

# **Masuta Producers' Company Limited:**

## **A case study in working capital finance**

Web Site: [www.masuta.org](http://www.masuta.org)



## Table of Contents

<b>S. No</b>	<b>Particulars</b>	<b>Page No.</b>
1.	Introduction	3
2.	Masuta Producers' Company Limited	3
2.(i)	Governance & Management Structure	5
2.(ii)	Operation	5
2.(iii)	Management Information System	7
2.(iv)	Infrastructure	7
2.(v)	Marketing	7
2.(vi)	Human Resource	8
2.(vii)	Financial	8
3.	Industry	8
4.	Challenges faced by the Company	10
5.	Objective of IFMR Trust	11
6.	Partnership with IFMR Trust	11
6.(i)	Structure of the loan	12
6.(ii)	Financing Structure	13
7.	Benefits to the Producers, MBTs & MPCL	14
8.	Annexure 1-Balance Sheet Analysis of MPCL	15
9.	Annexure 2-P&L A/c Analysis of MPCL	17
10.	Annexure 3-Transaction Structure	18
11.	Annexure 4- Projected Advance to MBTs	19

## **1. Introduction**

Women from interior villages of Bihar, Jharkhand and Chhattisgarh are employed in seasonal jobs such as agriculture, brick kiln, stone crusher, constructions etc. They are also employed in collection of firewood, mahua flowers, tendu leaves, and sal leaves which provides them irregular earnings whereas, livelihood based on Tasar yarn provide them regular earnings.

PRADAN (a society registered under the society registration act) promote the activity of Tasar yarn production and the process starts with organizing women in Self Help Groups (SHGs). SHGs are linked with banks, which enables them to access larger volumes of credit. At the same time, the process of livelihood planning is initiated in all SHGs in which each member is helped to make a livelihood plan for her family. Many such members, after assessing their resources and aspirations, opt for a livelihood based on Tasar yarn production.

Traditionally, the sericulture sector is unorganized and there are two parts to it namely cocoon production (raw material used for yarn production) and yarn production. Both are fragmented and unorganized and are confined to forest dwellers, tribal population and small weaving clusters.

As a step towards organizing the sector, all the yarn producers at the village level are clubbed together and are formed into a yarn producers' organization which is registered as Mutual Benefit Trust (MBT). So they elect their representatives at the Block Level which forms Unit-committee. The Unit-committees elect their representatives for the General Body of Masuta Producers' Company Limited (MPCL). They also elect their director in the MPCL Board of Directors.

## **2. Masuta Producers' Company Limited (MPCL)**

MPCL was registered on 26th December 2005 as a Producers' Company under Section 581c (5) of Part IXA of the Companies Act 1956.

MPCL is owned by the village level primary groups of shareholders, formalized as MBT which comprises of women from communities like tribals and various lower castes of the society. A Tasar yarn producer undertakes her production activity as an individual enterprise even though a group of producers often work under a common facility centre. MPCL helps them acquire productive assets for yarn making (like reeling machines etc.), supplies raw-materials and other inputs, provide on-job trouble-shooting support and finally market their produce. Further members of the company (MPCL) will remain as the beneficiaries of PRADAN.

MPCL became a collective of 90 MBTs which comprises of 2500 women yarn producers from disadvantaged rural families living across three eastern states of Bihar, Jharkhand and Chhattisgarh. The head office of the company is in Deoghar (Jharkhand) and presently it has its marketing units at Delhi and Bhagalpur. The company has production units at Godda, Dumka, Koderma and Petarbar of Jharkhand and at Raigarh of Chhattisgarh.

The reason behind forming the MPCL is the bulk demand of yarn by industry whereas the producers are small, fragmented, distributed in remote areas and produces in small quantities. Furthermore, producers cannot avail credit facilities individually because of the little net-worth. MPCL can aggregate the yarn, sort them, grade them and supply it to the market. The buying of raw material (cocoons) is capital intensive as well. Due to aggregation by MPCL, the producers through MBTs can avail the formal banking facilities and are able to purchase the cocoons and other materials in bulk.

The company helps the Yarn producers in acquiring technical skills and the entrepreneurship skills. Central Silk Board provides training to yarn producers on abovementioned skills. Salkhi Devi (Yarn producer) speaks about the training, “We learnt about the raw material (cocoons) and the reeling machine, how to improve our hand-eye coordination and understood quality parameters”. Additionally, entrepreneurship motivation training is conducted to help the women understand the business, its economics and their position in the overall business.

