
INDUSTRIAL FINANCE IN PAKISTAN

Mohammad Ameer Hussein

NEED FOR FINANCE

The process of industrialization in every under-developed country takes time and calls for much effort and sacrifice on the part of the people and the Government. The most striking feature of Pakistan's present economy is the marked contrast between her vast natural resources and her extreme industrial backwardness. This state of affairs has been mainly due to the unfair treatment, which the areas now comprising Pakistan received at the hands of the industrial planners of the undivided India.

After Partition, it was realized by the Government that overwhelming dependence on agriculture alone was not conducive to the economic development of the country and we could speed up the economic development by effective state measures. To embark upon development plans capital is a great necessity. It is needed mainly for two purposes.

Firstly, funds for block-capital, *i.e.*, to finance fixed capital expenditure upon land, building and machines and other appliances of a durable and permanent nature. In case of established industries, the need of long term capital is very intense for purposes of extensions, replacements, modernization and reorganization.

Secondly, working capital to finance floating assets for the purchase of raw materials and finished products and numerous other day-to-day needs of industries.

SUPPLY OF FINANCE

The principal agencies of finance now available in Pakistan are joint stock banks, co-operative banks, industrial corporations and to a very small extent the money lenders.

JOINT STOCK BANKS

Our banking system inherited the present pattern from the British banking system. Like the British banks, the Pakistani as well as Indian Joint Stock Banks deal mostly in financing the internal and external trade of the country. Though in the beginning the external trade was vested in the hands of Exchange Banks, but after Partition a large part of foreign trade business is undertaken by the Pakistani Banks.

LACK OF BANKING FACILITIES FOR NON-COMMERCIAL SECTOR OF THE ECONOMY

The reasons why our commercial banks have failed to help the non-commercial sector of the economy are given below:—

INDUSTRIAL FINANCE IN PAKISTAN

- (1) To serve the non-commercial sector of the economy, *i.e.*, industry, it is essential that the commercial banks should be able to lend long term credit to the industrialists. As the funds available with the Pakistani Banks are hardly sufficient to meet the seasonal demands of the market, it is not possible for them to block their capital for a long period.
- (2) Most of the deposits of the commercial banks are made up of “demand deposits” with the result that in the event of a sudden demand, it is not possible for them to meet the requirements of their constituents.
- (3) To lend against the mortgage of land, buildings and machinery, it is necessary that the bank should have a highly trained staff; which in the present conditions is not available.
- (4) In case of default, civil suits take a long time to decide.
- (5) There is every likelihood of fall in the value of land and machinery, if the borrowing companies were to cease production for a time.
- (6) Besides, the commercial banker thinks that the investment of short-dated deposits in non-convertible securities is hardly consonant with the sound canons of commercial banking. Any bank that dare to undertake the three lines of financing, agriculture, industry and commerce in its hands, is sure to come to grief.

CO-OPERATIVE BANKS

These banks were established mainly for meeting the credit requirements of our agriculturists. After Partition, the co-operative banks have changed their field of activity, *i.e.*, instead of supplying rural credit, they supply credit to commerce. These unpleasant changes occurred immediately after the Partition, when most of the non-Muslim banks migrated to India and closed their offices in Pakistan. They are even now playing a significant role in financing the operations of rice husking mills, oil expellers, cotton ginning, flour grinding and roller flour mills. Though this had its utility after Partition, but it cannot be said that industrial finance is the function of co-operative banks in Pakistan because the primary purpose of co-operative bank is to meet the requirements of agricultural finance.

As it has been explained above, the main function of the co-operative banks is to help the agriculturists, but keeping in view the shortage of finance for small industries, the Pakistan Industrial Co-operative Bank, Lahore was established about two years back.

The main functions of this Bank are as under:—

- (1) To finance co-operative industrial societies in the Punjab (Pakistan) affiliated to it and generally to carry on banking business.

INDUSTRIAL FINANCE IN PAKISTAN

- (2) To purchase and sell appliances and 'manufactured goods.
- (3) To purchase and sell raw material and other articles required by members of co-operative industrial societies and to sell on behalf of members of such societies finished products, etc.

But keeping in view the amount of its working capital which is only a meagre amount of sixty lakhs of rupees, it is not possible to help the cottage and small scale industries on a large scale.

