Dimensions of Development Banking
Finance is a vital element for any economic activity. It not only facilitates the start of the process of economic growth and development but also provides endurance and strength for its continuity. When finance becomes available to the prospective entrepreneurs, industrial development is initiated giving rise to new investment opportunities in the economy. The participation of new members as entrepreneurs in manufacturing or other economic activities may, however, be influenced by the availability of funds out of their own accumulation or some outside sources. Among outside sources, the most significant role is played by the specialised financial institutions or development banks established for the purpose.¹

2.1 Need for Development Banks

India has a fairly developed industrial structure even before Independence, but the existence of peculiar circumstances led to the concentration of its control by a few industrial houses originating from a small group of the society. They controlled banking, insurance and investment companies, the input supplying sources together with the network of manufacturing activities. Largely due to lack of

resources, knowledge and experience of running a business enterprise, or lack of risk bearing capacity or a combination of all the above factors, other entrepreneurs could not come forward to establish new ventures. There was utter lack of encouragement from the government as well as from the traditional financial intermediaries.

The existing financial arrangements were incapable of coping with the burgeoning financial requirements of upcoming enterprises. Although the country had a network of strong and developed commercial banks, these institutions, working on the British banking model, confined themselves to short-term financial activity and abstained from supplying long-term financial assistance. This resulted in new entrepreneurs finding it difficult to establish contact and obtain long-term credit from commercial banks. The commercial banks in India, before nationalisation in 1969, were under the control of one or the other of a few big industrial houses. Even after nationalization, every bank more or less continued with the past trend of patronisation of business houses, who were erstwhile controllers. The managing agency houses which had served as important adjuncts to the capital market were not able to cope with the requirements of the planned industrial development owing to their apathy to investment in risky ventures and their keenness to finance only interested
concerns. Furthermore, several malpractices such as the misuse of funds, excess speculation and manipulations, the high cost of promotion and financial and marginal managerial concentration were often detrimental to the interests of the investing public. There was, moreover, a dearth of issue houses and underwriting firms which sponsor security issues. As against the limited arrangement for the supply of long-term financial facilities, there was an enormous increase in the demand for long-term capital. Not only did existing industries require substantially large amounts of capital to meet their reconstruction, modernization, expansion and diversification programmes, the establishment of new industrial projects on a gigantic scale in the capital goods sector for the building of a strong and balanced structure of industrial development also called for enormous investment. But only a very small part of the total requirements could be met by the existing financial institutions and for the remaining, it became necessary to devise institutional machinery with sample financial resources and with relatively more comprehensive functions. In order to fill the gaps between demand for and supply of financial resources in the field of industrial finance and to foster economic development, ever since the attainment of Independence, several specialised financial institutions or development banks have been established in India either by
the government itself or under/with it's guidance/assistance.

The need for development banks is not only evident for developing economies like India where the capital market itself is in a rudimentary stage but also in developed countries where there are credit gaps with respect to certain specialised needs. One might refer here to the well known MacMillan gap in the UK, where specific attention was drawn (in the thirties) to the credit needs of medium term finance for industry and term finance for small and medium sized industries.

2.2 Concept of Development Bank

It is an extremely difficult task to define development bank. This is so because of the tremendous diversity in their forms and often the scarce similarity in their functions. There is no universal model to which development banks conform. Development banks are structured in every country in consonance with the existing political, social and economic climate. That is why the writers on development banking have emphasised on different dimensions as the function of development banks.

In his early work, Diamond defined "development bank as an institution to promote and finance enterprises in
the private sector". This shows that development banks do not simply finance development projects, but also provide related supportive services. Boskey somehow provided a broader view of the development banks. She defined development banks as 'institutions, public or private, which have as one of their principal functions, the making of medium and long-term investments in industrial projects'. This definition includes all institutions sponsored and managed by government as well as private groups. It also covers financing of all types of industrial projects whether in private sector or public sector or for that matter, even in joint sector.

Kane defined development bank as "a financial intermediary supplying medium and long-term funds to bankable economic development projects and providing related services". This definition also includes 'other related services' besides the provision of long and medium term funds as the functions of development banks. Development banks have been established to supplement the existing sources of industrial finance. They are expected not to compete with the normal channels of finance, rather their

role is that of gap fillers.⁵ These banks are intended to help stimulate the emergence of missing ingredients so essential for economic development. Houk emphasises that a development bank should perform both functions, i.e., banking and development.⁶ As a banker, development banks are intended to finance those projects which are bankable and a project is bankable if it is in the nature of profitably self-financing.

A financing institution which restricts its activities only to the banking functions should not be called a development bank. Therefore, it will have to attempt in addition to its banking functions, certain problems or bottlenecks to development, the magnitude and importance of which may vary from country to country.⁷ For development, it should attempt to foster the capital market, take initiative in the choice of viable projects, develop underdeveloped areas, and enlarge the entrepreneurial base by attracting new entrepreneurial talent.⁸

7. Ibid., pp.3-6.
Thus, the development banks, by and large are those institutions which provide medium and long term finances for productive investment and arrive at decisions with respect to such investments, not on the basis of security that can be offered by the client but on the criterion of a long-range economic viability of the enterprise being financed. While other factors might also be perceived to be missing (such as management and entrepreneurship), term capital was seen as the crucial one and providing it was necessary to attract and give effect to others.9

2.3 Features of Development Banks

The Development Banks (DBs) as distinguished from Commercial Banks (CBs) and other financial institutions have some unique features of their own. Some of the important features are given henceforth.

2.3.1 DEVELOPMENT OUTLOOK AND NON-ENCLEVISIST APPROACH

In contrast to 'patronage psychology', a hallmark of routine banking transactions, the Development Banks are marked by "Development outlook". According to H.T. Barekh10


"Development Banks should have the spirit of development finance". Development finance implies real investment in fixed assets and cannot be divorced from the concept of the development. Operationally, it signifies that development banks should not fall prey to encrusted approach or class orientation.

