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B.B.A. [Banking]

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DEVELOPMENT BANKING

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SYLLABI-BOOK MAPPING TABLE

Development Banking

Syllabi	Mapping in Book
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INTRODUCTION

NOTES

Development banks are those banks which have been established primarily to provide infrastructure facilities for the industrial growth of the country. They provide financial assistance for both public and private sector industries. In the West, development banking had a long period of evolution. It began with banks being set up in Europe in the early 1800s. In India, however, development banking began to take shape after independence with the first development bank Industrial Finance Corporation of India established in 1948.

Today, there are four types of development banks in India. These are Industrial Development Banks, Agricultural Development Banks, Export-Import Development Banks and Housing Development Banks. This book, *Development Banking*, will examine all aspects of development banking, with special reference to India.

This book is divided into fourteen units that follow the self-instruction mode with each unit beginning with an Introduction to the unit, followed by an outline of the Objectives. The detailed content is then presented in a simple but structured manner interspersed with Check Your Progress Questions to test the student's understanding of the topic. A Summary along with a list of Key Words and a set of Self-Assessment Questions and Exercises is also provided at the end of each unit for recapitulation.

BLOCK - I
BASICS OF DEVELOPMENT BANKING

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UNIT 1 DEVELOPMENT BANKING IN INDIA

Structure

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1.0 INTRODUCTION

Development banks are financial institutions set-up to provide long-term finance for capital-intensive social benefit projects that have a long gestation period with low rate of return such as infrastructure, mining and heavy industry, and irrigation systems. Credit is offered at low and stable rates of interest. Development banks are also referred to as term-lending institutions or development finance institutions. Throughout the unit, the focus is on acquiring knowledge regarding the necessity, establishment and functioning of development banks and the mechanism of development banking.

NOTES

1.1 OBJECTIVES

After going through this unit, you will be able to:

- Explain the origin of banking
- Discuss the structure of the banking system in India
- Describe development banking in India
- Explain the various types of development banks in India
- Recognize the need for development banking in India
- Analyze the management of change in the banking sector
- List the challenges faced by development banks

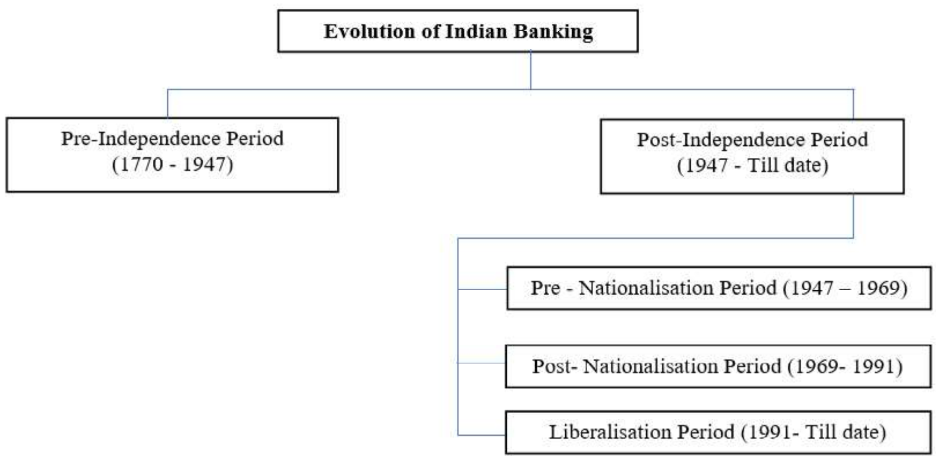
1.2 EVOLUTION OF BANKING

The history of banking is probably as old as the civilization. Even though it is almost impossible to agree on the exact time period when banking began, it is believed that it started around 8000 BC, although the form of it was way different from what we practice today. Back then, it was more of a record-keeping exercise than a banking activity wherein people kept record of their trades in a log. Transactional activities, which to a certain extent resembled modern banking although it did not involve financial lending, started around 2000 BC in Mesopotamian civilization where palaces and temples spread across Babylonia and Sumeria were engaged in lending that was in the form of seeds. It is believed that banking activities in Assyria, India and China also started flourishing during the same period and it involved monetary transactions. Also, around the same period, lenders based in temples in ancient Greece and the Roman empire provided loans.

Actual banking in modern sense originated from the prosperous cities of Venice, Florence and Genoa in Italy during the medieval period. Banking during the 14th century in Florence was dominated by the Bardi and Peruzzi families, who also established many branches across Europe. Medici Bank, the famous Italian bank was established in the year 1397 by Giovanni Medici. Banca Monte deiPaschi di Siena, operating since 1472, is the oldest known bank that is still operational and is headquartered in Siena, Italy. Previously, till the end of 2019, another bank Banco di Napoli, was considered the oldest bank in operation as it was operating since 1463. However, in the year 2002 Italian banking group Sampolo IMI acquired it and later it ceased to operate as an independent bank. The most formidable changes and innovations in banking came in between 17th and 19th century. During this period, major banking developments took place in Amsterdam, the Netherlands in the 17th century and in London in 18th century. Modern day banking activities like issuing debts and accepting deposits etc., were initiated in the 19th century by the banks in London. The Goldsmiths of London are considered to the first real banks, although they were involved in providing vault services where people used to deposit precious metals only to collect later, against fees. Later, they started offering loans. The Bank of London was the first bank to offer bank notes. With time, other facilities like cheque, overdraft and traditional banking activities were added.

1.2.1 Brief History of Indian Banking Industry

Modern banking in India originated at the end of the 18th century. The evolution of banking in India can be categorized into three distinct phases, namely The Pre-Independence Phase —1770 to 1947, Phase II — 1969 to 1991 and Phase III — 1991 and thereafter. Considering the developments that have taken place in the banking sector, we can classify them into the Early Phase that lasted from 1770 till 1969, then the Nationalization Phase from 1969 to 1991 and finally the Liberalization Phase (which is the current phase) from 1991 onwards and still continuing.



The first bank to come into existence in India was Bank of Hindustan in the year 1770 and was located in the then Indian capital Calcutta. However, it failed to continue its operation and closed in 1832. During the same period, another bank by the name of The General Bank of India came into existence in 1786 but ceased its operation just after five years in 1791. In 1881, Oudh Commercial Bank was established and it continued its operations till 1958. The State Bank of India is the largest and oldest bank in India. It was established as Bank of Calcutta in the year 1806 and was renamed as Bank of Bengal in 1809. Two other banks, namely, Bank of Bombay (1840) and Bank of Madras (1843) were established by the presidency government. These three banks were merged together later in 1921 and named the Imperial Bank of India. The Imperial Bank of India was finally renamed as the State Bank of India in the year 1955. The Reserve Bank of India, the central bank of the country, was established on 1st April, 1935 after the Reserve Bank of India Act was enacted in 1934.

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Seven state-controlled banks (State Bank of Patiala, State Bank of Hyderabad, State Bank of Bikaner & Jaipur, State Bank of Mysore, State Bank of Travancore, State Bank of Saurashtra and State Bank of Indore) came under the control of the State Bank of India in 1959 and were referred to as associate banks of the State Bank of India. Later, in 1969, the first phase of nationalization of banks took place when 14 major banks having deposits of more than 50 crores were nationalized. The second phase of nationalization in 1980 saw 6 more banks being nationalized. Of the associate banks, Bank of Saurashtra got merged with the State Bank of India in 2007 and Bank of Indore got merged in 2010. The remaining five associate banks got merged with the State Bank of India in 2017. In order to focus on rural development, Regional Rural Banks (RRBs) were established in 1975.

The final ongoing phase i.e. the Liberalization phase is perhaps the most happening stage in banking development and is witnessing major reforms. One of the most significant developments was the entry of the private sector banks and foreign banks in the Indian banking sector. This period saw the emergence of banks like HDFC Bank, ICICI Bank, UTI Bank (later renamed as Axis Bank), Global Trust Bank (later amalgamated with Oriental Bank of Commerce), IndusInd Bank, Yes Bank and many more.

1. Pre-Independence Period (1770-1947)

The first bank of India was the Bank of Hindustan established in 1770 and was located in the then Indian capital Calcutta. Nonetheless, this bank failed to perform and ceased its operations in 1832. During the Pre-Independence era more than 600 banks got enlisted in the country. However, only few survived.

Following the path of Bank of Hindustan, few other banks were set-up in India. They were:

- The General Bank of India (1786-1791)
- Oudh Commercial Bank (1881-1958)
- Bank of Bengal (1809)
- Bank of Bombay (1840)
- Bank of Madras (1843)

During the British rule in India, The East India Company had set-up three banks: Bank of Bengal, Bank of Bombay and Bank of Madras and considered them the Presidential Banks. These three banks were subsequently converged into one single bank in 1921, which was known as the Imperial Bank of India.

The Imperial Bank of India was subsequently nationalized in 1955 and was named the State Bank of India, which is presently the biggest public sector Bank.

Table 1.1 displays the list of other banks which were set-up during the Pre-Independence period:

Table 1.1 Banks in Pre-Independence Period in India

Pre-Independence Banks in India	
Bank Name	**Year of Establishment**
Allahabad Bank	1865
Punjab National Bank	1894
Bank of India	1906
Central Bank of India	1911
Canara Bank	1906
Bank of Baroda	1908

NOTES

The reasons for failure of many banks during this period were:

- Indian account holders had become increasingly inclined towards fraud
- Banking sector lacked machines and technology
- The banking process was bogged down by human blunders and time consumption process
- Inadequate facilities and
- Lack of appropriate management skills.

Following the Pre-Independence period was the Post-Independence period, which noticed some significant changes in banking operation and it has continued till date.

2. Post-Independence Period (1947-1991)

At the time of India's Independence from colonial rule, all the significant banks operating in the country were led privately which was a reason for worry as the people residing in the rural areas were still reliant on individual money lenders for financial support.

With an intention to resolve this issue, the then Government chose to nationalize the Banks. These banks were nationalized under the Banking Regulation Act, 1949. While, the Reserve Bank of India was nationalized in 1949, the State Bank of India was nationalized in 1955 and 14 other banks were nationalized between 1969 and 1991. The banks that were nationalized had deposits in excess of ₹ 50 crores.

The list of the 14 Banks that were nationalized in 1969 is as follows:

i. Allahabad Bank
ii. Bank of India
iii. Bank of Baroda
iv. Bank of Maharashtra
v. Central Bank of India
vi. Canara Bank
vii. Dena Bank

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viii. Indian Overseas Bank
ix. Indian Bank
x. Punjab National Bank
xi. Syndicate Bank
xii. Union Bank of India
xiii. United Bank
xiv. UCO Bank

In 1980, the following 6 banks were further nationalized, taking the total number of nationalized banks to 20. The banks nationalized in this phase included:

i. Andhra Bank
ii. Corporation Bank
iii. New Bank of India
iv. Oriental Bank of Comm.
v. Punjab & Sind Bank
vi. Vijaya Bank

In addition to the above mentioned banks, the seven associate banks of SBI that were nationalized in 1959 included:

i. State Bank of Patiala
ii. State Bank of Hyderabad
iii. State Bank of Bikaner & Jaipur
iv. State Bank of Mysore
v. State Bank of Travancore
vi. State Bank of Saurashtra
vii. State Bank of Indore

Of all the associate banks, the State Bank of Saurashtra was merged with the State Bank of India in 2008, State Bank of Indore got merged in 2010 and the remaining ones by 2017.

The need to focus on the rural areas and provide thrust to agriculture led the government to establish the Regional Rural Banks in the year 1975.

1.2.2 Impact of Nationalization

There were various reasons why the government chose to nationalize the banks. The nationalization drive impacted the banking sector and the economy in the following ways:

- This lead to an increase in the supply of funds leading to economic development.
- It enhanced competence level and productivity.

- Helped in boosting the rural and agricultural sector of the country.
- It opened up a significant work opportunity for the individuals.
- The government utilized the profit generated by the banks for the betterment of the society.

NOTES

The Post-Independence banking phase takes the credit of initiating major developments in the banking sector of India and also contributed significantly in the growth of the banking sector.

Liberalization Period (1991-Till Date)

The biggest reform during the liberalization period was the introduction of the private sector banking in India. RBI granted license to 10 private sector banks to establish and operate in the country. These banks were:

i. Global Trust Bank
ii. ICICI Bank
iii. HDFC Bank
iv. Axis Bank
v. Bank of Punjab
vi. IndusInd Bank
vii. Centurion Bank
viii. IDBI Bank
ix. Times Bank
x. Development Credit Bank

During this phase, the government, to give further impetus to the banking sector by initiating various banking reforms, set-up a committee under the leadership of Shri. M. Narasimham. The aim was to deliver solidity and effectiveness to the Nationalized Public sector Banks.

The measures taken included:

- Foreign banks were allowed to set-up branches in India.
- Scope of further nationalization was taken off the radar.
- Equal treatment for the public and private sector banks by the government and RBI.
- Joint venture between Indian and foreign banks was allowed.
- Payments banks made entry in banking and technology
- Small finance banks were granted permission to establish branches across the country.
- Indian banking moved online with internet banking and apps available for fund transfer.

NOTES

Thus, the historical backdrop of banking in India shows that with time and the necessities of individuals, significant advancements have been done in the banking sector with an aim to flourish it.

The evolution in the banking sector is still in progress, and every now and then, new reforms are adopted to provide stability to the banking industry that will lead to the economic development of the country.

Today, banks have broadened their activities and are making foray into new operations and services that comprise prospects in credit cards, consumer finance, wealth management, life and general insurance, investment banking, mutual funds, pension funds, stock broking services, and so on. Furthermore, the Indian banks are also going global by opening branches in foreign soil either by themselves or through their associate banks or subsidiaries.

1.3 BANKING SYSTEM IN INDIA

Banking is defined as 'the accepting for the purpose of lending or investment of deposits, money from the public, repayable on demand or otherwise and withdrawable by cheque, draft, order or otherwise'. This definition is given in Indian Banking Regulation Act (1949). This definition envisages two main features: (1) the bank accepts deposits of money which can be withdrawn by cheques, (2) the bank uses the deposits for lending. To be recognized as bank, an institution must use the deposits to give loans to the general public.

Any institution accepting deposits that can be withdrawn by cheques but is being used for its own purpose will be barred from being referred to as a 'Bank'. This is the reason why post offices and savings banks are not considered banks, because even though they accept cheques, they do not offer loans and advances.

1.3.1 Banking Structure in India

The Indian banking system can be broadly categorized as the following:

(a) Organized and unorganized banking

That portion of Indian banking system which are not governed by the banking regulations and work outside the purview of Reserve Bank of India is referred to as the unorganized banking sector e.g., indigenous banks. On the other hand, organized banking sector refers to that part of the Indian banking system which under the control, supervision, influence of RBI and are governed by the Banking Regulation Act, 1949. They are the Commercial Banks, Industrial Banks, Agricultural Banks and the Development Banks.

(b) Scheduled and Non-scheduled banks

Under the Reserve Bank of India Act, 1934, banks are classified as scheduled banks and non-scheduled banks. The scheduled banks are those which are entered in the second schedule of RBI Act, 1939. Scheduled banks are those banks which have a paid up capital and reserves of aggregate value of not less than ₹ 5 lakhs and satisfy terms and conditions set up by the RBI.

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All Commercial Banks, Regional Rural Banks, State Cooperative Banks are scheduled banks. On the other hand, non-schedule banks are those banks whose total paid up capital is less than ₹ 5 lakh and RBI has no specific control over these banks. These banks are not included in the second schedule of RBI Act, 1934.

(c) Indigenous Bankers

Indigenous banking was always different from the modern banking as it worked in the form of family or individual business. They were referred to by various names in different parts of the country, such as Shroffs, Sethus, Sahukars, Mahajans, Chettis and so on. Their size differed from petty money lenders.

(d) Central Bank

In every country, there exists a central bank (in the case of India, it is Reserve Bank of India) which controls a country's cash supply and money management exercised through the monetary policy. It is a bankers' bank and also the Government's Bank and hence is considered to be the lenders last resort. India's Reserve Bank of India (RBI) is the Central Bank.

(e) Commercial Banks

A commercial bank is one that deals with public by accepting deposits and providing loans and advances to individuals and corporates. Credit creation in the economy is done through the process of accepting deposits and providing loans. Some examples of commercial banks in India are the State Bank India (SBI), Punjab National Bank (PNB), HDFC Bank, Axis Bank etc.

(f) Development Banks

Development banks are specialized financial institutions whose primary objective is to stimulate economic development, for which they provide long and medium term loans to entrepreneurs at subsidized interest rates. To name a few, the Industrial Development Bank of India (IDBI), Industrial Financial Corporation of India (IFCI), Industrial Credit and Investment Corporation of India (ICICI) etc., are development banks.

(g) Co-Operative Banks

Co-operative banks are regulated by the provisions laid down in the Co-operative Societies Act. Co-operative banks were initially established in India to deliver credit to the farmers at lower rates. With time, their functioning has expanded into the urban sector also.

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(h) Land Mortgage Banks

The essential target of these banks is to give long term advances in the agricultural sector at low rates in issues related to land. The land mortgage banks are also referred to as Land Development Banks.

(i) Regional Rural Banks (RRBs)

The Regional Rural Banks were set up on the proposals of Narsimham Committee on Rural Credit. The RRBs were set-up so as to develop a banking institution which could work as a business association in rural areas. The main focus of RRBs is to develop agriculture, trade, commerce, industry and related activities among the petty and marginal farmers, agricultural labourers, handicrafts and skilled workers and small entrepreneurs.

(j) National Bank for Agricultural and Rural Development (NABARD)

This bank was established in 1982. The main objective of this bank is to enhance rural happiness by arranging rural credit to the farmers. Basically, it is an apex institution which co-ordinates the functioning of different financial institutions working in the field of rural credit. Further, NABARD has been working continuously endeavouring towards providing institutional credit through its micro-finance programme. One distinguishing feature of this bank was the setting-up of Self-Help Group (SHG) – Bank linkage programme in 1992 with the objective of providing financial services to the rural poor people on a sustainable basis.

(k) Exchange Banks

These banks are engaged in transacting foreign exchange. These banks promote international trade. The 'Export Import Bank' is one such bank that provide long-term financial assistance to the exporters and importers.

Check Your Progress

1. State the three distinct phases in the evolution of Indian banking.
2. Name the first bank that came into existence in India.
3. Mention one distinguishing feature of the liberalization phase of Indian banking.
4. What is the organized banking sector in India?
5. What are development banks?

1.4 DEVELOPMENT BANKING IN INDIA

Development banks are financial institutions that work towards infrastructure development and economic growth in a country. They provide long-term and medium-term finance to the government and private projects for this purpose. They are multi-dimensional and multi-purpose financial institutions involved in lending, investing in securities and also encourage the habit of saving and investment among the general public. With reference to banking, 'Development banks are financial institutions established to lend (loan) finance (money) on subsidized interest rate. Such lending is sanctioned to promote and develop important sectors like agriculture, industry, import-export, housing and allied activities'. Considering the societal aspect, we may refer to 'development banks' as 'those financial institutions whose principal motive is to finance the basic needs of the society.' Such financial assistance results in social and economic development.

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'Development Banking' is a much wider concept than development bank. In addition to the normal banking activities being performed by development banks, development banking also includes in its wings activities that link up of national and local development policies related to industry, agriculture, infrastructure, social and other economic activities. Development banking also includes identification, appraisal and evaluation of development projects and involves financial markets and international financing. Development banking, in general, is being discussed interchangeably with development banks, which, henceforth results in discussion about various development banks like IFCI, IDBI and other development banks. Development banking encourages banks to lend at subsidized or stable interest rates into projects that are necessarily long-term in nature and also have societal contribution.

1.4.1 Evolution of Development Banking

In India, development banking evolved after Independence, with the establishment of various development banks like IFCI (in 1948), IDBI (in 1964), IIBI (in 1972), NABARD and EXIM Bank (in 1982) and SIDBI (in 1992). These development banks were constituted to focus on specific sectors like heavy industries, agriculture, export, housing etc.

The worldwide foundation of development banking might be identified to the establishment of of 'Society General Pour Favoriser I' lndustrieNationale' in Belgium in 1822. It is to be noted that the major organization which became an industrial financer was the 'Credit Mobiliser' of France was set-up in 1852.

In 1920, the Industrial Bank of Japan was established in Japan with the objective of promoting industrial development. After the World Wars, the Industrial Development Bank of Canada (1944), the Finance Corporation for Industry Ltd. (FCI) and the Industrial and Commercial Finance Corporation Ltd. (ICFC) of England (1945), and others were established to give term credits to industry. In 1966, the UK government set up the Industrial Reorganization Corporation (IRC).

India's first development bank is Industrial Finance Corporation of India (IFCI), which was set-up in 1948.

1.4.2 Definition of Development Bank

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There is no single definition of development bank. Authors William Diamond and Shirley Bosky recognize industrial finance and development establishments as 'development banks'. Primarily, a development bank is a term lending institution.

In simple words, a development bank is a multi-purpose financial organization which has a development perspective. A development bank provides financial assistance of numerous kinds such as credits, underwriting, investment and guarantees, and ultimately work towards financial development and industrial progress.

1.4.3 Features of a Development Bank

The significant features of a development bank are the following:

1. It is a financial institution.
2. It offers medium and long-term finance to business enterprises.
3. In contrast to commercial banks, development banks cannot accept deposits from the public.
4. Its role is multi-dimensional as it not only provides term loans but also performs various other developmental financial activities.
5. It is basically a development-oriented bank. Its essential purpose is to stimulate monetary improvement by encouraging investment and entrepreneurship. It energizes new and smaller business entities and looks for balanced territorial development.
6. Development banks are financer to both, public and private sector organizations.
7. It promotes savings and investment.
8. It does not rival the typical channels of money, i.e., amounts previously made accessible by the banks and other regular monetary establishments. Its significant job is that of a gap filler.
9. The main intention is to aid public interest rather than rake up profits, as development banks works in the overall interest of the country.

1.4.4 Implications of Development Banking in India

Development banking has played a central role in the progress of the banking sector and the economy at large. Immediately after Independence, with the inception of IFCI, India's first development bank, the ball was set rolling for long-term financing. In the early 1950s, State Financial Corporations were created that started providing support to the State level SMEs.

ICICI was the established to take care of foreign exchange loans. Various other development financial institutions like Agriculture Refinance Corporation, Rural Electrification Corporation and Housing and Urban Development Corporation provided the requisite support to enterprises operating in agriculture, power and housing sector. The impact of the development banks gradually increased with time and grew to 10.3 per cent in 1990–1991 and 15.2 per cent in 1993-1994 from 2.2 per cent of GDP in 1970-71. This period from 1960s to 1990s is considered as the second phase of India's development banking, during which various sector specific development banks like NABARD to take care of agriculture and SIDBI for small industries development.

The implication of development banking can be gauged from the fact that the development banks contribution in the capital formation has steadily increased over the years. They contributed in the form of providing loans, participating in underwriting business and direct subscriptions of shares and debentures. Aggregate disbursals as a ratio of net capital formation in the private sector rose from 24 per cent in 1970-1971 to 80 per cent before the 1991 crisis. The facility of long-term industrial finance proved to be a major source of support for investment. The various sectors that were benefitted from the development financial institutions include manufacturing, agribusiness, infrastructure, services, energy and construction.

1.5 VARIOUS TYPES: DEVELOPMENT BANKS IN INDIA

During the Post-Independence era, India was served by an organization of development banks, both at the national and state levels. The Industrial Finance Corporation of India (IFCI), the primary development bank of the nation, was set-up in 1948. Gradually, many other financial institutions were set-up.

Types of Development Banks

Development banks in India may be classified into three groups:

(I) Industrial development banks, (II) Agricultural development banks, and (III) Export-import development bank.

I. Industrial development banks may further be divided into the following two groups:

   (A) All-India institutions, and (B) State-level institutions.

   There are five all-India industrial development banks at present operating in India. These are:

   i. The Industrial Finance Corporation of India (IFCI)
   ii. The Industrial Development Bank of India (IDBI)
   iii. The Industrial Reconstruction Bank of India (IRBI)
   iv. The National Small Industries Corporation (NSIC)

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v. The Industrial Credit and Investment Corporation of India (ICICI)

While the top four are state owned institutions, ICICI is a private sector bank. All these institutions, excepting the NSIC, accommodate the financial and improvement needs of the large industries, while the NSIC deals with the small-scale industries.

A foundation called the National Industrial Development Corporation (NIDC) was set-up by the Government of India in 1954 for the advancement and improvement of enterprises in India. Initially, it was a financer to the jute and cotton material enterprises. However, today it works just as a counselling office.

The state-level industrial development banks include; (i) the State Financial Corporation's (SFCs), (ii) the State Industrial Development Corporations (SIDCs), and (iii) the State Industrial Investment Corporations (SIICs).

II. Agricultural development banks are classified into:

(a) All-India level, (b) State-level, and (c) Local- level institutions

As of now, there is just a single all-India level agricultural development bank called the National Bank of Agriculture and Rural Development (NABARD). Initially, there was the Agricultural Refinance and Development Corporation (ARDC), set-up in 1963 to give medium and long-term assistance for the improvement of agriculture. NABARD replaced it in 1982.

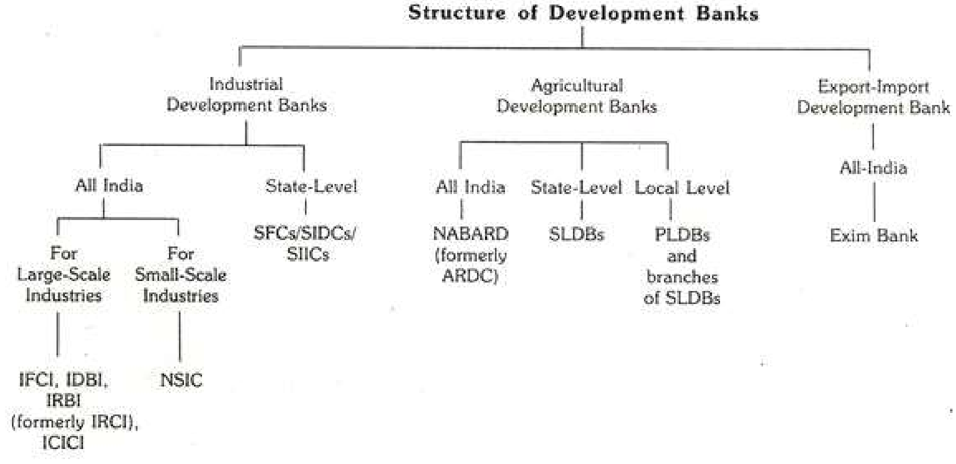
State Land Development Banks (SLDBs), formerly known as Central Land Mortgage Banks, exists at the state level and are providing medium and long-term credit to agriculture. Moreover, primary land development banks and the branches of SLDBs also operate at the local level.

III. Export – Import Development Bank

For encouraging and supporting exports and imports, Export-import Bank of India (EXIM Bank) was established in 1982.

The structure of development banks in India is outlined in the following chart:

Chart 1
Structure of Development Banks



1.5.1 The Need for Development Banking in India

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Development bank is a national or regional financial institution designed to provide medium- and long-term capital for productive investment, frequently supplemented by technical support, in underdeveloped and developing countries. In India, we have IFCI (Industrial Finance Corporation of India), IDBI (Industrial Development Bank of India), SIDBI (Small Industries Development Bank of India) to provide necessary capital for the industrial, agricultural and the services sector progress.

The development banking activity is needed to provide impetus to the inclusive development of the economy. Development banking contributes across all sectors for the overall development of the economy. The need for development banking can be enumerated as follows:

- Stimulating and improving small-scale industries (SSI) in India
- Undertake the development of the housing sector in India
- Financially facilitating large-scale industries (LSI) in India
- Assisting agricultural sector and rural India
- Increase the volume of foreign trade
- Reviewing and reviving sick industrial units
- Entrepreneurship development
- Usher in economic activities in backward regions of the country
- To contribute in the growth of capital markets

1. Stimulating and improving Small-Scale Industries (SSI) in India:

Development banks contribute in a significant way in the promotion and improvement of the small-scale sector. The Government of India (GOI) started the Small Industries Development Bank of India (SIDBI) to deliver long and medium-term loans to Small Scale Industries (SSI) units. Project and equipment financing to SSI is treated as a priority by SIDBI. In addition to it, it also refinances financial institutions that provide seed capital to SSI units.

2. Undertake the development of the housing sector in India

In order to support and finance the housing sector, GOI constituted the National Housing Bank (NHB) in 1988. NHB promotes the housing sector by refinancing banks and financial institutions that provide credit to the housing sector.

3. Financially facilitating large-scale industries (LSI) in India

The development bank like IDBI, IFCI, etc., facilitates the large-scale industries by providing medium and long-term loans to the corporate sector. Along with financial assistance, the development banks also provide merchant banking services that include doing feasibility studies, preparing project reports, making appraisals etc.

4. Assisting agricultural sector and rural India

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Development banks like the National Bank for Agriculture & Rural Development (NABARD) are primarily set-up to assist and develop the agricultural sector. NABARD, established in 1982, provides refinance to banks, which finances the agriculture sector and do financing for rural development. It also coordinates with every financial institution that is involved in the financing of agricultural activities. That includes training and agricultural research.

5. Increase the volume of foreign trade

Promoting foreign trade is one of the most important agenda for the Development banks. The Government of India constituted the Export-Import Bank of India (EXIM Bank) in 1982 to provide medium and long-term loans to exporters and importers from India. EXIM bank offers credit to foreign buyers to purchase Indian capital goods and also, encourages banks in foreign countries to provide financial help to the importers in their country to make purchases from India.

6. Reviewing and reviving sick industrial units

Development banks not only assess the financial distress but also revive sick-units through restructuring. For the purpose of revival of sick units, the GoI established the Industrial Investment Bank of India (IIBI) to help sick units. IIBI focusses on financing and revival of sick units. It accelerates modernization, restructuring, and diversification of units plagued by financial distress.

7. Entrepreneurship Development

Most of the development banks encourage entrepreneurship by imparting training to develop leadership and management skills. Seminars and workshops are conducted for the benefit of entrepreneurs.

8. Usher in economic activities in backward regions of the country

Development of the rural and backward areas is facilitated by development backs through financial assistance to regional entrepreneurs.

9. To contribute in the growth of capital markets

The development banks play a significant role in the growth of capital markets by investing in stocks and debt instruments like debentures of various companies listed in the stock exchanges. They also invest in mutual funds too.

1.5.2 Scope of Development Banks

Considering the state of the economy and the functioning of the financial system, the scope for development banking is widespread. Various areas where it can contribute and prove its relevance vary from providing funds, generate employment, support infrastructural facilities, accelerate industrialization, provide thrust to the development of backward areas, and be an active participant in planned development.

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Check Your Progress

6. Name few development banks established in India.
7. In which year was the Industrial Finance Corporation of India (IFCI) established in India?

1.6 MANAGEMENT OF CHANGE IN THE BANKING SECTOR

According to Lamarsh, 'Change Management is an organized, systematic application of the knowledge, tools, and resources of change that provides organizations with a key process to achieve their business strategy.'

With respect to the Indian banking industry, one can say that there has been a paradigm shift in the banking operation in the last two decades. Digitisation has replaced physical banking to a large extent. One can cite examples like interactions with digital anchors, branchless banking, contactless technologies etc.

One of the most notable changes in the banking sector is financial inclusion. The RBI has persuaded the Central Government to propagate financial inclusion through various schemes like:

- Pradhan Mantri Jan Dhan Yojana (PMJDY)
- Atal Pension Yojana (APY)
- Pradhan Mantri Vaya Vandana Yojana (PMVVY)
- Stand Up India Scheme
- Pradhan Mantri Mudra Yojana (PMMY)
- Pradhan Mantri Suraksha Bima Yojana (PMSBY)
- Sukanya Samriddhi Yojana
- Jeevan Suraksha Bandhan Yojana

Use of technology has changed the face of baking operations in the country. It has been able to profoundly contribute in enhancing productivity. The adoption of Core Banking Solutions (CBS) in 2002 initiated the usage of sophisticated technological solutions to enhance the operational performance of banking sector. The CBS technology has been useful in enhancing bank-to-client interactions and has eased the calculation of penalties, interests, and maturity amount. Moreover, the integration of technology in the banking operations has lead to greater customer experience. Presently, the following government approved digital banking platforms are in operation in India.

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- Unified Payment Interface (UPI)
- Bharat Interface For Money (BHIM)
- National Unified USSD Platform
- Aadhar Enabled Payment System

Mergers in recent times have almost reversed the much hailed nationalization of banks. The structural changes in the banking sector have reduced the number of public sector banks to 12 from 27. The list of most recent public sector banking mergers is as follows:

- Vijaya Bank and Dena Bank have merged with Bank of Baroda from April 2019.
- United Bank of India and Oriental Bank of Commerce have merged with Punjab National Bank in April 2020. Thus, PNB has become the second-largest public sector bank in India.
- Syndicate Bank has merged with Canara Bank from April 2020.
- Allahabad Bank has merged with Indian Bank with effect from April 1, 2020.
- Andhra Bank and Corporation Bank of India have merged with Union Bank of India from April 2020.

Apart from the above there were various banking sector reforms like:

- Recommendations of Narasimham Committee in the first phase of banking reforms were relating to (i) Reduction in Liquidity Ratio; (ii) Reduction in Cash Reserve Ratio; (iii) Abolition of Directed Credit Programmes; (iv) Free determination of Interest Rates; (v) Establishment of Special Tribunals; (vi) Improvements in Accounting System of Banks; (vii) Restructuring of Banking System; (viii) Licensing of Banks; and (ix) freedom of banks.
- The second phase of changes covered issues like strengthening of banking system, improve asset quality, strictly follow prudential norms and disclosure requirements, improve the systems and banking methods, and address structural issues like mergers, conversions, restructuring of weak banks.

1.7 CHALLENGES FACED BY DEVELOPMENT BANKS

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1. Development banks got disgrace due to the mounting non-performing assets.
2. This was primarily due to politically motivated lending and inadequate professionalism in project assessment and viability study.
3. Following the recommendations of the Narasimham Committee report in 1991, reforms were initiated and development finance institutions got converted to commercial banks.
4. This resulted in a steep fall in long-term credit from a tenure of 10-15 years to five years.

Check Your Progress

8. Mention one of the significant changes that have taken place in the Indian banking sector in recent times.
9. Name some of the digitally-enabled government-approved banking platforms that have come into effect in India.

1.8 ANSWERS TO CHECK YOUR PROGRESS QUESTIONS

1. The three distinct phases in the evolution of Indian banking are namely, The Pre-Independence Phase - 1770 to 1947, Phase II - 1969 to 1991 and Phase III - 1991 and thereafter.
2. The first bank to come into existence in India was Bank of Hindustan in the year 1770 and was located in the then Indian capital Calcutta.
3. One distinguishing feature of the liberalization phase of Indian banking was the entry of the private sector banks and foreign banks in the Indian banking sector. It is during this period that saw the emergence of banks like HDFC Bank, ICICI Bank, UTI Bank (later renamed as Axis Bank), Global Trust Bank (later amalgamated with Oriental Bank of Commerce), IndusInd Bank, Yes Bank and many more.
4. Organized banking sector refers to that part of the Indian banking system which under the control, supervision, influence of RBI and are governed by the Banking Regulation Act, 1949. They are the Commercial Banks, Industrial Banks, Agricultural Banks and the Development Banks.

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5. Development banks are specialized financial institutions whose primary objective is to stimulate economic development, for which they provide long and medium term loans to entrepreneurs at subsidized interest rates.
6. In India, development banking evolved after Independence, with the establishment of various development banks like IFCI (in 1948), IDBI (in 1964), IIBI (in 1972), NABARD and EXIM Bank (in 1982) and SIDBI (in 1992).
7. The Industrial Finance Corporation of India (IFCI), the primary development bank of the nation, was set-up in 1948.
8. Financial inclusion one of the significant changes that has taken place in the Indian banking sector in recent times.
9. Some of the present digitally-enabled government-approved banking platforms that have come into effect in India are the following:
   - Unified Payment Interface (UPI)
   - Bharat Interface For Money (BHIM)
   - National Unified USSD Platform
   - Aadhar Enabled Payment System

1.9 SUMMARY

- The history of banking is probably as old as the civilization. Even though it is almost impossible to agree on the exact time period when banking began, it is believed that it started around 8000 BC, although the form of it was way different from what we practice today.
- Actual banking in modern sense originated from the prosperous cities of Venice, Florence and Genoa in Italy during the medieval period. Banking during the 14th century in Florence was dominated by the Bardi and Peruzzi families, who also established many branches across Europe.
- The Bank of London was the first bank to offer bank notes. With time, other facilities like cheque, overdraft and traditional banking activities were added.
- Modern banking in India originated at the end of the 18th century. The evolution of banking in India can be categorized into three distinct phases, namely The Pre-Independence Phase —1770 to 1947, Phase II — 1969 to 1991 and Phase III — 1991 and thereafter.
- The first bank to come into existence in India was Bank of Hindustan in the year 1770 and was located in the then Indian capital Calcutta. However, it failed to continue its operation and closed in 1832.

