	7416	6336	15

Source : Computed from Company Annual Reports FA = Fixed Assets; LTF = Long Term Fund. DEF % = Deficit Percentage

5.32 Analysis of Long Term Funds

Long Term funds can be broadly grouped into Net Worth and borrowings. Net Worth includes share capital and reserves while borrowings consist of debentures, financial institutions loans, bank borrowings and public deposits.

The following table shows the relative proportion of various components in the long term funds of the industry at a glance.

Table No. 5.23

PROPORTION OF VARIOUS COMPONENTS IN LONG TERM FUND

Long Term Fund (Rs. in Lakhs)	33041	42421	55079	72302	92155
Net Worth (%)	21	19	18	17	16
Debentures and Financial Institution loans (%)	17	17	16	18	24
Bank (%)	19	23	22	23	19
Public Deposits (%)	43	41	44	42	41

Source : Computed from Company Annual Reports

The table highlights the excessive dependence of leasing industry on public deposits. The contribution of bank loan to the industry is steady while debentures and financial institution loans increased from 17 percent to 24 percent. The proportion of net worth registers a decline in long term funds over the years.

5.33 Since funds with companies increase with the passage of time, the long term funds of companies are analysed grouping the companies into old and new companies based on the number of annual reports in table No. 5.24.

Public deposits dominate the long term fund of the old companies. It forms on an average 50 percent of the long term funds of such companies.

Debentures and term loans of financial institutions come second with 18 percent on an average. Bank loan and net worth constitute 16 percent. Among these while the share of Bank loan increased from 13 percent to 20 percent in '89 and later reduced to 17 percent in 1990-91, the share of Net worth declined from 17 percent in 1986 to 14 percent in 1990-91.

In the new group, bank loan is the major component of Long term fund till 1990. Net Worth too forms a significant portion of the long term fund. Financial insitution loans and debentures and public deposits have increased over the years.

Company wise analysis makes it clear that only Sundaram Finance and Sakthi Finance have been able to mobilise substantial public deposits (due to their long track record and reputation) among the old companies.

Table No. 5.24 PERCENTAGE OF BANK, PUBLIC DEPOSIT DEB & F.I. LOANS & N.W. IN TOTAL LONG TERM FUND

	1986				1987				1988				1989				1990-91			
NAME OF COMPANIES	B.	P.D.	D&FI	NW	B.	P.D.	D&FI	NW	B.	P.D.	D&FI	NW	B.	P.D.	D&FI	NW	B.	P.D.	D&FI	NW
OLD COMPANIES																				
Sundaram Finance	16	75	-	9	18	73	-	9	14	74	-	12	20	68	-	12	22	59	7	12
Sakthi Finance Ltd.	12	73	-	15	7	79	-	14	6	79	-	15	4	78	6	12	3	81	4	12
First Leasing Company	11	34	24	31	10	32	35	23	14	33	30	23	23	26	32	19	20	26	38	16
20th Century Finance	9	5	57	29	19	4	50	27	26	6	45	23	29	7	43	21	14	15	51	20
TOTAL	13	52	18	17	16	50	18	16	16	52	15	17	20	48	17	15	17	48	21	14
NEW COMPANIES																				
United Leasing	22	2	31	45	45	3	22	30	33	12	25	30	28	12	35	25	25	14	35	26
World link finance	-	-	-	100	59	2	-	39	46	15	4	35	35	19	12	34	35	19	22	34
Grover Leasing	31	24	-	45	30	37	-	33	31	40	-	29	29	28	-	43	34	24	5	37
P.L. Finance	30	16	21	33	31	17	19	33	23	24	21	32	14	25	34	27	13	30	27	30
Integrated Finance	20	4	60	16	36	8	39	17	32	13	40	15	17	23	45	15	22	24	39	15
Nagarjuna Finance	34	28	22	16	46	24	16	14	38	29	19	14	37	27	21	15	32	31	17	20
Midwest Leasing	37	9	-	54	48	12	-	40	47	15	12	26	39	16	20	25	35	22	17	26
D.C.L. Finance	34	6	10	50	39	11	13	37	41	20	14	25	33	24	21	22	20	25	36	19
New Century Leasing	58	9	-	33	55	20	-	25	49	25	-	25	43	19	17	21	46	20	18	16
Kothari Orient Finance	34	33	11	22	31	40	7	22	27	47	5	21	29	47	5	19	31	38	13	18
Ashok Leyland Finance	60	5	-	35	26	15	34	25	23	33	30	14	22	35	14	19	10	29	45	16
TOTAL	35	16	17	32	41	18	16	25	35	26	19	20	30	27	22	21	23	27	30	20
Grand Total	**19**	**43**	**17**	**21**	**23**	**41**	**17**	**19**	**22**	**44**	**16**	**18**	**23**	**42**	**18**	**17**	**19**	**41**	**24**	**16**

Source: Computed from company Annual Reports; B = Bank Loan; PD = Public Deposit; D&FI = Debentures and Financial Insitution Loan; NW = Net Worth;

5.34 The individual companies in the new group, naturally rely more on net worth in the initial years. Bank loan too is a major component of their long term fund. Financial Institution loans are enjoyed by companies like Grover, Midwest and New Century leasing only after 1987.

To conclude, the fund pattern of companies are different. Public deposits are predominant only in long term fund of established companies with longer track records. Many new companies rely on bank borrowings excessively in their initial years. Later, these companies increased their borrowings from other sources as well.

Thus, leasing industry is found to have a mixed capital structure of equity and debt. They start with equity funds of various magnitudes matching their asset requirement. The pattern of financing of some new leasing companies in their inception period is give below in table no. 5.25.

Table No. 5.25

PATTERN OF FINANCING

Name of the company	First year	Amount of Capital
New Century Leasing	1985	128 lakhs Equity only
D.C.L. Finance	1984	184 Lakhs Equity only
World Link Finance	1986	193 Lakhs Equity and 03 Lakhs Borrowed Fund.

Source : Compiled from Company Annual Reports

5.35 Share Capital is the basic component of long term fund of all companies. Very few companies in the sample have resorted to further public issues for augmenting their resources, though it is practically cost free, during the period covered in the study. Most of the leasing companies are newly incorporated and additional equity issue may not be feasible within a short span of five years as observed from table no. 5.26.

Unlike manufacturing companies, leasing companies have no gestation period and can report profits in the initial year itself. This enables them to retain funds as reserves. Reserves of leasing companies are either general reserve or statutory reserve. Reserves of older companies are naturally larger than the young and new companies. This is presented in table no. 5.27. Hence their net worth is also high. Only old leasing companies have been able to capitalise their reserves.

5.36 Net Worth determines the eligibility of borrowings of leasing companies. The additional business of the industry is being financed by borrowings (percentage of networth in long term fund steadily declines as shown in tbale no. 5.28) from 21 to 16 over the years. Introducing debt in the capital structure enhances the leverage and allows trading on equity.

Table No. 5.26

LTF = Long Term Fund

EQUITY CAPITAL AND LONG TERM FUNDS

(Rs. in Lakhs)

Old Companies

Name of Companies	1986 Equity	1986 LTF	1986 %age	1987 Equity	1987 LTF	1987 %age	1988 Equity	1988 LTF	1988 %age	1989 Equity	1989 LTF	1989 %age	1990-91 Equity	1990-91 LTF	1990-91 %age	
First Leasing Company	370	3613	10	380	5208	7	630	6425	10	780	8892	9	780	10225	10	Public issue
20th Century Leasing	634	6014	6	634	6941	9	888	8754	10	888	12199	7	888	13700	6	Amalgamation + Bonus issue
Sakthi Finance	97	1390	7	204	3083	7	309	5313	6	309	8671	4	309	10296	3	Public issue
Sundaram Finace	600	13820	4	600	14913	4	600	17357	3	600	21195	3	600	28504	2	-
TOTAL	1701	24837	7	1818	30145	6	2427	37849	6	2577	50957	5	2577	62725	4	
New Companies																
United Leasing	110	370	30	111	560	20	112	637	18	112	834	13	112	970	12	-
World Link Finance	174	203	86	247	682	36	248	725	34	248	898	28	248	898	28	-
Midwest Leasing	391	790	49	392	1094	36	393	2060	19	400	2355	17	400	2481	16	-
DCL Finance	211	448	47	223	658	34	225	1065	21	225	1311	17	226	1547	15	-
New Century Leasing	146	465	31	146	698	21	147	874	17	148	1263	12	148	1694	9	-
Grover leasing	248	575	43	248	811	31	249	1026	24	249	754	33	249	890	28	-
Ashok Leyland Finance	244	826	30	249	1480	17	250	3381	7	500	5618	9	500	10615	5	Public issue
PL Finance	196	760	26	197	848	23	200	920	21	200	1057	19	200	1118	18	-
Integrated Finance	100	658	15	196	1208	16	197	1495	13	197	1685	12	197	1996	10	Public issue
Kothari Orient Finance	70	349	20	84	447	19	85	549	15	85	621	14	112	885	13	Right issue
Nagarjuna Finance	241	2760	9	242	3790	6	243	4498	5	244	4949	5	655	6336	10	Public issue
TOTAL	2131	8204	26	2335	12276	19	2349	17230	14	2608	21345	12	3047	29430	10	
Grand Total	**3832**	**33041**	**12**	**4153**	**42421**	**10**	**4776**	**55079**	**9**	**5185**	**72302**	**7**	**5624**	**92155**	**6**	

Source : Computed from Company Annual Reports

Table No. 5.27

R = Reserves
LTF = Long Term Funds

RESERVES AND LONG TERM FUNDS

(Rs. in Lakhs)

Old Companies	1986			1987			1988			1989			1990-91		
Name of Companies	R	LTF	%age	R	LTF	%age	R	LTF	%age	R	LTF	%age	R	LTF	%age
First Leasing	730	3613	20	820	5208	16	850	6425	13	930	8892	10	903	10225	9
20th Century Leasing	1086	6014	18	1226	6941	18	1128	8754	13	1637	12199	13	1869	13700	14
Sakthi Finance	111	1390	08	230	3083	7	478	5313	9	749	8671	9	938	10296	9
Sundaram Finance	659	13820	05	800	14913	5	1508	17357	9	1983	21195	9	2723	28504	10
TOTAL	2586	24837	10	3076	30145	10	3964	37849	10	5299	50957	10	6433	62725	10
New Companies															
United Leasing	54	370	15	57	560	10	76	637	12	99	834	12	137	970	14
World Link Finance	7	203	3	20	682	3	6	725	1	57	898	6	57	898	6
Midwest Leasing	33	790	4	47	1094	4	153	2060	7	184	2355	8	239	2481	10
DCL Finance	13	448	3	21	658	3	45	1065	4	66	1311	5	72	1547	5
New Century Leasing	9	465	2	25	698	4	71	874	8	119	1263	9	128	1694	8
Grover Leasing	10	575	2	16	811	2	44	1026	4	72	754	10	84	890	9
Ashok Leyland Finance	48	826	6	116	1480	8	215	3381	6	540	5618	10	1147	10615	11
PL Finance	58	760	8	81	848	10	99	920	11	87	1057	8	136	1118	12
Integrated Finance	7	658	1	11	1208	1	23	1495	2	54	1685	3	96	1996	5
Kothari Orient Finance	8	349	2	15	447	3	28	549	5	35	621	6	50	885	6
Nagarjuna Finance	200	2760	7	270	3790	7	376	4498	8	487	4949	10	600	6336	9
TOTAL	447	8204	5	679	12276	6	1136	17230	7	1800	21345	8	2746	29430	9
Grand Total	3033	33041	9	3755	42421	9	5100	55079	9	7099	72302	10	9179	92155	10

Source : Computed from Company Annual Reports

Table No. 5.28

NET WORTH AND LONG TERM FUND

OLD COMPANIES : Companies with more than 6 Annual Reports as on 1986
NEW COMPANIES : Companies with Six or Less than Six Annual Reports as on 1986

NW = Net Worth ie. Share Capital + Reserves
LTF= Long Term Fund
(Rs. in Lakhs)

Old Companies	1986			1987			1988			1989			1990-91		
Name of Companies	NW	LTF	%age	NW	LTF	%age	NW	LTD	%age	NW	LTF	%age	NW	LTF	%age
Sundaram Finance	1259	13820	9	1400	14913	9	2107	17357	12	2583	21195	12	3323	28504	12
Sakthi Finance	208	1390	15	434	3083	14	787	5313	15	1058	8671	12	1247	10296	12
First Leasing company	1102	3613	31	1202	5208	23	1479	6425	23	1710	8892	19	1683	10225	16
20th Century Finance	1720	6014	29	1860	6941	27	2016	8754	23	2524	12199	21	2756	13700	20
TOTAL	4289	24837	17	4896	30145	16	6389	37849	17	7875	50957	15	9009	62725	14
New Companies															
United Leasing	165	370	45	168	560	30	188	637	30	211	834	25	249	970	26
World Link Finance	201	203	99	267	682	39	254	725	35	305	898	34	305	898	34
Grover Leasing	258	575	45	264	811	33	293	1026	29	321	754	43	333	890	37
PL Finance	254	760	33	278	848	33	298	920	32	287	1057	27	335	1118	30
Integrated Finance	107	658	16	206	1208	17	219	1495	15	251	1685	15	293	1996	15
Nagarjuna Finance	433	2760	16	512	3790	14	619	4498	14	731	4949	15	1255	6336	20
Mid West Leasing	424	790	54	439	1094	40	545	2060	26	584	2355	25	639	2481	26
DCL Finance	224	448	50	244	658	37	270	1065	25	291	1311	22	298	1547	19
New Century Leasing	155	465	33	171	698	24	218	874	25	266	1263	21	276	1694	16
Kothari Orient Finance	78	349	22	100	447	22	113	549	21	119	621	19	162	885	18
Ashok Leyland Finance	291	826	35	365	1480	25	464	3381	14	1040	5618	19	1647	10615	16
TOTAL	2590	8204	32	3014	12276	25	3481	17230	20	4406	21345	21	5792	29430	20
Grand Total	**6879**	**33041**	**21**	**7910**	**42421**	**19**	**9870**	**55079**	**18**	**12281**	**72302**	**17**	**14801**	**92155**	**16**

Source : Computed from company Annual Reports.

Table No. 5.30

DEBT EQUITY RATIOS COMPANYWISE

(Rs. in Lakhs)

	1986			1987			1988			1989			1990–91		
Name of companies	Equity	Debt	Ratio	Equity	Debt	Ratio	Equity	Debt	Ratio	Equity	Debt	Ratio	Equity	Debt	Ratio
Predominantly Leasing Companies															
First Leasing	1101	738	.67	1202	1532	1.3	1479	1680	1.14	1710	2586	1.5	1683	3402	2
20th Century Finance	1720	3434	2	1860	3468	1.9	2016	3932	1.95	2524	5225	2.1	2756	6979	2.53
Grover Leasing	258	-	-	265	-	-	293	-	-	321	-	-	333	38	.11
PL Finance	254	157	.62	278	157	.56	298	182	.61	287	336	1.17	336	293	.87
TOTAL	3333	4329	1.3	3605	5157	1.4	4086	5794	1.4	4742	8147	1.7	5108	10712	2.1
Mixture of Leasing and Hire Purchase Companies															
United Leasing	165	118	.72	168	121	.72	188	157	.84	211	287	1.4	249	339	1.4
World Link Finance	201	-	-	267	-	-	254	-	-	305	-	-	305	-	-
Midwest leasing	424	-	-	439	-	-	545	230	.42	584	489	.84	639	426	.67
DCL Finance	224	43	.19	244	89	.36	270	147	.54	291	267	.92	298	559	1.88
New Century Leasing	155	-	-	171	-	-	218	-	-	267	200	.75	276	292	1.06
Sakthi Finance	208	-	-	434	-	-	787	-	-	1058	436	.41	1247	455	.36
TOTAL	1737	161	.09	1723	210	.12	2262	534	.24	2716	1679	.62	3014	2071	.69
Predominantly Hire Purchase Companies															
Ashok Leyland Finance	291	-	-	365	500	1.4	465	1051	2.3	1040	1358	1.3	1647	4226	2.6
Sundaram Finance	1259	-	-	1400	-	-	2108	-	-	2583	-	-	3323	1000	.3
Integrated Finance	107	331	3	207	395	1.9	219	395	1.8	251	745	2.9	293	772	2.6
Kothari Orient Finance	78	39	.5	100	26	.26	113	26	.23	119	26	.22	112	113	1
Nagarjuna Finance	433	564	.13	512	587	1.2	619	841	1.4	731	953	1.3	1255	1063	.85
TOTAL	2168	934	.43	2584	1508	.58	3524	2313	.66	4724	3082	.65	6630	7174	1.1
Grand Total	**6878**	**5424**	**.8**	**7912**	**6875**	**.87**	**9872**	**8611**	**.88**	**12282**	**12908**	**1.05**	**14752**	**19957**	**1.35**

Source : Computed from Company Annual Reports

DEBT : FINANCIAL INSTITUTION LOAN AND DEBENTURES

EQUITY: NET WORTH ie. Share Capital + Reserves

Table No. 5.31

DEBT - EQUITY RATIOS

	1986	1987	1988	1989	1990-91
Debt/Equity	3.6:1	4.2:1	4.5:1	4.8:1	5.2:1

Source : Computed from Company Annual Reports

The ratios are then higher and goes on increasing over the year from 3.6 to 5.2.

It is observed from table No. 5.32 that the debt equity ratios of predominantly leasing group increase from 2:1 to 4:1 while predominantly hire purchase group reports a higher debt equity ratio of 7.5:1 though the ratio reduced to 6.3:1 over the years. For the mixture group too,the ratio went upto 5 from 1.4.

Company wise analysis shows that the older companies in the first group have high debt equity ratios than the new companies in the group. Larger volumes of business necessitated more borrowings for these companies enhancing their debt equity ratios. Companies in the hire purchase group report higher debt equity ratios than companies in the other groups.

In the mixture group, all new companies have a low ratio in the initial years as their volume of business is low. Sakthi Finance, an old company in the group, has a high debt equiy ratio.

