CASE CODE 13

SCOOTERS INDIA LIMITED (A)

Towards end of January 1986, Shri P.S. Kapoor, the Chief Executive of Scooters India Ltd. (SIL) was wondering what action plan he should draw to bring back SIL on the rails. The company's losses were soaring. Though the company never made profits `ever since its inception, of late the performance had been deteriorating fast and company was incurring huge losses. (see exhibits 1 & 2).

History of the Company

In view of increasing demand and supply gap in the 2 wheeler scooter industry of the country, the Government of India decided in principle, around October 1962, to set up a public sector unit for manufacture of scooters with indigenous know how and without involving any foreign collaboration. However, owing to non-availability of indigenously developed design and mass production technology for the planned level of production of one lakh scooters annually, not much progress was made in this direction. Tenders were invited in 1970 from foreign parties for collaboration in the proposed project. Out of the two offers received, the offer of M/s Piaggio of Italy was considered serious and worthwhile.

In the meantime, while considering the applications of M/S Automobile Product of India Ltd. (API) for expansion of their manufacturing facilities with an additional capacity of 100,000 Lambratta 2 wheeler scooters annually by importing the manufacturing facilities of M/s Innocenti S. G. Milano, Italy, their erstwhile collaborators, and also for manufacture of 24,000 3 wheelers, the Government of India decided in July 1971 to accelerate the setting up of the public sector unit. Accordingly, discussions were held with API and Innocenti to explore the possibility of jointly implementing the scheme submitted by API. It was agreed in September 1971 to set up a joint sector company for manufacturing 100,000 two wheelers, with Government of India holding *51%* and API and Innocenti together holding 49% of equity capital of the new company.

As a sequel to the negotiations, an inspecting team of technical and financial experts of the Government of India and API was deputed to Italy in October 1971 to determine the life and condition of the plant offered by Innocenti, the reasonable price of the equipment, and also additional machinery that may be needed for replacement, adjustment and balancing the facilities, to achieve the level of production of 1,00,000 scooters annually. The services of an independent appraiser in London were also sought.

The. plant and equipment was being offered by Innocenti on "as is where is" basis. The plant was out of operation for two years as the factory was closed due to serious labour troubles. Most of the machines were old, over 70% of them being older than 10 years. The company Innocenti had also agreed to offer basic manufacturing drawings whatever available but nothing more in terms of "know-how".

Prepared by Prof. Krishna Kumar and Dr. Arun Sahay of Scooters India Ltd.

The report of the independent appraiser and the inspecting team said:

(i) The equipment offered was in reasonably good condition and on an average the economic life of the plant and machinery offered would extend to have production of 5 lakh scooters, equivalent to around 7-8 years of production.

(ii) While life of special purpose machines was over 8 years, that of general purpose machine was 4 years and above.

(iii) The total price of 3 million demanded by Innocenti was reasonable.

(iv) The production capacity of the individual equipment and tooling for particular operations (classified under good condition) was [1]suitable for production of more than 1,00,000 scooters per annum, however, the direct production shop would require balancing equipment of Rs.95.90 lakhs. Besides, various supporting facilities of Rs. 126 lakhs considered essential for the commencement of production were not included in the offer.

(v) Considering the technological involvement, the ultimate cost of production, and the aspect of a quality product, a provision was required to be made for shell moulding foundry along with forge and heat treatment shops estimated to cost about Rs. 66 lakhs.

(vi) Shifting of equipment to India would cost about US $0.5 million upto the port of embarkation and Rs. 9 million thereafter

TABLE-1

	ITEM	PLANT WITH ENTIRELY NEW EQUIPMENT OFFERED BY PIAGGIO	PLANT OFFERED BY INNOCENT
	For 100,000 per Annum		
1.	Total Fixed assets	Rs. 15.91 Cr.	Rs. 10.90.
2.	Foreign Exchange Element (Included in total fixed investment)	6.56	2.90
3.	Working Capital Requirements	5.00	5.00
4.	Production cost Scooter	Rs. 2022	Rs. 1989
5	Ex-Factory price at assumed level of 12.5% gross return on total fixed investment	Rs. 2321	Rs. 2225

The alternative offer of Piaggio with entirely new plant and equipment compared as shown in -table 1 above.