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- Seven state-controlled banks (State Bank of Patiala, State Bank of Hyderabad, State Bank of Bikaner & Jaipur, State Bank of Mysore, State Bank of Travancore, State Bank of Saurashtra and State Bank of Indore) came under the control of the State Bank of India in 1959 and were referred to as associate banks of the State Bank of India.
- The final ongoing phase i.e. the Liberalization phase is perhaps the most happening stage in banking development and is witnessing major reforms. One of the most significant developments was the entry of the private sector banks and foreign banks in the Indian banking sector.
- At the time of India's Independence from colonial rule, all the significant banks operating in the country were led privately which was a reason for worry as the people residing in the rural areas were still reliant on individual money lenders for financial support.
- The Post-Independence banking phase takes the credit of initiating major developments in the banking sector of India and also contributed significantly in the growth of the banking sector.
- The evolution in the banking sector is still in progress, and every now and then, new reforms are adopted to provide stability to the banking industry that will lead to the economic development of the country.
- Any institution accepting deposits that can be withdrawn by cheques but is being used for its own purpose will be barred from being referred to as a 'Bank'. This is the reason why post offices and savings banks are not considered banks, because even though they accept cheques, they do not offer loans and advances.
- Indigenous banking was always different from the modern banking as it worked in the form of family or individual business.
- The Regional Rural Banks were set up on the proposals of Narsimham Committee on Rural Credit.
- 'Development Banking' is a much wider concept than development bank. In addition to the normal banking activities being performed by development banks, development banking also includes in its wings activities that link up of national and local development policies related to industry, agriculture, infrastructure, social and other economic activities.
- In India, development banking evolved after Independence, with the establishment of various development banks like IFCI (in 1948), IDBI (in 1964), IIBI (in 1972), NABARD and EXIM Bank (in 1982) and SIDBI (in 1992). These development banks were constituted to focus on specific sectors like heavy industries, agriculture, export, housing etc.
- During the Post-Independence era, India was served by an organization of development banks, both at the national and state levels. The Industrial

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Finance Corporation of India (IFCI), the primary development bank of the nation, was set-up in 1948. Gradually, many other financial institutions were set-up.

- Development bank is a national or regional financial institution designed to provide medium- and long-term capital for productive investment, frequently supplemented by technical support, in underdeveloped and developing countries.
- In order to support and finance the housing sector, GOI constituted the National Housing Bank (NHB) in 1988. *NHB promotes the housing sector by* refinancing banks and financial institutions that provide credit to the housing sector.
- Development banks not only assess the financial distress but also revive sick-units through restructuring. For the purpose of revival of sick units, the GoI established the Industrial Investment Bank of India (IIBI) to help sick units.
- With respect to the Indian banking industry, one can say that there has been a paradigm shift in the banking operation in the last two decades. Digitisation has replaced physical banking to a large extent. One can cite examples like interactions with digital anchors, branchless banking, contactless technologies etc.

1.10 KEY WORDS

- **Commercial Bank:** This type of bank deals with public by accepting deposits and providing loans and advances to individuals and corporates.
- **Regional Rural Banks (RRBs):** These banks were set-up so as to develop a banking institution which could work as a business association in rural areas. The main focus of RRBs is to develop Agriculture, Trade, Commerce, Industry and related activities among the petty and marginal farmers, agricultural labourers, handicrafts and skilled workers and small entrepreneurs.
- **National Industrial Development Corporation (NIDC):** It was set-up by the Government of India in 1954 for the advancement and improvement of enterprises in India. Initially, it was a financer to the jute and cotton material enterprises. However, today it works just as counselling office.
- **Industrial Investment Bank of India (IIBI):** It was established to help sick units. IIBI focuses on financing and revival of sick units. It accelerates modernization, restructuring, and diversification of units plagued by financial distress.

1.11 SELF ASSESSMENT QUESTIONS AND EXERCISES

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Short-Answer Questions

1. What was the impact of nationalization on the Indian banking sector?
2. List the significant features of the liberalization phase of the Indian banking sector.
3. What are the features of a development bank?
4. What led to the rise of development banking in India?
5. List the challenges faced by development banks.

Long-Answer Questions

1. Discuss the history of Indian banking.
2. Explain the banking structure in India.
3. 'Development Banking' is a much wider concept than development bank. Elucidate the statement.
4. Examine the significant changes that have taken place in the Indian banking sector in recent times.

1.12 FURTHER READINGS

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UNIT 2 INDUSTRIAL FINANCIAL CORPORATION OF INDIA (IFCI)

Structure

2.0 Introduction
2.1 Objectives
2.2 IFCI: Introduction
  2.2.1 History of IFCI
  2.2.2 Vision
  2.2.3 Mission
  2.2.4 Values
2.3 Origin of IFCI
2.4 Financial Assistances Offered by IFCI
2.5 Functions and Objectives of the Industrial Finance Corporation
  2.5.1 Functions
  2.5.2 IFCI Subsidiaries and Associates
  2.5.3 Social Sector Initiatives: Societies
  2.5.4 Scope of IFCI
2.6 Answers to Check Your Progress Questions
2.7 Summary
2.8 Key Words
2.9 Self Assessment Questions and Exercises
2.10 Further Readings

2.0 INTRODUCTION

IFCI is India's first development financial institution. It was established on 1 July 1948. After liberalization started in the early 1990s, the constitution of IFCI changed from a statutory corporation to a company under The Companies Act, 1956. Subsequently, the name of the company was also changed to 'IFCI Limited' with effect from October 1999.

2.1 OBJECTIVES

After going through this unit, you will be able to:

- Explain the establishment and functioning of IFCI
- Analyze the contribution of IFCI in the industrial development of the country
- Discuss the various assistance schemes offered by IFCI

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2.2 IFCI: INTRODUCTION

The Industrial Finance Corporation of India is a Non-Banking Finance Company in the public sector. Set-up in 1948 as a statutory company, IFCI is right now an organization listed on BSE and NSE. There are six subsidiary companies and one associate company that are presently managed by the IFCI.

IFCI offer financial assistance for the multi-dimensional development of industries across the country. Its financing offerings cover different sort of various infrastructural projects that include airports, roads, telecom, power, housing and real estate, manufacturing, and also the services sector and such other united ventures. During its 70 years of presence, mega ventures, namely, Adani Mundra Ports, GMR Goa International Airport, Salasar Highways, NRSS Transmission, Raichur Power Corporation, have been set-up with monetary help of IFCI.

The organization has assumed a significant part in setting up different reputed market intermediaries in a few specialized segments like stock markets, entrepreneurship development institutions, consultancy associations, skill development and instructional institutions within the country.

The Government of India has set a Venture Capital Fund of ₹ 200 crores for Scheduled Castes (SC) with IFCI with an expectation to promote, educate and encourage entrepreneurship among the Scheduled Castes (SC) and to make concessional funding. IFCI has likewise dedicated a commitment of ₹50 crores as lead financial specialist and sponsor of the Fund. IFCI Venture Capital Funds Ltd., a subsidiary of IFCI Ltd., is the Investment Manager of the Fund. The Fund has been operationalized since FY 2014-15 and IVCF is in constant pursuit to attain the expressed goal of the plan.

Further, in March 2015, the Ministry of Social Justice and Empowerment, Government of India assigned IFCI as the nodal office for the implementation of the 'Credit Enhancement Guarantee Scheme for Scheduled Castes' and to make concessional funding to them.

2.2.1 History of IFCI

IFCI Ltd. was set-up in 1948 as Industrial Finance Corporation of India, a Statutory Corporation, through 'The Industrial Finance Corporation of India Act, 1948' of Parliament to offer medium and long-term fund to the industry. After cancellation of this Act in 1993, IFCI turned into a Public Limited Company enrolled under the Companies Act, 1956. On December 21 2012, IFCI turned into a Government controlled organization as a result of increase in Government of India's shareholding to 55.53 per cent. In April, 2015, the Government of India procured six crore Preference Shares of IFCI Ltd. of ₹10/ - each from six public sector banks. With this, the shareholding of the Government of India paid-up share capital of IFCI shot up to 51.04 per cent and IFCI has become a Government Company under

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Section 2(45) of the Companies Act, 2013. IFCI is additionally a Systemically Important Non-Deposit taking Non-Banking Finance Company (NBFC-ND-SI), enrolled with the Reserve Bank of India.

The essential business of IFCI is to give medium to long-term monetary assistance to the manufacturing, services and infrastructure sectors. Through its subsidiaries and partner associations, IFCI has entered into various other financial activities like including broking, advisory, depository and factoring services, venture capital, and so on. As a component of its development directive, IFCI was one of the sponsors of National Stock Exchange (NSE), Stock Holding Corporation of India Ltd (SHCIL), Technical Consultancy Organizations (TCOs) and socially contributing institutions like Rashtriya Gramin Vikas Nidhi (RGVN), Management Development Institute (MDI) and Institute of Leadership Development (ILD).

The Government of India, according to the Budget for FY 2014-15 ordered IFCI for setting up of a Venture Capital Fund under Social Sector activities with an objective to promote entrepreneurship among the Scheduled Castes (SC) and to give concessional funding.

2.2.2 Vision

To be the leading development institution for industrial and infrastructure sectors across the spectrum and be an influential partner in country's economic growth and development.

2.2.3 Mission

- To adopt the best practices in financing industry and infrastructure and leverage core competencies in promoting sustainable industrial and infrastructure development in the country.
- To act as a competitive, client friendly and development-oriented organization delivering financial products and services to the satisfaction of all stakeholders.

2.2.4 Values

- Zeal to shine and zing for change
- Integrity and decency in all issues
- Respect for poise and capability of people
- Strict adherence to responsibilities
- Ensure speed of reaction
- Foster learning, innovativeness and cooperation
- Loyalty and pride in IFCI

Check Your Progress

1. When was Industrial Finance Corporation of India established?
2. What is the vision of Industrial Finance Corporation of India?

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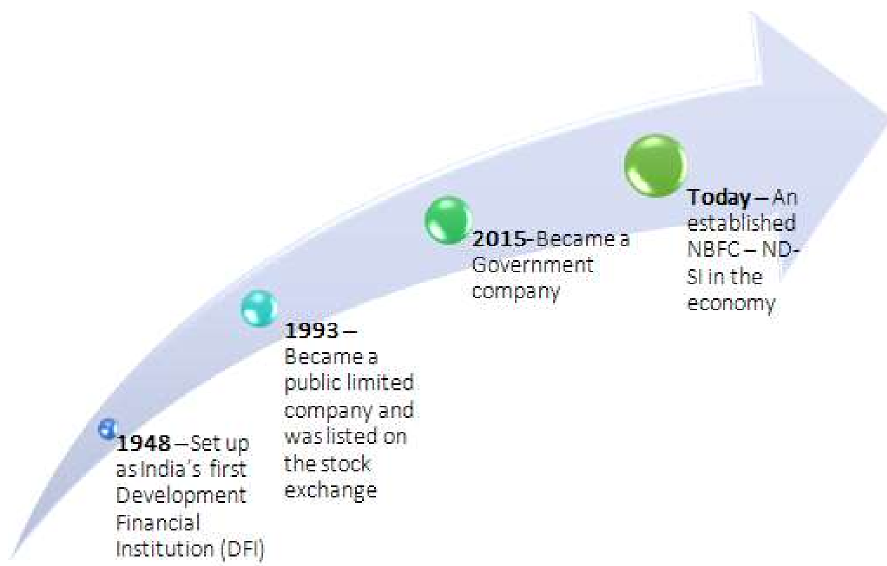
2.3 ORIGIN OF IFCI

The strategy of fast-tracking the pace of economic growth by equipping the enterprises with medium and long-term capital through state-supported specific financial institutions or development banks is not something new in India. Despite the fact that development banks came into existence after the independence, the Indian lenders and financiers had felt the need to promote businesses right at the beginning of the 20th century.

The Indian economy was exposed by the absence of financial intermediaries, promoters and underwriters. This obstructed the mobilization of savings leading to industrial development. Before 1906, domestic financiers were the primary financial source. However, their contribution could assist only small size businesses. The requirement was for long-term financing and at the same time the development of business entities in the economy. Truth be told, around then, a modest bunch of financial agents were catering to the needs of long-term finance in the industry, which was done from their own income. The Fiscal Commission detailed, 'In early days of industrialisation, when neither enterprise, nor capital was plentiful, the managing agents provided both, and India's well-established industries like cotton. Juteand steel owe their present position to the pioneering zeal and fostering care of several well-known managing agency houses.' But the so called financial agencies themselves disrupted the expansion of business venture. Because of its monopolistic nature, a balanced development of capital market was halted. Their inclination for early profit-making prompted advances being offered to only those manufacturing entities that have high profit possibilities. Their misconduct overwhelmed the financial scene not just at the expense of unprotected small businessmen but also neutralized the interest of the State and the local community.

C.D. Deshmukh, the Reserve Bank of India's first Indian Governor, worked out the plan and made a proposal for the establishment of an industry dedicated financial institution in the form of Industrial Finance Corporation and model it on the lines of the Finance Corporation in the United Kingdom. At that point, the Reserve Bank of India stepped up in drafting the bill for the foundation of an Industrial Finance Corporation and sent the proposal to the Central Government in January 1946. It was chosen to present the Bill in the Central Legislative Assembly during the budget session in 1946. However, due to immense work, the Bill could not be presented. Thereafter, the Bill was presented in the Constituent Assembly of Free India in November 1947 by the then Finance Minister, R.K.S. Chetty. While presenting the Bill, the minister described it as a measure of public significance, determined to enhance the industrial advancement of India. He, along these lines, unequivocally asked the House to acknowledge the Bill, which was a long overdue. During the debate on the Bill, B.P.Sitaramaya highlighted the increased resources of the Corporation and opined, 'an institution has to be brought into existence to lend to the manufacturers and to finance the financiers.' Simultaneously, proposals from all Sections of the house for the setting up of similar monetary institutions in various states were likewise received. In fact, the proposal for institutional financing of industry received praise from individuals across the political spectrum. Despite the fact that a few reactions were made with respect to the extension, assets and constitution of the organization, there was practically ideal unanimity of perspectives about the convenience of such a foundation. The report of the select council was introduced in the house on 28th January 1948 and the Bill was at last passed on 13 February 1948. It got the consent of the Governor-General on 27 March 1948 and it was known as the Industrial Finance Corporation Act 1948. Likewise, the IFCI appeared on 1 July 1948 signalling the commencement of the industrial development era in India.

IFCI: The Journey over the 70 Years



At the hour of independence in 1947, the Indian Capital Markets were comparatively less evolved. Even as the demand for capital was rising, there was a lack of suppliers of capital. Given their financial prowess, the commercial banks that existed at that time, were not prepared to accommodate long-term capital necessities in any critical way. Against this background and to connect the credit supply gap for capital requirements of the economy, the Government of India set-up The Industrial Finance Corporation of India (IFCI) on 1 July 1948 via an IFCI Act, 1948.

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IFCI was the principal development financial institution of India set-up to give a thrust to the economic growth through progress in infrastructural and industrial sector. From that point forward, IFCI has contributed essentially to the economy through its relentless help to projects in all the three circles of progress and growth-manufacturing, infrastructure & services and also farming and its related areas. The liberalization of the Indian economy in 1991 rolled out huge improvements in the Indian capital markets and financial system. To help raising of funds straight-forwardly through capital market, the constitution of IFCI was transformed from a legal enterprise to an organization under the Indian Companies Act, 1956. Accordingly, the name of the organization was changed to 'IFCI Limited' with effect from October 1999.

Since its beginning 70 years back, IFCI has seen and supported all business monetary cycles. IFCI has had the option to keep up the monetary supportability with the steady help and collaboration of every one of its partners and especially the Government of India. Notwithstanding its primary skill in long-term loaning to industrial and infrastructural sectors, IFCI is likewise improving its organizational relevance through upgrading value of core and non-core assets and investments. Over the years, IFCI assumed an essential part in the establishing various developmental organizations (that included its subsidiaries and associates) - that are well-regarded in their fields today, specifically Stock Holding Corporation of India Ltd (SHCIL), National Stock Exchange Ltd (NSE), LIC Housing Finance Ltd, Tourism Finance Corporation of India Ltd (TFCI), Management Development Institute (MDI), ICRA Ltd, among numerous others. Taking a cue from the learning's and experiences over some period, alteration in the provisions of the IFCI Act, 1948 was affected. A couple of the subsidiaries were stripped and right now IFCI Group has the company of Stock Holding Corporation of India Ltd, IFCI Venture Capital Fund Ltd, IFCI Factors Ltd, IFCI Infrastructure Development Ltd, IFCI Financial Services Ltd, MPCON, Management Development Institute and Institute of Leadership Development.

Taking a cue from the experiences and learning's from the functioning of IFCI and its impact on the economy, amendments were proposed and eventually affected on the IFCI Act, 1948. The three wide patterns of such amendments have been (a) to build the assets (b) to expand the extent of activities and (c) to improve the management. To guarantee more prominent adaptability to react to the changing requirements of the financial framework, IFCI was restructured as an organization under the Companies Act 1956, in 1993. IFCI was the first financial institution whose legal entity got converted from a statutory institution to a public limited company. As a principal promoter and financer in the industrial sector, IFCI had finished 52 years of operations altogether and twenty-seven years as a Company by 2020.

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2.4 FINANCIAL ASSISTANCES OFFERED BY IFCI

Various financial assistances offered by IFCI can be segregated under three categories, namely, financial products, debenture trustee and sale and NPA management.

1. Financial Products

- Loan Products

  IFCI Ltd., set up as the Industrial Finance Corporation of India (IFCI) on 1 July 1948, was the principal development financial institution in the country, established to meet the requirement of the long-term finances of the industrial segment. Since its foundation, IFCI has been an impetus in forming a vigorous industrial base for the country through modernization of Indian industry, trade advancement, import substitution, supporting start-ups and sunrishing industries and so forth through economically feasible and market-accommodating activities.

  To keep serving the requirements of the Industry and society, IFCI offers the few products that can be categorized under three aspects - Project Finance, Corporate Finance and Structured Finance spreading across businesses, services and Agriculture based areas.

- Undertaking Finance

  IFCI's group of experts with top to bottom understanding of the sectoral elements boasts of their capability to provide financial solutions that would meet the developing and enhanced necessity for various degrees of the activities like Greenfield projects, expansion and modernization of existing undertakings in infra and manufacturing sector.

  The different areas covered under Project Finance are power renewable energy, telecommunications, roads, oil and gas, ports, airports, basic metals, chemicals, pharmaceuticals, electronics, textiles, real estate, smart cities and urban infrastructure and so on.

- Corporate Finance

  IFCI takes into account the differed needs of assorted clients going across small, mid and large cap companies. IFCI offers monetary arrangements in regions of corporate finance through Balance Sheet Funding, Loan Against Shares, Lease Rental, Refinancing and Rediscounting, Promoter Funding, Long Term Working Capital necessities, Capital Expenditure and normal Maintenance Capex.

  IFCI additionally offers a Short-Term Loan item (usually upto 1 year) to meet different business necessities including bridge financing and recurring working capital requirements.

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- Loan Syndication and Advisory Services

  IFCI has displayed a drive to offer personalized corporate advisory services and facilitates financial restructuring of different corporate houses and organizations. It integrates the data sources collected through numerous instants of project appraisal undertaken over the years, documentation, partnership, and product design in giving an altered exhaustive start to finish monetary solution for corporates.

  In the zone of offering customary financial assistance and services, IFCI succeeded in roping in new tasks related investment evaluation, business reengineering and advisory activities.

- Structured Products

  IFCI likewise gives financing solutions for its customers through Structured Debt items and helps with giving ideal financing resolutions for different necessities, for example, support financing, procurement financing, pre-IPO financing and Off-Balance Sheet Structured Solutions among others.

2. Debenture Trustee

IFCI acts as a trustee to debentures and publishes various reports and also provide operations related information of its clients.

3. NPA Management

- NPA Resolution

  IFCI utilizes dedicated, multiple techniques for due recovery from non-performing assets. The procedures utilized by IFCI that are in agreement with the provisions of SARFAESI Act, are specified as under:

  o Taking legal action D recovery measures under legal arrangements including documenting of Original Application before the DRT and filing of petition for the closure of an organization under the watchful eye of the High Court.

  o Settlement of the due payable by borrower(s) D co-obligant.

  The above methodologies are utilized related to expand IFCI's ability to guarantee full recovery of public cash.

- NPA Sales

  A new strategy embraced by IFCI to strengthen its NPA portfolio is leading to the offer of selling NPAs on both SR and cash basis. With respect to the provisions issued by RBI, IFCI has agreed to sale the NPAs to Securitization Companies/Banks/Financial Institutions to decrease the concentration of NPAs and thus focus on to persistent NPAs.

Check Your Progress

3. Mention one significant function of IFCI.
4. What is the role of IFCI with reference to debenture trustee?

2.5 FUNCTIONS AND OBJECTIVES OF THE INDUSTRIAL FINANCE CORPORATION

The IFCI is liable for underwriting the shares, bonds, debentures of industrial houses on the condition that they are allowed to be sold off inside 7 years from the date of procurement. Long-term loans and advances are granted to industrial enterprises and furthermore guarantee is provided to these endeavours for the advance raised from the Scheduled or States Co-employable Banks. It can likewise straight-forward buy stocks or shares of any industrial company.

The fundamental target of IFCI is to give medium and long-term monetary help to large industrial enterprises, especially when common bank accommodation sometimes falls short for the enterprise or when it is difficult to raise funds profitably through the issue of shares.

2.5.1 Functions

The functioned performed by IFCI are the following:

i. To provide guarantee on agreed terms and conditions, to credits raised by industrial concerns repayable inside 25 years and are offered in the publicmarket.

ii. To guarantee, on approved terms, advances raised by industrial enterprises from Scheduled Banks or State Co-employable Banks.

iii. With the prior endorsement of the Central Government, to guarantee on approved terms, deferred payment due from any industrial company with respect to acquisition of capital goods inside or outside India.

iv. With the prior approval of the GoI, to guarantee on approved terms, advances raised from, or credit arrangements madewith, any banks or monetary organization in any country outside India by industrial enterprises, in foreign currency.

v. To endorse the issue of stock, shares, bonds or debentures by industrial companies.

vi. To go about as a specialist for the Central Government and IBRD for their exchanges with an industrial house with respect to allowance of loans or advances or subscription to debentures.

vii. To buy in to the stock or shares of any industrial enterprise.

viii. To receive commission on agreed terms with regards to the aboveservices.

ix. To allow credits or advances to buy debentures of industrial houses repayable inside 25 years.

In this way, the whole exercises of IFCI can be assembled under the main heads (a) guaranteeing (b) underwriting and (c) providing loans and advances. The financial space provided by IFCI under the points 1,2,3,4 and 9 above (i.e., guaranteeing and financing) must be made sure about by pledge, mortgage, hypothecation or assignment of securities, bullion, property or tangible assets or by a guarantee for the repayment of principal and the payment of interest either from the Central Government, State Government or a State Co-operative Bank. However, IFCI has been restricted to provide any loan on the security of its own shares. Furthermore, any organization that is either unable to offer satisfactory security or fails to get its monetary requirements guaranteed by any of the specified offices will not be helped by IFCI.

2.5.2 IFCI Subsidiaries and Associates

1. IFCI Factors Limited

IFCI Factors Limited, consolidated in February 1996 as Foremost Factors Ltd., was promoted by Mohan Group and Nations Bank Overseas Corporation of USA alongside Twentieth Century Finance Corporation Limited (TCFC Limited) and ICDS Group as institutional investors.

The Company commenced its operations in February, 1997 with domestic factoring exercises. The Authorized Dealer's permit was acquired for factoring exercise with respect to exports in November 1996. Export Factoring tasks were started from June, 1997. In April, 1999, IFCI subscribed the share capital of the Company other than securing the shareholding of Twentieth Century Group that propelled it into the largest investor. Moreover, IFCI additionally obtained the shareholding of Mohan Group and in 2009. Foremost Factors was renamed as IFCI Factors Limited and today it is a subsidiary of IFCI.

2. IFCI Factors Limited

IFCI Factors Limited is enrolled as a NBFC-Factor with the RBI and is occupied with the matter of factoring, offering products like Domestic Sales Bill Factoring, Purchase Bill Factoring, Export Bill Factoring, and Advances against Future Receivables. The Company additionally offers Corporate Loans for a period varying from one to four years that are secured about by tangible collateral as well as pledge of shares.

Being the pioneers in introducing International Factoring to India, IFCI Factors possesses rich experience which empowers it to comprehend the necessities of its customers with regards to their market and serve them in the most ideal manner. It gives creative, personalized solutions which are driven by a forward looking administration style, sound comprehension of the key credit issues and an exhaustive understanding of market rehearses.

A lean organizational structure, upheld by a universally recognized state of the art software platform, guarantees operational proficiency and converts into delivery of top notch services to the customers. IFCI Factors highly esteems reacting rapidly to the requests of its clients, which thus, engages them to benefit from the attractive prospects offered by a consistently dynamic market.

3. IFCI Financial Services Ltd (I-FIN)

IFCI promoted IFCI Financial Services Ltd (I-FIN) in 1995, to give a wide scope of financial products and services to investors, both institutional and retail. I-FIN is essentially associated with Stock Broking, Investment Banking, Mutual Fund Distribution and Advisory Services, Depository Participant Services, Insurance Products Distribution and such.

4. IFCI Infrastructure Development Limited (IIDL)

IFCI Infrastructure Development Limited (IIDL) was set-up by IFCI Limited (IFCI) as its wholly owned subsidiary in the year 2007 to engage into the real estate and infrastructure sector as an institutional player.

5. IFCI Venture

IFCI Venture was set-up in 1975 with an objective to expand entrepreneurship base in India by providing risk capital primarily to first generation entrepreneurs under 'Risk Capital Scheme'. In 1988, IFCI Venture launched 'Technology Finance & Development Scheme", to provide financial support for setting up projects intended to commercialize indigenous technologies.

6. MPCON

IFCI, since its origin has been assuming a vital part in fast-tracking the pace of industrial development in the country as well as being instrumental in establishing financial atmosphere helpful for accomplishing fast industrial growth within the country.

Keeping an eye on the formative necessities of the nation, IFCI, in the year 1979, took a step and promoted MPCON a Technical Consultancy Organization alongside other apex Financial Institutions, for example, IDBI, ICICI, PSU Banks and different state Government Corporations to cater the requirements of the industry and business people.

In December, 2009, IFCI became biggest investor of the entity at 80 per cent through which it brought MPCON under its umbrella for offering important help and consultancy to industry and business people on the loose.

MPCON is having its office in the States of Madhya Pradesh, Rajasthan, Chhattisgarh and is serving the following client base:

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i. Small and Medium Enterprises,
ii. Individual Entrepreneurs,
iii. Government Departments and Agencies,
iv. Various State/National Level Institutions,
v. Commercial Banks and
vi. Other Various Institutions.

The following sectors are covered by MPCON to serve the above client base elsewhere in India also and not just in Madhya Pradesh, Chhattisgarh and Rajasthan:

i. Quality Management Consultancy
ii. Consultancy for Urban Local Bodies
iii. Compilation of Project Reports and Studies
iv. Training and Capacity Building Programmes
v. Science and Technology Entrepreneurship Development (STED) Project
vi. Internship Programme in Entrepreneurship
vii. Training Programmes and Workshops on Medicinal Plants
viii. Job Oriented Training under Aajeevika Programme

7. Stock Holding Corporation of India Ltd. (SHCIL)

Stock Holding, a subsidiary of IFCI Limited, was sponsored by various public financial institutions and took shape of a public limited company on 28 July 1986. SHCIL provides post trading and safeguarding services to institutional investors, mutual funds, banks, insurance companies, etc.

8. KITCO (It was formerly known as Kerala Industrial and Technical Consultancy Organization Ltd.) was established in 1972. It is one of the foremost Engineering, Management & Project consultancy firms set-up in India. KITCO has provided considerable contribution in the fields of Energy Studies, Skill Certification and Placement services.

KITCO is the lone consultancy association in the state having EIA accreditation. As a component of business development another branch office was set-up in New Delhi for laisoning with different Ministries/Central Government divisions for taking up tasks all over India. During the year under report, KITCO has been instrumental in setting up of TCO consortium having its office in Delhi. While KITCO will be the National Coordinating office for the consortium, the other TCO individuals are: NITCON (Punjab), MITCON (Maharashtra), ITCOT (Tamil Nadu), APITCO (Andhra Pradesh), GITCO (Gujarat), HARDICON (Haryana), MPCON (Madhya Pradesh), UPICO (Uttar Pradesh), HIMCON (Himachal Pradesh) and RAJCON (Rajasthan).

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2.5.3 Social Sector Initiatives: Societies

1. Institute of Leadership Development (ILD)

The Leadership Development (ILD), formerly known as Institute of Labour Development, was set-up in 1992, identifying the fact that, alongside the administration, the specialists must be furnished with promising circumstances and external amenities of training and advancement evolving challenges.

The name was rechristened as the Institute of Leadership Development in the year 2008. ILD is running after its central goal to build capacities, sharpen up and inject leadership skills among all the in a wide workforce associated with the entire range of associations i.e., business and corporate houses, Banks, SMEs, NGOs, social action groups, key formative areas like training, healthcare, energy and climate and also across the public sector units. ILD is additionally occupied with teaching skill development programmes for the jobless young people of the province of Rajasthan and giving them placements and also access to CSR fund assistance from various associations. ILD is likewise an empanelled organization with Rajasthan Skill and Livelihoods Development Corporation (RSLDC), Jaipur, to do skill improvement programmes in the zones of Textile innovation, Fashion innovation, Hospitality and so forth

2. Management Development Institute (MDI), Gurgaon

As a feature of its development obligation, IFCI has encouraged advancement of India's premier Business Schools, namely, the Management Development Institute (MDI) at Gurgaon, Haryana. The Institute intends to instill polished skill in management education and upgrade the effectiveness of organizations through instruction, training and research.

MDI holds the distinction of being the first globally accredited Indian Business School having received global accreditation by AMBA in 2006. The long-time projects of MDI have gotten global, provincial and national accreditations from Accreditation of Association of MBAs (AMBA) London, South Asian Regional Accreditation (SAQS) and National Board of Accreditation (NBA). MDI additionally has the differentiation of being the solitary Indian B-school that has a local area outreach programme, the International Summer University (ISU) wherein MDI has joined hands with nine Indian colleges and organizations to create a learning network.

MDI is an autonomous and professionally managed institution enrolled under the Societies' Registration Act, 1860.

3. Rashtriya Gramin Vikas Nidhi (RGVN)

RGVN having its settlement in Guwahati, Assam was set-up in April 1990, as an independent, non-profit association enlisted under the Society's Registration Act of 1860 to advance, support and create willful associations engaged in the social and economic upliftment of the rural and urban poor, physically and socio-economically disabled individuals, improve the speed and nature of monetary turn of events, specially focussed related to the rural and unorganized sector, give extra attention to groups which are disadvantageously positioned in the public arena. However, they have the potential of performing socially and financially profitable exercises, help the metropolitan and rural poor particularly tribal, scheduled caste, women and children for their economic self- sustenance.

RGVN was initially established with the sole contribution of IFCI. However, with the passage of time, Industrial Development Bank of India (IDBI), the National Bank for Agriculture and Rural Development (NABARD) and the Tata Social Welfare Trust (TSWT) also became promoters of RGVN. RGVN has provided development and support services to the north-eastern states of India such as Assam, Arunachal Pradesh, Meghalaya, Mizoram, Nagaland, Manipur, Tripura, Sikkim. Further, RGVN increased its activities in poverty-stricken areas of Eastern Uttar Pradesh, coastal Andhra Pradesh and Chhattisgarh. NGOs and Self Help Groups (SHGs) are the two major wings which support RGVN in its development activities.

2.5.4 Scope of IFCI

IFCI has restricted the operational zone to large-scale industrial enterprises, and small-scale industrial concerns have been excluded. For the determination of eligibility— to get help an 'Industrial Concern' has been characterized by the Industrial Finance Corporation in the following way:

'Industrial concern implies any public limited company or co-operative incorporated by the Central Act or an Act of the Legislature of a State or under any law for the time being in force and registered in India which is engaged or is to be engaged in the manufacture, preservation or processing of goods or in shipping or in mining or in hotel industry or in the generation or distribution ofelectricity or any other form of power'. The expression 'Industrial Concern' has been revised multiple times to expand the territory of activity of IFCI. Numerous enterprises, which were not qualified initially for IFCI assistance according to the definition of the expression 'Modern Concern', are now covered. The Corporation would now be able to help any restricted company, joint or private sector or co-operative society incorporated and registered in India. The scope of IFCI goes through steady changes with the evolving financial, industrial, social, cultural and technological environment.

The Industrial Financial Corporation of India is approved to provide credits to industrial organizations repayable with quarter century grants, foreign currency loans to specific enterprises, underwrite bonds, shares and debentures and so forth provided they may be disposed off by the IFCI inside seven years, guarantee deferred payments by importers of capital goods by foreign manufacturers, accept deposits from the local institutions,guarantee advances from any bank of an outside nation, buy shares of industrial organizations.

The enterprise's job presently stretches across the industrial spectrum in the country. The amenities and services being given by IFCI can be considered to fall comprehensively under (a) project financing, (b) financial services and (c) promotional services.

The Industrial Finance Corporation has contributed substantially in our industrial development and also played a significant role. Since its establishment, the Corporation has given monetary help to the underdeveloped industrial concerns. The Corporation has the ability to analyse the financial aspects of the industrial houses and offer important guidance to the management for improving their plans.

IFCI has been involved in the launching of several promotional schemes like:

- Subsidy in interest for women entrepreneurs.
- Schemes for modernization of small scale units,
- Consultancy fee subsidy for giving marketing assistance,
- Pollution control plans and so on

It is also expanding its wings in the field of merchant banking to deliver other related financial services like project counselling, loan sanction etc. IFCI has also shown concern for the development of the backward areas of the country.

Criticism

IFCI and its activities are not free from criticisms. Few of the adverse observations are noted below:

- The Corporation has confined itself to providing financial assistance to only large industrial organizations and has disregarded small and medium enterprises.
- The Industrial Finance Corporation is not approved to sanction more than two crores of rupees to industrial houses.
- The Corporation may give loans and advances only if the Central Government is prepared to reimburse the principal with interest.
- The IFCI lacks regulatory proficiency. The individuals are not appropriately prepared and familiar with the issues revolving around industrial financing.
- The Corporation has an inclination towards the large industrial organizations.
- It has the disrepute of being deliberately delaying the loan process and is also charged with nepotism and bias.

Conclusion

Hence, steps have been suggested that should be implemented to improve the administrative functioning and mechanism of the Corporation and furthermore increase its financial base. The Industrial Finance Corporation needs to see that all States in India get monetary assistance from it on a sound financial basis.

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Check Your Progress

5. In which year was IFCI Venture established? What was its objective?
6. Mention the criticisms raised against the IFCI.

