CHAPTER 7

OTHER FINANCIAL INSTITUTIONS AND

IDBI
Development banking in India has had its genesis in the post independence period. In 1947, the country had the network of commercial banks only, which catered to the short term working capital requirements of trade and industry. The need was therefore, felt for the establishment of development banks to provide medium and long term finance for industry. The first development bank in the country – Industrial Finance Corporation of India (IFCI) was set up in circumstances where normal banking accommodation was in appropriate or recourse to capital issue method impracticable. The country today possesses a fine network of development banks, which have significantly contributed to the industrial development in the country.

AN OVERVIEW

IDBI was setup by an act of parliament as the principal financial institution in the country. IDBI through it’s various schemes of direct finance, refinance of industrial loans and bills finance assistance, caters to the growing and diverse needs of medium and large-scale industrial sectors. While assistance to small sectors is provided by it’s wholly owned subsidiary SIDBI, IDBI also extends resource support to all India and state level financial institutions and other intermediaries. Besides, IDBI is entrusted with the task of undertaking promotional activities for stimulating industrial development.
INDUSTRIAL FINANCE CORPORATION OF INDIA (IFCI)

IFCI was set up in 1948 under the Industrial Finance Corporation Act 1948 for the purpose of providing medium and long term finance to industry. Besides providing assistance by way of project finance it also extends financial services like equipment leasing, equipment procurement, buyer’s and supplier’s credit, finance to leasing and higher purchase concerns etc. It also provides merchant banking services. It also helps industrialization through a range of promotional activities.

The main object of the corporation is to render financial assistance to large scale industrial concerns, particularly when, ordinarily the bank accommodation does not suit the concern, or finance cannot possibly be raised by the issue of shares. The IFC Act defines an industrial concern as public limited company or cooperative societies, which is engaged in the manufacture, preservation or processing of goods, generation or distribution of electricity, and other forms of power, or mining or hotel industries. Thus, non-manufacturing concerns, private limited companies, partnership or sole – traders cannot get assistance from the corporation. State owned undertaking incorporated as public limited companies could also apply for assistance from the corporation under an announcement made in August 1970.

The IFCI generally deals with requests for loans for Rs. 30 Lac and more. The assistance of IFCI may take the following forms:

- Guaranteeing of loans or debentures raised or issued by companies floated publicly. The corporation can also guarantee loans raised from scheduled banks or state co-operative banks.

- Granting of loans or subscribing to debentures of approved industrial concerns. The corporation may convert part of such loans or debentures into equity at its option.

- Underwriting of the issue of shares or debentures.
- Subscribing directly to the shares of companies eligible for assistance.

- Guaranteeing deferred payments by importers of capital goods who are able to obtain such concessions from foreign manufacturers. The corporation can guarantee deferred payments for capital goods manufactured in India. Such guarantee can also be given for loans raised from foreign banks or financial institutions in foreign exchange. Prior approval of the central government is however, necessary for such arrangement.

- Acting as an agent of the central government and the World Bank in respect of loans sanctioned by them to industrial concerns.

The maximum amount, which can be given as loan to any industrial concern, is Rs. Two crore or 10% of the paid up share capital of the corporation, and the maximum period of a loan can be 25 years. Loans cannot be made unless proper security is given to the corporation through mortgage on the company’s property, or through hypothecation or assignment of securities, stocks, shares, debentures, bullion etc. If the corporation is called upon to subscribe to shares underwritten by it, such shares must be disposed off within seven years.

As to the purpose, for which loans may be sanctioned, the corporation’s assistance is meant for the establishment of new industrial undertakings, as well as for expansion, modernization and rehabilitation of existing ones. Loans for repayment of existing liabilities are given only in exceptional cases.

Interest is charged on the amount actually withdrawn. A commitment fee of 1% is charged on the amount sanctioned but not withdrawn. The rate of interest charged by the corporation has been progressively increased. The rate of interest is 15% P.a. with a rebate of 1% for punctual payment.
Forms of assistance: -

The Industrial Finance Corporation of India’s assistance to industrial concerns is in several forms.
- Providing long term loans, both in Rs. and foreign currencies.
- Underwriting of equity, preference and debenture issues.
- Subscribing to equity, preference and debenture capital.
- Guaranty of deferred payments in respect of machinery imported from abroad and purchased in India.
- Guaranteeing of loans raised in foreign currencies from foreign sources.

Terms of lending: -

The interest rate on rupee and foreign currency loans is 15% P.a. with a rebate of 1% for punctual payment. An additional charge of 2% P.a. is payable by way of liquidated damages for defaults in payment of principle and/or interest payable half yearly. Loans are generally repayable in equal half-yearly installment over a period of 5 to 12 years, depending on the profit capacity and cash flow position of the borrower. The repayment begins after an initial growth period of 2 to 3 years. A commitment charge of 1 % is levied on the unutilized portion of the loan after the prescribed period. Loans are generally secured by a first legal mortgage of all the fixed assets of the borrower, both existing and potential.

1 Under the act the IFCI could provide medium and long term credits to public limited companies and cooperative societies, particularly, in the circumstances where the rural banking accommodation is in appropriate or recourse to capital issue method is impracticable. Its assistance was meant for public limited companies and cooperatives engaged in the manufacture of goods, or generation or distribution of electricity and other forms of power and mining, shipping and the preservation of foods. Therefore private companies, partnerships and sole traders could not get financial assistance from it. However, by an amendment to the Act, now it is possible for private limited companies to get financial assistance from the corporations.