In view of the positive report of the experts the government approved the purchase of "Innocenti" including auxiliaries on the following considerations.

(a) Lower total fixed investment, foreign exchange involved and production cost compared to and entirely new plant.

(b) Generation of additional resources of about Rs. 4.80 cr. on the sale of 5,00,000 scooters in a period of 7-8 years, when the equipment by Innocenti would, on the average, have reached the end of its economic life. This would enable greater flexibility in replacement programme, phased modernisation, faster expansion and diversification.

(c) Profit of about Rs. 2 crores on the commencement of production by two years ahead with the old plant of Innocenti.

(d) Saving in foreign exchange as payment was to be made after adjustment of $0.40 million towards the equity of the company and the balance of $1.6m was payable out of export earnings over a period of 7 years, the first payment starting after a period of 2 years.

An agreement for the collaboration on above lines was signed on 16th June 1972 between the Government of India, API Innocenti and Innocenti Lambretta sPa (which had since taken over the scooters operations of Innocenti). To give effect to this agreement, Scooters India Ltd. (SIL) was incorporated on 7th September 1972 as a company under Companies Act, 1956.

While finalising the agreement, however, a serious snag cropped up. In respect of the payments to be spread over 7 years (expected to come out of exports), the vendors (Innocenti) insisted upon a guarantee which could be discounted in Italy. As no bank in Italy was willing to discount a guarantee payable over a period of 7 years, the vendors agreed to accept a cash payment of Rs. 1.45 million in lieu of payment of Rs.1.703 m (spread over 7 years). The amount of $1.6 m had increased to $1.703 m during the period due to devaluation of the dollar. The cash payment was approved by the Government of India on 15th March 1972.

Sometime in middle of 1972, Innocenti went into voluntary liquidation. No s aces, therefore, could be issued to the vendors (for $0.4 m). The vend rs, however, agreed for a cash payment of $0.2 m. in lieu of share equivalent of $0.4 m in order to compensate the company for delay on their part in supplying certain technical and other documents. Government of India agreed to contribute Innocenti's part of the share capital.

Mr. Soundararajan, Senior IA & AS Officer, was appointed as the first Chairman & Managing Director of the company. Prior to joining SIL, Mr. Soundararajan had a tenure in Garden Reach workship at Calcutta as Managing Director. He also brought with him Mr. Gangopadhyaya as Chief Engineer to look after the civil work.

The API was requested by the Government of India to prepare Detailed Project Report (DPR). The company submitted 2 out of 12 volumes of DPR by end of 1972. The terms and conditions were not settled in advance. While submitting the DPRs, API claimed a fee of Rs. 40 lakhs which was subsequently reduced to Rs. 30 lakhs. The Government, however, informed API that cost of preparing DPR was a matter for SIL to decide. The company felt that the information and data contained in DPR though useful for setting up the manufacture of scooters, could not be considered complete owing to non-inclusion of information of certain aspects e.g.:

(i) manufacture of J. Series scooters
(ii) detailed layouts of machine tools in the main plant and layout of ' services and
(iii) ordering for balancing equipment and machine tools.

API agreed to carry out modifications etc. in DPR. It was also agreed that a sum of Rs. 15 lakhs would be paid to API for this 'orlc in three equal instalments. While two instalments were paid, the last one was not released as certain items of work were not completed by API. API filed a suit in August 1976 for payment of last instalment which is still pending in court.