2.6 ANSWERS TO CHECK YOUR PROGRESS QUESTIONS

1. The Industrial Finance Corporation of India was established in 1948.
2. The vision of IFCI is to be the leading development institution for industrial and infrastructure sectors across the spectrum and be an influential partner in country's economic growth and development.
3. Over the years, IFCI assumed an essential part in the establishing various developmental organizations (that included its subsidiaries and associates) - that are well regarded in their fields today, specifically Stock Holding Corporation of India Ltd (SHCIL), National Stock Exchange Ltd (NSE), LIC Housing Finance Ltd, Tourism Finance Corporation of India Ltd (TFCI), Management Development Institute (MDI), ICRA Ltd, among numerous others.
4. IFCI acts as a trustee to debentures and publishes various reports and also provides operations related information of its clients.
5. IFCI Venture was set-up in 1975 with an objective to expand entrepreneurship base in India by providing risk capital primarily to first generation entrepreneurs under 'Risk Capital Scheme'.
6. It is to be noted that several criticisms have been raised against IFCI. The prominent criticisms are the following:
   - The Corporation has confined itself to provide financial assistance to only large industrial organizations and has disregarded small and medium concerns.
   - The Industrial Finance Corporation isn't approved to sanction more than two crores of rupees to industrial houses.
   - The Corporation may give loans and advances only if the Central Government is prepared to reimburse the principal with interest.
   - The IFCI lacks regulatory proficiency. The individuals are not appropriately prepared and familiar with the issues revolving around industrial financing.
   - The Corporation has an inclination toward the large industrial organizations.

- It has the disrepute of being deliberately delaying the loan process and is also charged with nepotism and bias.

2.7 SUMMARY

- Industrial Finance Corporation of India is a Non-Banking Finance Company in the public sector. Set-up in 1948 as a statutory company, IFCI is right now an organization listed on BSE and NSE. There are six subsidiary companies and one associate company that are presently managed by the IFCI.
- The organization has assumed a significant part in setting up different reputed market intermediaries in a few specialized segments like stock markets, entrepreneurship development institutions, consultancy associations, skill development and instructional institutions within the country.
- Further, in March 2015, the Ministry of Social Justice and Empowerment, Government of India assigned IFCI as the nodal office for the implementation of the 'Credit Enhancement Guarantee Scheme for Scheduled Castes' and to make concessional funding to them.
- The essential business of IFCI is to give medium to long-term monetary assistance to the manufacturing, services and infrastructure sectors.
- The strategy of fast-tracking the pace of economic growth by equipping the enterprises with medium and long-term capital through state-supported specific financial institutions or development banks is not something new in India.
- The Indian economy was exposed by the absence of financial intermediaries, promoters and underwriters. This obstructed the mobilization of savings leading to industrial development. Before 1906, domestic financiers were the primary financial source.
- C.D. Deshmukh, the Reserve Bank of India's first Indian Governor, worked out the plan and made a proposal for the establishment of an industry dedicated financial institution in the form of Industrial Finance Corporation and model it on the lines of the Finance Corporation in the United Kingdom.
- IFCI was the principal development financial institution of India set-up to give a thrust to the economic growth through progress in infrastructural and industrial sector.
- Since its beginning 70 years back, IFCI has seen and supported all business monetary cycles. IFCI has had the option to keep up the monetary supportability with the steady help and collaboration of every one of its partners and especially the Government of India.

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- Taking a cue from the experiences and learning's from the functioning of IFCI and its impact on the economy, amendments were proposed and eventually affected on the IFCI Act, 1948.
- Various financial assistances offered by IFCI can be segregated under three categories, namely, financial products, debenture trustee and sale and NPA management.
- IFCI takes into account the differed needs of assorted clients going across small, mid and large cap companies.
- The IFCI is liable for underwriting the shares, bonds, debentures of industrial houses on the condition that they are allowed to be sold off inside 7 years from the date of procurement.
- IFCI Factors Limited is enrolled as a NBFC-Factor with the RBI and is occupied with the matter of factoring, offering products like Domestic Sales Bill Factoring, Purchase Bill Factoring, Export Bill Factoring, and Advances against Future Receivables.
- IFCI Infrastructure Development Limited (IIDL) was set-up by IFCI Limited (IFCI) as its wholly owned subsidiary in the year 2007 to engage into the real estate and infrastructure sector as an institutional player.
- KITCO is the lone consultancy association in the state having EIA accreditation. As a component of business development another branch office was set-up in New Delhi for laisoning with different Ministries/Central Government divisions for taking up tasks all over India.
- It is also expanding its wings in the field of merchant banking to deliver other related financial services like project counselling, loan sanction etc. IFCI has also shown concern for the development of the backward areas of the country.
- The Corporation has an inclination towards the large industrial organizations.

2.8 KEY WORDS

- **Greenfield Project:** It means a project that represents a completely new industrial project which does not utilize any manufacturing assets other than wholly new and unused manufacturing assets.
- **Sunrise Industry:** It is a new industry that is expanding rapidly and is expected to be increasingly important in the future. The term was coined in 1983 to describe the then new, successful manufacturing industries, upon which the economic sun was supposedly rising.
- **Factoring:** It is a financial transaction and a type of debtor finance in which a business sells its accounts receivable (i.e., invoices) to a third party (called a factor) at a discount.

- **Nepotism:** It is a form of favouritism which is granted to relatives in various fields, including business, politics, entertainment, sports, religion and other activities.

2.9 SELF ASSESSMENT QUESTIONS AND EXERCISES

Short-Answer Questions

1. What are the main values of IFCI?
2. Briefly mention the types of financial assistance offered by IFCI.
3. Write a short note on the scope of IFCI.

Long-Answer Questions

1. Discuss the history of IFCI.
2. Critically analyze the journey of IFCI over a period of 70 years.
3. Explain the functions and objectives of IFCI.

2.10 FURTHER READINGS

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UNIT 3 INDUSTRIAL DEVELOPMENT BANK OF INDIA (IDBI)

Structure

3.0 Introduction
3.1 Objectives
3.2 Development and Growth of IDBI Bank Ltd
  3.2.1 Reasons for Establishing IDBI
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  3.2.3 Functions Performed by IDBI
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3.0 INTRODUCTION

IDBI was set-up in 1964 by the Indian Parliament as a completely owned subsidiary of the Reserve Bank of India. IDBIs ownership got transferred to the Government of India in 1976. The IDBI bank established SIDBI as a completely owned subsidiary to satisfy the requirements of small-scale sector. Moreover, IDBI has contributed in the development of capital market through the establishment of SEBI, NSE, NSDL, SHCIL, Clearing Corporation of India Ltd. (CCIL). In this unit, you will study about the need for the establishment of IDBI, its formation, functions, various assistance schemes in the offing, the services offered and the role it has played towards the development of industrial sector since its inception.

3.1 OBJECTIVES

After going through this unit, you will be able to:

- Discuss the establishment and functioning of IDBI

- Explain the various assistance schemes offered by IDBI
- identify the challenges being faced by IDBI

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3.2 DEVELOPMENT AND GROWTH OF IDBI BANK LTD

Industrial Development Bank of India (IDBI) was established under Industrial Development Bank of India Act, 1964 as a Development Financial Institution (DFI) and came into existence on 1 July 1964 vide GoI notice dated 22 June 1964. It was viewed as a Public Financial Institution as far as the arrangements of Section 4A of the Companies Act, 1956. It served as a DFI for 40 years till 2004 when it got converted into a bank.

Industrial Development Bank of India Limited

Felt need and commercial far-sightedness necessitated the transformation of IDBI into a bank and hence, Industrial Development Bank (Transfer of Undertaking and Repeal) Act, 2003 [Repeal Act] was passed revoking the Industrial Development Bank of India Act, 1964. In commensurate to the Repeal Act, another organization under the name of Industrial Development Bank of India Limited (IDBI Ltd.) was incorporated as Banking Company under the Companies Act, 1956 on 27 September 2004. From that point, the endeavour of IDBI was moved to and vested in IDBI Ltd. with impact from 1 October 2004.

Merger of United Western Bank with IDBI Ltd

The United Western Bank Ltd. (UWB), a private bank based in Satara, was set under suspension by RBI. IDBI Ltd. displayed interest to take over the ailing bank and work towards reviving it and subsequently UWB was amalgamated with IDBI Ltd. in accordance with the provisions of Section 45 of the Banking Regulation Act, 1949. The consolidation became effective from 3rd October 2006.

Change of name of IDBI Ltd. to IDBI Bank Ltd.

To genuinely cover all the functional aspects, the name of the bank was changed to IDBI Bank Ltd. with impact from 7 May 2008 and a fresh Certificate of Incorporation by Registrar of Companies, Maharashtra was issued.

Merger of IDBI Home Finance Ltd. and IDBI Gilts with IDBI Bank Ltd.

Two wholly owned subsidiaries of IDBI Bank Ltd., namely IDBI Home Finance Ltd. and IDBI Gilts Ltd. were merged with IDBI Bank Ltd. under Section 391-

394 of the Companies Act, 1956 vide Government of India, Ministry of Corporate Affairs request dated 8 April 2011. With respect to Section 394(3) of the Companies Act 1956, the Government of India's above order has been recorded with the Registrar of Companies on 26 April 2011.

Re-categorization of IDBI Bank Ltd. as a Private Sector Bank

LIC of India finished securing of 51 per cent controlling stake in IDBI Bank on 21 January 2019 making it the dominant investor of the bank. On the basis of LIC of India's action, on 21 January2019, the Reserve Bank of India issued a Press Release dated 14 March 2019, that IDBI Bank stands re-arranged as a Private Sector Bank, with review impact from 21 January 2019.

3.2.1 Reasons for Establishing IDBI

The Industrial Development Bank of India was established under the Industrial Development Bank of India Act, 1964 as wholly owned subsidiary of RBI. The ownership of IDBI has since then been transferred to the Central Government from 16th February 1976. The primary objective of establishing IDBI was to set-up an apex institution to coordinate the activities of other financial institutions and to act as a financial pool on which other financial institutions can rely. It provides direct financial support to industrial units in order to wipe out the gap between supply and demand of medium and long-term finance.

Change in Political India

The change of political approach initiated by the then Prime Minister Lal Bahadur Shastri who replaced Pandit Jawaharlal Nehru on his demise after a prolonged illness on 27 May 1964 resulted in liberal India thinking about financial development. Lal Bahadur Shastri was notable for his two-front approach of upgrading agriculture and enabling the armed forces. Till 1964 Indian economy was profoundly reliant on agribusiness. However, he realized that if India does not take strides in industrial development, it would not be possible to acquire global advantage.

The Constitution (Seventeenth Amendment) Act, 1964

Article 31A of the Constitution contains a law with regard to the procurement by the State of any estate or of any rights the therein or the adjustment of any such rights will not be considered to be void on the ground that it is conflicting with, or removes or condenses any of the rights gave by Article 14, Article 19 or Article 31.

The shield of this article is applicable to only such freeholds that were in existence on 26th January, 1950, when the Constitution came into power. The

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articulation 'estate' has been characterized contrastingly in various States and because of the exchange of land starting with one State then onto the next by virtue of the redesign of States, the articulation has come to be characterized diversely in different areas within the same State. Moreover, many such reforms associated with land were excluded from 'estate'. Even though the scenario was not directly connected with industrial development, it was expected that the said change would assist the government in expanding the industrial sector thereby resulting in sustained industrial growth.

1962 War with China

The war with China in 1962 literally rattled India on the financial front. The results were shocking for India. It made the Indian political establishment realize that liberal strategies and a solid political will was required to revive the economy. The war placed India in monetary unrest. The situation called for a structured framework that could give thrust to the economy and industry in particular. This aided in the foundation of a bank that upholds industries. All these conditions lead to the build-up of a banking institution that solely focus on industrial development and promote industrial enterprises in India.

3.2.2 Objectives of IDBI

i. The main goal of the Industrial Development Bank of India is to give advances both to the private as well as public sector industrial houses in the field of product creation, mining and service sector like travel and tourism industry and transportation.
ii. This bank gives advances to the industrial ventures directly.
iii. It likewise straight-forward puts resources into modern offers and guarantees protection.
iv. To actively involve in investment in industrial shares and act as underwriters of securities.
v. Offering discount in the trading bills.
vi. To facilitate refinancing. This led to merger of Refinance Corporation with IDBI in 1964.
vii. The bank has set-up the Development Assistance Fund. This was done to support those enterprises which failed to raise loan elsewhere. This asset is the central element of this bank. However, as a precautionary measure, prior to offering any help out of this fund, the bank needs authorization from the government.

viii. To organise investment assessments.

ix. Providing professional and technical support to the industrial enterprises.

x. The bank has a substantial pool of funds to finance. It can additionally get from the Central Government up to ₹ 10 crores interest free loan. It can likewise ask for credit from the Reserve Bank of India. Further, credit might be raised by this bank via issuing offers and debentures.

3.2.3 Functions Performed by IDBI

The IDBI has been set-up to perform the following functions:

- To offer assistance and advances to IFCI, SFCs or some other monetary establishment via refinancing of advances allowed by such enterprises which are repayable within a period of 25 years.
- To offer loans and advances to scheduled banks or state co-operative banks through refinancing of advances granted by such establishments which are repayable in 15 years.
- To award advances a lot to IFCI, SFCs, other establishments, scheduled banks, state co-operative banks by refinancing loans provided by such institutions to industrial houses to promote exports.
- To discount or rediscount bills of industrial establishments.
- To subscribe and/or underwrite shares or debentures of industrial companies.
- To buy stock, shares, bonds and debentures of other monetary organizations.
- To award credit extension or advances constantly to financial institutions like IFCI, SFCs, and so on.
- Provide loans to all industrial organizations.
- To ensure deferred payment due from any industrial concern.
- To guarantee advances taken by industrial enterprises from the market or from any other financial institution.
- To give consultancy and merchant banking services in India or overseas.
- To give specialized, legitimate, advertising and administrative help to any industrial house or individual for expansion, promotion and managing of any industry.
- Planning, elevating and creating businesses to bridge the gaps in country's industrial set- up.
- Performing the functions of trusteeship for the holders of debentures or any other security.

The significant members of the Indian monetary framework are the commercial banks, the Financial Institutions (FIs), including term-loaning institutions, investment companies, SFCs and the state-level development banks, Non-Banking Financial Companies (NBFCs) and other financial intermediaries like the stock brokers and moneylenders. The industrial banks and few variants of NBFCs are among the most seasoned of the market players. The FIs, as compared to others, are moderately new players in the financial market.

The Indian banking and financial framework is confronting new challenges in the new millennium. The Indian financial structure has a few extraordinary accomplishments based on its various capacities. In reality, Indian banking is not, at this point limited to metropolitan urban communities and huge towns. Rather, they are currently spread out in the distant zones of our country. This task encourages us to think about the working of banks for example various sorts of accounts in banks, banking structure, kinds of banks, banking reforms and so forth; and furthermore, it has incorporated numerous changes in financial framework, for example, web banking, plastic money, and so on.

Banks are among the primary members of the monetary framework in India. Banks offer several services and opportunities. This segment gives extensive and updated data, supervision and helps in all regions of banking in the country.

3.2.4 IDBI Schemes of Assistance

The IDBI gives monetary help either straight-forward or through various specialized financial establishments:

(I) *Direct Assistance*

The IDBI offers credits and advances to industrial entities. There is no limitation on the upper or lower limits to be offered to any entity. The bank ensures advances raised by industrial companies in the open market from the State Co-operative Banks, the Scheduled Banks, the Industrial Finance Corporation of India (IFCI) and other 'notified' monetary establishments.

(II) *Indirect Assistance*

The IDBI can renegotiate or refinance term loans to industrial houses repayable inside 3 to 25 years given by the IFCI, the State Financial Corporation (SFCs) and some other financial institutions. It also refinances SIDCs (State Industrial Development Corporations), Commercial banks and Co-operative banks which provide term loans not surpassing 10 years to industrial organizations. IDBI is involved in subscribing the shares and bonds of financial institutions and consequently give additional assets.

(i) Project Finance Scheme:

Under the Project Finance scheme, the IDBI bank provides financial assistance to the corporates for their projects. Project financing for Greenfield projects is done in both Indian and foreign currencies and are directed towards extension, enhancement and modernization. The IDBI bank follows the best global practices in project appraisal, monitoring and evaluation. It also boasts of having a well-spread out industry portfolio. The IDBI bank signed a Memorandum of Understanding (MoU) with LIC in December 2006 for undertaking joint financing of projects having long gestation period that includes infrastructural projects.

(ii) Infrastructure Finance Scheme:

The IDBI bank has been effectively taking an interest in organizing and financing of infrastructural projects related to power, telecom, roads, seaports, railways and supply chain as well as Special Economic Zones. The bank has additionally taken activities in subsidizing modernization of air terminals, other than part-financing improvement of global air terminals and seaports under the Public-Private Partnership route. The IDBI is also a member of the Core Committee of the government set-up for selection and finalisation of the Ultra Mega Power Projects. The IDBI bank associates with government and different partners and market members, on policy and operating aspects, enabling smooth progression of funds to projects related to infrastructure.

(iii) Working Capital finance Scheme:

Working capital assistance is given to the business to fund everyday operations and sales. With reference to production, funds are required to procure raw materials, stores, fuel, labour payment, power charges, for warehousing of finished product till they are sold out and for affect sales through debtors/receivables. Cash credit facility is allowed to the clients to overcome the working capital gap Short-term loan up to 1 year is also provided by IDBI to meet out financial requirement that arises out of reasons like default in timely receivables payment, routine capital expenditure (capex) and so forth.

(iv) Cash Management Services (CMS) Scheme:

The IDBI bank is an innovation and service driven financial institution managed with financial trustworthiness. The IDBI Bank Cash Management Services (CMS) has accomplished the ISO 9000 confirmation for its product base and technological upbringing. Cash Management Service offers three items – Collections, Payments and Cashweb- an online product offered.

The key item highlights of the IDBI bank are the following:

i. Confirmed measures
ii. Subcontracted logistics
iii. Improved clearing set-up
iv. Pooling/Single Payout Account
v. Personalized Reporting
vi. Detailed data collection

The innovation advantages provide better services, advantageous access channels and effective support to customers. Cash management is the practice of advancing receivables and payables while providing guaranteed consistency in the cash flows. Proficient Cash Management is associated with getting accessibility to funds on time, quick exchanges, proper and timely realization of local and outstation cheques, easy disbursements, reconciliation of accounts, controlled cycles and custom-made MIS. Hence, Cash Management Services (CMS) disposes off the innate deferrals of funds transfer machinery, accordingly upgrading liquidity and confirming optimal planning and use of funds.

IDBI's Bank Cash Management Services (CMS) incorporate the accompanying fundamental segments:

i. Receivables / Collection Management
ii. Payables / Payment Management

Advantages of Cash Management Services

i. *Monetary Benefits*

a. Interest cost is reduced through the collection and disbursement products as they enable to get access to the funds quickly thereby decreasing the borrowing cost. Moreover, it assists in improving the liquidity position by early realization of cheques, which also helps in improving the financial ratios and the Balance Sheet position.

ii. *Operational Benefits*

a. Banking and treasury issues can be dealt with far less number of individuals as IDBI has outsourced majority of the fund and liquidity management and furthermore will require less workforce for performing different payment related exercises.

iii. *Control Benefits*

a. The IDBI bank CMS items permit to keep up better authority over the different banking and treasury related exercises, improve speed and simplicity of reconciliation and also reduces the danger of financial fraud.

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(v) Exchange Finance Scheme

The IDBI bank has set-up devoted exchange outreach groups for products offered in key areas to have an engaged and concentrated way to deal with exchange management. The IDBI bank brings out Trade Finance activities through assigned branches, which offer foreign trade related finance Products like Letters of Credit (LC), Bank Guarantees, Collections, Remittances, Forward Contracts, Packing Credit, Post Shipment Finance, Maturity Factoring, Invoice Discounting and Trade Advisory Services. It is worthy of mention that the IDBI bank was among few of the selected banks which was selected under the protection of Indian Banks' Association (IBA) to test, pilot and execute Structured Financial Messaging System (SFMS) for local trade exchanges. The IDBI bank additionally went on to tie-up with Export Credit Guarantee Corporation (ECGC) for financing the export receivables fully supported by ECGC.

(vi) Tax Payments Assistance Scheme

The IDBI bank offers a wide exhibit of services under the umbrella of Central and State Government agency business (both direct and indirect taxes). The IDBI bank happens to be the first bank to offer online payment of direct taxes and likewise also the first bank to offer online payment of Central Excise Duty and Service Tax. The IDBI bank has the order to collect direct taxes at many designated branches and extension counters across the nation and is also entitled to collect Excise Duty and Service Tax at few nominated branches. Also, the IDBI bank has the directive for online collection of sale tax and stamp duty for certain State Governments and EXIM license charges.

(vii) Direct Discounting of Bills Assistance

IDBI offers deferred credit assistance for sale / purchase of domestic machinery / equipment under its easy to operate direct discounting scheme, to the monetarily stable hardware/equipment maker who wish to encourage sales. The assistance is to the tune of 100 per cent of the complete worth (including insurance, taxes and cargo). Financing cost/discount rate would be as per the prevailing rate at the hour of discounting of bills, depending upon the period of payment viz. monthly/quarterly/ half-yearly/yearly and as indicated by sequential profile of bills.

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(viii) SME Finance Scheme

The IDBI bank has been effectively occupied with giving a significant push to financing of SMEs. With the end goal of improving the credit delivery system and reduce the Turn Around Time (TAT), the IDBI bank has built up an exceptional plan of action to serve the SMEs in India. The bank has established 24 City SME Centres (CSCs) across India in Mumbai, Delhi, Kolkata, Chennai, Bangalore, Hyderabad, Pune among other cities. These CSCs are the bank's centre points while committed SME workstations have been set-up in a few branches across these cities. These branches work as front offices for sales and client care.

The IDBI bank also has a wide range of services and products meeting out the requirements of various segments within small enterprises. Long periods of involvement and the resultant experience gained from being a confidante of large and mid-size corporate houses has converted into comprehensive knowledge about the necessities of business and enterprises. The bank has instrumented items for carriers/transporters, sellers, brokers, and merchants. Moreover, it has a different Transaction Banking Group that has proficiency in items like cash management services, letter of credit, bank guarantee and treasury products.

3.2.5 Developmental Activities of IDBI

(1) Promotional Activities

While executing its developmental function, the bank keeps on playing out a wide scope of persuasive exercises that are associated with progressive ventures for new business entities, consultancy services for micro, small and medium enterprises and projects intended for licensed charitable agencies for the financial upliftment of the oppressed. The focus areas are entrepreneurship development, independent work and daily-wage work in the industrial segment for the more fragile segments of society through charitable organizations, assistance to Science and Technology Entrepreneurs' Parks, Energy Conservation, Common Quality Testing Centres for small enterprises.

(2) Technical Consultancy Organizations

With the objective of making accessible at a realistic cost, consultancy and counselling services to entrepreneurs, especially to new and budding entrepreneurs, IDBI, in a joint effort with other All-India Financial Institutions, has set-up an organization of Technical Consultancy Organizations (TCOs) covering the whole country. TCOs offer enhanced services to MSMEs for the identification, selection, creation and evaluation of projects, their execution and audit.

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(3) Entrepreneurship Development Institute

The realization of the fact that entrepreneurship development is the key to industrial upsurge, IDBI assumed a defining role in establishing Entrepreneurship Development Institute of India (EDI) for cultivating business in the country. It has additionally set-up similar institutions in Bihar, Orissa, Madhya Pradesh and Uttar Pradesh. IDBI likewise stretches out monetary help to different associations in guiding studies that are relevant to industrial progress.

3.2.6 Project Finance

The IDBI bank was set-up in the year 1994 by the esteemed Development Financial Institution Industrial Development Bank of India (IDBI) by revising the IDBI Act. IDBI became IDBI Ltd. on 1st October 2004 and before the completion of the financial year 2004, the consolidation of IDBI Ltd. with IDBI Bank was proposed and consolidation occurred in 2005. The newly formed entity with solid project loaning base and retail credit base was expected to broaden the credit backing to the industrial sector across the country.

A concise view IDBI Bank's lending activity can be viewed from two angles: (A) Corporate Banking and (B) Retail Banking.

Corporate Banking

In the Corporate vertical, the bank has the requisite Infrastructure and Conglomerates section, the Large Corporate section and the Mid-corporate section. The IDBI bank offers monetary types of assistance (both asset based and non-asset based) to large-cap and mid-cap companies. The bank gives both asset based and non-asset based help. Asset based assistance fundamentally includes term loans, cash credit, demand loans and bridge finances. Such services are given as project finance, non-project finance and working capital. Non-asset based assistance, on the other hand, involves Letters of Credit and Bank Guarantees.

Retail Banking

In the Retail vertical, the bank has the Personal Banking Section, SME section and the Agriculture Business Section. It offers a set-up of individual financial items including retail obligation, retail assets, retail payment items and retail investment/ insurance items. Agribusiness advances are reached out to both farm and non-farm segments and also to companies engaged in agricultural business. Procurement of food grains and support against Warehouse Receipts is also extended by the bank. Moreover, the bank also stretches out help to Self-Help Groups and Micro Finance Institutions. A number of transaction related banking services like (current account, cash management, foreign exchange services) are offered to SMEs section.

Fund related assistance is offered to meet capital expenditure necessity through term loans, cash credit and demand loan facilities to meet the working capital necessities of the sector. In this sector also, the non-asset based help comprises of Letters of Credit and Bank Guarantees.

Treasury Banking Operations

The treasury in IDBI Bank Ltd., essentially focuses on maintaining liquidity as it would help in meeting the fund requirements. The surplus funds is effectively managed by the treasury of the bank through a proper portfolio blend of government and corporate securities.

Investment Banking Operations

Playing the role of an investment bank, IDBI also offers Venture Capital Services that includes Loan Syndication services, Equity placements, IPO related activities that include advisory services, monitoring and underwriting, Carbon Credit Advisory, Securitisation, Project Advisory and Mergers and Acquisitions and Advisory services. Investment banking activities are likewise being dished out by the bank's subsidiary unit IDBI Capital Market Services Ltd. Every one of these services highlights the multi-dimensional banking operations taken up by IDBI.

3.3 THE ROLE OF INDUSTRIAL DEVELOPMENT BANK OF INDIA IN INDUSTRIAL PROMOTION OF INDIA

IDBI assists the needy entrepreneurs by offering seed capital and start-up funding for commencing production and related activities. Almost certainly, IDBIs initial move towards industrialization goes far in changing the industrial framework and structure of the economy.

IDBI continually tries through its activities of monetary help to industrial enterprises with an eye to create sustainable development in the regressive areas of the country and thereby lessen the glaring regional disparity that can be observed countrywide. Industrialists who contributed to this cause by trying to set-up modern units in those territories were delighted to be offered concessional loan rates and also received subsidies and backing from concerned State Government. However, the assistance by way of offering concessional rate were withdrawn in 1998.

IDBI today remains the chief term loan providing development banking institution operating in the country with the affirmed objective of pushing forward the country's industrial progress. In addition to providing long-term finance, IDBI is also actively involved in offering promotional support to the country's industrial sector.

IDBI not just carries forward the task of industrial development of the country but also pledges social equity by empowering improvement of businesses in the backward and underdeveloped areas of the country to uplift the nation's industrial benchmark. IDBI has immensely contributed towards balanced industrial progress as its services and activities matched the planning and targets set by the bank.

3.3.1 Challenges for IDBI Bank and the Road Ahead

After a dismal showing for a prolonged period, the IDBI bank is currently back to profitability days. However, of late, it is facing a challenging scenario in the midst of cash crunch and deterioration in asset quality. The following are the difficulties that the IDBI bank is facing and needs to settle:

i) Bottom of the pit as far as execution is concerned

Performance wise, IDBI, the 10th largest Indian bank is the worst performer among the other banks operating on the Indian shores. The net non-performing assets (NPAs) reached to the tune of 16.69 per cent in 2017-18 with provision coverage ratio of 48.43 per cent. The accumulated losses in the first three quarters of 2018-19 have crossed ₹ 10,000 crore. The road to recovery for the bank would be to initially improve its performance by zeroing in on high-yielding assets, fee based income, cross-selling and by additionally focusing on retail.

ii) Plan and need to emerge from RBIs Prompt Corrective Action

The bank is right now under the RBI's Prompt Corrective Action (PCA) system on account of a fall in capital adequacy, return on assets and profitability. LIC entering the system as a new promoter is expected to improve the capital shortage situation as it has ample funds to infuse in IDBI. LIC has, in fact, resolved the issue of long-term fund requirement. The success story of LIC out of its subsidiary LIC Housing Finance has indeed raised hopes that it can also turnaround the IDBI story.

iii) Stepping up the recovery process

Under the prevailing conditions, the most prompt assignment must be the recuperation. While asset reconstruction or sales generation require monumental effort and time, the IBC (Insolvency and Bankruptcy Code) is balancing out well in recovery of the bad loans. The bank needs a methodology to work with different banks to effect a quicker rebuilding of credits under IBC.

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iv) Review of credit standards

While IBC will ensure a decent conduct from corporate borrowers, the bank needs to update its credit guidelines. Technical issues like data analytics, Artificial Intelligence (AI), Machine Learning (ML) need to be exploited for exposing fraud and irregularity to make the credit cycle more secure. The need of the hour is to implement an effective risk management system to assess the creditworthiness of industrial borrowers.

v) Exploiting synergies with LIC

The synergy with LIC can be created through effective utilisation of LICs vast network across the country. LICs branches can be utilized to sell off policies.

viii) Sale of non-core assets

The IDBI bank, which got converted into a bank from being a development financial institution, has a great deal of investments in organizations. For instance, the IDBI bank is a stakeholder in insurance and asset management sector. IDBI, though, intends to sell stakes in these organizations.

Check Your Progress

1. When was the Industrial Development Bank of India (IDBI) established in India?
2. What was the main objective for establishing Industrial Development Bank of India (IDBI)?
3. What are the salient features of the Cash Management Services (CMS) scheme of IDBI?

3.4 ANSWERS TO CHECK YOUR PROGRESS QUESTIONS

1. Industrial Development Bank of India (IDBI) was established under Industrial Development Bank of India Act, 1964 as a Development Financial Institution (DFI) and came into existence on 1 July 1964 vide GoI notice dated 22 June 1964.
2. The primary objective of establishing IDBI was to set-up an apex institution to coordinate the activities of other financial institutions and to act as a financial pool on which other financial institutions can rely. It provides direct

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financial support to industrial units in order to wipe out the gap between supply and demand of medium and long-term finance.

3. The IDBI Bank Cash Management Services (CMS) has accomplished the ISO 9000 confirmation for its product base and technological upbringing. Cash Management Service offers three items – Collections, Payments and Cashweb- an online product offered. Cash Management Services (CMS) disposes off the innate deferrals of funds transfer machinery, accordingly upgrading liquidity and confirming optimal planning and use of funds.

3.5 SUMMARY

- LIC of India finished securing of 51 per cent controlling stake in IDBI Bank on 21 January 2019 making it the dominant investor of the bank.
- The Industrial Development Bank of India was established under the Industrial Development Bank of India Act, 1964 as wholly owned subsidiary of RBI. The ownership of IDBI has since then been transferred to the Central Government from 16th February 1976.
- The IDBI offers credits and advances to industrial entities. There is no limitation on the upper or lower limits to be offered to any entity. The bank ensures advances raised by industrial companies in the open market from the State Co-operative Banks, the Scheduled Banks, the Industrial Finance Corporation of India (IFCI) and other 'notified' monetary establishments.
- Under the Project Finance scheme, the IDBI bank provides financial assistance to the corporates for their projects. Project financing for Greenfield projects is done in both Indian and foreign currencies and are directed towards extension, enhancement and modernization.
- The IDBI bank is an innovation and service driven financial institution managed with financial trustworthiness. The IDBI Bank Cash Management Services (CMS) has accomplished the ISO 9000 confirmation for its product base and technological upbringing.
- IDBI offers deferred credit assistance for sale / purchase of domestic machinery / equipment under its easy to operate direct discounting scheme, to the monetarily stable hardware/equipment maker who wish to encourage sales.
- The realization of the fact that entrepreneurship development is the key to industrial upsurge, IDBI assumed a defining role in establishing

Entrepreneurship Development Institute of India (EDI) for cultivating business in the country.

- In the Retail vertical, the bank has the Personal Banking Section, SME section and the Agriculture Business Section. It offers a set-up of individual financial items including retail obligation, retail assets, retail payment items and retail investment/insurance items.
- IDBI assists the needy entrepreneurs by offering seed capital and start-up funding for commencing production and related activities. Almost certainly, IDBIs initial move towards industrialization goes far in changing the industrial framework and structure of the economy.
- While IBC will ensure a decent conduct from corporate borrowers, the bank needs to update its credit guidelines. Technical issues like data analytics, Artificial Intelligence (AI), Machine Learning (ML) need to be exploited for exposing fraud and irregularity to make the credit cycle more secure.

3.6 KEY WORDS

- **Forex:** It is the market in which foreign currencies are traded.
- **Seed Capital:** This term refers to the initial money that is required for starting a business.
- **Insolvency and Bankruptcy Code:** It is the bankruptcy law of India which seeks to consolidate the existing framework by creating a single law for insolvency and bankruptcy.

3.7 SELF ASSESSMENT QUESTIONS AND EXERCISES

Short-Answer Questions

1. What were the main reasons which led to the establishment of IDBI?
2. Write a short note on the development activities of IDBI.
3. Mention the challenges confronted by IDBI in the present scenario.

Long-Answer Questions

1. Explain the growth and development of IDBI bank.
2. Discuss the objectives and functions of IDBI.

3. Describe the financial assistance activities of IDBI.
4. Analyze the contribution of IDBI in the industrial growth of the country.

NOTES

3.8 FURTHER READINGS

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UNIT 4 TECHNICAL DEVELOPMENT FUND AND VENTURE CAPITAL FUND

Structure

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4.1 Objectives
4.2 Technology Development Fund (TDF)
  4.2.1 Technology Development Fund (TDF) Scheme
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4.0 INTRODUCTION

This unit discusses about the various types of funding that are primarily designed to provide financial assistance to new business ventures. These ventures can be either sector oriented like the case of Technology Development Fund that focuses on being self-reliant to enhance the defence capabilities or financing start-ups through seed financing or financing by venture capitalists. The banking operations involving bill rediscounting and refinancing also plays a vital role towards enhancing liquidity and loan restructuring respectively.

4.1 OBJECTIVES

After going through this unit, you will be able to:

- Discuss Technology Development Fund and Venture Capital Funds

- Explain the concept of Refinancing, Bill Rediscounting and Seed Capital
- Identify the various initiatives taken by the government to encourage new ventures

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4.2 TECHNOLOGY DEVELOPMENT FUND (TDF)

Let us study the concept of Technology Development Fund in detail in this section.

4.2.1 Technology Development Fund (TDF) Scheme

Innovation Technology Development Fund (TDF) has been set up to make India'a Defence Technology self-reliant under the 'Make in India' initiative. It is a programme of MoD (Ministry of Defence) performed by DRDO to meet the necessities of Tri-Services, Defence Production and DRDO.

The plan supports investment of public/private enterprises particularly MSMEs in order to build an eco-system for enhancing cutting edge technology capability for application in the defence sector.

The TDF programme includes the following technology development in terms of:

- Noteworthy improvements in the existing products/process/application etc.
- Technology inclination level up-gradation from TRL3 onwards to recognition of items according to Tri-Services necessities.
- Creation of innovative technologies/state-of-the-art products which can prove to be valuable for the defence applications
- Make import substitution possible for components whose technologies do not exist with the Indian firms.
- The plan will be restricted to improvement of technologies or prototype that is expected to prove useful for the services and have the expected timeframe for completion of two years.

The plan will cover subsidizing through arrangement of funds to the industry that may work in collaboration with the research organizations and academia to carry out innovation, research and development work. These select entities will be denoted as Development Agencies (DAs). However, it is decided that the level of involvement of academia or research institutions should not exceed 40 per cent of the entire effort.

Online applications may be submitted by the potential developers. The developer is shortlisted on the basis of criteria laid down in the Standard Operating Procedures (SOP). It may be noted here, that only Indian developers including Association of Persons (AoP) as mentioned in the SOP are eligible for participation.

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4.2.2 TDF Communities Details

- Academia / Research Institute
- TechnologyExperts
- Industry

Let us study them briefly here.

1. Academia / Research Institute

Academia is considered as a key influencer in shaping a society or a nation. Yesteryear experiences as well as current developments have proved that societies which have understood and successfully implemented technologies have progressed culturally and also became powerful military establishments. Example of Taxila and Patliputra from the history and MIT, Cambridge, Standford, Oxford etc., from the present era can be cited as great contributors towards societal development.

