

## **Part-II**

### **INDUSTRIAL FINANCE: SOURCES AND STRUCTURAL COMPOSITION**

#### **Chapter – 3**

#### **EVOLUTION OF SOURCES OF INDUSTRIAL FINANCE AND THEIR STRUCTURAL COMPOSITION**

3.1 Introduction

3 2 Sources of Industrial Finance.

3 2 1 Sources of Industrial Finance Before Independence.

3 2 2 Sources of Industrial Finance after Independence.

3 2 2 1 Term-Lending Financial Institutions at the National Level.

3.2 2.2 Term-Lending Financial Institutions at the State Level

## **Chapter - 3**

### **EVOLUTION OF SOURCES OF INDUSTRIAL FINANCE AND THEIR STRUCTURAL COMPOSITION.**

#### **3.1 INTRODUCTION:**

The success of industrialization depends on factors like entrepreneurship, efficient production techniques, skillful management methods and above all adequate financial resources. Hence, in order to facilitate the implementation of the industrial policies and the execution of the plan objective of rapid industrialization, adequate uninterrupted flow of industrial finance and reliable financial resources are required. Its availability in the requisite proportion on reasonable terms constitutes a significant factor in promoting industrial development.

Industrial finance itself bears a complex nature, although it is rather fascinating. Therefore, industry, whether large, medium or small, in the private or in the public sector, requires fixed capital and working capital as well at three different stage, at the inception, at the point of diversification and while in the stage of growth. In other words, capital is required for expanding, modernizing and developing an industry and on the other hand, for meeting recurring expenses of industry. The proportion of finance in the form of fixed capital and working capital requirement looks to the type of industry, the process of production and level of output to be achieved. In an industry with large scale production with capital-intensive technology, the requirement of fixed capital to working capital would call for very huge proportion. In a medium-sized industry, the proportion would be smaller, while in a case of a small scale industry with labour intensive technology, the proportion would be still smaller. Moreover, the nature of technology and the required length of time for installation are vital determinants of the requirement of finance. For instance, if a industry takes a long gestation period for operation, the requirement of finance would be more and the vice-versa. Besides the gestation period, the

length of operating cycle, terms of purchases and sales, growth and expansion policies of the firm, dividend policy, production policies, business cycle fluctuations and managerial efficiency of the firm are other factors to exert considerable implications on the requirement of finance. Thus, the requirement of finance may vary from industry to industry. The required quantum of finance would change with a changing structure of an industry and modifications in technology from time to time. Therefore, since the Independence, the financial institutions have been making adequate provision of finance to ensure rapid growth of industries in accordance with the priorities and programmes, envisaged in the plans and policies. They are constantly at work to accomplish the financial requirement of organized industries and of newly established industries.

### **3.2 SOURCES OF INDUSTRIAL FINANCE:**

In line with the above, the study seeks to explore the sources of finance on one hand and on the other, to analyze the changing structure of the industrial finance with the passage of time and with the changing global scenario of business. It may be noted at this point that the study restricts its scope to the term lending institutional finance, that the financial institutions of India keep facilitating since the independence. These financial institutions were established at the national and at the state levels by the Government of India, as the need arose with time to provide adequate finance to ensure the growth and development of the Indian industry.

#### **3.2.1 Sources Of Industrial Finance Before Independence:**

In order to workout the objective of the study, it would be worthwhile to have a quick glance at the change in the sources of finance, in the times before independence. Much earlier in the times prior to the First World War, the economic activities like agriculture, trade, commerce, and indigenous industries like Arts and handicrafts were financed by the internal savings of industry itself, entrepreneurial own resources and also by the small class of merchants, money

lenders, and indigenous private bankers. These sources of finance were limited and inadequate for industrial development. At that time, one would agree that the industrial development was almost neglected or ignored because of inadequate supply of finance (Joshi, 1965). This paucity of finance reflected upon the tendency of Indian investors of the time who were proverbially shy and reluctant to invest in industrial securities (Basu, 1939). Thus in those days, as Lal (1990) points out, a mere industrial development was just conspicuous in the absence of institutional promoter's investment, issue houses, underwriting agencies and financial intermediaries. This impeded a free flow of savings to industrial investments that would help industrial development. The managing agency system came into existence in India in the second half of the nineteenth century, when modern industries such as cotton textile, jute textile, coal mining and Iron and steel industries etc. existed. At that time, they were faced with multifarious problems like lack of entrepreneurial ability, dearth of capital and absence of technical and managerial know-how. At that time, the managing agency system emerged to organize, the managing and financing of industries. It means that they did the preliminary work to start new concerns, promote joint stock companies, employ their own funds, or arrange for finance, by acting as guarantors, and also manage the concerns. They provided finance not only for initial fixed capital but also for subsequent extensions, modernization and reorganization. Similarly, the studies conducted by the Dr. Raj K. Nigam (1957), Prof. S.K. Basu (1958), the N.C.A.E.R. (1959) and the Financial commission (1953) reported that in the early days of industrialization, when neither the entrepreneurship nor the capital was plentiful, the managing agents provided both the entrepreneurship and the capital. As a result, India could have well established industries like Cotton and Jute textile, Iron and Steel and plantations etc. They could reach to their present position of dignity due to the pioneering zeal and the fastening care of several well-known managing houses. Hence, in those days, in case the managing agents were absent, India's industrial development in the early part of the century would just be a dream. However, looking to the dominant nature and monopolistic tendencies