The Industrial Finance Corporation of India extends assistance to public limited companies, cooperative societies and public sector firms that are engaged in/or, which propose to engage in the different activities.
Sanctions of assistance:

When the corporation receives an application for loan, it is first examined by its technical and financial staff, which ascertains the soundness of the project. The views of the advisory committee in the particular industry are also obtained. As the Corporation has limited funds at its disposal, it wants to see that the loan is not only properly secured but also profitably used for the industrial development of the country. Therefore it is very careful in judging and evaluating each project before granting assistance. In taking decisions, the corporation keeps in view the following considerations:-

- Importance of the industry in the country.
- Feasibility of the project.
- Profit earning capacity.
- Availability of raw materials.
- Availability of the services of technical persons.
- Competence and experience of the management.
- The extent to which the assistance is likely to help the company in increasing its efficiency.
- Reputation of the company’s products.
- Security offered by the company.
- The position of demand and supply in the industry, concerned.

A company applying for finance from the corporation has to adopt a specific procedure.\(^1\) The corporation also sends its officials to access the progress of the project and also appoints its nominees on the board of directors of the borrower company in order to keep in touch with the project.

---

\(^1\) The Company has to submit an application for the loan along with complete financial and technical details of the proposed project. On receipt of the application the financial and technical staff of the corporation will scrutinize it to ascertain the financial and economic soundness of the profit. Then the board of directors of the IFCI takes the decision on the basis of the recommendations of the advisory committee. Thereafter the company is required to execute a loan agreement. After a loan is sanctioned the Borrower Company has to furnish securities for the loan. Then the loan amount is dispersed (usually in installments). The Borrower Company is required to send regular progress reports to the corporations.
PROMOTIONAL ACTIVITIES

IFCI has played an important role in financing projects in less developed areas. A scheme of concessional finance has liberalized and enlarged in recent years particularly industrial projects located in less developed areas irrespective of their capital cost.

IFCI has created a benevolent reserve fund to undertake various promotional activities that consist of conducting surveys, commissioning feasibility studies, setting up consultancy organizations etc. IFCI has sponsored management development institute. This institute inter-alia: - 1) Imparts training to the clients of IFCI, particularly new entrepreneurs and technocrats. 2) Conducts programs in development banks for the staff of various financial institutions and 3) Offers training programs on identification, promotion and implementation of industrial projects (IPIIP) for the officials of state governments and state level development agencies, industrial credit and investment corporations of India (ICICI).

IFCI CONVERTED INTO IFCI LTD.

For ensuring greater flexibility and an ability to IFCI to respond to the needs of the changing financial system, and enactment called the Industrial Finance Corporation (Transfer of undertaking and repeal) Act, 1993 was passed on 2nd April, 1993. Pursuant thereto, the IFCI Ltd. was incorporated as a company under the companies Act, 1956 on 21st May 1993 and certificate of commencement of business was issued on 24th June 1993. As per the notification issued by the Government of India on 7th June 1993, the undertaking of IFCI under IFCI Act 1948 stands transferred to and kept in the aforesaid Company with effect from July 1st, 1993. IFCI is the first institution in the financial sector in India to be converted from statutory corporation into a public Ltd. company under the Indian Companies Act, 1956. Every shareholder of IFCI became the shareholder of the Company with effect from the same date i.e. 1st July 1973.

Under the IFCI Act, 1948, IFCI was prohibited to enter into the capital market. As a joint stock company IFCI is now able to enter the capital market for resources, through debt and equity instruments.
RESOURCES OF IFCI

*Share Capital:* The authorized share capital of IFCI is Rs.1000 crore divided into equity shares of Rs.10 each. In 1996, 10% of this amount has been converted into cumulative redeemable preference shares of the face value of Rs.10 each.

The paid up capital as on 31st March, 1996 was 352.59 crore, out of which Rs.202.5 crore was allotted to erstwhile Industrial Finance Corporation in exchange of its shares. The balance was issued to public in 1993.

*Borrowings:* IFCI’s main dependence for funds has been on borrowings both within the country and outside. The principle source of rupee borrowings has been the Bonds issued by IFCI carrying Government guarantees. After the conversion of IFCI into a company, it has raised funds in the capital markets on market related terms by way of certificates of deposits, Bonds, fixed deposits and other borrowings.

**IFCI’s MAIN ACTIVITIES:**

IFCI is not only a term lending institution, but an active financial intermediary and a provider of a wide range of services to industry. Its main services fall under the following three broad categories:

- Project Finance.
- Financial Services (including merchant Banking and Allied Services).
- Promotional Schemes.

*Project Finance:* Project Finance is the main activity of IFCI like other development Banks. Under project finance, assistance is provided in the following ways:

1. Long term loans
2. Underwriting of equity, preference shares and debentures.
3. Subscribing to equity, preference shares and debentures.
4. Guaranteeing the deferred payments in respect of machinery imported from abroad / purchased in India.
5. Guaranteeing of loans raised in foreign currency from foreign financial institutions.
The financial assistance rendered by IFCI is meant for setting up of new Industrial projects and also for the expansion, diversification, renovation or modernization of existing ones.

**Financial Services:** Under this category, the following schemes of assistance have been introduced by IFCI.

1. Equipment Financing.
2. Equipment Leasing.
3. Equipment Procurement.
4. Installment Credit.
5. Equipment Credit
6. Suppliers' Credit and Buyers’ Credit.
7. Finance to Leasing and Hire Purchase Concerns.

These Financial services enable the existing concerns to opt for the facilities, which are most suitable and appropriate keeping in mind their specific requirements.

**Promotional Schemes:**

As part of its development role, IFCI has introduced a number of promotional schemes. 14 schemes have been devised under which various subsidies are provided to entrepreneurs desiring to start industrial activity, particularly in village, tiny and small-scale sector.