Table No. 5.32

DEBTI EQUITY RATIOS

Rs. in Lakhs)

Name of Companies	1986 Equity	1986 Debt	1986 Ratio	1987 Equity	1987 Debt	1987 Ratio	1988 Equity	1988 Debty	1988 Ratio	1989 Equity	1989 Debt	1989 Ratio	1990-91 Equity	1990-91 Debt	1990-91 Ratio
Predominantly Leasing Companies															
First Leasing Company	1101	2513	2.3	1202	4005	3.3	1479	4947	3.3	1710	7178	4.2	1683	8543	5.1
20th Century Finance	1720	3219	2	1860	3762	2	2016	5963	3	2524	9336	3.7	2756	10807	4
Grover Leasing	258	314	1.2	265	545	2.1	293	734	2.5	321	433	1.3	333	557	1.7
PL Finance	254	507	2	278	570	2.1	298	622	2.1	287	770	2.7	336	780	2.3
TOTAL	3333	6553	2	3605	8882	2.5	4086	12266	3	4842	17717	3.7	5108	20687	4
Mixture of Leasing and Hire Purchase Companies															
United Leasing	165	207	1.3	168	390	2.3	188	448	2.4	211	623	3	249	721	3
World Link Finance	201	3	-	267	416	1.6	254	472	2	305	594	2	305	594	2
Mid West Leasing	424	366	.9	439	653	1.5	545	1513	2.8	584	1772	3	639	1840	3
DCL Finance	224	224	1	244	414	1.7	270	795	2.9	291	1020	3.5	298	1251	4.2
New Century Leasing	155	309	2	171	527	3.1	218	656	3	267	997	3.7	276	1417	5.1
Sakthi Finance	208	1182	6	434	2649	6.1	787	4525	5.7	1058	7612	7.2	1247	9049	7.3
TOTAL	1737	2501	1.4	1723	5049	2.9	2262	8409	3.7	2716	12618	4.6	3014	14872	5
Ashok Leyland Finance	291	534	1.8	365	1114	3.1	465	2916	6.3	1040	4395	4.2	1647	8968	5.4
Sundaram Finance	1259	12560	10	1400	13513	9.7	2108	15249	7.2	2583	18612	7.2	3323	25181	7.6
Integrated Finance	107	551	5	207	1000	4.8	219	1275	5.8	251	1433	5.7	293	1701	5.8
Kothari orient Finance	78	272	3.5	100	348	3.5	113	436	3.9	119	502	4.2	112	723	6.5
Nagarjuna Finance	433	2324	5.4	512	3279	6.4	619	3879	6.3	731	4218	5.8	1255	5080	4
TOTAL	2168	16241	7.5	2584	19254	7.5	3524	23755	6.7	4724	29160	6.2	6630	41653	6.3
Grand Total	**6878**	**25085**	**3.6**	**7912**	**33185**	**4.2**	**9872**	**44430**	**4.5**	**12282**	**59495**	**4.8**	**14752**	**77212**	**5.2**

Source : Computed from Company Annual Reports

DEBT ALL BORROWINGS, EQUITY NET WORTH ie., Share Capital + Reserves and surplus

5.39 A higher debt equity ratio is justifiable as leasing is a capital intensive industry blocking nearly 86 percent of the funds in fixed assets. Generally, when debt is high, risk also is higher. But in a leasing company, operating risk is comparatively low due to regular and certain cash inflows in the form of lease rentals over the stipulated period. Hence, the capital structure of leasing companies can be highly geared.

5.40 **Eligibility to borrow:**

The leasing companies are eligible to borrow ten times their net worth. In the wake of the apparant shortage of borowed funds in the industry, it is desired to find out the extent of utilisation of their eligibility to borrow. It is found that only about 50 percent of eligibility is utilised by the industry. The table below gives the percentage of eligibility utilised over the years.

Table No. 5.33

ELIGIBILITY UTILISATION

(Rs. in Lakhs)

	1986	1987	1988	1989	1990-91
Eligibility	68,774	79,114	98,712	1,22,814	1,47,527
Utilised Amount	26,159	34,549	45,564	60,095	77,515
2/1	38%	44%	46%	49%	53%

Source : Computed from Company Annual Reports

5.41 A further analysis reveals that old leasing group have enjoyed upto 60 percent of their eligibility while new companies could exploit only 40 percent of the eligibility as shown in table no. 5.34

Table No. 5.34

ELIGIBILITY UTILISED COMPARISON

(Percentage)

	1986	1987	1988	1989	1990-91
Old Companies	48	52	49	55	60
New Companies	22	31	41	39	41

Source : Computed from Company annual reports

The older companies are established in the field, have more business, good reputation and have been in a position to get more credit. Still, 40 percent of the eligibility remain untapped.

Companywise analysis in table no. 5.35 shows that Sundaram Finance and Sakthi Finance are using about ¼ of their eligible borrowing. Sundaram Finance is using about cent percent in 1986) Other companies in the old group are seen to increase their utilisation percentage steadily.

Table No. 5.35

ELIGIBILITY UTILISATION COMPANYWISE

(Rs, in Lakhs)

Old Companies	1986			1987			1988			1989			1990–91		
Name of companies	EL	Loan used	%age	EL	Loan used	%age	EL	Loan used	%age	EL	Loan used	%age	EL	Loan used	%age
Sundaram Finance	12586	12556	100	14000	13513	97	21078	15248	72	25832	18612	72	33233	25181	76
Sakthi Finance	2078	1182	57	4342	2649	61	7872	4525	58	10580	7612	72	12468	9049	73
First Leasing Company	11017	2513	23	12019	4005	33	14786	4947	33	17097	7179	42	16831	8543	51
20th Century Leasing	17197	4293	25	18600	5081	27	20161	6737	33	25243	9673	38	27563	10943	40
TOTAL	42878	20544	48	48961	25248	52	63897	31457	49	78752	43076	55	90095	53716	60
New Companies															
United Leasing	1647	207	13	1681	390	23	1876	448	24	2112	624	30	2493	721	29
World Link Finance	2011	3	–	2672	416	16	2537	472	19	3051	594	20	3051	594	19
Grover Leasing	2579	314	12	2646	547	21	2929	734	25	3213	433	13	3333	558	17
PL Finance	2540	507	20	2781	570	20	2982	622	21	2865	770	27	3356	780	23
Integrated Finance	1073	551	51	2066	1000	48	2194	1275	58	2510	1433	57	2933	1701	58
Nagarjuna Finance	4327	2324	54	5117	3320	65	6186	3879	63	7306	4218	58	12553	5083	41
Midwest Leasing	4238	366	9	4387	653	15	5453	1513	28	.5835	1772	30	6389	1841	29
DCL Finance	2239	224	10	2437	414	17	2703	795	29	2909	1020	35	2979	1251	42
New Century Leasing	1550	309	20	1714	527	31	2182	1017	47	2666	1259	47	2759	1579	57
Kothari Orient Finance	777	272	35	998	348	35	1125	436	39	1194	502	42	1121	723	65
Ashok Leyland Finance	2914	534	18	3654	1114	31	4649	2916	63	10403	4395	42	16465	8968	55
TOTAL	25896	5615	22	30153	9301	31	34815	14107	41	44062	17019	39	57431	23798	41
Grand Total	**68774**	**26159**	**38**	**79114**	**34549**	**44**	**98712**	**45564**	**46**	**122814**	**60095**	**49**	**147527**	**77517**	**53**

Source : Computed from Company Annual Reports

EL = Eligibility

Among the new companies, Integrated Finance, Nagarjuna Finance, and Kothari Orient Finance are seen to utilise larger percentage of eligibility (Integrated Fianance -51, Nagarjuna Finance - 54, Kothari Orient Finance - 35) compared to others in 1986 itself. By 1990-91, many companies increased their eligibility utilisation. But only Integrated Finance, Nagarjuna Finance, New Century Leasing, Kothari Orient Finance and Ashok Leyland Finance have utilised more than 50 percent of eligibility.

5.42 It leads us to conclude that only companies with connection to reputed group like Sundaram Finance, Sakthi Finance, Nagarjuna Finance, Integrated Finance, New Century Leasing, Ashok Leyland Finance have used a higher percentage of their eligibility to borrow.

But, inspite of the shortage of long term funds to finance their main business, even these companies are not utilising the available limits of borrowal. The reasons for this state of affairs is to be examined.

5.43 The most obvious reason is the lowering of the profit margin i.e., the difference between the borrowing rate and the lending rate of companies. The EBIT is not found to increase with additional borrowings of the industry. In fact, it shows a decline during 1988 and 1989 as revealed in the following table.

Table No. 5.36

THE EBIT AND BORROWINGS

(Rs. in Lakhs)

Borrowings	25085	33185	44430	59495	77212
EBIT	4931	6523	8315	11195	15057
2/1	20%	20%	19%	19%	20%

Source : Computed from Company Annual Reports

Group wise analysis in Table No.5.37 shows that EBIT as a percentage of borrowings is decreasing from 26% to 20% for the leasing group and from 23% to 18% for the mixture group. But for the hire Purchase group, EBIT reports an increase from 17 percent to 20 percent.

Company wise analysis also reveals that all companies in the leasing group and mixture group except New Century Leasing reports a decline in EBIT percent. (New century Leasing shows a sudden increase in its leasing activities from 1988 onwards)

In Hire purchase group, EBIT of all companies are found to increase except Nagarjuna, which is having a steady EBIT. The borrowings of this group is more than the other groups and their volume of leasing business has not declined as in other groups.

Table No. 5.37

EBIT AND BORROWINGS COMPANYWISE

(Rs. in Lakhs)

Name of the company	1986 Borrow-ings	1986 EBIT	1986 %age	1987 Borrow-ings	1987 EBIT	1987 %age	1988 Borrow-ings	1988 EBIT	1988 %age	1989 Borrow-ings	1989 EBIT	1989 %age	1990-91 Borrow-ings	1990-91 EBIT	1990-91 %age
Predominantly Leasing companies															
First Leasing company	2513	578	23	4005	802	20	4947	822	17	7178	1322	18	8543	1682	20
20th Century Finance	3219	890	28	3762	970	26	5963	1233	21	9336	1452	16	10807	2161	20
Grover Leasing	314	88	28	545	107	20	734	131	18	433	126	29	557	115	21
PL Finance	507	142	28	570	157	28	622	163	26	770	175	23	780	165	21
TOTAL	6553	1698	26	8882	2036	23	12266	2349	19	17717	3075	17	20687	4127	20
Mixture of Leasing and Hire purchase Companies															
United Leasing	207	66	32	390	63	16	448	105	23	623	131	21	721	165	23
World Linkd Finance	3	8	-	416	37	9	472	88	19	594	75	13	594	75	13
Mid West Leasing	366	119	33	653	162	25	1513	239	19	1772	395	22	1840	392	21
DCL Finance	224	69	31	414	106	26	795	148	19	1020	188	18	1251	213	17
New Century Leasing	309	44	14	527	109	21	656	172	26	997	251	25	1417	303	21
Sakthi Finance	1182	223	19	2649	465	18	4525	806	18	7612	1197	16	9049	1463	16
TOTAL	2291	529	23	5049	942	19	8409	1613	19	12618	2237	18	14872	2611	18
Predominantly Hire Purchase Companies															
Ashok Leyland Finance	534	129	24	1114	310	28	2916	576	20	4395	1372	31	8968	2418	27
Sundaram Finance	12560	1967	16	13513	2386	18	15249	2659	17	18612	3212	17	25181	4409	18
Integrated Finance	551	76	14	1000	147	15	1275	241	19	1433	283	20	1701	[illegible]	19
Kothari Orient Finance	272	46	17	348	81	23	436	102	23	502	112	22	723	[illegible]	[illegible]
Nagarjuna Finance	2324	486	21	3279	621	19	3879	775	20	4218	905	21	5080	1040	20
TOTAL	16241	2704	17	19254	3545	18	23755	4353	18	29160	5883	20	41653	8319	20
Grand Total	**25085**	**4931**	**20**	**33185**	**6523**	**20**	**44430**	**8315**	**19**	**59495**	**11195**	**19**	**77212**	**15057**	**20**

Source : Computed from Company Annual Reports

EBIT - Earnings Before Interest and Tax

5.44 The predominantly leasing and mixture groups have reported a decline in their lease business and their lease income too registered a decrease. Increased volume of hire purchase business of these companies requried more funds. But, the earnings are not as attractive as during the earlier times.

Naturally, the companies may not be interested in introducing further credit into their capital structure as it would reduce the spread between the rate of interest and rate of return.

5.45 **Low Spread:**

The spread between the rate of interest and rate of return is less than 3 percent for the industry as observed in the following table.

Table No. 5.38

SPREAD BETWEEN RATE OF INTEREST AND RATE OF RETURN

	1987	1988	1989	1990-91
Average rate of interest	15.1	14.9	15	15.7
Return on Investment	17.3	17.1	17.6	18.3
Spread	2.2	2.2	2.6	2.6

Source : Computed from Company Annual Reports

Table No. 5.39

SPREAD BETWEEN RATE OF INTEREST AND RETURN ON INVESTMENT COMPANYWISE

(On Average Borrowed Fund and Capital Employed)

(Percentages)

	1987			1988			1989			1990-91		
Name of Companies	Interest	ROI	Margin	Interest	ROI	Margin	Interest	ROI	Margin	Interest	ROI	Margin
First Leasing	17	18	+1	15	14	-1	16	17	+1	16	18	+2
20th Century Finance	14	15	+1	14	16	+2	12	14	+2	15	17	+2
Grover Leasing	14	15	+1	15	14	-1	16	14	-2	15	14	-1
PL Finance	16	20	+4	16	18	+2	16	18	+2	14	15	+1
United Leasing	14	14	-	14	17	+3	15	18	+3	16	18	+2
World Link Finance	11	8	-3	17	13	-4	12	9	-3	11	8	-3
Midwest Leasing	15	17	+2	14	19	+5	18	18	-	16	16	-
DCL Finance	15	19	+4	13	17	+4	14	16	+2	15	15	-
New Century Leasing	15	19	+4	16	20	+4	20	22	+2	20	23	+3
Sakthi Finance	15	21	+6	13	19	+6	13	17	+4	14	15	+1
Ashok Leyland Finance	21	27	+6	19	24	+5	25	31	+6	25	30	+5
Sundaram Finance	15	17	+2	15	16	+1	14	17	+3	14	18	+4
Integrated Finance	15	16	+1	14	18	+4	16	18	+2	15	17	+2
Kothari Orient Finance	16	20	+4	16	20	+4	15	19	+4	14	18	+4
Nagarjuna Finance	17	19	+2	17	19	+2	17	19	+2	18	18	-

Source : Computed from Company Annual Reports

ROI = Return on Investments

An examination of the spread between interest and return for individual companies in table No. 5.39 reveals that in predominantly leasing group, Grover Leasing has a negative margin, while others report positive margins.

In the mixture group, United Leasing, New Century Leasing and Sakthi Finance have positive spreads. While it is break-even for Mid West and DCL Finance, World Link Finance reports a negative margin.

In the Hire purchase group there is a wider spread for all companies except Nagarjuna which shows a break-even position. (EBIT is high for all companies in the group)

The reason for the low spread can be attributed to the reduced earnings as well as the increased cost of external funding. In order to enquire into the cost of borrowed funds, an analysis of the various components of borrowed funds and their magnitude are attempted. The funding pattern, in its turn, is influenced by the cost of financing as well as the availability of funds.

5.46 Borrowed funds and Rate of Interest

The following table illustrates the extent of borrowed funds and the effective rate of interest.

Table No. 5.40

BORROWED FUNDS AND RATE OF INTEREST

(Rs. in lakhs)

	1987	1988	1989	1990-91
Average borrowed fund	30335	39858	52612	68688
Finance Expense	4573	5944	7869	10774
Effective interest rate	15.1%	14.9%	15%	15.7%

Source : Computed from Company Annual Reports

The reduction in financial expense in 1988 is due to the decline in the rate of interest on debentures and company deposits by one percent. (from Ist April 1987, interest rate on debentures & company deposits are reduced from 15 percent to 14 percent).

5.47 Besides, during the year 1988, young and small leasing companies managed to enjoy institutional loans which are relatively cheaper than bank term loans. These companies had to depend on bank borrowings or public deposits for their initial requirements (besides net worth) as they were not eligible to get institutional loans or issue debentures. But they failed to canvass much public deposits, as the common public preferred only established group companies with longer track record. Thus, bank borrowing formed the inevitable source of financing of such companies.

5.48 In order to worsen the situation, Reserve Bank of India restricted banks from offering term loans to leasing companies from 1988 onwards. Thereafter, leasing companies could enjoy only cash credit and that too at a higher interest rate of 17.5 percent. Reserve Bank of India directives frequently revised the interest rates on cash credits pushing the lending rates to 22.5 percent as on October 1, 1991.

The steep increase in the rate of bank interest from 17.5 percent to 22.5 percent boosted the effective interest rate to 15.7 percent in 1990-91. Therefore, in spite of the reduction in the percentage of bank borrowing in total borrowings during 1990-91, the leasing industry has not been able to reduce the financial expenses.

5.49 Companywise analysis in tbale no. 5.41 shows that inspite of the huge debt equity ratio, Sundaram Finance and Sakthi Finance have been able to report comparatively lower interest rates (around 14 percent). A further probe into their borrowings reveals that public deposits dominate their borrowings (as seen in table 5.24) On the other hand, New Century Leasing and Nagarjuna Finance with high debt equity ratios report higher interest rates of around 18 percent due to the predominance of bank borrowings in their total borrowings. Ashok Leyland

Table No. 5.41

AVERAGE BORROWINGS AND FINANCE EXPENSES

(Rs. in Lakhs)

Name of Companies	1987 Average Borrowings	1987 Finance Expense	1987 % age	1988 Average Borrowings	1988 Finance Expense	1988 % age	1989 Average Borrowings	1989 Finance Expense	1989 %age	1990-91 Average Borrowings	1990-91 Finance Expense	1990-91 % age
Predominantly Leasing Companies												
First Leasing	3258	564	17	4475	672	15	6062	968	16	7861	1224	16
20th Century Finance	4687	636	14	5910	810	14	8206	968	12	10309	1557	15
Grover Leasing	431	59	14	640	98	15	583	92	16	495	72	15
PL Finance	539	84	16	596	93	16	696	110	16	776	107	14
TOTAL	8916	1343	15	11620	1673	14	15546	2138	14	19440	2960	15
Mixture of Leasing and Hire - Purchase Companies												
United Leasing	299	42	14	420	58	14	536	79	15	672	107	16
World Link Finance	209	22	11	443	77	17	532	65	12	593	65	11
Midwest Leasing	510	75	15	1084	149	14	1643	294	18	1807	290	16
DCL Finance	319	49	15	605	79	13	908	127	14	1134	168	15
New Century Leasing	419	64	15	592	97	16	826	163	20	1207	245	20
Sakthi Finance	1916	283	15	3588	480	13	6071	785	13	8332	1145	14
TOTAL	3671	535	15	6731	940	14	10515	1513	14	13745	2020	15
Predominantly Hire Purchase Companies												
Ashok Leyland Finance	825	169	21	2016	383	19	3747	924	25	6773	1699	25
Sundaram Finance	13036	1898	15	14381	2103	15	16931	2313	14	21897	2962	14
Integrated Finance	776	116	15	1138	160	14	1355	210	16	1569	231	15
Kothari orient Finance	310	50	16	392	62	16	469	71	15	612	88	14
Nagarjuna Finance	2802	462	17	3579	623	17	4049	700	17	4650	814	18
TOTAL	17748	2695	15	21506	3331	16	26549	4218	16	35497	5794	16
Grand Total	**30333**	**4573**	**15**	**39856**	**5944**	**15**	**52610**	**7869**	**15**	**68684**	**10774**	**16**

Source : Computed from Company Annual Reports

Finance reports an exorbitant interest of 24 percent and seems to be an exception among the companies.