India, in spite of making great advancements in science and technology, is yet to achieve any substantial progress in defence technology, which eventually has resulted in high expenditure towards defence procurements. However, sustained efforts have made India a name to reckon with in missile technology. The present NDA Government has realized this shortcoming and in order to address it without delay has launched various schemes and programmes and pushed the 'Make in India' initiative.

TDF Scheme is one such scheme which allows the academia to participate extensively at every level i.e., from identification of the technology gap to devise a technology to fulfil it.

2. Technology Experts

Technology Development Fund Scheme actually laid a red carpet to the experienced, dynamic and energetic technical experts from the science and technology domains that have passion and will to contribute for the national cause. A subject-matter expert or an expert can be referred to be a person who is a specialist in a specific area, topic or domain. Experts are always an asset as their services are required from the inception to completion stage. An expert plays multiple role of being a mentor, to motivator, to teacher and a path-guiding driver. Indulgence of an expert invariably increases the probability of success. The Technology Development Fund Scheme focuses on a highly specialized and niche area. Involvement of the experts will make sure achieving the goals set for the scheme which in turn will help the nation to build a strong defence technological base. The entire process is expected to take India to the path of self-reliance in the defence sector.

3. Industry

The wholehearted participation of the industry is a prerequisite to achieve self-reliance, be it any sector. Indian industry is required to assume a vital and indispensable part in defence manufacturing. Government of India focusses on utilizing the emerging enthusiasm of the Indian industry and eagerly waits for the private sector to actively participate towards achieving self-reliance, especially in the defence sector.

Technology Development Fund Scheme emphasizes on the development of technologies that will form the core of components/assemblies, which will be in turn used to develop defence equipment/systems/sub-systems/platforms. The country not only looks forward to being completely self-reliant in the manufacturing of defence equipment but also become a global defence equipment supplier.

The following industries are on the watch list of the TDF Scheme:

Public Limited Company, Private Limited Company, Partnership Firm, Limited Liability Partnership, One Person Company, Sole Proprietorship registered as per applicable Indian Laws.

Guidelines to be a member of TDF Industry Community are the following:

- The industry has to be owned and controlled by an Indian Citizen.
- The Industry with excess of 49 per cent foreign investment will not be eligible.
- Industry shall also possess or be in the process of acquiring license/ development of products if the product/ technology under project requires license as per DPIIT's licensing policy.
- Company/ Organization which have not been debarred/ banned/ blacklisted or the business dealings with whom have been 'suspended' / 'put on hold' by the Ministry of Defence.

4.2.3 Eligibility for TDF

- All Indian public and private enterprises, including MSMEs.
- Projects up to INR 10 Crores are eligible for funding; subject to a maximum of 90 per cent of the entire cost of the project. However, 100 per cent of funding may be considered on a case-to-case basis.
- The contribution of academia and research organisations is limited up to 40 per cent of the efforts.

4.2.4 Key Features

- The scheme is solely applicable to the development of technologies or prototype of product having potential use for the services and has a development period not exceeding two years.

- The scheme inspires public/private industries, especially MSMEs to participate to create an atmosphere for improving cutting edge technology, which when applied enhances the efficiency of the military establishment.
- The scheme will cover funding through provision of grants to industry that may work in collaboration with academia or research institutions to carry out innovation, research and development; such chosen entities will be referred to as Development Agencies (DAs). In cases where academia or research institutions are involved, their work involvement cannot exceed 40 per cent of the total effort required.

4.3 VENTURE CAPITAL

Venture Capital may be referred to as investment in long-term equity finance of high risk project with reward possibilities particularly associated with new innovations.

Venture Capital is 'equity support to fund new concepts that involve a risk and at same time, have high growth and profit potential'. Venture capital (also known as VC or Venture) is a type of private equity capital typically provided to early stage, high potential, growth companies in the interest of generating a return through an eventual realization event such as an IPO or Trade Sale of the company. Venture capital investments are generally made as cash in exchange for shares in the invested company.

Venture capital funds are collective investment funds that manage the private investor's money who seek private equity stakes in technology oriented start-ups and small to medium-sized enterprises with high-risk and strong growth potential. These investments are generally characterized as very high-risk/high-return opportunities.

4.3.1 Understanding Venture Capital Funds

Venture Capital (VC) can be defined as a form of equity finance which provides enterprises or companies the chance to raise funds even before they begin they become functional in the market. Venture capital funds are private equity investment instruments which invest in companies that have a rise risk along with a high return profile.

It is significant to note that venture capital funds are different from mutual funds and hedge funds. Venture capital funds are invested in enterprises which have a high risk profile, growth prospects and long investment perspective.

4.3.2 Aims of Venture Capital

- Inspires entrepreneurs and enterprises by fuelling ambitions and dreams, breathing life into promising business ventures, providing foresight, complimenting business acumen etc.

- Promoting R & D
- Financing promising business ventures and funding in the initial stages of life-cycle.

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4.3.3 Features of Venture Capital

- It is a high-risk venture.
- It finances high-tech projects.
- They have a long gestation period.
- It provides managerial and marketing assistance.
- It provides conditional loans.
- It is an equity fund.
- It is a long-term investment and returns are in the form of capital gain.

4.3.4 Operating a Venture Capital Fund

Various phases of venture capital financing may be categorized into seed capital, expansion stage financing and bridge financing depending on the status / stage of the business at the time of the financing. However, regardless of the investment stage, all venture capital funds operate in much the same way.

I. Seed and Start-Up stage

- Conditional loans
- Equity support schemes
- Social development funds
- Informal sources
- Centure leasing

II. Growth & Expansion stage

- Equity support from financial institutions
- Private equity
- Convertible debentures
- Cumulative preference shares

III. Bridge Financing

- Bank loans
- Special purpose vehicles

The various forms or stages of venture capital funding are the following:

Seed Money Stage: Small amount of financing needed to prove a concept or develop a product.

Start-up: Financing for a firm that has started up in the past one year. Funds are likely to pay marketing and product development.

First - Round Financing: Additional money to begin sales and manufacturing after a firm has spent its start-up capital.

Second - Round Financing: Funds earmarked for working capital for a firm that is selling its product, but is still losing money.

Third - Round Financing: Financing for a firm that is breaking even and is contemplating an expansion project.

Fourth - Round Financing: Money provided for firms that are likely to go public soon. This is also known as bridge financing.

4.3.5 Advantages of Venture Capital Financing

(i) Economy Oriented
   - o Pushes industrialization
   - o Technological development
   - o Generates employment
   - o Helps in developing entrepreneurial skills

(ii) Investor Oriented
   - o High profitability, comparatively low risk
   - o Easy exit route

(iii) Entrepreneur Oriented
   - o Helps small and medium first generation entrepreneurs to translate their ideas into reality
   - o Promotes and fosters entrepreneurship in the country

4.3.6 Key Takeaways

- Venture capital funds are investments made in enterprises or start-ups which promise high growth, enhanced risk and long-term investment scenario.
- Hedge funds are also investments made in enterprises which handle high risk and high growth.
- Venture capital funds promise to provide 'seed capital' essential for start-ups or enterprises promising fast growth and high risk.
- Investors in a VC fund will earn a return when a portfolio company exits, either through an IPO, merger, or acquisition.

4.4 SCHEMES OF INDIRECT ASSISTANCE

Let us study about the schemes offering indirect assistance.

4.4.1 Refinancing

A *refinance,* or 'refi' as it is often referred to as, is basically a process of revising and replacing the terms and conditions of an existing debt obligation or credit agreement. A refinancing activity is actually seeking favourable changes in the interest rate, payment schedule, and/or other terms defined in the contract. Once approved, the original / older agreement gets replaced by the modified terms and conditions.

How does a Refinance works / The Methodology?

The primary objective behind opting for a refinance by borrowers is to modify the existing debt terms by more favourable borrowing terms, often initiated by the necessity to tackle shifting economic conditions. Usually, during refinancing, efforts are made to reduce the interest burden over the loan period, make possible changes in the duration of the loan and/or repayment schedule or to switch from a fixed-rate mortgage to an adjustable-rate mortgage (ARM) or vice versa.

Refinancing may also be requested to take advantage of an improved financial status, or a revised investment plan, or in an effort to pay off existing debts by consolidating them into one low-priced loan.

The most common motivational factor for opting refinancing is the fluctuations in the interest-rate environment. Since interest rates are cyclical, it has become a common practice for the consumers to go for refinancing when interest rates drop. Various factors like alterations in the monetary policy, the economic cycle, and market competition can contribute towards a fluctuating interest rate scenario. These factors are most likely to impact interest rates covering all kinds of products such as loans and credit cards. Consequently, a customer with a variable-interest-rate product will tend to pay more interest in such a scenario.

In order to refinance, a borrower must approach either his existing lender or a new one with the request and complete a new loan application. It is to be noted that refinancing involves re-evaluating a customer's credit terms and financial strength. Mortgage loans, car loans, and student loans are common consumer based loans that are put up for refinancing. At the same times, business houses may also want to refinance mortgage loans on commercial properties.

Types of Refinancing

There are several kinds of refinancing options. The type of loan a borrower decides to get depends on the requirements of the borrower. Some of the common refinancing options are the following:

- **Rate-and-term refinancing**: This is the most common type of refinancing. Rate-and-term refinancing allows a borrower to alter the terms of the current mortgage and replace them with terms that are more favourable for him. The older loan is paid off, a new loan is sanctioned with new terms and conditions and the borrower continues to repay the new loan under the modified conditions.

- **Cash-out refinancing**: A cash-out refinance replaces an existing mortgage with a new loan agreement that is more than what the borrower owes on the existing mortgage. The difference goes in cash and the amount can be spent towards debt consolidation or meeting out other financial needs or any other cause. However, the value of the asset must have appreciated during this time. The transaction engages withdrawing the value or equity in the asset in exchange for a higher loan amount (and often a higher interest rate). To put it simply, when an asset enhances in value on paper, the individual can obtain that value with a loan rather than by selling that asset. This alternative increases the total loan amount but gives the borrower access to cash immediately while still retaining ownership of the asset.
- **Cash-in refinancing**: This is an arrangement that allows the borrower to repay a portion of the loan to reduce the loan-to-value (LTV) ratio and improve the value of equity on the mortgage. This results in smaller loan payments for the remaining period.
- **Consolidation refinancing**: A consolidation of an existing loan is of the effective way to refinance. This method can be applied when an investor obtains a single loan at a rate that is lower than their current average interest rate across several credit products. This type of refinancing requires the customer or enterprise to apply for a new loan at a lower rate and then pay off the existing debt with the new loan, leaving their total outstanding principal with considerably lower interest rate payments.

4.4.2 Bills Rediscounting

Rediscounting of commercial bills is a system wherein a financial institution rediscounts unmatured discounted commercial bills with any other financial institution.

Bills Rediscounting Scheme

The Reserve Bank of India (RBI) introduced the Bills Market Scheme (BMS) in 1952, which was later restructured and renamed as the New Bills Market Scheme (NBMS). This scheme allowed the commercial banks to rediscount the bills which were initially discounted by them with approved institutions such as Commercial Banks, Development Financial Institutions, Mutual Funds, and Primary Dealers etc. serving the purpose of rediscounts.

Objectives of the BRS scheme

The objectives of the BRS scheme are as follows:

- To offer to create an instrument which inspires more disciplined use of bank credit
- To expedite liquidity in the banking system.

Eligibility

A. for Banks

Rediscounting is allowed for all the scheduled banks and they can rediscount the bills with the Reserve Bank of India or any other institution.

B. Eligibility of Bills

In order to become eligible for rediscounting, the bills must possess the following characteristics:

- The front portion of the bill indicates the nature of the transaction.
- The usance period is not more than ninety days.
- Purchaser's licensed bank must have accepted the Bill.
- The bill should consist of two proper signatures, one of which should be of the bank.
- It is not eligible for commodities of the Reserve Bank of India.

Rediscounting Procedure by Banks

Commercial banks are permitted to draw derivatives of usance promissory notes for maturities of up to ninety days depending on the strength of commercial bills discounted by their respective branches. The entire operation is centralized with the bank's main fund activity for effective control.

Timeline of the Approved Rediscounting

The term period approved for normal rediscounting is one year unless the same is immediately cancelled, suspended, amended or extended by the Credit Committee. The rediscounting can be renewed annually by submitting an application in this regard at least a month before the expiry of the specified date. It may be noted, that, for newly merged or consolidated banks, a temporary rediscounting may be granted for 180 days.

RBI's Derivatives regarding Bill Rediscounting

The RBI has made the following directives concerning bill rediscounting:

- Rediscounting of the ineligible bill will be handled as an unsecured loan.
- Only usance bills held by other banks can be rediscounted.

- Finance companies cannot avail this facility.
- Banks should not rediscount bills discounted by non-banks.
- Accommodation bill has no scope for rediscounts.

Lodging of Bills with RBI

The usual procedure involving rediscounting required the banks to lodge all such bills with RBI. This amplified the volume of operations. Of late, the RBI has done with the requirement of lodging of eligible bills up to face value of ₹ 10 lakh. Hence, the banks have the liberty to keep the bills even after rediscounting with them as agents of RBI once the due date payment is made.

Various rates prevailing in the Bill Markets

- SBI hundi rate – the rate at which SBI used to discount hundis of indigenous bankers.
- SBI discount rate – the rate at which SBI discounts first class usance bills.
- Commercial banks rate – the rate at which the commercial banks get the bill discounted with each other.
- Bank rate – the rate at which the RBI discounts eligible bills from commercial banks

Importance of Bill Rediscounting Scheme (BRS) in Funds Management

The importance of BRS in funds management is as follows:

- BRS always have a definite maturity period.
- If dishonoured, provisions for the penalty are substantial.
- Risk is minimized as can be honoured with two good signatures.
- BRS proves to be the better utilization of credit.
- Banks can meet their fund's requirements by discounting with RBI.

4.4.3 Seed Capital

Seed capital, in simple words is the initial amount of capital needed to start a business. When this initial capital is borrowed, it is seed capital financing for the borrower and seed capital investment for the lender. This, seed capital investment may be referred to as the initial round of investment required to start and set-up a business, the initial money that give wings to the idea to get off the ground. The word 'seed' is used as the entire scenario is compared to growing of a tree. The initial fund i.e., the seed capital is compared to the seed of the plant which grows up to take the shape of a tree, just like the start-ups growing to become prominent business houses. It refers to the type of financing used in the formation of a start-up. Funding is done by private investors, usually against an equity stake or on profit-sharing basis. Under normal circumstances, the seed capital of a company is raised from close and known quarters like family, friends or other known person of the promoter. Obtaining seed capital is the first of four funding stages required for a start-up to become an established business.

Nowadays, there are many young and upcoming entrepreneurs coming with innovative business ideas that are feasible and have the viability of turning them into a successful business venture. However, the biggest hurdle they face in making their dream a reality is the scarcity of funds. Seed funding is a boon to these budding entrepreneurs who are extremely eager to establish their own start-up.

Three of the most profound challenges that an aspiring entrepreneur faces are access to capital, a proper roadmap for execution that all likely would get to success and a viable environment that facilitates execution of the idea. Seed capital financing comes to the rescue as apart from funding, the seed capitalists also share their experiences and learning's gathered from previous ventures. In addition to access to capital, their guidance also proves to be a vital input.

However, one need to understand the fact that the risk involved with seed fund is more when compared to general investments in the sense that these investments are intended for new untested ventures whereas in the latter case, funding is done to an established businesses. Seed capital providers, unlike the Venture Capitalists and Equity Financers, are quite willing to provide the Seed Fund for these Start-up Companies. In return for these investments, they ask for an equity stake in the company. In addition to the funding, the seed fund investors also offer financial and legal support to the start-up companies. Trends suggest that the number of such seed fund investors is on the rise, which augments well for the upcoming entrepreneurs.

The advantage of seed capital financing is that the amount of capital to be initially invested is relatively low when compared to other sources of funding like venture capital assistance etc., since the business is still in the conceptual stage, and hence the financial risk involved is less. The financing is at a pre revenue stage aimed towards covering the research and development expenses until reaching a stage where a product or service can start generating revenue. If on reaching this stage, the product or service looks promising and has marketability, it attracts the attention of the venture capitalists who then do the bulk funding.

Famous Seed Funding Agencies

The following are some well-known seed funding agencies operating in India:

- Indian Angel Network
- The Hatch
- Technology Business Incubator, IIT Delhi
- SeedInvest

- Seedrs
- Crowdcube

Start-up India Seed Fund Scheme (SISFS)

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The scheme has been approved for the period of next four years starting from 2021-22. It will be implemented with effect from 1st April 2021. The scheme aims to provide financial assistance to start-ups to cover expenses on concept development, prototype development, product trials, market entry and commercialization. A corpus of ₹ 945 crore will be divided over the next four years for providing seed funding to eligible start-ups through eligible incubators across India. The scheme is expected to support about 3600 start-ups.

A number of measures announced under 'Atmanirbhar Bharat' Package are beneficial for start-ups. Some of these benefits are given below:

Benefits under 'Atmanirbhar Bharat' for start-ups:

- With respect to *Rescheduling of Payments – Term Loans and Working Capital Facilities*
  i. A cushion was provided during COVID-19 pandemic times in respect of all term loans (including agricultural term loans, retail and crop loans), all commercial banks (including regional rural banks, small finance banks and local area banks), co-operative banks, all-India Financial Institutions, and NBFCs (including housing finance companies) ("lending institutions") by way of granting permission for a moratorium of three months on payment of all instalments falling due between March 1, 2020 and May 31, 2020. In view of the extension of lockdown and continuing disruption on account of COVID-19, all lending institutions were permitted to extend the moratorium by another three months i.e., from June 1, 2020 to August 31, 2020 on payment of all instalments in respect of term loans.
  ii. In respect of working capital facilities sanctioned in the form of cash credit/overdraft, lending institutions were permitted to defer the recovery of interest applied in respect of all such facilities during the period from 1 March 2020 upto 31 May 2020. Further extension was granted up to 31st August 2020.
  iii. Kamath Committee: An expert committee formed by the Reserve Bank of India (RBI) under the chairmanship of Shri K.V. Kamath made recommendations on the required financial parameters to be factored in the resolution plans under the 'Resolution Framework for Covid19-related Stress' along with sector specific benchmark ranges for such parameters. The recommendations of the Committee have

been broadly accepted by RBI. Accordingly, RBI has specified five specific financial ratios and the sector-specific thresholds for each ratio in respect of 26 sectors to be taken into account while finalizing the resolution plans.

iv. Easing of Working Capital Financing: Similar relief was announced in respect of working capital facilities also. To cover up the financial stress faced by the borrowers on account of the economic fallout of the pandemic, lending institutions were permitted to recalculate the 'drawing power' by reducing the margins and/or by reassessing the working capital cycle.

- *Measures for businesses including MSMEs - These measure would support eligible start-ups*

i. ₹ 3 lakh crore Emergency Working Capital Facility for Businesses including MSMEs.

ii. ₹ 20,000 crore Subordinate Debt for Stressed MSMEs.

iii. ₹ 50,000 crore Equity infusion for MSMEs through Fund of Funds.

iv. New definition of MSME: The structures of MSMEs were revamped. Micro manufacturing and services unit will now be defines through an investment of ₹ 1 crore of investment and a turnover of ₹ 5 crore. The limit of small unit increased to ₹ 10 crore of investment and ₹ 50 crore of turnover. Similarly, the limit of a medium unit increased to ₹ 20 crore of investment and ₹ 100 crore of turnover. The limit for medium manufacturing and service units was further increased to ₹ 50 crore of investment and ₹ 250 crore of turnover. It has also been decided that revenue generated from exports will be kept out of the purview of calculation of turnover for any category of MSME units whether micro, small or medium.

v. Global tenders has been disallowed upto ₹ 200 crore, giving preference to domestic suppliers and boost to start-ups.

vi. Production-Linked Incentive (PLI) Scheme

vii. Reliefs through Employee Provident Fund (EPF)

viii. EPF contribution reduced for Business & Workers for 3 months.

Difference between Seed Capital and Venture Capital

- In the case of seed capital, the primary purpose is to assist technocrats in 'gap - filling'. Technocrats are entrepreneurs setting up manufacturing activities to meet promoter's contribution.
- In the case of venture capital, the return is in the form of capital gain by investing in companies having attractive growth and earning potential.

NOTES

Check Your Progress

1. What are the guidelines to be a member of TDF Industry Community?
2. List the features of venture capital.
3. What is the primary objective behind opting for a refinance?
4. What are the objectives of the BRS scheme?
5. State the importance of BRS in funds management.
6. Mention one advantage of seed capital financing.

4.5 ANSWERS TO CHECK YOUR PROGRESS QUESTIONS

1. Guidelines to be a member of TDF Industry Community are the following:
    - The industry has to be owned and controlled by an Indian Citizen.
    - The Industry with excess of 49 per cent foreign investment will not be eligible.
    - Industry shall also possess or be in the process of acquiring license/ development of products if the product/ technology under project requires license as per DPIIT's licensing policy.
    - Company/ Organization which have not been debarred/ banned/ blacklisted or the business dealings with whom have been 'suspended' / 'put on hold' by the Ministry of Defence.
2. The features of venture capital are the following:
    - It is a high-risk venture.
    - It finances high-tech projects.
    - They have a long gestation period.
    - It provides managerial and marketing assistance.
    - It provides conditional loans.
    - It is an equity fund.
    - It is a long-term investment and returns are in the form of capital gain.
3. The primary objective behind opting for refinance by borrowers is to modify the existing debt terms by more favourable borrowing terms, often initiated by the necessity to tackle shifting economic conditions.

4. The objectives of the BRS scheme are as follows:
   (i) To offer to create an instrument which inspires more disciplined use of bank credit
   (ii) To expedite liquidity in the banking system.
5. The importance of BRS in funds management is as follows:
   - BRS always have a definite maturity period.
   - If dishonoured, provisions for the penalty are substantial.
   - Risk is minimized as can be honoured with two good signatures.
   - BRS proves to be the better utilization of credit.
   - Banks can meet their fund's requirements by discounting with RBI.
6. The advantage of seed capital financing is that the amount of capital to be initially invested is relatively low when compared to other sources of funding like venture capital assistance etc., since the business is still in the conceptual stage, and hence the financial risk involved is less.

4.6 SUMMARY

- Innovation Technology Development Fund (TDF) has been set up to make India'a Defence Technology self-reliant under the 'Make in India' initiative. It is a programme of MoD (Ministry of Defence) performed by DRDO to meet the necessities of Tri-Services, Defence Production and DRDO.
- The plan will cover subsidizing through arrangement of funds to the industry that may work in collaboration with the research organizations and academia to carry out innovation, research and development work. These select entities will be denoted as Development Agencies (DAs).
- Academia is considered as a key influencer in shaping a society or a nation. Yesteryear experiences as well as current developments have proved that societies which have understood and successfully implemented technologies have progressed culturally and also became powerful military establishments.
- Technology Development Fund Scheme actually laid a red carpet to the experienced, dynamic and energetic technical experts from the science and technology domains that have passion and will to contribute for the national cause.
- The wholehearted participation of the industry is a prerequisite to achieve self-reliance, be it any sector. Indian industry is required to assume a vital and indispensable part in defence manufacturing.

- Venture Capital may be referred to as investment in long-term equity finance of high risk project with reward possibilities particularly associated with new innovations.
- Venture Capital (VC) can be defined as a form of equity finance which provides enterprises or companies the chance to raise funds even before they begin they become functional in the market.
- Various phases of venture capital financing may be categorized into seed capital, expansion stage financing and bridge financing depending on the status / stage of the business at the time of the financing.
- The primary objective behind opting for a refinance by borrowers is to modify the existing debt terms by more favourable borrowing terms, often initiated by the necessity to tackle shifting economic conditions.
- Rediscounting of commercial bills is a system wherein a financial institution rediscounts unmatured discounted commercial bills with any other financial institution.
- Commercial banks are permitted to draw derivatives of usance promissory notes for maturities of up to ninety days depending on the strength of commercial bills discounted by their respective branches. The entire operations is centralized with the bank's main fund activity for effective control.
- Seed capital, in simple words is the initial amount of capital needed to start a business. When this initial capital is borrowed, it is seed capital financing for the borrower and seed capital investment for the lender.
- The advantage of seed capital financing is that the amount of capital to be initially invested is relatively low when compared to other sources of funding like venture capital assistance etc., since the business is still in the conceptual stage, and hence the financial risk involved is less.

4.7 KEY WORDS

- **Venture Capital:** It may be referred to as investment in long-term equity finance of high risk project with reward possibilities particularly associated with new innovations.
- **IPO:** Initial public offering is the process by which a private company can go public by sale of its stocks to general public.
- **Technocrats**: These are entrepreneurs setting up manufacturing activities to meet promoter's contribution.

4.8 SELF ASSESSMENT QUESTIONS AND EXERCISES

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Short-Answer Questions

1. What is the Technology Development Fund (TDF)?
2. List the salient features of the Technology Development Fund.
3. Write a short note on venture capital funds.
4. Mention the advantages of venture funds.
5. How does refinancing work in the banking sector?
6. What is the rediscounting procedure adopted by banks?
7. List the well-known seed funding agencies operating in India.

Long-Answer Questions

1. Discuss the key features of Technology Development Fund.
2. Explain the functioning of a venture capital fund.
3. Describe the various types of refinancing.
4. Analyze the significance of seed capital.
5. Examine the significant features of the Start-up India Seed Fund Scheme (SISFS).

4.9 FURTHER READINGS

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BLOCK - II
TCOs & NSIC

UNIT 5 TECHNICAL CONSULTANCY ORGANIZATIONS AND FEE BASED ACTIVITIES OF IDBI

Structure

5.0 Introduction
5.1 Objectives
5.2 Technical Consultancy Organizations
  5.2.1 Activities of TCOS
  5.2.2 List of Primary TCOS
5.3 Industrial Development Bank of India (IDBI)
  5.3.1 Scope of IDBI
  5.3.2 Assistance Schemes
5.4 Answers to Check Your Progress Questions
5.5 Summary
5.6 Key Words
5.7 Self Assessment Questions and Exercises
5.8 Further Readings

5.0 INTRODUCTION

Technical Consultancy Organizations (TCOs) were established to provide technical consultancy to industrial outfits. These associations were set-up by the All India Financial Institutions (IDBI, ICICI, IFCI, and so forth) in alliance with the state level financial/development institutions and commercial banks. In this unit, you will study about TCOs and the fee based services of IDBI.

5.1 OBJECTIVES

After going through this unit, you will be able to:

- State the objectives of Technical Consultancy Organizations (TCOs)
- List the major TCOs operating in India
- Describe the various services offered by IDBI

5.2 TECHNICAL CONSULTANCY ORGANIZATIONS

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There are on the whole 18 state-level TCOs across India. During its operations, the TCOs have become multi-functional from just being consultancy firms to organizations who also take care of project reports, market reviews, and so forth. Some TCOs, for example, KITCO have expanded to bring to the table consultancy services for execution of ventures under one umbrella from 'Idea generation to Implementation'.

The Technical Consultancy Organizations (TCOs) have mainly flourished in the post-independence era. Of late, Indian TCOs have flourished across various sectors ranging from food processing to advanced areas like energy, electronics and power generation etc. A number of Indian TCOs have made sustained efforts to be a part of the international market in the field of technical consultancy services. However, the success rate, as of now, is not very encouraging.

5.2.1 Activities of TCOs

The activities provided by the TCOs may be summed up as below:

- Development of industry clusters
- Conducting Industry Potential Surveys /Techno-Economic Viability (TEV) studies
- Infrastructure Planning
- Energy and Environment Research and Management
- NPA Resolution
- Vocational Training
- Technology Facilitation / Preparation of Project Profiles
- Conducting Entrepreneurship Development Programmes
- Conducting Market Research for specific products
- Merchant Banking Services
- Consultancy to Export-oriented Units

5.2.2 List of Primary TCOs

The following is a list of the major TCOs operating in India.

- APITCO Ltd. (Andhra Pradesh)
- GITCO Ltd. (Gujarat)
- HIMCON Ltd. (Himachal Pradesh)
- ITCOT Consultancy and Services Ltd. (Tamil Nadu)
- KITCO Ltd. (Kerala)

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- Technical Consultancy Services Organisation of Karnataka (TECSOK) (Karnataka)
- Madhya Pradesh Consultancy Organisation Ltd. (MPCON) (Madhya Pradesh)
- MITCON Consultancy and Engineering Services Ltd. (Maharashtra)
- North India Technical Consultancy Organisation Ltd. (NITCON)
- UP Industrial Consultants Ltd. (UPICO) (Uttar Pradesh)
- West Bengal Consultancy Organisation Ltd. (WEBCON)

5.3 INDUSTRIAL DEVELOPMENT BANK OF INDIA (IDBI)

As you have learnt in an earlier units, the Industrial Development Bank of India (IDBI) was set-up in July 1964 as a wholly owned subsidiary of the Reserve Bank of India (RBI) as per the Industrial Development Bank of India Act, 1964.

IDBI was assigned to perform the following functions:

- Synchronize the activities of other financial institutions;
- Complement their resources; and
- Plan and stimulate the growth of high priority industries

It is very clear from the above objectives that IDBI's operational area and scope is very wide. IDBI, in fact, covers every activity that is somehow related to industrial financing and growth. IDBI got autonomy in February 1976 when its ownership was passed on from the RBI to the Government of India. Now the 'Bank' can do any business with the prior approved of the Central Government.

5.3.1 Scope of IDBI

The scope of work of the IDBI is rather very wide. No restrictions have been placed with regards to:

(i) The nature, size, type of industry to be financed;

(ii) Quantum of funds to be supplied;

(iii) Period for which accommodation can be made available, or

(iv) The form of security to be accepted.

IDBI has been given free hand to finance all types of industrial concerns, be it in the public sector or the private sector. Moreover, it can also finance other financial institutions and can start its own units. 'Industrial Concern' to be financed by IDBI 'means any concern engaged or to be engaged in the manufacture, preservation or processing of goods or in shipping or in mining or in the hotel industry or in the transport of passengers or goods by road or by water or by air or in the generation or distribution ofelectricity or any other form of power.'

The tenure of direct financing by IDBI is not limited. However, there is restriction in the case of refinancing wherein the maximum period might extend from 3 to 25 years with an exception that in the case of a scheduled or state cooperative bank, the facility is available only for loans repayable from 3 to 10 years. Also, export financing for specific products can be refinanced for a period from 6 months to 10 years. Thus, it can be opined that only refinancing activities of the bank have been defined.

The activities of IDBI had been planned in such a way that it encompasses all kinds of enterprises, from large to medium to small industries.

5.3.2 Assistance Schemes

The assistance schemes of IDBI may be divided into four broad groups:

1. Direct Assistance Schemes: Direct financial assistance in the form of loans, shares-subscription, guarantees etc. is being provided by IDBI under the Direct Assistance Scheme.
2. Indirect Assistance Schemes: These schemes comprise:
   - Refinancing of industrial loans granted by financial institutions;
   - Rediscounting of bills arising out of routine business functioning;
   - Assistance to other financial institutions by way of subscription of their shares.
3. Export Financing Schemes: The assistance under this scheme involves financing through direct loans and guarantees to exporters by participating with banks, refinancing of medium term export credit granted by banks and overdue buyer's credit.
4. Promotional Schemes: These schemes are meant for bringing about the viable process of industrialization. The various promotional schemes of IDBI include the following:
   (i) Assistance for backward area development;
   (ii) Assistance to small, medium entities and so on.

5.3.3 Fee Based Services of IDBI

IDBI, right from its inception, has been continuously assisting the industry through a wide range of fee based financial products and advisory services like corporate advisory services, loan syndication, debenture trusteeship, forex services and so forth. It shaped IDBI as a one stop financial supermarket for all financial needs. In recent years, IDBI has added to its repertoire merchant banking services also. Currently, it provides the following services and products:

1. Fund Based Products

- Term Loan: Both rupee and foreign currency
- Direct subscription and underwriting of equity and debt instruments

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- Guarantee
- Venture Capital
- Equipment leasing
- Bills Finance
- Refinance to state level institutions/ banks

2. Merchant Banking

The merchant banking services that IDBI provides include pre-project counselling, project appraisal, placement of equity with banks, foreign institutional investors, high net worth investors, mutual funds, institutional investors and private equity funds, placement of preference shares and debentures with domestic investors, structuring and syndication of bought out deals, loan syndication, syndication of structured debt instrument, co-ordinating the financial participation of multilateral agencies and international banks, issue management offering advice on the management of tender offer. IDBI focuses on managing only select large sized equity issue which would attract investors' interest. Even during the subdued stock market condition in 1999-2000, IDBI successfully managed 40 public and right issues involving mobilization of ₹ 5,136 crore. During 1999-2000, IDBI also undertook two assignments for private placement of equity and bonds aggregating to ₹ 120 crore. It also carried out appraisal of four large capital investments planned by 'Navaratna' PSUs.

It was only in 1967 that Grindlays Bank started merchant banking services in India. Initially, till 1970s, merchant banking services were limited to providing management of share issues and sub-aspects of financial consultancies. The mid 1970s saw the boom in the capital market with the introduction of Foreign Exchange Regulation Act (FERA) (1973). This boom increased awareness about the capital market among common investors. Few commercial banks and financial institutions soon followed suit and set-up merchant banking divisions. In addition, private financial brokers also started private merchant banking organizations. Today, merchant banking set-up in the country is broadly divided into the following groups:

i. **Foreign Banks:** Today foreign banks like Citibank, Standard Chartered Bank and HSBC are also active in providing merchant banking services.

ii. **Indian Banks**: State Bank of India, which incidentally is also the largest of all Indian banks, took the lead among Indian banks and is at present well-established in the merchant banking sector. The other banks that followed suit are Bank of India, Central Bank of India, Bank of Baroda, Punjab National Bank, UCO Bank and Canara Bank.

iii. **Private Merchant Bankers:** The leading private broker firms who were already involved in providing portfolio management services joined the merchant banking bandwagon. Today, firms like J.M. Financial Consultants, Champaklal Investments and Financial Consultancy, V.B. Desai Consultants etc., are some of the leading private merchant bankers operating in our country.

iv. **Financial Institutions:** Financial institutions like ICICI and Industrial Reconstruction Corporation of India (IRCI) are also into merchant banking operations and their main focus and attention is on mergers, amalgamations and takeovers. As already mentioned, the role of merchant banking in India in the early stages was largely confined to public issue management. In those years, the country felt a strong requirement of merchant banking firms as several public issues (which came to be popularly known as FERA issues) came to the market at that time. Today, the scope and coverage of merchant banking activities goes beyond the realm of just issue management.

- **Project Finance**

Once a specific project is decided upon by a client, the merchant banking division makes a framework of the package to be provided. It includes all issues related to financial structuring and financing. Both, the merchant banking division and the client work in tandem along with the technical consultants to prepare a comprehensive financial file. As a loan syndication service, the division as a representative of the client enters into negotiation with respect to various terms and conditions relating to financing with the financial institutions and also complete the documentation process. Preparing a full and final project finance report tests the skillset and creativity of the merchant banker. In addition to loan syndication, it also covers matters related to issue management, euro-currency financing and supplier or buyer credits.

IDBI provides project finance, both in rupee and foreign currencies, to boost capital formation and infrastructure development in the country. The bank is involved in funding for Greenfield Projects as well as expansion, diversification and modernization of projects. While performing project appraisal and monitoring, the bank strictly adheres to the best global practices. IDBI is also involved in non-project financing through short-term loan.

- **Corporate Finance**

External financing also includes raising funds from the market by issuing shares and debentures. The merchant banker is expected to manage the concerned public issue that includes structuring the issue, obtaining the requisite approvals (including the consent of the Controller of Capital Issues), selection and appointment of underwriters, brokers and bankers for the issue, preparation of the prospectus, and also coordination with all the other related agencies. Issue management has been a very important aspect in the basket of services provided by the merchant bankers and its importance can be gauged from the increased participation of the investors in the capital market. The expertise and experience of the merchant bankers and their relationship with the underwriters and brokers helps to create a proper synchronization between the activities related to the issue.

- **Entrepreneur Starting a New Project**

An entrepreneur who has decided to set-up a new project needs to first obtain a Letter of Intent (LoI) from the Government of India which later gets converted into an Industrial Licence for the proposed project. In most of the circumstances, by the time the merchant banker is approached by the client, the draft project report is already prepared and the company is already incorporated. It is generally observed that the merchant bankers are approached for projects costing more than ₹ 1 crore even though they are equipped and willing to handle the affairs of projects of any size.