Proposal for the Three Wheeler Project

In January 1973 a proposal was made by Innocenti for sale of world rights to manufacture three wheeler Lambros, technical documentation and the plant and equipment having a capacity to manufacture 30,000 Labros per annum. SIL approached the Government of India in January 1973 for approval to extend its manufacturing activities to cover manufacture of 30,000 three wheelers, and purchase from Innocenti the technical documentation, equipment, tooling etc., at a cost not exceeding 185 m lire (Rs. 25 lakhs), on the following considerations.

(a) Likely popularity of the three wheelers as a light'transport vehicle with a pay load of 600 kgms.
(b) Greater export potential to developed countries in Europe.
(c) Considerable economies in the initial investment and reduction in the cost of production by integrating the three wheeler and two wheeler production.
(d) Attractive price of the technical documentation and equipment.
(e) Minimum additional investment for the three wheeler by resorting to more intensive use of the plant and equipment available for the two wheeler production.
(f) The additional investment of Rs. 47 lakhs would result in the plant being able to add a product line valued at about Rs. 16.5 crores and additional profit of Rs. 1.50 crores per annum.

The above proposal was agreed to by the Government of India subject to following conditions;

(i) The cost of plant and/ machinery including documentation and world rights not to exceed Rs. 25 lakhs (185 million lire):
(ii) The capital cost of setting up the plant would be approx. Rs.72 lakhs including foreign exchange element of Rs. 35 lakhs:
(iii) Profitability of the integrated scooter project to be re-calculated and DPR already prepared to be.suitably modified and submitted to the Government for approval.

Withdrawal by API

In January 1973 the API was requested to bring its contribution of share capital. However, in July 1973 API declined to-do so on the grounds that the company had (i) not accepted API as technical collaborators (ii) decided to take over the-three wheeler project which was to be taken up ,by API in terms of an understanding between API and Government of India.

The Managing Director of the Company stated to Committee on Public Undertakings (COPU) in 1983 that:

"API had been having certain discussions with the Government where they had proposed that they should be entrusted with the task of preparation of DPR and should also become technical consultants of SIL. The Government mentioned to them that this was a matter to be decided by the company. The company felt that the technical consultancy was not essential because the type of consultancy which they were prepared to give was on general aspects of the company and not on the technical details of the components and other things. This was too high a price to pay. We told them we did not require this type of consultancy. API had planned that the money they would get on technical consultancy from SIL they will invest back in equity. Since they were not getting this money from SIL, they refused to participate in the equity".

The Secretary, Department of Heavy Industry added.

"The API could not be engaged as a consultant because it is not that any body who is manufacturing something is knowledgeable enough about the design of products. The most important thing which a collaborator should provide us is know-why of the product and not know-how. This know-why was not available with API".

A Senior executive of the company, however, said:

"The API was really pulled down, the Chief Executive thought he could do every thing himself and therefore no external help was required".

Project Costs

The capital investment plan involving an expenditure of I . 12,crores for two and three wheeler pro e t was prepared by the company and sent to the Government of India in March 1973 for approval. The ‘approval of the Government to the said plan was accorded for Rs. 11.90 crores in 1974.

The estimates were further revised by the company to Rs. 12.7 crores in November 1974 which too was approved by the government in September 1975. A further sum of Rs. 75 lakhs was sanctioned by the Govt. on April 1976 for the Foundry Projects; thereby increasing the estimates to Rs. 13.45 crores. As against the total sanctioned estimates of Rs. 13.45 crores an expenditure of Rs. 19.48 crores (approx.) was incurred on the project upto March 1980 as per the details given in exhibit 3. The excess of expenditure over Rs.13.45 crores was primarily owing to the expenditure on acquisition of 'Fans unit (Rs. 54.78 lakhs) of the Ganesh Flour Mills (Delhi) and supporting facilities in tool regrinding and inspection area (Rs. 104.50 lakhs) renewal and replacement programme (Rs. 460.02 lakhs) and certain cost overruns in building, import of machinery from Innocenti, furniture/fixtures etc. It may be noted that the above included an amount of Rs. 309 lakhs incurred upto March 1980 on an unapproved power pack project, subsequently treated as an expenditure on supporting tool/inspection area facilities and renewal/replacement of machinery.