5.50 **Pattern of Borrowings:**

An examination of the borrowing pattern in table no. 5.42 shows that it consist of debentures, financial institution loans, bank loans and public deposits. Debentures form only a meagre part of the funds and many companies have not issued debentures at all. Debenture issues are subject to several conditions and formalities. Besides, they are costly and not popular among the public as it is a long term liability which cannot be redeemed before the stipulated period. Moreover, many new leasing companies were not eligible to issue debentures (Market price of shares should be more than the par value in the preceeding 6 months of the issue) Hence, there has been a stagnation in the volume of debenture utilised for funding the activities of leasing companies.

5.51 With liberal sanctioning of term loans by financial institutions from 1987-88 periods leasing companies shifted to term loans as an easy method of borrowings. Financial Institutions advance term loans for a period of 6 years at a rate of 14 percent.

5.52 Predominantly leasing companies with larger volumes of five year lease commitments utilise more debentures and financial institution loans in order to finance their leasing activities than predominantly hire purchase

Table No. 5.42

COMMON SIZE BALANCE SHEET FOR THE LEASING COMPANIES (BORROWINGS ONLY)

During 1986, 1987, 1988, 1990-91 (Percentage to Total Liabilities)

Name of Companies	Financial Institution Loans					Debentures					Bank Loans					Public Deposits				
	1986	1987	1988	1989	1990-91	1986	1987	1988	1989	1990-91	1986	1987	1988	1989	1990-91	1986	1987	1988	1989	1990-91
First Leasing	<1	<1	7	12	17	14	25	14	11	9	8	9	12	19	16	26	27	27	21	20
20th Century Finance	1	<1	10	19	29	34	27	20	13	12	8	17	22	23	12	4	3	5	6	12
Grover Leasing	–	–	–	–	4	–	–	–	–	–	27	27	29	27	30	16	28	36	26	22
PL Finance	–	–	3	15	10	18	14	13	12	11	26	24	19	11	11	13	14	20	21	25
United Leasing	–	–	3	12	13	24	16	11	9	8	16	34	19	18	15	2	2	7	7	8
DCL Finance	–	–	4	11	25	8	11	7	5	5	27	31	33	27	16	5	9	16	20	20
Midwest Leasing	–	–	9	17	14	–	–	–	–	–	30	37	38	31	29	7	9	12	13	19
New Century Leasing	–	–	–	9	11	–	–	–	–	–	41	41	29	25	30	7	15	15	11	13
Sakthi Finance	–	–	–	4	4	–	–	–	–	–	10	6	5	4	2	60	64	66	70	72
World Link Finance	–	–	–	–	–	–	–	–	–	–	–	48	36	18	18	–	1	12	13	13
Ashok Leyland Finance	–	20	18	12	19	–	–	–	–	5	39	15	13	11	6	3	9	18	18	17
Sundaram Finance	–	–	–	–	3	–	–	–	–	–	12	14	11	15	16	56	55	57	51	43
Kothari Orient Finance	–	–	–	–	8	8	5	4	3	2	25	24	21	23	25	24	31	37	38	30
Integrated Finance	–	–	–	14	13	38	23	18	17	15	15	25	23	12	16	03	06	09	16	17
Nagarjuna Finance	–	–	4	4	6	13	10	10	10	7	22	31	28	27	25	18	16	21	20	24

Source : Computed from Company Annual Reports

companies mainly with three year hire purchase commitments as shown in tbale no. 5.43.

Table No. 5.43

EXTENT OF UTILISATION OF DEBENTURES AND

FINANCIAL INSTITUTION LOANS

(Rs. in lakhs)

	Predominantly Leasing Co.			Predominantly Hire Purchase Co.		
Year	Deb. & F.I.	LTF	%	DEB. & F.I.	LTF	%
1986	3255	10962	30	934	18413	5
1987	3838	13808	28	2442	21838	7
1988	5019	17125	30	2313	27280	9
1989	7810	22902	24	3082	34068	9
1990-91	10576	25392	41	7174	48336	15

Source: Computed from Company Annual Reports

Deb. & F.I. = Debentures and Financial Institution Loans

As in the case of debentures, new leasing companies are not eligible to get accommodation from financial institution, abiding the various regulations.

5.53 Term Loans from Banks:

Many leasing companies depend more on bank loans in their initial years and bank loans constitute around 20 percent of all long term fund of the industry.

BL = Bank Loan

LTF = Long Term Fund

Table No. 5.44

BANK LOAN AND LONG TERM FUND

(Rs. in Lakhs)

Old Companies	1986			1987			1988			1989			1990-91		
Name of the companies	BL	LTF	%age	BL	LTF	%age	BL	LTF	%age	BL	LTF	%age	BL	LTF	%age
Sundaram Finance	2149	13820	16	2674	14913	18	2456	17357	14	4196	21195	20	6367	28504	22
Sakthi Finance	161	1390	12	225	3083	7	305	5313	6	371	8671	4	274	10296	3
First Leasing Company	413	3613	11	543	5208	10	908	6425	14	2085	8892	23	2087	10225	20
20th Century Leasing	555	6014	9	1329	6941	19	2315	8754	26	3551	12199	29	1945	13700	14
TOTAL	3278	24837	13	4771	30145	16	5984	37849	16	10203	50957	20	10673	62725	17
New Companies															
United Leasing	80	370	22	251	560	45	210	637	33	236	834	28	245	970	25
Grover Leasing	176	575	31	246	811	30	313	1026	31	221	754	29	300	890	34
PL Finance	229	760	30	263	848	31	214	920	23	143	1057	14	148	1118	13
Midwest Leasing	294	790	37	524	1094	48	973	2060	47	912	2355	39	860	2481	35
DCL Finance	152	448	34	254	658	39	435	1065	41	435	1311	33	304	1547	20
New Century Leasing	268	465	58	382	698	55	426	874	49	541	1263	43	780	1694	46
Integrated Finance	134	658	20	434	1208	36	484	1495	32	283	1685	17	46	1996	22
Kothari Orient Finance	118	349	34	138	447	31	146	549	27	181	621	29	275	885	31
Nagarjuna Finance	945	2760	34	1736	3790	46	1710	4498	38	1824	4949	37	2033	6336	32
Ashok Leyland Finance	497	826	60	391	1480	26	765	3381	23	1234	5618	22	1097	10615	10
World Link Finance	-	203	-	401	682	59	336	725	46	314	898	35	314	898	35
TOTAL	2893	8204	35	5020	12276	41	6012	17230	35	6324	21345	30	6802	29430	23
Grand Total	**6171**	**33041**	**19**	**9791**	**42421**	**23**	**11996**	**55079**	**22**	**16527**	**72302**	**23**	**17475**	**92155**	**19**

Source : Computed from Company Annual Reports

Groupwise analysis of bank loan in table no. 5.44 reveals that while the proportion of bank loan is only 13 percent for the old companies, it is 35 percent for the new companies in 1986. In spite of the uneconomical interest rate, they rely on bank borrowing as they have less access to other sources of borrowings.

5.54 Companywise analysis points out that among the old companies only Sakthi Finance, a successful company in canvassing public deposits, with a wide net work of branches, is seen to reduce the bank loan content from 12 percent to 3 percent of long term fund. There is even a reduction in the amount of loan in absolute terms from the 1989 level, during 1990-91 (371 lakhs to 274 lakhs).

Companies in the new group are able to reduce their dependence on bank loan with the passage of years only as they began to enjoy more institutional loans & public deposits.

5.55 Leasing companies are eligible to borrow from bank upto 3 times the net owned funds. But due to uneconomical interest rates, (22.5%) companies are reducing the volume of bank loans. During the year 1990-91 the percentage of bank loan came down from 20 percent in the previous year to 17 percent for old companies and from 30 percent to 23 percent for new companies. Certain companies like Midwest Leasing, DCL Finance, Ashok Leyland Finance, 20th Century Finance have even reduced the volume of bank loan in real termsas seen in table no. 5.44.

The companies have not utilised the full eligibility to raise bank loans. The relevant data is provided in table no. 5.45. It shows that the industry as such is using only around 40 percent of the eligible bank loan. The old companies are using on an average only 35 percent of their eligible loans, while new companies use 47 percent of the eligible loans.

5.56 Companywise analysis of utilisation of bank loan reveals that while Sundaram Finance uses more than 50 percent of their eligibility throughout, Sakthi Finance is using only less than 20 percent of eligibility among the old companies. New Century Leasing is using upto 94 percent of eligibility while PL finance is using only 15 percent. Ashok Leyland finance utilises 22 percent and Kothari Orient Finance uses 57 percent of eligibility limit.

Thus, there are noticeable differences among companies regarding the utilisation of bank loans. But there is an attempt on the part of many companies to reduce the volume of bank borrowings.

5.57 **Public Deposits**

As an alternative to Bank loan, many leasing companies intensified their public deposits canvassing.

Table No. 5.45

BANK LOAN - ELIGIBILITY UTILISATION (Rs. in Lakhs)

OLD COMPANIES	1986				1987				1988				1989				1990-91			
Name of Companies	NW	ELE	Loan	%age	NW	ELE	Loan	%age	NW	ELE	Loan	%age	NW	ELE	Loan	%age	NW	ELE	Loan	%age
Sundaram Finance	1257	3776	2149	57	1400	4200	2674	64	2107	6323	2456	39	2583	7750	4196	54	3323	9970	6367	64
Sakthi Finance	208	623	161	26	434	1302	225	17	787	2362	305	13	1058	3174	371	12	1247	3740	278	7
First Leasing	1102	3305	413	12	1202	3606	543	15	1479	4436	908	20	1710	5129	2085	41	1683	5049	2087	41
20th Century Leasing	1720	5159	555	11	1860	5580	1329	24	2016	6048	2315	38	2524	7573	3551	47	2756	8269	1945	24
TOTAL	4289	12863	3278	26	4896	14688	4771	32	6389	19169	5984	31	7875	23626	10203	45	9009	27028	10677	40
NEW COMPANIES																				
United Leasing	165	494	80	16	168	504	215	43	188	563	197	35	211	633	236	37	249	748	245	33
World Link Finance	201	603	-	-	267	801	401	50	254	761	336	44	305	915	314	34	305	915	314	34
Grover Leasing	258	774	176	22	264	794	246	31	293	879	313	36	321	964	221	23	333	1000	299	30
PL Finance	254	762	229	30	278	834	263	32	298	895	214	24	287	860	143	17	335	1007	148	15
Integrated Finance	107	321	134	42	206	620	434	70	219	658	484	74	251	753	283	38	293	880	446	51
Nagarjuna Finance	433	1298	945	73	512	1535	1736	113	619	1856	1709	92	731	2192	1824	83	1255	3766	2033	54
Midwest Leasing	424	1271	295	23	439	1316	523	40	545	1636	973	59	584	1751	912	52	639	1917	860	45
DCL Finance	224	672	152	23	244	731	254	35	270	811	435	54	291	872	435	50	298	894	305	34
New Century Leasing	155	465	268	58	171	514	382	74	218	655	426	65	266	800	541	68	276	828	780	94
Kothari Orient Finance	78	233	118	51	100	299	138	46	113	338	146	43	119	358	181	51	162	485	275	57
Ashok Leyland Finance	291	874	497	57	365	1096	391	36	464	1394	766	55	1040	3121	1050	34	1647	4940	1097	22
TOTAL	2590	7767	2894	37	3014	9044	4983	55	3481	10446	5999	57.5	4406	13219	6140	47	5792	17376	6802	39
Grand Total	6879	20630	6172	30	7910	23732	9754	41	9870	29615	11983	40	12281	36845	16343	44	14801	44404	17479	39

Source : Computed from Company Annual Reports NW = Net Worth ELE = Eligibility (3 times Net worth)

Upto April 1989, finance companies were having an edge over the manufacturing companies in deposit mobilisation offering 14 percent of interest even on short term deposits of 6 months to 12 months.

Groupwise analysis in table no. 5.46 reveals that public deposits dominate the long term funds (around 50%) of old companies indicating the success of these companies in deposit mobilisation. But analysing individually, it is noticed that, only Sakthi Finance and Sundaram Finance collected large volumes of public deposits.

5.58 Among the new companies, only companies with group connection, such as Kothari Orient Finance and Nagarjuna Finance obtained public deposits early in 1986 whereas other companies could increase their public deposits only in later 1988-'89 periods.

Comparison of bank borrowings and public deposits indicates that there has been a shift among companies towards public deposits from bank loans over the years. Companies are opening more branches and offer several incentives to depositors to canvass more deposits.

To conclude, leasing companies are not having enough long term funds. Equity issues are not feasible and possible frequently. Borrowed funds have proved costly, especially in the light of reduced earnings.

Table No. 5.46

PUBLIC DEPOSITS AND LONG TERM FUNDS

PD = Public Deposits

LTF = Long Term Funds

(Rs. in Lakhs)

Old Companies

Name of Companies	1986 PD	1986 LTF	1986 %age	1987 PD	1987 LTF	1987 %age	1988 PD	1988 LTF	1988 %age	1989 PD	1989 LTF	1989 %age	1990-91 PD	1990-91 LTF	1990-91 %age
Sundaram Finance	10410	13820	75	10839	14913	73	12793	17357	74	14416	21195	68	16764	28504	59
Sakthi Finance	1021	1390	73	2424	3083	79	4221	5313	79	6809	8671	78	8320	10296	81
First Leasing Company	1244	3613	34	1682	5208	32	2144	6425	33	2304	8892	26	2692	10225	26
20th Century Leasing	289	6014	5	259	6941	4	491	8754	6	898	12199	7	2019	13700	15
TOTAL	12964	24837	52	15204	30145	50	19649	37849	52	24424	50957	48	29795	62725	48
New Companies															
United Leasing	09	370	2	18	560	3	75	637	12	99	834	12	135	970	14
World Link Finance	-	203	-	12	682	2	110	725	15	172	898	19	172	898	19
Grover leasing	102	575	18	250	811	31	397	1026	39	208	754	28	217	890	24
PL Finance	121	760	16	147	848	17	225	920	24	266	1057	25	340	1118	30
Integrated Finance	28	658	4	96	1208	8	195	1495	13	380	1685	23	474	1996	24
Nagarjuna Finance	778	2760	28	925	3790	24	1319	4498	29	1354	4949	27	1970	6336	31
Midwest Leasing	72	790	9	130	1094	12	306	2060	15	366	2355	16	555	2481	22
DCL Finance	29	448	6	71	658	11	213	1065	20	314	1311	24	382	1547	25
New Century Leasing	42	465	9	139	698	20	221	874	25	246	1263	19	338	1694	20
Kothari Orient Finance	114	349	33	177	447	40	259	549	47	291	621	47	335	885	38
Ashok Leyland Finance	37	826	4	224	1480	15	1100	3381	33	1986	5618	35	3045	10615	29
TOTAL	1332	8204	16	2189	12276	18	4420	17230	26	5682	21345	27	7963	29430	27
Grand Total	**14276**	**33041**	**43**	**17393**	**42421**	**41**	**24069**	**55079**	**44**	**30106**	**72302**	**42**	**37758**	**92155**	**41**

Source : Computed from Company Annual Reports

5.59 Bank funds are not available at rates lower than 22.5 percent from october Ist 1991 onwards. Public deposits are not easily accessible except for good groups. Even though interest rates are restricted to 15 percent, the advertisement and brokerage cost would increase the cost further. Similar is the case with debentures. Eventhough the rate of interest was only 15 percent, issue management cost pushed the cost further. (Now, the rate of interest on debentures are determined by market forces.)

Hence, due to the high cost of borrowings companies are using short term funds as well to finance their long term activities.

5.60 **Current liabilities and provisions:**

Current Liabilities and provisions together constitute the short term funds. The structure of short term funds over the years is examined in table no. 5.47.

Table No. 5.47

STRUCTURE OF SHORT TERM FUNDS FOR THE INDUSTRY
(Figures in bracket denote percentage to total short term Funds)
(Rs. in Lakhs)

	1986	1987	1988	1989	1990-91
Short term Funds	9,417	12,354	16,371	23,842	30,168
Provisions	596 (6%)	910 (7%)	1,515 (9%)	2,246 (9%)	2,809 (9%)
Current liabilities	8,821 (94)	11,444 (93)	14,856 (91)	21,596 (91)	27,359 (91)

Source : Computed from Company Annual Reports

The current liabilities dominate the short term funds, the percentage being 90 percent each year. A further analysis of the current liabilities is attempted in the following table.

Table No. 5.48

COMPONENTS OF CURRENT LIABILITIES (Rs. in Lakhs)

	1986	1987	1988	1989	1990-91
Current Liabilities	8821	11444	14856	21596	27359
Creditors	963 (11)	1152 (10)	1560 (11)	1763 (08)	4377 (16)
Dividend	28 (<1)	155 (1)	137 (1)	155 (1)	171 (1)
Other dues	7825 (89)	10138 (89)	13159 (89)	19678 (91)	22810 (83)

(Figures in brackets denote percentage to total Current Liabilities)

Source : Computed from Company Annual Reports

It is noticed that other dues form a major part of the current liabilities of the industry over the years. Similar pattern is revealed by individual companies as well. Hence it is desirable to find out what constitutes the other dues.

Other dues are seen to include various items such as acceptance, interest accrued, advance lease rentals and hire purchase instalments, unmatured hire purchase finance charges and other liabilities. But it is the unmatured hire purchase finance charges which form a major slice of the other dues as seen from Table No. 5.49.

The unmatured finance charges, included in other dues, formed 63 percent on an average for the industry. Taken individually, it is seen that more than 50 percent of other dues constitute unmatured finance charges for majority of the sample companies.