INSURANCE COMPANIES

The Insurance Companies have played a great role in the industrial finance in other countries. In Japan and the United States particularly, they have provided long term finance by investing in mortgages on real estate and on factories as well as on industrial securities. In our country, these insurance companies invest their funds in government securities and have generally avoided industrial securities and real estate mortgages. The principal reason for this is that the industrial securities are generally non-marketable and hence cannot help them to get accommodation against them.

BILL MARKET

The bill market is still non-existent in our country though some efforts are being directed towards development of Stock Exchange and other organized markets. The funds raised through the issue of debentures constitute a very small proportion of the total share capital of industrial enterprises in our country. The proceedings of the Central Banking Enquiry Committee reveal that industrial concerns which had issued debentures were not looked upon with favour by the commercial banks/ simply because a concern was not exclusively financed by its share capital and was not eligible for banking accommodation.

PRIVATE SECTOR

Before Partition, the system of managing agents was very popular. These managing agents used to *promote* and manage, finance and guarantee the loans advanced by the commercial banks. In Pakistan, however, the managing agency system has become considerably less important as a source of industrial finance. The Pakistan Industrial Development Corporation is at present acting as managing agents for a number of industrial undertakings.

MONEY LENDERS

The role of money lenders in regard to financing of industries is insignificant. Before Partition, the big *sahukrs* used to help the industrialists to some extent, but since then the rote of money lenders has almost disappeared. There are a few Afghans who are euphemistically called mobile, bank, and who advance small loans to the labourers and charge exorbitant rates of 20 to 30% per month.

INDUSTRIAL FINANCE IN PAKISTAN

EXTERNAL RESOURCES

As far as obtaining the foreign capital for the industrialization of our country is concerned, Pakistan would welcome the participation of foreign capital seeking investment from a purely industrial and economic objective and not claiming any special privileges and provided participation of indigenous capital is given proper opportunities and monopolies were avoided. The Government of Pakistan in her latest announcement on the industrial policy welcomed the entry of foreign capital into Pakistan industries and stressed that at least 51% of all classes of share capital and debentures,¹ in certain specified industries should be subscribed by the Pakistani nationals. In case indigenous capital is not forthcoming the balance may be subscribed by the foreign investors with the approval of the Government. Such facilities have been afforded to the foreign investor, in order to attract foreign investment and also give an opportunity to the Pakistani investors.

INTERNATIONAL BANK FOR RECONSTRUCTION AND DEVELOPMENT

So far our Government has taken three loans from the International Bank for Reconstruction and Development, amounting to \$ 27.2 million \$ 3.25 million and \$ 14 million for the rehabilitation of Railway, agricultural development and construction of natural gas transmission line. Private foreign capital so far received in Pakistan has not exceeded 75 million rupees. The Commonwealth Finance Corporation is also giving some help to us. But, keeping in view the foreign exchange needed for our industrial development, it is necessary that the Government of Pakistan should make strenuous efforts to obtain foreign capital on a large scale though the interest and repayment of these loans will in the future absorb a major part of our foreign exchange earnings, but within a period of 10 to 20 years these loans will become self liquidating and the economic development of the whole country will considerably increase. We have, in history, instances of economic development by many countries with the help of foreign capital. Germany, Japan and even United States are the important examples.

PAKISTAN INDUSTRIAL FINANCE CORPORATION

The Corporation was established in July 1949 with an issued and paid up capital of Rs. 2 crores and was entrusted with the important function of providing industrial facilities to industrial concerns in the country. The Corporation has been given the authority to guarantee loans raised by industrial concerns which are repayable within a period not exceeding 20 years and which are floated in the public market. It can grant loans to or subscribe to the debentures of industrial concerns provided the loans or debentures are payable within a period not exceeding 20 years. It can also underwrite

1. The ratio of foreign capital investment has been relaxed and ranged to 60% of the total share capital.

INDUSTRIAL FINANCE IN PAKISTAN

their issue of stock shares, bonds or debentures. It is, however, not authorized to subscribe directly to the shares or stock of any company having limited liability.

The Corporation started functioning in October 1949 and has so far sanctioned loans to the extent of Rs. 5,08,00,804 (as on 30.6.1954). The share capital offered to the public was over-subscribed. The amount sanctioned by the Corporation is quite substantial but a major part of the amount sanctioned to the prospective borrowers has declined because of certain unbusinesslike conditions.

