CHAPTER ONE

INTRODUCTION

1.1 Background of the study

Economic development, a complex phenomenon having multiple dimensions, is determined by the interplay of a wide range of factors, which includes, inter alia, physical, financial, structural, psychology of the masses and institutional. Therefore, measuring economic development too calls for adoption of a multiple of criteria involving literacy, mortality, health, sanitation, infrastructure development, urbanization, agricultural productivity, non-agricultural contribution to domestic product and a wide range of other dimensions. Economic development is considered as synonymous with industrialization because of a very high degree of positive correlation of industrialization with a majority of these indicators of development (Dholakia, 1989). The present level of development in the advanced countries is generally regarded as the outcome of a change set in motion by the industrial revolution (Kaur, 2007). Economic development necessarily is accompanied by a transition from an agriculture dominated to an industrialized economy. Manufacturing industry represents a higher stage of production in advanced countries. The development of manufacturing industry has been associated in these countries with spectacular progress and rise in the levels of living. Even in the developing countries, the productivity in industry tends to be considerably higher than in traditional agricultural pursuits (Gupta, 1993).

Emphasizing the importance of industrialization in the development process, Goswami (1981) observed that, industrialization is necessary not because of the existence of a large army of underutilized labour force in traditional agriculture with zero marginal productivity and loosely organized allied activities in underdeveloped economies alone. Industrialization is but also of crucial importance to development strategy because of its
capability of radiating stimulus throughout the economy by increasing the productivity of labour, increasing national (state) income and output, facilitating further investment by enhancing the rate of saving and capital formation. Besides such forward linkages, industrialization also is characterized by strong backward linkages, strengthening the market for both farm and non-farm products. Industrial development of a region is both the cause and consequence of infrastructural development of the region. It also leads to greater skill formation, increased literacy, increased wages and a resultant higher standard of living. The industry has greater opportunities of technical advancement; it possesses relatively a high marginal propensity to save and invest, produces commodities having different income elasticity of demand and contributes to the eventual achievement of a self-sustaining economy with sustained high level of investment (Arora, 1992).

The under developed countries (UDC’s) of the world have considered massive industrialization as a strategy towards their objective of achieving fast paced development. Industrialization is considered to be the only way through which the objectives of national policy viz. removal of poverty, balanced regional development and national defense can be effectively realized (Kaur, 2007). It is a widely accepted instrument for increasing the general production and national income of a country. Nations, rich or poor, have therefore, emphasized the need to build a strong and diversified industrial base. The secondary sector is essentially the kingpin of providing self reliance, balanced growth and a stable economy. It is not surprising that India too embarked upon programmes of massive industrialization after her independence in 1947.

It must be noted here, that, despite the increasing emphasis on industrial development, the progress of UDC’s has been impeded by the lack of various ingredients for industrial development. Such bottlenecks include shortages of factors of production; lack of entrepreneurship, competent management and skilled personnel, lack of modern technology and technical know-how, inadequate markets and the lack of adequate finance. Lack of adequate finance is looked upon as the main deterrent to economic and industrial development in these countries. Although capital alone does not constitute a sufficient condition for solving the problem of underdevelopment, it nevertheless plays a crucial role
in providing access to the multiplicity of other ingredients, whose intelligent combination is likely to raise the rate of industrial growth in an economy (Arora, 1992).

The post-independence era was characterized by a deep urge to industrialize the Indian economy for achieving the desired level of growth and development of the country. This was at par with the notions in the other developing countries noted after the post World War II period. It was widely felt then, that, sustainable and self-reliant industrial machinery would be possible only with the establishment of new gigantic scale industrial projects. As is well-known, financial requirements are high in higher capitalization of production process. Thus, it became imperative to devise new industrial machinery in the country with ample financial resources so as to deal with the increasing financial requirements of the industrial sector. What was required for industrialization was not just the availability of finance for industries, but availability in a massive scale and for an elongated period, that is medium and long term finance. The network of commercial banks in existence shyed away from such term financing and the capital market did not adequately evolve to the need of the time. Accordingly, development banks were initiated in the country as gap-fillers to compensate for the lack of term finance at the time of independence of the country. In this light, it is rightly observed that, the creation of development banks was the most outstanding development in the sphere of industrial finance and a cornerstone in the financing mechanism in India (Borbora, 2001).

1.2. Development Banks

Development banks are a heterogeneous group of financial institutions concerned with extending medium and long term credit for projects and development programs. They are, usually, a form of government intervention in the financial system of an economy, aimed at addressing the financial needs of those sectors which have failed in the competition for raising funds. They may also be a way for the government to provide assistance for achieving the socio-economic objectives of poverty reduction, equity and growth. Development banks are, in short, multipurpose financial institutions with a
development outlook (Desai, 2009). They simultaneously act as a visionary, promoter, a mobilizer of resources, an innovator, a creative leader as well as an entrepreneur and are called the institutional entrepreneurs engaged in the process of enterprises creation. They are the catalyst in the development process.

Development bank is an institution which promotes and finance enterprises in the private sector (Sharma, 1989). However, looked in this way, the role of development bank is narrowed down, for this definition ignores their role in mixed economies where they are popular models of growth (Sharma, ibid.). Development banks are generally regarded as a post World War II phenomenon and are attributed to the policy-making in developing countries. Development banks have undoubtedly been the most popular tools in the developing world, being the result of their urge to strive for development in the pace of the advanced countries of the world. However, similar institutions existed even in the nineteenth century Europe as well, catering to the needs for development in the countries where they existed. Lack of adequate availability of resources hampered the development of many countries in the post World War II period for which development banks were devised as an institutional mechanism to fill such gaps. Soon these caught the attention of the developing world and development banks came to be established in almost all the developing countries in Africa, Asia and Latin America (Shobha Rani and Appa Rao, 2010).