Subsidy is provided for:

- Meeting cost of feasibility studies.
- Consultancy to industries relating to Animal Husbandry, Dairy farming, Poultry farming and Fishery.
- Industries based on agriculture, horticulture, sericulture and pisciculture.
- Meeting cost of market research / surveys.
- Providing marketing assistance to small units.
- Consultancy on use of non-conventional source of energy conservation measures and subsidy for control of pollution in village and small industries sector.

7.8
IFCI has also devised schemes for encouraging entrepreneurship development in Tourism and allied activities and for encouraging self-employment amongst persons after retrenchment or rationalization in a sick industrial unit in the organized sector.

IFCI has established a Merchant Banking Division also, which renders a wide variety of services needed for the establishment of industrial enterprises. These services include project counseling, credit syndication, issue management, Debenture Trusteeships etc.

INSTITUTIONS PROMOTED BY IFCI

IFCI has promoted the following specialized institutions to cater to the needs of industry:

Risk Capital and Technology Finance Corporation Limited (RCTC):
This corporation provides risk capital to the first generation entrepreneurs and also Finance for Technology Development particularly for advancement, promotion, transfer or adoption of Technology.

Tourism Finance Corporation of India Limited (TFCI):
This corporation provides finance to Tourism, hotel and other Tourism related projects.

Management Development Institute (MDI):
This institute provides training in modern management techniques to entrepreneurs and technologists starting industries and also to executives. The institute also undertakes research in industrial and Business Management, development Banking and related matters.

Technical consultancy Organizations (TCO):
These organizations have been established in various states to provide total package of consultancy from the concept stage to the commissioning of industrial projects with special emphasis on tiny and small-scale entrepreneurs.
Tourism Advisory and Financial Services Corporation of India Ltd. (TAFSCI):

It undertakes micro level project consultancy, preparation of project
profits and building up of data Bank.

INSTITUTIONS CO-SPONSORED BY IFCI:

IFCI has also co-sponsored the following national institutions:
- Stock Holding Corporation of India Ltd.
- Over the Counter Exchange of India.
- National Stock Exchange of India Ltd.
- LIC Housing Finance Ltd.
- GIC Housing Finance Ltd.
- Entrepreneurship Development Institute of India.

INDUSTRIAL CREDIT AND INVESTMENT CORPORATION OF
INDIA (ICICI)

ICICI was established as a public limited company in January 1955 with support from
government and active participation of the World Bank. The primary objective of IDBI is to
meet the foreign exchange requirements of industrial projects and to promote industries in the
private sector. ICICI also provides project finance by way of rupee and foreign currency loans,
underwriting and direct subscription to shares, debentures and guarantees. With a view to
making available assistance to industry in different forms, ICICI has consciously diversified
it’s activities and expanded it’s financial services segments to cover leasing, asset credit
deferred credit and installment sale. It also provides merchant banking services. ICICI
sponsored the first issue of the OTC exchange of India in August 1992.

ICICI seeks to provide assistance to units in the private sector particularly to meet
their foreign exchange requirements. Although it began its operations as a wholly privately
owned institution, yet with the nationalization of life insurance business, the LIC became a
relatively large shareholder in it. Unlike other corporations this one is international, both in its
ownership and operations. Its share capital is subscribed by both India and foreign investors
from the UK and the USA.

7.10
RESOURCES:

ICICI has raised increasingly large funds in the capital market every year, both in Indian rupees and foreign currencies. The principal sources of funds are:

*Share Capital:*

The authorised capital of the corporation is rupees 500 crore. In Feb.1991, ICICI made a public issue of equity capital at a premium and during 1995-96, the corporation raised preference share capital of rupees 75 crore. The total paid up capital thus amounts to rupees 376.30 crore as on 31st March 1996. The capital has become 962.66 crore in Dec.2003 as per the details available on the website.

*Borrowings:*

The corporation’s main source of funds is the amount raised through bonds in the Indian capital markets. In the past the corporation was permitted, like other development banks, to raise resources through the government guaranteed bonds, which used to meet the Statutory Liquidity Requirements of commercial banks. But the funding pattern has changed significantly during recent years. The government guaranteed bonds which constituted 87% of ICICI’s rupee resources in 1985, accounted for no more than 30% during 1991-92*. Since 1992-93 corporation has not got any allocation from government guaranteed bonds and almost the entire requirement of resources has been raised through borrowings in the capital market. These bonds are distinct from government guaranteed bonds.

The above shift from government guaranteed bonds to market rates – related bonds has the impact on the cost of funds raised by the corporation. While the outstanding government guaranteed bonds maturing from 1998 to 2002 carry interest rates in the range of 6.5% to 9.75%, the bonds in the latter category carry interest at higher rates upto 16%. This has narrowed down the margin between the cost of funds and lending rates.

*Loans and advances from government:*

ICICI has also availed loans and advances from the Government of India, which are

in terms of agreements under World Bank Credit, for various purposes. These loans are also
eout of interest Differential Funds in terms of various agreements. Advances have also been
received by ICICI from Industrial Development Bank of India against issue of special
redeemable debentures.

*Other sources of Borrowings:*

During recent years the corporation has tapped other non-conventional sources of
funds also as follows:
- Inter-Corporate Deposits.
- Certificates of Deposits.
- Loans and Deposits from other financial institutions and banks.

*Foreign currency:*

The corporation has raised foreign currency loans in the following ways
- From multi-lateral/ bilateral credit agencies, guaranteed by the Government of
  India.
- From international banks, institutions and consortiums guaranteed by the
government of India.
- Bonds guaranteed by the Government of India in foreign currencies.
- US $ convertible bonds, convertible at premium into equity share at the option
  of the bondholders.
- US $ bonds issued at discount redeemable at Par.

