CHAPTER-I
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Industrialization has a strategic role in accelerating the pace of socio-economic development for the simple reason that, as the classical economists emphasized, industry is subject to the law of increasing returns to scale, while the primary land-based sector is subject to diminishing returns to scale (Kaldor). Rapid rate of growth in industrial output results in quickening the pace of technological change in the industrial sector and in accelerating the process of technological change in all the other sectors like agriculture and services.

However, industrial growth critically depends on the extent of the market for industrial goods because of the circular cumulative interaction between the extent of the market and technical change. As Adam Smith perceptively observed, increase in the size of the market leads to new opportunities for division of labour or technical change and the latter tends to increase the size of the market; hence the phenomenon of increasing returns to scale.

Market size depends on the growth in agriculture and exports of industrial goods and services. In many developing countries it may be difficult to accelerate the pace of change in the agricultural sector initially as decisions for technological change have to be made by a large number of farmers, while it may be easier to concentrate on raising the rate of growth of exports of industrial goods and services. A strategy of export-promoting industrialization process leads to increasing the size of the market and thus accelerating the process of technical change and industrial development and
employment; it also quickens the pace of technological change in agriculture by withdrawing labor from that sector for industrial employment and promoting innovations in agricultural processes and methods of operation. This is so not only because the growth rate of productivity in the industrial sector itself rises but also because the growth rate will tend to increase the rate of productivity growth in the other sectors. This may happen both in agriculture and in the distribution trades, partly on account of the absorption of surplus labor and partly because of a faster increase in the flow of goods into consumption. But, more generally, industrialization tends to accelerate the rate of change of technology, not just in one sector, but in the economy as a whole. "There can be little doubt that the kind of economic growth which involves the use of modern technology and which eventuates in high real income per capita, is inconceivable without industrialization. In that sense there are no alternative roads to economic development" (Kaldor).

It is not possible to initiate and sustain such an industrialization process without an active role of the State in developing and adopting an institutional and policy framework to evolving circumstances and environment and specific instruments of industrialization suited to the stage of development of a country. One of the strategic instruments has been historically a development bank or non-banking financial institution called in different contexts by different names—which is distinguished from other financial institutions by its development orientation and emphasis on the spirit of enterprise.

A development bank cannot act like a normal commercial bank; it has no raison d'être unless it seeks to promote a viable and widely diffused process of industrial development consistent with the country's development objectives. It is essential,
therefore, that in view of the general shortage of entrepreneurial talents in the initial stages of development, the available talents should be harnessed in a development bank because of its strategic location with a large leverage for industrial development.

1.1 Non-Banking Financial Institutions (NBFIs): A Conceptual Framework

Diamond has defined a non-banking financial institution or a development bank in following words:

*Development bank is an institution to promote and finance enterprises in the private sector.*

Particularly, it is oriented not only towards free-economy and private sector dominated philosophy, it finances long-term capital formation in a manner directed and related in accordance with the development priorities of the country. The twentieth century development bank combines the functions of banking and development institutions. It is the promotional aspect of the functions. Thus a development bank may be defined as:

*A private and public institution, which provides promotional services and medium and long-term finance to public or private projects, which are development (economic) oriented and bankable.*

Financial Institutions, more appropriately designated as 'Development Banks' in economic literature are a "chosen instrument for facilitating and stimulating economic growth." These institutions emerged as a consequence of the special needs and circumstances of the time. Carrying variegated nomenclatures, Non Bank Financial Institution, Development Corporation or Development Finance Institution, such
institutions have concentrated on formulating and executing techniques of development bank for financing industry. Development banking comes to be significantly recognized as means of economic development in a country. "Financial Institutions need not be passive instruments of economic activity, with dynamic management and adequate permissive environment of available opportunities and of favorable policies, they can be active engines of economic development" (Bhatt).

A distinction is often made (by the United Nations, for instance) between a 'development bank' or 'finance corporation' defined as an institution 'concerned primarily with long-term loan capital', and a 'development corporation', which is 'concerned primarily with equity capital' and with 'fostering and managing specific companies as well as providing financial support. This distinction may be conceptually valid but is usually too blurred to be useful in practice. In some cases, banks or corporations, created to invest in both loans and equity have gradually moved, in their actual operations, to one or the other end of the spectrum; and others, created to serve one purpose, have evolved in a quite contrary direction, as a result of changing circumstances or shifting government policy. Moreover, in the area between outright debt and common shares lies a broad range of useful investment possibilities. All those possibilities can be of great importance in the stimulation of a capital market, which is another objective of many development banks.

Although the distinction between loan-providing development banks and equity-providing development corporations may be blurred, it does help to point up the two objectives common to virtually all such institutions: the provision of capital and the provision of enterprise when either or both of those requisites of economic growth is
thought to be lacking. Though the emphasis may sometimes be on one and sometimes on the other, the purpose of setting up a development bank or corporation is usually to supply these two factors of production in order to speed up the process of development. The development bank, defined as an institution to promote and finance enterprises in the private sector, is not a new device. Institutions to mobilize capital and to promote productive investment have existed for more than a century. They exist today in countries as diverse in background and circumstances as France, Chile, Puerto Rico, Turkey, India, Great Britain and Indonesia.

It is an extremely difficult task to define Development Banks. This is so because of the tremendous diversity in their forms and often the scarce similarity in their functions. There is obviously no dispute about their target, viz. acceleration of the rate of economic growth through speeding up the process of industrialization and introducing a qualitative change in the pattern of investment. Many a term is used to describe in the so-called development banks.