A development bank may be defined as a specialized financial institutions established at private and public initiative to render promotional services and medium and long term finance to development-oriented and bankable projects in the public or private sector (Pandey, 1983). The development-oriented projects are those that fulfill any one of the following objectives, as given below, laid down by the government of developing countries:

1. Helps the rapid economic growth and industrialization of the economy to create necessary climate for all round development
2. Earns return on investment and thus generate resources for development
3. Promotes redistribution of income and wealth
4. Creates employment opportunities
5. Promotes balanced regional development
6. Assists the development of small scale and ancillary industries
7. Promotes imports substitution and helps in earning foreign exchange for the economy

On the other hand, a bankable project is a self financing project capable of generating enough income within a given period of time to:

1. Cover the cost of operation once the plan comes into action
2. Repay the principal of bank’s loan
3. Pay the interest charges of the loan and leaves a residual profit large enough to induce the entrepreneurs to undertake and remain with the operations (Kane, 1975).

Models of development bank lack uniformity. Disparity is observed in their form, structure, mode of working and functions of development banks both in a country and across countries. They differ not only in size or volume of operations but also in corporation as well as functionally. The diversity originates because the structure of a development bank is greatly influenced by the social, political and economic environment of its operation (Sharma, 1989). Each development bank is repose to the particular needs of the country which it serves and to the political, economic and social environment in which it has to function (Arora, 1992). However, beneath the apparent diversity there is a close similarity in the scope of their basic functions and purpose because all development banks have been devised to provide at best a fare if not all the fundamental ingredients of development so as to accelerate the pace of industrial and at large economic growth. To quote Gupta (1993): a development bank is one that is intended, “to provide the necessary capital, enterprise, managerial and technical know-how where these are clearly inadequate or non-available and to assist in building up financial and socio-economic infrastructure in order to speed up economic development.”
A development bank may be defined only with regard to the hybrid financial and developmental character which is also more pronounced in its name. All financial institutions which are development-oriented are development banks. The very name ‘development bank’ reflects the basic idea behind such institutions, i.e. their banking functions and the nature of their financing which is primarily developmental or long term. Development banks and development finance institutions are interchangeably used terms to refer to the vehicle for extending development finance (Shobha Rani and Appa Rao, 2010). However, in recent years the term development bank has become relatively more popular, in usage, reflecting a greater emphasis on their banking role (Bruck, 2005). Another study terms this category of institutions as non-bank statutory financial organizations, with the justification that they have in common only their statutory status even though there is some private sector participation in ownership and functioning (Bhole, 2007). Again, considering that they also provide promotional services for industries, they are called as special finance institutions (Goswami, 1988 b).

It may be noted that, earlier development and finance corporations were treated as separate entities and only financial corporations were considered as development banks. While the former were to undertake promotional and managerial activities besides providing equity capital, the later were to provide term finance by way of loans and advances. However, over time the differences between the two became blurred (Arora, 1992). Both these institutions were termed as development banks by the World Bank too (Sikidar, 1982). It may be noted that, a ‘corporation’ is a group of people authorized to act as an individual and recognized in law as a single entity [Illustrated Oxford Dictionary, 2008]. Thus, it is an association of persons recognized by the law as having a collective personality. A corporation incorporated under the special act of legislature is considered as a public corporation. Such public corporations set up with the specific purpose of dealing with finance to mobilize resources for investment and using the same for the development of a certain area of operations of the national economy, are considered as public financial corporations and are legally termed as
public financial institutions. These are not profit oriented undertakings; they finance
the expansion and development of industries. Accordingly, the public finance
institutions are termed as development banks by the World Bank authority (Sikidar,
1982).

1.2.1 Evolution of development banking in the global perspective:

Development banks along with the embryonic growth of the banking system had
their origin in some of the most developed countries of Europe. A review of the evolution
of the concept and form of development banking across the globe holds much significance.
Firstly, they reflect the background, situation and needs of the countries in which they
appear, (Sharma, 1989) which are revealed by an insight to the history of the same. The
developing countries, does look up to the developed countries for the pattern of their
progress. Secondly, such an exercise is presumed to reveal the need and importance of
development banking, as felt by the policy makers in India who adopted the same in the
country. A brief country-wise account of the evolution in the pattern of development
banking is presented in the following paragraph, which is also arranged in the
chronological order of the birth of such institutions.

1.2.1. (a) Development Banks in the nineteenth Century:

Industrial revolution first started in England and so also most of the economic
changes following industrial revolution. But the origin of development banks was not in
England but in some other countries of the continent of Europe. The Societe-Generale de
Belgium was the first prototype development bank established in 1822, set up to finance
and promote industry in Belgium (Biswaasroy et al., 2006). In the thirties, it became the
main promoter and supporter of industries in the country, promoting many coal mining,
railway and canal companies and forming a number of subsidiaries, even though its
activities are seldom recognized. However, being in serious financial trouble, the bank was
directed to pay more attention to ordinary deposit banking business in 1851 and therefore it
lost its status of a development bank since then. The indiscriminate use of funds by the
Societe-Generale and its huge investments in unsecured loans were the reasons for which it
met its fate.

The conditions in the European countries in the early part of the 19th century were
almost the same. On the one hand, they were keen to catch up with the progress of England
and on the other they faced serious shortage of capital and other resources for the same.
The capital needed in the process was huge and that banks played an important role in this
context. Yet, the assistance of banks was not adequate and this necessitated the birth of
specialized financial institutions in these countries (Shobha Rani and Appa Rao, 2010).
Accordingly, several specialized institutions like Compteir’d Escompte, the Societe
Generale pour Favourise’ Industries et le commerce de la France, and others were
established in France, in the mid-nineteenth century. Of these the ‘Credit Mobilier’ was
the most important bank set up by the Pereiere Brothers in 1852. It is said that, of its
contributions, the most significant was the ‘idea’ of development and the ‘spirit’ of
enterprise, implicit in its conception (Shobha Rani and Appa Rao, ibid.). It financed
numerous industrial undertakings at home and abroad. It provided great impetus for growth
of new banking techniques and for similar institutions throughout Europe in the nineteenth
century. Despite a stormy career of fifteen years, that is, the bank was closed down in
1867, due to improper management of its risky investment portfolios which led to heavy
losses.