Unmatured hire purchase finance charges occur when the stock on hire purchase account is shown in at full instalment value receivable from the hirer and not just the principal amount. The interest not still due is credited to Interest Suspense Account (Otherwise known as unmatured hire purchase finance charges *). Hence, this method of short term financing is popular among leasing/hire purchase companies.

As funds are the key raw material for leasing companies, they would have to constantly tap alternative funding sources to reduce the cost of funds. At the same time the company should strive to increase the margin between the cost of funds and rate of return. An attempt is made in the following chapter to analyse the profitability of leasing companies.

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* Kothari Viond, Lease Financing and Hire Purchase, (1991), page. 872.

Table No. 5.49

UNMATURED FINANCE CHARGES INCLUDED IN OTHER DUES OVER THE YEARS

(Rs.in Lakhs)

Name of Companies	1986 Other dues	1986 U.F.C.	1986 %age	1987 Other dues	1987 U.F.C.	1987 %age	1988 Other dues	1988 U.F.C.	1988 %age	1989 Other dues	1989 U.F.C.	1989 %age	1990–91 Other dues	1990–91 U.F.C.	1990–91 %age
First Leasing Company	127	49	39	354	201	57	711	502	71	1296	1118	86	1938	1518	78
20th Century Finance	535	107	20	701	338	48	1208	884	73	2241	1363	61	2462	1611	65
United Leasing	89	40	45	149	91	61	392	77	20	463	88	19	587	96	16
World Link Finance	–	–	–	143	115	80	172	108	63	266	88	33	266	88	33
Grover Leasing	24	–	–	407	–	–	55	–	–	50	–	–	63	–	–
PL Finance	80	69	86	107	87	81	114	93	82	105	85	81	95	55	58
Integrated Finance	175	170	97	476	463	97	543	519	96	591	560	94	643	603	94
Nagarjuna Finance	1481	444	30	1722	610	35	1514	529	35	1725	416	24	1610	493	31
Midwest Leasing	138	85	62	251	163	65	389	269	69	399	238	60	308	81	26
DCL Finance	73	67	92	100	82	82	208	132	63	204	144	71	269	152	57
New Century Leasing	159	157	99	204	197	97	187	176	94	608	231	38	530	252	48
Kothari Orient Finance	111	100	90	95	79	83	126	105	83	125	111	88	181	163	90
Sakthi Finance	275	199	72	628	419	67	940	636	68	913	713	78	1030	744	72
Sundaram Finance	4348	3607	83	4488	3713	83	4694	3791	81	6229	4856	78	9158	6904	75
Ashok Leyland Finance	210	68	32	681	195	29	1905	367	19	4463	828	19	3934	1454	37
TOTAL	7825	5162	66	10138	6753	67	13159	8188	62	19678	10839	55	22810	15214	67

Sources : Computed from Company Annual Reports U.F.C. = Unmatured Finance Charges

CHAPTER - VI

PROFITABILITY OF LEASING COMPANIES

6.1 The survival of any business depends essentially on its profit earning capacity. In the words of Lord Keynes, "Profit is the engine that drives the business enterprise ." A business needs profit not only for its existence, but also for expansion and diversification. Profit is also an effective tool to measure the overall efficiency of a business. The earnings and the nature of costs determine the profits of a concern.

6.2 **Analysis of Profits:**

In absolute terms, the net profits of the leasing industry registers a constant increase from Rs.1,600 lakhs in 1986 to Rs.4269 lakhs in 1990-91. But taken individually, there are fluctations in the net profits of companies over the years. While certain companies report steady increase in net profits, certain other companies report wide fluctations during this short period. Table No. 6.1 gives the net profit earnings of the sample companies.

Table No. 6.1

NET PROFITS IN ABSOLUTE TERMS

(Rs. in Lakhs)

Name of Companies	1986	1987	1988	1989	1990-91
First Leasing	238	238	150	354	458
20th Century Finance	375	334	423	484	604
Grover Leasing	50	48	33	34	43
PL Finance	63	73	70	65	58
United Leasing	46	21	46	52	58
World Link Finance	08	15	11	10	10
Midwest Leasing	74	87	146	101	102
DCL Finance	45	57	69	61	45
New Century Leasing	29	45	75	88	58
Sakthi Finance	117	182	326	412	318
Nagarjuna Finance	143	159	152	205	226
Kothar Orient Finance	15	31	40	41	47
Integrated Finance	29	31	81	72	86
Sundaram Finance	288	488	556	899	1447
Ashok Leyland Finance	80	141	193	448	719
TOTAL	**1600**	**1950**	**2371**	**3326**	**4269**

Source : Computed from Company Annual Reports

6.3 Since a comparison of net profts in absolute terms is meaningless, net profit ratios are used to measure the operating efficiency of leasing companies. Table No. 6.2 shows that net profit ratio declined from 20 percent in 1986 to 17 percent in 1988. But during 1989 and 1990-91, the ratio reported an increase to 17.5 percent and 18 percent respectively.

Table No. 6.2

NET PROFIT RATIOS FOR THE INDUSTRY

(Rs. in Lakhs)

		1986	1987	1988	1989	1990-91
Total Income	1	8112	10771	14242	19016	24190
Net Profit	2	1600	1950	2371	3326	4269
Net Profit Ratio	$\frac{2}{1}$	20%	18%	17%	17.5%	18%

Source : computed from company annual reports

6.4 These ratios present only a gross picture of the industry. To have a clear picture of profitability, a company wise analysis is resorted to in table no. 6.3. It is observed that there are significant variations between the net profit ratios of various companies. While Sundaram Finance shows a steady increase in net profit ratios, PL. Finance, DCL Finance and New Century Leasing

Table No. 6.

Name of Comp
First Leasing
20th Century
Grover Leasing
PL Finance
United Leasin
World Link Fin
Midwest Leasi
DCL Finance
New Century L
Sakthi Financ
Ashok Leyland
Sundaram Fina
Integrated Fi
Kothar Orient
Nagarjuna Fin
TOTAL

Source ; Comp

Table No. 6.3

NET PROFIT AND INCOME COMPANWISE

(Rs. in Lakhs)

Name of Companies	1986 Income	1986 N/P	1986 N/P Ratio	1987 Income	1987 N/P	1987 N/P Ratio	1988 Income	1988 N/P	1988 N/P Ratio	1989 Income	1989 N/P	1989 N/P Ratio	1990-91 Income	1990-91 N/P	1990-91 N/P Ratio
First Leasing Company	920	238	26	1352	238	18	1801	150	08	2573	354	14	3302	458	14
20th Century Finance	1770	375	21	2147	334	16	2636	423	16	3322	484	15	4112	604	15
Grover Leasing	155	50	32	204	48	24	269	33	12	257	34	13	248	43	17
PL Finance	206	63	31	262	73	28	258	70	27	327	65	20	293	58	20
United Leasing	99	46	46	143	21	15	199	46	23	251	52	21	314	58	18
World Link Finance	20	08	40	77	15	19	221	11	05	291	10	03	291	10	03
Midwest Leasing	186	74	40	247	87	35	395	146	37	544	101	19	610	102	17
DCL Finance	106	45	42	164	57	35	222	69	31	298	61	20	345	45	13
New Century Leasing	60	29	48	150	45	30	242	75	31	388	88	23	488	58	12
Sakthi Finance	324	117	36	749	182	24	1271	326	26	1984	412	21	2406	318	13
Ashok Leyland Finance	169	80	47	422	141	33	772	193	25	1761	448	25	3022	719	24
Sundaram Finance	3239	288	09	3661	488	13	4357	556	13	5072	899	18	6455	1447	22
Integrated Finance	106	29	27	216	31	14	333	81	24	403	72	18	481	86	18
Kothar Orient finance	59	15	25	106	31	29	140	40	29	181	41	23	186	47	25
Nagarjuna Finance	693	143	21	871	159	18	1126	152	13	1364	205	15	1637	226	14
TOTAL	**8112**	**1600**	**20**	**10771**	**1950**	**18**	**14242**	**2371**	**17**	**19016**	**3326**	**17.5**	**24190**	**4269**	**18**

Source ; Computed from Company Annual Reports

N/P = Net Profit

register a steady decline over the years. A steady trend is projected by a few companies. Many companies reported lower net profit ratios especially during 1987 and 1988. The irregular fluctuations in net profits of several companies make it difficult to arrive at a conclusion about their profitability.

6.5 In these circumstances, return on capital employed is made use of as a better tool of analysis, in order to measure the overall return. Table no. 6.4 gives the return on investment for the industry.

Table no. **6.4**

RETURN ON INVESTMENT FOR THE INDUSTRY

(Rs. in Lakhs)

		1986	1987	1988	1989	1990-91
Capital employed (NW + all borrowings)	1	33041	42421	55079	72302	92154
Profit before interest & tax	2	4931	6523	8315	11195	15054
Return on Investment for the industry	2	15	15	15	15	16

Source : Computed from company annual reports

NW = Net Worth

The Return on Investment for the industry shows that returns are steady at 15 percent over the years and reported an increase to 16 percent during 1990-91.

6.6 The variation in profits of individual companies may be due to the differences in activities of these companies. Hence a further analysis is required classifying the companies on the basis of their activity. Accordingly the companies are classified into three. Companies predominantly doing leasing, (more than 70% in leasing activity), companies predominantly doing hirepurchase (more than 70% in hire purchase activity) and companies doing leasing and hire purchase.

6.7 Groupwise analysis in table no. 6.5 shows that returns are high and registers an increasing trend by the predominantly hire purchase companies. The return increased from 14.7 percent to 17.2 percent. On the contrary, predominantly leasing companies report lower returns and a decreasing trend. (from 15.5 percent the return declined to 13.5 in 1989 though it slightly increased to 15.7 percent.) Returns for the combined group is in between the two.

All companies in the predominantly leasing group revealed a declining tendency in returns during 1987 and 1988. Companies in the other two groups have not shown such a tendency. These companies report mostly, either a steady

Table No. 6.5

RETURN ON INVESTMENT COMPANYWISE

(Earnings before interest and tax and capital employed) (Rs. in Lakhs)

	1986			1987			1988			1989			1990-91		
Name of Companies	C.E.	EBIT	ROI	C.E.	EBIT	ROI	C.E.	EBIT	ROI	C.E.	EBIT	ROI	C.E.	EBIT	ROI
Predominantly Leasing Companies															
First Leasing Company	3613	578	16	5208	802	15	6425	822	13	8892	1322	15	10225	1682	16
20th Century Finance	6014	890	15	6941	970	14	8754	1233	14	12199	1452	12	13700	2161	16
Grover Leasing	575	88	15	811	107	13	1026	131	13	754	126	17	890	115	13
PL Finance	760	142	19	848	157	19	920	163	18	1057	175	17	1118	165	15
TOTAL	10962	1698	16	13808	2036	15	17125	2349	14	22902	3075	14	25932	4127	16
Mixture of Leasing and Hire Purchase Companies															
United Leasing	370	66	18	560	63	11	637	104	16	834	131	16	970	165	17
World Link finance	203	08	04	682	37	05	725	88	12	898	75	08	898	75	08
Midwest Leasing	790	119	15	1094	162	15	2060	295	14	2355	395	17	2481	392	16
DCL Finance	448	69	15	658	106	16	1065	148	14	1311	188	14	1547	213	14
New Century Leasing	465	44	10	698	109	16	874	172	20	1263	251	20	1694	303	18
Sakthi finance	1390	223	16	3083	465	15	5313	806	15	8671	1197	14	10296	1463	14
TOTAL	3666	529	14	6775	942	14	10674	1613	15	15332	2237	15	17886	2611	15
Predominantly Hire Purchase Companies															
Ashok Leyland Finance	826	129	16	1480	310	21	3381	576	17	5618	1372	24	10615	2418	23
Sundaram Finance	13820	1967	14	14913	2386	16	17357	2659	15	21195	3212	15	28504	4409	16
Integrated Finance	658	76	12	1208	147	12	1495	241	16	1685	282	17	1996	317	16
Kothari Orient Finance	349	46	13	447	81	18	549	102	19	621	112	18	885	135	15
Nagarjuna Finance	2760	486	18	3790	621	16	4498	775	17	4949	905	18	6336	1040	16
TOTAL	18413	2704	15	21838	3545	16	27280	4353	16	34068	5883	17	48336	8319	17
Grand Total	**33041**	**4931**	**15**	**42421**	**6523**	**15**	**55079**	**8315**	**15**	**72302**	**1195**	**15**	**92154**	**15057**	**16**

Source · Computed from Company annual reports

C.E. = Capital Employed; EBIT = Earnings before interest and Tax; ROI = Return on investments return or increased returns. Hence it follows that the returns of predominantly leasing companies have suffered a set back lowering the Net Profit ratios of the industry during 1987 and 1988.

6.8 **Evaluation of Income;**

In order to explain the variation in the return of individual companies, the income side is evaluated so as to have a clear picture. Table no.6.6 shows that income from leasing, and hire purchase as a percentage of activity decreased from 18.9 percent in 1986 to 17.07 percent in 1990-91 for the industry.

Table No. 6.6

INCOME AS A PERCENTAGE OF ACTIVITY

(Rs. in Lakhs)

		1986	1987	1988	1989	1990-91
Income (L + HP)	1	7532	10058	13172	17107	21381
Activity (L + HP)	2	39766	54186	71656	97012	125279
% of Income to activity	½	18.9	18.56	18.38	17.73	17.07

Source ; Computed from Company Annual Reports

L = Lease
HP = Hire Purchase

The trend ratios of activity and income shows that deceleration in income gathers momentum rapidly within a short span of five years.

Table No. 6.7

TREND OF ACTIVITY AND INCOME (Percentage)

	1986	1987	1988	1989	1990-91
Activity	100	136	180	244	315
Income	100	134	175	227	284
Difference	-	-2	-5	-17	-31

Source : Computed from Company Annual Reports

6.9 A further analysis becomes essential to find out the reasons for lower income, in the light of the declining percentage of income to activity as well as the lower trend ratios of income. The income of these companies include lease income, hire purchase income and other income. The structure of total income over these years is shown in table no. 6.8

Table No. 6.8

STRUCTURE OF INCOME (Percentage)

	1986	1987	1988	1989	1990-91
Lease Income	54.3	54.6	52.9	47.2	43.7
Hire Purchase Income	40.8	40.2	40.9	45.2	46.3
Other Income	4.9	5.2	6.2	7.6	10

Source : Computed from Company Annual Reports

It is seen that the percentage of lease income to the total income declined steeply from 54.3 percent to 43.7 percent during the period, while the other components steadily increased. The following table makes clear the decline in lease returns for the industry.

Table No. 6.9.

LEASE INCOME AS A PERCENTAGE OF LEASED ASSETS

	1987	1988	1989	1990-91
Average leased assets (Rs. in Lakhs)(1)	20985	27516	34714	42130
Average Lease income (Rs. in Lakhs)(2)	5792	7426	8740	10531
Return $\frac{2}{1}$	27.7	26.99	25.18	25

Source : Computed from Company Annual Reports

6.10 While there is a general decline in lease returns over the years for the industry, there are significant variations among the lease returns of different companies. Classifying companies into two groups, old and new, based on the number of their annual reports, (Old companies with more than six annual reports as on 1986, New companies with six or less than six annual reports as on 1986), it is seen that the returns vary noticeably as given in Table No. 6.10.

Table No. 6.10

COMPARISON OF THE LEASE RETURNS OF OLD AND NEW COMPANIES

(Percentage)

	1987	1988	1989	1990-91
Old Companies	26	25	24	23
New Companies	36	34	29	30

Source : Computed from Company annual reports

6.11 The high returns for many new companies is due to the differences in income accounting practices. There are different methods such as sum of digits method and accrual basis for accounting income. These methods of recognition of income are arbitrarily determined and not through generally accepted accounting principles. Obviously, no standard practice is adopted by all companies as reflected in the wide variation in lease returns. Hence it would be difficult to arrive at a meaningful comparison of companies. However, the decrease in the lease returns of these companies (from 36% to 30%) substantiates the decline in lease income.

6.12 **Decline in lease returns:**

The reasons for the decline in lease returns are not far to seek. By 1987, a large number of banks formed subsidiary leasing units. Financial institutions widened their leasing activities. Major industrial groups formed in-house leasing companies. The resultant competition depressed the lease rentals from Rs.33 PMPT during 1982-83 to less than Rs.25 PMPT during 1987 and further down to Rs.23.75 PMPT during 1988-89. Consequent on the steep decline in rentals, the exciting profits generated by leasing companies met with a set back. The decline is noticeable particularly after 1987, when the impact of leasing operations of the new entrants came into force. Company wise analysis in table no. 6.11 shows that there are variations in the decline in lease returns among the companies in the old group itself. Sundaram Finance is the only company in the group which is consistently increasing lease returns over the years. Lease returns of First Leasing and 20th Century Finance are more or less similar. Sundaram Finance reports a lower lease return of 18 percent, while First Leasing and 20th Century report more than 25 percent returns in 1987. Sundaram finance is a predominantly hire purchase company with hire purchase income and for it, leasing is only an additional activity. The outcome of such a situation is that the company can offer lower rental rates to "buy" depreciation and save taxes. Obviously, predominantly leasing companies like First Leasing and 20th Century Finance are not in a position to offer such lower rates as their main income is lease income and depreciation can be set off only against their lease income. Sakthi Finance, another company in the group, with substantial volume of both leasing and hirepurchase shows abnormal lease returns.