- (a) The Corporation grants loans for the expansion of industries, but the method of exhibiting the present assets and assessing the total amount of loan is not encouraging. Generally loans are granted in the ratio of 50% of the total value of the assets owned by the borrowers.
- (b) Refugee industrialists are not given any assistance.

THE PAKISTAN INDUSTRIAL DEVELOPMENT CORPORATION

The Corporation was established on 12th January 1952 under the P.I.D.C. Act, 1950. It is entrusted with the task of industries with 'equity' finance, as distinct from 'loan' finance.

So far the Corporation has participated in 30 projects, with investment of approximately Rs. 35 crores. In addition to this it has been successful in getting private capital to the tune of Rs. 25 crores. The International Bank for Reconstruction and Development has agreed to subscribe Rs. 5 crores for one of the-projects, viz., The Sui Gas Project. Apart from this, Rs. 5 crores is contributed by friendly Governments through United States and Commonwealth Aid Programmes. It is estimated that after deducting the recurring expenditure in foreign exchange on import of raw materials, it shall cause savings in foreign exchange expenditure and additional earnings of approximately Rs. 50 crores per annum (from 1956 onward). In terms of employment it is estimated that over 90,000 persons will be directly engaged on working of the factories. The progress made by the Corporation during the last three years is spectacular. But to issue the qualitative progress in the production of its products, these mills and factories should be transferred to the private ownership. While transferring these enterprises, shares should be sold out to the workers of the factories. In this way, the unrest and discontentment will be alleviated and the Government would, be able to achieve the goal of "Welfare State".

INDUSTRIAL INVESTMENT AND FINANCE CORPORATION

In India, an Industrial Credit and Investment Corporation of India, Ltd., has recently been set up. Its share capital has been fixed at Rs. 25 crores. For the present Rs. 5 crores has been issued for public subscription. Apart from the private investment, part of the capital will be subscribed by the International Bank for

INDUSTRIAL FINANCE IN PAKISTAN

Reconstruction and Development. The principal objects of this Corporation are (i) providing finance in the form of long or medium term loans or equity participations, (ii) sponsoring and underwriting new issues of shares and securities, (iii) guaranteeing loans from other private investment sources.

INVESTMENT AND FINANCE CORPORATION (PAKISTAN)

It is reported that a similar Investment Corporation is also being established in Pakistan. The International Bank for Reconstruction, and Development will also contribute a part of its capital. The capital of the Corporation will be about Rs. 10 crores. It is hoped that with the establishment of this giant Corporation, the huge industries like the iron, steel and petroleum will be set up. A recent communiqué of the APP adds “plans to establish Rs. 60 crore iron and steel factory have been finalized by the Pakistan Industrial Development Corporation,” — The factory it is stated, will be built according to the designs and recommendations of the German Consultants of the Corporation. The annual capacity of steel factory is expected to be of one lakh tons. Daudkhel deposits will supply 2,50,000 tons of quality iron ore annually.²

INTERNATIONAL INVESTMENT FINANCE CORPORATION

Further recommendations for the establishment of an International Investment Finance Corporation are under active consideration of the United Nations and, when established, will accelerate the industrialization of the under-developed countries. The capital of this Corporation is reported to be much more than the IBRD. The surplus funds available with advanced countries will be pooled-together and channelled toward the development of under-developed countries.

THE INDUSTRIAL BANK OF PAKISTAN

Though the PIDC and PIFC are playing their role quite satisfactorily, but the role which an Industrial Bank can play is far more attractive. According to Mr. Muhajir, the proposals regarding the establishment of the Industrial Bank were tentative and at the stage of discussions. Neither the State Bank nor the Government of Pakistan have yet made any commitments in this behalf. But he was sure that proposals would soon be finalized and the Industrial Bank would come into being. It will finance small and medium sized industries.

According to one information, half of its initial capital of two crore rupees would be raised in Pakistan, while the rest would be subscribed in America and Great Britain. It is also expected that the State Bank of Pakistan, the Pakistan Government and the International Bank for Reconstruction and Development would advance substantial

2. Mr. Roth, Chairman, I.M.F. after a recent visit to Pakistan has promised to plead the case of Pakistan Investment Corporation for substantial grant.