of managing agents, the Government of India thought it wise and inevitable to regulate agency houses through the amendments of the Indian Companies Act in 1936 and 1951. Ultimately in 1970 the system was abolished by amending further the Companies Act of 1956 (Kuchhal, 1966). The abolition of this system brought about a replacement of the personal financing system with the institutional financing and it happened in the post Independence period.

Secondly during the mid-wars time, many businessmen moved into industry renouncing their businesses in trading and money lending. The move to industry was stimulated by the Swadeshi Movement. As a result of the spirit of the Swadeshi Movement of 1906-13 many commercial and industrial bank were established to provide industrial finance to industries (Singh, 1974). One such bank was the Tata Industrial Bank established in 1917 and it was followed by other banks. The commercial banks, by their very traditional nature and conservative outlook were, however, reluctant to advance medium and long-term finance to industry. The same view is reiterated by S.K. Basu and Rosen in their study. These industrial banks went into voluntary liquidation within a period of four to five years and failed to provide effective term finance to industries.

The fixed deposits from the public were yet also another source of industrial finance. In fact, the cotton and Jute textile industry were set up in Bombay and Ahmedabad on the basis of this source (Lokanathan, 1935). However, it did not prove a sound source of finance to meet long term investment with short term deposits. In addition to public deposits, there is another form of finance that provided term finance to industry. It is known as public securities market. In the early days of the Independence, it was undeveloped, and devoid of institutions at back up. It means that there were no issue houses or investment trusts or unit trusts to facilitate the placing of new securities like shares or debenture (Gupta, 1969).

Thus, prior to the Independence, India could not achieve much on the front of industrial development and it was because of the absence of term lending financial institutions in India. Hence, a need was felt acutely to have financial institutions to act as an instrument of rapid industrialization. The point was first reiterated by the Industrial commission of 1916-18 and the Indian Central Banking Enquiry Committee in 1931. They suggested setting up of industrial banks to provide for term lending finance to industries. Further P.S.Lokanathan (1969) and S.K.Basu also recommended a setting up of industrial Banks. Although the fact remains that throughout the nineteenth century and right up to the middle of the present century, the concept of separate industrial banks as a force for industrial development did not emerge in India.

In the absence of adequate arrangements for raising long-term finance from external sources, the growth of industry depended mainly on the capital accumulated in entrepreneurial hands, or on a close connection that existed between the sources of entrepreneurship and the sources of finance such was the scenario of the pre-Independence times.

The above overview brings us to agree with L.C. Gupta (1969) whose study states that during the pre independence period, the structure of industrial finance had the closed-circle character of industrial entrepreneurship and a semi-organized and narrow industrial securities market. It was devoid of issuing institutions and virtual absence of participation by intermediary financial institutions in the long term financing of industry. As a result of it, small and medium sized industries were facing a problem of specific financial gaps for industrial development during the post Independence period.

### **3.2.2 Sources of Industrial Finance After Independence:**

Immediately after the Independence, the Government of India played an active role in the providing industrial finance in consistent

with its policy and according to the priorities and programmes of rapid industrialization. Since then the government has taken several significant steps towards creating a network of financial institutions to bridge the gaps in the supply of long-term finance to industries.

#### **3.2.2.1 Term – Lending Financial Institutions at the National Level:**

As a sequel to the above, the Government of India established financial institutions at the national and the state levels. They provide medium and long-term financial assistance to affect rapid industrialization, in conformity with the plans and policies laid down by the government. From a modest beginning in 1948, with the setting up of the IFCI, the structure of financial assistance has been strengthened from time to time. It is done by an addition of new institutions with more flexible structures and by enlarging the resources and the scope of operations of the existing institutions. The present structure of industrial finance comprises following financial institutions at the national level:

##### **1. Industrial Financial Corporation of India (IFCI):**

The Industrial Finance corporation of India is the pioneer of financial institution. It was established in July, 1948. It is by nature a shareholders' corporation. Its purpose to cater to the financial requirement of industries and is to make medium and long term credits readily available to industrial concerns, more particularly in circumstances like the normal banking accommodations are inappropriate, or recourse to the capital issue channels is impracticable (IFCI, 1949). According to L. C. Gupta (1969), the circumstances that are mentioned in the objective of IFCI, have come to be known as the 'Macmillan Gap'. It means that the IFCI envisages its role as that of a gap filler.