2.3.2 DEVELOPMENT PRIORITIES

The development banks are opposed to the 'let the clients approach' - again a benchmark of commercial banks. In other words, finance and other services are made available to only those projects which ensure priority test, commercial viability and technical feasibility. It implies that adequate funds should be provided to desirable projects in consonance with the objectives of national policy and planning.

2.3.3 DEVELOPMENT STRATEGY

Apart from development outlook, the development banks are also expected to adopt and implement 'Development Strategy'. Diamond says "Development Strategy implies a level of knowledge of wider opportunities, an entrepreneurial capacity and a systematic overview of

alternatives which development banks can have and a role for development banks which goes far beyond the realities. I prefer the more modest characterisation of this process as directing the development banks' efforts towards new opportunities for investment and for services which are both profitable and economically sound.13

2.3.4 SOCIAL PROFIT ORIENTATION

In contrast to commercial profit (CP) maximization, an objective of the commercial financial institutions, the development banks are pre-eminently concerned with the optimisation of social profits (SP). While commercial profit is quantifiable and has monetary connotations, the social profit may defy both. Moreover, while commercial profit tends to be concentrated in the hands of the rich, social profit is designed to be diversified widely among the rank and file of a social unit. Further, an activity resulting in negative capital profit may lack operational feasibility, while an activity ending with negative social profits would be devoid of theoretical justification.14


2.3.5 ENTERPRISE CREATION AND PROMOTION

Another point on which development banks stand apart from other financial institutions is their role pertaining to creation, widening and promotion of enterprise including grooming for entrepreneurial responsibilities.\textsuperscript{15}

2.3.6 ACTIVE ENGINES OF DEVELOPMENT

The development banks looked upon not only as engines of development, but also as a growth sector in themselves. It has been observed that development banks need not be passive instruments of economic activity. With dynamic management and an adequately permissive environment of available opportunities and of favourable policies, they can be active engines of development as they have been in the past.\textsuperscript{16}

2.3.7 DECENTRALISED, DIVERSIFIED AND DIFFUSED GROWTH

Development banks have been entrusted with a very vital responsibility of promoting balanced regional growth. In India, this role has been emphasised unequivocally by the Planning Commission in the statement that "the pattern of investment must be so devised as to lead to balanced regional development".\textsuperscript{17} In the words of Simha, "balanced

\textsuperscript{15} Madan, \textit{DFIs in Asia and the Pacific}, p.2.


\textsuperscript{17} Planning Commission, \textit{Second Five Year Plan}, (New Delhi, Government of India, 1956), p.3.
regional development and encouragement to small and new entrepreneurs are now almost universally considered to be essential aspects of the functioning of a development bank.18

2.3.8 ENHANCING PRODUCTIVITY OF INVESTMENT

Development banks are enjoined not only to supply adequate investible funds but also to encourage the productivity of investment already made. This can be achieved through technological progress, managerial efficiency and increased capital stock. In underdeveloped countries, where these are in relatively short supply, development banks can be used to provide some of them.

2.3.9 TECHNOLOGICAL UPGRADEATION

It is a recognised fact that without up-to-date know-how, the goal of rapid economic development would remain a distant dream in the field of technology. The Development Financial Institutions (DFIs), with their technical advisory departments, would be well advised to give a high place to upgradation of indigenous technology and processes.19

2.3.10 SKILL FORMATION

An important task of development banks is to

generate or enhance required skills through appropriate training and other incentives. Dearth of technical and managerial skills also constitute impediments to progress and development banks can render assistance in the development of these skills too, to a modest extent.  

2.3.11 DEVELOPMENT OF CAPITAL MARKET

Inadequate capital supply coupled with and sometimes a byproduct of imperfect capital market is a marked feature of developed economies and ill developed capital market, is a predominant characteristic of developing economies. Hence, a strong case for development banks is felt in both types of economies. Therefore, development banks have to improve the capital market by providing medium term and long-term loans.

2.3.12 EDUCATION, EXPERIENCE SHARING AND COUNSELLING

The role of development bank as an educator and counsellor right from the stage of appraisal process of a project to its effective implementation as well as management has rightly been stressed by Diamond. According to him development banks force their clients to re-examine their plans, to spell them out in unaccustomed and explicit 

detail and to understand their implications more clearly. They, thus, effect the working habits, thinking and attitudes not only of their clients but of the business community generally. This quiet revolution in the techniques of project formulation and appraisal is a major innovation for which development banks can take some of the credit. The development banks' creative role does not stop with the decision to finance a project. It's relationship with it's clients grows more intimate thereafter, if it is doing the job of supervision effectively.\textsuperscript{23}

2.3.13 RESEARCH

A related area of activity where development banks can contribute in a big way is Research & Development. Development Banks should build up a report of case studies based on their own abundant experience of various approaches to the problem of putting soundly based enterprises on foot as well as of the snags and pitfalls into which projects fall before they falter and flounder in their course.\textsuperscript{24}

2.3.14 ACQUISITION AND ALLOCATION OF FOREIGN CAPITAL

An important feature of the development bank is that it tries to tap the foreign capital resources and to allocate it in the desired channels in consonance with the priorities of economic planning and national development.\textsuperscript{25}


\textsuperscript{24} Madan, Op.cit., p.4.
In developing countries, where there is need to obtain foreign capital and to mobilise and disburse it in the country, the services of an institutional development bank could be very helpful.

2.3.15 ENTREPRENEURIAL ROLE

Along with creation and promotion of an enterprise, at times the development banks themselves can assume the entrepreneurial role. Madan has rightly pointed out- "In countries or parts of countries which are specially backward in industrial development with lack of entrepreneurship, it may be necessary for development banks, if not directly through their subsidiaries or developmental counterparts, to assume entrepreneurial role in respect of worthwhile projects which fail to find a promoter".\(^{25}\)

2.4 Objectives of Development Banks

So far as the objectives of the development banks are concerned, they differ widely from one country to the other, from one region in a country to the other and from the objects at some stage of economic development to the other. This is manifested by the fact that development banks have been established in countries which differ widely from one another in their socio-economic environment. In developed countries, development banks generally evolve

through the normal process of market pressure and their main concern is to increase the rate of growth of the economy.\textsuperscript{26} In developed countries, the development banks are not required to fill up the gaps in the industrial structure of the economy.\textsuperscript{27} On the other hand, the objectives of a development bank in an underdeveloped economy are much different. Because of the peculiar structural drawbacks in underdeveloped economies, the responsibilities of development banks increase manifold. It has to increase capital formation, induce the investors and entrepreneurs, seal the leakages of material and human resources by careful allocation thereof, to fill the gaps in the industrial structure of the economy, to ensure that no good project suffers for want of financial and/or technical resources.