The company also invested in two subsidiary companies promoted by it, namely U.P. Instruments Ltd. (Rs. 15.68 lakhs) and U.P. Tyres and Tubes Ltd. (Rs. 52.28 lakhs) to ensure supply of instrumentation panels, and tyres and tubes at local levels instead of long lead time procurements from other states.

Funding of the Project

The financing of the project was through equity capital and loans from government and other agencies. The company was registered with an authorised capital of Rs. 5.5 crores (55,00,000 shares of Rs. 10 each), which was raised to Rs. 8 crores in 1976. The paid up capital as on March 1982 was as under:

Shareholder	No.of shares (Lakhs)	Value of shares (Rs. in Lakhs)	% of share holding
1. Govt. of India	32.60	326.00	62.1

2. Financial Institution	10.90	109.02	20.8
3. General Public	8.96	89.63	17.1
Total	**52.46**	**524.65**	**100.0**

Rest of the financing of assets has been through loans from the Government of India and financial Institutions (LIC, IDBI etc.) and a commercial bank (exhibit-4)The Government have a moratorium of 2-3 years for the payment of principal as well as interest. The company, however, had not been able to pay the principal as well as interest. The perennial loss position of the company was reflected in a continuous cash crisis in the company and it had to borrow constantly an increasing amount to sustain the operation which default in payment of principal as well as interest occasionally resulted even in defaulting in timely payment to suppliers.

Questions

(a) Critically examine the factors responsible for the company's poor performance
(b) What action plan do you suggest to bring the company out from the position it is in?

EXHIBIT-1
COMARATIVE PROFIT AND LOSS ACCOUNT OF THE COMPANY

(Rupees in lakhs)

	1979-80	1980-81	1981-82	1982-83	1983-84	1984-85
Income						
Sale of Products	2257.75	2778.01	2850.78	2793.11	2620.73	2780.22
Other Sales	31.92	41.41	56.34	65.65	36.98	48.05
Miscellaneous	131.09	79.84	61.22	75.19	184.77	75.16
Income Increase in stock	93.06	50.06	(19.46)	546.95	(285.68)	(119.64)
Total	2513.81	2949.23	2948.86	3480.90	2556.80	2783.79
Expenditure						
Raw Material Consumed	1303.14	1424.26	1498.72	1758.12	1273.07	1487.78
Purchase for Service Stations	18.55	20.14	27.11	29.22	31.70	36.36
Factory Expenses	240.00	277.43	302.10	355.72	332.82	270.38
Employee Remuneration & Welfare Expenses	349.65	468.49	519.82	565.37	651.55	684.94
Administrative Expenses	47.27	54.05	53.26	55.30	58.51	53.64
Selling & Distribution Expenses	384.63	487.85	481.96	524.06	347.36	509.79
Reserve for doubtful debts/advances	--	1.52	12.75	.36	1.32	21.23
Reserve for Inventory Obsolescence	--	4.77	29.57	--	.20	.30
Assets Written Off*	5.63	35.18	23.36	39.87	42.06	40.12
Depreciation	137.51	133.60	139.38	154.69	163.99	151.51
Interest	402.51	503.88	619.94	698.66	831.91	936.09
Total	2933.88	3410.67	3707.37	4181.37	3734.49	4192.14
Loss of the year	(420.06)	(461.33)	(758.51)	(700.47)	(1177.69)	(1408.35)
Adjustment for Prior Periods (Net Debit)	(25.35)	(28.69)	(9.56)	(9.63)	(44.57)	(2821)
Net loss of the Year	(445.42)	(490.05)	(768.06)	(710.10)	(1222.26)	(1436.56)
Loss brought forward from previous year	(1532.32)	(1977.74)	(2467.76)	(3235.52)	(3945.95)	(5168.21)
Balance of loss carried over to balance sheet	(1977)	(2467.76)	(3235.82)	(3945.95)	(5168.21)	(6604.77)

- Includes preliminary expenses, deferred revenue expenditure off bank charges.