## **2. (i) Governance & Management structure**

For better governance, the company (MPCL) is divided into eight different clusters alias unit which has Unit-Committee comprised of representatives of the various MBTs. The Unit-Committee meets every month. Also, in the board of the company, every unit has representative who is the Director of the company. The board also has four co-opted Directors and a Managing Director apart from the eight elected Directors. The Board of Directors meet on a quarterly basis to monitor the performance of the company.

The Management Committee of the company is comprised of the Managing Director, Manager (Marketing) and Executive (Finance). The Managing Director, lead the operation of the company and is assisted by managers, executives, officers and assistants. The management committee meets once in every two months to take care of operational decisions.

## **2. (ii) Operation**

### **Raw Material Procurement**

The operation of the company starts with the bulk procurement of raw material i.e. Tasar cocoon by its cocoon business branch. The member MBTs assess their annual requirements of cocoons well ahead of its harvest and inform the company. Company then purchases raw material (cocoon) from local cocoon rearers as well as by taking part in state auctions conducted by sericulture department of different states. Cocoon is stored in Storage-houses and women producers purchase cocoon from the company as and when it is required. These producers make Tasar silk yarn from cocoon and sell it back to the company.

### **Storage-house management**

Once cocoons are purchased for the whole year, it is stifled and stored properly at storage-houses. Stifling helps preserve cocoon by reducing moisture and killing the pupae. Company has 3 big storage-houses and 8 smaller ones. For each big storage-house, one caretaker is deployed from the same village where it is situated.

## **Cash and Inventory management**

The company has created a separate branch (in its accounts) for its captive on-lending operations to its member MBTs only. The Micro Finance branch of the company takes loan from banks and lends to its member MBTs (at the same rate of interest).

Company purchases cocoons on behalf of the MBT from its cocoon branch with full payment and supply to the MBT. In the company's books, the price of cocoons is advanced to the MBT account. The sales price of cocoon is fixed by the Board of Directors of the company and is based on the silk content of the cocoon. The value of the cocoon is debited as advance to the respective member. The member producer converts cocoon into yarn. Company lifts the entire yarn at perceived market price (lifting price, also decided by the board of the company) from the MBT and pool it together in the company's office. It pays the price of the yarn less the price of the cocoon used to manufacture the yarn. In company's book the price of cocoon used is deducted and adjusted with the cocoon advance account of that particular MBT. MBTs distribute the money among producers on the same basis (price of yarn price less cocoons issued, less other expenses).

## **Finished Goods**

After lifting of yarn, company aggregates, grades, sorts, based on the colour and quality. It also stores and maintains a stock of all the varieties of yarns.

Commercially two types of yarns are extracted from Tasar cocoon namely Spun yarn (coarse) and Reeled yarn (fine). Spun yarn is usually produced (process called spinning) from cocoons already pierced by moth or inferior in quality and not fit for reeling. Reeled yarn is produced (process called reeling) by un-winding the single thread of the whole cocoons (un-pierced) after desiccation of pupa inside.



Reeled Yarn



Spun Yarn

### **2. (iii) Management Information System**

Just after the grading, the centre manager provides all data to computer *Munshi* (a set of trained local youth provide computer services on payment) placed at a centralized location who enters the entire transaction into specially developed computer software. On receipt of the transaction detail, company makes final payment to the producers. The software generates all sorts of MIS and accounts related data for the MBT and its members.

### **2. (iv) Infrastructure**

The company operates from a rented house, which is equipped with office equipments like computers, scanners etc.

At present, the company only has three big cocoon godowns, attached with stifling chamber and drying floor in each. They were created with the financial assistance from Ministry of Rural Development and Central Silk Board. The Company has also taken cooperative buildings on rent, created for the rearers from the same project

### **2. (v) Marketing**

The company has two avenues to market its yarn. Either, it sells yarn directly to the market or to its Joint-Venture (JV) Company (Eco-Tasar Silk Private Limited) which converts yarn into fabrics and sell it. Eco Tasar Silk Private Limited is registered as

Private Limited Company and it is a Joint venture between MPCL (76% stake) and a private entrepreneur (24% stake). It started functioning since October 2007 with an authorized share capital of Rs. 20 lacs with the objective of purchasing Tasar yarns from MPCL, exploring new designs and the promotion of MPCL products as fabric in the market.