The objectives of development banking in India are\textsuperscript{28}:

1. Activising the dormant entrepreneurship through various types of assistance-technical, managerial, financial, marketing and so on.

2. No entrepreneur with worthwhile project should be allowed to go without implementing it for want of funds


and to make available the medium and long-term credit at reasonable cost of such aspiring entrepreneurs.

3. To develop over a period of time, efficient managerial resources to help rapid industrial development of the country. As production gets diversified, technology becomes more and more complex, the demand for efficient and well trained managerial personnel will be progressively increasing. So, management development is an important responsibility of the development banks.

4. In countries like India sheer vastness of size necessitated considerable attention to be paid to the objective of regional development. In a federal set up like India, unless the problem of regional economic inequalities is tackled as an integral part of overall national development, national unity and smooth working of democracy themselves may be threatened. The development banks in the deployment of credit have to pay adequate attention to the regional development objective. Development of relatively backward regions should constitute an important consideration in determining the quality and composition of the assistance rendered by the development banks.

5. India had considerable industrial growth experience in the pre-independence period. But, the industries so developed have been in need of modernization as they
also happen to be important export industries which have to sell in highly competitive world markets. In this respect the development banks have to play a key role through enabling these industries to modernise themselves.

6. The factor endowments of India are such (more labour relative to capital) that labour-intensive industries and other economic activities should constitute an important part of the economic structure of the country. Unless the small scale and tiny sectors receive all attention they deserve, the problem of poverty and unemployment cannot be solved. Therefore, one of the objectives of development banks in India is to facilitate small industry and enterprise development.

7. Given the growing import requirements of the development programmes, foreign exchange continued to be one of the scarce inputs into the development process. The development banks as purveyors of assistance in terms of foreign exchange must assure themselves that the scarce foreign exchange goes to the most needy and productive enterprises. The strain on balance of payments can never be eliminated or even mitigated, unless the foreign exchange allocation will enable the country eventually to become free of the aid requirement.
2.5 Functions of Development Banks

Conceptually, the development banks have to perform functions which are partly financial and partly developmental/promotional. Financing constitutes the hard core of the activities of development banks. Development banks render financial assistance directly as well as indirectly. The direct financial instruments are - granting of loans, underwriting of shares, bonds and debentures and guaranteeing of domestic and foreign loans. In addition, the development banks render indirect financial assistance in the form of refinancing and rediscounting.

2.5.1 DIRECT FINANCIAL FUNCTIONS

Direct financing of an industrial units is an important function of the development banks which is given in the form of a) grant of loans, b) underwriting, c) direct subscription and d) guaranteeing.

2.5.1.1 Grant of Loans

The important function of most of the development banks is to provide loan assistance to industrial concerns. Loans are provided by development banks both in local and foreign currencies. Foreign currency loans play a significant part in the industrialization of underdeveloped countries which find it rather difficult to procure the
required quantum of foreign exchange for importing the necessary capital goods and technical know-how.

In the case of IFCI, it does not provide loans to the working capital requirements of the industrial units. But, wherever working capital requirements form a part of the cost of the project, IFCI renders assistance. IFCI does not provide rupee assistance for sum below Rs.10 lakhs except in the case of 'over-run'. The maximum amount of assistance which can be provided to any single borrower without the prior approval of the IDBI is Rs.2 crores. These limits have been fixed to avoid competition with SFCs, operational convenience, concentration on large units etc.

ICICI plays a predominant role in foreign currency loans. When India has been experiencing a chronic shortage of foreign exchange and due to stringent import controls, various entrepreneurs in the country have failed to implement their schemes of expansion, modernisation or establishment of projects. In certain cases import content becomes unavoidable. In such circumstances, much of the popularity and success of ICICI emerges out of the functions of providing medium and long-term loans in foreign

currencies. It has placed ICICI in a unique position. In order to distribute equitably its scarce currency resources, ICICI generally limits its foreign currency loans for all companies in one group to Rs.30 million. The corporation confined its investment activities upto Rs.1 crore to any one industrial concern but not less than Rs. 5 lakhs to diversify the investment of it's resources.

IDBI as an apex institution gives loans and advances to large scale industries only when the finance is not available from any other source. It is also empowered to provide loans in foreign currencies. IDBI extends assistance for setting up new projects as well as for expansion, modernisation or renovation of existing units. IDBI generally extends its assistance to public limited companies. Assistance is given to those projects which involve large capital outlays or sophisticated technology. Special consideration is given to those projects which are located in specified backward area of the country.

2.5.1.2 Underwriting

Another financial instrument of development banks is underwriting. The development banks are authorised to Underwrite the shares, bonds and debentures raised by the industrial concerns. To discharge the underwriting

obligations, IFCI can retain the shares, bonds and debentures for a period of seven years only. If IFCI wants to retain these securities for more than seven years, approval of the IDBI should be obtained.

ICICI has acquired a very important place in the sphere of underwriting of corporate securities as it is highly beneficial for the new industrial concerns. At the time of the incorporation of ICICI, there was no other proper agency undertaking the risk of underwriting. ICICI has taken initiative in underwriting of industrial securities.

IDBI is also authorised to underwrite public issues of shares, bonds etc. made by the industrial concerns. Instead of underwriting this function, the bank always tries to persuade the other financial institutions to participate in that, but when no underwriting is available, it takes up the duty of underwriting. It has also underwritten public issues in close co-operation with ICICI, IFCI, LIC, UTI, SIDCs and SFCs, such operations lead to better institutional understanding and co-ordination of activities among the institutions.