1.2 Financing for Development

In an underdeveloped economy, there is a general paucity of capital because of various socio-economic factors such as lower savings rate from low incomes, conspicuous consumption by wealthy households, wasteful expenditure on ceremonies, and inadequate channelisation of savings towards productive endeavors. A desire for quick returns makes investors reluctant to invest in long-term projects and that too with tangible collateral. Also, because of lack of adequate banking facilities and financial
institutions other than those in public sector, a major source of capital are the unorganized financial intermediaries such as money lenders and family investment house. Most of these features of underdeveloped economies characterized the Indian capital market before independence. In fact, these have been major impediments to industrial development in a country, which possessed—and still does—some of the most vital prerequisites for industrialization such as raw materials, trained manpower and above all, an assured and vast domestic market. Industrialization, involving installation, growth and diversification of large and medium scale industries, is painful but regarding economic path to complex economic growth which, among other things, is a function of new capital formation. Three stages, namely, creation of savings, mobilizing and canalizing of savings and acquisition of capital goods out of such savings, in their totality comprise the process of capital formation. The process of industrialization requires huge financial resources in their manifold and variegated manifestations—fixed and circulating capital—to establish the business and for its day-to-day working. Industrial finance conveys the creation, organization and mobilization of different types of finances needed for a project depends, inter alia, on the nature of that project. In industries like, cotton, sugar and jute, about 60 percent of their value of production is needed as capital whereas in bicycle industry capital measuring to the total value of annual output is needed whereas total capital needed is generally much more than the value of annual output in industries like paper, glass, cement, etc. Thus projects of different dimensions, characteristics and complexion require widely divergent and different magnitude and types of financial resources to sustain and support them in their existence, growth and diversification.
It is a historical fact that in the earlier phase of development of what are now industrially advanced countries, their governments played a dominant role in providing various incentives, particularly financial assistance in various forms. The most common method has been the setting up of financial institutions, known as Development Banks, to provide the necessary long term finance, as also guidance, assistance and encouragement in various aspects of industrialization such as marketing, research and development, by extending technical know-how and trained manpower.

A development bank must be an organic body that acts and reacts to the needs of its environment. It must strive to find its appropriate palace in the economy and create a proper image for itself with government, industry, agriculture and other sectors that it serves. This is, of necessity, a slow process. A development bank must proceed cautiously particularly during the initial years of its existence when mistakes or false moves can irreparably damage its reputation. The most important function of a development bank is to assist the process of development and the criterion for success is the extent to which it helps the process of development of resources: human, material, regional and financial.

"Among the proximate causes of economic development, the supply of entrepreneurial and management abilities now occupies in official documents a position of pre-eminence at least equal to that of capital" (Hirschman). A development bank plays a part in promoting the growth of both managerial and consultative talent through the constant advice and assistance.

There are divergent views about the functions, duties and responsibilities of a development bank and no finality has yet been reached about it.
The underlying assumption of traditional concept of development banking are that all the resources needed for investment are available, finance is a key factor and once finance is arranged investment will automatically step-up. These assumptions are questionable especially in developing economies where non-financial activities, sometimes called entrepreneurial activities, also come under the purview of these banks.

The structural drawbacks in developing countries make process of development unsmooth thus non-banking institutions face multifarious problems. “Capital may be in short supply, then again it may exist but be timid, in which event what may be want, particularly in untried lines of activity, is initiative. Again both capital and initiative may be present, but there may be lack of experience-technical or managerial – to set up and operate the enterprise”(Diamond). Development banking institutions come to the rescue. Such institutions can be instrumental in alleviating and minimizing the obstacles to investment. Joseph Akane has considered development banks as a financial intermediary supplying medium and long-term funds to bankable economic development projects and providing related services. Productivity of investment can be improved by these bands by providing the required ingredients as technological and managerial process. These institutions act as instrument for accelerating the rate of growth and per capita real national income and to put developing economy on sound footings of self – sustained growth.

In the developed countries, which enjoy self, sustained growth the development banks generally evolve ‘through the normal process of market pressure’ and strive for increase in growth rate. Development banks stress more on underwriting and subscribing to
capital rather than giving loans. Further in these countries assistance is more for expansion, modernizing and reorganizing rather than to new projects. Such banks in developed countries emphasize more on financial functions as compared to promotional functions. Many of such banks in such countries have broadened their field of operation by making overseas investments and economic cooperation like ‘commonwealth Development Finance Company’ assists industrial uplift in Commonwealth Countries.

On the role of these banks H.T. Parekh has observed that these “do not and are meant to provide not the total finance required for development, but such marginal amount as would fill the gap in a given situation. Their role is that of catalysts which serve to mobilize much larger capital from other sources.” Thus these banks provide different ingredients of economic development, but depending on socio-economic set up of the country, emphasis of their activities shifts.

Mr. Baldev Pasricha, Ex-Chairman of IFCI once observed, “It had been well recognized that the task of industrial development and promotion of economic growth could best be handled through development banks rather than through normal process of governmental machinery." He also considered these banks as a means of translating planned targets in the field of economic development into reality by playing their role at micro level.

1.3 Evolution of Non-Banking Financial Institutions (NBFIs)

Development banks or NBFIs (Non-Banking Financial Institutions) reflect the background, situation and needs of the country in which they appear (Diamond). Since,
Europe was the leader in modern economic development, the embryonic growth of banking as well as development, banking emerged first in that region of the world. It started with France. In the French social structure, the businessman had always held an inferior place. Consequently, he had been trying to earn a respectable social status for himself by imitating the superior groups. Thus, the financial resources of the businessman were diverted towards conspicuous consumption, which obstructed the smooth natural growth of industries in France during the first half of the 19th century. The conditions in other countries of the continent were not much different from that of France. They were confronted with the shortage of capital and other factors of industrialization. As the birth pangs of the Industrial Revolution were first felt on this continent, these countries witnessed the birth of a number of new institutions and relevant legal codes. Corporate enterprises were born, capital markets developed, and their utilization in building up overhead facilities (railways, canals and public utilities) provided the base for transforming their economies rapidly. In this process, the banks on the continent of Europe played an important role. From this background specialized financial institutions, a prototype of today's development banks, emerged on the European continent during the 19th century.