Table No. 6.11

LEASE RETURNS OF INDIVIDUAL COMPANIES
(On the basis of average Leased assets)

(Rs. in lakhs)

Name of Companies	1987 Leased Assets	1987 Lease income	1987 Rate	1988 Leased Assets	1988 Lease Income	1988 Rate	1989 Leased Assets	1989 Lease Income	1989 Rate	1990-91 Leased Assets	1990-91 Lease Income	1990-91 Rate
Old Companies												
First Leasing	4896	1178	24	6377	1426	22	7262	1483	20	8194	1818	22
20th Century Finance	7497	2032	27	9254	2330	25	11233	2683	24	13485	2922	22
Sakthi Finance	808	474	59	1567	798	51	2776	1100	40	3689	1214	33
Sundaram Finance	3788	689	18	4781	975	20	5812	1227	21	7044	1666	24
TOTAL	16989	4373	26	21979	5529	25	27083	6493	24	32412	7620	24
New Companies												
Grover Leasing	452	153	34	545	196	36	563	179	32	605	186	31
PL Finance	653	222	34	754	206	27	814	207	25	919	194	21
United Leasing	368	106	29	453	147	32	574	186	32	784	243	31
World Link Finance	59	17	29	185	109	59	495	155	31	727	155	31
Midwest Leasing	373	123	33	485	145	30	712	213	30	924	225	24
DCL finance	255	84	33	355	105	30	472	130	28	586	121	21
New Century Leasing	168	78	46	427	141	33	753	209	28	953	291	31
Ashok Leyland Finance	349	122	35	649	205	32	1150	331	29	1943	556	29
Integrated Finance	273	98	36	360	119	33	456	115	25	609	157	26
Kothari Orient Finance	112	37	33	149	45	30	163	44	27	225	65	29
Nagarjuna Finance	848	378	45	1178	478	41	1483	473	32	1808	717	40
TOTAL	3906	1419	36	5537	1897	34	7631	2247	29	9718	2911	30
Grand Total	**20895**	**5792**	**28**	**27516**	**7426**	**27**	**34714**	**8740**	**25**	**42130**	**10531**	**25**

Source : Computed from Company Annual Reports

are lower. After 1987, profits started declining fast for leasing, primarily due to acute competition and consequent reduction in lease rentals. Indian economy witnessed a boom in hire purchase business because of the middle class mania for acquiring white consumer durables, automobile manufacturers resorting to hirepurchase tie up for overcoming recession in the automobile industry and soon as a result, there was a spurt in the hire purchase activities of many leasing companies. Table No. 6.13 tells us that while hire purchase business recorded a compound growth rate of 28 percent over the years, leasing business reported only a lower growth rate of 21 percent.

Table No. 6.13

COMPOUND GROWTH RATE OF HIRE PURCHASE AND LEASING

(Rs. in Lakhs)

	1986	1987	C.G.R. (%)
Hire Purchase Activity	20509	71489	28%
Lease Activity	17842	46641	21%

Source : Computed from Company annual reports

C.G.R. = Compound Growth Rate

6.15 It is clear that as against the steep decline in lease returns, hire purchase returns are steady for the industry over the years, from tale no. 6.14

Table No. 6.14

HIRE PURCHASE RETURNS

(Rs. in Lakhs)

	1987	1988	1989	1990-91
Average Hire Purchase assets(1)	24487	33063	45299	62214
Average Hire Purchase Income(2)	4266	5746	8367	11005
Average Hire Purchase return $\frac{2}{1}$	17.4%	17.4%	18.47%	17.69%

Source : Computed from company annual reports

Groupwise analysis in table no. 6.15 shows that older companies (Sundaram Finance and Sakthi Finance) doing hire purchase business report a steady return of around 18 percent while new entrants to this field registered an increase in returns from 16.6 percent to 18 percent over the years.

Company wise analysis in the same table clearly points out that First Leasing and 20th Century Finance have rapidly increased their hire purchase business over the years compared to other predominantly leasing companies. Ashok Leyland Finance also reports a substantial increase in hire purchase activity since 1986, the company's first year of operation.

6.16 **Diversification:**

Besides, shifting to Hire purchase activities, leasing com[illegible] ef[illegible]cted diversification into non fund

Table No. 6.15

HIRE - PURCHASE BUSINESS AND HIRE - PURCHASE INCOME COMPANYWISE

(On the basis Average Hire Purchase Business) **(Rs. in Lakhs)**

Name of Companies	1987 H.P.B.	1987 H.P. Income	1987 Return	1988 H.P.B.	1988 H.P. Income	1988 Return	1989 H.P.B.	1989 H.P. Income	1989 Return	1990-91 H.P.B.	1990-91 H.P. Income	1990-91 Return
Old Companies												
Sakthi Finance	1363	229	17	2500	366	15	3677	741	20	4550	978	21
Sundaram Finance	13971	2516	18	14868	2845	19	17672	3110	18	23925	3931	16
TOTAL	15334	2745	18	17368	3211	19	21349	3851	18	28475	4909	17
New Companies												
First Leasing	385	133	35	1103	315	29	2955	867	29	5354	1289	24
20th Century Finance	827	69	8	2060	185	9	3766	448	12	5111	643	13
Grover Leasing	210	40	19	238	49	21	204	58	28	201	49	24
PL Finance	212	30	14	282	44	16	348	92	26	326	86	26
United Leasing	229	29	13	313	44	14	328	54	17	394	56	14
World Link Finance	204	34	17	430	79	18	434	75	17	414	75	18
Midwest Leasing	730	112	15	1290	241	19	1746	317	18	1731	371	21
DCL Finance	365	66	18	609	91	15	855	131	15	1052	195	19
New Century Leasing	553	70	13	653	93	14	818	137	17	1100	168	15
Ashok Leyland Finance	1542	296	19	3286	506	15	6344	1160	18	10909	1969	18
Integrated Finance	963	105	11	1543	180	12	1779	244	14	1941	290	15
Kothari Orient Finance	356	63	18	424	85	20	512	84	16	630	98	16
Nagarjuna Finance	2583	474	18	3469	622	18	3866	849	22	4587	797	17
TOTAL	9153	1521	17	15695	2535	16	23950	4516	19	33739	6096	18
Grand Total	**24487**	**4266**	**17**	**33063**	**5746**	**17**	**45299**	**8367**	**18**	**62214**	**11005**	**18**

Source : Computed from Company Annual Reports

Old Companies - Established hire purchase companies doing leasing

New Companies - Leasing Companies doing hire purchase activities like merchantbanking, consultancy services, Port-folio management etc. The income from these non-fund activities are included under the head 'other income', besides profit on sale of assets, interest, dividends and bill discounting charges. The proportion of this income to the total income of leasing companies is very meagre, only 5 percent in 1986 though it increased to 10 percent in 1990-91. It is revealed that only old and established companies have significant other income, vide table no. 6.16.

Among the various components of other income, interest income accounts for 37 percent on an average (earned by all companies on their bank deposits), whereas dividend formed only 05 percent, Profit on sale of assets formed 29 percent as reported only by old and established companies. Bill discounting, charges consultancy fees, factor charges and other miscellaneous income formed 29 percent. Table no. 6.17 shows the names of companies with large other income.

Table No. 6.16

OTHER INCOME

(Figures in brackets indicate percentage to total income)

(Rs. in Lakhs)

Name of Companies	1986	1987	1988	1989	1990-91
First Leasing	32 (5%)	42 (6%)	59 (6%)	223 (12%)	195 (7%)
20th Century Finance	42 (7%)	46 (6%)	120 (11%)	191 (10%)	547 (21%)
United Leasing	6	8	7	10	15
World Link Finance	19	26	34	46	46
Grover Leasing	6	11	25	21	13
PL Finance	15	10	9	28	14
Integrated Finance	4	13	33	43	34
Nagarjuna Finance	29 (5%)	26	26	42	124 (5%)
Midwest Leasing	7	12	9	13	14
DCL Finance	7	14	26	36	29
New Century Leasing	4	2	8	42	29
Kothari Orient Finance	2	7	11	23	23
Sakthi Finance	27 (5%)	46 (6%)	107 (10%)	143 (8%)	214 (8%)
Sundaram Finance	379 (66%)	456 (63%)	537 (50%)	735 (39%)	857 (32%)
Ashok Leyland Finance	<1	3	61 (6%)	270 (14%)	497 (19%)
TOTAL	578	720	1071	1866	2648

Source ; Computed from Company Annual Reports

Table No. 6.17

NAME OF COMPANIES WITH SIGNIFICANT OTHER INCOME

Other Income Components	Name of companies	Percentage to total other income
Interest	Earned by All Companies (Majority Sundaram Finance)	37
Dividend	Earned by Several Companies (Leading companies are 1) First Leaisng Company 2) 20th Century Finance 3) Nagarjuna Finance 4) Sundaram Finance	05
Profit on sale of asset and investments	Earned by 20th Century Finance and Sundaram Finance	29
Factor Charges, Commission, Consultancy, bill dicounting	1) First Leasing Company 2) 20th Century Finance 3) Midwest Leasing 4) Kothari Orient Finance 5) Sakthi Finance 6) Sundaram Finance 7) Ashok Leyland Finance	29
Miscellaneous	All Companies	
TOTAL		100

Source : Computed from Company Annual Reports

6.17 In recent years many leasing companies are increasing their volume of non-fund activities. Companies like First Leasing, 20th century Finance, Kothari Orient Finance, World Link Finance etc. generate income by engaging in non-fund activities. Companies like Ashok leyland Finance, Sundaram Finance and World Link Finance resort to bill discounting for augmenting their other income.

Analysis of the income side thus leads to the conclusion that lease returns have declined over the years due to intensified competition and uneconomic rental rates. Hence leasing companies diversified into hire purchase business as well as non-fund activities to increase their earnings. But profit is a function of income earned as well as expenses incurred. The expense pattern of leasing companies is also to be examined to supplement the aforesaid conclusion.

6.18 **Analysis of Expenses:**

It is observed that total expenses as a percentage of activity decreased from 16 percent in 1986 to 15.33 percent in 1990-91. At the same time expense ratios when related to income increased from 79.76 percent in 1986 to 80.89 percent in 1990-91. Table no. 6.18 gives a picture of these ratios.

Table No. 6.18

EXPENSE RATIO FOR THE INDUSTRY

(Rs. in Lakhs)

		1986	1987	1988	1989	1990-91
Total Expense	1	6316	8667	11678	15186	19210
Total Activity	2	39766	54186	71656	97012	125276
Income	3	7919	10617	140479	18512	23749
Expenses as % of activity	½	16%	16%	16%	15.6%	15.3%
Expense as % of Income	$\frac{1}{3}$	79.76	81.63	83.12	82.03	80.89

Source : Computed from Company Annual reports

Common size profit and loss account vide table no. 6.19 prepared for the leasing companies reveals that while total expenses remain more or less steady around 80 percent there are variations in the total expenses incurred among the different groups.

6.19 Predominantly leasing group report higher total expenses than the other two groups. The expenses of this group reported an increase from 76 percent to 85 percent over the years. The predominantly hire purchase group, on the contrary, reveals a declining tendency in total expenses percentage. It came down from 85 percent to 79 percent over the period. The mixture of leasing and hire purchase group steadily increased the percentage of expense from 59 to 84 during the same period.

Table No. 6.19

COMMON SIZE PROFIT AND LOSS ACCOUNT OF SAMPLE LEASING COMPANIES OVER THE YEARS - 1986 to 1991

Name of Companies	Operating Expense					Finance Expense					Cash Expense					Cash Profit				
	86	87	88	89	90-91	86	87	88	89	90-91	86	87	88	89	90-91	86	87	88	89	90-91
Predominantly Leasing Companies																				
First Leasing	8	7	6	6	5	37	42	37	38	37	45	49	43	44	42	55	51	57	56	58
20th Century	4	5	6	6	8	29	30	31	35	38	33	35	37	41	46	67	65	63	59	54
Grover Leasing	28	33	25	23	16	24	29	36	36	29	52	62	61	59	45	48	38	39	41	55
PL Finance	10	10	16	14	14	39	32	36	34	37	48	42	52	47	51	52	58	48	53	49
TOTAL	7	7	8	8	7	32	34	34	36	37	39	41	42	43	44	61	59	59	57	56
Mixture of Leasing and Hire Purchase Companies																				
United Leasing	14	11	12	17	10	20	29	29	32	34	34	40	41	49	44	66	60	59	51	56
DCL Finance	15	13	16	18	13	22	30	36	43	49	37	43	52	60	52	63	57	48	40	48
Midwest Leasing	22	21	15	16	13	24	30	38	54	48	46	51	53	70	61	54	49	47	30	39
New Century	17	15	13	12	13	26	43	40	42	50	43	58	53	54	63	57	42	47	46	37
Sakthi Finance	18	21	20	24	21	33	38	38	40	48	51	49	58	64	69	49	41	42	36	31
World Link Finance	16	39	17	23	23	-	28	35	22	22	16	67	52	45	45	84	33	48	55	55
TOTAL	18	19	17	20	18	26	35	37	40	45	44	54	54	60	63	56	46	46	40	37
Predominantly Hire Purchase Companies																				
Sundaram Finance	12	11	11	10	9	29	40	50	52	56	41	51	61	62	65	59	49	39	38	35
Ashok Leyland Finance	11	10	11	10	11	55	54	51	49	48	66	64	62	59	59	34	36	38	41	41
Kothari Orient Finance	14	12	15	14	15	53	47	44	47	47	67	59	59	61	62	33	41	41	39	38
Integrated Finance	19	22	17	18	19	44	54	48	52	48	63	75	65	70	67	37	25	35	30	33
Nagarjuna Finance	15	14	13	14	19	50	53	55	51	50	65	67	68	65	68	35	33	32	35	32
TOTAL	12	11	11	11	12	53	51	49	48	51	65	62	60	59	63	35	38	40	41	37
Grand Total	11	11	11	12	11	42	43	42	43	45	53	54	53	55	56	47	46	47	45	44

Name of Companies	Non-Cash Expense					Net Profit					Total Expense				
	86	87	88	89	90-91	86	87	88	89	90-91	86	87	88	89	90-91
Predominantly Leasing Companies															
First Leasing	29	33	48	43	44	26	18	9	13	14	74	82	91	87	86
20th Century	46	50	47	44	40	21	15	16	15	14	79	85	84	85	86
Grover Leasing	16	14	26	29	38	32	24	13	12	17	68	76	87	88	83
PL Finance	21	30	26	33	30	31	28	22	20	19	69	72	78	80	81
TOTAL	37	41	46	42	41	24	18	12	15	15	76	82	88	85	85
Mixture of Leasing and Hire Purchase Companies															
United Leasing	19	45	36	31	37	47	15	23	20	19	53	85	77	80	81
DCL Finance	19	22	18	19	25	44	35	30	21	23	56	65	70	79	77
Midwest Leasing	14	14	10	12	23	40	35	37	18	16	60	65	63	82	84
New Century	8	13	16	23	25	49	29	31	23	12	51	71	69	77	88
Sakthi Finance	13	17	16	16	18	36	24	26	20	13	64	76	74	80	87
World Link Finance	41	13	43	20	20	42	20	5	35	35	57	80	95	65	65
TOTAL	15	19	20	17	21	41	27	26	23	16	59	73	74	77	84
Predominantly Hire Purchase Companies															
Sundaram Finance	11	16	14	12	11	48	33	25	26	24	52	67	75	74	76
Ashok Leyland Finance	24	22	24	22	17	10	14	14	19	24	90	86	86	81	76
Kothari Orient Finance	8	12	13	12	12	25	29	28	27	26	75	71	72	73	74
Integrated Finance	9	11	10	12	15	28	14	25	18	18	72	86	75	82	83
Nagarjuna Finance	14	15	18	15	18	21	18	14	20	14	79	82	86	80	86
TOTAL	20	19	20	17	16	15	19	20	24	21	85	81	80	76	79
Grand Total	27	27	30	25	24	20	19	17	19	20	80	81	83	81	80

Source : Computed from Company Annual Reports

6.20 Company wise analysis shows that all companies in the first group have increased their expense percentages. In the predominantly hire purchase group Sundaram Finance has made a noticeable reduction in the expense percentage from 90 to 76 and this reduction accounts for the declining tendency of expense percentage of the group. Companies in the mixture of leasing and hire purchase group also are seen to increase the expense percentage over the years.

Thus it is observed that, though there are slight variations, among companies in the total expenses incurred, all companies except Sundaram Finance report higher expense ratios. To arrive at the reasons for this increase, a scrutiny of the total expenses is required. Total expenses can be grouped under two major heads-cash expenses and non cash expenses.

6.21 **Cash Expenses:**

Common size profit and loss account shows that cash expenses for the industry increased from 53 percent to 56 percent over the years while non cash expenses declined from 27 percent to 24 percent.

Groupwise analysis shows that cash expenses are the lowest for the predominantly leasing group and the highest for the predominantly hire purchase group. No doubt it is the non cash expenses which boosted the expense percentage of the predominantly leasing group. The following table gives a snapshot of the position.

Table No. 6.20

CASH EXPENSES AND NON CASH EXPENSES OF THE DIFFERENT GROUPS

	1986	1987	1988	1989	1990-91
Predominantly Leasing Companies					
Cash Expenses	39%	41%	42%	43%	44%
Non Cash Expenses	37%	41%	46%	42%	41%
Predominantly Hire Purchase Companies					
Cash Expenses	65%	62%	60%	59%	63%
Non Cash Expenses	20%	19%	20%	17%	16%
Mixture of Leasing and Hire Purchase Companies					
Cash Expenses	56%	46%	46%	40%	37%
Non Cash Expenses	15%	19%	20%	17%	21%

Source : Computed from Company Annual Reports

6.22 It is noticed that non cash expenses of the predominantly hire purchase group and mixture group is marginal when compared to the non cash expenses of the leasing group which is almost equal to the cash expenses of the group.

Predominantly leasing companies with large volumes of leased assets report large depreciation (non-cash) as well. For hire purchase assets, the lessor cannot claim depreciation. Therefore the depreciation for the predominantly hire purchase group and mixture group is negligible as it is determined by their volume of leasing activity which is lower than the leasing group.

6.23 The disparity in non cash expenses among groups being understood, it is desirable to probe into the reasons for the variations in cash expenses among them.

Cash expenses can be categorised into finance expenses and operating expenses. Common size profit and loss account shows that finance expense dominates the cash expenses of the industry.

Table No. 6.21

STRUCTURE OF CASH EXPENSES
(Percentage)

	1986	1987	1988	1989	1990-91
Cash Expenses	53	54	53	55	56
Finance Expneses	42	43	42	43	45
Operating Expenses	11	11	11	12	11

Source : Computed from Company Annual Reports

But there are significant variations in the percentages among various groups of leasing companies.

6.24 **Finance Expenses:**

Groupwise analysis reveals that finance expenses are the lowest for the predominantly leasing group and the highest for the predominantly hire purchase group.

Table No. 6.2

COMPARISON OF FINANCE EXPENSE OF THE GROUPS

	1986	1987	1988	1989	1990-91
Predominantly Leasing	32	34	34	36	17
Predominantly Hire Purchase	53	51	49	48	51
Mixture of leasing & Hire Purchase	26	35	37	40	45

Source ; Computed from Company annual reports

Finance expenses of the mixture group makes a significant increase over this short duration.

Companywise analysis of the first group shows that significant variations between one company and another do not exist. In the predominantly hire purchase group, its position is reflected in the percentages of individual companies except Sundaram Finance which shows a substantial reduction in finance expenses over these years. But the effect of this reduction is off set by the sudden increase in the finance expenses of Ashok Leyland Finance - a new company.