2.5.1.3 Direct Subscriptions

Another method by which the development banks can provide financial assistance is through direct subscriptions
to shares, bonds etc. of industrial concerns. Prior to 1960, IFCI had no power to subscribe directly to the capital of industrial concerns and the IFCI Amendment Act 1960 authorised the corporation to subscribe directly to the share capital of industries.

ICICI occupies a unique position amongst the financial institutions/development banks to undertake the function of subscribing directly to the corporate securities especially the equity capital. Till ICICI came into existence, there was no other financial institution in the country providing direct subscriptions and there existed a serious gap in the field of industrial finance. So, ICICI has helped many industrial concerns to come up subscribing directly to corporate securities. IDBI also provide financial assistance by subscribing to shares, bonds etc.

2.5.1.4 Guaranteeing

Development banks assist industrial concerns also by providing guarantees of various types such as guaranteeing on behalf of the industrial concerns in respect of a) the loans raised by them in the open markets or from the local/foreign financial institutions, b) the deferred payments due from such concerns arising out of the domestic purchase or import of capital goods, c) the issue of clients securities etc. Some development banks are also authorised to guarantee the obligation of various financial
institutions to come forward and participate in industrial finance which is very much important in case of underdeveloped economies. The Industrial Development Bank of India is authorised to engage in this activity.

IFCI is empowered to provide guarantees in respect of the loans raised by industrial concerns in the public market, provided the period of the loans so raised does not exceed twenty five years. Till IFCI Act 1960 came into force, IFCI had no power to provide guarantees in respect of the loans raised by the industrial concerns from banks. This amendment has conferred such a power upon IFCI.32 The IFCI can also guarantee deferred payments due from any industrial concerns in connection with its import of capital goods from foreign countries often getting the approval of the government. ICICI also undertakes the function of guaranteeing loans raised by the industrial concerns from investment sources.

IDBI guarantee the loans in the public market and/or from IFCI, SFCS, Scheduled Banks, State Co-operative Banks or any other financial institutions which may be notified by the central government in this behalf. It is also empowered to guarantee foreign loans and deferred

payments due from the industrial concerns. The sphere of guaranteeing activities of IDBI is much wider than that of IFCI or ICICI. IDBI can guarantee the loans raised by the industrial concerns even from these development banks.

2.5.2 INDIRECT FINANCIAL FUNCTIONS

Development Banks assist the industrial units not only through direct financing but also by indirect financing. To build a sound industrial base, direct financial assistance is highly useful but indirect financial assistance is not less important. The indirect financial assistance is given in the form of rediscounting and refinancing.

2.5.2.1 Refinancing

The IDBI provides refinancing facilities to the eligible financial institutions in respect of loans to be granted or proposed to be granted by them to various industrial concerns. The borrowing financial institutions are liable to pay interest and principal to the IDBI irrespective of whether they are able to recover the amount which they lent or not. The entire risk is shouldered by the financial institutions for recovery of loans. IDBI do not interfere in any matter regarding margin/security/terms and conditions etc. These are left to the discretion of the financial institutions themselves.
The main objective of refinancing is to strengthen the financial resources of the financial institutions, particularly the banks so that they may participate increasingly in providing term finance to industry at reasonable rate of interest. Moreover, refinancing instrument has enabled IDBI to have a check on the industrial advances made by the financial institutions.

The facility of refinancing scheme was available to a few scheduled banks when it was implemented by the then Refinance Corporation of India (RCI). The IDBI has brought into the scope of scheme all the important scheduled banks, co-operative banks, SPCs, SIDCs and even IFCI and ICICI. Though the scheme is applicable to all types of industries, preference is accorded to the priority industries.

2.5.2.2 Rediscounting

Another form of indirect finance is the rediscounting of machinery bills which was introduced in April, 1965. The scheme has been designed to promote the sale of indigenous machinery on deferred payment basis. Under the scheme, the seller realises the proceeds of sales through discount of relative bills or notes with this bank which in turn rediscount the bills or notes with IDBI. The scheme enables the entrepreneur to acquire the machinery on deferred payment terms without going through the usual procedures involved in obtaining project loan. The scheme
is near automatic in operation and has been of special assistance to industries.

2.5.3 PROMOTIONAL FUNCTIONS

Besides financial functions, development banks also undertake promotional/developmental functions. As a matter of fact, these functions are more important for a development bank to perform than the financial functions. This is because in almost all the underdeveloped countries, some institutions exist for the provision of financial assistance to industries but very few banks undertook the promotional/developmental functions. Such activities cover a wide range of functions including the promotion of new industries to fill up the gaps in the industrial structure, assisting in the formation of other development banks, provision of technical, managerial and administrative advice, conduct of techno-economic surveys, market and investment research improving the investment opportunities etc.

According to IFCI, all activities of IFCI in a way are promotional or developmental in nature. However, the activities other than the project financing operations such as dispersal of industries to backward areas, broadening of entrepreneurship, upgradation of managerial skills, bringing professionalisation in management, providing consultancy and extension services to the tiny and small enterprises are
termed as promotional activities. The thrust in the area of promotional activities is on providing supportive measures so as to improve the productivity of human and material resources and to accelerate the process of industrialisation.33

Kupier too has listed a wide range of promotional activities that the development banks expected to undertake so as to achieve rapid industrialisation. These activities are:

1. arranging for general industrial surveys and feasibility studies for special projects,
2. formulating specific proposals for new enterprises,
3. assisting in finding technical and entrepreneurial partners for local clients or for foreign investors,
4. investing in share capital and underwriting securities in order to attract other investors,
5. arranging mergers in order to create more economic industrial units,
6. developing a capital market by trying to broaden ownership and by other devices and
7. encouraging the acceptance of new ideas in the economic sector.34

Baldev Parricha\(^{35}\) emphasised the need of promotional activities, but in his opinion, infrastructural facilities should be provided before taking up the promotional activities. He further stated that improving the quality of the products before their presentation to a development bank is an important contribution.