## 2. (vi) **Human resource**

The company has at present a work force of 30 staff with varied qualifications and experiences. Each of the important functions like production, finance and marketing are headed by a professional from relevant fields. They are assisted by a pool of supervisory staff and field staff. Each unit is manned by a Production officer, an Account officer and few other support staff.

## 2. (vii) **Financial**

The company started with the paid-up capital of Rs. 1 Lac in the financial year 2005-06 and over the period of three year its equity base increases to Rs. 93 Lacs by the injection of non withdraw-able capital fund and ploughing back of the surplus generated from the business of the company. The company raises debt with different institutions to finance the expanding assets, as on 31<sup>st</sup> March 2008 its debt outstanding was Rs. 403 Lacs. Within two years of operation its ownership base has increased from nil to 2500 women which is organised into 90 MBTs with annual turnover of Rs. 971 Lacs in the financial year 2007-08.

## 3. **Industry**

Percentage of World Raw silk Production by India (M.T)

Country	2002	2003	2004
India	16319	15742	16500
Total World Production	95858	117042	125605
%	17.02	13.45	13.14

(Source : <http://texmin.nic.in/Silk%20Industry.pdf>)

Production of Raw silk (Tasar)

(In tonnes)

Yrs	Tasar
2002-03	284
2003-04	315
2004-05	322
2005-06	308
2006-07	350

(Source: <http://texmin.nic.in/Silk%20Industry.pdf>)

Tasar Production (State wise)

State	AP	Bihar	Chhattisgarh	Jharkhand	MP
2005-06	20	14	90	96	16

State	Maharashtra	Manipur	Orissa	UP	Uttaranchal	West Bengal	Total
2005-06	6	3	21	3	5	34	308

(Source: <http://texmin.nic.in/Silk%20Industry.pdf>)

Imports

(Rs. Crore)

Particulars	2002-03	2003-04	2004-05	2005-06
Raw silk	647.15	628.41	607.21	779.71

(Source: <http://texmin.nic.in/Silk%20Industry.pdf>)

Export

(Rs. Crore)

Particulars	2002-03	2003-04	2004-05	2005-06
Silk Goods	474.08	604.70	640.90	721.53

(Source: <http://texmin.nic.in/Silk%20Industry.pdf>)

There is steady increase in production of Raw silk (Tasar). However, the increasing import of Raw silk and silk fabric at low prices from China since 2001 has adversely affected the domestic markets thereby distracting farmers and other stakeholders from sericulture activities as it has reduced the remunerative gains for seri-culturists and weavers which can be seen from the data provided below

**Prices of the Reeling cocoon & Raw silk**

	2001-02	2002-03	2003-04	2004-05	2005-06	2006-07
Reeling cocoon (Rs/000nos )	500-1650	800-1800	825-1725	863-1300	1010-1210	1000-1300
Raw silk (Rs./kg)	1200-1390	1230-1450	1025-1700	825-1475	1400-1700	1500-1850

(Source: <http://texmin.nic.in/ermiudel/At%20a%20glance.pdf>)

The availability of credit to the rural industry sector was identified as a bottleneck. Also, continued restraints on sale of cocoons worked adversely for this sector. 75% of Seed supply falls in the private sector under license by the state governments. The Government control on licensed seed producers are so poor that they sells untested, un-authorized and un-guaranted seeds to the farmers.

**Demand Supply gap**

The domestic production of Raw silk is not adequate to meet the domestic and export demand. It is estimated that against the demand of around 26000 ton per annum the domestic production is around 17300 tonnes

(Source: <http://texmin.nic.in/Silk%20Industry.pdf>)

**4. Challenges faced by the Company**

Within a very short period, the company established itself strongly in the yarn market inspite of threat from cheaply imported Tasar yarns. But, the problem in this business is that cocoon is available once in a year, one needs to procure and store for the whole year. As a result the business cycle becomes longer.

The company is facing problem in raising business capital (both equity and loan). The company, being a poor women's collective, is not able to invest sufficient equity in the company.

The company has problems on two fronts for its sources of funds which are: -

- Short term nature of the funds
- High cost of capital.

The Total Debt to Total Equity ratio is at higher side i.e. the company is highly leveraged and it keeps showing increasing trend. To maintain a manageable debt-equity ratio, company need to raise its equity. The present equity (own fund) is not enough to leverage required fund.

### **5. Objective of IFMR Trust**

The IFMR Trust intends to connect small & medium enterprises with domestic capital markets and investors such as banks, insurance companies and mutual funds which could greatly increase the funds available to these critical sectors. The small and medium enterprises in India traditionally rose financing via equity or by tapping microfinance institutions at lower rates.