According to the role of a gap filler assigned to the IFCI, it is supposed to provide a term financial assistance to large industrial concerns in the public sector and the co-operative sector as well since its inception, and to the private sector since 1972-73. These industrial sectors are engaged in manufacturing, mining, shipping, generation and distribution of electricity.

Therefore, in order to provide finance to the above industries, the corporation is authorised to grant long-term loans as well as to underwrite new issues of industrial securities. These functions of lending or financing have been carried out by the corporation for almost a decade after its establishment. But with the passage of time, the IFCI Act of 1948 was amended from time to time to enable it to diversify its activities and also to keep pace with the all prevailing spirit of industrialization. Accordingly, the Act of the corporation was amended in 1953, 1955, 1957 and 1960. They were a view to expanding the IFCI's operational or financial activities both in scope and size. It was again also to make the provision of financial assistance to the industries through the help of different financial components or instruments.

Since its inception, the corporation was authorised only to transact financial assistance in the form of rupee loans. But with new amendments in the Act, it has now extended its financial operation gradually to cover deferred payment guarantee, foreign currency, guarantees, loans and advances in terms of rupee and foreign currency. It further ventured into promotional activities of public issues in the form of equity and preference shares and debentures, as well as direct subscriptions in the shares and debentures of industrial units. However, its underwriting activity is limited so far to debentures only. These financial provisions are made by the IFCI primarily for setting of new industrial projects and as well for expansion, renovation, modernization and diversification of the existing units.



From the year 1964, the IFCI has become a subsidiary of the IDBI. It continued its financial activities to provide financial assistance to industries. In 1975, it established the Risk Capital Foundation with a view to providing supplementary finance to new entrepreneurs on soft terms. These entrepreneurs were particularly technologists and professionals who would promote medium sized industrial projects.

During 1975-76, the IFCI, along with the IDBI and the ICICI, operated a scheme of granting bridge loans to tackle the time lag problems in project implementation and to achieve greater managerial efficiency. Similarly, a 'Soft Loans Scheme' was introduced by the IDBI in 1976-77. Under this scheme, the IFCI granted financial assistance to traditional industries, particularly Sugar and Jute industries. It was expected that it would solve the problem of aging of equipment and machinery, or help to overcome the back-log of modernization and rehabilitation or replacement, renovation of plant and machinery of these industries. Further, during the period of 1978 to 1984, the IFCI introduced seven non-financial (promotional) activities bearing the nature of 'supportive measures' in relation to promoting the small scale industries.

Since 1986, the IFCI diversified its promotional and financial activities in the field of merchant banking and allied services department. The idea was to encompass other financial services particularly for assignments of capital restructuring, merger and amalgamation, loan syndication, project counseling and trusteeship assignments. It also imparted guidance to entrepreneurs in project formulation and raising resources for meeting project cost.

Further during 1988-89, the IFCI introduced two schemes of financial assistance to industries, viz. (a) equipment leasing scheme for acquiring imported or indigenous machinery and (b) equipment procurement scheme for procuring equipment to industry and then resell the same by endorsement of documents to the existing industrial

concerns. These schemes were floated to promote medium sized industrial projects.

Finally, since its establishment in 1948, the scope and extent of the activities run by the corporation grew over years. With effect from July 1993, the IFCI was converted into a public limited company and it is now known as Industrial Finance Corporation of India Ltd. This liberalized form of the IFCI, incorporated three new companies as subsidiaries during the financial year 1995-96, viz. 1. IFCI Financial Service Ltd., which was supposed to offer merchant banking services, 2. IFCI Custodial Services Ltd., which was supposed to act as a depository and 3. the IFCI Investors Services Ltd., which would act as Registrar and Transfer agents. Further, it also set up a commercial bank and an Asset Management Company and the Mutual fund. All there were done to ensure rapid industrial development.

The Industrial Finance Corporation undoubtedly strengthened the network of financial institutions. However, quite obviously they suffered from flexibility, initiative and drive that were required of a financial institution primarily to cater to financial requirements of industries in the private sector. This led to the creation of two new institutions, viz., the National Industrial Development Corporation (NIDC) and the Industrial Credit and Investment Corporation of India (ICICI).

## **2. National Industrial Development Corporation (NIDC):**

The NIDC was established in October 1954 as a wholly owned Government company. It was not purely and even chiefly, a financial agency. Its objective was to promote industries and it considered it vitally important to fill up the gap in the country's industrial structure. Since 1963, the NIDC ceased to be a financing institution for private industry.