The development banks in India undertake various types of promotional activities such as industrial potential surveys, technical consultancy service, entrepreneurial training promotion of technology culture in industry etc.

2.5.3.1 Industrial Potential Surveys

For accelerated industrial development, it is necessary to make a correct diagnosis of the factors inhibiting the industrial growth of different regions of the country and to evaluate their growth potentialities in the light of these factors. On the basis of this survey, specific project ideas are to be pinpointed in different regions, taking into consideration the availability of natural resources and infrastructural facilities. Under the 'Institutional Intensive Developmental Effort Programme' All India Financial Institutions, under the aegis of the IDBI, initiated industrial potential survey of backward

states in 1970 for identifying specific project ideas for implementation, in the light of their resource endowments, demand potential and the availability of infrastructural facilities. These studies are carried out by teams of their officials with experience in scrutinising. According to Victor S. Barrios, to determine the potential of a project, the identifier must be analytical, have a good head for business, the ability to define and present the reasons for a project and the skill of mediation is necessary to act between investor groups - local and foreign.36 So, industrial potential survey is an important instrument in generating large volume of data relating to project ideas.

2.5.3.2 Follow-up of Project Ideas

In order to ensure that the identified project ideas were converted into viable projects the development banks initiate follow-up measures. The project ideas, identified as a result of the surveys conducted by development banks, have to be further screened and developed before arriving at some firm decisions about their implementation. This process is initiated soon after the finalisation of survey reports, following discussions with state level institutions. To expedite the implementation, the follow up work is reinforced by

reconnoissance activity on a selected basis.

2.5.3.3 Preparation of Feasibility Reports

The development banks conduct feasibility studies for certain project ideas and feasibility reports are prepared to induce the state level agencies/entrepreneurs to take up these projects for implementation.

2.5.3.4 Evolving suitable strategy

With a view to give concrete shape to project ideas and to evolve suitable strategy for industrial development, an informal forum of all the agencies concerned with industrial development was constituted. The Inter-institutional Groups (IIGs) are the fulfilment of this end. The IIGs help to accelerate the process of industrial development in a state with particular emphasis on less developed areas and evolve suitable strategies for industrial development within the framework of national and state policies and local requirements. The decisions of the IIGs are expected to relate a wide variety of practical considerations connected with the identification of project ideas and potential entrepreneurs, undertaking of studies and surveys of industrial possibilities, the nature and type of training to be provided to new entrepreneurs, the type of institutions or organisations to be approached for providing technical and managerial assistance to entrepreneurs, the type of technical assistance needed by the financial
institutions to appraise projects and so on.  

2.5.3.5 Technical Consultancy

The need of new projects for consultancy assistance, ranging from information on market to actual implementation, is much greater and demands a permanent solution. With the emphasis on the development of the tiny and small-scale sector and of the backward areas, a new brand of inexpensive consultancy services was found to be necessary. With a view to provide consultancy services particularly to small and medium units and the State level financial institutions, the Technical Consultancy Organisations (TCOs) are supposed to work as an independent corporate entities on business principles. Though the primary objective of the TCOs is to provide a wide range of consultancy services to their target clientele viz. entrepreneurs, financial institutions and government agencies, they also undertake other activities such as identification of industrial potentialities of regions and potential entrepreneurs, preparation of project profiles, feasibility reports, carrying out techno-economic appraisals and market research etc.

2.5.3.6 Entrepreneurial Development

Entrepreneurs play an important role in widening

the country's industrial base, generating self-employment, reducing income inequalities and regional disparities. Entrepreneurship in our country has been rather limited. However, the commonly held notion is that an entrepreneur is born and not made is being increasingly questioned and some recent researches and successful experiments in promoting entrepreneurship have shown that entrepreneurship can be developed. Thus, an appropriate framework for the entrepreneurial training programmes with emphasis on local entrepreneurial talent is strongly felt for stepping up industrial growth on a self-sustained basis. As such, the IDBI has been placing great emphasis on the organisation of Entrepreneurship Development Programmes (EDPs) to provide a proper motivational training to the prospective entrepreneurs and to equip them with the know-how to tackle the various problems likely to be faced by them. Entrepreneurial Development Programmes (EDPs) are being conducted by agencies such as TCOs, banks and other agencies.38 In order to provide a forum to the institutions and individuals involved in conducting EDPs for exchange of views on various related aspects, sharing of experience and to evolve a well planned integrated national approach, IDBI organised, 'National Seminar on Entrepreneurship

Development'. The major recommendations made at the seminar related to innovations in designing. EDPs suited for different groups, identification of the right kind of training institution linking technical institutions to industrial estates for inplant training and conducting courses in regional languages.

Entrepreneurship Development Institute of India (EDII) was set up in 1983 as the principal entrepreneurship development agency for training of trainers, running model training programmes, undertaking research in the field etc.

Further, Science and Technology Entrepreneurship Parks (STEPS) are set up in order to develop ongoing interaction between science and technology institutions and industry to encourage entrepreneurship among science and technology graduates and to induce entrepreneurs to adopt sophisticated technology.

In addition to the above mentioned promotional activities, the development banks also take up others such as conducting research, seminars and publications to provide useful information on the matters connected with the industrial development of the country.

2.6 Capital Structure

Generally, three types of resources constitute the capital structure of development banks viz. Government, private and foreign/international. The resources of the government in the capital structure of a development bank may take several forms viz. contribution to the share capital of the bank, contribution to the bonds, debentures and other securities floated by the bank, guaranteeing the repayment of the principal amount invested by the investors in shares, bonds etc, of the development bank, guaranteeing the payment of dividend at a certain minimum rate on it's shares by the bank and the payment of interest on it's bonds and debentures, provision of long-term loans to the bank, guaranteeing the loans raised by the bank from foreign investors/financial institutions providing the bank at periodical intervals a slice from the budget revenue, creation of special funds/receipts etc.40

Coupled with the role of government, central banks also contribute to the share capital of the development banks and/or provide long term loans. In some cases central banks also create special funds/reserves for meeting the capital requirements of the development banks.