INDUSTRIAL FINANCE IN PAKISTAN

loans to the new start.³ In almost all the advanced countries Industrial Banks are running successfully. In Turkey, the Industrial Development Bank has a net work of branches all over the country and has done great service in the field of industrialization.⁴

SMALL INDUSTRIES CORPORATION

Cottage and small scale industries, despite their unassuming name, have a very important position in the economic standard of Pakistan, for they supplement Pakistan's agricultural economy, and are the fore-runners of the industrial era in the country.

The Government of Pakistan has now taken a step in the right direction and a Small Industries Corporation with its headquarters at Karachi has been set up by an Ordinance promulgated by the Governor General. The authorized capital of this Corporation will be Rs. 1 crore, divided into one lakh fully paid up shares each. The Central Government will hold 51% of the total share capital and the rest will be open for public subscription. According to statement of an official spokesman of the Corporation, it will have a two-phase programme.

The first phase comprises the opening of a general purposes workshop at Lahore which will be mostly manned by American experts primarily to plan modernization of small-scale industry. Measures regarding the movements of existing industries will also be taken in hand.

The second phase of the programme will include planning of certain essential industries. The machinery and the raw material will be imported from abroad and kept ready for sale to anybody who really wanted to start the industry to eliminate the long painful process of imports on individual basis. "Training will also be given to the industrialists" with the improvement in the techniques of these cottage and small scale industries. It is hoped that Pakistan will be able to save a substantial amount of her foreign exchange earnings. These earnings will then be utilized for the import of capital goods. In Pakistan, the Batala Engineering Co., Ltd. is also producing fine machinery for tube wells, etc., and it is hoped that the establishment of steel and iron industry at Daudkhel will cater a substantial part of our requirements. The small scale industries have so far been neglected, but now with the establishment of this Corporation it is expected that the internal trade of Pakistan will increase with the employment of surplus manpower for these industries, and the whole economy will be benefitted.

According to the Ordinance the functions of the Corporation will be as under:

- (a) to give loans to cottage and small scale industries.

3. State Bank of Pakistan will advance Rs. 2 crores at a nominal interest rate and the Central Government will provide funds to the tune of Rs. 3 crores with without interest (Finance Minister's Budget Speech, 1955).

4. Speech of Prof A. A. Kuyucuk, Professor of Economics, Istanbul University.

INDUSTRIAL FINANCE IN PAKISTAN

(b) to give loans to subsidiary Corporations and Commercial Cooperative Banks for the development of cottage and small scale industries.⁵

The limit of loans for an individual and subsidiary corporation or a company or a bank or co-operative society has been fixed at Rs. 10,000 and Rs. 1,00,000 respectively.⁶

In addition to above, even foreign loans will also be made available to the prospective borrowers.

CONCLUSION

In going through all the financial institutions, one observes that there is very little co-ordination in the facilities afforded to the industrial sector.

There are at present three corporations working for the finance and development of the industries. In addition to these, schemes for establishing an Industrial Bank of Pakistan and the Investment Corporation are also under active consideration. In order to co-ordinate the activities of different financial institutions, it is necessary that two Institutions should emerge out of all these Corporations. One should be the Industrial Bank of Pakistan and the other Industrial Development Corporation. It is possible that the whole task should be entrusted to only one institution, but in the beginning it would become very difficult to carry on different types of work. The Small Industries Corporation and the Industrial Finance Corporation can be merged into Industrial Bank of Pakistan and the funds set apart for the Investment Corporation. Large number of such organizations will result in heavy cost of maintaining establishments at many industrial centres moreover, the programme of opening branches of Industrial Bank in all the important cities of the country will not be possible. Further, there will be clash of the same kind of facilities offered by different institutions. The Development Corporation should open its branches only in important industrial centres. Facilities of loans through the National Bank of Pakistan should also be provided.

In the end, I hope that with the closer co-ordination and cooperation of these financial institutions, the pace of industrialization will be speeded up. If funds are available with cooperative and commercial banks, these should also be made use of for the execution of our development projects like the State Bank's Officers Training Scheme. A scheme for sending educated young men for higher education in industrial banking to foreign countries should immediately be implemented thus allowing the industrial finance flow and economic development proceed on a sound footing.

5. A Committee has recently been set up to investigate into prospects and problems of the handloom industry and make recommendations.

6. The Central Government have earmarked Rs. 75 lakhs and Provincial Governments have reserved Rs. 5 lakhs each for the Corporation.