The Societe-Generale de Belgique, found in 1822 in Belgium, was the first development bank that came into existence to foster the development of industry.

In France, the specialized institutions like Comptoir d'Escompte, the Societe Generale pour Favouriser l'Industries et le Commerce de la France and others were established in the mid 19th century. But the most important was the Credit Mobilier, which was established in 1852 by the Pereire brothers. It was through this institution that France
was exporting capital, and industrial and organizational skills not only to Asia and the
Near East but also to European countries like Austria, Germany, Hungary, Rumania,
Serbia, Spain, Switzerland, Italy and even Russia. The banking system of America also
showed a keen interest in the enterprises they financed.

The bank floated and underwrote government and municipal bonds, subscribed to the
debentures of companies and granted loans to the industrial concerns on the security of
real estates, land and factory. Premises, and to the small industrialists on their personal
securities.

Before 1931, however some efforts had been made to bridge the credit gap. In 1927,
the Securities Management Trust Ltd. was set up as a private company entirely owned
by the bank of England. In 1930, the Bankers Industrial Development Company was
formed. In 1934, the Credit for Industry Ltd. was established to assist small business
firms. But all these attempts could not eliminate the "Macmillan gap"

Therefore, during the post-war period the Industrial and Financial Corporation was
established in 1945, the Colonial Development Corporation in 1948, the Commonwealth
Development Finance Company in 1952 and other specialized institutions came into
existence.

The history of development banking in India dates back to the Swadeshi Movement
period of 1906-13 during which many commercial banks were established to provide
industrial finance. They remained confined particularly to the State of Punjab of those
days and undertook several kinds of business activities.

Due to its bad financial policies ‘Societe-General de Belgique’ became seriously
financially involved and in 1951, it was directed to pay more attention to ordinary deposit
banking business. Thus in the early stage of their inception development bank had to veer round into an ordinary commercial banking business. In mid-century this new financing technique gained acceleration and France established a series of development banks. The most important was 'Credit Mobilier' which aroused greater interest and was established in 1852 by the Pereire brothers. It was chiefly interested in public utility concerns, which had comparatively long gestation period. This agency not only gave impetus to home industry, but also turned to the task of promoting and financing industries in other countries. After playing considerably outstanding role in Europe, though had to close down in 1867 due to its faulty investment policies yet it did become a model for similar investment banks established in Germany, Austria, Belgium, Netherlands, Italy, Switzerland and Spain. In Germany, the bank combined both the functions of providing short-term and long-term capital and came to practice what has been termed as universal banking. In England, where investment banking was rather comparatively late in coming, the commercial banks played a reluctant, though, increasing and often unrecognized role in financing fixed long-term investment and the line between credit and capital, the short-term and long-term became somewhat blurred.

In the twentieth century special needs of small and medium enterprises came to be recognized along with the needs of large-scale sector. Development banks no longer remained confined to Europe, other parts of the world also resorted to this new idea. Japan initiated by establishing 'Industrial Bank of Japan' in 1902 for financing her industrial development and it remained as the only type of a specialist bank designed to foster industrial progress till the close of First Great War. Highly industrialized countries
of the world had also gradually to resort to the formation of development finance institutions. U.S.A. decided to establish ‘Reconstruction Finance Corporation’ for economic rehabilitation of the country ravaged by the depression of thirties.

Financial experts of Allied Nations early in Second World War began to consider a variety of proposals intended to help realize economic goals of the allies. In 1944, after a prolonged and intensive discussion, the proposal for International Bank for Reconstruction and Development (IBRD) was formulated. The Bank (IBRD) started its operations in June 1946. On the international scene this was the first effort to have a Development Bank.

The emergence of IBRD provided impetus to development banking. It provided incentives to the creation of many specialized financial institutions at national levels, besides the institutions set up directly by the World Bank itself (68 development banks in 44 countries). Development banks came up not only on national or international level but also on regional level to serve countries in their ambit of geographical influence. ‘The African Development Bank’, ‘Inter-American Development Bank’, are some such institutions. A resume would show that Development banks have been set up in almost all countries of the world.

Regarding evolution and growth of development and economic growth in underdeveloped countries’, refers to two views. As per the first view lack of such institutions in underdeveloped countries signifies the lack of adequate demand for services of development institutions. Second is that development bank should deliberately be created in order to act as an effective stimulant to industrial development. Second point of view, which is supply-oriented and optimistic in
approach, is more generally and specifically followed by developing countries and India is one of such countries. Soon after independence, an array of such institutions came up at national as well as state level in India.

1.4 Growth of NBFIs in India.

At the time of independence the Indian capital market was characterized by lack of institutions such as issue houses, investment trusts and unit trusts, for placing the shares or debentures issues on the capital market. It was felt that the existing financial institutions could go only part of the way in meeting the requirements of industrial finance. It was, therefore, necessary to devise new agencies for attracting long-term capital into both large scale and small scale industries.

In 1948, the industrial Finance Corporation of India had come into existence to fill up this gap. The Report of the Committee on Finance for the private sector emphasized the need for more special institutional devices that would:

".....add to the confidence of the investors and increase the marketability of shares and debentures, attracting thereby new private investors into the field. As industrial expansion gathers momentum, new units will come into existence. Also, the operation of the units which are at present organized on a proprietary partnership or private limited company basis grew in size, the tendency to convert these into public limited companies will be strengthened and will lead to an increased resort to the capital market for procuring long-term finance. In such a contingency there will be room for
several types of agencies for mobilizing inevitable resources and promoting further growth.

A rapid development of both agriculture and industry in India necessitated specialized term financial institutions. Although India had a fairly long history of traditional industries, the dynamics of industrialization was slow because the structural imbalances and discontinuities had their dampening effect.

"This called for efforts in other areas to convert the emerging opportunities and catalyze the growth impulses into productive enterprises. For realizing these objectives, there was a special role to be played by the financial institutions insofar as the financial input of the right magnitude, right types, and at accessible sources was the missing link around which the human and material resources could be harnessed to generate increasing volumes of real outputs and services (Pai)."