A look at the history of financing industries in Germany is mandatory in this
context, as it demonstrated the most significant connection between industries and banks.
Due to lack of independent investors and the non existence of link between the holders of
capital and the avenues of investment, industries had to depend upon the banking network
for their funds. Besides, the process of cartel, or horizontal association of like industries to
build up competition, induced more of the closeness with banks. The banking network in
Germany thus secured all such functions that were necessary to live up to the requirements
of industries. These were the ‘mixed banks,’ which have inspired institutional development
in many developing nations later. The banking structure there, though apparently so broad, being cartelized to share the credit requirements and the risk of investments among them and performing so many varied functions, was yet, internally very specialized (Das, 1956).

1.2.1. (b) Development Banks in the twentieth Century:

Development banks continued to be set up in the European continent with time and country specific objectives and organization. The evolution pattern in the twentieth century in Europe has been segregated into three causes of origin, which were affected both by World War I and World War II and the post-Great Depression economies. However, the twentieth century development banks in Europe are different from their predecessors in the nineteenth century on several fronts. The nineteenth century development banks were mostly private in origin and mostly concentrated on large scale enterprises. The twentieth century depressions and the Second World War devastated the small and medium industries. The twentieth century development banks upheld the concern of existing enterprises and extended loan capital but did not foster the development of new enterprises. Besides, the countries of Europe by then have attained economic growth and did not require development assistance as the meaning of development bank of present times feature. These were, therefore, hardly development banks but they did cast important influence on the developing economies for building up the necessary financial institution framework for their much desired development (Shobha Rani and Appa Rao, 2010). To quote Saxena (1970), “In the wake of the growing urge for accelerated economic growth, especially in the post-World War II period, most of the countries in the ‘Free World’ have realized the edge of the technique of development bank financing of industry over the technique of governmental and/or market financing. Hence, development banks have been established in almost all the countries: advanced and underdeveloped.” However, the development banks in the later featured more of developmental functions than in the former to foster increased industrial and overall economic development.
At the initial phase of industrial development in England, the country did not face any shortage of the ingredients necessary for the same. Industrial development was not sudden but occurred in small doses and hence the country enjoyed the availability of a vast pool of entrepreneurs, an effective banking system that provided adequate working capital, a fairly-high level of income and savings and a consequent ploughing back of profits from agriculture, foreign-trade, etc. The historical reasons behind industry preceding commerce in England were the existence of a class of investors with independent judgments of where to invest, the doctrine of laissez-faire upheld in the country and the conservative banking system with only short term lending worked extremely well for industries for so long (Das, 1956). But the increasing industrial development of America and European countries, increased competition and the consequent urge in England for faster development led to the tendency of businessmen to find new institutional assistance to industries. Towards the end of the nineteenth century specialized financial institutions emerged in the country like issue houses, underwriters, company promoters, etc. to provide necessary help to individual and small firms that later on expanded to corporations. Mention here must be made of the Report of the MacMillan Committee (1930-31). The report, as observed by Shobha Rani and Appa Rao (2010), revealed that there exists a gap in the existing arrangements for the provision of credit due to the absence of financial machinery to provide business with finance. Thus, thereafter, a number of development banks were initiated in England. In 1945, the Industrial and Commercial Finance Corporation Ltd. (ICFC) was established to financially assist the small and medium enterprises that were unable to raise the same. However, ICFC did not receive any government aid or subsidy. Another development bank, namely the Colonial Corporation, was established in 1948 to assist the development of Commonwealth countries. The Commonwealth Development Finance Company Ltd., incorporated in 1953, was also another development bank of England that assisted the development of Commonwealth countries, especially India.

The highly advanced capitalist economy of America hardly required any specialized financial assistance to foster in development. Investment for industrial development was met out of profits in other spheres and that profit margins, income and
savings were very high in America. Besides, required capital was secured through bonds, shares and the like. But since the depressions such a need was realized even in this country. In 1932 the Reconstruction Finance Corporation was set up to reconstruct and rehabilitate the American economy that was devastated after the depressions of the 1930’s. Since this was a temporary institutional arrangement, it was dissolved in 1953 and replaced by the Small Business Administration. This was a development bank proper as it performed both the financial and development banking functions. Besides, several other similar institutions flourished in the United States of America assisting economic or industrial development there as well as in overseas. Here, mention must be made of the Industrial Development Bank of Canada, set up in 1944. The organizational set up of this particular institution was similar to that of Industrial Development Bank of India (IDBI) in India and had influenced the policy makers in our country to establish the same (Saxena, 1970).

Industrial development in Japan, especially in the post-World War II period, was mostly assisted by development banks. The development banks in Japan are classified as being private or government owned. The Industrial Bank of Japan Ltd. was initiated in 1902 but then it was a semi-governmental organization. It was established in the pattern of the Credit Mobilier of France. Later on, in 1951, it was completely privatized. The private development banks of Japan have been the core providers of Credit. The Japanese economy is assisted by a network of development banks; each designed to assists every sector of the economy (Saxena, 1970).

Besides these country specific account of development banking, there were the regional development banks created jointly by two or more countries for the purpose of assisting development in some region or sub-regions of the world. The Asian Development Bank, the African Development Bank, European Investment Bank are some such examples. There is also the case of the World Bank striving for development across the world. The contribution of each of these can in no way be ignored. The technique of industrialization of an economy through the development banking framework has been adapted by the underdeveloped countries as well, since after the World War II. This was
mostly due to their urge to achieve rapid development of their economies and come at par with the advanced countries. Be it the Latin American countries, the comparatively developed or underdeveloped countries in Asia or any other country seeking development across the globe, most of them have adapted such a strategy.

1.2.2. Development Banking in India:

The significance of provisioning for long and medium term finances for fostering industrial development was realized in the country much before independence. There exists several instances of provisional governments demanding establishment of setting up industrial banks and providing various assistance to small scale industries during the British rule. The organized thoughts initiated by various commissions and committees during the colonial rule were directed at setting up of industrial banks for providing term finances. After the World War II, the need for such specialized banks became more pronounced. However, these claims were realized only after independence with the initiation of Industrial Finance Corporation of India (IFCI) in 1948. Thereafter, large numbers of such institutions were established at both the national and regional level.