- **Existing Units**

Issues popping up for the existing companies are related to expansion, diversification, or modernization of the existing set-up. The merchant bankers are also well-equipped to assist the promoters in all these aspects. They also manage internal reconstruction related matters like amalgamation, absorption and reconstruction.

The basket of services offered by the merchant bankers may be broadly grouped under two heads, viz., counselling and procuring finance. Let us look into the various activities undertaken by a bank offering merchant banking services:

I. Project counselling or reinvestment studies for investors

The merchant banker contributes by way of

i. Identifying promising projects,
ii. Preparing feasibility studies (both economic and financial),
iii. Preparing exhaustive project reports,
iv. Assisting investors in obtaining licences,
v. Deciding on the capital structure,
vi. Negotiate and make arrangements for foreign collaborations and
vii. Provide guidance on M&As and amalgamation

II) Loan Syndication and project finance

The steps that follow once a project is cleared by the government are the following:

i. Preparing the dossier required for applying to financial institutions, banks and other sources of finance.

ii. Educate the promoter about government policies, demand-supply gaps, raw material availability, product-mix, plan capacity utilization, requirements of plant and machinery etc.
iii. Search for alternate sources of funds.
iv. Coordinating with related government departments, financial institutions, banks etc.
v. Advice and assist for modernization, expansion and diversification.

3) Issue management (including equity dilution)

One of the most coveted services provided by the merchant bankers includes managing the public issue of shares/ debentures and also an offer for sales. Issue management is done by the merchant banker by performing the following services:

i. Decide the size and timing of a public issue.
ii. Complete the documentation and liaison with the Controller of Capital issues for clearances etc. It also looks after the marketing and creating awareness regarding the issue.
iii. Selection and appointment of underwriters,
iv. Appointment of the bankers and brokers as well as issue houses,
v. Issue management,
vi. Proper coordination with stock brokers, portfolio managers and press for pre-selling and media coverage,
vii. Prepare draft prospectus and other related documents,
viii. Establish network throughout the country to collect applications and
ix. Provide marketing assistance by preparing advertising and promotional plan and material.

4) Provision of working capital

Working capital is an integral part for running a business activity and the merchant bankers being a part of the banking system, are expected to assist to arrange for working capital finance especially for the new ventures. The face of the working capital financing has changes in recent times with raising funds through issue of debentures on 'Rights' basis. Merchant Bankers play a pivotal role in completing the necessary paper work required by various financial institutions such LIC, GIC, UTI and others. Trustees for the debentures are also arranged by the merchant bankers and it is ensured that the balance portion is tied up with the other bankers.

5) Foreign Currency Loans

The merchant banker makes arrangement for export credit and foreign currency loans.

6) Portfolio management for non-residents

The merchant bankers assists NRIs in identification and selection of projects and issues related to raising of funds from the market. Their services include the following:

i. Guidance on purchase and sale of securities
ii. Handling of such transactions
iii. Educate and provide information on market conditions
iv. Keep safe custody of documents
v. Collection of earnings (dividend, interest etc.)
vi. Acts as a link between non-residents and the Reserve Bank of India for obtaining necessary permission.

In addition to the above mentioned traditional services, the merchant bankers are also entering into leasing services, which has added a new dimension to their ever growing basket of services.

The merchant bankers are also always on the prowl to identify opportunities for new ventures in the country. In this regard, they gather information from the Controller of Capital Issues, Registrar of Companies and State and Central financial institutions.

- **Project Counselling**

Project counselling is about confirming the feasibility and viability of the project. This is done on the basis of the technical appraisal, done with the help of the Technical and Industrial Consultancy Division. Once convinced of the technical feasibility and commercial viability of the project, the merchant banker moves on to prepare the financial structure. The aspects that are studied to reach to a conclusion regarding financial structure are a) the norms laid down by term-lending institutions regarding the debt-equity ratio and the promoter’s minimum contribution to the total cost of the project; b) the availability of various backward area subsidies; and c) in case of equity issue the norms laid down by the stock exchanges for the listing of shares.

The financial structuring assistance also covers advice about setting up of units in the ‘joint sector’, where state level financial institutions contribute 26 per cent of the equity share capital, while the private promoter contributes 25 per cent and the balance of 49 per cent of the shares are made available to the public. On the other hand, in a ‘state assisted unit’, state financial institutions contribute 11 per cent, the promoters 40 per cent and the pubic 49 per cent of the equity shares capital. For the purpose of listing in the stock exchanges, minimum 60 per cent of the equity share capital has to be offered to the public incase of units promoted by private promoters and 49 per cent in the case of a joint sector or state assisted project.

7. Corporate Advisory Services

Various services that are offered by the merchant bankers that fall under the category of corporate advisory services include equity and business valuation; provide advice with respect to merger and acquisitions, business and financial restructuring, privatization and restructuring/rehabilitation of weak units. Among non-fund business, the IDBI has focused more on providing advisory services to the corporate sector. IDBI boasts of delivering advisory services and loan syndication services to large projects, mainly in power, petroleum, telecommunications and steel sectors. As a part of advisory services, IDBI has also provided consultancy services to the Government of India on its disinvestment policy for two public sector enterprises. IDBI offers a wide array of corporate banking services under various business services.

To provide advisory services, IDBI has a dedicated team that works out on the terms and conditions for the services offered. Special designated branches of the bank offers trade finance operations, which provide products that include Letters of credit, Bank Guarantee Collections, Remittances, Forward Contracts, Packing Credit, Post shipment finance, Maturity factoring, Invoice Discounting and Trade Advisory services. IDBI happens to be the first bank to offer online payment facility for payment of direct taxes, Central Excise Duty and Service Tax at select branches. Also, it has the additional responsibility of collecting sales tax, stamp duty and import / export licence fees for certain state governments.

8. Trusteeship Services

Trusteeship services are being provided by IDBI since 1992-93. Acting as a trustee, the bank represents and protects the interest of debenture/bond holders. Moreover, IDBI also performs the functions of security agent and mortgage trustee in respect of loans granted by domestic and foreign lenders to companies.The Bank accepts trusteeship only on the condition that the companies have SEBI ratio not exceeding 2:1, current ratio of 1.33:1 and holds a satisfactory credit rating in the case of a public issue. The large volume of assistances rendered by IDBI has resulted in the creation of strategic capabilities for various industries. One may cite the example of how the refinancing activity has contributed towards the development of large and well dispersed Small Scale Sector (SSS).

IDBI has also played a strategic role in diverse areas such as entrepreneurship development, capital markets and technology and consultancy services. It has also contributed towards balanced regional development. In its role as the apex financial institution for the industrial sector, IDBI apart from providing financial resources and other support to development financial institutions, both at the all India and state levels, have synchronized the operations and mobilized their assistance in such a way that they are in tune with the national priorities. While focusing on all these activities, IDBI has always been watchful about its own financial health. Alongside the activities, the bank itself has grown in size and stature and

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today ranks, amongst the first ten largest development banks of the world. IDBI has to its credit the introduction of innovative financial services like equipment finance, asset credit, equipment leasing, corporate loans and bridge loans against public issues. One of the most significant contribution of IDBI is the setting up of the stock Holding Corporation of India Ltd.(SHCIL) in 1987, providing custodial facilities and initiating the era of demat account. IDBI was also entrusted with the responsibility of setting up Securities and Exchange Board of India (SEBI) and the bank responded by offering organizational and resource support to SEBI in the initial years. IDBI is also the nodal agency for establishing the National Stock Exchange. Other institutions promoted by IDBI include Credit Analysis and Research Limited and Investor Services of India Limited.

9. Forex Services

The Development Bank Strategic Business Unit (DBSBU) of IDBI opens Letters of Credit (LCs) and effect Foreign Currency (FC) remittances on behalf of its assisted companies for imports of goods and services. It also disburses foreign currency loans to its clients for end-uses as permitted under the prevailing External Commercial Borrowing (ECBs) guidelines. The Commercial Bank Strategic Business Unit (CBSBU) of IDBI provides various trade finance products viz. Letters of Credit, Standby Letters of Credit, Bank Guarantees, Collections, Remittances, Forward Contracts, Packing Credit, Post Shipment Finance, Maturity Factoring, Invoice Discounting and Trade Advisory.

10. Treasury Operations

A separate treasury department with an Integrated Dealing Room (Comprising Rupee and FC) has been set-up by IDBI that exclusively monitors the overall liquidity position, investment of surplus funds with the objective of enhancing fields and to take an integrated view of the developments in both money and forex markets. The bank focuses on maximizing the returns on its short-term surplus funds through efficient treasury operations.

With respect to treasury operations, special emphasis has been given to risk management. Introduction of customized software packages has facilitated speedy processing of information that would assist in taking a decision. The treasury office has put all the segments viz. Money Market, Foreign Exchange, Derivations Equity and Liquidity Management under one roof for better management of funds and enhanced customer service. The integrated IT platform has enabled IDBI to extend the services to more branches. IDBI's treasury successfully manages the liquidity requirements of the bank that helps to meet the requirement of maturing bonds as well as the other disbursements by using judicious mix of domestic and foreign currency liabilities. IDBI also uses financial instruments like Certificate of Deposits, Inter Bank borrowings, Bonds, Refinance from various institutions that have varying maturity period to manage the Asset-Liability mismatch as well as to meet the liquidity requirements. Treasury is invested in central and state government securities to progressively build the SLR portfolio for the bank. The SLR portfolio sometimes helps to manage the short-term liquidity mismatches. The return on large corpus is maximized through active treasury operations which involves both Indian currency and foreign exchange and also includes operating in derivations like interest rate swaps. The credibility of the operations has made IDBI the only financial institution in India to acquire an ISO certification for its treasury operations.

11. Insurance

The opening up of the insurance sector has expanded the horizon for the financial institutions as it has provided new opportunities for sourcing long-term finance. The IDBI has of late decided to enter into the insurance sector. For this purpose, it has collaborated with the Dutch Financial Services giant, ING group for insurance. The tie up is one of the biggest collaborations in insurance sector. The IDBI is the largest financial institution in India and ING group is one of the largest financial groups operating in the world. The IDBI-ING alliance will stretch to be life and general insurance areas. The IDBI will give foreign equity in the venture to ING as per prevalent insurance guidelines. The bank has also decided to add pension funds, while expanding the asset management/ mutual funds activities. With the entry into the insurance sector, IDBI will almost cover all the aspects that can be served by a financial institution.

Check Your Progress

1. Name some of the major TCOs operating in India.
2. When was the Industrial Development Bank of India (IDBI) established in India?
3. What are the merchant banking services offered by IDBI?
4. Mention any one significant contribution of IDBI.
5. When did merchant banking services begin in India?

5.4 ANSWERS TO CHECK YOUR PROGRESS QUESTIONS

1. Some of the major TCOs operating in India are the following:
   - APITCO Ltd. (Andhra Pradesh)
   - GITCO Ltd. (Gujarat)
   - HIMCON Ltd. (Himachal Pradesh)
   - ITCOT Consultancy and Services Ltd. (Tamil Nadu)
   - KITCO Ltd. (Kerala)

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2. The Industrial Development Bank of India (IDBI) was set-up in July 1964 as a wholly owned subsidiary of the Reserve Bank of India (RBI) as per the Industrial Development Bank of India Act, 1964.
3. The merchant banking services that IDBI provides include pre-project counselling, project appraisal, placement of equity with banks, foreign institutional investors, high net worth investors, mutual funds, institutional investors and private equity funds, placement of preference shares and debentures with domestic investors, structuring and syndication of bought out deals, loan syndication, syndication of structured debt instrument, co-ordinating the financial participation of multilateral agencies and international banks, issue management offering advice on the management of tender offer.
4. One of the most significant contribution of IDBI is the setting up of the stock Holding Corporation of India Ltd.(SHCIL) in 1987, providing custodial facilities and initiating the era of demat account.
5. It was only in 1967 that Grindlays Bank started merchant banking services in India.

5.5 SUMMARY

- Technical Consultancy Organizations (TCOs) were established to provide technical consultancy to the industrial outfits. These associations were set-up by the All India Financial Institutions (IDBI, ICICI, IFCI, and so forth) in alliance with the state level financial/development institutions and commercial banks. There are on the whole 18 state-level TCOs across India.
- The Industrial Development Bank of India (IDBI) was set-up in July 1964 as a wholly owned subsidiary of the Reserve Bank of India (RBI) as per the Industrial Development Bank of India Act, 1964.
- Direct financial assistance in the form of loans, shares-subscription, guarantees etc. is being provided by IDBI under the Direct Assistance Scheme.
- IDBI, right from its inception, has been continuously assisting the industry through a wide range of fee based financial products and advisory services like corporate advisory services, loan syndication, debenture trusteeship, forex services and so forth.
- State Bank of India, which incidentally is also the largest of all Indian banks, took the lead among Indian banks and is at present well-established in the merchant banking sector.

- Financial institutions like ICICI and Industrial Reconstruction Corporation of India (IRCI) are also into merchant banking operations and their main focus and attention is on mergers, amalgamations and takeovers.
- Once a specific project is decided upon by a client, the Merchant Banking Division makes a framework of the package to be provided. It includes all issues related to financial structuring and financing.
- An entrepreneur who has decided to set-up a new project needs to first obtain a Letter of Intent (LoI) from the Government of India which later gets converted into an Industrial Licence for the proposed project.
- Working capital is an integral part for running a business activity and the merchant bankers being a part of the banking system, are expected to assist to arrange for working capital finance especially for the new ventures.
- Project counselling is about confirming the feasibility and viability of the project. This is done on the basis of the technical appraisal, done with the help of the Technical and Industrial Consultancy Division.
- Various services that are offered by the merchant bankers that fall under the category of corporate advisory services include equity and business valuation; provide advice with respect to merger and acquisitions, business and financial restructuring, privatization and restructuring/rehabilitation of weak units.
- IDBI has also played a strategic role in diverse areas such as entrepreneurship development, capital markets and technology and consultancy services. It has also contributed towards balanced regional development.
- The opening up of the insurance sector has expanded the horizon for the financial institutions as it has provided new opportunities for sourcing long-term finance. The IDBI has of late decided to enter into the insurance sector.

5.6 KEY WORDS

- **Merchant Banking:** It involves the provision of banking services and consultancy to its customers regarding financial, marketing, managerial and legal services.
- **Issue Management:** It is the practice of managing problems, episodes and obstacles that might come in the way of a project, task or process.
- **Loan Syndication:** It is the process of involving a group of lenders in funding various portions of a loan for a single borrower.
- **Project Counselling:** It is about confirming the feasibility and viability of the project.

5.7 SELF ASSESSMENT QUESTIONS AND EXERCISES

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Short-Answer Questions

1. What are the major activities of Technical Consultancy Organizations?
2. Write a short note on the scope of Industrial Development Bank of India (IDBI).
3. What are the assistance schemes of IDBI?
4. Mention the portfolio management services provided by IDBI to NRIs.

Long-Answer Questions

1. Explain the fee-based services of IDBI.
2. Discuss the corporate advisory services provided by IDBI.
3. Examine the services provided by IDBI in the forex, treasury and insurance sectors of the country.

5.8 FURTHER READINGS

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UNIT 6 INDUSTRIAL CREDIT AND INVESTMENT CORPORATION OF INDIA (ICICI)

Structure

6.0 Introduction
6.1 Objectives
6.2 Introduction to ICICI
- 6.2.1 Objectives
- 6.2.2 Resources of the ICICI
- 6.2.3 Functions of the ICICI
- 6.2.4 Types of Financial Assistance Provided by the ICICI
- 6.2.5 Role of the ICICI
- 6.2.6 Activities of the ICICI Bank

6.3 Small Industries Development Bank of India (SIDBI): Forms of Assistance
- 6.3.1 Modes of Finance
- 6.3.2 Functions of SIDBI
- 6.3.3 Features of SIDBI
- 6.3.4 Benefits of Availing Loans From SIDBI
- 6.3.5 Loan Products Offered by SIDBI

6.4 Answers to Check Your Progress Questions
6.5 Summary
6.6 Key Words
6.7 Self Assessment Questions and Exercises
6.8 Further Readings

6.0 INTRODUCTION

The Industrial Credit and Investment Corporation of India (ICICI) was established in 1955 with sponsorship received from the World Bank. Its primary objective was to offer financial assistance to industrial enterprises. However, with the passage of time, it diversified its portfolio and expanded its scope.

Likewise, SIDBI is a financial institution aimed at developing and financing the micro, small and medium enterprise sector. It provides loan facility to small and industrial enterprises in India.

6.1 OBJECTIVES

After going through this unit, you will be able to:

- List the functions and objectives of the ICICI

- State the types of assistance offered by the ICICI
- Identify the main features of SIDBI
- Explain the loan products offered by SIDBI

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6.2 INTRODUCTION TO ICICI

The Industrial Credit and Investment Corporation of India (ICICI) was established under the Companies Act in the year 1955 as public limited company. It was set-up for the purpose of channelizing financial assistance to enterprises in the private sector. It gave impetus to the Indian capital market.

The market intermediaries like IFCI and SFCs confined themselves to the lending activity only and kept away from investing and underwriting in business. Further, they were not in a position to securitize the desired amount of loan assistance due to their low equity base. Therefore, the ICICI was established in 1955 to fill this gap and to overcome the market from liquidity crunch.

The following table illustrates the history of the journey of ICCI Bank from 1995 to 2013.

1995	The ICICI Bank founded in collaboration with the World Bank to extend financial support
1994	It started banking business in India.
1998	The ICICI Bank launched internet banking facility.
2000	The ICICI was the first Indian bank shortlisted on New York Stock Exchange.
2001	The ICICI Bank acquired the Madura bank.
2002	The regulators approved the reversed merger of ICICI company and ICCI Bank.
2003	It opened more branches in Canada, Singapore, UK, Dubai and Shanghai respectively.
2004	The new office in Bangladesh was opened.
2005	ICICI inaugurated the new branch in Dubai and Hong Kong.
2006	Bangkok, Jakarta and Kuala Lumpur representative offices were developed. Antwerp and Belgium are two branches that were developed by the ICICI Bank.
2007	The Sangli Bank was acquired by ICICI.
2008	It converts its New York office into an ICCI Bank.
2013	ICICI launched for the first time a mobile branch along with ATM in Maharashtra.

6.2.1 Objectives

The primary objectives of the ICICI are the following:

i. To extend facility for long-term and medium-term loans in Indian rupee and foreign currency.
ii. To underwrite issue of shares and debentures in the primary market.
iii. Providing technical and managerial services for industrial undertakings.
iv. Subscribing to new issues of shares and debentures.

6.2.2 Resources of the ICICI

The authorized capital was ₹ 50 crores divided into 50 lakh equity shares of ₹. 100/- each. Further, the paid-up capital was ₹. 40.49 crores. The ICICI reserves and surpluses was ₹. 92.25 crores. The total resources available for disposal were ₹. 1802 crores and the major portion of the resources was in the form of loans. In fact, ICICI funded almost 93 per cent of its total funds from borrowed sources. Bulk of the loan funds i.e., nearly 50 per cent was raised by floating bonds.

6.2.3 Functions of the ICICI

The significant functions of the ICICI are the following:

i. To providing long and medium-term loans in finance and equity participation.
ii. Sponsoring and underwriting issues of shares and other securities in primary market.
iii. Guaranteeing loan from other private investment sources.
iv. Ensuring funds availability for reinvestment by revolving investment.
v. Project advisory services i.e., offering advice –
    - to private sector companies in the pre-investment stages on government policies and procedures, feasibility studies and joint venture search, and
    - to Central and State Governments on specific policy related issues.

6.2.4 Types of Financial Assistance Provided by the ICICI

i. Underwriting of public issues and offer or sale of industrial securities.
ii. Direct subscription to public issue securities.
iii. Securing loans in rupees payable over periods up to 15 years.
iv. Providing similar loans in foreign currencies for payment of imported capital equipment and technical service.
v. Guaranteeing payments for credit made by others.

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vi. Providing credit facilities to manufacturers for promoting sale of industrial equipment on deferred payment terms.

vii. Providing financial services like leasing, installment sale and asset credit.

The ICICI also sells portfolio securities to the investors whenever reasonable price is available. It serves the purpose of revolving its resources for new investments and encourages the investment habit in others. Therefore, encouraging diversification in distribution of private industrial securities.

The ICICI also assisted industries in all sectors raging from the joint sector, the private sector, the public sector and the cooperative sector. But the private sector remained the major beneficiary. ICICI's assistance includes the foreign currency loans, Indian rupee loans, guarantees, and subscription of shares and debentures. The ICICI showed an increasing interest in the development of backward regions and new industries.

Important Assistance by the ICICI

- *Direct Financial Assistance to Industries:* The ICICI extends direct assistance in the form of underwriting, loans and direct subscription to shares and debentures and guarantees.
- *Indirect Financial Assistance to Industries:* Under this, assistance is given in form of industrial loans in refinancing, shares and bonds subscription of financial institution and rediscounting of bills and capital assistance.
- *Assistance to Backward Areas and Small-scale Industries:* The ICICI was backed by a mission from the World Bank with the objective of developing small and medium industries in the private sector in the country. In January 1955, this was registered under the Indian Companies Act and authorized with a capital of ₹. 60 crore and a subscribed capital of ₹. 22 crore. The issued capital of ICICI was subscribed by the Indian banks, insurance companies, individuals and corporation of the United States, the British eastern exchange banks and the general public in India.

6.2.5 Role of the ICICI

In 1973, the ICICI started a Merchant Banking Division for advising clients on a selective basis and allowed raising finances in suitable forms and restructuring of finances in the existing companies. It also extended services to clients on amalgamation proposals. The ICICI also extended assistance in preparing project proposals for submission to financial institutions and banks and for providing negotiation services on behalf of client for loans and underwriting. This division acts as managers to the issue of capital and also assisted for completion of formalities connected with the public issue and of legal formalities while raising loans.

The ICICI in 1982 gave a new dimension to its merchant banking division by offering counselling for industrial investment in India to non-resident Indians.

This proved not only the least expensive route for technological upgradation but also a source of foreign currency funds by way of risk capital.

It also set-up Venture Capital Funds for the promotion of Greenfield companies and risk capital investment and joined the other financial institutions in setting up SHCIL, CRISIL and OTC Exchange of India Ltd. It has also set-up its own bank and a mutual fund like the UTI.

The ICICI vision has been extending far beyond its immediate function of funding industrial projects. It has been looking at all sectors of the economy and wherever a need was perceived, has designed either a new concept or a new instrument, or even a new institution to cater to it. In this regard, its development activities have encompassed such diverse areas as technology, financing, project promotion, rural development, human resources development and publications.

It has set-up ICICI Brokerage Services Limited in March 1995. It is a 100 per cent subsidiary of I-SEC. It commenced its securities brokerage activities in 1996. It is registered with the National Stock Exchange of India Limited and the Mumbai Stock Exchange.

ICICI set-up ICICI Credit Corporation in 1997, which later got renamed as ICICI Personal Financial Services Limited in 1999. It offers a comprehensive range of goods and services to retail customers.

ICICI Capital Services Limited was originally set-up as SCICI Securities Limited as a wholly owned subsidiary of erstwhile SCICI Ltd. in 1994. Its objective was to provide stock broking services to the institutional clients and undertaking activities such as underwriting, primary market placements and distribution, industry and company research, etc. It became a wholly owned subsidiary of ICICI with effect from 1 April 1996.

ICICI established the ICICI bank for performing commercial banking functions in 1994. The bank offers a wide variety of domestic and international banking services.

The ICICI Bank got established in 1994 by the Industrial Credit and Investment Corporation of India, an Indian financial institution, as a wholly owned subsidiary. The parent company was formed in 1955 as a joint-venture of the World Bank, India's public-sector banks and public-sector insurance companies to provide project financing to the Indian industry. The bank was initially known as the Industrial Credit and Investment Corporation of India Bank, before it changed its name to the abbreviated ICICI Bank. The parent company was later merged into the ICICI Bank. ICICI Bank Limited is an Indian financial services company headquartered in Mumbai, Maharashtra. It is the second largest bank in India by assets and third largest by market capitalization. It offers a wide range of banking products and financial services to corporate and retail customers through a variety of delivery channels and through its specialized subsidiaries in the areas of investment banking, life and non-life insurance, venture capital and asset management.

6.2.6 Activities of the ICICI Bank

Let us briefly study the activities of the ICICI Bank.

i. Project Finance

Project finance is provided to industries for the cost of establishment, modernization or expansion of manufacturing and processing activities in the form of rupee and foreign loans, underwriting, subscription to shares and debentures and guarantees to supply of equipment and foreign donors.

The rupee loan is given for the purchase of equipment and machinery, construction and preliminary expenses. The foreign currency loans are provided for the purchase of imported capital equipment.

ii. Leasing

The leasing operations of the ICICI commenced in 1983. Leasing assistance is given for computerization, modernization/replacement, equipment of energy conservation, export orientation, pollution control etc.

iii. Project Advisory Services

The project advisory services are provided to the Central and State Governments and public sector and private sector companies. Advice to the governments is provided on policy reforms and on value chain analysis and to private sector companies on strategic management.

iv. Facilities for Non-resident Indians

The information regarding facilities and incentives given by the Government of India to the Non-Resident Indians for judicious investing in India are offered.

v. Provision of Foreign Currency Loans

The ICICI has a provision of foreign currency loans and advances to enable Indian Industrial concerns to secure essential capital goods from foreign countries.

vi. Other Institutions Promoted

- ICICI promoted the Housing Development Finance Corporation (HDFC) to provide long-term finance to individuals in middle- and lower-income groups, co-operations, etc., for the construction and purchase on ownership basis of residential houses all over the country.
- Credit Rating Information Services of India Ltd. (CRISIL) set-up by the ICICI in association with the Unit Trust of India (UTI) to provide credit rating services to the corporate sector.
- Technology Development and Information Company of India Ltd. (TDICI), promoted by ICICI, to finance the transfer and upgradation of technology and provide technology information.

- Programme for the Advancement of Commercial Technology (PACT) set-up with a grant of US $10 million provided by USAID (United States Aid) to assist market-oriented R&D activity, jointly undertaken by the Indian and US companies. The ICICI has been entrusted with the administration and management of PACT.
- Programme for Acceleration of Commercial Energy Research (PACER) funded by USAID with a grant of US $ 20 million which supports research and technology development proposals in Indian energy sector.

6.3 SMALL INDUSTRIES DEVELOPMENT BANK OF INDIA (SIDBI) : FORMS OF ASSISTANCE

The SIDBI a wholly owned subsidiary of Industrial Development Bank of India (IDBI) was established in 1988 and started its operations on 2nd April 1990. Further, it also started administering Small Industries Development Fund and National Equity Fund which were earlier administered by IDBI. It is the principal financial institution for the promotion, financing and development of the Micro, Small and Medium Enterprise (MSME) sector. It is consists of a team of 10 Board of Directors and the authorized capital of the Bank is ₹. 1000 crore and the paid-up capital is ₹. 531.92 crore as on 31.03.2019.

SIDBI Associates

i. Credit Guarantee Fund Trust for Micro and Small Enterprises (CGTMSE)
ii. India SME Technology Services Ltd. (ISTSL)
iii. SME Rating Agency of India Ltd. (SMERA)
iv. India SME Asset Reconstruction Company Ltd
v. SIDBI Trustee Company Limited (STCL)
vi. Receivables Exchange of India Ltd (RXIL)

SIDBI Subsidiaries

i. SIDBI Venture Capital Limited (SVCL)
ii. Micro Units Development & Refinance Agency Ltd (MUDRA)

6.3.1 Modes of Finance

SIDBI provides direct, indirect and micro finance facilities.

i. **Direct Finance:** In the form of Term Loan Assistance, Working Capital Assistance, Support against Receivables, Foreign Currency Loan, Scheme of Energy Saving for MSME sector, equity support etc.

ii. **Indirect Finance:** The Indirect assistance in the form of refinance is provided to Primary Lending Institutions (PLIs), comprising banks, State Level

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Financial Institutions, etc., having a wide network of branches across the country. The main objective of the Refinance Scheme is to increase the resource position of PLIs which would ultimately facilitate the flow of credit to MSME sector.

iii. **Micro Finance:** SIDBI provides micro finance i.e., credit to small entrepreneurs and businessmen for establishing their business.

6.3.2 Functions of SIDBI

Let us briefly study the primary functions of SIDBI.

i. SIDBI refinances loans extended by the primary lending institutions to small scale industrial units, and also provides resources support to them.

ii. SIDBI discounts and rediscounts bills arising from sale of machinery to or manufactured by industrial units in the small scale sector.

iii. To expand the channels for marketing the products of Small Scale Industries (SSI) sector in domestic and international markets.

iv. It provides services like leasing, factoring etc. to industrial concerns in the small scale sector.

v. To promote employment-oriented industries especially in semi-urban areas to create more employment opportunities and thereby checking migration of people to urban areas.

vi. To initiate steps for technological upgradation and modernization of existing units.

vii. SIDBI facilitates timely flow of credit for both term loans and working capital to SSI in collaboration with commercial banks.

viii. SIDBI Co-promotes state level venture funds in association with THE respective state government.

ix. It grants direct assistance and refinance loans extended by primary lending institutions for financing exports of products manufactured by small scale units.

6.3.3 Features of SIDBI

- SIDBI provides refinance support to Small-Scale Industries (SSIs).
- It provides funding support to the MSME sector.
- It helps in discounting the bills of Small-Scale Industries.
- It provides refinance to financial institutions, including banks, NBFCs and Small Finance Companies.
- It offers financial services, such as hire purchase, factoring and leasing services.

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- It promotes employment opportunities among SSIs.
- It provides assistance to exports.
- It offers bank loans to women and underprivileged sections of the society.

6.3.4 Benefits of Availing Loans from SIDBI

The significant benefits of availing loans from SIDBI are the following:

i. Reasonable interest rates
ii. Credit and loans customization
iii. Collateral free loans
iv. Customize funding for MSMEs
v. Provide subsidies for various schemes
vi. Transparent funding process
vii. Ensure capital growth for business owners
viii. Assistance and advice provided by relationship managers

6.3.5 Loan Products Offered by SIDBI

The various prominent loan products offered by SIDBI are the following:

1. **SMILE (SIDBI Make in India Soft Loan Fund for MSME):** This emphasized on the covering of financial requirements for new enterprises which are in the manufacturing or in the services sector. The loan amount offered under this scheme is minimum ₹. 10 lakh for equipment finance and ₹. 25 lakh for other purposes. Repayment tenure is maximum up to 10 years, including moratorium period of up to 36 months.
2. **SMILE Equipment Finance (SEF):** SEF has a simplified application format with competitive interest rate. MSME entities those wish to purchase any new equipment or need financing for the same are covered under this loan scheme. Repayment period is of 72 months and the loan amount starts from ₹. 10 lakh.
3. **Loans under Partnership with OEM (Original Equipment Manufacturer):** This loan scheme is helpful for MSMEs that can purchase machines from OEMs. Minimum 3 years of business existence is required and the repayment period is of 60 months. Loan amount offered for a maximum amount of ₹. 1 crore.
4. **Working Capital (Cash Credit):** Under this scheme, it ensures the working capital availability for MSME units. Working Capital offers seamless approvals, as per the loan applicant's requirement.
5. **SIDBI Trader Finance Scheme (STFS):** This loan scheme is for MSME Retails/Wholesalers who are in existence for at least 3 years with a satisfactory financial position. The minimum loan amount offered is ₹. 10

lakh and maximum up to ₹. 1 crore. However, the repayment period shall depend on the cash flow and size of business. However, the repayment tenure is maximum up to 60 months.

6. **Loan for Purchase of Equipment for Enterprise's Development (SPEED):** Under this scheme, SIDBI offers 100 per cent financing with loan amount up to ₹. 1 crore for New to Bank and ₹. 2 crore for existing customers. Minimum 3 years of operations are required to get this loan wherein the repayment period is 2 to 5 years, including Moratorium period of 3-6 months. Borrowers can avail this loan at an interest rate of 9.25 per cent to 10 per cent per annum.

Check Your Progress

1. When was the Industrial Credit and Investment Corporation of India (ICICI) established in India?
2. In which year did the ICICI began its Merchant Banking Division?
3. When was SIDBI established in India?
4. List the essential features of SIDBI.

6.4 ANSWERS TO CHECK YOUR PROGRESS QUESTIONS

1. The Industrial Credit and Investment Corporation of India (ICICI) was established in India in the year 1955.
2. In 1973, the ICICI started a Merchant Banking Division for advising clients on a selective basis and allowed raising finances in suitable forms and restructuring of finances in the existing companies.
3. The SIDBI a wholly owned subsidiary of Industrial Development Bank of India (IDBI) was established in 1988 and started its operations on 2nd April 1990.
4. The essential features of SIDBI are the following:
   - SIDBI provides refinance support to Small-Scale Industries (SSIs).
   - It provides funding support to the MSME sector.
   - It helps in discounting the bills of Small-Scale Industries.
   - It provides refinance to financial institutions, including banks, NBFCs and Small Finance Companies.
   - It offers financial services, such as hire purchase, factoring and leasing services.
   - It promotes employment opportunities among SSIs.

- It provides assistance to exports.
- It offers bank loans to women and underprivileged sections of the society.

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6.5 SUMMARY

- The Industrial Credit and Investment Corporation of India (ICICI) was established under the Companies Act in the year 1955 as public limited company.
- The market intermediaries like IFCI and SFCs confined themselves to the lending activity only and kept away from investing and underwriting in business.
- The ICICI also sells portfolio securities to the investors whenever reasonable price is available. It serves the purpose of revolving its resources for new investments and encourages the investment habit in others. Therefore, encouraging diversification in distribution of private industrial securities.
- In 1973, the ICICI started a Merchant Banking Division for advising clients on a selective basis and allowed raising finances in suitable forms and restructuring of finances in the existing companies. It also extended services to clients on amalgamation proposals.
- It has set-up ICICI Brokerage Services Limited in March 1995. It is a 100 per cent subsidiary of I-SEC. It commenced its securities brokerage activities in 1996. It is registered with the National Stock Exchange of India Limited and the Mumbai Stock Exchange.
- ICICI established the ICICI bank for performing commercial banking functions in 1994. The bank offers a wide variety of domestic and international banking services.
- The leasing operations of the ICICI commenced in 1983. Leasing assistance is given for computerization, modernization/replacement, equipment of energy conservation, export orientation, pollution control etc.
- The SIDBI a wholly owned subsidiary of Industrial Development Bank of India (IDBI) was established in 1988 and started its operations on 2nd April 1990.
- Under this scheme, it ensures the working capital availability for MSME units. Working Capital offers seamless approvals, as per the loan applicant's requirement.

6.6 KEY WORDS

- **Floating Bonds:** It is a bond with a variable interest rate.
- **Leasing:** It is a process by which a company can obtain the use of certain fixed assets for which it must pay a series of periodic tax deductible payments.

- **Microfinance:** It is a category of financial services targeting individuals and small enterprises that lack access to conventional banking and related services.

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6.7 SELF ASSESSMENT QUESTIONS AND EXERCISES

Short-Answer Questions

1. Mention the primary objectives and functions of the ICICI.
2. What is the type of financial assistance provided by the ICICI?
3. Write a short note on the role of the ICICI.
4. Briefly mention the modes of finance provided by SIDBI.

Long-Answer Questions

1. Discuss the activities of the ICICI Bank.
2. Explain the functions of SIDBI.
3. Examine the loan products offered by SIDBI.

6.8 FURTHER READINGS

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UNIT 7 NATIONAL SMALL INDUSTRIES CORPORATION (NSIC)

NOTES

Structure

7.0 Introduction
7.1 Unit Objectives
7.2 Introduction to NSIC
7.2.1 Organizational Set-Up
7.2.2 Vision and Mission of NSIC
7.3 Forms of Assistance
7.3.1 Marketing Support
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7.4.1 Role and Responsibility of NSIC
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7.6 Answers to Check Your Progress Questions
7.7 Summary
7.8 Key Words
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7.10 Further Readings

7.0 INTRODUCTION

The National Small Industries Corporation Ltd. (NSIC) is an ISO 9000 certified Government Enterprise under Micro, Small and Medium Enterprises. Its primary objective is to promote, aid and foster growth of small-scale industries and industry related to small-scale services/businesses in the country. NSIC came into existence in the year 1955.