**FORMS OF ASSISTANCE**

ICICI offers assistance in the form of long term and medium term loans,
both in Rs. and in foreign currencies, repayable in a period of fifteen years. In
addition the corporation offers underwriting of capital issues, subscription to equity
and preference share capital. The ICICI also offers assistance by:
1. Guaranteeing Rupee payments of loans from other sources in the case of deferred payments for capital equipment.
2. Loans in foreign currency towards the cost of imported capital equipment.
3. Managerial, technical and administrative advice and assisting in obtaining such services to the Indian industry.
4. ICICI provide assistance to units whether organized as a joint stock company, firm or a proprietorship concerns.

TERMS OF LENDING

The normal lending rate on rupee and foreign currency loan is 14%. A commitment charge of 1% is payable on the undrawn amount of the loan for the first year and beyond the first year the commitment charge is ½ %.

Loans are generally granted for a period upto 15 years. Loans are secured by a first legal mortgage of all the fixed assets of the borrower, both existing and potential. Where a project is financed jointly with other financial institutions, pari-passu charge on the mortgaged assets, is created in Favour of the other financial institutions.

ACTIVITIES OF ICICI

The present activities of ICICI are classified as below: -

<table>
<thead>
<tr>
<th>PROJECT FINANCE</th>
<th>ASSET FINANCE</th>
</tr>
</thead>
<tbody>
<tr>
<td>1. RUPEE LOANS.</td>
<td>1. ASSET CREDIT.</td>
</tr>
<tr>
<td>2. FOREIGN CURRENCY LOANS.</td>
<td>2. DEFERRED CREDIT</td>
</tr>
<tr>
<td>3. UNDER WRITING.</td>
<td>3. LEASING.</td>
</tr>
<tr>
<td>4. DIRECT SUBSCRIPTION.</td>
<td>4. SHORT-TERM</td>
</tr>
<tr>
<td>5. GUARANTEES TO SUPPLIERS.</td>
<td>NON-PROJECT FINANCE</td>
</tr>
<tr>
<td>FINANCIAL ADVISORY AND CONSULTANCY</td>
<td></td>
</tr>
<tr>
<td>BUSINESS.</td>
<td></td>
</tr>
</tbody>
</table>

The significant feature of ICICI’s operation is the significant share of foreign currency loans sanctioned by it, in the total sanctioned assistance. This has been made possible because of the facility it enjoys of raising funds in foreign currencies. The word bank has been sanctioning to it lines of credit for lending to the private industrial sector. It has raised foreign currency loans from other institutions abroad and has entered international capital markets also. Recently it has granted assistance for technology up-
gradation and modernization of balancing equipment out of word bank's lines of credit. New projects with export potentials have also been financed.

ASSET FINANCING

The ICICI has recently expended its asset financing activities. In the field of leasing of industrial equipment the corporation maintains its dominant position. The leased assets are diverse in nature and include various types of plant and machinery. The clients include both in the medium and large-scale sectors. The corporation has written a few foreign currency leases also.

Under deferred payments financing of sale of industrial equipment, ICICI provides assistance to the suppliers of such equipment who sale their equipment on deferred payment terms.

The corporation also provides non-project-based finance for short periods mainly in the form of bridge loans etc.

DEBENTURE TRUSTEESHIP

ICICI acts as a trustee for the holders of debentures and bonds issued by the companies to the public, by way of rights or on private placement basis with financial institutions, mutual funds and others.

CAPITAL MARKET OPERATIONS

ICICI plays an important role in the development of capital market in India. It underwrites the issues of shares & debentures by companies. During 1995 – 1996 twenty-five issues of shares and debentures for Rs. 182 crore were underwritten by ICICI. Out of which Rs. 91 crore were devolved on it forming 50 % of the amount underwritten. It was due to depressed market conditions during the previous year it constituted just 4% of the amount underwritten.

The corporation also pursues a more active policy with regard to disinvestment of the investments at a good return and realizes higher capital gains. During 1995 – 96 Rs. 70.41 crore (net) were realized as capital gains.

CUSTODIAL SERVICES

The corporation also offers these services to its clients, which include foreign financial institutions, offshore funds and overseas depository banks for Euro-issues. The services rendered by it include assistance in obtaining necessary approval from regulatory bodies, besides extensive custodial functions of settlement, safe-keeping, benefit collection, corporate action and valuation of portfolio.

ADVISORY SERVICES AND CONSULTANCY
The advisory services division of the corporation provides fee based advisory services to clients in the private corporate sector and government and quasi-government organizations. The primary objective of the division is to facilitate the creation of better projects and improve the business environment. The corporation has developed a keen insight into various facets of the business environment in India and the investment opportunities available in India.

BUSINESS CONSULTANCY DIVISION

Since 1994 this division provides consultancy service to Indian corporate for restructuring their operations and reshaping their strategies to attain global competitiveness. The team of experts under this division handles various assignments.

PROMOTIONAL ACTIVITIES

In conformity with overall governmental policies, ICICI has set up a project promotion department which: 1.) Provides promotional services and assistance to individual projects on a selective basis 2.) Participates in the coordinated efforts of the state level finance and promotional agencies, nationalized banks, and all India financial institutions in identifying and developing projects and entrepreneurs in backward regions and 3.) Works with other institutions in preparing techno-economic surveys for backward states, conducting feasibility studies and implementing identified projects.

MERCHANT BANKING DIVISION

ICICI has established merchant banking division. This division:

➢ Advises clients on raising finance in a suitable manner.
➢ Provides guidance on restructuring of finances for existing companies.
➢ Assists in preparing proposals for submission to financial institutions and banks.
➢ Serves as managers to the issue of capital.