Private financial resources comprise the capital contributed by financial institutions and/or the investing

public reserves, if any, accumulated by the bank, loans raised in the market and the deposits received.

Development banks also receive foreign/international funds for channelisation into domestic investment channels. Further, a substantial amount of loans to development banks all over the underdeveloped world have been provided by the World Bank and USAID to facilitate economic growth. These foreign/international resources, though not substantial in quantity compared to their total funds play a very dominant role in the operations of the development banks.

The capital structure of development banks in India chiefly comprises four elements viz., paid-up capital, reserves and surplus, bonds and debentures and borrowings besides other liabilities.

2.6.1 PAID-UP CAPITAL

An adequate equity base in a development bank is as important as in any other business concern. With a strong equity capital position, a bank can meet the financial needs of deserving projects. Besides, it serves as a cushion and absorbs the losses that may occur. It serves as a guarantee fund to creditors and protects the institution against liquidation. However, an exclusive reliance on equity capital is not considered as financially expedient.
The total paid up capital of the development banks during 1970-71 constituted Rs.45.85 crore which was 7.27 per cent of the total liabilities. But the share of it has declined year after year and it constituted only 2.35 per cent in 1992-93.

Among the development banks, the IDBI being an apex bank is at the top in raising its resources through share capital. During 1970-71 the IDBI received 10.57 per cent of its total resources through paid up capital followed by ICICI (4.78 per cent) and IFCI (4.70 per cent). The same hierarchy is observed in almost all the selected years except in 1992-93 where the share of paid-up capital was 2.90 per cent in case of IFCI while it was 1.87 per cent and 2.42 per cent in case of ICICI and IDBI respectively (Table-2.1).

2.6.2 RESERVES AND SURPLUS

Another important source of the development banks is reserves and surplus. This is important to meet the unforeseen expenditure of the banks from time to time.

The total reserves and surpluses of the development banks constituted 5.87 per cent of the total resources of the banks during 1970-71. The share of reserves and surpluses has increased to 7.11 per cent in 1992-93.
<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Paid-Up Capital</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>(a) IFCI</td>
<td>8.35</td>
<td>17.50</td>
<td>135.00</td>
<td>220.50</td>
</tr>
<tr>
<td>(b) ICICI</td>
<td>7.50</td>
<td>24.75</td>
<td>114.58</td>
<td>241.08</td>
</tr>
<tr>
<td>(c) IDBI</td>
<td>10.00</td>
<td>145.00</td>
<td>703.00</td>
<td>753.00</td>
</tr>
<tr>
<td>(d) TOTAL</td>
<td>45.85</td>
<td>187.25</td>
<td>952.58</td>
<td>1196.58</td>
</tr>
<tr>
<td><strong>Reserves &amp; Surplus</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>(a) IFCI</td>
<td>11.46</td>
<td>31.98</td>
<td>391.32</td>
<td>542.56</td>
</tr>
<tr>
<td>(b) ICICI</td>
<td>7.34</td>
<td>30.12</td>
<td>505.93</td>
<td>965.35</td>
</tr>
<tr>
<td>(c) IDBI</td>
<td>18.22</td>
<td>129.00</td>
<td>1380.00</td>
<td>2119.00</td>
</tr>
<tr>
<td>(d) TOTAL</td>
<td>37.03</td>
<td>191.10</td>
<td>2777.25</td>
<td>3636.91</td>
</tr>
<tr>
<td><strong>Bonds &amp; Debentures</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>(a) IFCI</td>
<td>57.69</td>
<td>409.54</td>
<td>3105.23</td>
<td>4104.71</td>
</tr>
<tr>
<td>(b) ICICI</td>
<td>11.00</td>
<td>333.65</td>
<td>2570.89</td>
<td>3223.30</td>
</tr>
<tr>
<td>(c) IDBI</td>
<td>7.00</td>
<td>43.84</td>
<td>33.58</td>
<td>24.93</td>
</tr>
<tr>
<td>(d) TOTAL</td>
<td>66.69</td>
<td>1933.10</td>
<td>26984.12</td>
<td>22826.01</td>
</tr>
<tr>
<td><strong>Borrowings</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>(a) IFCI</td>
<td>101.82</td>
<td>91.52</td>
<td>1900.82</td>
<td>1545.32</td>
</tr>
<tr>
<td>(b) ICICI</td>
<td>127.92</td>
<td>313.10</td>
<td>4315.91</td>
<td>7925.94</td>
</tr>
<tr>
<td>(c) IDBI</td>
<td>81.49</td>
<td>43.04</td>
<td>54.02</td>
<td>61.32</td>
</tr>
<tr>
<td>(d) TOTAL</td>
<td>268.23</td>
<td>788.67</td>
<td>8455.86</td>
<td>20555.60</td>
</tr>
<tr>
<td><strong>Other Liabilities</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>(a) IFCI</td>
<td>10.40</td>
<td>41.77</td>
<td>999.34</td>
<td>595.06</td>
</tr>
<tr>
<td>(b) ICICI</td>
<td>3.21</td>
<td>26.11</td>
<td>328.41</td>
<td>569.89</td>
</tr>
<tr>
<td>(c) IDBI</td>
<td>7.49</td>
<td>34.51</td>
<td>1617.00</td>
<td>2157.00</td>
</tr>
<tr>
<td>(d) TOTAL</td>
<td>21.10</td>
<td>414.39</td>
<td>2944.75</td>
<td>3321.95</td>
</tr>
<tr>
<td><strong>Total Liabilities</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>(a) IFCI</td>
<td>189.72</td>
<td>592.31</td>
<td>6531.71</td>
<td>6990.15</td>
</tr>
<tr>
<td>(b) ICICI</td>
<td>156.97</td>
<td>727.93</td>
<td>7655.72</td>
<td>12924.56</td>
</tr>
<tr>
<td>(c) IDBI</td>
<td>283.85</td>
<td>362.83</td>
<td>22768.00</td>
<td>31084.00</td>
</tr>
<tr>
<td>(d) TOTAL</td>
<td>630.54</td>
<td>4683.07</td>
<td>36955.43</td>
<td>50998.71</td>
</tr>
</tbody>
</table>

Note: Figures in parentheses indicate percentages.
Among the development banks, initially the IDBI owned reserves to the extent of 6.42 per cent of total resources followed by IFCI (6.04 per cent) and ICICI (4.68 per cent). With the passage of time, the reserves and surpluses more or less proportionately increased in all the banks and they constituted 7.76 per cent, 7.47 per cent and 6.82 per cent of IFCI, ICICI and IDBI respectively.