Note: Company annual reports figures format to conform to same format of presentation.

EXHIBIT- 2
SALES/PRODUCTION PERFORMANCE OF SIL

Particular	Licenced Capacity	Installed Capacity	1984-85	1983-84	1982-83	1981-82	1980-81	1979-80	1978-79
2 Wheeler	1,00,000	60,000	27722 (284559)	22619 (29328)	36756 (29419)	31769 (31003)	35502 (35715	33304 (33635)	23027 (23523)
2 wheeler Power Packs		20,000	17	3456	10981	10278	12540	12079	15773
3 Wheeler Vikram	30,000	2,500	950	788	385	711	532	284	102
3 Wheeler Power Packs	- -	1 (1)	- -	1 -	23 (23)	10 (10)	- -	373 (373)	
* Vinai Moped Ganesh Fans	50,000 75,000	- 60,000	- 37259 (37020)	- 37679 (39995)	10 - (38482)	- 45685 (44490)	- 41107 (40114)	- 32890 (32044)	15 29707 (30896)

* Never manufactured

Note: Figures in bracket indicate turnover or sales

DE-RATION OF PLANT CAPACITY

Particular	Licenced Capacity	Installed Capacity	1984-85	1983-84	1982-83	1981-82	1980-81	1979-80	1978-79
2 Wheeler	1,00,000	-	60000	** 60000	60000	80000	80000	80000	80000
2 wheeler Power Packs	-	10,000	20000	20000	20000	-	-	-	-
3 Wheeler	30,000	7,500	2500	2500	2500	60000	60000	60000	60000
3 Wheeler Power Packs	-	-	-	-	-	-	-	-	-
* Moped Vinai Ganesh Fans	50,00 75,000	- -	- 60000	- 60000	- 60000	- 60000	- 60000	- 60000	- 60000

*Never Manufactured

** Includes 20,000 Mopeds

EXHIBIT-3
BREAK-UP OF THE PROJECT COST

	Item of expenditure	Cost as per Capita investment plan	Original cost as approved by Govt. in March 74-June76	Revised Cost approved (Sept.75&June 76)	Actual expenditure incurred upto 31.3.1980	31.3.1982
	1	2	3	4	5	6
1.	Land and land development including bountry walls, outside drainage and roads	27.00	27.00	29.60	18.10	18.10
2.	Main factory building storage shed, mezzanine floor for office, drainage, water supply and horticulture	223.00	223.00	281.13	339.97	348.82
	(Including electric installati a mounting to Rs. 101.25 Lakhs)					
3.	Machinery imported from Innocenti for the two wheeler plant including freight, customs duty etc.	289.00	289.00	354.75	402.80	402.80
				354.75	402.80	402.80
4.	Mechinery imported from Innocenti for the three wheeler plant including freight, customs duty etc.	50.50	50.50			
5.	Balancing machinery for the two wheeler and three wheeler plant	350.00	350.00	391.02	339.15	402.48
6.	Installation cost of capital repairs to plant and mechenery obtained from Innocenti prior to their installation.	30.00	30.00	35.00		
7.	Furniture, fixture, office equipments and vehicle.	35.00	35.00	35.00	44.15	48.16
8.	Pre-production expenses to be treated as deferred revenue	75.00	75.00	100.00	106.00	106.00

	expenditure					
9.	Installation of diesel generating set for total power 3000 KVA.	40.00	40.00	35.50	20.95	20.95
10.	Residential coloney for staff	70.00	60.00	--	--	--
11.	Development of land and other municipal fecilities for work men's coloney	10.00	10.00	10.00	1.12	1.12
12.	Foundry project approved by Govt. in April 1976	--	--	75.00	54.78	60.77
13.	Fan unit, ancillary estate and tools and equipment for retail outlet managers (not completed in the Capital Investment plan)	--	--	--	55.92	87.54
14.	Supporting fecilities in tools room, tooll regrinding and inspenction areas (Rs. 104.50 Lakhs) and renewal and replacement programme (Rs. 460.02 lakhs)		--	--	564.92	690.40
		1190.50 or Say 1200.00	1189.93	1345.00	1947.86	