The purpose of setting up the Industrial Development Bank of India in 1964 could be best described in the words of the then Finance Minister of India, Shri T.T. Krishnamachari who said, while introducing the bill on IDBI in the Parliament that "where a long-term view is necessary and certain amount of risk has to be taken, the existing institutions tend, by reason of their statutory obligations and traditions, to the conservative and cannot in any case be very helpful.

Since independence, India has embarked upon planned development programs. While there has been development through the years, its fruits have not been reaped to the socially desirable extent by all the regions and people. Successive Plans have drawn attention to the fact that unless the growth potential of backward areas is exploited by actively involving the local people in the development process, the ideal of an
egalitarian and just society will not be realized. Conscious efforts, therefore, have to be made to hasten the pace of development in these regions.

At the time of the formulation of the fourth plan the Planning Commission, on the recommendation of the National Development Council, constituted two Working Groups in 1968—one under the chairmanship of Shri B.D. Pande to recommend the criteria for the identification of backward areas, and the other under the chairmanship of Shri Wanchoo to suggest fiscal and financial incentives to those who establish industries in the backward areas. The Pande Committee, on the basis of certain economic criteria, classified the States of Andhra Pradesh, Assam, Bihar, Jammu & Kashmir, Madhya Pradesh, Nagaland, Orissa, Rajasthan and Utter Pradesh and all Union Territories except Chandigarh, Delhi and Pondicherry as industrially backward regions. On the basis of the criteria of the Pande Committee, and also some additional indicators, the planning Commission classified 229 districts as industrially backward districts eligible for concessional financial assistance by financial institutions. In consonance with the government policy, in 1970 a package of concessional financing was introduced with a view to pumping sizable amounts of money into the notified industrially less developed areas.

However, the scheme of concessional financing did not yield the desired results, and development banking institutions could not achieve any worthwhile success in directing resources to the backward pockets of the economy.
1.5 Objectives of NBFIs.

The diversified activities, which constitute the scope of these banks have an ultimate objective of economic growth. Economic growth in fact is a national aspiration especially for developing countries. The impact of economic growth is measured differently by different authors. Some consider increase in per capita output as an indicator of economic development while some others view increase in per capita output as an indicator of economic development while some others view increase in total and per capita income as an important characteristic. It is an outcome of interaction of many interdependent and independent economic variables. Importance of capital has been emphasized in this process by Schumpeter. He establishes link of capital and economic development by observing that capital is nothing but the levers by which the entrepreneur subjects to his control concrete the goods, which he needs. Capital in his view is a means of diverting the factor of production to new uses or of dictating a new direction of production. Nurkse observed that capital is a necessary but not a sufficient condition of progress.

The overall objective of development banks in our country, as stated above, is to cover gaps of capital and enterprise. With this end in view these institutions supplement rather than supplant those providing long-term financial support and entrepreneurial and managerial assistance to all the deserving projects whose access to the existing facilities was limited and which, because of this fact, would be likely to be held up. Such assistance was provided for fostering the growth of new industrial projects of national
importance and for the modernization, expansion, renovation and diversification of existing projects. Financial assistance is provided mainly:

(a) To provide term lending facilities;
(b) To subscribe to shares and debentures;
(c) To underwrite security issues of industrial concerns;
(d) To guarantee term loans raised by industrial concerns;
(e) To extend guarantees in respect of deferred payments by importers who are able to make such arrangements with foreign manufacturers.

In recent years all-India development banks have helped industrial enterprises to raise funds by way of rendering financial services such as merchant banking, leasing, venture capital, etc.

1.6 Role of NBFIs (Non-Banking Financial Institutions) in Industrialization

Development bank or Non-Banking Financial Institutions (NBFIs) is an institutional mechanism, which functions as an active agent for promoting a balanced and viable process of economic development. Development bank working in any economic setup gives shape to its functions and forms accordingly. Types, functions, ownership and policies of development banks vary to such an extent that it is hard to define development bank. Diversity of functions provides one basis of defining development bank. **J.T. Dock Houk** in his book, ‘Financing and Problems of Development Bank’ adopted functional approach to define development bank. Development bank has been defined as an institution, which undertakes to perform banking functions as well as
development functions. Banking functions are like—provision of medium and long-term capital to economic development projects, — investment in equity of a borrower—guaranteeing of loans by a third party to borrower—underwriting of attempts by borrowers to raise equity and debentures—financial contacts both within and outside the country, whereas development functions include, inter alia—overcoming shortage of viable projects—development of business skill—fostering a capital market.

On the other hand E.T. Kaupier in his work 'The Promotional Role of a Development Finance Company' has attempted to define development bank by distinguishing and demarcating it from commercial banks. S.L.N. Sinha in his book observed that "Development Banks in fact are something more than pure financial institutions. They are, to an extent, development agencies". Diamond has called a development bank "a financing institution to promote and finance enterprise in private sector".

The modern concept of a development bank is closely related to the urge on the part of a backward and underdeveloped country to achieve a quick rate of all-round economic development and its search for an appropriate instrument through which such development can be promoted and financed.

Thus main functions of these banks can be divided into two parts—financial and developmental.

(a) Financial Functions

The conventional function assistance has diverse forms. The charter of development bank specifies the assistance it can render like fixed interest bearing loan, subscribing and underwriting of shares and debentures, convertible loans, etc. Some of these banks provide capital either in the form of loan or equity. In underdeveloped countries larger
number of these banks provides equity as well as loan facilities. British FCI, IFCI, ICICI, Development Finance Corporation of Ceylon, Industrial Development Corporations of Burma and Ghana are some of such banks which provide equity capital as well as loan facilities.