The working capital finance program of the organisation is designed to help SMEs access lower cost capital using their assets as collateral, such as raw materials, finished goods or receivables. Therefore, the partnership is in line with the objective of the organisation and will incentivise the company to scale up and that will help the producer of Tasar to reduce their cost of funding.

### **6. Partnership with IFMR Trust**

Initially, the model is tested in pilot phase in which fund is provided to 13 MBTs having approximately 300 women producers within a pocket in Jharkhand state. The total fund requirements in the pilot phase is estimated to be Rs.75 lacs, which includes Rs.40 lacs for cocoon purchasing by MBTs and Rs.35 lacs for working capital requirement of the company (MPCL).

The entire financing amount of Rs.75 lacs went directly to women producers of MBT which further on-lent 35 lacs to MPCL. The detailed information of the women members (each “Client”) like name, address, occupation, purpose of loan, amount of loan sanctioned and total amount produced was captured in the system. The system also records movement of cash and inventory on a periodic basis.

#### **6. (i) Structure of the Loan**

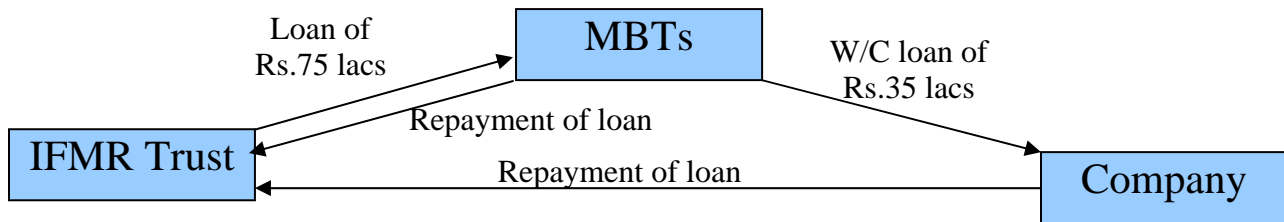
IFMR Trust structured the loan as a “Commodity backed financing product” under which the cocoons are stored in Storage-house managed by the company (MPCL) against the storage-house receipt which certifies the quantity and quality of the commodity being held. The “collateral” consists of the specific storage house receipt and the commodity underlying such storage-house receipt. The loans are to be extended to each woman producer and are secured by the respective collateral.

MPCL is managing the storage of raw material and work in progress and provides the guarantee on the quality, quantity and storage of the collateral to the lender. The Company is also providing the administrative services related to the loan such as disbursement, documentation, data collection, information system, collection and collateral management.

The loans will be pooled into portfolio (“Storage-house receipt loan portfolio”) and be purchased by the IFMR Capital at a mutually agreed price, provided the origination process meets the underwriting guidelines.

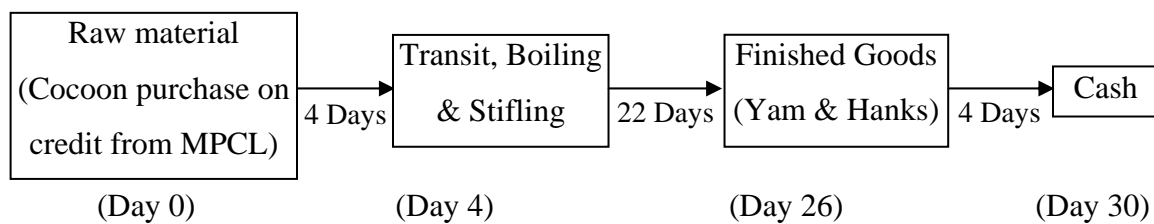
The company already owns the existing storage-houses. However, additional storage-houses will likely be required in the expansion of this programme after the pilot. The company will provide the equity contribution which finances the construction and operation of the storage-houses. Moreover, the company funded the first loss piece of the storage-house receipt loan portfolio.