MANAGEMENT AND WORKING

The management of ICICI is vested in a board consisting of 11 directors of these 7 represent Indian shareholders, 2 British, 1 American, and 1 is nominated by the Government of India. The ICICI has a commendable record of assistance to industrial enterprise. Assistance has been provided in the form of Rupee loans, foreign currency loans, guarantees, underwriting and direct subscriptions to securities.

ICICI commenced leasing operations in 1983. The industries helped, under leasing, included textiles, engineering, chemical fertilizers, cements, sugar etc. Between 1983 & 1994 (March) ICICI had sanctioned nearly Rs. 1800 crore as leasing assistance.

Apart from these, ICICI has promoted the following companies and institutions in recent years:
Technology development and Information Company of India ltd., promoted by ICICI to finance the transfer and upgradation of technology and provide technology information.

Credit rating information services of India Ltd. set up by ICICI in association with Unit Trust of India to provide credit rating services to the corporate sector.

Program for acceleration of commercial energy research, funded by U.S.A.I.D. with a grant of US. $20 million to support selected research and technology development proposals in Indian energy sector. PACER was launched by ICICI.

ICICI introduced two new projects with the help of U.S.A.I.D i.e.,
1.) Agricultural commercialization and enterprise project with a grant of US. $20 million and,
2) Trade in environmental sciences and technologies program with a grant of US. $25 million.

STATE FINANCIAL CORPORATIONS (SFCs)

SFCs were setup under the SFCs act 1951. SFCs operating at the state level form an integral part of the development of the financing system in the country. They function with the objective of financing and promoting small and medium enterprises for achieving balanced socio-economic growth, catalyzing higher investments, generating greater employment opportunities and widening the ownership base of industry. They extend financial assistance to industrial units by way of term loans, direct subscription to equity and debentures, guaranteeing and discounting of bills of exchange. SFCs also operate a number of schemes of refinance and equity type of assistance formulated by IDBI / SIDBI. Some of the schemes, which seem worth mentioning are the schemes for artisans, special large groups like SC & ST. women, ex-servicemen, physically handicapped for transport operators, setting up of hotels, tourism – related activities, hospitals and nursing homes etc.

To sum up it can be said that although economic growth is visualized since second world war Indian economy experienced the essence of it only after first and second five year plans. Economic growth has been widely accepted by economists as a major goal of national policy in both the industrialized as well as developing countries. Experts have left no room to bring out the definition of economic growth. Difference in their style of representation is obvious but there seems a little dissimilarity as all of them adept to comply with economic
growth in order to increase national income. Observing the definitions from close corners it is said that the economic growth implies long-term rise in per capita national output and national income, without affecting the face value and intrinsic value of the currency in an economy. Economic growth is keenly associated with capital, which constrained capital formation. The process of capital formation involves three distinct but inter dependent activities such as saving, finance and investment. Effective mobilization of savings is most desirable and productive investment gives rise to capital formation in an economy.

OBJECTIVES OF SFCs

Basically the object of SFCs is to provide medium and long-term financial assistance to smaller industrial concerns. These corporations are closely modeled on the lines of the IFCI and are empowered to provide assistance for purposes of modernization, renovation, expansion and diversification. However, the scope of activities of the SFCs is wider than that of the IFCI in that there is no restriction on industrial concerns with regard to the form of business ownership and organization. Thus, they are authorized to assist public limited companies, private companies, partnership and proprietary concern. These corporations are permitted to provide assistance to industrial concerns in the following forms:

⇔ Granting loans or advances or subscribing to debentures of industrial concerns repayable within 20 years.
⇔ Guaranteeing loans raised by industrial concerns on such terms and conditions as may be mutually agreed upon but they should be repayable within 20 years:
⇔ Underwriting the issue of stocks, bonds or debentures of industrial concerns subject to their being disposed of in the market within 7 years.

It is noteworthy that SFCs are prohibited from directly subscribing to the stocks, shares, bonds or debentures of industrial concerns, except out of the special capital. A SFC is prohibited from granting any assistance to a concern whose paid-up capital and free reserves together exceed Rs. 1 crore. The under limit to the aggregate assistance that could be granted
by SFCs to any single company or cooperative society is Rs. 30 Lac and Rs. 15 Lac to all other borrower.

RESOURCES OF SFCs

The resources consist of:
(a) Share capital and reserves
(b) Borrowings
   (i) Bond issues
   (ii) From Reserve Bank of India, scheduled banks, institutions and also by the members of the public,
   (iii) From the State Governments, and
   (iv) Re-finance from the IDBI, and
(c) Fixed deposits.

The authorized capital of the SFCs ranges between Rs. 1 crore and Rs. 5 crore. The members of the public cannot hold more than 28 percent of the shares. The shares are to be guaranteed both with regard to principal and interest by the State Government concerned. For the purpose of augmenting the resources, bonds and debentures can be issued in consultation with the Reserve Bank of India under the overall condition that the total liabilities of a corporation should not exceed 5 times its paid-up capital and reserves. Public deposits for a period of not less than 5 years and up to an amount equal to the paid-up capital of a corporation can also be accepted.

OPERATIONAL POLICIES

Some of the salient features of the operational policies of the SFCs are:
(1) Assistance to small and medium enterprises on liberal terms, such as the requirements of margin, rates of interest and period of loans, and so on.
(2) Assistance to backward areas with a view to promoting a more balanced regional distribution of industrialization.

(3) Assistance to technician entrepreneurs under the special scheme ranging between Rs. 2 Lac and Rs. 3 Lac on liberal terms. A recent development in this area is that the SFCs are providing Seed Capital assistance from their special share capital exclusively subscribed by the IDBI and the State Governments to the needy small entrepreneurs.