The structure of financial institutions that evolved in the country since independence can be stratified into: (a) All-India development banks, (b) specialized financial institutions, (c) general investment institutions and (d) the regional level development banks (Biswasroy et al., 2006). The all-India development banks include the present Industrial Finance Corporation of India Limited (IFCI), Industrial Development Bank of India (IDBI), Industrial Credit and Investment Corporation of India (ICICI), Small Industries Development Bank of India (SIDBI) and the Industrial Investment Bank of India (IIBI) (Biswasroy et al., ibid.; IDBI, 1999-2000). The erstwhile IFCI was initiated to cater to the term requirements of industries. In 1955, the ICICI was established. This was a pioneer development bank in several aspects. Besides being a wholly privately owned institution it also served for the foreign currency term requirements of industries. Presently ICICI ceases to exist being replaced by the new entity ICICI Bank. In the history of
development banking in the country, a significant step was taken in 1964 when the IDBI was established. It was set up to coordinate and regulate the activities of the other term financing institutions in the country and to meet effectively the growing challenges in the industrial scene of the country. It was converted to an autonomous institution wholly owned by the government of India in 1976. For rehabilitating the sick units the Industrial Reconstruction Corporation of India was established in 1971. Later on, in 1985 it was converted to a statutory corporation renamed as Industrial Rehabilitation Bank of India. In 1997 it was converted to a full fledged development bank renamed as Industrial Investment Bank of India Limited. The Seventh Plan document observed the inadequacy of credit to the small scale sector and pursuant to this SIDBI was established in 1989 to act as a principal financial institution exclusive to the needs of the small scale industries sector.

Considering the sub-continental size of the country, it was relevant to cater to the unique developmental requirements of each region to foster balanced and inclusive development across the country. Accordingly, the State Finance Corporations (SFC) was established to cater to the needs of the small scale sector at the state level, by enacting the State Financial Corporations Act in 1951. Another landmark was the initiation of the State Industrial Development Corporations (SIDCs) in the 1960’s. Following this the Assam Industrial Development Corporation (AIDCs) was established in 1965. There exist 18 SFC’s and 28 SIDC’s in the country. To this class of regional level development banks another addition was the North East Development Finance Corporation Ltd (NEDFi).

Besides, there came up various financial institutions to promote various specialized sectors of the country’s economy. These include the investment and savings mobilization organizations, Life Insurance Corporation of India (LIC) in 1958, Unit Trust of India (UTI) in 1961, the General Insurance Corporation (GIC) in 1973. They are, therefore, the general investment institutions. They have been significantly catering to the financial needs of the industrial sector directly or through the specialized financial institutions. Again, there are the financial institutions catering to the long term finance requirements of some special sectors of the economy. They include the Export-Import Bank of India (EXIM) for facilitating the export-import activities, Tourism Finance Corporation of India Ltd and so
on. These institutions are called the specialized financial institutions and are not development banks in the general sense of the term (Biswa roy et al., 2006; Goswami, 1988 b).

1.3 Statement of the problem

The present study is an attempt to gauge the role played by the regional level development banks, namely Assam Financial Corporation (hereinafter referred to as AFC) and North East Development Finance Corporation Limited (hereinafter referred to as NEDFi) in the process of industrialization of Assam. AFC was established in 1954 in pursuance of the State Financial Corporation Act, 1951 with its headquarters at Guwahati. It may be noted that the State Financial Corporations were established in order to facilitate adequate term credit supply across the country, to cater to the financial needs of the small scale industries and to promote a balanced industrial development. This has also been mentioned in the State Financial Corporation Act, 1951 [available online, last assessed on 23.3.14]. Accordingly, like its counterparts in other states, AFC is assigned the role of being the prime purveyor of term loans to small scale industries within its jurisdiction in the states of Assam, Meghalaya, Tripura and Manipur. On the other hand, the origin of NEDFi as a development bank to cater to the unique financial and developmental needs of the northeastern region was conceptualized in the I. K. Borthakur Committee report of 1994. Consequently, in 1995 NEDFi was established, being incorporated in the Companies Act, 1956 and it commenced its operations from 1996. As a development bank specific to the northeast, NEDFi strives at identifying and financing commercially viable industries in the region. This has even been specified in the mission statement of NEDFi. Besides financing, it caters to the various developmental needs of the micro, small and medium enterprises through provisioning of a wide variety of the industry extension services.

Assam, located in the northeastern region of the Indian subcontinent comprises of a total land area of 78,438.08 sq. km. and a total population of 31.17 million as per 2011 census, (Government of Assam, statistical handbook, 2012). It therefore constitutes 2.39%
of the total land area of the country and has 2.58% of the country’s population. The state of Assam reflects a paradox of opportunity and low economic development. This Indian state has a vast availability of natural resources on one hand and on the other it lags behind the rest of the country in aspects of economic development. The blame for the poor economic performance of the state has been mainly put on the slow pace of industrial development. Industrialization has been a subject of concern and serious deliberation mostly because Assam was put on the industrial map of the world much before the country attained independence. The tea and oil industries brought in much acclaim to the state since the colonial rule. Yet, the plight of Assam in the industrial front is pathetic. The statement may be supplemented with an instance that in 2009-10, the percentage contribution of industrial sector to the gross state domestic product in Assam was 24.29% of which manufacturing sector contributed a mere 8.05% (www.planningcommission.nic.in). The contribution of the secondary sector has remained static and low for the state while that of agriculture is declining and services increasing substantially. For instance, in the same year 2009-10, the contribution of the primary sector to the state was 25.83% and that of service sector was an appreciable 49.88%. The sorry plight of the secondary sector in the state would be clearer if we compare the percentage contribution of this sector to that in the more industrially developed states of the country. For instance, in Gujarat, the manufacturing sector contributed 30.69% to the respective gross state domestic product while, in Maharashtra this contribution was 21.17% and in Karnataka 17.90% for the year 2009-10. For India as a whole, the manufacturing sector contributed 16.17% of the gross domestic product in this year.