Development banks provide loans both in foreign or/and local currencies. IDB of Turkey, IDB of Pakistan, Japan Development Bank is some of such banks, which provide both types of loans. Development banks provide generally long and medium term loans only whereby for working capital other sources are to risen to provide working capital thus also act as commercial banks like Nepal Industrial Development Corporation and National Credit Bank of Laos.

More conscious of earning and less of security, some development banks provide equity capital. Equity capital is more appropriate type of assistance by development banks. What industry requires is not only loaned capital but risk capital is also needed to rise faster. Sometimes even a token participation in equity of client’s project is more then sufficient as even a modicum of such participation inspires the confidence of investors. ‘Philippines National Development Company’ is one of such development banks, which provide only equity capital. The ability of these banks to participate in risk capital depends on development of capital market and circumstances of the country. Certain development banks are circumstances of the country. Certain development banks are not authorized to provide equity capital. State Financial Corporations in India are examples of such type of development banks.

Underwriting is another related financial facility provided by almost all development banks. Some banks, even though permitted by their statute to underwrite, yet do not
undertake this activity and 'Commonwealth Bank of Australia' is one of such development banks. While undertaking this proposal, banks view the fact that in case the whole issue is not taken up by the public it may be lift with a fairly large amount which has to be disposed off eventually by the bands on the emergence of favorable market conditions. In terms of the provisions and constraints of statutes, some bands have to dispose of underwritten shares within a specific period irrespective of the market conditions, as in the case of IFCI where such shares acquired in discharge of its underwriting obligation have to be disposed of within a period of seven years.

Still another category of financial assistance is providing guarantees of loans whether taken from domestic market or from foreign sources, deferred payments for import of machinery etc. Sometimes development banks undertake guaranteeing the issue of client's securities as well as the obligations of other financial institution to encourage them to participate in industrial finance. Nepal Industrial Development Corporation, ICICI, IDBI and IDB of Canada are some of the banks, which undertake and perform guaranteeing function.

Investment lies at the hearts of economic development and to boost up investment activities prosperous capital market is an essential pre-requisite. In underdeveloped countries capital market is sluggish as incentives for savings in multiple new ways are lacking. Development banks in such countries also perform the function of developing capital market. These banks induce capital market by various means like-sale of investment from own portfolio-sale of industrial securities accompanied and supported by its guarantees-equity participation-sale of its own obligation to public. Depending on the investment environment, contribution of such banks to this end varies in different
countries. For a developing country, sale of investment from its own portfolio may be more useful as in this way development band turns out to be developer of securities as well as of market. It is helpful to revive moribund capital market.

(b) Developmental Functions

Diamond in his lecture in the series “Silver jubilee Memorial Lectures IFCI” observed that “the ‘developmental role’ of a development bank is precisely that mix of a functions or tasks which called for linking the words ‘Development’ and ‘Bank’ together and which justified governments in sponsoring and financing them.” Recognizing the fact that financial assistance alone cannot ensure the industrial development. Development banks simultaneously undertake developmental or promotional functions. Need of such functions, which go beyond the traditional functions of development banks, was felt urgently by underdeveloped and developing countries. A development bank must, in addition to its banking function attempt to relate to certain problems of, or bottlenecks to, development, the magnitude and importance of which may vary from country to country. The bottlenecks envisaged are critical shortage of viable projects, lack of business skill, fostering a capital market and implementation of development plans.

Diamond also observed that promotional function involves the formulation and development of a proposal, the mobilizing and organization of the various elements those are needed to give life to it and actively assisting in its execution.

But a development bank need not undertake the entire process itself. What is needed is that these banks should only support and should help a half baked inadequate proposal to be transformed into a well conceived, well planned, financially well
disciplined enterprise so that it becomes profitable to investors as well as to the economy.

These banks in developing and underdeveloped countries undertake the following promotional measures:

(a) Identifying and motivating the entrepreneurs, as they are chief forces in development process: From masses of aspirants identify them and then train and motivate them.

(b) Revealing the industrial gaps: These banks must have a continuous system of identifying the opportunities where prospective entrepreneurs can enter.

(c) Preparation of feasibility studies and project reports: For small units and new aspirants these banks are of great use in this regard as such parties rarely take benefits of consultants.

(d) Suggest improvements in submitted proposals: The proposals coming for assistance to such bands are polished further in light of their experience and expertise.

(e) Providing technical, managerial and administrative advice to clients so as the floated projects can prosper.

(f) Guidance and assistance to businessman: After a project has commissioned it may face difficulties on account of demand constraints, finance etc. These banks act as guides and assistants in such conditions and also when there is proposal for expansion or diversification.
Promotional functions to a great extent are decided by the present situation of the economy and developmental policies of government. Non-Banking Financial Institutions (NBFIs) as a potential instrument of economic growth must be very dynamic. These should not forget that their business goes far beyond the daily bread and butter of providing capital on a 'yes' or 'no' basis to entrepreneurs who apply for it. The impact of promotional activities is felt only in the long run and their effectiveness depends on availability of other ingredients of investment. H.E. Bachem (Member, Board of Management KFW, Federal Republic of Germany) observed that "It may be said with a claim to generality that a 'Development Bank ' which deserves its name legitimately, will give priority to development objective, while other selection criteria, though not excluded at all, will clearly range second to the aims of development policies.

NBFIs have made to function within the broad framework laid down by a country to achieve her economic objectives. Technique of development banking has been adopted by different countries for their economic uplift. Variations in emphasis in different economic can be well understood, obviously resulting in corresponding variations in the role of these banks in different economies.

The role of NBFIs differs between an advanced economy and an underdeveloped economy. In the case of the former, 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 & they have no problems of "take-off into the phase of self-sustained growth". This the development banks do by collecting small savings from a
large number of people spread over a wide area, allocating the funds so collected among different sectors for maximum return with the help of their technical and financial expertise and in this process reducing the risk of the investors. In an advanced economy, save in some exceptional cases, the development banks are not required "to fill up the gaps in the industrial structure of the economy."