(4) Meeting the foreign exchange requirements of medium and small projects. This has been possible due to the sanction of lines of credit to the IDBI by the international development association (IDA). The IDA credit is available to the IDBI for re-financing loans, granted by SFCs to the industrial concerns. These loans are granted for the setting up of new projects as also for expansion, diversification, modernization, or renovation of existing units, particularly in cases where, a portion of the loan is for financing imports of equipment from abroad and/or for technical know how, in special cases.

OPERATION OF THE SFCs

The overall policy and operation of the SFCs are shaped by the RBI rulings and the respective State Governments. The equity capital of each SFC is contributed mainly by the state governments and others as stated earlier. Moreover the state government stands guarantee for the loans received by SFCs in the market and fixed deposits collected from the public.

SFCs grant loans and advances not only to public limited companies and co-operative societies, but also to private limited companies, partnerships, joint Hindu families or sole proprietor concerns, SFCs can finance both new and existing concerns, for providing working and fixed capital. Small-scale sector receives the major chunk of assistance provided by the SFCs.

A state Finance Corporation can charge commission for the services rendered by it in connection with (i) Underwriting and (ii) Guaranteeing types of business mentioned. In
case it has to retain any shares or debentures under an underwriting agreement, it must dispose
off them as early as possible but not later than 7 years from the date of acquisition.

The corporations have mostly given assistance by way of loans. The financial
assistance by a corporation is provided only when there is sufficient security by way of a
pledge, mortgage, hypothecation of Government securities, stocks or movable or immovable
property \(^1\). There is a margin of 50 percent on the security, furnished by the applicant. The
rate of interest varies between 14 to 18 percent.

**SMALL INDUSTRIES DEVELOPMENT BANK OF INDIA (SIDBI)**

In the field of financing of small-scale industries in India, a separate Apex
Development Bank started its operation from April 2, 1990. The Small Industries
Development Bank of India (SIDBI) has been set up under an Act of Parliament as the
principal financial institution for promotion, financing and development of industries in the
tiny and small scale sector. It coordinates the functions of other institutions engaged in similar
activities.

The major activities undertaken by this Bank are as follows:

- Refinancing of term loans granted by banks and other eligible financial
  institutions, namely the State Financial Corporations and State Industrial Development
  Corporations.

- Direct discounting as well as re-discounting of bill arising out of sale of
  machinery or capital equipment by manufacturers in small scale sector on deferred credit.

---

\(^1\) State Finance Corporation are now functioning almost in all the states. The bulk of the assistance sanctioned
by the State Finance Corporation went to projects of small-scale industries and particular units located in
backward areas/districts. The State Finance Corporation is playing an important role in the sphere of industrial
finance.
⇒ Equity type assistance under National Equity Fund and by way of seed capital to entrepreneurs.
⇒ Re-discounting of short-term trade bills arising out of sale of products of small-scale sector.
⇒ Resources support to National Small Industries Corporation and other institution concerned with small industries.
⇒ Share capital and resources support to factoring organizations.

Besides its share capital (Rs. 450 crore) which is wholly subscribed by IDBI, the Bank has been sanctioned limits by the Reserve Bank of India out of National Industrial Credit (Long Term Operations) Fund. Government of India has also provided its long-term, interest-free loan and also contributed to the National Equity Fund maintained by the Bank. SIDBI has also raised resources in foreign currencies from the following two sources:

⇒ OECE, Japan has sanctioned loans for on lending to small-scale units through the refinance scheme of SIDBI.
⇒ The Asian Development Bank of India has sanctioned the line of credit of US $100 million to IDBI for on lending to small-scale and medium scale units, through selected SFCs. IDBI has drawn from this line of credit against its refinance assistance to small-scale units.

In recent years IDBI has established a number of subsidiaries. SIDBI is one of them.

"IDBI BANK Ltd." established during Nov 1995 has also opened more branches, Indore & Hyderabad is important amongst them.

"IDBI CAPITAL MARKET SERVICES Ltd." is a wholly owned subsidiary of IDBI and operates in the areas of stock-broking and other related activities.

"IDBI INVESTMENT MANAGEMENT Co. Ltd." set up a mutual fund as a trust under the Indian trust act in 1994 - 95.
NEW INSTITUTIONS CO-SPONSORED BY IDBI

Besides setting up the above subsidiaries, the IDBI has co-sponsored a number of new institutions in the financial sector in India, i.e. the National Stock Exchange of India, Over the Counter Exchange of India, Discount and Finance House of India, Stock Holding Corporation of India, Credit Analysis and Research Ltd.

IDBI has thus played a significant role as institution builder in the country and is expected to play a much vital role in future for the growth and development of India’s economy.

A CRITICAL ASSESSMENT

Financial institutions are the intermediaries through which savings are pooled to put in productive capital. They help in allocation of funds between different industries in consonance with the priorities laid down in plan. Financial institutions provide both direct and indirect financial assistance to the industrial units.

There are quite a number of financial institutions that have come into existence to meet the financial requirements of industrial units. Among them IDBI, IFCI, IRBI and SIDBI are categorized under development banks, while RRTC, TDICI, SCICI and TFCI are the specialized financial institution. The investment institutions are LIC, UTI and GIC. Further SFCs and SIDCs are coming under state level financial institution.