### **3. Industrial Credit and Investment Corporation of India(ICICI):**

The World Bank advised the Government of India that there was an urgent necessity to set up a special institution in India. The new institution was called the Industrial Credit and Investment Corporation of India. It was sponsored by the U.S. Government. Accordingly, the ICICI was established in 1955. It was basically to promote and assist large industrial enterprises in the private sector. Further to fulfill the purpose, the corporation extends assistance in the creation, expansion and modernisation of industrial enterprises. It also encourages and promotes the participation of private capital, both internal and external, in ownership of industrial investment and the expansion of investment market as well.

In order to pursue the objectives of promoting industrial development like IFCI, the ICICI renders its direct assistance in number of ways: (a) granting long-term loans and advances in terms of rupee and foreign currency, (b) underwriting shares and debentures of industrial units, (c) subscribing directly to their shares and debentures, (d) guaranteeing deferred payments and (e) issuing bonds in the foreign money market etc. It is although a financial institution, that is authorised to provide foreign currency loans to new as well as existing industries in the private sector. In fact, the ICICI is lending bulk of foreign currencies loans as compared to the other financial institutions. The distinguishing feature of its functioning is that, it provides underwriting facilities, which are generally avoided by the previously established financial institutions (Gupta 1969). Thus, it has remained from its very inception an issuing-cum-lending institution.

The ICICI in its original was supposed to cater financial needs of the private sector. Yet with the passage of time, it has diversified its financing activities. It has also extended or enlarged the scope of its operation from private sector to joint sector, public sector and co-operative sector. Since 1969, the ICICI started providing foreign currency loans to proprietary and partnership concerns, either directly

or in association with the other institutions such as SFC's and banks. Similarly it also availed foreign currency loans to the industries like chemicals, petrochemicals, heavy engineering and metal products with the idea that it would help them in importing capital equipments from the foreign countries. In 1973, the ICICI started guaranteeing of loans raised from the other private investment sources.

Besides the above direct assistance, the ICICI has participated in the soft loan scheme floated by the IDBI in 1976. The loans under it are given to selected industries particularly in engineering industries for the modernization of their plant and machinery.

In the latter half of the eighties, the ICICI widened the sphere of its financial operations considerably. It set up Merchant Banking Division, that works to raise the finance for industries. It as well undertook the sanctioning of financial assistance in the form of different operations, such as deferred credit, leasing assistance, installment sale assistance, asset credit and venture capital assistance. The ICICI provides leasing assistance for computerization, modernization, replacement of equipment of energy conservation, orientation, pollution control balancing and expansion, etc., in view of these operations.

Further with the changing environment in global business the ICICI diversified its financial and promotional activities. Since 1993, it initiated Project Advisory Services (PAS) to offer advice to private sector companies. It also set up different subsidiary agencies such as the ICICI Securities and Finance Co. Ltd., followed by the ICICI Asset Management Co. Ltd., the ICICI Mutual Fund, the ICICI Investors Services and the ICICI Banking Corporation Ltd., etc., that may provide a variety of financial and promotional services to industries.

The ICICI as well promoted different companies and institutions viz., Credit Rating Information Services of India Ltd., (CRISIL), Technology Development and Information Company of India Ltd., (TDICI) (it may be noted that from October 1998, TDICI is known as

the ICICI Venture Funds Management Company Ltd.). Shipping Credit and Investment Company of India Ltd. (SCICI). (It was then merged with the ICICI in April 1996). The ICICI also introduced Programme for Advancement of Commercial Technology (PACT), Programme for Acceleration of Commercial Energy Research (PACER) and Venture Capital Funds, etc. They provided information on financial and other services to industries in the private sector. Recently, the ICICI also set up a foundation for globalization of Indian industry. It is a trust engaged in activities to strengthen Indian industry for the new international challenges and competitive environment.

In short, the ICICI established itself as one of the top term-lending institutions for industries in the country on the basis of the above operational, financial and promotional activities. It has proved its value in the task of rendering advice and assistance on issues like managerial, technical and administrative. Through it, it has contributed to ensure rapid industrial development in India.

#### **4. National Small Industries Corporation (NSIC):**

The National Small Industries Corporation (NSIC) was established at about the same period of 1955. The purpose was to assist the small-scale industry in promotional, marketing, financing and other support activities. At present, it is emphasized in the field of supply of machinery to small-scale units on hire-purchase basis. But it was difficult for the NSIC to operate effectively, as small industries at were scattered numerously by regional levels. Therefore, the state Governments supported and established Small Industries Development Corporations during the 1960 to 1970. They are modeled broadly on the lines of the NSIC at the national level. Hence, at present, the operations of the NSIC are rightly directed to reach the development to the interiors of backward and rural areas.