7.1 UNIT OBJECTIVES

After going through this unit, you will be able to:

- Explain the organizational set-up of NSIC
- State the primary functions of NSIC
- Discuss the forms of assistance provided by NSIC
- List the steps involved in NSIC registration procedure

7.2 INTRODUCTION TO NSIC

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NSIC has a strong network of Technical Centres and offices through which it operates across the entire nation. NSIC, apart from India, has its footprint in the Gulf and selective African countries, whose affairs are managed from Dubai and Johannesburg, South Africa respectively. Additionally, the National Small Industries Corporation has also set-up Training cum Incubation Centres that are operated by highly trained professionals.

During the six decades of its existence, NSIC has left an overwhelming impact by promoting modernization, assisting in upgradation of technology, ushering in quality consciousness, strengthening linkages with large and medium enterprises and increasing export projects and products from small-scale enterprises.

Presently, the NSIC is operating through 9 Zonal Offices, 33 Branch Offices,15 Sub-offices, 10 NSIC Business Development Extension Offices, 5 Technical Services Centres, 3 Extension Centres and 2 Software Technology Parks supported by a team of over 5000 professionals spread across the country. Its overseas centres in the Gulf countries and African countries are managed from offices in Dubai and Johannesburg.

7.2.1 Organizational Set-Up

The policy guidelines to the NSIC are provided by the Board of Directors consisting of a full-time Chairman-cum-Managing Director, two Functional Directors, two Government Nominee Directors, one SIDBI Nominee Director, and six Non-official part-time Directors. The Corporation is manned by the dedicated team of professionals at different levels.

7.2.2 Vision and Mission of NSIC

Vision

To become a leading organization fostering the growth of MSMEs Sector in India.

Mission

To support and promote MSMEs Sector by providing combined support services for Finance, Marketing, Technology and other Allied Services.

7.3 FORMS OF ASSISTANCE

The National Small Industries Corporation facilitates MSMEs with customized schemes that build and boost their competitiveness. The National Small Industries Corporation provides complete integrated services under Finance, Marketing, Technology and other allied Support services.

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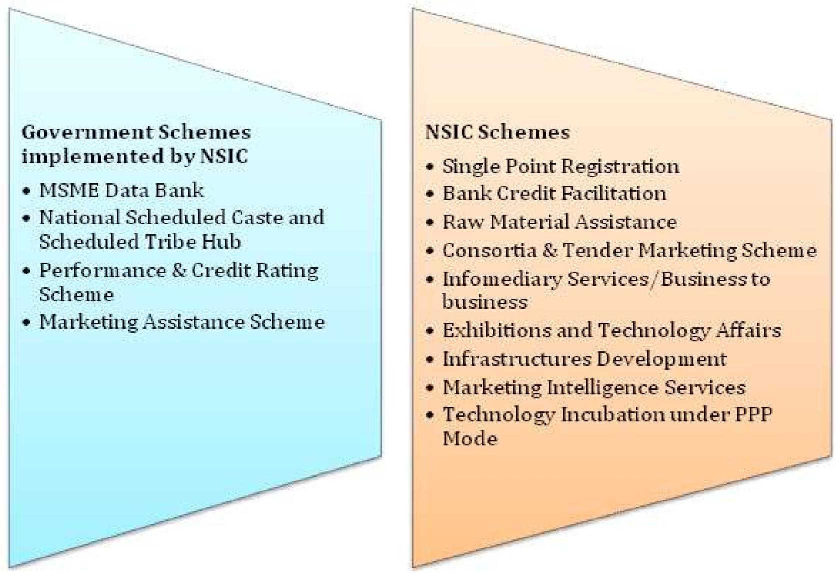

Schemes of the National Small Industries Corporation

Various schemes initiated by NSIC that can be broadly segregated under the categories like marketing support, credit support, credit rating and technical support are the following:

- Marketing Intelligence Services
- Performance and Credit Rating Scheme
- Raw Material Assistance
- Consortia & Tender Marketing Scheme
- Single Point Registration Scheme
- Credit Facilitation through Bank, etc.

7.3.1 Marketing Support

One of the most significant contributors towards the growth of a business is a strong marketing support. Micro, Small and Medium Enterprises today need robust marketing intervention to survive in the intensely competitive market. The National Small Industries Corporation has devised numerous marketing support schemes that supports MSMEs, both in domestic and foreign markets.

These various supportive schemes formulated and exercised are briefly described as follows:

- **Consortia and Tender Marketing**

Micro and Small Enterprises have to encounter and overcome several bottlenecks to get and deliver large orders. The difference in the size and capacity creates a discriminatory situation against the large enterprises that result in the MSMEs losing ground and eventually thrown out of the competition. The National Small Industries

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Corporation creates a consortium that houses number of MSMEs manufacturing same or similar product or products that enable to combine their capacity and size.

On applying and securing orders against tenders, the National Small Industries Corporation acts on behalf of a single Micro and Small Enterprise/ Consortia of Micro and Small Enterprises. Once allotted, these orders are dispensed amongst Micro and Small Enterprises as per their production capacity.

- **Marketing Intelligence**

Access to marketing information and related database is of high relevance to survive the competitive storm. Hence, both dissemination and collection of both international as well as domestic marketing intelligence becomes very important for the survival of Micro and Small Enterprises. NSICs Marketing Intelligence cell, not only spreads awareness about several schemes for MSMEs but also maintains a database in detail and provides information.

- **Exhibitions and Technology Fairs**

National and international trade fairs are a good platform to showcase the core competencies of the Indian Micro and Small Enterprises. Participation in these trade fairs provides an opportunity to identify and explore market opportunities. The National Small Industries Corporation facilitates MSEs to participate in these fairs by offering concessions in rental etc. Through the participation in these national and international events, the Micro and Small Enterprises get exposed to international practices which help them to improve their business competencies and prowess.

- **Single Point Registration Scheme**

The government is the largest purchaser of a variety of goods of the small-scale sector. Therefore, the general purpose of this scheme is to increase the share of purchase from the small-scale industries under the Government Stores Purchase Programme, launched in 1955-56. These industries can participate in these purchase programmes by registering under the NSIC through the Single Point Registration Scheme (SPRS).

7.3.2 Credit Support

The National Small Industries Corporation enables credit requirements of MSEs in the following areas:

- **Financing for Raw Material Procurement**

The National Small Industries Corporation has formulated a scheme for assistance in procurement of raw material by the MSEs. The assistance is provided by financing the procurement of raw material (both indigenous and imported). The salient features of the said scheme are as follows:

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i. Purchasing basic raw materials in bulk quantities at competitive rates.
ii. Financial assistance for raw materials procurement up to 90 days.
iii. Facilitating the import of scarce raw materials.
iv. The National Small Industries Corporation supports the documentation and procedural aspects as well as issuance of a letter of credit in case of imports.

- **Financing for Marketing Activities**

The National Small Industries Corporation provides financial assistance for marketing actives such as Exports, Internal Marketing and Bill Discounting.

- **Finance through Syndication with Banks**

NSIC has entered into a strategic alliance with a handful of commercial banks and financial institutions to ensure smooth flow of credit to MSMEs. The flow of credit is maintained by providing working capital/ long-term financing of the MSEs across the country. The National Small Industries Corporation forwards the loan application of the interested MSMEs and also shares a portion of the processing fee.

7.3.3 Credit Rating Scheme and Performance for Small Industries

The Union Budget of 2004-05 highlighted the need for a Credit Rating Mechanism and Performance appraisal for MSMEs. This led to a scheme related to the rating of MSEs that was drafted in consultation with the Rating Agencies and IBA (Indian Banks' Association). The National Small Industries Corporation acts as the nodal agency for implementation of this scheme through empanelled agencies.

Benefits of Performance and Credit Rating

The following benefits are been derived by the MSEs whose performance is rated by the credit rating agencies:

i. It makes possible easy availability of credit at attractive interest rates.
ii. It gives the MSEs access to an independent third party opinion on credit-worthiness and capabilities of Micro and Small Enterprises.
iii. It sanctions credit from Banks and Financial Institutions with promptness.
iv. It gets recognized on the global platform.
v. The ratings act as a ready reckoner for the buyers/vendors in capacity and capability assessment of MSMEs.
vi. It reduces the rating fee structure for Micro and Small Enterprises
vii. It enables MSMEs to make a SWOT analysis and subsequently take corrective measures.

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7.3.4 Technology Support

The Technical Services Centres of NSIC offers the following support services to the small enterprises:

i. Testing of raw materials in accredited laboratories.
ii. Provides advice on the usage of new technology and techniques.
iii. Common facility support in machining, EDM, CNC, etc.
iv. Product designing including CAD.
v. Provides energy and environment services at selected centres.
vi. Conducts workshops to impart practical training for skill upgradation.

7.4 FUNCTIONS OF NSIC

NSIC provides a wide array of services, mostly promotional in character, to small-scale industries.

Its main functions are related to:

i. It makes machinery available to small-scale industries on hire-purchase.
ii. It provides equipment leasing facility.
iii. It provides assistance in export marketing of the products of small-scale industries.
iv. It provides assistance in procurement of materials by participating in the bulk purchase programme of the government.
v. It develops the prototype on behalf of the MSEs and later pass on to them for commercial production.

In addition to the above, many schemes like National Scheduled Caste and Scheduled Tribe Hub, MSME databank, and organizing exhibitions for promoting the marginalized sections of the society and small-scale and associated sector in India are also formulated and put into practice by NSIC.

7.4.1 Role and Responsibility of NSIC

The National Small Industries Corporation (NSIC) came into existence in the year 1955 as a central government undertaking. It focuses on the fulfilment of the requirement of machinery and equipment to support the small entrepreneurs. The biggest bottleneck that the entrepreneurs face is the lack of availability of funds required to be invested in acquiring equipment and machinery. It is observed that many a times, the non-availability of funds deprives many small yet budding entrepreneurs to realise their dreams.

NSIC was set up to cater to this need of the entrepreneur. Under a scheme, an entrepreneur may be provided indigenous as well as imported equipment, plant, and machinery on a hire-purchase basis. However, the hire-purchase scheme is not applicable to second-hand machinery and machinery costing less than ₹ 1000. Being a registered member of NSIC makes it easy for the entrepreneurs to bag government orders.

New entrepreneurs, units of scheduled castes, scheduled tribes, and persons with disabilities, ex-servicemen, and women are given special preferences and incentives. However, in the case of machinery imports, an entrepreneur has to secure a license from the government.

Since its inception, NSIC has been overtly successful in its role of promoting modernization, upgrading technology, quality consciousness, strengthening linkages with large and medium enterprises, and enhancing export projects and products from small-scale enterprises.

7.4.2 NSIC Registration

The MSMEs and small entrepreneurs are expected to reap numerous benefits by getting them registered with NSIC.

Advantages of NSIC Registration

The Benefits of NSIC Registration under the Single Point Registration Scheme are as follows:

- Becomes eligible to enjoy certain benefits in Tender Participation
- Procurement from Micro and Small Enterprises
- Exemption from Earnest Money Deposit (EMD)
- Do not have to pay for the tender set
- Get access to 358 items that are reserved to be purchased exclusively from the MSMEs.

Documents to be furnished for NSIC Registration

The following documents in duplicate (duly self-attested) are to be submitted in order to get registered with NSIC:

- Self-declaration regarding entry in MSME Data Bank
- A Self-attested copy of PAN, Udyog Adhaar Memorandum (UAM) Number {Entrepreneur's Memorandum (EM) Part-II (optional)}
- Proof of ownership of Plant & Machinery/ Equipment & Tools and Raw Material showing the date/ year of purchase & Original Purchase value of individual machinery (as per Annexure 'B').
- The Performance Statement, according to the Performa Annexure-F of the application.
- A Self-attested copy of documents of ownership of the premises or copy of the lease deed.

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- Certificate from the Proprietor/ Partner/ Directors even if they do not have any link with large scale Unit(s).

In addition to the above, the following documents/ statements must be furnished, duly signed by the authorized person;

- A List of technical personnel employed in production and services.
- A brief on quality control measures carried out to ensure the quality of raw material and finished products.
- A List of testing facilities and quality control equipment available with the firm.
- A test report from an independent lab, where applicable as per the required standards.
- A copy of the latest electricity bill.
- Audited Balance Sheet, Profit & Loss Account and Trading Account of the last 3 years duly signed by the authorized person under his seal.
- A Statement or Declaration showcasing the Results of Operation for the last 3 years signed by an authorized person under his seal (as per the Annexure 'C').
- Bankers' Report showcasing the details of the financial status of the applicant firm as per Performa (Draft at Annexure 'E').
- Copy of PAN.

Fees distribution for obtaining NSIC Registration

The total fee for NSIC registration is commensurate to the turnover of the business as per the latest audited financial statements.

Fee for NSIC registration can be divided into three parts namely, registration fees, inspection charges and professional fees.

Registration Fee

The National Small Industries Corporation charges the following fee for new registration based on turnover and MSME classification:

Turnover less than ₹1 Crore	₹3000 for Micro enterprises having a turnover of less than ₹1 crore.- ₹5000 for Small enterprises having a turnover of less than ₹1 crore
More than ₹1 Crore turnover	₹3000 plus ₹1500 for each crore of additional turnover for Micro enterprises.- ₹5000 plus ₹2000 for each additional crore for Small enterprises having a turnover of under ₹1 crore

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There is a maximum cap of ₹ 1 lakh as Registration fee.

Inspection Charges

Micro-enterprises have to pay ₹2000 and small-enterprises have to pay ₹3000 as inspection charges, which is in addition to the registration charges.

Professional Fee

Professional fees to the tune of ₹6000 for micro-enterprises and ₹ 8000 for small enterpriseshave to be paid to RITES Limited and the Consultancy Development Centre for conducting a physical inspection.

Eligibility for NSIC Registration

Everybody who wishes to register his/ her enterprise under the NSIC needs to satisfy the following criteria:

- Every Micro and Small Enterprises (MSEs) having Udyog Aadhaar Memorandum (UAM) or EM-Part II (Optional) can obtain NSIC registration under the Single Point Registration Scheme (SPRS).
- Whereas, MSEs already involved in production but have not accomplished one year of existence may get the Provisional Registration Certificate under NSIC's Single Point Registration Scheme. It is issued with the monitory limit of ₹ 5 lakh which stands valid for one year from the date of issuance.

Validity of NSIC Registration

Any NSIC registration that is issued under the Single Point Registration Scheme, 2003 to the Micro and Small Enterprises (MSEs) is valid for two years. However, the concerned firm is needed to review and renew it every two years.

On the other hand, the provisional registration certificate provided to MSEs under SPRS with a monetary limit of ₹ 5 lakhs is valid only for one year.

NSIC Registration procedure

You may obtain the NSIC registration both online or offline. For the online registration of NSIC, you can follow the steps given below:

- Stage 1: Visit the official portal of National Small Industries Corporation.
- Stage 2: On the home page of National Small Industries Corporation, click on the option 'Apply Online' given on the left side of the page.
- Stage 3: A new page will appear where you have to fill the details of your company.
- Stage 4: Once you have filled up the form completely, click on 'Register'.
- Stage 5: Then, you have to pay the recommended NSIC registration fees.

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- Stage 6: Furthermore, the NSIC will send a duplicate copy of the documents and application to the concerning inspecting agency for the technical inspection.
- Stage 7: Once the technical report comes, the NSIC issues the license.

7.5 NSIC TRAINING AND INCUBATION CENTRE (PUBLIC-PRIVATE PARTNERSHIP PPP MODE)

With an intention to achieve the objective of reaching out to entrepreneurs from every corner of the country, NSIC decided to forge a partnership with the private players so that the cost can be minimized. Under this concept, NSIC invited partners who would associate themselves with NSIC to offer various courses. Players possessing experience of the education sector were selected to be a part of the franchise to ensure services offered in the incubation centres are of high standards. The incubation centres were given autonomy faculty selection and hiring, promotion of the courses and admission procedure. The mandatory resource requirements to run each course were clearly described and were strictly adhered to by each private player who is a part of the franchise.To be a part of the franchise; the partners need to deposit an amount of ₹ 25,000 per course in addition to three months of the operating expenses as a security to NSIC.

An online platform has been developed where all the details are to be uploaded by the training partners. To expand the network and make more partners get associated, NSIC also supports its partners to arrange finances. A portion of the promotional expenses of the partner is also shared by NSIC, on the condition that the promotional material bears NSIC's logo. The promotional material is required to be approved by NSIC before printing. As per the policy, NSIC will bear the office expense and the fees to be charged by the partners will be decided by NSIC. Out of the total fees, 15 per cent goes to NSIC as affiliation fees.

Check Your Progress

1. In which year was the National Small Industries Corporation (NSIC) established in India?
2. What are the main functions of NSIC?
3. List the benefits of NSIC Registration under the Single Point Registration Scheme.

7.6 ANSWERS TO CHECK YOUR PROGRESS QUESTIONS

1. The National Small Industries Corporation (NSIC) was established in India in the year 1955.

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2. The main functions of NSIC are the following:
   i. It makes machinery available to small-scale industries on hire-purchase.
   ii. It provides equipment leasing facility.
   iii. It provides assistance in export marketing of the products of small-scale industries.
   iv. It provides assistance in procurement of materials by participating in the bulk purchase programme of the government.
   v. It develops the prototype on behalf of the MSEs and later pass on to them for commercial production.
3. The benefits of NSIC Registration under the Single Point Registration Scheme are as follows:
   - Becomes eligible to enjoy certain benefits in Tender Participation
   - Procurement from Micro and Small Enterprises
   - Exemption from Earnest Money Deposit (EMD)
   - Do not have to pay for the tender set
   - Get access to 358 items that are reserved to be purchased exclusively from the MSMEs.

7.7 SUMMARY

- The National Small Industries Corporation Ltd. (NSIC) is an ISO 9000 certified Government Enterprise under Micro, Small and Medium Enterprises.
- NSIC has a strong network of Technical Centres and offices through which it operates across the entire nation.
- Presently, the NSIC is operating through 9 Zonal Offices, 33 Branch Offices,15 Sub-offices, 10 NSIC Business Development Extension Offices, 5 Technical Services Centres, 3 Extension Centres and 2 Software Technology Parks supported by a team of over 5000 professionals spread across the country.
- The National Small Industries Corporation facilitates MSMEs with customized schemes that build and boost their competitiveness. The National Small Industries Corporation provides complete integrated services under Finance, Marketing, Technology and other allied Support services.
- Small and Medium Enterprises today need robust marketing intervention to survive in the intensely competitive market.
- Access to marketing information and related database is of high relevance to survive the competitive storm.

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- The National Small Industries Corporation has formulated a scheme for assistance in procurement of raw material by the MSEs.
- NSIC has entered into a strategic alliance with a handful of commercial banks and financial institutions to ensure smooth flow of credit to MSMEs.
- The National Small Industries Corporation (NSIC) came into existence in the year 1955 as a central government undertaking.
- New entrepreneurs, units of scheduled castes, scheduled tribes, and persons with disabilities, ex-servicemen, and women are given special preferences and incentives.
- The MSMEs and small entrepreneurs are expected to reap numerous benefits by getting them registered with NSIC.
- The total fee for NSIC registration is commensurate to the turnover of the business as per the latest audited financial statements.
- Any NSIC registration that is issued under the Single Point Registration Scheme, 2003 to the Micro and Small Enterprises (MSEs) is valid for two years. However, the concerned firm is needed to review and renew it every two years.

7.8 KEY WORDS

- **Syndication:** It is a temporary coalition formed by professionals to handle a large transaction that would be extremely difficult to execute individually.
- **CAD:** It is an important industry within the tech world. It involves using computers to help with engineering and design for a wide range of projects.
- **Incubation Centre:** These are centres where transitory and facilitative assistance is given to small enterprises or start-ups.

7.9 SELF ASSESSMENT QUESTIONS AND EXERCISES

Short-Answer Questions

1. Write a short note on the organizational set-up of NSIC.
2. Mention the support services offered by the Technical Services Centres of NSIC.
3. What are the advantages of NSIC registration?
4. Briefly mention the NSIC Training and Incubation Centre.

Long-Answer Questions

1. Discuss the various schemes of NSIC.
2. Examine the role and responsibility of NSIC.
3. Explain the registration procedure of NSIC.

NOTES

7.10 FURTHER READINGS

Desai, Vasant. 2011. *Development Banking in India, Vol. I & II*. India: Himalaya Publishing House.

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UNIT 8 STATE FINANCE CORPORATIONS (SFCs)

Structure

8.0 Introduction
8.1 Unit Objectives
8.2 Capital Structure of the State Finance Corporation
  8.2.1 Organization and Management
  8.2.2 SFCs in India
  8.2.3 The SFCs Establishment in States
  8.2.4 Objectives of State Finance Corporations
  8.2.5 Functions
  8.2.6 Forms of Assistances
  8.2.7 Problems of the State Corporations
  8.2.8 Suggestions for the Improvement of Working of SFCs
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8.7 Further Readings

8.0 INTRODUCTION

The State Finance Corporations (SFCs) have a very important role to play in the economic growth of a country. They have contributed in the development of the institutional finance structure in India. SEC extends support and also promotes small and medium industries located in various states of the country. In addition to the above, SFCs also focus to boost and ensure balanced regional development, generating more employment through increased investment and broad base ownership of industries across the states.

As of now, there are 18 State Finance Corporations (out of which 17 SFCs were established under the State Financial Corporation Act, 1951). Besides, Tamil Nadu Industrial Investment Corporation Ltd. established in 1949, is also working in the capacity of a State Finance Corporation.

8.1 UNIT OBJECTIVES

After going through this unit, you will be able to:

- State the objectives and functions of SFCs established in India
- Identify the problems faced by SFCs in India
- List the major SFCs operational in India

8.2 CAPITAL STRUCTURE OF THE STATE FINANCE CORPORATION

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The maximum authorised capital of a SFC is ₹ 5 crores and the general public is also eligible and can become a shareholder of the State Finance Corporations. To entice the potential shareholders, respective State Governments associated with a SFC offer a guaranteed dividend of 3.5 per cent on the share capital, with a cap that it cannot exceed 5 per cent on the share capital. The SFCs are allowed to enhance their financial resources through floating bonds and debentures. The SFCs used this leverage and by March 1974, they had issued bonds amounting to ₹ 116 crores. The corporations hold the right to borrow from the Reserve Bank of India as well as from the concerned State Governments.

8.2.1 Organization and Management

The Board consists of 10 Directors vested with the powers to run the corporation. In addition, the State Government appoints the Managing Director generally in consultation with the RBI and also nominates three other directors. Out of the ten directors, three are appointed by the scheduled banks, investment trusts, insurance companies, co-operative banks and other financial institutions. Therefore, almost all the directors are nominated by the government and quasi-government institutions.

8.2.2 SFCs in India

The SFCs contribute in the development of Small, Medium and Micro Enterprises in their respective States. The financial assistance from the SFCs is provided in the form of direct subscription to debentures/equity, term loans, discounting of bills of exchange, guarantees, & seed/ special capital, etc. The very purpose of setting up SFCs is to give stimulus to higher investment, creating more employment and also extending the ownership base of industries. Moreover, SFC's dole out whole-hearted support to innovative businesses like tissue culture, floriculture, poultry farming, and services related to engineering, marketing and commercial complexes.

The 18 State Financial Corporations (SFCs) that are operating in the country are the following:

- Andhra Pradesh State Financial Corporation (APSFC)
- Himachal Pradesh Financial Corporation (HPFC)
- Madhya Pradesh Financial Corporation (MPFC)
- North Eastern Development Finance Corporation (NEDFI)
- Rajasthan Finance Corporation (RFC)
- Tamil Nadu Industrial Investment Corporation Limited(TIIC)
- Uttar Pradesh Financial Corporation (UPFC)

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- Delhi Financial Corporation (DFC)
- Gujarat State Financial Corporation (GSFC)
- The Economic Development Corporation of Goa (EDC)
- Haryana Financial Corporation (HFC)
- Jammu & Kashmir State Financial Corporation (JKSFC)
- Karnataka State Financial Corporation (KSFC)
- Kerala Financial Corporation (KFC)
- Maharashtra State Financial Corporation (MSFC)
- Odisha State Financial Corporation (OSFC)
- Punjab Financial Corporation (PFC)
- West Bengal Financial Corporation (WBFC)Andhra Pradesh State Financial Corporation (APSFC)

8.2.3 The SFCs Establishment in States

- **Andhra Pradesh State Financial Corporation (APSFC)** was incorporated in 1956 to promote SMEs in Andhra Pradesh under the provisions of the Sate Financial Corporation' Act, 1951. To its credit, APSFC introduced many entrepreneur-friendly schemes which provide support and thrust through long-term working capital loans and seed capital support depending upon the needs of various categories of entrepreneurs. This Corporation has over 45 years of experience and expertise in industrial financing to the tiny, small and medium scale industries. The financial assistance provided to such sectors has resulted in balanced regional development of the state.
- **Arunachal Pradesh Industrial Development and Financial Corporation (APIDFC):** Comparatively new, the APIDFC was incorporated in the year 1978 as a company under the Companies Act, 1956 for promotion of industries in Arunachal Pradesh. It actually performs the dual role of State Industrial Development Corporation and State Financial Corporation.
- **Assam Financial Corporation (AFC)** took shape as a Joint State Financial Corporation under Section 3(A) of the SFC Act 1951 in 1954 and apart from covering the erstwhile-undivided Assam; it also has the additional responsibility of Manipur and Tripura. Operating for over five decades, AFC, as the premier most Financial Institution in the North-East Region, has extensive outreach at the grassroots level and is more approachable compared to other Financial Institutions (FIs) and banks operating in the region.
- **Bihar State Financial Corporation (BSFC)** came into existence in the year 1954 under SFC Act, 1951 to encourage small time industrialists,

businessmen and entrepreneurs to set-up small and medium scale industries by providing support and financial assistance. Even though it was incorporated in erstwhile Bihar, currently it is in charge of both Bihar and Jharkhand and is dedicated to the upliftment of SMEs in both the states.

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- **Delhi Financial Corporation (DFC)** has been rendering service to small scale entrepreneurs in Delhi and Chandigarh. It has made finance available to existing and prospective entrepreneurs at very reasonable terms. The corporation also supports schemes for the needs of different categories of entrepreneurs.
- **Gujarat State Financial Corporation (GSFC)** was established under the provisions of State Financial Corporation Act of 1951. Since inception, GSFC has played a significant role in the development and industrialization of Gujarat by extending credit assistance to suit individual requirements. The primary objective behind the establishment of GSFC was to encourage development activities that lifts the social status, ensures proper regional dispersal of industrial activities and henceforth, add to the GDP of the country.
- **Haryana Financial Corporation (HFC)** has its Head Office at Chandigarh. It has been set-up under the State Financial Corporation Act, 1951. The. HFC, by way of dispersing term loans to small/medium scale industrial units, meets their credit requirement. These loans are directed towards acquiring fixed assets such as land, building, plant & machinery etc.
- **Himachal Pradesh Financial Corporation (HPFC)** was established under a Central Act, viz. the State Financial Corporation Act, 1951. By way of financing and other related activities, it acts as a catalyst that stimulates the development of small scale and medium scale industries in the State. The HPFC is jointly owned by the State Government and SIDBI and operates under the administrative control of the State Government.
- **Jammu & Kashmir State Financial Corporation (J&KSFC)** was incorporated under the State Financial Corporation Act, 1951 on 2nd December 1959 to play the role of a Regional Development Bank with the aim of encouraging economic development in the State. Its objective is to provide financial support to Small-Scale Industries, hotels, houseboats and transport sector in Jammu & Kashmir.
- **Karnataka State Financial Corporation (KSFC)** gives financial assistance in the form of term loans to new and existing units up to ₹ 500 lakhs for corporate entities and registered co-operative societies. Term loans up to ₹ 200 lakhs are sanctioned to proprietary; partnership and Hindu Undivided Family (HUF). KSFC offers lease financing and hire purchase assistance for acquisition of machinery/equipment/transport vehicles. KSFC also boasts of a dedicated merchant banking division and falls under Category 1 merchant banker approved by SEBI. The merchant banking department

offers services related to managing public issues, underwriting of shares, preparation of project report, deferred payment guarantee, loan syndication, bill discounting etc.

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- **Kerala Financial Corporation (KFC)** incorporated under the State Financial Corporations Act of 1951, is one of the top performers among the SFCs and is regarded as a trend setter in industrial financing to the service sector projects.
- **The Economic Development Corporation (EDC) of Goa**, established in 1975 was incorporated as a State Industrial Development Corporation and a limited company. However, later it was also accorded twin status of SFC by IDBI/SIDBI.
- **Madhya Pradesh Financial Corporation (MPFC)** was established in 1955, under the State Financial Corporation Act, 1951 (No. LXIII of 1951). It is the premier financial institution of the State engaged in providing financial assistance and related services to small, medium and micro sized industries. Like KSFC, MPEC is also registered as Category-I Merchant Banker with Securities Exchange Board of India and hence have a separate division of merchant banking, which is called MPFC Capital Markets.
- **The Orissa State Financial Corporation (OSFC),** which was incorporated as a primary state level financing institution in the year 1956 under the State Financial Corporations Act, 1951 extends term loan with an upper limit of ₹ 150 lakhs for acquiring various fixed assets and margin money for working capital. OSFC has formulated a Single Window Scheme under which it provides working capital. While providing financial assistance, priority is given to small and micro sector industrial units in the backward areas.
- **Punjab Financial Corporation (PFCs),** a premier leading institution of Punjab, came into existence on 1st February 1953. It is a body incorporated under the State Financial Corporation Act, 1951. PFCs primary job is to act as a Development Bank in the State of Punjab. The Corporation was established with the objective of granting loans for the establishment of new industrial concerns, modernization, expansion/diversification of existing activities and so forth.
- **Rajasthan Financial Corporation (RFC)** was constituted on the basis of a notification issued by the State Government on 17 January 1955 under the State Financial Corporation Act, 1951. It was constituted to providing long-term financial support to micro, small and medium scale industries in the State of Rajasthan. RFC is playing its role to perfection by acting as a catalyst of development by ensuring proper and effective implementation of the industrial policies and priorities of the Central and the State Governments.
- **Maharashtra State Financial Corporation (MSFC)** has been set-up under the State Financial Corporation Act, 1951. **The** Corporation has

been operating in **the State of Maharashtra** from 1962 and in State of Goa and Union Territory of Daman and Diu since 1964.

- **The Uttar Pradesh Financial Corporation (UPFC)** was established in 1954 under the State Financial Corporation Act, 1951 and its head office is located at Kanpur. The UPFC's contribution is widely acknowledged as it has nurtured numerous small and medium enterprises which have now grown into large units.
- **West Bengal Financial Corporation (WBFC)** is a State level financial institution that assists the small, medium and micro sector enterprises to execute their plans with respect to expansion, diversification, modernization or technological upgradation. WBFC has devoted itself to promote and develop the small industries sector within the state for more than half a century now. In spite of all the constraints, the Corporation has progressively contributed by registering increases in the figures of sanction, disbursement and recovery.

8.2.4 Objectives of State Finance Corporations

Broadly speaking, the main objective of SFCs is to provide financial assistance to medium and small scale industries which are outside the purview of IFCI.

The objectives for the establishment of SFCs are the following:

i. To ensure that there is uniformity in regional industries and their development.
ii. To provide incentives to new industries.
iii. To enhance efficiency in small and medium industrial units.
iv. To develop a pool of regional financial resources.
v. To provide finance to small scale, medium sized and cottage industries in the state.

8.2.5 Functions

i. The SFCs grant loans mainly for acquisition of fixed assets like land, building, plant and machinery.
ii. The SFCs provide financial assistance to industrial units whose paid-up capital and reserves do not exceed ₹ 3 crore (or such higher limit up to ₹ 30 crore as may be specified by the Central Government).
iii. The SFCs underwrite and subscribes new stocks, shares, debentures etc., of industrial concerns.
iv. The SFCs provide guarantee loans raised in the capital market by scheduled banks, industrial concerns, and state co-operative banks to be repayable within 20 years.
v. It offers deferred payment facilities for purchasing capital goods.

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In addition to the above, the SFCs according to Section 2(C) of the SFC Act, 1951 as amended in 1961, can assist an industrial concern that is engaged in any of the following activities:

- Manufacture, preservation and / or processing of goods
- Hotel Industries
- Road Transport
- Power Generation and distribution in any form
- Developing an area of land as industrial estate
- Involved in fishing activity or manufacturing of fishing products
- Providing expert or technical knowledge that can push industrial growth

8.2.6 Forms of Assistances

As far as assistance by SFCs is concerned, they primarily provide financial assistance but technical assistance is offered as well. The financial assistance takes shape by way of either permitting loans or advances or subscribing to debentures of industrial concerns, or by guaranteeing loans raised by industrial concerns or by underwriting the stocks, shares, bonds and debentures. The corporation can and also assist private limited concerns and partnership firms as well. The loans are granted against mortgaged assets and technical soundness of the project is given foremost consideration while granting loans.

Apart from financial help, SFCs provide the following services that are non-financial in nature:

- It offers project advisory and investment appraisal of small scale units;
- It offers project conceptualization and related services. It includes (i) assisting in selecting a project (ii) conducting and preparing feasibility reports, advice on capital structuring, project management and design etc.
- It acts as a guarantor for the industrial entities who have raised loans from commercial banks and state cooperative banks.
- It is primarily involved in subscribing shares, bonds and debentures of industrial concerns but not of any company having limited liability.
- It provides underwriting services for shares, bonds and debentures of industrial concerns.
- It assists in project documentation.
- It helps in the placement of debt-equity including (i) design of the structure of instruments, (ii) placement of instruments with financial institutions, bank etc.

8.2.7 Problems of the State Corporations

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Let us go through some of the problems faced by the State Finance Corporations.

i. The rate of default is high in repayment in loans.
ii. The functioning of SMEs lack transparency due to inability to adopt global practices.
iii. The assessment of creditworthiness of the small scale industries becomes difficult as usually they are promoted by individuals and the operations of the firm get adversely affected on the demise of the promoter. Thus, it is very difficult to assess the efficiency of the management.
iv. It is expected that loans are granted against proper security. However, this does not happen all the time. In the absence of security, the surety of repayment cannot be guaranteed and hence, SFCs find it difficult to safely advance loans.
v. The Corporations do not have adequately trained staff that can provide advisory services to the industry in the case of a receipt of a request for financial assistance. Recruitment of qualified and permanent staff is a costly affair and quality service cannot be expected from ad hoc staff.
vi. Due to lack of professional set-up the policy formulation and implementation is not consistent.
vii. As compared to the volume of requests the SFCs receive from the new and upcoming industries, the resources for disbursement are very paltry.
viii. The Corporation does not have adequate resources to survey the backward areas which have potential for growth. This hinders the growth of areas with high possibilities.
ix. In reality, the activities of SFCs and Commercial Banks overlap, resulting in competition rather than cooperation. This increases the complexity.
x. It is observed that the same set of rules is applied for both long-term and short-term financing, which is grossly unjust.
xi. Due diligence is not always maintained by the industries. They conceal information about production capacity, actual production and sales thereby making it difficult to truly assess the repayment capacity.

8.2.8 Suggestions for the Improvement of Working of SFCs

i. There is a strong voice that due consideration should be given to the integrity and honesty of the persons applying for the loan, instead of firm observance of the rules.
ii. Conduct conferences for the representatives of the Corporations to exchange ideas that would potentially educate and enhance the knowledge base of the staff. This would in turn improve the efficiency and performance.

iii. The State Government should grant interest-free loans.

iv. More concession to be allowed to the SMEs.

NOTES

Check Your Progress

1. Name few of the State Financial Corporations (SFCs) operating in India.
2. Mention the objectives for the establishment of State Financial Corporations (SFCs).
3. State any two non-financial services provided by the SFCs.