2.6.3 BONDS AND DEBENTURES

Another way of securing financial resources to development banks is through issue of bonds and debentures. The bonds and debentures issued by IFCI are guaranteed by the central government as to the repayment of principal and interest at a specified rate. It can also raise long-term financial resources by regulating IDBI to subscribe its bonds and debentures if necessary. The bonds and debentures issued by IFCI from time to time carry different rates. The ICICI also raises its resources through bonds and debentures, but gives much importance to borrowings from foreign financial institutions.

Like IFCI and ICICI, the IDBI is also authorised to raise its financial resources by issuing bonds and debentures to the industrial concerns. The central government may provide guarantee to the bonds and debentures issued by the bank at the request of IDBI as to the repayment of principal and interest at a specified rate.

The resources raised by the development banks through bonds and debentures increased from time to time and constituted 10.89 per cent during 1970-71, which ultimately
increased to 45.96 per cent during 1990-91. (Table 2.1) Later, the resource mobilisation through bonds and debentures declined to 44.76 per cent in 1992-93. Among the different development banks, the share of resource mobilisation through bonds and debentures is the highest in case of IFCI followed by IDBI and ICICI in that order.

2.6.4 BORROWINGS

Generally, the development banks borrow the resources from Government of India, Reserve Bank of India and foreign financial institutions so as to strengthen their resource position.

Table 2.1 clearly shows that the total borrowings borrowed by the development banks from various organisations constituted 73.62 per cent of the total resources during 1970-71 which subsequently decreased to 39.27 per cent in 1992-93.

Among the development banks, ICICI received the largest share of resources in the form of borrowings in comparison with IFCI and IDBI.

Thus, it can be concluded that bonds and debentures and borrowings constitute the important source of capital to development banks in India.
2.7 Management and Organisational
Set Up of Development Banks

The management and organisational set up of a development bank represent its decision-making apparatus and operational processes which in turn are attuned to its operational objectives covering the areas of the economy which it serves (sectors assisted) and the types of operations it engages in (loan assistance, underwriting, direct investment and guarantee support, pre and post finance, promotional and supervisory activities). Besides, the geographical area of the country or the state falling within the operational sphere of the development bank, its age and maturity, its operational resources and the staff expertise built up by it, its ownership, constitution and operational philosophy and institutional environment influence its management and organisational set up.

2.7.1 MANAGEMENT SET UP OF DEVELOPMENT BANKS

The composition of the Board of Directors is very important because the ultimate success of a development bank, as of other business enterprises, depends on the quality of the members of the board. While constituting the Board every care should be taken to see to it that persons with expertise and experience in the field of institutional financing are included in it. Further, men with a wide practical knowledge of industry, business and finance, and
also representatives of the different regions and sub-regions should be included in it. More precisely, the directors and senior officers should be drawn from among the economists, chartered accountants, managerial experts, financial and investment analysts and industrialists.

The Board of Directors of a privately owned bank chooses a chairman from amongst themselves, but in the government controlled institutions, the appointment of the chairman is subject to the approval of the government. In such cases, the government indicates its choice and the chosen person, who is generally top ranking government official, is elected.

The Board of Directors in a development bank is generally concerned with formulating, lending, investing and other policies. The detailed operations relating to lending and investing are looked after by a committee known as the executive committee, comprising some members of the Board including the chairman. This is done to facilitate the speedy execution of business. The Board members cannot meet very often to attend to the minute details of the loan and investment proposals. The executive committee, being a smaller body meets very often to attend to the minute details of the loan and investment affairs. It has the authority to take final action on behalf of the Board or to
ct subject to the ratification of its decisions by the board of Directors. However, it should be remembered that the executive committee, which is armed with wide powers to deal with all the problems of the institutions, may tend to become an absolute authority and usurp the functions of the board, which may merely rubberstamp its decisions. Against this background, the Management set up of each development bank is discussed.

2.7.1.1. Management Pattern of Industrial Finance Corporation (IFCI)

The Board of Directors of the IFCI is much more broad based than that of other financial institutions because of the pattern of its ownership. It consists of 14 members including the chairman who is appointed by the Government of India after consulting the IDBI (formerly a subsidiary of the RBI). The Chairman works on a whole time basis and his term of office is three years, which may be extended by the Government.

Of the remaining 13 Directors, four are nominated by the IDBI, two by the union government, two by scheduled banks, two by co-operative banks, and the remaining two by the other financial institutions, like the insurance companies and investment trusts. It has been the practice of the IDBI to have three outside nominees who are experts in the field of industry, labour and economics. The fourth
is the General Manager of the IDBI. There is an executive director in the corporation.

It is evident from the composition of the Board of the IFCI that half of the number of the Board members (7 out of total 14 members) are nominated by the Central Government and the IDBI. This is one of the major factors which has influenced the operational strategy of the corporation. The directors nominated by scheduled banks, co-operative banks, and insurance and investment companies hold office for a term of four years.

The Board meets once a month usually on the last Thursday. It is supposed to act on business principles with due regard for the interests of industry, commerce and the general public. It is guided in policy matters by such instructions as it receives from the government and the IDBI from time to time. In all matters of dispute between the corporation and government, the decision of the latter is final. The central government reserves the power to supercede the Board and appoint a new one in its place. The supreme authority in respect of all matters of policy and the operations of the corporation vests with the Central Government.

The Board is assisted by a Central Committee, which consists of the chairman of the Board (who shall be
the Chairman of the Committee), two directors elected by the nominated directors and two directors elected by the elected directors. The Central Committee assists the Board of Directors in the discharge of its functions. It is competent to deal with any matter with in the limits of the directors received by it from the board.