All companies in the mixture group have reported significant increase in finance expenses over these years. An attempt is made in table no. 6.23 to find out the extent of activity that is being financed by borrowed funds.

6.25 **Finance expenses and borrowings:**

Finance expenses are high for the predominantly hire purchase group as they finance on an average 64 percent of their activity using borrowed funds. Companywise analysis shows that in the case of Sundaram Finance there has been a reduction in the activity percentage in business financed by borrowed funds (72% to 66%) and hence the company reports a reduction in financial expenses. On the contrary, Ashok Leyland Finance enhanced the portion of activity financed by borrwed funds (43% to 53%) and shows increased finance expenses.

6.26 Finance expense of the predominantly leasing group are lower because they finance on an average only 54 percentage of their activity with borrowed funds. There are no significant variations in the pattern of fund used by the individual companies in this group and all companies enjoy comparatively lower finance expenses.

In the mixture group, the finance expenses are higher than in predominantly leasing group. The group finance on an average 62 percent of activity using

Table No. 6.23

ACTIVITY AND BORROWED FUNDS

(Rs. in Lakhs)

Name of Companies	1986 Activity	1986 B.F	1986 %age	1987 Activity	1987 B.F	1987 %age	1988 Activity	1988 B.F.	1988 %age	1989 Activity	1989 B.F.	1989 %age	1990-91 Activity	1990-91 B.F.	1990-91 %age	
Predominantly Leasing Companies																
First Leasing Company	4391	2511	57	6525	4005	61	9004	4945	55	12457	7178	58	16184	8543	53	
20th Century Finance	7194	4293	60	9859	5081	52	13238	6738	51	19117	9674	51	21536	10943	51	
Grover Leasing	599	314	52	841	547	65	980	733	75	782	433	55	972	557	57	
PL finance	837	507	61	1013	570	56	1142	621	54	1280	770	60	1318	781	59	Avg.
TOTAL	13020	7625	59	18238	10203	56	24364	13037	54	33636	18055	54	40010	20824	52	54%
Mixture of Leasing and Hire Purchase Companies																
United Leasing	463	207	45	775	390	50	808	449	56	1056	623	59	1379	721	52	
World Link Finance	49	03	06	578	415	72	812	471	58	1188	593	50	1188	593	50	
Midwest Leasing	912	366	40	1347	654	49	2444	1514	62	2720	1771	65	2679	1842	69	
DCL Finance	515	224	44	744	414	56	1230	795	65	1519	1020	67	1881	1249	66	
New Century Leasing	593	310	52	859	528	62	1312	656	50	1831	996	54	2277	1418	62	
Sakthi Finance	1366	1182	87	3072	2649	86	5297	4526	85	8097	7615	94	9538	9049	95	Avg.
TOTAL	3888	2292	59	7375	5050	69	11903	8411	71	16411	12618	77	18942	14872	79	62
Predominantly Hire Purchase Comapnies																
Ashok Leyland Finance	1234	534	43	2546	1115	44	5787	2916	50	10303	4578	44	16980	8968	53	
Sundaram Finance	17482	12559	72	19328	13513	70	21524	15249	71	27715	18612	67	38153	25181	66	
Integrated Finance	773	551	71	1703	1001	59	2109	1275	61	2380	1434	60	2777	1703	61	
Kothari Orient Finance	433	271	63	509	348	68	663	436	66	717	501	70	1010	723	71	
Nagarjuna finance	2936	2325	79	4487	3279	74	5306	3879	73	5850	4218	72	7407	5081	69	
TOTAL	22858	16240	71	28573	19256	67	35389	23755	67	46965	29343	63	66327	41656	63	Avg 64%
Grand Total	**39766**	**26157**	**66**	**54186**	**34509**	**64**	**71656**	**45203**	**63**	**97012**	**60016**	**62**	**125279**	**77352**	**62**	

Source : Computed from Company Annual Reports

B.F. = Borrowed Funds

borrowed funds. (Sakthi Finance reporting exceptional borrowed funds has been excluded) Individually, the companies are seen to enhance the use of borrowed funds to finance their activity over the years and hence finance expense has been increasing.

6.27 The pattern of financing revealed that young and new companies depending more on bank loans incur more financial expense than older companies depending on public deposits or financial institution loans.

It can be concluded that the variation in finance expense is due to the difference in the volume and pattern of financing among leasing companies. Besides, the availability of funds and their cost also influence the finance expense. This aspect has already been explained while analysing fund management.

6.28 **Operating expenses:**

Since operating expenses form a part of cash expenses besides finance expenses, an analysis of the operating expenses is also attempted.

Common size profit and loss account reveals a steady trend in operating expense percentage of around 11 percent for the industry. But it is observed that companies like First Leasing and 20th Century Finance in the predominantly leasing group report lower operating expenses than Sundaram Finance and Ashok Leyland Finance

Table No. 6.24

OPERATING RATIOS
FOR DIFFERENT COMPANIES

(Rs. in Lakhs)

	Activity		Operating Expenses		Ratio	
Name of Companies	1986	1990-91	1986	1990-91	1986	1990-91
First Leasing	4391	16184	76	168	2%	1%
20th Century Finance	7193	21536	72	317	1%	1.5%
Sundaram Finance	17482	38153	344	659	2%	1.7%
Ashok Leyland Finance	1234	16980	21	270	2%	1.6%
United Leasing	463	1379	14	32	3%	2.3%
Grover Leasing	599	1972	43	39	7%	4%
PL Finance	837	1318	20	42	2.4%	3.2%
Integrated Finance	773	2777	20	93	2.6%	3.3%
Nagarjuna Finance	2936	7407	100	304	3.4%	4.1%
Midwest Leasing	912	2679	41	79	4.5%	3%
DCL finance	515	1881	16	46	3%	2.4%
New Century Leasing	93	2277	10	66	1.7%	3%
Kothari Orient Finance	433	1010	8	28	1.8%	2.8%
Sakthi Finance	1366	9538	58	504	4.2%	5.3%

Source : Computed from Company annual reports

in the predominantly hire purchase group.(Predominantly Leasing 7 percent, Predominantly Hire purchase 11 percent). All other companies among the various groups incur a very high operating expense percentage. It is also noticed that large sized concerns (on the basis of activity) like First Leasing, 20th century Finance, Sundaram Finance and Ashok Leyland Finance report comparatively lower operating expenses when related to activity. Unlike large sized companies, companies with a lower activity level report a higher operating ratio. This picture is presented in Table No. 6.24

6.29 Operating expenses can further be classified into personnel expenses, administration expenses and other expenses. It is seen that while personnel and administration expenses reported a steady or even declining trend, the 'other expenses' are seen to increase over the years for the industry.

Table No. 6.25

STRUCTURE OF OPERATING EXPENSES

	1986	1987	1988	1989	1990-91
Activity (Rs.in Lakhs)	39766	54186	71656	97012	125279
Personnel Expenses 2	214	280	376	531	653
P. Exp. Ratio 2/1	0.53	0.52	0.52	0.55	0.52
Adm. Expenses 3	326	407	555	732	902
A. Exp. Ratio 3/1	0.82	0.75	0.77	0.75	0.72
Other Expneses 4	307	489	641	914	1146
Other Expenses Ratio 4/1	0.77	0.90	0.89	0.94	0.91

Source : Computed from Company Annual Reports

Groupwise analysis in table no. 6.26 reveals that personnel and administration expenses percentages are the lowest for the predominantly leasing group and they have managed to reduce the percentage from 0.22 percent to 0.18 percent and 0.49 percent to 0.26 percent respectively over the years.

Predominantly hire purchase group reports higher personnel and administration expenses percentage than the leasing group. They too have managed to reduce the percentage from .68 percent to 0.56 percent and from .90 percent to .77 percent.

6.30 Mixture of leasing and hire purchase group, reporting the highest personnel expenses and administration expenses percentage are seen to increase the personnel expenses percentage over the years from 0.75 to 1.10 while no reduction is reported in the administration expenses.

Companywise analysis confirms that First Leasing and 20th Century Finance have lower personnel and administration expense percentage than the new companies in the first group.

In the predominantly hire purchase group, Ashok Leyland finance and Sundaram Finance show comparatively lower personnel and administration expense percentage.

Table No. 6.26

PERSONNEL EXPENSES AND ACTIVITY

(Rs. in Lakhs)

Name of Companies	1986 Activity	1986 P. Exp.	1986 %age	1987 Activity	1987 P. Exp	1987 %age	1988 Activity	1988 P. Exp.	1988 %age	1989 Activity	1989 P. Exp.	1989 %age	1990-91 Activity	1990-91 P. Exp	1990-91 %age
Predominantly Leasing Companies															
First Leasing Company	4391	09	.20	6525	10	.15	9004	12	.13	12457	18	.14	16184	14	.09
20th Century Finance	7193	09	.13	9859	13	.13	13238	18	.13	19117	23	.12	21536	36	.17
Grover Leasing	599	08	1.3	841	14	1.7	980	17	1.7	782	21	2.7	972	15	1.5
PL Finance	837	03	.36	1013	04	.39	1142	06	.53	1280	09	.7	1318	08	.61
TOTAL	13020	29	.22	18238	41	.22	24364	53	.22	33636	71	.21	40010	73	.18
Mixture of Leasing and Hire Purchase Companies															
United Leasing	463	04	.86	775	05	.65	808	08	.99	1056	11	1.04	1379	12	.87
World Link Finance	49	-	-	578	08	1.4	812	13	.12	1188	13	1.09	1188	13	1.09
Midwest Leasing	912	10	1.1	1347	11	.82	2444	13	.53	2720	20	.73	2679	23	.86
DCL finance	515	05	.97	744	08	1.1	1230	12	.98	1519	16	1.05	1881	20	1.06
New Century Leasing	593	02	.34	859	03	.35	1312	06	.46	1831	09	.49	2277	13	.57
Sakthi Finance	1366	09	.65	3072	29	.94	5297	50	.94	8097	103	1.27	9538	127	1.33
TOTAL	3888	29	.75	7375	62	.84	11903	101	.85	16411	172	1.05	18942	208	1.1
Predominantly Hire Purchase Companies															
Ashok Leyland Finance	1234	04	.32	2546	10	.39	5787	16	.28	10303	35	.34	16980	58	.34
Sundaram Finance	17482	125	.72	19328	131	.68	21524	154	.72	27715	177	.64	38153	228	.60
Integrated Finance	773	05	.65	1703	08	.47	2109	12	.57	2380	19	.80	2777	23	.83
Kothari Orient Finance	433	03	.69	509	04	.79	663	07	1.06	717	10	1.39	1010	10	.99
Nagarjuna Finance	2936	19	.65	4487	24	.53	5306	33	.62	5850	47	.80	7407	53	.72
TOTAL	22858	156	.68	28573	177	.62	35389	222	.63	46965	288	.61	66327	372	.56

Source : Computed from Company Annual Reports

P. Exp. = Personnel Expenses;

Table No. 6.27

ADMINISTRATION EXPENSE AND ACTIVITY

(Rs. in Lakhs)

Name of Companies	1986 Acti-vity	A. Exp	%age	1987 Acti-vity	A. Exp	%age	1988 Acti-vity	A. Exp	%age	1989 Acti-vity	A. Exp	%ge	1990-91 Acti-vity	A. Exp	%age
Predominantly Leasing Companies															
First Leasing Company	4391	22	.50	6525	24	.37	9004	32	.36	12457	41	.33	16184	37	.22
20th Century Finance	7193	14	.19	9859	15	.15	13238	26	.2	19117	33	.17	21536	35	.16
Grover Leasing	599	20	3.33	841	23	2.73	980	31	3.2	782	22	2.81	972	16	1.65
PL Finance	837	8	.96	1013	8	.79	1142	14	1.2	1280	16	1.25	1318	17	1.3
TOTAL	13020	64	.49	18238	70	.38	24364	103	.42	33636	112	.33	40010	105	.26
Mixture of Leasing and Hire Purchase Companies															
United Leasing	463	7	1.5	775	8	1.03	808	10	1.2	1056	11	1.04	1379	18	1.31
World Link Finance	49	2	4.1	578	13	2.2	812	15	1.8	1188	20	1.68	1188	20	1.7
Midwest Leasing	912	17	1.9	1347	19	1.4	2444	23	.94	2720	33	1.21	2679	32	1.2
DCL Finance	515	6	1.2	744	9	1.2	1230	15	1.2	1519	25	1.65	1881	20	1.1
New Century Leasing	593	6	1.01	859	12	1.4	1313	15	1.14	1831	23	1.26	2277	27	1.2
Sakthi Finance	1366	19	1.4	3072	50	1.6	5297	85	1.6	8097	143	1.77	9538	172	1.8
TOTAL	3888	57	1.5	7375	111	1.5	11903	163	1.4	16411	155	1.6	18942	289	1.5
Predominantly Hire Purchase Companies															
Ashok Leyland finance	1234	10	.81	2546	18	.71	5787	40	.69	10303	78	.76	16980	128	.75
Sundaram Finance	17482	128	.73	19328	120	.62	21524	160	.74	27715	168	.61	38153	259	.68
Integrated Finance	773	11	1.4	1703	20	1.2	2109	26	1.23	2380	32	1.34	2777	31	1.11
Kothari Orient Finance	433	3	.69	509	5	.98	663	6	.90	717	6	.84	1010	6	.6
Nagarjuna Finance	2936	53	1.81	4487	63	1.4	5306	57	1.07	5850	81	1.4	7407	84	1.13
TOTAL	22858	205	.9	28573	226	.8	35389	289	.82	46965	365	.78	66327	508	.77

Soruce : Computed from Company annual reports

A. Exp. = Administration Expense

Table No. 6.28

OTHER EXPENSES AND ACTIVITY

(Rs. in Lakhs)

Name of Companies	1986 Activity	1986 O.E.	1986 %age	1987 Activity	1987 O.E.	1987 %age	1988 Activity	1988 O.E.	1988 %age	1989 Activity	1989 O.E.	1989 %age	1990-91 Activity	1990-91 O.E.	1990-91 %age
Predominantly Leasing Companies															
First Leasing Company	4391	46	1.05	6525	65	1.00	9004	63	0.7	12457	97	0.78	16184	117	0.72
20th Century Finance	7193	49	0.68	9859	73	0.74	13238	113	0.85	19117	97	0.51	21536	246	1.14
Grover Leasing	599	15	2.50	841	31	3.69	980	20	2.04	782	15	1.92	972	09	0.93
PL Finance	837	09	1.08	1013	14	1.38	1142	22	1.93	1280	20	1.56	1318	17	1.29
TOTAL	13020	119	0.91	18238	183	1.00	24364	218	0.89	33636	229	0.68	40010	389	0.97
Mixture of Leasing and Hire Purchase Companies															
United Leasing	463	04	0.86	775	03	0.39	808	06	0.74	1056	20	1.89	1379	03	0.22
World Link Finance	49	01	2.04	578	09	1.56	812	10	1.23	1188	20	1.68	1188	20	1.68
Midwest Leasing	912	14	1.54	1347	21	1.56	2444	25	1.02	2720	34	1.25	2679	24	0.90
DCL Finance	515	05	0.97	744	05	0.67	1230	08	0.66	1519	12	0.80	1881	06	0.32
New Century Leasing	593	02	0.34	859	07	0.81	1312	09	0.69	1831	14	0.76	2277	26	1.14
Sakthi Finance	1366	29	2.12	3072	76	2.47	5297	124	2.34	8097	227	2.80	9538	205	2.15
TOTAL	3888	55	1.4	7375	121	1.64	11903	182	1.53	16411	330	2.01	18942	283	1.49
Predominantly Hire Purchase Companies															
Ashok Leyland Finance	1234	07	0.57	2546	17	0.67	5787	31	0.53	10303	59	0.57	16980	84	0.49
Sundaram Finance	17482	91	0.52	19328	107	0.55	21524	126	0.59	27715	142	0.51	38153	172	0.45
Integrated Finance	773	05	0.65	1703	19	1.11	2109	20	0.95	2380	21	0.9	2777	39	1.40
Kothari Orient Finance	433	02	0.46	509	05	0.98	663	08	1.21	717	05	0.7	1010	12	1.19
Nagarjuna Finance	2936	28	0.95	4487	37	0.82	5306	56	1.1	5850	128	2.2	7407	167	2.26
TOTAL	22858	133	0.58	28573	185	0.65	35389	241	0.68	46965	355	0.76	66327	474	0.72
Grand Total	39766			54186			71656			97012			125279		

Source : Computed from annual reports of companies.

O.E. : Other Expenses

It is observed from table no. 6.28 that unlike the personnel and administration expenses, other expenses are higher for the predominantly leasing group (around 1 percent) than the predominantly hire purchase group (less than 0.75 percent) Mixture group report the highest operating expenses (above 1 percent)

6.31 Other expenses of First Leasing and 20th Century Finance in the predominantly leasing group, are comparatively lower than the new companies in the group. Ashok Leyland Finance and Sundaram Finance report lower other expenses than the remaining companies in the predominantly hire purchase group.

All companies in the mixture group except United Leasing and DCL finance incur higher other expenses.

The impact of other expenses is seen to influence operating expense than personnel and administration expense as is shown in Table No. 6.29.

Table No. 6.29

PERSONNEL, ADMINISTRATION AND OTHER EXPENSES AS PERCENTAGE TO TOTAL INCOME

	1986	1987	1988	1989	1990-91
% of Personnel Exp. to total income	2.7%	2.6%	2.7%	2.9%	2.7%
% of Adm. Exp. to total income	4.1%	3.8%	4%	4%	3.81%
% of other Exp to total income	3.9%	4.6%	4.6%	4.9%	4.8%

Source : computed from company annual reports

6.32 A further probe into the other expenses shows that miscellaneous expenses dominate the other expenses head. A detailed analysis of miscellaneous expenses is not possible in the absence of adequate information in annual reports. Majority of leasing companies are not reporting fixed deposit mobilisation expenses though they have substantial deposits. Hence miscellaneous expenses and advertisement expenses are treated as expenses incurred for Fixed Deposit mobilisation (All leasing/finance companies are resorting to tempting advertisements in leading news papers and journals frequently)

Table No. 6.30 shows that companies with huge fixed deposits like Sakthi Finance, Sundaram Finance, Kothari Orient Finance, First Leasing, Ashok Leyland Finance incur large miscellaneous expenses.

6.33 Thus, an enquiry into operating expenses brings out the fact that new companies with lower activity levels fail to attain the standard of large sized companies, which maintain the operating expenses to less than 2 percent of activity. Moreover, it is the other expenses which go up year after year which is to be controlled severely.