Financial institutions play a significant role in economic development through capital formation. Development banks can influence the investment pattern by increasing investment factor and set the pace for additional investment. Development of entrepreneurship and managerial capacity are other important ingredients for economic uplift. These banks certainly have prominent role in this field. Labor productivity also influence the process of economic development. The non-banking financial institution through training programme and inducing the assisted units to apply better labour management techniques can achieve the object of high labour productivity. Besides increasing labour productivity, development banks are instrumental in enhancing productivity of investment by guiding the entrepreneurs about latest technology for production and management and assisting them in proper implementation of projects. A net resultant of increased productivity is increased income and it ultimately increases savings of the economy, which is another ingredient of economic development. Development banks can also give a boost to the export business of the country by increased production, quality and quantity-wise. These agencies of government or otherwise can plan, promote and develop industrial organization in the economy. This all highlights, in nutshell, the position of development banks in the context of economic development of the economy.
Development being the function of capital, as the tempo of development grows, so does the requirement for capital. The need for capital is continuous and also boundless. However, capital, is not only necessary for development but capital is also generated by development. Economic progress creates its surpluses with which further development is achieved, often at an accelerated rate. India's five year-plans are a proof in them that substantially larger resources used in each successive plan came from the economic growth resulting from investment in the preceding plans. Only a relatively small part of the resources came from external sources though they were crucial to development.
1.7a Structure of All Non-Banking Institutions (NBFIs) in India

Chart 1.7.1 showing organisation structure of financial institutions in India.

Organizational Structure of Financial Institutions

All Financial Institutions

All India Financial Institutions

State Level Institutions

Other Institutions

- All India Development Banks
  - IDBI (1964)
  - ICICI (1955)
  - SIDBI (1990)
  - RBI (1997)
  - IFCI (1948)

- Specialized Financial Institutions
  - EXIM Bank (1982)
  - IVCF (formerly)
  - RCTC (1988)
  - ICICI Venture
    - (formerly TDICI)
    - (1988)
  - TFCI (1989)
  - IDFC (1997)

- Investment Institutions
  - UTI (1964)
  - LIC (1956)
  - GIC & subsidiaries
    - (1972)

- Refinance Institutions
  - NABARD (1982)
  - NHB (1980)

- SFCs
  - (18)

- SIDCs
  - (28)

- ECGC
  - (1957)

- DICGC
  - (1962)

Source: Bankers India May 2002
1.7 a (i) Industrial Finance Corporation of India (IFCI)

Industrial Finance Corporation of India (IFCI) was established in 1948 with an objective to make medium and long-term funds more readily available to industrial concerns particularly in those circumstances in which banking accommodation is inappropriate or recourse to capital market is impractical.

The authorized capital of the IFCI is the Rs. 20 crores. Fifty percent of the paid-up capital now standing at the Rs 10 crores in held by the Industrial Development Bank of India (IDBI). scheduled banks, cooperative banks, insurance concerns and investment trusts, etc hold the remaining 50 percent.

**Management**

The Board of Directors consists of a whole-time Chairman and twelve directors. The Chairman is appointed by the Central Government after consultation with the IDBI. Six Directors are elected by shareholders other than the IDBI.

**Functions and Lending Policies**

Any limited company or co-operative society incorporated and registered in India which is engaged, or proposes to engage itself, in the manufacture, preservation or processing of goods, or in the shipping, mining or hotel industry, or in the generation or distribution of electricity or any other form of power, is eligible for financial assistance.

Public sector projects are also eligible for financial assistance from the Corporation on the same basis as industrial projects in the private and joint sectors.

The assistance may take the form of long-term loans, both in rupees and foreign currencies, the underwriting of equity, preference and debenture issues; subscribing to
objectivity, preference and debenture capital; guaranteeing of deferred payments in respect of machinery imported from abroad or purchased in India; and guaranteeing of loans raised in foreign currency from foreign financial institutions. Financial assistance from the Corporation is available for the setting-up of new industrial projects and for the expansion, diversification, renovation or modernisation of existing ones. Financial assistance on confessional terms is available for the setting-up of new industrial projects in industrially less developed districts in the States/Union Territories notified by the Central Government.

1.7a (ii) The Industrial Development Bank of India (IDBI)

The Industrial Development Bank of India (IDBI) was established on 1st July 1964 under the Industrial Development Bank of India Act, 1964, as a wholly owned subsidiary of the Reserve Bank of India. In terms of the Public Financial Institutions Laws (Amendment) Act, 1975, the ownership of the IDBI has been transferred to the Central Government with effect from 16th February 1976. The most distinguishing feature of the IDBI is that it has been assigned the role of the principal financial institution for coordination, in conformity with national priorities, the activities of the institution engaged in financing, promoting or developing industry. The IDBI has been assigned a special role to play in regard to industrial development.

Objectives & Functions
1.7 a(iii) The Industrial Credit And Investment Corporation of India (ICICI)

The Industrial Credit and Investment Corporation of India (ICICI) was sponsored by the World Bank to render financial assistance to medium and small scale industries. It was established in 1955 with an authorized capital of Rs. 25 crores and subscribed capital of Rs. 5 crores. Indian commercial banks, individuals and business corporations in the USA, the British banks, other companies and the general public have subscribed its capital.

Finance for Industry

Over the past thirty years, the ICICI, in pursuit of its objective of promoting industrial development, has provided financial assistance in various forms, such as:
(a) Underwriting of public and private issues and offers of sale of industrial securities
- ordinary shares, preference shares, bonds and debenture stock;
(b) Direct subscription to such securities;
(c) Securing loans in rupees, repayable over periods up to 15 years;
(d) Providing similar loans in foreign currencies for the payment for imported capital
equipment and technical services;
(e) Guaranteeing payments for credits made by others;
(f) Providing credit facilities to manufacturers for the promotion of the sale of
industrial equipment on deferred payment terms.