8.3 ANSWERS TO CHECK YOUR PROGRESS QUESTIONS

1. Few of the State Financial Corporations (SFCs) operating in India are as follows:
   - Andhra Pradesh State Financial Corporation (APSFC)
   - Himachal Pradesh Financial Corporation (HPFC)
   - Madhya Pradesh Financial Corporation (MPFC)
   - North Eastern Development Finance Corporation (NEDFI)
   - Rajasthan Finance Corporation (RFC)
   - Tamil Nadu Industrial Investment Corporation Limited(TIIC)
   - Uttar Pradesh Financial Corporation (UPFC)
   - Delhi Financial Corporation (DFC)
   - Gujarat State Financial Corporation (GSFC)
2. The prominent objectives behind the establishment of SFCs are the following:
   (i) To ensure that there is uniformity in regional industries and their development.
   (ii) To provide incentives to new industries.
   (iii) To enhance efficiency in small and medium industrial units.
   (iv) To develop a pool of regional financial resources.
   (v) To provide finance to small scale, medium sized and cottage industries in the state.
3. Two non-financial services provided by the SFCs are the following:
   (i) It acts as a guarantor for the industrial entities who have raised loans from commercial banks and state cooperative banks.

(ii) It is primarily involved in subscribing shares, bonds and debentures of industrial concerns but not of any company having limited liability.

NOTES

8.4 SUMMARY

- The State Finance Corporations (SFCs) have a very important role to play in the economic growth of a country. They have contributed in the development of the institutional finance structure in India.
- As of now, there are 18 State Finance Corporations (out of which 17 SFCs were established under the State Financial Corporation Act, 1951).
- The SFC's contribute in the development of Small, Medium and Micro Enterprises in their respective States. The financial assistance from the SFCs is provided in the form of direct subscription to debentures/equity, term loans, discounting of bills of exchange, guarantees, & seed/ special capital, etc.
- Kerala Financial Corporation (KFC) incorporated under the State Financial Corporations Act of 1951, is one of the top performers among the SFCs and is regarded as a trend setter in industrial financing to the service sector projects.
- Broadly speaking, the main objective of SFCs is to provide financial assistance to medium and small scale industries which are outside the purview of IFCI.
- The corporation can and also assist private limited concerns and partnership firms as well. The loans are granted against mortgaged assets and technical soundness of the project is given foremost consideration while granting loans.
- It is expected that loans are granted against proper security. However, this does not happen all the time. In the absence of security, the surety of repayment cannot be guaranteed and hence, SFCs find it difficult to safely advance loans.

8.5 KEY WORDS

- **Scheduled Banks:** These are the banks, which are accounted in the Second Schedule of the Reserve Bank of India (RBI) Act, 1934.
- **Loan Syndication:** It refers to a practice in which several banks each lend an amount of money to a borrower at the same time and for the same purpose.
- **Working Capital:** It is basically an indicator of the short-term financial position of an organization and is also an assessment of its overall efficiency.

8.6 SELF ASSESSMENT QUESTIONS AND EXERCISES

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Short-Answer Questions

1. What is the capital structure of State Finance Corporation?
2. What are the problems faced by the SFCs?
3. Write a short note on the methods of overcoming the problems being faced by the SFCs.

Long-Answer Questions

1. Discuss the establishment of SFCs in the different states of India.
2. Explain the primary functions of the SFCs.
3. Analyze the contribution of the SFCs in the economic development of the country.

8.7 FURTHER READINGS

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BLOCK - III
EXIM BANK FUNCTIONS

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UNIT 9 EXIM BANK AND NHB

Structure

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9.0 INTRODUCTION

The need of the hour in the post-independence era was to constitute a dedicated institution that would not only finance but also promote and regulate the export-import sector. This led to the establishment of the EXIM Bank. Similarly, providing affordable homes to all has long been the priority of the government. Hence, the housing sector also craved for a dedicated institution that can manage the finances and also regulate the related issues. This led to the formation of the National Housing Bank (NHB). In this unit, you will study about the inception, functioning and the contribution both these institutions have put in towards the development of the respective sector.

9.1 OBJECTIVES

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After going through this unit, you will be able to:

- Discuss the functioning, role and contribution of the EXIM Bank in foreign trade
- Explain the role, functions and objectives of the National Housing Bank (NHB)

9.2 INTRODUCTION TO FOREIGN TRADE

Foreign trade is the trading of capital, products and services across global boundaries or regions. It refers to the movement of goods across national borders and relates to export and import. Thus, the scholastic study of foreign trade is related to flow of trade; business strategies; asset allocation and adjustments in capital movements; study of balance of payments and global monetary measures. 'Foreign trade is a process of taking the goods from producers of one country to customers of another country.' Therefore, foreign trade may be referred as a business transaction during which the merchandise and ventures created in one nation are promoted in numerous nations and through which ownership of goods and services are transferred to consumers located in different countries.

9.2.1 Historical Background of Foreign Trade in India

Previously, foreign trade in India was conducted through the barter system or by exchange of gold coins or bars. The establishment of British Rule gave India's foreign trade an organized shape. At that time, India ranked fifth among the largest trading nations in the world. Jute and Jute goods, tea, cotton, oilseeds, mica, spices and tobacco were India's main exports then. After gaining Independence, Indian enterprises were given a lot of significance to be in the race of industrialization which cemented the way for external trade to a great extent. Foreign trade is highly regularized. Tariffs, import quotas, duties, trade agreement, import licensing, trading blocs are various types of restrictions levied to curb down free movement of goods and services across the nations. All these purposefully enforced hurdles are called trade barriers. However, the international bodies like General Agreement on Tariffs and Trade (GATT); [which has been replaced by World Trade Organization (WTO) in 1995] and United Nations Conference on Trade and Development (UNCTAD) are constantly in pursuit of eliminating such obstacles prevailing in foreign trade. Beside this, certain environmental issues like cultural, political, regulatory, economic, legal, social, human, technological, trade etc., also impact foreign trade. Before India got independence, specific policy on import and export was missing.

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During the British Rule, the colonial government wanted India to serve as a colony that would supply raw materials and in turn purchase the goods manufactured there. The main items that comprised India's exports were jute, tea, cotton etc., particularly to England and the imports consisted of consumer goods from England. Thus, the outline of pre-independence exports and foreign trade at large was very much colonial and agriculture based. Major portion of India's foreign trade was restricted to Britain and other Commonwealth countries. However, post-independence, India has witnessed significant industrial development, which is reflected in the complete turnaround in India's foreign trade volumes and stature. The list of commodities transacted during foreign trade has expanded enormously and is not confined to just a few products. Moreover, India has been able to link itself with mostly every other country of the world. India's exports stood at $272.4 billion till 2015. The major chunk of India's exports consisted of products and services like software, petrochemicals, agriculture, leather, jewellery, engineering goods, pharmaceuticals, textiles, chemicals, transportation, ores etc. India's main foreign trade partners as of now are the European Union (EU), the United States (USA), United Arab Emirates (UAE) and Hong Kong. As compared to the exports, the imports stood at $409.2 billion and it comprised products like crude oil, gold and precious stones, electronics, chemicals, plastics, iron and steel, vegetable oils etc.

9.3 EXIM BANK OF INDIA: FUNCTIONS

The Export-Import Bank of India is the foremost financial institution to finance foreign trade of the country that look to create value by integrating foreign trade and investment with the economic upsurge in the country. The proficiency of the Board members, senior policy makers, expert bankers, leading players in industry and international trade as well as professionals in exports, imports or financing bank have been the guiding force behind the establishment and functioning of the EXIM Bank. The bank has its branches located not only across many cities in India but also at select locations around the globe. The EXIM Bank seeks enhancement in the business volume of industries and SMEs.

The EXIM Bank of India addresses an uncommon instance of an institution where the idea and need for such an establishment had been argued for a significant stretch of time that lasted over twenty years – before it was at last set-up in 1982. India's industrial and trade scenario witnessed significant changes in the two decades leading up to the establishment of the EXIM Bank. Traditional commodities like jute and cotton textiles dominated the Indian exports during the fifties and the early sixties. The principal view with respect to India was that there should be growth in domestic demand which would actually serve as the device for economic growth, since the opportunities in growth in exports was limited due to lack of fundamental constraints like inadequate infrastructure. The philosophy involving manufacturing sector was to promote industrialization through import substitution. This resulted in exports being neglected and had a minor share in India's GDP.

In any case, the cycle of industrial advancement in India stimulated through the import substitution technique acted as a catalyst to the development of a large and expanded industrial base, especially the engineering sector. Various emerging industrial sub-areas also started to be globally competitive. The sixties saw the commencement of the alterations in India's export profile with an increase in share of non-traditional manufactured merchandise and other value added items.

The Ministry of Finance, in 1978-79, organised meetings to deliberate on the suggestions related to establishing of an Export-Import Bank. At these gatherings, it was agreed that there was a rationale behind the establishment of a separate organization on the ground that it is ready to commit whole-heartedly to the requirements of exporters and investigate new techniques for expanding credit on sensible footing. The proposed bank would also involve itself in financing projects linked to export oriented production houses.

By the year 1980, the proportion of export of engineering goods had risen to 13 per cent of the total exports. Project exports also got a boost and persistent demand of project exporters to set up an EXIM Bank, spirited push from the Ministry of Commerce and growing importance on export promotion collectively pushed the government into taking a final call. Shri R. Venkataraman, the then Finance Minister, in his budget speech in Parliament on 18 June 1980, announced the historic decision to launch an EXIM Bank.

The Export-Import Bank of India was along these lines brought into existence following twenty years of discussion on the requirement for a particular export credit organization for India that would assess and provide thrust to accelerate India's economic development.

The Export-Import Bank of India Act was passed in September 1981 and EXIM Bank commenced its operations in March 1982.

Today, the EXIM Bank of India serves as a vehicle of development for numerous ranges of Indian products and services. This includes import of technology and export product development, export production, export marketing, pre-shipment and post-shipment and overseas investment. In a rapidly changing financial scenario, the EXIM Bank of India is an impetus and central member in the advancement of cross border exchange and investment.

The EXIM Bank currently has a network of sixteen (16) EXIM Bank offices in India and overseas which are as follows:

Domestic Offices: Ahmedabad, Bangalore, Chandigarh, Chennai, Guwahati, Hyderabad, Kolkata, New Delhi and Pune.

Overseas Offices: London, Addis Ababa, Dubai, Johannesburg, Singapore, Washington D.C., and Yangon.

9.3.1 Objectives

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The primary objective as has been penned down in the Export-Import Bank of India Act, 1981is '…act on business principles with due regard to public interest.' The other objective that has been envisaged by the EXIM Bank is '….providing financial assistance to exporters and importers, and ... functioning as the principal financial institution for coordinating the working of institutions engaged in financing export and import of goods and services with a view to promoting the country's international trade...' The Export-Import Bank (Exim bank) was constituted on 1 January 1982 by an Act of the Parliament 'THE EXPORT-IMPORT BANK OF INDIA ACT, 1981' to carry on the functional activities of international finance wing of the IDBI and to provide financial support to the exporters and to act as a coordinating financial institution with all the institutions involved in financing of foreign trade. The EXIM Bank basically fills the institutional gap in India's foreign trade financing. In 1983, the EXIM Bank introduced 'Exim Syndicate Facility', a facility that calls the commercial banks in India, who are authorized dealers in foreign exchange, for maximum participation in export credit. As per Memorandum of PEM (Memorandumof Instructions on Project and Service Exports) of Reserve Bank of India, the following constitutes project exports:

- Supply of goods / equipment on deferred payment terms
- Civil construction contracts
- Industrial turnkey projects
- Consultancy / services contracts Exim Bank extends and serves funded and non-funded facilities for overseas turnkey contracts, construction contracts, supply contracts and consultancy contracts.

According to the booklet of the EXIM Bank of India: *Objectives, Operations and Organization, EXIM Bank Publication, 2007*, the objectives of EXIM Bank are discussed as follows:

- To translate national foreign trade policies into firm action plans.
- To provide alternate financing remedies to the Indian exporter, aiding him in his efforts to be internationally competitive.
- To develop mutually beneficial relationships with the international financial community.
- To initiate and participate in debates on issues those are central to India's international trade.
- To forge close working relationships with other export development and financing agencies, multilateral funding agencies and national trade and investment promotion agencies.
- To predict and absorb new developments in banking, export financing and information technology.

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- To be responsive to the export problems of Indian exporters and pursue policy resolutions.
- To conduct service, technical and economic studies and research projects with a view to enhance India's foreign trade so as to formulate a big plan for financing this sector.
- To provide technical, administrative and financial assistance to exporters of India.
- To plan, develop and encourage the cause of export promotion through financing a few vital export houses.
- To pool international information on international trade, marketing and credit aspects.
- To analyse and publish information on export trade.
- To function as an International Merchant bank through its various advisory services wings.

9.3.2 Products Offered by EXIM Bank

The EXIM Bank offers a range of monetary products that oblige organizations across layers to investigate new grounds and expand their business horizon. The products are discussed at length in this section.

1. Buyer's Credit

Buyer's credit is a remarkable credit service programme that inspires Indian exporters to investigate new geographical boundaries. Through this facility, an overseas buyer can open a 'letter of credit' for the Indian exporter and can import products and services from India on deferred payment terms. The exporter not only enjoys multiple benefits like reduction in the transaction costs and getting absolved from the complications of international trade transactions, but this facility also provides an opportunity to the Indian exporter to participate in the international market and also continue to judiciously use his working capital to expand operations. While Indian organizations avail buyer's credit from other global monetary institutions to fund their imports at competitive LIBOR rates, buyer's credit offered by the EXIM Bank can only be utilized for exporting Indian products.

2. Corporate Banking

The EXIM Bank offers 360 degree assistance to export-oriented units by satisfying their long-term loan requirements that would help exporters to finance new projects, expand, modernize or purchase new equipment or carry out R&D; and also meet out their working capital and overseas investment requirements. The corporate banking services are offered through specific schemes addressing corporate needs, grassroot requirements and emergency credit line. Financing to the corporates are offered through programmes like Research & Development Finance for Export Oriented Units, Pre-Shipment/Post-Shipment Credit Programme, Import Finance Programme, Production Equipment Finance Programme.

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At the grassroots level, the EXIM bank assists the artisans/producer groups/clusters/small enterprises throughout the country to rake up returns on their produce as it facilitates export of products from these units.

With an objective to bring back international trade on the tracks that had been derailed due to the unprecedented COVID-19 pandemic, the Finance Minister, unveiled a relief package for the Micro, Small and Medium Enterprises (MSMEs). Acting on these lines, the National Credit Guarantee Trustee Co. Ltd. (NCGTC), has introduced a scheme named Guaranteed Emergency Credit Line (GECL) that would provide 100 per cent guarantee coverage for the long-term working capital term loans to eligible MSMEs / Business Enterprises.

3. Lines of Credit

Right from its inception, the EXIM Bank is offering Lines of Credit (LOC) to empower Indian exporters to enter new topographies or extend their business in existing international markets free of any payment default from foreign importers. LOC is extended to overseas financial institutions, regional development banks, sovereign governments and other overseas entities, to permit importers in those countries to buy developmental and infrastructure projects, equipment, goods and services from India, on deferred payment terms. The LOCs are extended on the basis of the bank's own study and also as per the directive and with the support of Government of India.

4. Overseas Investment Finance

The access to foreign shores has been made easy by the EXIM Bank by offering

(a) Term-loans to Indian exporters for the purpose of
   - Equity investment in their overseas Joint Venture (JV)/Wholly Owned Subsidiaries (WOS), and
   - Onward lending to their overseas JV/WOS

(b) Term loans to overseas JV/WOS of Indian Companies towards part financing
   - Capital expenditure towards acquisition of assets
   - Working capital requirements
   - Equity investment in another company
   - Acquisition of brands/patents/rights/other IPR
   - Acquisition of another company

- Any other activity that would otherwise be eligible for finance from the EXIM Bank had it been an Indian entity
- Guarantee facility to the overseas JV/WOS for raising term loans/working capital

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5. Project Exports

In view of the remarkable performance of the Indian enterprises in bagging international projects that showcased their technological prowess and versatility, the EXIM Bank took steps to encourage project exports from India. The bank has in fact enabled many India companies to secure project from foreign countries in the past two decades.

The various types of projects that attracted the EXIM Bank's support include civil engineering and construction projects, turnkey projects, technical and consultancy projects and also supplies. The different aspects in which the support is provided includes the provision of specific equipment related to supplies, construction and building materials, consultancy, technical know-how, technology transfer, design, engineering (basic or detailed).

9.3.3 Services Offered by the EXIM Bank

The think tank at the EXIM Bank offers in-depth understanding on global economics, innovative research techniques and thorough analytical support. All this is done to build and improve global competitiveness and export ability. The various services that are offered by the EXIM Bank are the following:

1. Marketing Advisory Services

The EXIM Bank's Marketing Advisory Services (MAS) Group assumes a persuasive role to create and improve export capacities and global competitiveness of Indian organizations. The physical presence of the EXIM Bank provides support to the Indian exporters in their external marketing ventures. The key role played by the MAS Group include assisting Indian exporting companies to locate overseas distributors/buyers/partners for their products/services and also in identification of opportunities wherein they can set-up plants or projects or even acquire foreign companies.

In this endeavour, the EXIM Bank has been successful in placing a number of products in international as well as domestic markets. Products like handmade paper, handicrafts, vegetables and fresh fruits, garments, home décor, marine products, spices and agri-equipment are placed in Singapore, Africa, Brazil, Middle East and the US. Workshops and related events to facilitate designing and packaging are also organized by the MAS Group.

2. Research and Analysis

The EXIM Bank's Research & Analysis Group (RAG) expertly monitors the developments in international and domestic economies to evaluate their effect not only on the Indian economy but also other developing economies. Apart from serving its own constituents, the group also connects with the government, RBI, exporters/importers, trade and industry associations, external credit agencies, academic institutions and researchers. The group study profiles of other countries to assess risk involved related to economy, political, currency, and credit. In addition to that, the group identifies export possibilities in those countries, comes up with short to medium term outlook of the economy of that country.

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Furthermore, the said group also fixes an exposure limit for the countries where there is business interest and also tracks development in the critical ventures to assist the bank's business operations in these enterprises.

3. Export Advisory Service

The EXIM Bank possesses a dedicated Export Advisory Services Group (EAS) that offers a wide array of information, consultative and support services, which empower exporters to assess global risks, exploit export prospects and develop competitiveness. Customized research activities are conducted by the group in various areas that cover market potential, marketing arrangements and distribution channels. Additional services like developing market entry strategies, acquiring quality certification as per international standards and participation in international trade fairs to display the products are also provided EAS.

9.4 NATIONAL HOUSING BANK (NHB)

Housing is fundamental for respectable living of a man. The Government of India's primary motive is to provide housing for all. Working towards achieving this objective, GoI constituted the National Housing Bank in the year 1988 which has enabled various housing finance companies to provide housing loans. Here, we highlight the role played by the NHB towards the development of housing sector in India. Refinancing facility provided by NHB to the various housing finance companies contributed significantly in attaining this goal.

The National Housing Bank (NHB) is an apex financial institution for the housing sector which was established by the Government of India on 9th July 1988 under the National Housing Bank Act, 1987. It is an apex institution that provide stimulus to the housing finance companies, both locally and regionally, by providing financial and other allied supports to all the institutions which are involved in housing finance. It enl ists, directs and manages the Housing Finance Companies and synchronizes their activities with various regulators. In order to strengthen the functioning of NHB, the Government of India has recently undertaken it in its own fold. The total ownership of the NHB was assumed by the Government of India through an investment of ₹1450 crore. Prior to this, NHB was partly owned by the Reserve Bank of India but following the recommendations of Narasimham-II Committee, now, it has been released. A notification in this regard was issued by the Ministry of Finance on 29th April 2019.

The vision of the NHB is 'Promoting inclusive expansion with stability in housing finance market'. The mission statement issued by the NHB in pursuit of fulfilling this vision is 'To harness and promote the market potentials to serve the housing needs of all segments of the population with the focus on low and moderate income housing'. The vision and mission of the NHB clearly indicates that its objective to provide housing to all at affordable prices. The various policies, principles, guidelines and procedures framed by NHB are in line with them.

9.4.1 Sequence of Events Leading to Establishment of NHB

- It was during the Seventh Five Year Plan (1985-90) that The Sub-Group on Housing Finance brought into fore the actual reason that was acting as a hindrance in the progress of the housing sector. It was opined that the absence of any meaningful long-term finance to individual households was the main lacuna in the system and hence, recommended to set-up a dedicated national level institution that would cater to the needs of housing sector.
- The Committee of Secretaries accepted the recommendation and High Level Group under the Chairmanship of Dr. C. Rangarajan, the then Deputy Governor, RBI was set-up to scrutinize the proposal. The committee, after a lot of deliberations, recommended setting up of National Housing Bank as an independent housing finance institution. Later, the Government of India accepted the recommendation of the High Level Group.
- During his budget speech for 1987-88 on 28 February 1987, the then Prime Minister of India announced the decision to establish the National Housing Bank (NHB) as an apex level institution for housing finance. Following that, the National Housing Bank Bill (91 of 1987) providing the legislative framework for the establishment of NHB was passed by Parliament in the winter session of 1987 and with the assent of the President of India on 23 December 1987, became an Act of Parliament.
- Visualization by The National Housing Policy, 1988 to set-up NHB as an apex housing finance institution.
- Giving a concrete shape to the vision, NHB was finally established on 9 July 1988 under the National Housing Bank Act, 1987.
- The entire paid-up capital was contributed by the Reserve Bank of India.
- As per the provisions of the Act, Board of Directors of NHB will take care of all the affairs related to superintendence, direction and management.
- The Head Office of NHB is located at New Delhi.

9.4.2 Preamble, Vision, Mission and Objectives

The Preamble

The Preamble of the National Housing Bank Act, 1987 describes the basic functions of the NHB as '… to operate as a principal agency to promote housing finance institutions both at local and regional levels and to provide financial and other support to such institutions and for matters connected therewith or incidental thereto …'

Vision

'Promoting inclusive expansion with stability in housing finance market'

Mission

'To harness and promote the market potentials to serve the housing needs of all segments of the population with the focus on low and moderate income housing'

Objectives of the NHB

The objectives assigned to NHB are the following:

- Its main objective is to promote an economical, practical and feasible housing finance system for all sections of the society and to interlink the housing finance system with the overall financial system.
- It ensures to create a network of housing finance institutions solely for the purpose of fulfilling the dreams of owning a house of all sections of the population.
- It aims to increase resources for the housing segment to be used wholly for this segment.
- To make housing credit more affordable.
- To oversee the activities of housing finance companies based on the supervisory powers derived under the Act.
- To motivate public agencies to assist in providing services and facilities for the housing segment.

9.4.3 Role of NHB

- The NHB creates and supports the financial institutions which are involved in financing the housing sector.
- Loans and advances are being granted by the NHB against pledge of jewellery and/or mortgage of properties and also various other assets.
- It acts as a guarantor for the loans provided by housing finance companies.
- The NHB is also actively involved in underwriting activities.
- Bill of exchanges of various housing finance companies is dealt by the NHB.
- The NHB is also in to the purchase and sales, and mortgage of immovable properties.
- It makes a significant contribution in laying down housing schemes for the economically weaker section of the society.

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- The NHB acts as the principal coordinator between other financial institutions who provide housing finance projects like LIC, GIC and UTI.
- The National Housing Bank regularly conducts research and development activities related to construction work.
- The extension of housing credit schemes are framed by the NHB.

9.5 HOUSING FINANCE

Housing is an indispensable part for each person and it comprises socio-economic status of a man. In reality, the issue of housing in India is gigantic as bigger part of populace is still homeless and such homeless people exists both in the urban and rural areas. The deficiency of housing is a socio-economic and financial issue of a country and it requires the governments and other allied authorities' focus and will to resolve the problem. The housing sector has multi-dimensional impact as it would also boost infrastructure, household wealth, employment opportunities, education, health, eradication of poverty, women's participation in workforce, maternal and child mortality and many other wellness indicators. High growth in population and urbanization created huge demand of housing, both quantitatively and qualitatively. This led to the housing segment attracting special focus resulting in increase in supply.

9.5.1 Functions of NHB

The different functions of NHB are as follows:

- **Financing**

  The principal activity of the National Housing Bank is financing housing projects.The financial assistance to the sector is extended through refinancing and direct financing to various financial institutions who are involved in lending to the housing sector.

- **Refinancing**

  Refinance facility is offered to Primary Lending Institutions (PLIs) against eligible housing loans extended by them to individual house seekers. The refinancing facility is delivered through NHB's various schemes which accommodate all the segments of the population, in both rural and urban areas. These PLI's include housing finance companies, scheduled commercial banks, scheduled state cooperative banks, scheduled urban cooperative banks, Small Finance Banks, Regional Rural Banks, Apex Cooperative Housing Finance Societies (ACHFs) and Agriculture and Rural Development Banks (ARDBs).Refinance is also provided to HFCs for the financing they have granted to various implementing agencies.

- **Project Financing**

  NHB also directly finances public housing agencies such as State Level Housing Boards and Area Development Authorities who set up large scale integrated housing projects and slum redevelopment projects.

- **Equity Support**

  NHB has subscribed equity share capital of HFCs and other related companies.

- **Securitization**

  NHB in the past has also played the role of a Special Purpose Vehicle (SPV) for securing the housing loan receivables i.e., Securitization.

- **Guarantee**

  NHB also offers schemes that would guarantee the repayments of principal and payment of interest on bonds issued by HFCs.

9.5.2 Promotional Activities (HFCs Promotion and Development)

The chief mandate of the bank is to elevate housing finance institutions to improve/reinforce the credit delivery network for housing finance in the country. Rather than putting effort in opening of new housing financial institutions, NHB has judiciously played the role of a facilitator. To address the issue, NHB has issued the Model Memorandum and Articles of Association. NHB has also issued guidelines for participating in the equity of housing finance companies. All housing finance companies registered with NHB u/s 29A of the National Housing Bank Act, 1987 and scheduled commercial/co-operative banks are eligible for refinance support subject to terms and conditions as laid down under the respective refinance schemes. In pursuit of promoting the housing sector, NHB has also articulated a scheme that guarantees the bonds to be issued by the housing finance companies.

Considering the need for trained personnel for the sector NHB has designed and conducted various training programmes.

Conclusion

The EXIM Bank is the principal provider of medium and long-term export finance and also acts as a financer for export oriented units. Additionally, it also contributes by providing value-added services aimed at exports promotion. Studies portray that Export Credit Guarantee Corporation of India (ECGC) reinforces the export promotion by covering the risk associated with export credit. This arrangement, in a way, offers insurance protection to exporters against payment risks. In addition to this, it also provides financial guarantees to exporters in the form of packing credit guarantee, export production finance guarantee, post-shipment export credit guarantee, whole turnover post shipment guarantee, export finance guarantee, export performance guarantee, transfer guarantee and export finance (overseas lending) guarantee.

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The Government of India is making all efforts to provide housing to the homeless. However, few of the formalities and procedures including paperwork practiced by various housing finance institutions causes delay in the implementation of the housing finance schemes. Efforts should be made to simplify the procedure and make it more effective. Securitization is one such aspect that had been introduced to facilitate the housing sector. The first structured securitization deal took place in India in 1991 when securitization was trying to find space in India. Ever since, there have been numerous deals in the areas of auto loans, credit card and other receivables of various institutions. Even though, considering the potential of the Indian market, the growth is said to be very modest. The principal investors in the securities have all been institutional players and mostly all the securitized debt pools have been privately placed with single investors who have held them till maturity. In the field of Mortgage backed securitization, NHB launched a pilot project named Residential Mortgage Backed Securities (RMBS) in August 2000. Since then, there have been other issuances of RMBS by Banks and Financial Institutions. NHB has continuously put its effort in developing the systems and establishing institutions so as to make the RMBS market sustainable in the long run. NHB has directed its efforts at furnishing the market participants with ample knowledge of the RMBS products and creating adequate awareness about the issues, risks and benefits associated with the RMBS instruments, and also worked at length to broaden the investor base, which is a must for the development of a successful secondary mortgage market in the country.

Considering the fact that the expansion of secondary mortgage market in India largely depends on a sustainable securitization transaction mechanism, NHB has put in sustained efforts to address all the issues relating to mortgage backed securitization and develop legally accepted suitable securitization transaction structures that would make the transactions simple and practical in order to make it acceptable in the market.

While implementing the government sponsored housing schemes, the NHB to a certain extent is successful in wiping out the shortages of housing. It has also played an important role in making housing more affordable to the urban and rural poor. Furthermore, the entire housing finance mechanism is predominantly regulated by the NHB through its regulations and policies. Its principal contribution to the society is to facilitate a decent living at an affordable rate.

Check Your Progress

1. When was the Export-Import Bank of India established?
2. State one significant feature of the buyer's credit service programme.
3. When was the National Housing Bank (NHB) established?

9.6 ANSWERS TO CHECK YOUR PROGRESS QUESTIONS

1. The Export-Import Bank of India Act was passed in September 1981 and EXIM Bank commenced its operations in March 1982.
2. Buyer's credit is a remarkable credit service programme that inspires Indian exporters to investigate new geographical boundaries. Through this facility, an overseas buyer can open a 'letter of credit' for the Indian exporter and can import products and services from India on deferred payment terms.
3. The National Housing Bank (NHB) is an apex financial institution for the housing sector which was established by the Government of India on 9th July 1988 under the National Housing Bank Act, 1987.

9.7 SUMMARY

- Foreign trade is the trading of capital, products and services across global boundaries or regions. It refers to the movement of goods across national borders and relates to export and import.
- Previously, foreign trade in India was conducted through the barter system or by exchange of gold coins or bars. The establishment of British Rule gave India's foreign trade an organized shape.
- During the British Rule, the colonial government wanted India to serve as a colony that would supply raw materials and in turn purchase the goods manufactured there. The main items that comprised India's exports were jute, tea, cotton etc., particularly to England and the imports consisted of consumer goods from England.
- The Export-Import Bank of India is the foremost financial institution to finance foreign trade of the country that look to create value by integrating foreign trade and investment with the economic upsurge in the country.
- In any case, the cycle of industrial advancement in India stimulated through the import substitution technique acted as a catalyst to the development of a large and expanded industrial base, especially the engineering sector.
- The Export-Import Bank of India Act was passed in September 1981 and EXIM Bank commenced its operations in March 1982.
- The EXIM Bank offers a range of monetary products that oblige organizations across layers to investigate new grounds and expand their business horizon.

- The EXIM Bank offers 360 degree assistance to export-oriented units by satisfying their long-term loan requirements that would help exporters to finance new projects, expand, modernize or purchase new equipment or carry out R&D; and also meet out their working capital and overseas investment requirements.
- Right from its inception, the EXIM Bank is offering Lines of Credit (LOC) to empower Indian exporters to enter new topographies or extend their business in existing international markets free of any payment default from foreign importers.
- In view of the remarkable performance of the Indian enterprises in bagging international projects that showcased their technological prowess and versatility, the EXIM Bank took steps to encourage project exports from India.
- The EXIM Bank's Research & Analysis Group (RAG) expertly monitors the developments in international and domestic economies to evaluate their effect not only on the Indian economy but also other developing economies.
- The EXIM Bank possesses a dedicated Export Advisory Services Group (EAS) that offers a wide array of information, consultative and support services, which empower exporters to assess global risks, exploit export prospects and develop competitiveness.
- The National Housing Bank (NHB) is an apex financial institution for the housing sector which was established by the Government of India on 9th July 1988 under the National Housing Bank Act, 1987.
- The vision of the NHB is 'Promoting inclusive expansion with stability in housing finance market'. The mission statement issued by the NHB in pursuit of fulfilling this vision is 'To harness and promote the market potentials to serve the housing needs of all segments of the population with the focus on low and moderate income housing'.
- The housing sector has multi-dimensional impact as it would also boost infrastructure, household wealth, employment opportunities, education, health, eradication of poverty, women's participation in workforce, maternal and child mortality and many other wellness indicators.
- NHB also directly finances public housing agencies such as State Level Housing Boards and Area Development Authorities who set up large scale integrated housing projects and slum redevelopment projects.
- The chief mandate of the bank is to elevate housing finance institutions to improve/reinforce the credit delivery network for housing finance in the country. Rather than putting effort in opening of new housing financial institutions, NHB has judiciously played the role of a facilitator.

9.8 KEY WORDS

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- **Foreign Trade:** It is the trading of capital, products and services across global boundaries or regions. It refers to the movement of goods across national borders and relates to export and import.
- **Gross Domestic Product:** GDP is a monetary measure of the market value of all the final goods and services produced in a specific time period.
- **Letter of Credit:** It is a document that guarantees the buyer's payment to the sellers. It is issued by a bank and ensures the timely and full payment to the seller.

9.9 SELF ASSESSMENT QUESTIONS AND EXERCISES

Short-Answer Questions

1. Mention the objectives of the EXIM Bank of India.
2. Briefly mention the sequence of events leading to the establishment of NHB.
3. Write a short note on the role of the National Housing Bank (NHB).

Long-Answer Questions

1. Discuss the history of the beginning of foreign trade in India.
2. Explain the backdrop which led to the establishment of EXIM Bank of India.
3. Describe the products and services offered by the EXIM Bank of India.
4. Discuss the functions of the National Housing Bank.

9.10 FURTHER READINGS

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UNIT 10 UNIT TRUST OF INDIA: RESOURCES AND ACTIVITIES

Structure

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10.2 The Unit Trust of India (UTI)
  10.2.1 Investment Company
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10.0 INTRODUCTION

The Unit Trust of India (UTI) is considered the pioneer of the mutual fund industry in India. The very concept of unit based investment was introduced by UTI. Initially, after its inception in 1963, UTI was the sole player in mutual fund sector for more than two decades, and only faced challenges from the public and private players since 1990s. The entry of public and private sector banks and other financial institutions as well as foreign players heated up the mutual fund market and have eventually forced UTI to introduce diversified investment options and have provided an opportunity to the investors to spread their portfolio. In this unit, you will study about the concept, history, current status of the mutual fund industry and also the various investment options offered by the numerous players.

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10.1 OBJECTIVES

After going through this unit, you will be able to:

- Explain the concept of mutual funds
- Explain the history and progress of mutual funds in India
- Discuss the activities of UTI in the mutual fund sector
- Identify the various mutual fund instruments offered by UTI

10.2 THE UNIT TRUST OF INDIA (UTI)

UTI is an abbreviation for the Unit Trust of India. The Unit Trust of India was set-up on 1 February 1964 under the Unit Trust of India Act, 1963. It is a legal public sector investment organization whose essential target is to boost savings and mobilize those savings towards industrious investment opportunities.

10.2.1 Investment Company

Any organization or trust which has engaged itself in investing the pooled capital from investors in financial securities is an investment company. Investment is done through a financial instrument called mutual fund, which might be open-ended or close-ended.

'Fund company' or 'fund sponsor' are other names by which an investment company is referred to. The investment companies frequently tie-up with outsider merchants (agents or brokers) to sell the mutual funds.

Understanding an Investment Company

Investment companies, which may be both privately and publicly owned, are business organizations who are into managing, selling and marketing funds to the public. Even though the principal activity of an investment company is to hold and manage financial instruments for investment purposes, they also offer a collection of investment related services like portfolio management, record-keeping, custodial, legal, accounting and tax management. Thus, we can very well say that:

- An investment company is a firm or trust engaged in the business of investing collective capital into financial securities.
- Investment companies can be either privately or publicly owned. They are primarily engaged in the management, sale, and marketing of investment products to the public.
- Investment companies earn profits through buying and selling of shares, bonds, property, funds and other assets.

10.2.2 Meaning of Unit Trust of India

Unit Trust is basically an investment option wherein the funds are pooled together and then invested. Each individual investor, whose has a share in the pooled fund that is invested, is referred to as a 'unit holder'. He or she holds a certain number of units. The management of the fund and the resultant investment is bestowed upon a second party, who is referred as the fund manager and is responsible for the daily running of the trust and for investing in the funds. The trustee, governed by the Trust Companies Act in the year 1967, is the third party. The third party plays the role of a watchdog that ensures that the fund manager's performance is in accordance with the trust deed. The purpose of the deed is to encapsulate the objectives and imperative information about the trust. In addition, the assets of the trust are held in the name of the trustee. Consequently, they are held 'in trust' for unit holders.

10.2.3 Objectives and Functions of Unit Trust of India

Let us study about the primary objectives and functions of the Unit Trust of India.

The Primary Objectives of UTI

1. The primary goal of UTI is to motivate and collect the small savings from the lower and middle-class income groups, especially those who have no awareness about stock exchange.
2. Another objective is to such income groups to provide them with an opportunity to share the benefits of success resulting in rapid industrialization in India.