## **5. Re-Finance Corporation for Industry Ltd. (RCI):**

Commercial banks in India are following so far traditional and orthodox policies of liquidity and safety. Their direct contribution to the field of industrial finance has been very limited. Hence, in June 1958, the Government of India resolved to establish the Re-Finance Corporation for Industry (RCI). It was supposed to extend refinance facilities to banks that provided medium term loans to industry. In this way, banks are permitted to provide 'term' loans on the basis of relending facilities provided by the Re-finance Corporation (RCI). The RCI, in a way, did not finance to industrial concerns directly. Since 1962, the terms of granting relending facilities were largely liberalized with a view to extending its scope and activities. However, with effect from 1<sup>st</sup> September 1964, the entire business of the RCI was taken over by the Industrial Development Bank of India.

## **6. Industrial Development Bank of India (IDBI):**

India had its own national level competent financial institution, when it set up a body called the IDBI in 1964. Prior to it, India had a wide network of financial institutions and they all had done commendable work in the field of industrial finance, following the objective of rapid industrialization. However, in terms of range and magnitude of finance, these institutions could not meet adequately the requirements of long-term finance for new and growing industries. Further more, their functions were overlapping enough to create confusion among industrial borrowers and there was an absence of the apex organization to co-ordinate diverse functions of diverse industrial financing institutions.

Therefore, a need was felt acutely to have an apex financial institution to facilitate a cohesive structure of industrial finance. It was expected that the apex body would address to the changing needs of emerging industrial structure and growing complexity of their inter-relationship. L.C.Gupta in his study (1969) states that a necessity of

apex financial institution was felt in view of a rapidly rising demand for industrial finance as a result of the large industrial programme. Likewise, V.V.Bhatt (1974) in his study, states that the India needed a central development institution to provide for a "dynamic leadership" in the task of promoting a widely diffused, diversified and yet viable process of industrialization. It was under these circumstances that the IDBI was established in 1964. Initially, it was put as subsidiary to the RBI. It bore dual objectives of promoting all kinds of industries by mobilizing financial resources and coordinating as well as controlling the functions of other financial institutions. It was entrusted with an additional responsibility of acting as the principal financial institution for co-ordinating activities of institutions engaged in the finance, promotion and development of industry.

In 1976, the IDBI delinked its operations with the RBI. It then emerged as an apex agency or a milestone in the operation of institutional finance. It provides, since then, direct or indirect financial assistance to coup the gaps left out in the industrial finance. The purpose is to bridge the gap between supply and demand of industrial finance and to meet the needs of rapid industrialization in the manner the IFCI and the ICICI did. The IDBI grants direct financial assistance to industrial concerns under its project finance scheme. According to the scheme, facilities like financial assistance in terms of rupee and foreign currency loans, underwriting of and direct subscription to shares and debentures, guarantees for loans on deferred payments basis etc. are extended to new and existing industrial projects for expansion, diversification and modernization.

The IDBI also provides indirect assistance to industrial concerns. It is in the forms of (a) refinancing of loans that is given by the SFC's, banks; and (b) subscribing to resources (shares, bonds and debentures) of notified financial institutions like the SFC's, the IFCI, the ICICI, the IRBI and the like. However, it was in regards to raising the volume of refinancing of loans to other institutions that the RCI was merged with the IDBI in 1964, right at its inception. It has diversified

and restructured its operational activities keeping the above lines and keeping right tunes with changing times.

The IDBI introduced the Bills Rediscounting Scheme in 1965 under which bills finances are granted to industrial concerns for the use of indigenous machinery. In 1966, it introduced the scheme for participating in industrial loans and guarantees for widening the area of assistance to large industrial sectors. Further in 1976, it introduced the Soft Loan Scheme for modernization of plant and equipments of cotton textiles and cement industries.

The IDBI introduced the Bridge Finance Scheme in 1976. Under the scheme, loans were provided to industrial concerns for implementation of project as per the schedule. It as well introduced the Seed Capital Assistance Scheme in the same year to augment resources of entrepreneurs for setting up new industrial units in the medium scale sector. In 1977, it introduced the Technical Development Fund Scheme. It was meant to support imports of balancing equipment and the technical know-how to affect technological upgradation of industrial units. Whereas in 1978, it floated the Automatic Refinance Scheme with an objective to finance small scale industries and small road transport operators.

The Government of India revised its policy in 1984 and in the light of the new industrial policy, the IDBI evolved number of innovative schemes of assistance to meet the growing needs of industrial sectors. Accordingly, it modified the Soft Loan Scheme for modernization to finance projects of modernization of production units. The scheme was modified for the upgradation of process, products and technology of industrial sector, energy saving, prevention of pollution and recycling of wastes and byproducts, etc. In 1986, the IDBI launched several other schemes: (a) the Textile Modernization Fund, for modernization of textile industry. The scheme came up at the time when the industry was growing sick very fast largely on account of old and obsolete machinery, (b) the Venture Capital Fund, for the purchase of



technology from abroad and for promoting development of indigenous technology. This fund was modified further in 1994 and it was now called a New Venture Capital Fund. It was meant to provide finance for adaptation and development of imported technology, innovative products and services as well as high-risk, high-return ventures including those in the Information Technology (IT) sector.