The primary purposes for which assistance is extended is the purchase of capital assets
in the form of land, buildings and machinery. Of the alternative types of assistance
providing by the ICICI, the one best calculated to assure the success of enterprises is
chosen in each case.

Any company with a limited liability (or the promoter of such a company), any sole
proprietary concern, partnership firm or any co-operative society may approach the
ICICI for assistance in financing a sound proposal for the establishment, expansion or
modernization of an industrial enterprise.

The applicant may be an Indian or foreigner; his plans may provide for investment in
any part of India; he may require assistance in any form. He must, however, be
prepared to make a reasonable contribution to the resources required for the
implementation of his proposal. The enterprise should have, or should undertake to
obtain, experienced management and expert technical personnel and advice. Special
consideration is given to projects promoted by new entrepreneurs and those who desire to set up industries in backward areas.

There are no firm limits to the size of the enterprises the ICICI is prepared to assist, nor is there a maximum or a minimum limit to the assistance that it may offer. In practice, the lower limit of the finance provided by the ICICI is set at Rs. 5 lakhs because there are other institutions, which provide assistance for smaller amounts. However to meet the requirements of industry for loans in foreign currency, the ICICI may offer assistance below this limit. At the upper end, prudence requires that it limit the proportion of its resources which it can safely invest in a single enterprise. However, no proposal is too large for the ICICI to handle; it is prepared to enlist the co-operation of other financial institutions, in India and abroad, to share in the investment.

In promoting industrial investment, the ICICI is anxious not only to invest, but also to encourage others to invest. Accordingly, it seeks to encourage other financial institutions and individuals, both Indian and foreign, to co-operate with it in its investment and lending operations.

In order to promote new industries, to assist in the expansion and modernisation of existing industries, and to furnish technical and managerial assistance, the ICICI grants long-term loans, subscribes to shares, underwrites new shares and debentures, guarantees loans from other private investment sources, and provides managerial and technical advice. ICICI also provides assistance by way of supplier's credit, equipment leasing, and installment sale and venture capital and renders merchant banking services. Technology Development and Information Company of India Ltd. (TDICI), establishment by ICICI in 1988 provides technological information and finances
technology intensive development activities including commercial R & D schemes. It also manages the venture capital fund of Rs. 20 crores that ICICI had established along with UTI in 1988.

1.7a(iv) Industrial Reconstruction Bank of India (IRBI)

Industrial Reconstruction Bank of India (IRBI) was constituted by the government of India in March, 1985 to act as the principal credit and reconstruction agency for reconstruction and rehabilitation of sick industrial units through assistance for their modernization, diversification, expansion or rationalisation and for co-ordinating of similar work of the other institutions enjoyed therein.

1.7a(v) Small Industries Development Bank of India (SIDBI)

The Small Industries Development Bank of India (SIDBI) was set up as a wholly-owned subsidiary of IDBI by an Act of Parliament in 1989. The SIDBI commenced its operations from April 2, 1990. The basic idea underlying the formation of the SIDBI was to foster the growth of small scale sector which occupies a pivotal position in Indian economy. Thus, the Bank has been assigned the role of the principal financial institution for promotion, financing and development of industry in the small, tiny and cottage sectors and to coordinate concentrated attention to the multi-dimensional growth and development of industries in the small scale sector, with special emphasis on the village, cottage, and tiny sectors.
Initially, SIDBI business comprised refinancing to term loans granted by SFCs, SIDCs, banks and other eligible financial institutions; direct discounting and rediscounting of bills arising out of sale of machinery/capital equipment by manufactures in the small scale sector on deferred credit and rediscounting of short-term trade bills arising out of sale of products of the small scale sector.

At present SIDBI renders equity type of assistance to special target groups like new promoters, women and ex-servicemen under National Equity Fund, and voluntary agencies working for development/to the upliftment of underprivileged women. It also provides resource support to NSIC and SSIDCs for their material supply and marketing of SSI products as well as their hire-purchase and leasing activities. For promotion, development and growth of small scale sector, SIDBI extends technical and related support services.

1.7a(vii) State Financial Corporations (SFCs)

State Financial Corporations (SFCs) have been set up to provide firm finance to medium and small industries in the 18 states. In the last new years, they have also been entrusted with the task of providing assistance to those entrepreneurs who are willing to set up industries in backward areas. The recent trends in the working of 18 SFCs show that they are moving towards these objectives at an accelerated pace.

1.7a(viii) State Industrial Development Corporations (SIDCs)
During 1960s different State Governments, in their frantic desire to accelerate the pace of industrial development in their territories, established Industrial Development Corporations. The Andhra Pradesh and Bihar Governments took the lead and set-up such corporations in 1960. They were followed by U.P. and Karnataka (in 1961), Maharashtra, Gujarat and Orissa (in 1962), Mysore (in 1964), Madhya Pradesh and Madras (in 1965), and Punjab (in 1966). In the subsequent years, the governments in other States realized the importance of SIDCs/SIICs and organised them in their States. Presently, there are 26 SIDCs operating in different States.

There are at present 28 SIDCs in the country, 11 of them functioning also as SFCs to provide assistance to small scale sector and to act as promotional agencies such firm – function SIDCs are in Andaman & Nicobar, Arunachal Pradesh, Daman & Diu and Dadra & Nagar Haveli, Manipur, Meghalaya, Mizoram, Nagaland, Tripurs, Goa, Pondichery and Sikkim. Seven SIDCs are also involved in infrastructure development and other extension services for the small sector.

Though wholly owned by State Governments, the SIDCs have been incorporated either as limited liability companies under the Indian Companies Act, or as autonomous corporations under specific State Acts. This arrangement has given the SIDCs a sufficient measure of flexibility in their operations.

Subject to overall guidance by State Governments, the affairs of the SIDCs are conducted by a Board of Directors nominated by the State Government. Wherever necessary, special committees have been set-up to advise the Board on the conduct of the business of the Corporation. The day-to-day management is entrusted to the managing director, who is the Chief Executive of the Corporation. In many SIDCs, the
managing directors have also been vested with limited powers of approval/disbursal of assistance.