A COMPARISON TABLE FOR A “ONCE-EYE” VIEW

<table>
<thead>
<tr>
<th>NAME OF THE INSTITUTION</th>
<th>YEAR OF ESTABLISHMENT</th>
<th>OBJECTS</th>
<th>FORMS OF FINANCIAL ASSISTANCE</th>
<th>ELIGIBILITY FOR ASSISTANCE</th>
</tr>
</thead>
<tbody>
<tr>
<td>IFCI</td>
<td>1948</td>
<td>Provision of medium and guaranteeing</td>
<td>Large-scale enterprises in the</td>
<td></td>
</tr>
<tr>
<td>SFCs</td>
<td>1951</td>
<td>Provision for medium and long-term finance to small and medium sized industries and state level.</td>
<td>Same as IFCI.</td>
<td>Industrial Enterprises in private sector organized as private companies, public limited companies, partnerships and sole proprietorships.</td>
</tr>
<tr>
<td>--------</td>
<td>------</td>
<td>------------------------------------------------------------------------------------------------</td>
<td>----------------</td>
<td>----------------------------------------------------------------------------------</td>
</tr>
<tr>
<td>ICICI</td>
<td>1995</td>
<td>Assisting in the creation of new, and expansion and modernization of existing enterprises in the private sector.</td>
<td>Granting and guaranteeing loans, underwriting, direct subscriptions, provision and managerial, technical and private sector organized as public limited companies, cooperatives, joint and public sector undertakings.</td>
<td></td>
</tr>
</tbody>
</table>
IDBI 1964
Assisting, supplementing and coordinating the financial and development institution in both private and public sectors.

Direct and indirect assistance, and promotional activities.

All types of enterprises

SCORING PATTERN OF FINANCIAL PERFORMANCES

Some of the data relating to financial performance of IDBI has been compared with the data of ICICI and IFCI. The year 1999 – 2000 and 2000 – 2001 is taken into study for their income, expenditure and profit. Comparative percentages have been worked out in connection with their performances and even operating profit, net profit, and provisions etc. have been taken into account.

Comparative data will give once eye view so far as their financial performances are concerned: -
Financial performance of IDBI, ICICI and IFCI


<table>
<thead>
<tr>
<th>ITEM</th>
<th>IDBI</th>
<th>ICICI</th>
<th>IFCI</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td></td>
<td>Percentage</td>
</tr>
<tr>
<td>A. Income</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>i) Interest income</td>
<td>6224.31</td>
<td>6191.38</td>
<td>-31.13</td>
</tr>
<tr>
<td></td>
<td>8117.43</td>
<td>8836.17</td>
<td>718.74</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>ii) Other income</td>
<td>1635.11</td>
<td>1640.39</td>
<td>8.28</td>
</tr>
<tr>
<td></td>
<td>348.96</td>
<td>461.88</td>
<td>112.92</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>B. Expenditure</td>
<td>6912.62</td>
<td>7143.80</td>
<td>231.18</td>
</tr>
<tr>
<td></td>
<td>7260.64</td>
<td>8760.78</td>
<td>1500.14</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>i) Interest expensed</td>
<td>6370.00</td>
<td>6594.91</td>
<td>224.91</td>
</tr>
<tr>
<td></td>
<td>3782.23</td>
<td>6376.78</td>
<td>591.53</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>ii) Provisions</td>
<td>80.00</td>
<td>43.00</td>
<td>-37.00</td>
</tr>
<tr>
<td></td>
<td>244.00</td>
<td>918.90</td>
<td>674.90</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>iii) Other Expenses</td>
<td>462.62</td>
<td>505.89</td>
<td>43.27</td>
</tr>
<tr>
<td></td>
<td>1231.41</td>
<td>1465.10</td>
<td>233.69</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Operating profit</td>
<td>1027.00</td>
<td>733.97</td>
<td>-293.03</td>
</tr>
<tr>
<td></td>
<td>1449.75</td>
<td>1456.17</td>
<td>6.42</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Net profit</td>
<td>947.00</td>
<td>690.97</td>
<td>-256.03</td>
</tr>
<tr>
<td></td>
<td>1205.75</td>
<td>537.27</td>
<td>-668.48</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Total Assets</td>
<td>72285.4</td>
<td>71783.4</td>
<td>-502.02</td>
</tr>
<tr>
<td></td>
<td>65389.5</td>
<td>73413.7</td>
<td>8024.17</td>
</tr>
</tbody>
</table>

(Source – WWW.RBL.ORG October 2003)

On the basis of figures available, financial ratios are worked out to have clear-cut comparative study, so far as IDBI, ICICI and IFCI are concerned. Data pertaining to Year 1999 – 2000, 2000 – 2001 are taken into study.
### Financial ratios (Percentage ratio to total assets)