## 6. (ii) Financing Structure



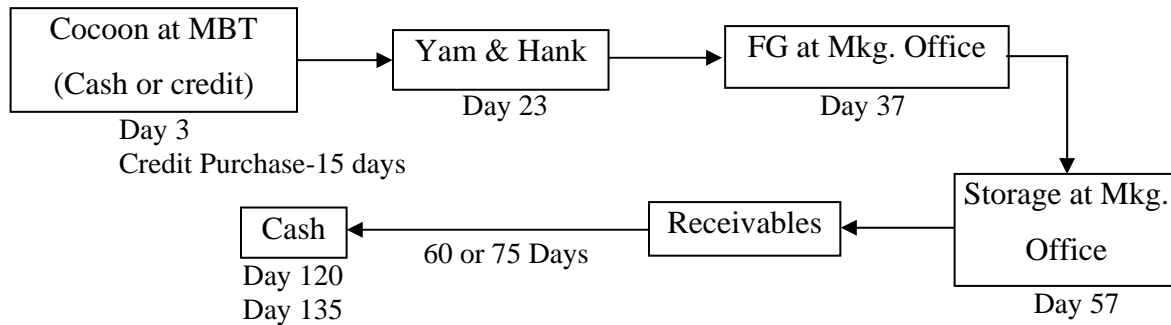
IFMR Trust disbursed the Rs.75 lacs loan directly to the 13 MBTs for cocoon purchasing and working capital requirement of the Company (MPCL). Out of the loan of Rs.75 lacs, Rs.40 lacs are to be utilised for cocoon purchasing by producer members of each MBT. The MBTs will outsource raw material (cocoon) procurement process to company. This loan will be secured by the commodity and the storage-house receipt which will be guaranteed by the company. This will be re-paid via the sale of silk yarn to the company. Rest of the loan amount i.e. Rs.35 lacs is on-lent to the company for its working capital requirement. This will be repaid via the sale of silk yarn by the company to the end buyer. (Details of the transaction structure is in annexure 3)

### Working Capital Cycle (In case of MBT)



In the case of MBT, working capital cycle is of 30 days as women producer purchase Cocoon from MPCL on credit. They return finished goods (Yarn and Hanks) which take 22 days and the realization of cash to women producer normally takes 4 days (Cocoon purchase price is deducted while paying the cash).

### Working Capital Cycle (In case of MPCL)



In case of MPCL, the working capital cycle is of 120 days in case of bulk marketing and 135 days for retail marketing. The credit purchase of raw material is of 15 days whereas realization of receivables takes 60-75 days depends on the bulk sale or retail sale.

The working capital is calculated on the basis of the retail marketing business of the company and it turned out to be approximately 75 lacs. After consideration of the cash flow, company is provided with the 3 months of moratorium period for principal repayment whereas no any such period for MBT.

### 7. Benefits to the Producers, MBTs & the Company

This structure suffices the liquidity need of the MBTs and MPCL. The company has steady availability of working capital financing to scale up its operations which enhance its reach and lead to regular cash inflow to the yarn producers. It is envisaged that the cost of funding can further be reduced by streamlining of processes and operations as it will reduce variable costs, mitigate operational risks and the mainstream capital market investors will be attracted for the funding.

Annexure 1

Balance Sheet Analysis of MPCL

(Amount in 000s)

Particulars	2005-06	2006-07	2007-08
<b>Assets</b>			
<b>Fixed Asset</b>			
Gross Fixed Assets		419.92	1602.10
Depreciation Reserve		48.13	175.00
Net Fixed Asset		371.79	1427.11
Non Current Asset			
Investments		2500.00	2520.00
Loans & Advances		0.00	28.89
Staff loans & advances		479.29	620.13
Other Non Current Asset		1666.30	1631.42
Total Non Current Asset	0	5017.38	6227.55
<b>Current Asset</b>			
Stocks		23328.55	27256.69
Cash & BB	99.93	36.33	0.00
Sundry Debtors (Up to 6 month)		7848.89	10787.75
Deposits		3494.76	4857.32
other current asset		638.73	412.02
Advances to Groups		6048.05	11186.82
<b>Total Current Asset</b>	99.93	41395.31	54500.60
<b>Total Asset</b>	99.93	46412.7	60728.15
<b>Liability &amp; Stockholder's Equity</b>			
<b>Current liabilities</b>			
ICICI Working Capital		15000.00	7051.36
Creditors		1229.40	8889.87
Other Current Liability & provisions	5.63	611.31	2142.94
<b>Total Current Liability</b>	5.63	16840.72	18084.17
<b>Non Current Liability</b>			
Unsecured Loan		14453.35	33311.93
Due to Prada		6805.09	0.00
Non Current Liability	0	21258.44	33311.93
<b>Total Liability</b>	5.63	38099.16	51396.10