The IFCI also has standing advisory committees - one each for textiles, sugar, jute, hotels, engineering and chemical processes and allied industries. These committees assist the corporation in the efficient discharge of its functions. The advisory committees have a special role to play in any development bank. It is not possible for a single institution to have on its regular paid staff experts in all fields of economic activity. Therefore, it becomes necessary for it to take the benefit of such experts on an adhoc basis. It is with this objective in view that advisory committees have been constituted for the corporation. The Chairman of the IFCI is the ex-officio chairman of the Advisory Committee, which, besides a few directors of the corporation includes outside experts and officers of the Government.

The headquarters of the IFCI is at New Delhi. The corporation has 17 branch offices all over the country, including a separate office at Delhi. It has constituted local advisory committees at almost all the branch offices
to advice the management on the industrial climate in the respective areas covered by them.

2.7.1.2 Management Pattern of Industrial Credit & Investment Corporation of India (ICICI)

Since the ICICI has been set up on joint stock company basis, its managerial pattern is governed by its articles of association prepared with in the broad framework of the Companies Act, 1956. The Board of Directors of the ICICI consists of 16 members including the chairman. Of the 15 members, two are foreigners, one director is nominated by the Government of India in terms of the agreement between the ICICI and the government. The directors are men who have distinguished themselves in such fields as industry, finance and law.

Another important aspect of the managerial structure of the ICICI is that it does not have any regular advisory committee for advice on the proposals for financial assistance.

2.7.1.3. Management Pattern of IDBI

The IDBI charter provides that the general superintendence, direction and management of the affairs and business of the bank vests in a Board of Directors consisting of a chairman and a managing director appointed by the Government of India, a Deputy Governor of the Reserve
Bank of India nominated by that bank, and 20 other directors (officials of the Government of India - 2 representatives of the financial institutions, 5 representatives of public sector banks, 5 representatives of SFCs, 6 employees of financial institutions and 2 persons with special knowledge and professional experience, all nominated by the Central Government.

The Board has consisted an executive committee which has the authority to excercise all such powers as can be excercised by the Board. The Committee consists of 10 members, all from the Board. It meets every month, and is presided over by the Chairman of the IDBI. From the practical point of view, this body is the chief managerial organ of the bank.

The IDBI has formed a panel of technical advisors and consultants by drawing upon experts from various sectors of the industry. Adhoc advisory committees have been constituted from various projects, the members of which are drawn from the panel. The adhoc committee is charged with the responsibility of reviewing the project appraisal reports earlier to their placement before the executive committee, and offering suggestions wherever necessary. As a matter of fact, it is the experts on such committees who are found to possess the required technical and financial acumen to assess the desirability of projects.
2.7.2 ORGANISATIONAL SET UP OF DEVELOPMENT BANKS

Broadly speaking, there can be two broad patterns of organisational structure-function oriented and expertise oriented. In a function oriented structure the organisation is structured according to the functional areas of the organisation: project appraisal, legal, disbursement, accounting, follow-up, project promotion and development training. Each department is staffed with the experts it requires to perform its functions; wherever necessary, professionals from other departments are drawn upon. The expertise-oriented departments are created around individual disciplines such as technical, financial analysis, legal and economic research. Under the aegis of a co-ordinating department, individual experts are deployed in suitable teams to perform various functions such as evaluation of projects, project follow-up and supervision, project development and promotion.

2.7.2 Organisational Set Up of IFCI

In India one or the other pattern of organisational structure has been adopted by development banks in their central offices. The entire organisation of the IFCI is departmentalised on a functional basis, with the Board of Directors as the supreme body and the General Manager as the Chief Administrative Officer, who is directly
accountable to the chairman. At the centre, there are 13 specialised departments viz., projects, advisory services, administration, personnel, Board and co-ordination, legal, economic and planning, statistics, internal audit and inspection, management and productivity services, public relations, foreign currency loans and accounts.

A new department viz., the management and productivity services department has been created recently by the corporation to undertake a systematic and comprehensive review of the organisational set up and the systems of work in the corporation with the help of modern management techniques.

2.7.2.2. Organisational set-up of the ICICI

At the apex of the organisation is the Board of Directors, with the Chairman who is also the managing director of the corporation. To carry out financial activities, the corporation has organised a number of departments, each one staffed with experts. The departmental heads are responsible to the general manager of the corporation.

A new department known as the project promotion department was set up in 1973 in order to help the corporation in its efforts to promote new investment opportunities in backward areas.
The corporation also has set up a merchant banking division in 1973 with the objective of assisting upcoming enterprises in raising funds from the capital market.

The corporation has three regional offices at Calcutta, Madras and Delhi. Each one is headed by a regional manager. The regional office has been given the authority for the preparation of appraisals, follow-up of projects and legal documentation. It is staffed adequately to perform project appraisal, project follow-up, as also development activities. Operationally, the concerned staff of the regional office maintain a close liaison with the functional departments at the central office.41

An important organisational feature of the ICICI is the informality existing in the corporation. Till sometime back, the ICICI did not even have a standard application form. In fact, it functions with minimum of note writing and the maximum of informality, through discussions and oral instructions. This is contrary to practice in the IFCI and IDBI which are run on semi-bureaucratic lines, with tons of noting on every subject, major and minor.

2.7.2.3 Organisational Set up of the IDBI

The entire organisational structure of the IDBI was restructured in March 1978 following its delinking from the RBI. The principal functions and operations of the IDBI have been entrusted to two separate wings. The Domestic Finance Wing and the International Finance Wing, are having the same status as the other, and each under the control of an Executive Director having knowledge of and experience in their respective fields. Certain departments, including the chairman’s secretariate which assist the management in evolving policies, assessing performance, developing innovation activities and overseeing the functions of both the wings in the light of the policy guidelines evolved by the Board of Directors, function directly under the Chairman and Managing Director.
CHAPTER III

Development Banks: A Functional Analysis