Industrialization being imperative for overall economic development, the governmental agenda had emphasized upon various dimensions to promote industrialization in the state. Despite various efforts, industrial development has not, yet, gained momentum in the state. Many studies have been pursued, analyzing the causes of industrial backwardness of the state. A meticulous perusal of these studies reveals that a combined effort of different hindering forces has resulted in the industrial backwardness of the state. These include the location and the geography of the state, lack of
entrepreneurship, lack of capital, inadequate infrastructure and the socio-political unrest. Capital inadequacy surfaces in almost all these studies as a major hindrance. To meet the aforesaid requirements the development banking framework was initiated in the country. It may be noted that all India level development banks have extended their assistances to Assam as well. Besides the state or regional level development banks were also established in the state to bring forth a balanced development and industrialization at par with the rest of the country which included the AFC, AIDC and NEDFi. Considering the inadequacy of the national level development banks in the context of the state, as well as the entire northeast region, as several earlier studies point out, the regional level development banks become more significant to the development of the state.

Moreover, in recent times development banks are facing a threat in their very existence. There are two forces attributing to this: firstly, their poor performance augmented by the economic liberalization. And, secondly the external competition experienced from other financial institutions both in raising funds and lending activities (Bajpai, 2004). It may be noted that development banks across the globe are facing a threat of shut down or conversion to some other form of financial intermediation or conversion to a universal bank, the main reasons being their inefficiency in management of portfolios of investment, focus on one type of investment which raises risk, failure in project evaluation, etc. all resulting in their huge and mounting losses, a loss of public money. This is more significant in a country with low income, low savings and low capital formation. There is a noted drive in the country following financial reforms to convert DFIs into banks and Non Bank Financial Companies (NBFC). In fact, it is suggested that in the long run only two forms of financial intermediary would stay, i.e. the banks and NBFC’s experiencing relevant regulations. The immediate cause of the downturn of the development banking framework is the chronic and huge losses incurred by development banks in the country.

Though the conversion of development banks on the grounds outlined above seems justified, there exists a globally emerging body of literature that supports the cause of development banking and urges the same to stay. As they argue development banks foster industrial and overall economic development and therefore cannot be substituted by any
other form of financial intermediation. What development banks extend is not mere financial assistance but much beyond. In the Indian context too, a number of arguments are put forward. One important area of their relevance is in the field of infrastructural development (Gupta, 1999), the need of which has augmented in the era of reforms. This concern is also raised in a discussion paper on development banks released by RBI (1997). Besides, another study notes that mega projects in the fields of oil, gas, petrochemicals sectors and projects in textiles, sugar and food products and the fast developing software industry will have to depend upon DFIs in the absence of any adequate alternative source of term finance (Srivastav and Nigam, 1999).

Further, various committees have been constituted by the government to promote the small scale sector. Most of these committees invariably considered the significance of state financial corporations in providing term finances to this sector. It has been emphasized that commercially viable SFCs are necessary for funding the SME and tiny sector due to inadequacy of banks or other alternative sources to meet their financial requirements. This is especially in the northeastern region where SME sector has a special case for enhancing the pace of development (RBI, 2004b.). Another line of argument favoring development bank suggest that the time is not ripe for initiating universal banks (Simha, 1999; Sabnami, 2000). As one study states, besides concentrating power in the hands of few large financial houses, they lead to managerial inefficiencies. Accordingly, the study opines that development banking through their immense experience in project financing and industrial promoting services must continue in the interest of the development of the country industrially (Simha, ibid.).

In the light of the arguments stated above, if the regional level development banks, namely, AFC and NEDFi, hold any significance to promote industrial development in the state they must continue to operate and be re-engineered, if necessary, to ensure industrial development in the state of Assam. Accordingly, the present study attempts to assess whether these two institutions have any proactive role in promoting industrialization or they continue to be yet other names of financial institutions functioning in the state.
1.4 Review of Literature

The framework of development banks that has evolved in the country reflects wide changes over time in their structure, organization and mode of functioning. Therefore, it is imperative that the present study reviews the same initially. Das (1956) in his book deals with the problem of institutional finance for industries, the various sources of industrial finance and the genesis and role of development banks in the context. The book contains a comprehensive summary of the history of industrial financing in the country and in England and Germany.

Saxena (1970) provides an account of development banking, its evolution and growth in the country as well as in the world context. It traces the origin of such institutions and also examines their organization, management and the mode of functioning in details. The work examines the operations, procedures, terms and conditions and the developmental functions of term lending of development banks and of IFCI, IDBI, ICICI and SFC’s in particular.

Desai (2000) elaborates the genesis, pre-reforms structure, functions and the role of development banks in India. Datt and Sundharam (2010) describes the initial and present status of the development banking framework in the country. Akhan (2010) provides an outline of the nature and functions of the financial intermediaries in India and emphasizes upon the significant role of development financial institutions.

Bhole (2007) makes a comprehensive study on the role, nature and structure of the Indian financial system. It also details the role, structure and components of the different financial intermediaries and the financial markets, inclusive of development banks.

1.4.1 Development banks and industrialization:

The role of development banks in the context of the industrial sector has attracted academicians, writers, administrators and various statutory committees to study the different aspects of their functioning. Goswami (1988 a) illustrates on the process of industrialization in India and also that of northeast India. It highlights the role of financial
institutions in the context and elicits the rather insignificant assistance contributed by the all India development banks, which were sought to foster industrial development, to Assam and the northeast. Again, Goswami (1988 b) study portrays the imbalance in the assistances provided by the different development banks to the northeast vis-à-vis the other states of the country and identifies the factors inhibiting adequate flow of finances to the region from them. Similar conclusions have also been drawn by Sarma (1988) in his study.

Sharma (1989) studies the role of development banks in the process of industrialization of Punjab. For the study, besides studying the role of all India development banks the study emphasizes on the role of Punjab State Industrial Development Corporation, Punjab Financial Corporation and Punjab Small Industries and Export Corporation.