The broad classification of cash expenses into finance expenses and operating expenses for the purpose of analysis, now reveals that operating and finance expenses are lower for the predominantly leasing group, especially

Table No. 6.30

FIXED DEPOSITS AND MISCELLANEOUS EXPENSES

(Total of five years)

(Rs. in Lakhs)

Name of companies	P.D.	T.B.	%age	A.D.V.T & M.E.	Total O.E.	% age
First Leasing	10065	27186	37	311	387	80
20th century Finance	3955	33087	12	285	579	49
United Leasing	335	2387	14	11	35	31
World Link Finance	466	2079	22	26	60	43
Grover Leasing	1175	2583	46	36	90	40
PL Finance	1100	3249	34	69	82	84
Integrated Finance	1175	5960	20	73	104	70
Nagarjuna Finance	6350	18780	34	175	416	42
Midwest Leasing	1430	6145	23	64	118	54
DCL Finance	1000	3704	37	25	36	69
New Century Leasing	985	3906	25	25	58	43
Kothari Orient Finance	1175	2281	52	22	32	69
Sakthi Finance	22800	25017	91	406	661	62
Sundaram Finance	65220	85115	77	393	638	62
Ashok Leyland Finance	6390	18111	35	158	198	80

Source ; Computed from Company annual reports

P.D. = Public Deposits ; T.B. = Total Borrowings;

ADVT & M.E. = Advertisement and Miscellaneous Expense;

Total O.E. = Total Other Expenses

the older companies in the group. Hence the cash expense of the first group are the lowest.

Predominantly hire purchase companies show the highest finance expenses though their operating expenses are low, pushing the cash expenses of this group to the fore front.

The mixture group with a finance expense percentage on the increase, in between the two groups, reports highest operating expenses and increases the cash expense percentage substantially over the years.

6.34 **Non-cash Expenses:**

An analysis of non cash expenses shows that the percentage of depreciation to leased assets increased from 13.67 percent to 14.18 percent over a period of 5 years as is shown in table no. 6.31.

Table No. 6.31

DEPRECIATION PERCENTAGE TO LEASED ASSETS

	1987	1988	1989	1990-91
Average Assets (1) (Rs. in lakhs)	20895	27516	34714	42495
Depreciation (Rs. in Lakhs) (2)	2918	4163	4898	5734
% of Dep. to L. Assets $(\frac{2}{1})$	13.97%	15.02%	14.1%	14.18%

Source : Computed from Company Annual Reports

Groupwise analysis in table No. 6.32 shows that there are variations in the depreciation rates charged among the various groups. Comparatively lower depreciation rates are charged by the predominantly leasing group. On the other hand higher rates of depreciation are charged by the predominantly hire purchase group. Mixture group reported higher rates during the first two years but later the rates came down.

Company wise analysis shows that there is no uniformity among companies regarding the depreciation rates in any group.

6.35 The differences in the depreciation rates charged by leasing companies is due to the adoption of different methods of providing of depreciation. Leasing companies have various options for providing depreciation such as the following.

a. Depreciation charged over primary lease period (SLM)
b. Depreciation as per Company Law (Schedule XIV) (SLM)
c. Depreciation as per Company Law (WDV)

A reference to the notes on accounts attached to the annual reports of various companies for these years reveals that there is no uniformity among companies in adopting these methods. Seven companies follow Straight Line Method and rates as per Income Tax Rules are charged.

Table No. 6.32

AVERAGE LEASED ASSETS AND DEPRECIATION RATE

(Rs. in lakhs)

	1987			1988			1989			1990-91		
Name of Companies	Average Leased Assets	Dep.	Rate	Average Leased Assets	Dep.	Rate	Average Leased Assets	Dep.	Rate	Average Leased Assets	Dep.	Rate
Predominantly Leasing Companies												
First Leasing Company	4896	452	9	6377	871	14	7262	1096	15	8194	1451	18
20th Century Finance	7497	1076	14	9254	1246	13	11233	1475	13	13485	1634	12
Grover leasing	452	30	7	545	70	13	563	74	13	605	94	16
PL Finance	653	79	12	754	85	11	814	102	13	919	107	12
TOTAL .	13498	1637	12	16930	2272	13	19872	2747	14	23203	3285	14
Mixture of Leasing and Hire Purchase Companies												
United Leasing	368	65	18	453	71	16	574	78	14	784	116	15
World Link Finance	59	10	17	185	95	51	495	53	11	727	53	7
Mid west Leasing	373	35	9	485	50	10	712	63	9	924	138	15
DCL Finance	255	36	14	355	39	11	472	57	12	586	86	15
New Century Leasing	168	19	11	427	40	9	753	91	12	953	120	13
Sakthi Finance	808	129	16	1567	207	13	2776	314	11	3689	439	12
TOTAL	2031	294	15	3472	502	15	5782	656	11	7663	952	12
Predominantly Hire Purchase Companies												
Ashok Leyland Finance	349	66	19	649	109	17	1150	216	19	1943	334	17
Sundaram Finance	3788	753	20	4781	1000	21	5812	1017	18	7044	1066	15
Integrated Finance	273	23	8	360	34	9	456.	50	11	609	71	12
Kothari Orient Finance	112	12	11	149	18	12	163	18	11	225	23	10
Nagarjuna Finance	848	133	16	1178	200	17	1483	203	14	1808	294	16
TOTAL	5370	987	18	7117	1361	19	9064	1504	17	11629	1788	15
Grand Total	**20895**	**2918**	**14**	**27516**	**4135**	**15**	**34714**	**4907**	**14**	**42495**	**6025**	**14**

Source : Computed from Company Annual Reports DEP. = Depreciation, Certain companies adopt Straight Line Method and depreciation rate as per company Law, Schedule XIV is charged. Written Down Value Method as per Company Law is followed by Sundaram Finance throughout the period and United Leasing after 1988. Nagarjuna Finance now follow accounting policy no. 8 for charging depreciation. The information is given in the following Table No. 6.33.

6.36 The rates prescribed in Schedule XIV of the Companies Act for different items are as follows:-

Plant and Machinery	-	5%
Motor Vehicles	-	7%
Furniture & Fixtures	-	3%

Companies like Sakthi Finance are charging higher rates than prescribed in Schedule XIV (12.5% on these items) Ashok Leyland Finance is charging 13.57/16.21 per cent for Plant and Machinery while 20th Century Finance is charging 11.88 percent. Certain companies charge a higher rate of 33.33 percent on consumer durables leased out.

The varied depreciation methods and rates result in differences in the reported profits and offers much scope, for window dressing. Consistent criticism has centered around the mismatch between lease period and depreciation written off in the books.

Table No. 6.33

METHODS OF DEPRECIATION

First Leasing Company	:	Straight Line Method for all the years
20th Century Finance	:	Straight Line Method - Section 205 (2)(b) of the companies Act till 1988 after that straight line method based on new rates under Income Tax Rules - Leased Assets @16% Machine Tools @33 1/3% for other assets @19%.
Grover Leasing	:	Upto 1-4-1987 straight line method Section 205 (2)(b) of the Companies Act, Income Tax Rate - after 1-4-1987, rates specified in Schedule XIV, Companies (Amend) Act 1988.
PL Finance	:	Upto 1-1-1988, straight Line Method, Income Tax Rate - after 1988 Straight Line Method Schedule XIV, Companies Act - has provided terminal depreciation.
United Leasing	:	Till 1988 Straight Line Method Section 205 (2)(b) - after 1988 Written Down Value Method Schedule XIV rates.
World Link Finance	:	Upto 1988 Straight Line Method, Income Tax Rate.
Midwest Leasing	:	Upto 1-4-1989 Straight Line Method Schedule XIV , after 1989 Matching Depreciation Provided.
DCL Finance	:	Straight Line Method Companies Act rates Scheduled XIV - amended in 1988.
New Century Leasing	:	Straight Line Method - Income Tax Rates
Sakthi Finance	:	Upto 31-2-1987 Straight Line Method, Income Tax Rate after 31-3-1987 higher rates than Scheduled XIV rate is 12.5% - Scheduled XIV (Plant Machinery 5%, Vehicle 7%, Furnitures and Fixtures 3%).

Ashok Leyland Finance	:	Straight Line Method, rates, Plant and Machinery 13.57/16.21, Vehicles 19%, Computers 16%, Consumer Durables 33.33%, Other Assets 13.57%.
Sundaram finance	:	Written Down Value, Scheduled XIV.
Integrated Finance	:	Upto 2-4-1987, Straight Line Method Income Tax Rate after 2-4-1987 Plant and Machinery 13.57%, Furniture 3.39%, Building 5%.
Kothari Orient Finance	:	Straight Line Method, Scheduled XIV
Nagarjuna Finance	:	Accounting Policy No.8

Source : Complied from Company annual reports orders to stall the adoption of ICAI guidelines. Sundaram Finance and 20th Century Finance, two leading players in the leasing field, claim that they are providing depreciation equivalent to the ICAI guidelines.

6.40 The analysis points out that with the increase in leased assets every year, the depreciation also would increase and that predominantly leasing companies report only lower net profits. On the other hand predominantly hire purchase companies need provide depreciation on their leased assets only and report higher net profits.

It can thus be concluded that profitability of leasing primarily depends on

a. lease rental rates.
b. availability of funds and their cost
c. ability of leasing companies to expand their business every year.
d. Planning an optimum lease hire purchase mix.

CHAPTER - VII

PROSPECTS OF LEASE FINANCING

7.1 India is on the threshold of a major break through in industrial development, thanks to the farsighted and liberalised economic policy and measures initiated by the government at the centre. Rapid industrialisation is the motto behind every economic measure taken by the government. The equipment leasing industry is fully committed to do its part on the financing side, in the wake of anticipated surge in demand for term funds.

72. Units with investment below Rs. 5 crores were exempted from seeking industrial licence[1]. Delicensing of MRTP and FERA companies in respect of 22 out of 27 industries exempted under sec 22A of the MRTP Act was another step taken for accelerating industrial growth[2]. In general, procedural delays in the clearance of projects were avoided by the middle of 1980s. As a result of policy initiatives, a large number of companies were newly formed. The number of letters of intent issued during 1985 was 1456 - an increase of 37 percent over those issued in 1984[3]. There

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1. Indian Economic Diary, Jan 8-14, 1986, Page 10620
2. Ibid ....
3. Indian Economic Diary, July 9-15, 1986.

was a substantial increase in the number of new capital issues by non government public limited companies - from 225 issues in 1987-'88, the number went up to 517 in 1991-'92[4]. Similarly consents/proposals granted by Controller of Capital Issues (CCI) to non government public and private limited companies also show a tremendous increase - The consents jumped to Rs. 6124.0 crores by 1990-91 from Rs.2164.6 crores in 1987-'88[5].

7.3 For the year 1991, the forecast of total capital expenditure of the private corporate sector was Rs. 16,927 crores[6]. Considering the consents given in the year to the extent of Rs. 6124.0 crores, there was a gap of about Rs. 10,000 crores in 1991. According to Equipment Leasing Association (ELA) representative, leasing industry accounts for nearly 10 percent of the incremental capital formation[7]. Based on this estimate, leasing companies forsee an yearly business of Rs. 1,000 crores.

7.4 During the eighth five year plan period (1990-95), a major role has been assigned to the private sector and a

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4. 'Capital Market', Report on Currency & Finance, 1991-'92, Page 296.
5. Kothari Industrial Directory of India, 1990
6. "A study on corporate investment in 1991", RBI Bulletin - Bombay, March 1991.
7. The Economic Times, Bombay, July 26th, 1993.

total investment of about Rs. 3,00,000 crores is envisaged[8]. According to the Associated Chambers of Commerce & Industry (Assocham), the gap between gross savings and the projected investment in the private corporate sector during the plan period has been estimated at Rs. 43,000 crores[9]. If ten percent of this gap is routed through leasing, there is a scope for an yearly business of about Rs. 900 crores.

7.5 Availability of funds from capital market:

The funding pattern of the eighth five year plan included raising of Rs. 50,000 crores from the capital market[10]. Consents/proposals granted by Controller of Capital Issues (CCI) to non government public and private limited companies during the initial periods of the eighth five year plan shows that the target is not attainable.

Table No: 7.1 Consents/Proposals granted by CCI to non-government Public and Private Limited Companies. (Rs.in crores)

Year	Equity Shares& Pref Shares	Debentures	Total
1990	1688	5879	7567
1991	2553	3571	6124

(Amount include premium on shares)

Source: Bombay Stock Exchange Directory.

8. The Indian Economic Diary - Sept 24-30, 1989, Page 12164
9. Indian Express Oct. 17, 1989, Page 12.
10. The Economic Times, Bombay, June 12, 1989.

Even if the present trend is maintained, on an average, there is going to be a gap of Rs. 3,000 crores a year. The corporate sector in bound to look to other alternative means of financing, especially leasing.

7.6 Raising of funds from the capital market by public issues is becoming unattractive especially for small issues since on an average, more than 10 percent of the funds raised went towards issue expenses. It has been observed that, net public offer did not exceed Rs. 5 crores in 75 percent of cases out of 514 issues studied. The issue expenditure as proportion to net public offer was highest for these issues. Among these, the position of smaller issues was considered even worse. Net public offers ranging between Rs. 1 to 2 crores numbering 90, spent on an average 12.89 percent of net public offer as issue expenditure[11]. In such a situation, companies venturing for a small issue may think of leasing arrangements. According to prime data base report, out of 90 issues made during the month of February 1994, 69 companies resorted to public issue for financing specific projects[12]. Prudent promoters will look into the possibility of the acquisition of assets by leasing.

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11. "Cost of raising capital - A study of public issues made during 1992-93", Company News & Notes, Nov. 1993, Vol XXXI, No. 5

12. The Economic Times, Bombay, March 19th, 1994, Page 18

7.7 Fund raising is not only becoming very costly but also risky. Capital market is becoming highly competitive due to the presence of public limited companies as well as public sector units (PSU). Government has made known its intention to withdraw the budgetory support to public sector undertakings. They had informed the World Bank in December 1992, that it would phase out budgetory support to all public sector units by the end of March 1994 and the budgetory support to most of the profit making public sector undertakings have already been withdrawn.[13] Consequently, the profit making Public Sector Units are entering the capital market for raising fund requirements, thereby posing severe threats to the private sector companies relying solely on capital market. Of late, in a rare move, one of the Public Sector Units, the Metal scrap Trade corporation (MSTC) is planning a right issue at a premium.[14] Prime Data Base reports that public issues are on the poor front. During February 1994, out 90 issues, 21 companies failed to close their issues on the earliest dates and 11 companies extended the closing dates.[15]

7.8 In such situations, promoters with unproven track records will be exploring other financing modes including leasing. During February 1994, out of 90 public issues in

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13 The Economics Times, Bombay, March 21st 1994.

14 Ibid. . . .

15 The Economic Times, Bombay, March 19th, 1994, page 18

the fray, 87 issues were offered by companies making their maiden appearance in the capital market[16]. In a period of poor response from the investing public, the appearance of further companies in the capital market will be limited. Among other modes of finance for asset procurement, leasing will definitely be an important source.

7.9 Resource crunch for Financial Institutions:

Industrialisation process has been accelerated very much resulting in the registration of more and more new companies. Public limited companies registered in 1987-88 was 946 and it increased to 1589 in 1990-91[17], a growth of 68 percent over 4 years. But there is no significant increase in the growth rate of total financial assistance disbursed by all the financial institutions put together.

Table No: 7.2 Loans disbursed by Financial Institutions and the growth rate.

Year	Loans disbursed by financial Institutions (Rs. in crores)	Growth (in percentage)
1986-87	5655.6	-
1987-88	6788.4	20
1988-89	9163.1	35
1989-90	10240.2	12
1990-91	12480.3	22

Source: 43rd Annual Report of IFCI, 1990-91

16. Ibid....

17. "Company Statistics", Company News and Notes, Various Issues.

In order to tide over the resource crunch of financial institutions, IDBI wanted the business houses to reduce their dependence on financial institutions[18]. Sanction of loans by IDBI, the premier financial institution slowed down during the year 1990-'91 to 22 percent from 31 percent in 1989-90[19]. IDBI raised resources from capital market towards the end of 1991-'92, in order to overcome the resource crunch[20] and appeared in the market with bond issues.

7.10 Meanwhile, policy changes taken will continue to reduce the inflow of institutional funds to the corporate sector. The norms fixed for promoter's contribution for purposes of eligibility for getting loans from financial institutions were changed - the minimum contribution of promoters in their projects was hiked to 25 percent. Moreover, with effect from August 16, 1991 the interest rates on financial assistance provided by term lending institutions were made flexible with a floor rate of 15 percent per annum. Institutions are now free to charge higher interest rates on their loans taking into account factors such as credit worthiness of the borrowing units[21].

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18. Indian Economic Diary, Vol XII, Dec 3-9, 1984, No.49
19. Business India, Bombay, July 23rd-Aug 5, 1990,Page 19
20. The Economic Times, Bombay, March 12th, 1991,
21. "Capital Market", Report on currency & Finance 1991-'92 Page 296.

7.11 Of late, promoters with a good track record and sound project, finance cost overruns as well as bridge finance through lease finance route without approaching term lending institutions. New projects floated by entrepreneurs are being partly financed by lease finance. Recent issues such as Peacock industries, Phelix Appliances, Ankit Yarns and Good Earth organic have resorted to lease finance of Rs. 120 lakhs, Rs. 40 lakhs, Rs. 50 lakhs and Rs. 196 lakhs to finance Capital outlay of Rs. 9.6 crores, Rs. 5.6 crores, Rs. 4.50 crores, and Rs. 11.30 crores respectively[22]. Advocates of leasing forsee very good prospects if this tempo continues.

7.12 Long term borrowings of public limited companies from financial institutions as a percentage of net fixed assets shows the reduced inflow of funds from that source. The ratio shows a declining trend over the years.

Table No: 7.3 Long term borrowings as a percentage of net fixed assets.

	1982-83	1983-84	1984-85	1985-86	1986-87
Long term borrowing from financial institutions as percentage of net fixed assets	20.7	20.9	20.7	19.6	19.1

Source: Reserve Bank of India Bulletin, 1987-88

Inability of financial institutions to cope with the demands of companies projects much scope for leasing.