Further, in order to provide financial assistance to tiny and small scale industries, the IDBI created a Small Industries Development Fund in May 1986 and the National Equity Fund in August 1987. It provided an equity-type of assistance for setting up new units after the rehabilitation of sick small units. During the same period, it has also introduced the Single Window Scheme for granting term loans and working capital assistance to new tiny and small-scale industry.

Moreover, in order to provide a wide range of financial assistance to industries, the IDBI introduced new schemes with products-base and services-base under the direct finance scheme. They were: (a) Equipment Finance Scheme, to provide foreign currency loans to industrial concerns for the import of capital goods and equipment, (b) the Equipment Refinance Scheme, to provide for expeditions assistance to small and medium enterprises for the acquisition of capital goods, (c) Asset Credit Scheme, to acquire new machinery and equipment and to meet the capital expenditure needs of industrial units, (d) Equipment Leasing Scheme, to purchase industrial equipment on lease basis and (e) the Direct Discounting of Bills Scheme, to sell industrial machinery and equipments on a deferred payment basis, etc. All these schemes were devised with an objective to meet specific needs of the modernization of operational industrial units. In addition, the IDBI also provided non-project finance assistance under schemes like bridge loans, asset credit and equipment finance for Energy Conservation and Energy Audit Subsidy. It also provided corporate loans and long term working capital loans to meet an additional margin money requirements for working capital, that might arise out of increase in volume of operations, expansion and diversification of industrial concerns.

Recently to raise short-term resources, IDBI has introduced a new scheme for working capital finance, which will enable the Bank to serve its customers better and provide greater flexibility in resource mobilization and deployment.

Recently, there arose a need to meet challenges of the emerging competitive environment. In its light the IDBI has changed its pattern of providing financial assistance and also undertaking various types of promotional activities for future industrial development. It has as well diversified its business strategies and expanded the range of products and services. Besides the asset based financing and equipment leasing, the IDBI also provides services like merchant banking, debenture trusteeship and forex services to cater to the varied needs of the corporate sector. Under these services it offers professional advice and services to industry for capital market issues, loan syndications, project appraisal, capital restructuring and host of foreign exchange related services, etc. Through such services, it seeks to promote industry in the corporate sector.

Further, in the post-reform period, the IDBI has set up a number of organizations in collaboration with some other institutions. They are: (a) Entrepreneurship Development Institute of India (EDII): It is a national institute to foster entrepreneurship development. (b) Securities and Exchange Board of India (SEBI): It operates as a capital market regulator committed to orderly market development and investor protection. (c) National Stock Exchange of India Limited (NSEIL): It provides nationwide screen-based trading system. (d) Stock Holding Corporation of India Ltd. (SHCIL): It provides custodial services. (e) Investor Services of India Ltd. (ISIL): It provides varied investor support services. (f) Credit Analysis and research Ltd. (CARE): It is involved in credit rating of instruments. (g) Innovative Funding Scheme for Energy Saving (INFUSE): It looks after conservation of various industrial units. (h) National Securities Depository Ltd. (NSDL): It seeks to usher in an era of script less trading. etc., for the development of capital market infrastructure and the entrepreneurship development.

The IDBI also set up in 1990 a fully-owned stock broking subsidiary such as Small Industries Development Bank of India (SIDBI). It is meant to provide assistance to the small scale sector. It set up several other subsidiaries like: (1) IDBI Capital Market Services Ltd. (ICMS), to provide a range of capital market related services, (2) IDBI Investment Management Co. Ltd. (IIMCo), to manage mutual fund and other investment products to investors; (3) IDBI Bank Ltd., to offer high-tech commercial banking services; (4) the North-Eastern Development Finance Corporation Ltd. (NEDFL) to provide financial assistance to backward regions in the north-east; (5) IDBI Intech Ltd. (IIL), to undertake Information Technology (IT) related activities and (6) Depository participant with the National Securities Depository Ltd. (NSDL), etc. They are established to ensure healthy development of institutional infrastructure of the IDBI and to vitalize a more rapid industrial development.