Sharma (1991) in his book makes a comprehensive analysis of the role of different all India DFIs in entrepreneurship development in the country, their various schemes, policy and strategies for the same, their objectives and lending- sanctioned and disbursed. Entrepreneurship development is significant for industrial development. The DFIs must attempt through their lending activities to create infrastructure and entrepreneurial development so as to bring about industrial growth.

Arora (1992) highlighted the importance of industrialization for economic development and the importance of development banks in the institutional framework for financing industries. The assistance by development banks under different broad dimensions is analyzed for development banks and IDBI, in particular. Also, the study evaluates the various developmental activities of the same which he differentiates into financial and non-financial nature.

Gupta (1993) evaluated the role of the regional development banks in particular and the role of development banks in general, in the industrial development of Himachal Pradesh. The study examines the financial assistance sanctioned and disbursed by the development banks to the state. Besides, there is a detailed account of the procedures, terms and conditions of term lending by development banks in the state followed by an analysis of the simplicity and non-redundancy in the same. The study focuses on the promotional role of development banks in the industrialization process of Himachal
Pradesh and in this attempt an institution wise account of the different schemes and policies for the same is reflected. The study also makes an analysis of the schemes of development banks for the detection and revival of the sick units.

Kaur (1995) make a comprehensive study on the working of Punjab Financial Corporation (PFC) consisting of an analysis of sanctions and disbursements of PFC, the financial performance analysis of the same and a study of the overall working of PFC from the angle of its borrowers.

Dangwal (1999) in his work examines the organizational set-up, the term lending sanctioned and disbursed and the policies of Uttar Pradesh Financial Corporation (UPFC) with emphasis on its contribution to the industrialization of Garhwal region.

Laxmisha (2004) make a detailed analysis of the role of different financial institutions along with DFIs in entrepreneurial promotion with special emphasis on Karnataka State Financial Corporation. In a similar approach, it was observed certain reasons like lack of follow-ups, inadequate or no assistance direct or indirect to secure loans by new entrepreneurs in the role of entrepreneurial promotion of development banks (Dutta, 2000).

Biswasroy et al. (2006) studied the working of IDBI in relation to the industrialization of the country. Besides, giving an account of development banks in the light of industrial development of the country, the study examines in detail the operational performance as contained in the sanctions and disbursements and the promotional activities of IDBI.

Kaur (2007) encompasses the status, policy perspectives and the different aspects of industrial development of Punjab and Uttarakhand and describes the profile of some regional development banks operating in the two states. Thereafter, the study incorporates an analysis of the performance of some of UPFC and PFC in the light of industrialization in Punjab and Uttarakhand.
Sudheer et al. (2010) in their study makes a different approach altogether in the literature of development banking as they analyze the role, working and performance of Kerala Financial Corporation and Kerala State Industrial Development Corporation, all from the viewpoint of loanee concerns. They have included in their study the views of loanee concern on the procedures, terms and conditions, the growth analysis, assets and financial structure which they have tested statistically for significance of the views.

There exist as well a number of research studies made by academicians on the role of development banks in the context of industrialization. Sikidar (1982) observed that AFC is a major financial institution of Assam in terms of its assistance to the state. It makes a detailed analysis of the sanctions and disbursements of AFC and the role of AFC in the process of industrialization including thereof the limitations of the institution in carrying out its activities.

Borpujari (1994) analyzed the role of the Industrial development bank in the region and concluded that the all India development banks have failed to deliver their much expected role in the region.

Das (2000) analysed the role of three promotional organizations in the development of small scale industries in the state of Assam including that of Assam Financial Corporation and reflected upon the operational performance of the same.

Reji (2004) has made a detailed analysis of the operational and financial performance of SIDBI. Also included in the analysis is a comparative study of the role of SIDBI in the industrial development of Kerala through a comparison of SIDBI aided industrial units and other agency aided industrial units.

Articles on the role of development banks in the context of industrialization are also found in various research journals. Narta and Sharma (1997) examined the operational performance of the development banks operating in Himachal Pradesh and finds that their contribution is very meager. As they observe, finance is the most needed factor for
industrial growth. As Himachal Pradesh is an industrially backward state what is required is to enhance the financial share on the part of DFIs to the state.

Ramakrishnaiah et al. (1998) make an analytical study of the financing pattern of Andhra Pradesh State Finance Corporation (A.P.S.F.C.) to the SSI sector. Term loans, working capital, bridge and soft loans are provided to the SSI sector though the term loans occupy a major share of assistance provided. Besides inequality is observed in assistance disburse between regions and industry groups.

Kamalakannan (2005) provides a case for entrepreneurship development in the country and the importance of generating increased women entrepreneurs. He analyses the various products and schemes of different DFIs for promotion of women entrepreneurs.

Swargiary’s (2012) study raises an alarming feature of NEDFi that even though the term sanctions recorded a considerable progress, the degree of increase in the disbursements has been less pronounced. Similar conclusions are drawn in another study by Swargiary (2013). The study highlights the increasing gap between the sanctioning and disbursement of loans which reduces the utility of assistance because; the applicant (borrowers) may not get the required help at right time.

1.4.2 Development banks and other performance analysis:

Sikidar (1988) make an analysis of the distribution of credit to industries in the northeast by public sector banks and DFI and also evaluates the financial performance of DFIs, which he however finds not very satisfactory.

In yet another study by Pati (1996), the operational efficiency of IDBI is comparatively studied with that of the performances of ICICI and IFCI. For the purpose, the financial ratios, namely, return on equity, return on assets and return on capital employed, during the pre and post liberalization period, that is from 1985-86 to 1994-95 were used. The study observes that return of equity of about 20% of IDBI is appreciable, whereas return of assets and return of capital employed of 1-2% is very poor.
Development banks were expected to remove regional imbalances existing in the country through financial assisting and promoting industries even in the less developed areas. But several studies have reported their failure in this direction. Pati (2001) found in his study that the share of the northeastern states in the total sanctions of the all India development banks was also found to be very meager in the study period 1986-87 to 1997-98. Borbora and Dutta (2002) found a statistically significant and increasing trend for funding to be directed away from selected ‘backward’ states to more developed states during 1994-99, compared to the pre-liberalisation period of 1982-87.