22. The Economic Times, Bombay, July 26th, 1993

7.13 **Availability of Term loans from Banks:**

The industrial sector was relying heavily on the banking sector for meeting their requirements - At one time, the latter had very little to spare for industries. Owing to high SLR and CRR consequent deposits with Reserve Bank of India, the banks were left with hardly 44 percent of their incremental deposits. This was warranted due to the high inflation which existed at around 17 percent. Out of this, the banks have to meet their obligations towards the priority sector, leaving only a minimal allocation for the industrial and commercial sector.

7.14 There was a hope that the lending obligation to the priority sector will be reduced from 40 percent to 10 percent, as per the recommendations of the Narasimham Committee. In such a situation, banks will be having enough funds for corporate lending. Now the Union Government has rejected the recommendation to cut the banks' priority sector lending[23]. In 1992-93, 22 public sector banks had fallen short of the stipulated priority sector lending target[24]. RBI had warned these banks in November 1993, of

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23. The Economic Times, March 20th, 1994, Page 1

24. The Economic Times, March 23rd, 1994

taking stern action, including the raising of reserve requirements and withdrawal of refinance facilities, if they did not reach their target by March, 1994[25]. With this end in view, RBI has relaxed the priority sector lending norms of all scheduled commercial banks.

Moreover, banks are facing stiff competition posed by non banking financial companies, in the matter of deposit mobilisation. The rate of growth of bank deposits for the year ending March, 31, 1990, has dropped sharply to 17.6 percent from 23.8 percent in the previous year (1989).[26] Consequently, the advances by banks rose from Rs. 34,623 crores at the end of March 1989 to Rs. 39,418 crores at the end of March, 1990, showing a rise of 13.8 percent only during the year as compared to the 21.6 percent rise in 1989[27]. It was reported that in the light of inadequate deposits, certain banks had resorted to rationing of credit also. According to R.L. wadhwa, Chairman cum MD Of Allahabad Bank, the bank may resort to 'rationing of resources' owing to inadequate growth in deposits[28]. For the year ended 30th June, 1991 also there

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25. Ibid.....

26. "Banking and Finance" Business world, Bombay, Aug 1-14, 1990, Page 22.

27. Report on Currency & Finance, 1989-90

28. The Banker, New Delhi, DEc. 1990, Vol.37, Page 8

has been a sharp decline in bank credit[29]. The inflow of deposits to banks are likely to be further affected due to the reduction in the interest rate and tax on interest income at source.

Eventhough the Government has reduced the SLR and CRR rates in the light of reduced inflation rates (around 7 percent in 1993) the recent increase in inflation rate to 10.62 percent in May, 1994 from 5.39 percent in July 1993[30] may pose problems again to the banking sector. Now, the margin between the interest rate offered and the inflation rate is very narrow (or may even become negative) and in such a situation, the flow of deposits to banks will be severely affected, thereby the ability of banks to advance to the industrial sector will be bleak. Meanwhile, the Government has removed all restrictions on interest rates on debentures and public sector bonds other than tax free bonds of public sector undertakings. The interest rate on these debt instruments will be governed by the market forces. Given a choice between bank deposits and company debentures / PSU bonds with better rates, the investor's preference may be for the latter

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29. "Banking and Finance", Business world, Bombay, Sept 25th - Oct. 8th, 1991.

30. The Economic Times, Bombay, May 2nd, 1994

ones in the present circumstances.

The slow flow of bank credit to industrial sector reflects the reluctance of banks to advance to the corporate sector. The Union Finance Secretary Dr. Montex Singh Ahluwalia has pointed out to RBI that there have been repeated complaints about banks going slow on giving credit to the corporate sector[31].

In the wake of insufficiency of funds from Capital market and term lending institutions and inadeqacy of bank loans, the prospects of leasing are excellent.

7.17 **Prospects of Import leasing:**

During the seventh five year plan, the total imports were estimated at Rs. 95,000 crores of which capital goods import will alone be Rs. 20,000 crores or Rs. 4,000 crores per annum as mentioned earlier. Even if a small percentage of such assets are imported under lease basis, the leasing companies forsee very good prospects. Approvals granted for the import of Capital goods during 1989-90 rose to Rs.1,633 crores from Rs. 1,037 crores in the previous year[32]. The eighth five year plan (1990-95) aims

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31 The Economic Times, Bombay, July 27th, 1993.

32 Fortune India, Sept. 1, 1990.

at freeing the Indian industry from licensing procedures for import of capital goods and then leasing activities will be popularised further.

7.18 **Prospects In The Light Of Policy Changes:**

Removal of investment allowance with effect from April 1, 1987 has made leasing very attractive to the corporate sector. Similarly reduction of depreciation for the assessment year 1991-92 (The Taxation Laws Amendment Act 1990) to 75 percent of what would otherwise be allowable have vastly changed the leasing scenario and more companies prefer to go in for lease finance rather than outright purchase of equipment - Based on the increasing scope for lease financing, Equipment Leasing Association of India's asset base is expected to cross Rs. 10,000 crores mark in the next two years from Rs.7,500 crores in 1993[33].

7.19 **Prospects For Sales Aid Leasing:**

It is a common practice in developed countries - especially in the US - for vehicle manufacturers to provide credit for the purchase of vehicles through finance companies promoted and managed by them.

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33. Financial Express - July 25th , 1993.

Corporations like General Motors and chrysler have subsidiary finance corporations providing finance for the purchase of cars and trucks. A similar phenomenon is now emerging in India. Vehicle manufacturers have found that it is useful and necessary to offer financial support through finance companies promoted and operated by them.

With a general recession hitting the automobile industry, owing to reduced demand, two wheeler as well as four wheeler manufacturers are tieing up with finance/leasing companies to move their products (Example: Kinetic Honda has tied up with 20th Century Finance - Ashok Leyland started Ashok Leyland Finance).

7.20 **Increased Scope for Consumer Finance:**

As the production of TV, VCR, VCPs, washing machines records a phenomenal growth, the need for consumer finance becomes more and more imperative. Leasing / finance companies have a major role to play as a catalyst in increasing the sales of these household items. The growth in consumer finance has been fuelled by the burgeoning middle class which has grown from a bare 10 million out of a total population of 350 million in 1947 to 150 million out of over 800 million today.

It is reported that Indian middle class is growing by 20 percent every year[34].

7.21 Experts say that only eight million of the middle class own any one form of consumer durables. Changed attitudes to borrowing, double income families, growing meterialism etc. contributed to the boom in hire purchase financing of consumer durables. The share of consumer durables is expected to grow with the introduction of more white goods such as washing machines.

Consumerism defies the policy makers attempts to curtail consumption of luxuries which, the middle class regards as necessities. Given below are ownership levels amongst high income families (monthly income more than Rs. 3,500).

Product Category		Ownership Level (%)
Telephone		50%
Two Wheelers		50%
Cameras		50%
Stereo System		50%
Refrigerator		88%
Mixer Grinders		85%
VCP		36%
Passenger Car		30%
TVS	(Double Ownership of TVS)	106%

Sources : The Economic Times, Bombay, April 30th, 1991

34. The Economic Times, Bombay, April 30th, 1991

7.22 The business of extending hire purchase facility for consumer durables is attractive for other reasons too. Interest rates are higher on consumer hire purchase than in industrial deals because the former are in no mood to bargain over percentages. In addition, the financing company can also claim the statutory deduction on depreciation by merely including a clause in the agreement. "After all, the consumer is not always a businessman and is unlikely to want this deduction for himself. What pleases him most is that he has technically became the owner of his cherished asset[*].

7.23 Most of the finance companies are designing innovative consumer financing schemes to attract this sector - Apple Leasing Company's two schemes - 'Apple car Finance' and 'Apple consumer Durable Finance' have attracted the employees of Rashtriya Chemicals and Fertilizers Ltd., E Merck (1) Ltd., Rallis India Ltd., Unichems Laboratories Ltd., etc - Apple Leasing company's disbursement in this consumer finance area alone was encouraging at Rs. 12 crores during 1989-90 while it was only Rs. 8 crore during the previous year[35]. Consumer services division of Gujarat Lease Financing Ltd. is

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* Ibid

35 Apple Leasing Company Annual Report.

growing at the rate of 50 percent per annum - Disbursement in 1993 of GLFL were to the tune of Rs. 41.04 crores[36].

7.24 **Diversification to non fund activities:**

Besides, in response to the need for progressive diversification of activities and the changes in the business environment, the leasing companies have started offering services in the field of non fund activities - Almost all leasing companies have received SEBI authorisation as category I Merchant banker. Many have associated with a good number of issues. During 1993, Gujarat Lease Financing Ltd., has associated with over 38 issues, mobilising funds to the tune of Rs. 500 crores in the capital market[37]. Leasing companies are competing with each other in the formation of mutual funds, where as some are keenly interested in stock broking - PL Finance has recently acquired a card in Madras stock exchage. Other non fund activities include mergers and acquisitions, advisory services in respect of deciding the funding pattern, marketing of issue, etc. All these diversification avenues offer great potential for growth.

7.25 At the sixth world leasing convention in sydney, Mr. Farouk Irani, the President of the First Leasing Company of India, Madras, has been more precise in his

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36. Dalal Street Supplement, March 7-20, 1994, Vol IX, No.5

37. Ibid....

estimate of Indias' 'big ticket' leasing requirements over the next ten years as approximately \$ 18.9 billion. His estimate is based on the following.

India's general purpose equipment purchase needs to annualise at US \$ 15 billion over the next decade. Similarly special purpose specific project equipment needs on a partial estimation, approximate \$ 3.9 billion and relate to the under mentioned details.

a) India's steel mills, especially the Rourkela and Durgapur plants, are projected to require an outlay \$ 1.3 billion on modernisation and upgradation activities.

b) The oil and Natural Gas Commission of India (ONGC), the govt. agency entrusted with India's off shore and on shore oil exploration, anticipated a need to purchase equipment valued at US \$ 1.4 billion for its southern India operations alone.

c) Indian Airlines alone may purchase 32 commercial air craft for approximately \$ 1.2 billion over the next five to ten years - Indian Airlines long term perspective plan indicates that by AD 2001 Indian Airlines expects to move 40 million passengers annually, requiring 45000 seats.

d) India will unquestionably be in the market for super computers.

Thus, based on this factual assessment, the prospects of lease financing in India are bright indeed and it can play a significant role in the industrial development of the country in the years to come.

CHAPTER - VIII

FINDINGS, CONCLUSIONS AND SUGGESTIONS

8.1 Lease financing as a mode of corporate finance emerged popular in India during the early eighties. Inspite of the spectacular growth in leasing companies as well as their volume of business, after 1986, the leasing scenario totally underwent drastic changes. Sufficient literature does not exist on the subject and the present state of lease financing in India and its prospects are still unclear. There are confusions about the impact of government regulations on leasing industry. Hence, the present study is an attempt to fill this gap in knowledge.

8.2 The primary objective of the study is to examine the present state of leasing industry and to assess the prospects of leasing in India. The evaluation of the financial performance and examination of the impact of Government regulations on leasing industry are the secondary objectives.

8.3 The study is an exploratory one and descriptive methods are used for presenting the information. The findings are based on both primary and secondary data. Detailed analysis of companies is made taking a sample of 15 companies at random from a universe of 75 leasing companies.

8.4 **Findings:**

There has been a phenomenal growth of leasing companies in India after 1982. Bank subsidiaries and financial institutions entered the leasing scenario and big ticket leases began to be undertaken. Currently, a market segmentation has emerged, with private sector leasing companies confining to smaller corporate requirements while the public sector lessors concentrate on big ticket leases.

8.5 The lease returns have declined over the years due to intensified competition and uneconomic rental rates. Hence there has been a fall in the net profit ratios of leasing companies. Consequently many companies switched over to hirepurchase and other activities to augment their earnings. Recently, leasing and hire purchase companies in the private sector are seeking diversification in fund based and non-fund based activities for enhancing the bottomlines. The select areas are bill discounting, merchant banking, portfolio management, consultancy services and so on.

8.6 Leasing is a hedge against obsolescence and in advanced countries sophisticated items prone to become outdated like computers dominate the assets leased. But in India Plant and machinery is the major item leased. However, the leasing of assets likely to become obsolete rapidly is emerging popular recently.

8.7 Guidelines on capital issues of leasing companies intended to curb the entry of fly by night operators to the leasing scene, ensured healthiness for the industry. It facilitated the entry of only financially sound companies especially when credit rating became compulsory for finance companies before they entered the capital market.

8.8. Though state Governments are imposing sales tax on lease transactions, treating it as a sale, leasing industry is not permitted to issue 'C' form as the Central Sales Tax Act is not yet amended suitably. Hence leasing companies have to pay around 10 percent or the applicable rate in that state whichever is higher on the assets procured from other states.

8.9. The directive insisting stock exchange listing for undertaking import leasing will only prevent the bank subsidiary leasing companies from doing import leasing.

8.10 Sec. 370 and Sec. 372 of the Companies Act make it difficult for leasing companies, mostly in the private sector, to deploy large amounts as loans and advances during times of low business.

8.11 Reserve Bank of India prohibited commercial banks from extending term loans to leasing companies from 1988 onwards. This restricted the leasing companies to avail only cash credits and this increased the financial burden as cash credit is costlier than term loans. Frequent interest rate revision by commercial banks pushing the rate to 22.5 percent as on october Ist, 1991 from around 17.5 percent in 1988 made this source unattractive. Only if other sources are not adequate and available, leasing companies utilised bank borrowings. Inspite of the shortage of long term funds, they are not using the full eligibility utilisation of their net owned funds. It is seen that only around 40 percent of the eligibility is utilised by the industry. The percentage of bank loan in total fund declined from 23 in 1987 to 19 in 1990-91.

8.12 The redefinition of deposit liability for ensuring the safety of depositors (including debentures, intercorporate deposits along with public deposits) as per Shah committee report will adversely affect companies with mixed portfolio (debentures, intercorporate deposits and deposits) due to the necessity of maintaining more funds as liquid assets. Companies depending solely on public deposits gain while others stand to lose as funds that could be invested to finance their main activity will have to be deployed in other less rewarding assets inorder to satisfy the liquidity requirements.

8.13 Investments of leasing companies are maintained for complying with the statutory requirements of liquidity norms negating the talk in the industry circles that leasing companies are syphoning funds to group/subsidiary companies by way of investments.

8.14 Substantial reduction in leasing activity during 1987 and 1988 generated surplus funds. Inspite of the applicability of Sec. 370 and Sec. 372, such funds were deployed as loans and advances until new leases at remunerative rates came along.

8.15 Well managed leasing companies have efficient debt collection polices. They report nil/low debtor balances and shorter collection period which in turn, have enhanced their profits.

8.16 Though the prudent financial policy is to finance fixed assets and hard core current assets using long term funds, leasing companies resort to short term funds for financing fixed assets which is very risky, following a highly aggressive financing policy.

8.17 Leasing companies are eligible to borrow 10 times the net worth. But the full eligibility is not utilised inspite of the shortage of long term funds. This is so because the spread between Return on Investment (ROI) and the cost of borrowing is very thin.

8.18 Public deposits are the cheapest source of borrowed funds. But this source is more accessible to companies with reputed group backings. Hence, the finance cost of such companies are maintained at a lower level. The cost of borrowing of young and new companies are high as they have to depend heavily on bank borrowings. There is a visible attempt on the part of many companies to reduce the volume of bank borrowings.

8.19 Finance expense are high for the predominantly hire purchase group as they finance a larger percentage of their activity using borrowed funds compared to the predominantly leasing and mixture group. Moreover, it is found that the pattern of financing also had an impact on the finance expenses. Young and new companies depending more on bank loans incur more financial expenses than older companies depending on public deposits or financial institution loans.

8.20 The operating expenses of large sized companies are nominal being around 6 percent of their income, where as young and new companies incur a higher percentage (around 16 percent) as operating expenses.

8.21 Among the components of operating expenses, it is the other expenses which go up year after year which is to be controlled severely. It is noticed that companies with huge fixed deposits incur large other expenses.

8.22 A variety of accounting practices are adopted by leasing companies in India. The council of ICAI has issued draft guidance note for standardising the accounting procedures of leasing companies. Yet, so far ICAI guidelines are not adhered to by many companies and there exist a lot of mismatch in lease accounting and reported profits.

8.23 Profits of leasing companies do not lend themselves to mutual comparison as there is no uniformity among the companies regarding the charging of depreciation. Majority of the companies are not providing sufficient depreciation to recoup the cost of the asset within a five year period. (Indian leases are mainly for five years).

8.24 Insufficiency of funds from capital market, resource crunche faced by financial institutions and inadequacy of bank loan to corporate sector projects excellent prospects for lease financing.

8.25 Of late, Vehicle manufacturers are competing with each other to offer financial support through finance companies promoted and operated by them to move their products and this adds to the propularity of leasing.

8.26 Leasing/Finance companies are designing innovative consumer financing schemes to attract the burgeoning Indian middle class. These companies have a major role to play as catalyst in increasing the sale of several household items.

8.27 **Conclusions and Suggestions:**

Anticipating the increased scope for leasing, there has been a mushrooming growth of leasing/finance companies in the past few years. But it has not been an easy win for all as only a few have been able to make it to the top. Those in the traditional business of leasing, hire purchase and bill discounting are in for trouble not because of the lack of business opportunities. The margins from leasing and hire purchase have become thin and the bill discounting market is choked by Reserve Bank of India banning banks from rediscounting bills originally discounted by finance companies. Yet many companies have managed to face the rough weather. The timely spin off into other fee based activities like merchant banking, forex and corporate advisory services, mutual funds etc. have come to their rescue.

8.28 With the increasing need for capital investments, coupled with inflationary conditions, the demand for long term funds will always outweigh the supply of funds. Thus there is vast scope for leasing companies in the years to come - But all leasing companies will not be a great success. Their success will depend upon how judiciously they pick and choose their business and manage the funds.

8.29 Eyeing the booming financial services sector for increasing the profits will compensate the reduced margin caused by the entry of financial institutions including banks to the leasing arena. Dependence on public deposits rather than bank loans by leasing companies will reduce the funding cost and withstand the reduced return from traditional business line.

8.30 Inspite of the stumbling blocks in the path to prosperity, sufficient scope for leasing companies can be anticipated. The present lack lustre of leasing industry is likely to be short lived. The pragmatic policies of the Government for economic revival through liberalisation offer ample possibilities for reducing the cost of borrowings. Then sufficient spread between Return on Investments (ROI) and cost of funds can be expected. Leasing companies can strive to reduce the operating expenses to the desired level for improving the profits. Besides, diversification to non-fund activities can bring in much returns.

8.31 In short, the future of leasing industry is not as rosy, in the Indian Situation - but it is not bleak either. The important thing is how leasing companies administer their business.

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