EXHIBIT- 4
PROJECT FINANCING

	1974-75	**1975-76**	**1976-77**	**1977-78**	**1979-80**	**1980-81**	**1981-82**	**1982-83**	**1983-84**	**1984-85**
Sources of Founds										
a) Paid Up Capital					513.71	524.82	524.82	524.82	656.13	706.13
b) Reserves & Surplus					1.83	6.72	6.72	6.72	6.72	6.72
c) Loans i) Secured ii) Unsecured					 1008.48 2619.85	 1022.67 3024.88	 1120.43 3816.38	 1317.27 4540.28	 1535.38 5453.80	 1528.29 5453.81
d) Deferred payments and other current liabilities					827.72	915.14	1010.86	1471.89	1173.09	1062.62
Total					**4971.59**	**5494.23**	**6590.22**	**7886.00**	**8825.14**	**9954.86**
Application of funds										
a) Net fixed Assets					1243.81	1300.78	1223.97	1176.79	1148.23	1078.24
b) Investments					25.00	30.01	30.01	35.51	58.99	60.01
c) Current Assets					1557.42	1530.68	1855.20	2619.63	2317.14	2170.33
d) Misc expenditure (Not written off)					2.28	2.25	1.94	1.68	1.32	0.97
e) Profit & Loss A/C					1917.73	2407.35	3175.45	3886.00	5168.82	6549.15
Total					**4971.59**	**5494.23**	**6579.22**	**7886.00**	**8825.14**	**9954.86**

EXHIBIT-5

DETAILS OF LOANS AND ADVANCES OF THE COMPANY

(Rs. in Lakhs.)

		1979-80	1980-81	1981-82	1982-83	1983-84	1984-85
1)	Debentures	50.00	50.00	50.00	50.00	50.00	50.00
2)	Second loans and Advances						
	a) IDBI	143.00	143.00	143.00	143.00	143.00	143.00
	b) IFCI	50.00	50.00	50.00	50.00	50.00	50.00
	c) SBI	486.78	475.25	512.33	633.48	700.40	683.08
	d) IDB	186.80	167.04	190.13	212.07	311.88	281.76
	e) Interest accrued and due but not paid	91.89	137.39	174.75	228.51	279.90	320.78
	Total	**1008.48**	**1022.67**	**1120.21**	**1317.05**	**1535.67**	**1506.84**
3)	Unsecured loans						
	a) Long term Loans from Govt. of India	1783.26	1923.26	2234.16	1565.04	2933.74	3433.74
	b) Long Term Loans from IDBI	39.90	53.80	53.80	53.80	53.80	53.80
	c) Long Term Loan from HUDCO	--	11.59	37.59	42.81	39.11	35.15
	d) S.T. Loans from Govt. of India	87.01	87.01	87.01	87.01	87.01	87.01
	e) S.T. Loans from IDBI	187.51	161.88	260.45	259.54	160.45	157.57
	f) S.R. Bridging Loans	1.90	0.71	0.22	0.22	0.22	0.22
	g) S.T. Loans from UPSIDC	17.90	15.40	15.40	13.40	13.40	13.40
	h) Int. Accrued & due but not Paid	506.36	771.23	1127.96	1518.68	2166.29	2767.86
	Total	**2619.85**	**3024.89**	**3831.68**	**4540.50**	**5454.02**	**6650.76**
	Grand Total	**3628.33**	**4047.56**	**4951.89**	**5859.55**	**6989.69**	**8157.60**