## **7. Industrial Reconstruction Bank of India (IRBI):**

India was much troubled with industrial sickness growing since 1965 onwards and spreading the adverse effect in industrial sectors. The problem occurred due to factors like old and obsolescent machinery, poor management, shortages of raw materials and lack of infrastructure facilities, etc. These factors are concomitant to the ending process of the industry. Hence to eliminate the problem, a new corporation called Industrial Reconstruction Corporation of India (IRCI) was established in 1971. The aim was to provide assistance of rehabilitation and reconstruction to sick and lockout Industrial Units. If necessary, it would also provide managerial and technical assistance for modernization, expansion and diversification of industries. Dr. P. D. Ojha (1984) states in his study that to reduce the problem of industrial sickness, the institutional framework was developed in the country to take care of industry on a 'cradle to grave basis'. As he points out rightly, the government put up the Industrial Reconstruction Bank of India (IRBI) in 1985. It took over the IRCI. It was basically to overcome inherent difficulties, faced by the IRCI in its efforts to

rehabilitate sick industrial units. The principal function of the IRBI is to finance sick and closed industrial units. It was similar to that of the IRCI. However, the IRBI assists sick industrial units by way of term loans and advances, underwriting of equity shares, bonds and debentures. It also guarantees for loans and deferred payments. It held an authority to provide financial services such as equipment leasing, hire-purchase and equipment finance and to make provision of infrastructure facilities, consultancy, managerial and merchant banking services which are incidental and allied to the task of rehabilitation of sick and closed industrial units.

In the post reform period, although the IRBI set up the Board for Industrial and Financial Reconstruction (BIFR), the principal function of financing rehabilitation of sick industrial units turned out to be irrelevant. As a sequel to it, the IRBI was reconstituted into a full-fledged all purpose development financial institution with adequate operational flexibility and functional autonomy. Accordingly, in March 1997 the IRBI was converted into a government company and incorporated as Industrial Investment Bank of India Ltd. (IIBI). Like the IRBI, IIBI also provides financial assistance to sick industrial units on products and services bases. The only remarkable point of difference was that activities of financing industry shifted its focus from reviving sick units to promote business-oriented activities for rapid industrial development.

#### **8. Shipping Credit and Investment Company of India Ltd. (SCICI Ltd.):**

In view of providing debt and equity finance to the Indian shipping, fishing and related industries the Shipping Credit and Investment Company of India Ltd. (SCICI Ltd.) was incorporated in 1986. During 1992-93, the SCICI diversified its financial activities in manufacturing, infrastructure and service sectors in India. It was mainly promoted by the ICICI and carried out its lending operations in consortium with the ICICI and other two financial corporations bearing

the similar organizational financial structures as well as business ethos. On account of such commonality the SCICI, was finally merged with the ICICI in April 1996. The purpose for the merger was to have a strong capital base and optimize operational efficiency and financial requirement of industries.

### **9. Small Industries Development Bank of India (SIDBI):**

Promotion and sustenance of small scale industries continued to be the central plank of the macro-economic reforms that the Government of India introduced after 1988. It was evident from the initiative taken by the IDBI in setting up the Small Industries Development Bank of India (SIDBI). The SIDBI commenced its operations on 2<sup>nd</sup> April 1990 taking over the operation of the IDBI in the small sector. It was setup as a wholly owned subsidiary of the IDBI. It is a principal financial institution for promotion, financing and development of industry in the small, tiny and cottage sectors. Further, it is supposed to co-ordinate the functions of other institutions engaged in similar activities.

The SIDBI has floated various schemes of assistance comprising: (a) refinance of term loans granted by SFCs / SIDC / Banks and other eligible financial institutions. (b) discounting and rediscounting of bill, i.e. Bill Finance that would arise out of the sale of machinery/capital equipment /components by manufacturers in the small scale sector. It also provides equity type support to specific groups viz. Women entrepreneurs, ex-serviceman and new promoters.

The SIDBI introduced two new schemes during 1992-93: (a) Equipment Finance Scheme, to provide direct finance to existing well-run small scale units that planned for projects like technology upgradation and modernization and (b) Refinance to help resettlement of voluntarily retired workers of NTC (National Textile Corporation) units.

During 1992-93, the SIDBI set up the Venture Capital Fund exclusively for small scale units. Further, the SIDBI offers assistance for seed capital and soft loan assistance through National Equity Fund and through seed capital schemes of specialized lending institutions. It as well offers to the small scale sector refinance loans and services like factoring, leasing, etc.

During 1996-97, the SIDBI introduced a direct assistance scheme viz. Vendor Development Scheme. It offers to the SSIs a package of financial assistance including equity and loans both in rupee and foreign currency.

Again to extend grant or assistance to SSIs, the SIDBI introduced in 1996-97 various agencies and schemes: the Accredited credit rating Agencies, Line of credit, Technology Development and Modernization Scheme, single window scheme, Automatic Refinance Scheme and scheme of Direct Assistance for Development of industrial infrastructure for SSI sector etc.

Recently in 1998-99, the Government has proposed the delinking of the SIDBI from the IDBI. It also proposed to transfer the IDBI's shareholding in SFCs to the SIDBI.

#### **3.2.2.2 Term Lending Financial Institutions at the State Level:**

All the term lending financial institutions, mentioned above are found so far operating at the national level. They offer financial assistance to industries for rapid industrialization in the country. Likewise the State Financial Corporations and the State Industrial Development Corporations, operate simultaneously at the state level, and provide financial assistance to the industries. In both the cases, the objective is to achieve balanced regional growth and to widen the ownership base of industry in the country.