Shobha Rani and Appa Rao (2010) have elaborately discussed the literature on development banking and more particularly that of State Financial Corporations. The study especially focuses on the working and performance of Andhra Pradesh State Financial Corporation (APSFC) in the light of total financial assistance dispersed, their functional performance and recovery performance.

1.4.3 Studies by Statutory Committees:

RBI (1992), Committee to Examine the Adequacy of Institutional Credit to the SSI sector and Related Aspects: Under the chairmanship of Shri P.R. Nayak a committee was constituted by the RBI particularly to examine the adequacy of institutional credit to the SSI sector. Of the major findings of the committee one pertains to that commercial banks have furnished only the working capital needs of the MSME sector and that the system of both banks and SFC’s furnishing both term loans and working capital to this sector causes problems of coordination among them. The committee emphasized the role of SFC’s in financing this sector in districts with high SSI density.

RBI (1997), Working Group for Harmonizing the Role and Operations of Development Finance Institutions (DFIs) and Banks: This working group was constituted under the chairmanship of Shri S.H. Khan to review the role, structure and operations of DFIs and commercial banks in the emerging operating environment and suggest changes. It were to
suggest measures for bringing about harmonization in the lending and working capital finance by banks and DFIs it was also expected to examine whether DFIs could be given an increased access to short term funds and the setting up of the regulatory framework needed for the purpose. It was also to suggest measures for the strengthening of different issues of SFIs and banks in the light of capital account convertibility. Of the recommendations made, one striking aspect was that the committee noted the inadequacy of lending towards the priority sector by the banks. Instead of making a percentage allocation of banks mandatory in the context, it was recommended that an alternative mechanism be set up. This might well suit the need for provisioning concessional funds in this direction if need arises. Moreover, in advocating conversion of DFIs to banks, the committee also notes that if the development banks are to perform a developmental role than financial support by the government must be provided.

RBI (1998), High Level Committee on Credit to SSIs: A one man committee was constituted by the RBI under the chairmanship of Shri S.L.Kapur to study the various problems of credit flow to the SSI sector. The terms of reference include primarily- to review the working of the credit delivery mechanism for SSIs with a view to making the system more effective, simple and efficient to administer and to study whether the banks have adhered to the recommendations of the earlier Nayak committee (1992) and implemented its seven point plan of credit delivery to the SSI units. The committee noted the inadequacy of institutional credit to the SSI sector. Moreover, the committee put much emphasis on augmenting the role of SIDBI in this light and suggests a wide number of ways in this direction.

RBI (2004a.), Working group on Development Finance Institutions: In the Mid-Term Review of the Monetary and Credit Policy for 2004, a Working Group under the chairmanship of Shri N. Sadasivan was constituted to review the prospects of transformation of DFI’s into banks following the recommendations of Narasimham Committee report-II and the RBI discussion paper released for public debate titled, ‘Harmonizing the Role and Operations of Development Finance Institutions (DFIs) and Banks’ and also to study the experiences so far of DFIs in this regard. The committee has
made an in-depth study on the meaning of development finance institution and there evolution and also the status of functioning DFIs in the country. Despite a detailed procedure on the future evolution of DFIs into banks or NBFC’s it must be highlighted that the committee recommends that the government must undertake a social cost-benefit analysis in areas needing development finance and on that basis continue with DFIs if need be.

RBI (2004b.), Working Group on Flow of Credit to SSI sector: As per the announcement made by the Governor, Reserve Bank of India, in the Mid-Term Review of the Monetary and Credit Policy 2003-2004, a Working Group on Flow of Credit to Small and tiny industrial sector was constituted under the chairmanship of Dr. A.S. Ganguly. The working group acknowledges the importance of SIDBI in creating venture capital vital for promoting SME sector. Of particular importance in the report is the concern over industrialization of northeast region. The report addresses various problems of this region in this regard. The report considers that SFC’s are vital to foster development of SME sector and therefore the SFC framework must be revoked to take up the task.

RBI (2005), Report of the Internal Group to Review Guidelines on Credit Flow to SME Sector (2005): In 2005 an ‘internal group’ was constituted under the chairmanship of Shri. C.S. Murthy mostly to review existing guidelines issued by RBI regarding financing of SME’s and nursing sick SME’s in the light of fostering this sector so as to enable them to face the challenges of competitions in the liberalized economy. The group makes a number of observations about the significance and also relating to the hindrances faced by this sector. The committee also addressed the concern of lack of timely availability of credit to SSIs in the context and suggest increased role of SIDBI in the same.

1.4.4 Development Banks and the debate on their sustenance:

In the post liberalization era a trend favouring discontinuation of the development bank framework has been noted in the country as in other countries of the world. Yet there exists a contradictory view that there exists enough justification for their sustenance. In this light, Gupta (1999) reflect upon the significance of the development finance
institutions in industrial development in the country. DFIs promoted a large number of new and varied types of financial institutions; they enjoy high credibility amongst the investing public and are a major source of venture capital. Thus, there is ample justification for their sustenance even in the present times. Srivastava and Nigam (1999) make a similar observation in their work. The paper cites various justifications to the aspect of retaining the development bank framework even in the era of liberalization. Sabnani (2000) also address the issues involved in the conversion of development banks to universal banks. Borbora (2001) traces the evolution of development banking in India and provides a number of recommendations on the mode of operations for this group of institutions in the post liberalization era keeping in view their evolving objectives, operations and role.