1.8 Major Non-Banking Financial Institutions in India at a Glance

Table 1.1.1 showing NBFIs in India with their forms of organisation & year of establishment

<table>
<thead>
<tr>
<th>Sr. No.</th>
<th>Name of Institution</th>
<th>Abbreviation</th>
<th>Year of Establishment</th>
<th>Form of Organisation</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>Industrial Development Bank of India</td>
<td>IDBI</td>
<td>July 1, 1964</td>
<td>IDBI Act, 1964</td>
</tr>
<tr>
<td>2</td>
<td>Industrial Finance Corporation of India</td>
<td>IFCI</td>
<td>July 1948</td>
<td>IFCI Act, 1948</td>
</tr>
<tr>
<td>3</td>
<td>Industrial Credit and investment Corporation of India ICICI</td>
<td>ICICI</td>
<td>January 5, 1955</td>
<td>Public Limited Company</td>
</tr>
<tr>
<td>4</td>
<td>Small Industries Development Bank of India</td>
<td>SIDBI</td>
<td>April 2, 1990</td>
<td>SIDBI Act, 1989</td>
</tr>
<tr>
<td>5</td>
<td>Shipping Credit and Investment Corporation of India SCICI</td>
<td>SCICI</td>
<td>December, 1986</td>
<td>Public Limited Company</td>
</tr>
<tr>
<td>6</td>
<td>Tourism Finance Corporation of India</td>
<td>TFCI</td>
<td>February, 1989</td>
<td>Public Limited Company</td>
</tr>
<tr>
<td>7</td>
<td>Industrial Reconstruction Bank of India</td>
<td>IRBI</td>
<td>1985</td>
<td>IRBI Limited Company</td>
</tr>
<tr>
<td>8</td>
<td>Risk Capital &amp; Technology Finance Corporation of India RCTFCI</td>
<td>RCTFCI</td>
<td>January, 1988</td>
<td>Former RFC of IFCI set up in 1975</td>
</tr>
<tr>
<td>9</td>
<td>Technology Development and Information Company of India Ltd</td>
<td>TDICI</td>
<td>July 1988</td>
<td>Public Limited Company</td>
</tr>
<tr>
<td>10</td>
<td>State Finance Corporations SFCs</td>
<td>SFCs</td>
<td>1951</td>
<td></td>
</tr>
<tr>
<td>Sr.No.</td>
<td>Institution</td>
<td>Main Objectives</td>
<td></td>
<td></td>
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<td>-------------------------------------------------</td>
<td>--------------------------------------------------------------------------------</td>
<td></td>
<td></td>
</tr>
<tr>
<td>1.</td>
<td>IDBI</td>
<td>Main objective is to serve as the apex institution for term finance for industry by providing direct and indirect assistance and also to coordinate the working of other DFIs in the country.</td>
<td></td>
<td></td>
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<tr>
<td>2.</td>
<td>IFCI</td>
<td>Basic objective is to make medium and long term credit more readily available to industrial concerns in India.</td>
<td></td>
<td></td>
</tr>
<tr>
<td>3.</td>
<td>ICICI</td>
<td>Primarily for financing the foreign exchange component of industrial projects and for promoting industrial enterprises in the private sector by way of term financial assistance.</td>
<td></td>
<td></td>
</tr>
<tr>
<td>4.</td>
<td>SIDBI</td>
<td>Principal Financial Institution for promoting and financing small industry and to coordinate the functioning of institutions engaged in similar activities.</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>
5. **SCICI**

It is nodal agency for assisting shipping, fishing and related industries in the form of rupee and foreign currency loans etc. It acts as agent and renders advisory services for shipping and related activities.

6. **TFCI**

Provides financial assistance for the development of Tourism and Tourism related activities.

7. **IRBI**

Principal Agency for Assisting rehabilitation of sick and closed industrial units. It also provides various forms of financial assistance to healthy units also.

8. **RCTC**

Provides risk capital assistance to first generation entrepreneurs on soft terms and assistance for commercialization of new technologies.

9. **TDICI**

Primarily to provide project loans (venture capital) direct subscription, etc. to small and medium scale projects conceived by technocrat interpreters including first generation entrepreneurs to provide R & D funds, technology and information.

10. **SFCs**

Provision of medium and long term financial assistance by way of term loans, underwriting, etc. to small and medium scale units, renders promotional services for entrepreneurs in small and medium scale sectors.

11. **SIDCs**

Grant of financial assistance, direct promotion of medium and large industrial units. Provision of technical services etc.

12. **UTI**

To mobilize savings of community, particularly small and medium income group of savers by way of sale of units and channelise the savings into productive investment.
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<tbody>
<tr>
<td>13.</td>
<td>LIC</td>
<td>Exclusively managing the life insurance business and deploying the funds of the policy holders within the framework of Government guidelines.</td>
</tr>
<tr>
<td>14.</td>
<td>GIC</td>
<td>Operates a number of insurance schemes to suit the needs of the society and channelizes invisible funds to various sectors including industry.</td>
</tr>
<tr>
<td>15.</td>
<td>DICGC</td>
<td>To provide insurance protection to small depositors in banks and providing guarantee cover to credit facilities extended to certain categories of small borrowers particularly those belonging to weaker sections of society and small scale units.</td>
</tr>
<tr>
<td>16.</td>
<td>ECGC</td>
<td>To offer financial protection to the exporters for improving their financial standing vis-à-vis his bankers. It provides two types of services: i. Export Credit Insurance; and ii) Export Credit Guarantee.</td>
</tr>
</tbody>
</table>

**Source:** Compiled from annual reports of respective NBFIs
References


Development Banking Centre, Selected Readings in Development Banking, New Delhi, 1982.


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**ARTICLES /REPORTS**