## **1. State Financial Corporations (SFCs):**

When the IFCI was set up in 1948. The purpose was to bridge the gap in institutional finance for large-scale industries and to offer financial assistance to these industries only. It did not consider the problem of term financial requirements of small and medium sized industries. Moreover, a single corporation would not be expected to cater to financial requirements of diversified small industrial units scattered over the vast country like India. To overcome this situation, the government set up separate corporations in various states of India.

The state level financial corporations (SFCs) were established as counterpart of the IFCI. It was accordance with the state Financial Corporation Act 1951. The objective was to cater the financial requirements of small and medium scale industries in states. According to S.K.Basu (1965), the "SFCs constitute the first experiment in the state field of organizing institutional arrangements for providing industrial finance to small and medium sized industry." Similarly, L.C.Gupta (1969) in his study states that, the SFCs were closely modeled on the lines of the IFCI, however, they intended to serve the financial requirement of small and medium sized enterprises according to the general framework prescribed by the State Financial Corporation Act, 1951. Under the Act, different state Governments were supposed to set up SFCs as specialized state level institution to provide term finance to small and medium enterprises in respective regions in line with the priorities of industrial plans.

At present, there are eighteen SFCs that function in different states of India. They are set up to extend long term finance to small and medium scale industrial units organized as public or private companies, co-operatives, partnership or proprietary concerns.

The State Financial Corporations are authorized to render financial assistance to the above industries in the form of term loans and advances, direct subscriptions to equity, debentures, guarantee

loans, deferred payment and underwriting the issue of stocks, bonds or debentures of industrial concerns since its inception.

The state level finance corporations have been offering financial assistance as well to small and medium scale industries since 1970. It is carried out through number of financial schemes like discounting bills of exchange, seed/special capital scheme and scheme of refinance and equity type assistance. They offer such schemes on behalf of the IDBI and the SIDBI. Under the refinance and equity type assistance schemes, the SFCs provides assistance to small road transport operators, artisans in special target groups that hail from social segments like SC/ST, women, ex-service men, physically handicapped and entrepreneurs who have requisite technical expertise to start an industry. Under the seed/special capital scheme, they provide equity type support up to Rs. 4 lakhs on soft terms to small entrepreneurs to bridge the gap between the normal expected level of promoter's contribution and the actual amount the promoters could put in. Since 1989, the SFCs have been extending the scheme to women entrepreneurs too. In addition, to accelerate the industrial development in backward areas, the SFCs have worked out a preferential scheme of concessional financial assistance to industrial units located in the specified backward area. Under this scheme, they offer financial assistance to the industries at a concessional rate of interest, lower margins and reduced service charges. It may be noted that the IDBI recently offers a liberal refinance to the SFCs in view of the loans they extend to industries in backward areas at concessional rate. It is to help to promote balanced regional distribution of industrialization.

In the recent past, the Indian industry experienced increased diversification. To be attuned with it the SFCs offer assistance to units engaged in floriculture, tissue culture, poultry farming, commercial complexes and services like engineering, technical, financial and marketing, etc. In view of the changing business environment, the SFCs have offered equipment leasing facilities and, thus, entered into



fields of technical consultancy, merchant banking, debenture trusteeship, investment activities and capital market related operation. However, all these types of assistance that they offer fall on the same line as those of the IFCI, the IDBI and so on.

Besides the above financial activities, the SFCs can also act as agents of the central and state governments and the government finance organization like the IDBI and the IFCI. It may go in respect of granting loans or advances or subscription to bonds or debentures.

The SFCs have one significant aspect. The financial and promotional activities that they perform for small and medium scale industries vary from corporation to corporation. The difference is marked in the levels of industrial growth in respective states and in their needs and efficiency of administration.

## **2. State Industrial Development Corporations (SIDCs):**

Another significant institutional development occurred in the form of a new set of state level institutions, called State Industrial Development corporations, or State Industrial Investment Corporations (SIDCs/SIICs). They were set up during the sixties and early seventies under the Companies Act, 1956. They were owned wholly by the state Government undertakings to promote and develop medium and large industries in respective states. In order to carry out the functions efficiently the SIDCs were delegated with powers to plan, formulate and execute industrial undertakings or projects or enterprises. In this respect they were supposed to act as an instrument to accelerate the pace of industrialization in relatively backward areas in the state.

At present, there are twenty eight SIDCs/SIICs functioning in the different states of India. They are authorized to provide financial assistance to large and medium industrial concerns in the form of term-loans, underwriting and direct subscriptions to shares and debentures, guarantee for loans and differed payment. In addition to them, the

SIDCs provide risk capital to entrepreneurs by way of equity participation and seed capital assistance. They are also eligible for refinance and rediscounting facilities from the IDBI under its indirect scheme of assistance.