<b>Equity</b>			
Subscribe & Paid up Capital	100	100.00	100.00
Share Application Money		0.00	4900.00
Reserve & Surplus			
Non Withdrawable Capital Fund		5098.71	1101.37
Non Eroding Corpus		3000.00	3000.00
Reserve & Surplus	-5.70	104.00	209.01
Total Equity	94.305	8302.714	9310.376
Deferred Tax Liability		10.83	21.67
<b>Tangible Net Worth</b>	94.31	8313.54	9332.05
<b>Total Liability &amp; Stockholder's Equity</b>	99.93	46412.70	60728.15

## P&amp;L A/c Analysis of MPCL

(Amount in 000s)

	2005-06	2006-07	2007-08
Sales	0	74,084.82	97,178.83
Interest received	0	50.38	71.43
Sundry Income	0	120.42	2,176.98
Income from MF	0		1.38
			31.17238001
<b>Total Revenue</b>	<b>0</b>	<b>74,255.62</b>	<b>99,428.61</b>
Revenue Growth (%)			25.32
COGS	0	63,787.32	87,189.74
<b>Gross Profit</b>	<b>0</b>	<b>10,468.31</b>	<b>12,238.87</b>
Operating Expenses		2,577.10	3,574.88
Selling, adm. & other expenses	-5.695	4,138.57	5,230.99
<b>PBDIT</b>	<b>-5.695</b>	<b>3,752.64</b>	<b>3,433.01</b>
Depreciation	0	48.13	126.87
<b>PBIT</b>	<b>-5.695</b>	<b>3,704.52</b>	<b>3,306.13</b>
Interest Expense	0	1,343.14	2,249.15
<b>PBT</b>	<b>-5.695</b>	<b>2,361.38</b>	<b>1,056.98</b>
Taxes	0	116.45	85
<b>PAT</b>	<b>-5.695</b>	<b>2,244.93</b>	<b>971.98</b>

## Transaction Structure

Facility	Secured Loan facility for the working capital financing  The facility will consist of working capital finance loans to each Mutual Benefiting Trust (the “MBT Loan”)
Initial Nominal Amount	INR 75,00,000
Borrower	Each of 13 Mutual Benefiting Trusts located in the region of Jharkhand
Servicer	Masuta Producers Company Limited
Lender	IFMR Trust
Date of Execution	15 <sup>th</sup> January 2009
Maturity Date	12 Months from settlement date
Rate of Interest	14 % on outstanding nominal amount
Repayment Frequency	Monthly
Moratorium Period	3 Month on Principal repayment of MPCL for its working capital requirement
Security	The loan will be secured by a first ranking security over all the assets of the borrower and servicer
Credit Enhancement	The Servicer will provide a FLDG of up to 15 % of the outstanding nominal amount on any date

### Projected Advance to MBTS

<b>Years: 2009-10</b>	Apr	May	June	July	Aug	Sept	Oct	Nov	Dec	Jan	Feb	Mar	Total
<b>Opening Balance</b>	128.00												
Loan Disbursed during the Year	49.95	49.95	49.95	49.95	49.95	49.95	0.00	0.00	49.95	49.95	49.95	0.00	449.53
Loan Recovered during the Year	49.95	49.95	49.95	49.95	49.95	49.95	0.00	0.00	49.95	49.95	49.95	0.00	449.53
Closing Balance	128.00	128.00	128.00	128.00	128.00	128.00	128.00	128.00	128.00	128.00	128.00	128.00	
<b>Years: 2010-11</b>													
<b>Opening Balance</b>	128.00												
Loan Disbursed during the Year	82.64	82.64	82.64	82.64	82.64	82.64	0.00	0.00	82.64	82.64	0.00	0.00	743.75
Loan Recovered during the Year	82.64	82.64	82.64	82.64	82.64	82.64	0.00	0.00	82.64	82.64	0.00	0.00	743.75
Closing Balance	128.00	128.00	128.00	128.00	128.00	128.00	128.00	128.00	128.00	128.00	128.00	128.00	
<b>Years: 2011-12</b>													
<b>Opening Balance</b>	128.00												
Loan Disbursed during the Year	131.74	131.74	131.74	131.74	131.74	131.74	0.00	0.00	131.74	131.74	0.00	0.00	1185.63
Loan Recovered during the Year	131.74	131.74	131.74	131.74	131.74	131.74	0.00	0.00	131.74	131.74	0.00	0.00	1185.63
Closing Balance	128.00	128.00	128.00	128.00	128.00	128.00	128.00	128.00	128.00	128.00	128.00	128.00	