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Operating profit</td>
<td>1.42</td>
<td>1.02</td>
<td>-0.40</td>
<td>2.22</td>
<td>1.98</td>
<td>-0.24</td>
<td>1.02</td>
<td>1.03</td>
<td>0.01</td>
</tr>
<tr>
<td>Net profit</td>
<td>1.31</td>
<td>0.96</td>
<td>-0.35</td>
<td>1.84</td>
<td>0.73</td>
<td>-1.11</td>
<td>0.25</td>
<td>-1.15</td>
<td>-1.40</td>
</tr>
<tr>
<td>Income</td>
<td>10.87</td>
<td>10.91</td>
<td>0.04</td>
<td>12.93</td>
<td>12.67</td>
<td>-0.28</td>
<td>12.41</td>
<td>12.69</td>
<td>0.28</td>
</tr>
<tr>
<td>Interest income</td>
<td>8.61</td>
<td>8.63</td>
<td>0.02</td>
<td>12.41</td>
<td>12.04</td>
<td>-0.37</td>
<td>12.17</td>
<td>12.64</td>
<td>0.47</td>
</tr>
<tr>
<td>Other income</td>
<td>2.26</td>
<td>2.29</td>
<td>0.03</td>
<td>0.53</td>
<td>0.63</td>
<td>0.10</td>
<td>0.24</td>
<td>0.05</td>
<td>-0.19</td>
</tr>
<tr>
<td>Expenditure</td>
<td>9.56</td>
<td>9.95</td>
<td>0.39</td>
<td>11.10</td>
<td>11.93</td>
<td>0.83</td>
<td>12.15</td>
<td>13.84</td>
<td>1.69</td>
</tr>
<tr>
<td>Interest expended</td>
<td>8.81</td>
<td>9.19</td>
<td>0.38</td>
<td>8.85</td>
<td>8.69</td>
<td>-0.16</td>
<td>10.85</td>
<td>11.06</td>
<td>0.21</td>
</tr>
<tr>
<td>Other expenses</td>
<td>0.64</td>
<td>0.70</td>
<td>0.06</td>
<td>1.88</td>
<td>2.00</td>
<td>0.12</td>
<td>0.54</td>
<td>0.60</td>
<td>0.06</td>
</tr>
<tr>
<td>Provisions &amp; contingencies</td>
<td>0.11</td>
<td>0.06</td>
<td>-0.05</td>
<td>0.37</td>
<td>1.25</td>
<td>0.88</td>
<td>0.76</td>
<td>2.18</td>
<td>1.42</td>
</tr>
</tbody>
</table>

With a variegated structure the development banking institution as a group, have played a significant part in the economic development of India via investment market and 7.26
have emerged as the backbone of the financial system. With the above table comparative figures, so far as IFCI and ICICI are concerned, have been taken into account. IDBI as compared to these institutions have played a different role. Ratios of their enhancement as also their downfall have been taken into study. The table reveals that:

- The income of IDBI in 2000 – 2001 has gone down by 0.23% as compared to the year 1999 – 2000. The major downfall is of interest income. Although the other income has increased.

- The expenditure in the same period has increased by 3.34%. Although the provisions made by IDBI were reduced by 46.25%.

- ICICI during this period has enhanced their income by 9.82%. But IFCI’s income got down by 0.32%.

- So far as the enhancement of expenditure was concerned, ICICI and even IFCI have increased their expenditure by 20.66% and 10.98% respectively.

- Provisions made during the year by ICICI and IFCI have shown a good sign. ICICI has increased their provisions by 276.60% and IFCI enlarged their provisions by 176.97% during this period.

- The operating profit of IDBI in 2000 – 2001 gone down by 28.53% as compared to the year 1999 – 2000. Both ICICI and IFCI also showed a decreasing trend. Although ICICI earned an overall profit, but the net profit for this period decreased by 55.44%.

The financial ratios as shown by the above table reveal that, both the net profit and operating profit of IDBI have reduced. These ratios were compared with their total assets. The ICICI and IFCI have also shown a reducing trend. The total assets of IDBI in 2000 – 2001 reduced by 0.69% as compared to the year 1999 – 2000. Similarly IFCI also declined by 2.53% during this period. The total assets of ICICI which were 65389.56 crore in 1999 – 2000 have increased to 73413.73 crore in the year 2000 – 2001, which shows an increase of 12.27% as compared to the previous year. The total expenditure ratio to fixed assets of IDBI was 9.56% in 1999 – 2000, which increased to 9.95% i.e. 0.39% enhancement in 2000 – 2001. This ratio of ICICI was 11.10%, increased to 11.93% i.e. 0.83% enhancement in 2000 – 2001 as compared to the year 1999 – 2000. IFCI during this period spent more i.e. 12.15% in the
Year 1999 – 2000 and 13.84% in 2000 - 2001. The ratio of expenditure increased by 1.69%. The above comparative study initially approaches to make an institutional comparison of the institutions.

**Issues and Suggestions**

With an overview of financial institutions it can be said that the country today possesses a fine network of development banks, which have significantly contributed to the development in the country. IFCI, ICICI and SFCs along with IDBI have done well in the area of development. However some important suggestions can be given in this regard.

- Undoubtedly these institutions have played a very significant role in the industrial development of the country, but still a lot is required to be done so far as their financial strength is concerned.

- All the financial institutions are required to adopt containment of non-performing Assets. Although all the above have initiated several measures for containment of NPAs, but still a well equipped monitoring system is required to improve recovery and initiate timely remedial action.

- ICICI, IFC and IDBI should increase the utilization of sanctions in backward areas and should follow a different set of norms for disbursements in backward areas than those in the developed areas.

7.28
- Regarding sanctions and disbursements, it can be suggested that the institutions should make attempts to reduce disparities between the states. In addition to this attempt should be made to overcome the regional imbalances.

- Socio – Political environment prevailing in a particular region closely influences the process of industrialization. These factors have led several entrepreneurs to prefer setting up their units. However the government has been alive to the problem of inadequate industrialization. It has formulated its industrial policy incorporating, inter-ilea various incentive schemes for units to be setup in industrially backward areas.

- Our country is witnessing a gradual unshackling of the Indian economy from being inward looking, heavily regulated, controlled and high cost economy to an open minimally controlled and internationally competitive economy. With a view to provide greater Phillip to the industrialization as also to attract outside entrepreneurs these institutions are required to adopt several measures which include up gradation and expansion of infrastructure.
- A Venture Capital Fund should be planned to formulate and channelised by these investment financial institutions, which will help to overcome resource gap faced by entrepreneurs for Technology Oriented Projects and shall encourage industries utilizing new and innovative technology as well as Project and Technology up gradation based on research and development.

- One of the most important suggestions for these financial institutions is that, they should restrict and control their administrative and general expenditure. This will help these national level institutions to maintain income as well as their financial strength also.