Mathur (2003) in his article revealed the trend of discontinuation of the DFI framework in the country with the conversion of ICICI and IDBI, IFCI facing similar fate. Karungaran (2005) in his study highlighted the adverse impacts of the poor financial performance of DFIs in the country and argue on the sustenance of this framework. Bajpai (2004) emphasizes that in today’s changing economic environment there is increased need for huge investments and the continuity of DFI framework is therefore of greater significance. But for their own survival and growth, DFIs need to reorient their working and structure so as to operate with greater efficiency. Gokarn (2004) elicits that the cause of the breakdown of the DFI framework in the country since mid-90’s was there incompetence to evaluate projects in the light of stringent competition that followed 1991 reforms. But similar DFI framework did succeed elsewhere in the world. Besides, with no alternatives of long-term finance to industry, there is a case for sustenance of DFIs in the country. Jhaveri (2004) points out that the erstwhile DFI framework of the country is not efficient especially in the present market driven economy. But as risk factor prevents most other financial intermediaries into investing in term financing there is a case of resurrecting the DFI framework. Simha (1999) talks of serious limitations of universal banking like mismanagement risks, monitoring and regulating difficulties and the like. These have been actually witnessed in the developed countries, where we now find a reverse trend from
diversification to concentration in core activity. As he writes, though some blending of commercial banking is unavoidable, yet there is the need of DFIs in the country.

1.4.5 Development banks- changing role and outreach:

Changed economic perspectives in the light of liberalization, privatization and globalization have changed the circumstances of operation of development banks. The economic contexts in which such institutions operate have significant bearing on the organization, form and structure as well as the role playing of development banks. Bruck (2005) elicits a vivid account of such role playing and relevance of development banks in the present times. Poor financial performance of development banks has led to the discontinuation of such institutions. Though profitability is considered important yet it is debated that development oriented institutions must be assessed in parameters beyond mere financial assessments. Attainment of professionalism to enhance performance is proposed by many writers in the context of development banks. Several arguments are cited in this regard.

Nyhart (1964) in his study states in that the staff must be engineered to take up the unique task and challenges in development banking and discusses various attributes of development bankers in the context. Yaron (2005) reflects that the environment of political economy in which DFIs operate is often the cause of the poor financial performance of DFIs. The performance assessment framework of DFIs must emphasize on two criteria, namely, outreach and sustainability.

Francisco et al. (2008) trace the evolving literature relating to the social cost-benefit analysis of DFIs. As is stated by their mission, objectives and nature of performance, DFIs cannot excel in financial performance like other profit oriented financial institutions and therefore an analysis of the benefits they extend to society is very important.

Thorne et al. (2009) argue that in the context of the ongoing debate regarding the social desirability of DFIs the role of DFIs under the socio-economic conditions of their working
needs to be reassessed. They have developed a framework for the successful working of DFI s on the basis different parameters and have stressed upon the social performance assessment of DFI s

1.5 Objectives

The present study attempts to make an in-depth analysis of the role of AFC and NEDFi, the two regional level development banks functioning in Assam, in fostering rapid industrialization in the state, in the light of the following objectives:

1. To analyze the trend and pattern of flow of financial assistance from development banks to Assam.
2. To evaluate the procedures, terms and conditions and developmental functions of development banks.
3. To evaluate the impact made by development banks assisted units on the industrial development of the state.
4. To study how far development banks have been successful in achieving their objective of achieving rapid industrialization in the context of Assam.

1.6 Research Questions

1. Is there any difference in the trend and pattern of credit flow to Assam from the all India development banks and the region specific development banks?
2. Is obtaining loans from development banks less difficult (difficulty perceived as procedures) than obtaining loans from other institutions of term finance?
3. Are there significant differences in terms and conditions of securing term loans from development banks as compared to that from such other sources?
4. Are the developmental functions of development banks necessary for a sustained industrial development of the state?
5. Have development banks assisted industrial units created more impact in the industrial development of the state as compared to other institution assisted units?
6. How far has the development banks succeeded in benefiting their target clients in the light of their objective of achieving rapid industrialization in Assam?

7. How far has the development banks succeeded in benefiting the society in the light of their objective of achieving rapid industrialization in Assam?

1.7 Need for the study

Development banks in India are a post independence phenomenon. They were initiated to bridge the gap between the need of long and medium term credit supply to industries and their availability. Their objectives were later broadened to include the underprivileged clients or sectors as well. Development banks were instrumental in enhancing the pace of industrialization, setting up of new enterprises and promoting balanced industrial development in the country. They were governmental tools in the development process and accordingly their commercial viability was not of prime concern. Since the liberalization of the economy, concern was raised regarding the functional inefficiency of development banks and their mounting losses. Studies conducted earlier on development banks were therefore mostly pertaining to their role and performance in terms of their credit flow, assistance to the industrial sector, development of backward regions, rehabilitation of sick units and their financial and recovery performances. This was also true for studies focusing on the all-India and the regional level development banks functioning in Assam.

The dispersal of financial assistance, the trend and pattern of such dispersal, by AFC and NEDFi, to Assam has been presently studied in comparison with the all-India development banks. With economic reforms and globalization, promoting the competitive efficiency of industries and meeting their increased financial requirements is of utmost importance. In this light, the present study is expected to throw light on the significance of development banks in the state. Findings of the study can be expected to help the policy framers in designing appropriate strategies for assistance-financial or otherwise for industrial development of the state. This is especially so considering the industrial backwardness of the state. Thirdly, there exist no studies on the role of the regional level
development banks, AFC and NEDFi, focusing on their impact on industrialization in Assam in the post liberalization period. The present study makes an effort at this, using diverse dimensions at assessing such impact. Further, it is also believed that like studies at regular intervals hold relevance for an appraisal of the latest trends in the role and operations of such key development institutions of the country.

1.8 Organization of the Thesis

The present study comprises of six chapters, organized as under.

Chapter I provides an insight to the topic of the study, including the sub-topics-introduction, statement of the problem, review of literature, objectives of the study, research questions and the need of the study.

Chapter II consists of the theoretical framework of the study and the methods and methodology adopted for the study.

Chapter III consists of the study of the comparative evaluation of the operational performance of regional level development banks with the all India development banks.

Chapter IV includes a comparative analysis of the functional performance of the regional level development banks with other term loan providing institutions in the state.

Chapter V is a study of the promotional role of the regional level development banks in Assam in the light of their role in industrial development.

Chapter VI consists of the summary of findings of the study, suggestions based on the study and also includes the limitations of the present study and the scope of future research in related aspects of the present topic.