Functions of Unit Trust of India (UTI)

The major functions of UTI are the following:

i. The UTI activates the savings of the comparatively small investors.
ii. It also diverts small savings into productive investments.
iii. It allows the distribution of the large-scale economies among the small income groups.
iv. The Unit Trust of India promotes the savings of the lower and the middle-class people.
v. It converts small savings into industrial finance.
vi. It gives investors an opportunity to share the benefits of industrialization in the country.
vii. It also provides liquidity to the units.
viii. It accepts the discounts, purchases or sells a bill of exchange, warehouse receipt, documents of the title to goods, etc.
ix. It also grants loans and advances to the investors.

x. It provides leasing and hire purchase business.

xi. It permits buying or selling or making transactions in foreign currency.

10.2.4 The Advantages of UTI

The following are the benefits of UTI:

i. The investments are extremely safe and the risk factor is evenly spread over a wide variety of securities.

ii. UTI follows a policy of 90 per cent pay out. Hence, the investors may expect a regular and reasonable return.

iii. It provides high degree of liquidity as the units can be sold back to the trust at any point of time at the prevailing rate.

iv. The trust is managed by a team of highly professional and technically equipped fund managers.

v. There are several unit trusts for selection.

vi. It helps the investors to suitably expand the investments.

10.2.5 Organization and Management of Unit Trust of India

The Unit Trust of India (UTI) was established primarily with capital of ₹ 5 crore. This initial capital amount was contributed by the RBI (Reserve Bank of India), LIC (Life Insurance Corporation of India), SBI (State Bank of India) and its subsidiaries. In addition, the scheduled banks and the financial institutions also contributed to the capital of ₹ 5 crores. The initial capital was divided into 1000 certificates each priced at ₹ 50,000. To fulfill its financial requirements, the UTI is permitted to borrow from the RBI (Reserve Bank of India) on the condition that the amount should be repaid within a period of 18 months.

The Management at UTI consists of a Board of Trustees along with a Chairman and eight other members. Four members are nominated by the RBI (Reserve Bank of India), one member by LIC, one member nominated by SBI (State Bank of India), and the remaining two members are elected by contributing institutions.

10.2.6 The Unit Trust of India Schemes

- Unit scheme - 1964
- Unit Linked Insurance Plan - 1971
- Children Gift Growth Fund Unit Scheme - 1986
- Rajyalakhmi Unit Scheme - 1992
- Senior Citizen's Unit Plan - 1993
- Monthly Income Unit Scheme
- Master Equity Plan - 1995

- Money Market Mutual Fund Scheme - 1997
- Unit Trust of India (UTI) Growth Sector Fund - 1999
- Growth and Income Unit Schemes

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10.3 SUBSIDIARIES OF UTI

Let us briefly study about the subsidiaries of UTI.

10.3.1 UTI Ventures

One of the subsidiary firms of UTI is UTI Ventures, which is a leading private equity (PE) firm and investment arm of UTI Asset Management Co. Pvt. Ltd. With its orientation towards capital growth, UTI Ventures provide thrust to the ambitions of enthusiastic Indian entrepreneurs through superior returns tothe investors. Its fund happens to be one of the top performing funds in the country as it is led by an experienced asset management team.

10.3.2 UTI International Ltd

UTI International Ltd (UTI IL) is a 100 per cent subsidiary of UTI Asset Management Company Ltd. (UTI AMC). UTI International plays the dual role of managing the offshore interests of UTI Asset Management Company and global marketing of the firm's Investment strategies. To perform its services, two separate business entities are incorporated at Guernsey and Singapore. The Guernsey entity is named UTI International Ltd. and the Singapore unit is named as UTI International Singapore Private Ltd. respectively. UTI International Singapore Private Ltd. is primarily entrusted with the responsibility of representing the offshore interests of UTI AMC. Its primary job is to give a thrust to global investment in India and bring in foreign investment in the country. The pool of investors comprises Family Offices, Insurance companies, pension funds and other financial institutions. UTI Asset Management Company (UTI AMC) is considered to be one of India's largest Money Managers and the leading manager of Indian Equities, Fixed Income and Private Equity and is listed on both the NSE and BSE. With a vigorous yet healthy investment process that has survived the testing times, the group currently has an AUM of USD 150.31 billion (as on Dec 31st 2020) and manages money for more than 11 million clients.

10.3.3 UTI RSL (Retirement Solutions Limited)

UTI Retirement Solutions Ltd. (UTI RSL) is a 100 per cent subsidiary of UTI Asset Management Company Ltd. and was incorporated on 14th December, 2007. It commenced its business in 2008. The Board of Trustees of the New Pension System Trust, set-up under the Indian Trust Act, 1882, directed UTI RSL to perform operations as a Pension Fund. Moreover, it was also directed by the Government or Pension Fund Regulatory and Development Authority (PFRDA) to assume wholesale asset management. PFRDA initially appointed UTI RSL to manage Pension Funds of the government employees.

On 13th March 2009, UTI RSL also handed over the letter of appointment for Management of Pension Funds under the New Pension System for all citizens, apart from Govt. Employees covered.

10.4 UTI ASSET MANAGEMENT COMPANY: AN INTRODUCTION

UTI AMC is a company incorporated under the Companies Act 1956. The investment agreement between UTI Trustee Company Ltd and UTI AMC was executed on 9 December 2002. Later in January 2003, UTI AMC was registered by SEBI and was permitted to act as as Asset Management Company for UTI Mutual Fund vide a letter in this regard.

For almost two decades, since its inception in 1963 by an Act of Parliament, the Unit Trust of India enjoyed undisputed monopoly. As it was established by the Reserve Bank of India, it operated under the regulatory control of the RBI till 1978 when the two were de-linked and the entire control was transferred from RBI to the Industrial Development Bank of India (IDBI). The Unit Scheme 1964 (US-64) was the first scheme that UTI had launched in the year 1964 and became very popular resulting in the largest number of investors getting attracted to any single investment scheme over the years. 1970s and 1980s witnessed the introduction of many more innovative schemes by UTI, aimed at meeting the expectations of various types of investors. ULIP scheme was launched in 1971 followed by six more schemes between 1981 and 1984, namely Children's Gift Growth Fund and India Fund (India's first offshore fund) in 1986, Mastershare (India's first equity diversified scheme) in 1987 and Monthly Income Schemes (offering assured returns) during 1990s. As a result, by the end of 1987, UTI's AUM grew ten times to ₹ 6700 crores.

The UTI Asset Management Company (UTI AMC) is currently the seventh largest asset management company in India with respect to mutual fund QAAUM as of 30 September 2019, according to CRISIL. With an excess of 11 million Live Folios as of 30 September 2019, the customer base of UTI AMC records for 12.8 per cent of the roughly 86 million folios that, as indicated by CRISIL, are overseen by the Indian mutual fund sector. UTI AMC, in addition to managing the schemes of UTI Mutual Fund, also manages the various schemes transferred/ migrated from the erstwhile Unit Trust of India, in accordance with the provisions of the Investment Management Agreement, the Trust Deed, and the SEBI (Mutual Funds) Regulations. The experience and track record of UTI AMC, solid brand acknowledgment, reach to the customers and connection with them and the execution has created a platform for strong future growth.

UTI AMC is an expertly managed organization driven by the Board of Directors and a committed and experienced team of fund managers. In line with the SEBI Mutual Fund Regulations, its four patrons are the State Bank of India (SBI), Life Insurance Corporation of India (LIC), Punjab National Bank (PNB) and Bank of Baroda (BOB) (altogether, referred to as the Sponsors), where the Government of India is the principal shareholder in each of them. T. Rowe Price Group, Inc., a global asset management company, through its subsidiary T. Rowe Price International Ltd. (TRP), is UTI AMC's other major shareholder.

Reaching the potential investors through a diverse range of instruments and distribution channels has enabled to register a national presence. As of 30 September 2019, the distribution network consists of 163 UTI Financial Centres ('UFCs'), 273 Business Development Associates ('BDAs') and Chief Agents ('CAs') (46 of whom operate Official Points of Acceptance ('OPAs') and 33 other OPAs.

UTIAMC has a nationwide network comprising 143 UTI Financial Centres (UFCs) and UTI International offices in London, Dubai and Bahrain. The mutual fund industry registered its footprints in India with the introduction of the concept of mutual fund by UTI in the year 1963. Despite the fact that the pace of initial development was slow to moderate, yet it quickened from the year 1987 when non-UTI players entered the business. In the past couple of decades, there has been remarkable progress in the Indian mutual fund industry, both qualitatively and quantitatively. The Assets Under Management (AUM) base was ₹ 67bn by the time monopoly was waning and the influx of private players in this sector saw a manifold rise in the AUM to ₹ 470 bn in March 1993 and by April 2004, it reached the height of 1,540 bn. Even after substantial improvement, the AUM of the Indian Mutual Funds Industry stood at mere 11 per cent of the total deposits held by the Indian banking industry. In fact, it was less than the deposits of SBI alone.

10.5 UTI MUTUAL FUNDS

Let us study about the origin and growth of UTI mutual funds.

10.5.1 Vision

To be the most Preferred Mutual Fund.

10.5.2 Mission

- The most trusted and admired brand for all stakeholders.
- The most efficient wealth manager with a global presence.
- Deliver best-in-class customer service.
- The most preferred employers.

- Create innovative products that maximise ROI.
- Socially responsible corporation that focus on well-being of all.

10.5.3 Genesis

The UTI Asset Management Company provides back-end support to all the services delivered by the UTI Mutual Fund (excluding fund management) in accordance with the provisions of the Investment Management Agreement, the Trust Deed, the SEBI (Mutual Funds) Regulations and the objectives of the schemes. UTI AMC was registered as a portfolio manager under the SEBI (Portfolio Managers) Regulations, 1993 on 3rd February 2004. Its primary objective was to take on portfolio management services and also play the vital role of a manager and marketer to offshore funds through its 100 per cent subsidiary, UTI International Limited, registered in Guernsey, Channel Islands.

The UTI Asset Management Company Ltd. (UTI AMC) has been sponsored by the State Bank of India, Life Insurance Corporation of India, Punjab National Bank and Bank of Baroda, with each holding 25 per cent of the paid up capital. UTI AMC is the investment manager to the schemes of UTI Mutual Fund. The offshore funds are managed by it along with providing support to the Specified Undertaking of the Unit Trust of India. It is the holding company for UTI Venture Funds Management Company which manages venture funds and UTI International Ltd., which markets offshore funds to foreign investors. After UTI came into existence in 1963, it remained the sole vehicle for investment in the capital market by the Indian citizens for more than two decades. In mid-1980s public sector banks got permission to join the mutual funds industry. The genuine energy and rivalry in the MF business started with the setting up of the Regulator SEBI and its laying down the MF Regulations in 1993.UTI enjoyed dominance till 2001, even after the mutual fund market was crowded by various banks. However, things took a backward turn when the market indices declined massively due to negative investor sentiments after Ketan Parekh scam created uncertainties about the capability of UTI to meet its obligations to the investors. The sentiments got a further hit after its flagship and largest scheme US 64 was sold and re-purchased not at intrinsic NAV but at artificial price.

10.5.4 The Mutual Fund Concept

The Unit Trust of India Act was introduced in the year 1963 to provide for the establishment of a corporation with a view to encouraging saving and investment and the participation in the income, supports, and the gains accruing to co-operation from the holding, management, and disposal of the securities.

The concept of mutual fund is fairly simple and structured. It is the moderation of risk through creating a portfolio i.e., spreading of investments across multiple entities, which is achieved by the pooling of funds in the form of small size investment by large number of investors ultimately forming a large bucket to invest from.

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However, it has been the subject of maybe the most intricate and delayed administrative exertion throughout the entire existence of the country. The mutual fund industry has struggled to rapidly progress mainly due to lack of mass awareness and safety assurance. Thus, it becomes mandatory on the part of all mutual fund companies, to market the product without misleading the customers. Mutual funds are the easiest way to invest in stock exchange, bonds and other security funds. Mutual funds provide a god choice of investment due to the following reasons:

- Mutual funds are professionally managed by fund managers, so most of the investment research is done the general public in advance.
- An investor can make investment in various financial products; thus, diversifying his investment risk.

Transaction costs are often lower than if you invested in individual securities (the mutual fund buys and sells large amounts of securities at a time). Mutual Funds are significant investment instruments for those people who share similar investment objectives and then invest their money accordingly. Each unit of any scheme represents the proportion of pool owned by the unit holder (investor). The Net Asset Value (NAV) reveals the appreciation or reduction in value of investments of the concerned scheme, which is declared by the fund from time to time.

Mutual fund schemes are managed by the respective Asset Management Company (AMC). It is to be noted that various business groups/ financial institutions/ banks have sponsored these AMCs, either single-handedly or in collaboration with renowned international companies.

The Indian capital market has witnessed remarkable development and changes particularly during the decades of 1980s and 1990s. These changes refer particularly to new financial instruments, new financial institutions such as mutual funds, and a variety of financial services like merchant banking, credit rating, factoring and others.

Rapid changes have been witnessed in the investment outlook. The mutual funds are playing a significant role in financial intermediation, development of capital markets and the growth of the corporate sector. The Indian mutual fund industry is comparatively new yet it has grown at a rapid speed influencing numerous sectors of the financial market and the economy. Mutual funds have now become an important medium of investment for the average Indian investor. Mutual funds enable the investor to be a part of the capital market in an indirect manner and thus earn revenue from diversification and fund management. Theoretically, a mutual fund is a single large professionally managed investment fund that pools the money of numerous individual investors having similar investment goals. It invests this money in a wide variety of securities and individual investors accordingly earn income from it. In simple words, a mutual fund is a type of an investment instrument, which mobilizes savings of individuals and institutions and diverts these savings in corporate securities to provide investors a steady flow of returns and capital appreciation. Thus, the two significant benefits of investment in mutual funds are diversification and professional investment management.

Historically, the mutual fund industry in India has been in existence since 1964 when the Government of India established the Unit Trust of India (UTI) under a special Act of the Parliament. Since then, UTI has been offering various schemes to the investors to suit their requirements. The uniform structure of mutual fund industry was, however, broken in the year 1987 when the Government of India permitted commercial banks and insurance corporations to launch their own funds. The first bank to enter the field was the State Bank of India (SBI) in 1987 sponsoring (SBI) mutual funds followed by Can bank mutual funds set-up by Canara Bank. In the same year, the other banks, namely, Punjab National Bank (PNB) Bank of India (BOI) Bank of Baroda (BOB) and Indian bank entered the mutual fund sector. The insurance companies such as Life Insurance Corporation of India (LIC) and General Insurance Corporation of India (GIC) also entered the mutual fund sector in 1989 and1990, respectively. Later, liberalization policy opened up the market for other public sector financial institutions as well. Private sector players too were allowed and entered the mutual fund business in 1993. Thus, at present, the industry has three types of players' viz. (i) public sector (ii) financial institutions and (iii) private sector.

During the previous four decades, the business has grown tremendously with reference to size and tasks. Thus, it is essential for both the fund managers and also the investors to know how they have performed throughout the long-term. The investment performance of mutual funds has been extensively examined for the developed capital markets such as those of the US, UK, Australia, UK, Australia and to a much lesser degree for other capital markets such as those of Singapore, Japan and other developing countries. Of late, the Indian capital market and, in particular, mutual fund sector has come under the scanner and some efforts are underway to examine the performance of Indian mutual funds.

10.6 SCHEMES AND SERVICES OFFERED BY UTI MUTUAL FUND (UTIMF)

The various products and services offered by UTIMF may be categorised as follows:

I. Asset Class

(A) Equity Funds

i. UTI Banking & Financial Services Fund
ii. UTI Core Equity Fund
iii. UTI Dividend Yield Fund
iv. UTI Flexi Cap Fund

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v. UTI Healthcare Fund
vi. UTI India Consumer Fund
vii. UTI Infrastructure Fund
viii. UTI MNC Fund
ix. UTI Mastershare Unit Scheme
x. UTI Mid Cap Fund
xi. UTI Nifty Index Fund
xii. UTI Nifty Next 50 Index Fund
xiii. UTI Small Cap Fund
xiv. UTI Transportation & Logistics Fund
xv. UTI Value Opportunities Fund

(B) Debt Funds

i. UTI Banking & PSU Debt Fund
ii. UTI Bond Fund
iii. UTI Bond Fund (Segregated - 17022020)
iv. UTI Corporate Bond Fund
v. UTI Credit Risk Fund
vi. UTI Credit Risk Fund (Segregated - 06032020)
vii. UTI Credit Risk Fund (Segregated - 13092019)
viii. UTI Credit Risk Fund (Segregated - 17022020)
ix. UTI Dynamic Bond Fund
x. UTI Dynamic Bond Fund (Segregated - 17022020)
xi. UTI Floater Fund
xii. UTI Gilt Fund
xiii. UTI Medium Term Fund
xiv. UTI Medium Term Fund (Segregated - 17022020)
xv. UTI Money Market Fund
xvi. UTI Short Term Income Fund
xvii. UTI Treasury Advantage Fund

(C) Overnight and Liquid Mutual Funds

i. UTI Liquid Cash Plan
ii. UTI Overnight Fund

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(D) Hybrid Funds

i. UTI Arbitrage Fund
ii. UTI Equity Savings Fund
iii. UTI Hybrid Equity Fund
iv. UTI Multi Asset Fund
v. UTI Regular Saving Fund (Segregated - 17022020)
vi. UTI Regular Savings Fund
vii. UTI Unit Linked Insurance Plan

II. Exchange Traded Funds

i. UTI Gold Exchange Traded Fund
ii. UTI Nifty Next 50 Exchange Traded Fund
iii. UTI Bank Exchange Traded Fund (UTI Bank ETF)
iv. UTI Nifty Exchange Traded Fund
v. UTI S&P BSE Sensex Next 50 Exchange Traded Fund
vi. UTI Sensex Exchange Traded Fund

III. Solution Based Funds

(A) Wealth Builder (UTI Multi Asset Fund)
(B) Child's Career Planning (UTI Children's Career Fund (UTI CCF) - Savings Plan
(C) Tax Saving
  i. UTI Long Term Equity Fund (Tax Saving)
  ii. UTI Childrens Career Fund (UTI CCF) - Investment Plan
  iii. UTI Retirement Benefit Pension Fund
(D) Retirement Planning (UTI Retirement Benefit Pension Fund)
(E) Core Portfolio Builder
  i. UTI Mastershare Unit Scheme
  ii. UTI Children's Career Fund (UTI CCF) - Investment Plan
  iii. UTI Flexi Cap Fund
  iv. UTI Value Opportunities Fund

IV. SNew Fund Offers

i. UTI Nifty200 Momentum 30 Index Fund

V. Other Businesses

i. Offshore Business
ii. Alternative Investment Funds
iii. National Pension Scheme
iv. Portfolio Management Services

Conclusion

After a careful presentation of the introduction and concept of UTI mutual funds investment or unit trusts as they are known elsewhere, the concept, their schemes and classes, and their objective, we attempt to summaries the findings, and drawn conclusions regarding the mutual fund sector and UTI in particular.

As studied and observed, it may be said that there are certain aspects on which the mutual fund industry should focus for future growth. They are:

i. Information regarding mutual fund should be disseminated through appealing advertisement, supporting project and holding seminar and workshop programmes. The effort would educate the investors and also create a powerful investor mindset about the mutual fund.
ii. Awareness regarding mutual fund should not be limited to only men or working women, the industry should also make awareness regarding mutual fund to housewives about the benefit of investing in mutual fund, they should make such awareness through TV, radio, newspaper and magazine.
iii. Since people are more inclined to invest in the private sector than the public sector sponsored mutual fund, the public sector should introduce innovative mutual funds that would compete with the private sector mutual funds and also should not get stuck with age old products.
iv. Investors should be made aware regarding the safety of the foreign sponsored mutual fund and convinced to invest their money in the foreign sponsored mutual funds.
v. The UTI should recruit professional fund manager in their AMC as majority of investors feel that fund manager is the face of the Mutual Fund Company and the company should also check insider trading and keep a watch on investment made by the fund manager in the stock market.
vi. As various regulations with respect to mutual funds are laid down by SEBI and AMFI, investors' safety has increased and they are now more confidant. Nevertheless, it is still the responsibility of the SEBI and AMFI to assure that investors' money are safe and their grievances and other disputes are resolved properly and timely.

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vii. The industry needs to penetrate more and bridge the urban-rural divide. The potential of the rural market should be tapped and the focus should shift towards dismantling the big city mentality and penetrate among the rural investors.

viii. Various scams and market failures had necessitated the requirement for implementing more stringent measures to enhance investor protection. Safeguarding the interest of investors is paramount and gains more significance in a volatile market.

Check Your Progress

1. When was the Unit Trust of India established?
2. Mention the advantages of UTI.
3. Name some of the significant schemes of UTI.
4. When was the UTI Asset Management Company established in India?

10.7 ANSWERS TO CHECK YOUR PROGRESS QUESTIONS

1. UTI is an abbreviation for the Unit Trust of India. The Unit Trust of India was set-up on 1 February 1964 under the Unit Trust of India Act, 1963.
2. The advantages of UTI are the following:
   (i) UTI follows a policy of 90 per cent pay out. Hence, the investors may expect a regular and reasonable return.
   (ii) It provides high degree of liquidity as the units can be sold back to the trust at any point of time at the prevailing rate.
   (iii) The trust is managed by a team of highly professional and technically equipped fund managers.
   (iv) There are several unit trusts for selection.
3. Some of the significant schemes of UTI are the following:
   - Unit Linked Insurance Plan - 1971
   - Children Gift Growth Fund Unit Scheme - 1986
   - Rajyalakhmi Unit Scheme - 1992
   - Senior Citizen's Unit Plan - 1993
   - Monthly Income Unit Scheme
   - Master Equity Plan - 1995

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4. UTI AMC is a company incorporated under the Companies Act 1956. The investment agreement between UTI Trustee Company Ltd and UTI AMC was executed on 9 December 2002. Later in January 2003, UTI AMC was registered by SEBI and was permitted to act as as Asset Management Company for UTI Mutual Fund vide a letter in this regard.

10.8 SUMMARY

- The Unit Trust of India (UTI) is considered the pioneer of the mutual fund industry in India. The very concept of unit based investment was introduced by UTI.
- The Unit Trust of India was set-up on 1 February 1964 under the Unit Trust of India Act, 1963. It is a legal public sector investment organization whose essential target is to boost savings and mobilize those savings towards industrious investment opportunities.
- 'Fund company' or 'fund sponsor' are other names by which an investment company is referred to. The investment companies frequently tie-up with outsider merchants (agents or brokers) to sell the mutual funds.
- Unit Trust is basically an investment option wherein the funds are pooled together and then invested. Each individual investor, whose has a share in the pooled fund that is invested, is referred to as a 'unit holder'.
- One of the subsidiary firms of UTI is UTI Ventures, which is a leading private equity (PE) firm and investment arm of UTI Asset Management Co. Pvt. Ltd.
- UTI Retirement Solutions Ltd. (UTI RSL) is a 100 per cent subsidiary of UTI Asset Management Company Ltd. and was incorporated on 14th December, 2007. It commenced its business in 2008.
- UTI AMC is a company incorporated under the Companies Act 1956. The investment agreement between UTI Trustee Company Ltd and UTI AMC was executed on 9 December 2002. Later in January 2003, UTI AMC was registered by SEBI and was permitted to act as as Asset Management Company for UTI Mutual Fund vide a letter in this regard.
- The Unit Trust of India Act was introduced in the year 1963 to provide for the establishment of a corporation with a view to encouraging saving and investment and the participation in the income, supports, and the gains accruing to co-operation from the holding, management, and disposal of the securities.

10.9 KEY WORDS

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- **Investment Company:** It refers to any organization or trust which has engaged itself in investing the pooled capital from investors in financial securities.
- **Mutual Fund:** It is a professionally-managed investment scheme. It is generally operated by an asset management company that brings together a group of people and invests their money in stocks, bonds and other securities.
- **Hybrid Fund:** These are funds that invest in a blend of more than one asset class.
- **Asset Management Company:** It is A company registered with SEBI, which takes investment/divestment decisions for the mutual fund and manages the assets of the mutual fund.

10.10 SELF ASSESSMENT QUESTIONS AND EXERCISES

Short-Answer Questions

1. List the salient features of an investment company.
2. Write a short note on the objectives and functions of the Unit Trust of India.
3. Briefly discuss the UTI Asset Management Company.

Long-Answer Questions

1. Discuss the organization and management of Unit Trust of India.
2. Explain the various subsidiaries of UTI.
3. Describe the schemes and services offered by UTIMF.
4. Analyze the significant areas of focus for ensuring future growth of mutual funds in India.

10.11 FURTHER READINGS

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UNIT 11 LIC AND GIC: THEIR ROLE IN INDUSTRIAL DEVELOPMENT

Structure

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11.0 INTRODUCTION

Life Insurance Corporation (LIC) and General Insurance Corporation (GIC) are the flag bearers of Indian insurance business. While LIC's business revolves around life insurance, GIC is into non-life insurance and reinsurance business. This unit covers the history and evolution of insurance sector in India, objectives behind their operations, various activities covered by the insurance companies and the role they play in bringing more citizens within the ambit of insurance.

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11.1 OBJECTIVES

After going through this unit, you will be able to:

- Discuss the insurance sector of India
- Discuss about LIC and its functions and role in the insurance sector
- Explain the role and functions of GIC in the insurance sector

11.2 INSURANCE BUSINESS

The term 'insurance' has different facets and can be differently defined, both financially and legally. The financial aspect focuses on the funding for ensuring financial security against a probable mishap whereas the legal aspect deals with provisions relating to a legally enforceable contract.

Definition in Financial sense

Insurance is a monetary course of action, which reallocates the expenses of unforeseen misfortunes among the individuals from the pool. The pool is a group of individuals facing common risks. All members contribute a pre-determined fixed sum called premium towards the pool. The premium paid ensures that the concerned person gets an assurance that a certain sum of money will be paid to him on the happening of the event against which he is insured. In the entire arrangement, there exists an assurance that in the case of a loss, he will be financially compensated. Thus, an insurance agreement involves the transfer of losses to an insurance pool and the reallocation of losses among the members of the pool.

Definition in Legal sense

From the legal aspect, insurance may be referred to as a contract between two parties during which one party accepts to take guarantee of any financial loss suffered by other party, in consideration of a sum of money, on the happening of a specified event; for example, fire, accident or death. The party agreeing to take guarantee to pay for the losses is known as the 'insurer' whereas the party who receives the claim from the 'insurer' as the 'insured'. The consideration amount which the insured pays to the insurer, in lieu of which the coverage of his loss in guaranteed, is known as the premium. The insurance contract is known as a policy. To sum up, insurance is a transfer of risk from the individual to the group and there is a sharing (pooling) of losses on some equitable basis such that unexpected losses can be guaranteed.

11.2.1 Nature of Insurance

Insurance has the following characteristics, which are observed in case of life, marine, fire and general insurance.

- **Sharing of risk**

Insurance is a financial instrument that shares the financial losses which might occur to an individual or his family on the happening of a specific event which is covered by the said insurance policy. The event may be death in case of life insurance, fire in fire insurance etc. When insured, the loss arising from these events will be shared by all insured against the payment of a premium.

- **Co-operative device**

The most significant aspect of every insurance plan is that it results in the pooling of large number of persons who, through paying a premium, in effect, agree to share the financial loss arising due to a particular risk which is insured. It is not possible by an individual insurer to compensate all the losses (claims) from his capital and hence, a pool of funds is created by the premium collected from a large number of persons which enables him to meet all the losses (claims).

- **Value of risk**

To fix the amount of premium to be charged, risk evaluation is done and the value of the risk is reached at. There are numerous methods to evaluate risk. Higher risk attracts higher premium. So, the probability of loss is calculated at the time of taking insurance policy and the premium is decided on the basis of degree of risk.

11.2.2 History of Insurance

The very existence of insurance can be matched with the existence of mankind. It is almost as old as that. Primeval men, then, displayed the same instincts that are noticed amongst modern day businessmen with respect to securing themselves against unforeseen events causing loss. They also looked to prevent the evil impact of fire and flood and loss of life and were prepared to make some sort of sacrifice in order to attain security. So, we can very well say that, even though insurance as a business is practiced more since the industrial era in the past few centuries, yet its concept has roots dating back almost 6000 years.

The modern concept of life insurance came to India from England in 1818. The first life insurance company on Indian soil, namely, Oriental Life Insurance Company was started in Kolkata (then Calcutta) by the Europeans. The focus of all the insurance companies established during that period was to insure the European community and Indian people were deprived of this facility. The scenario improved later after sustained efforts by eminent people like Babu Mutty Lall Seal, when the foreign life insurance companies agreed to insure Indian lives. However, the Indians were charged extra heavy premium and they were considered as sub-standard lives. In 1870, the first Indian life insurance company, Bombay Mutual Life Assurance Society came into existence and provided insurance cover to Indian lives at normal rates. The Indian insurance companies countered their European counterparts with patriotism and carried the message of insurance and social security through insurance to various sectors of society. Bharat Insurance Company (1896) was another company that ventured into insurance business very much inspired by nationalism. More Indian companies entered the fray during the Swadeshi movement of 1905-1907. To name a few, The United India in Madras, National Indian and National Insurance in Calcutta and the Co-operative Assurance at Lahore were established in 1906. In 1907, Hindustan Co-operative Insurance Company took its birth in one of the rooms of the Jorasanko, house of the great poet Rabindranath Tagore, in Calcutta. The Indian Mercantile, General Assurance and Swadeshi Life (later Bombay Life) were some of the other companies established during the same period. Before 1912, there were no regulatory regulations in India related to insurance business. To regulate the insurance sector in India, the Life Insurance Companies Act and the Provident Fund Act were passed in 1912. The Life Insurance Companies Act, 1912 made it mandatory that the premium fixed and periodical valuations of companies will have to be certified by an actuary. Yet, there were many anomalies between Indian and European companies and such discrimination had put the Indian companies at a disadvantage.

The first two decades of the twentieth century witnessed four-fold increase in the insurance business. The fleet of 44 companies with total business-in-force of ₹22.44 crore rose to 176 companies with total business-in-force of ₹298 crore in 1938. This period witnessed the entry of many financially unsound insurance companies which failed miserably and eventually fizzled out. The Insurance Act 1938 regulated and exercised strict control over both, life insurance as well as non-life insurance. There was constant clamour about nationalizing life insurance industry but the demand gathered thrust in 1944 when a bill in this regard i.e., to amend the Life Insurance Act 1938, was put forward in the Legislative Assembly. Finally, life insurance in India was nationalized on the 19th of January 1956. The insurance industry at the time of nationalisation comprised of about 154 Indian insurance companies, 16 non-Indian companies and 75 provident companies. The execution of nationalization was done in two phases; initially the government took over the control of the management through an Ordinance, and later, the ownership was also transferred by means of a comprehensive bill. The Indian Parliament passed the Life Insurance Corporation Act on the 19th of June 1956, and the Life Insurance Corporation of India was created on 1st September 1956, with the objective of enhancing the reach of life insurance to all insurable persons in the country including the rural areas thereby providing them adequate financial cover at a reasonable cost.

In 1956, apart from its corporate office, LIC had 5 zonal offices, 33 divisional offices and 212 branch offices. Considering the fact that life insurance contracts are long-term contracts and various services to the policy holders may have to be served during the tenure of the policy, it was decided to expand the operations and place a branch office at each district headquarter. This led to restructuring within LIC and opening up of numerous branch offices across the country. The restructuring process resulted in the branch offices being made service points and also functions as accounting units. A visible improvement in the performance of LIC was marked after the restructuring took place. However, it took a little over ten years and only in 1969-70, the business volume crossed the 1000.00 crores

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from that of around 200.00 crores in 1957. Another ten years down the line, the business touched the 2000.00 crore mark. By the mid-eighties i.e., by 1985-86 LIC's sum assured on new policies crossed 7000.00 crore.

Today, LIC functions with 2048 fully computerized branch offices, 113 divisional offices, 8 zonal offices, 1381 satellite offices and the corporate office. LIC's Wide Area Network covers 113 divisional offices and connects all the branches through a Metro Area Network. Meanwhile, LIC has also had a tie up with some banks and service providers to offer on-line premium collection facility in selected cities. LIC has added ECS and ATM premium payment facility to facilitate the customers and enhance their convenience. Online Kiosks, IVRS, and Info Centres have been commissioned in various cities like Mumbai, Ahmedabad, Bangalore, Chennai, Hyderabad, Kolkata, New Delhi, Pune etc.

Satellite Sampark offices were launched in many cities with the objective of providing easy access to its policyholders. Smaller and leaner in size, the satellite offices are closer to the customer and are more accessible. It is expected that the digitized database maintained at the satellite offices will facilitate anywhere servicing and many other conveniences in the future. With all these efforts bearing results, LIC continues to be the dominant life insurer even in the liberalized scenario of the Indian insurance sector and is moving fast on a new growth trajectory surpassing its own past records.

11.2.3 Timeline of the Life Insurance Business in India

- 1818: Oriental Life Insurance Company, the first life insurance company on Indian soil began functioning.
- 1870: Bombay Mutual Life Assurance Society, the first Indian life insurance company started its business.
- 1912: The Indian Life Assurance Companies Act enacted as the first statute to regulate the life insurance business.
- 1928: The Indian Insurance Companies Act enacted to enable the government to collect statistical information about both life and non-life insurance businesses.
- 1938: Earlier legislation consolidated and amended to by the Insurance Act with the objective of protecting the interests of the insuring public.
- 1956: 245 Indian and foreign insurers and provident societies are taken over by the central government and nationalised. LIC formed by an Act of Parliament, viz. LIC Act, 1956, with a capital contribution of ₹ 5 crore from the Government of India.

11.2.4 Timeline of the Life Insurance Business in India

- 1850: Triton Insurance Company Ltd., the first general insurance company established in the year 1850 in Calcutta by the British.

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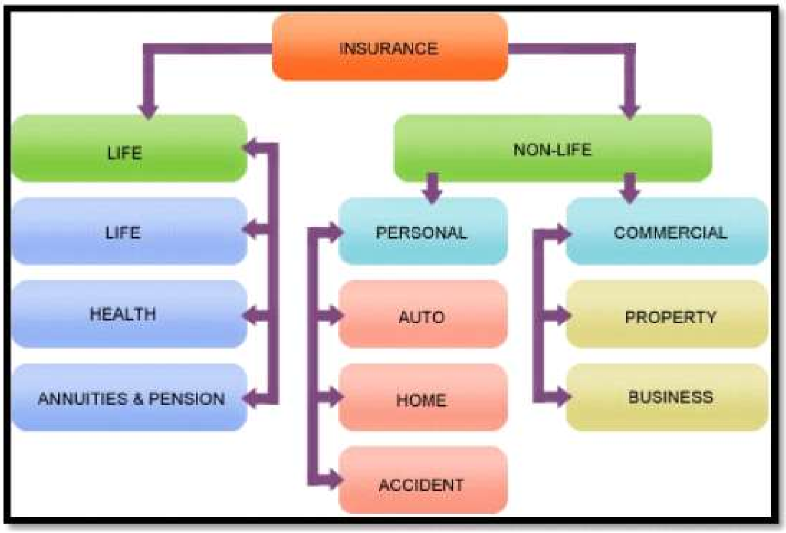
- 1907: The Indian Mercantile Insurance Ltd. Set-up, the first company to transact all classes of general insurance business.
- 1957: General Insurance Council, a wing of the Insurance Association of India, frames a code of conduct for ensuring fair conduct and sound business practices.
- 1968: The Insurance Act amended to regulate investments and set minimum solvency margins and the Tariff Advisory Committee set-up.
- 1972: The General Insurance Business (Nationalisation) Act, 1972 nationalised the general insurance business in India with effect from 1st January 1973. 107 insurers amalgamated and grouped into four companies viz. the National Insurance Company Ltd., the New India Assurance Company Ltd., the Oriental Insurance Company Ltd. and the United India Insurance Company Ltd. GIC incorporated as a company.

11.2.5 Insurance Sector in India

The insurance sector happens to be one of the booming sectors of the Indian economy and is growing at the rate of 15-20 per cent per annum. Along with the banking industry, it contributes to about 7 per cent of the country's GDP. Insurance is a federal subject in India and the insurance industry in India is governed by the Insurance Act, 1938, the Life Insurance Corporation Act, 1956 and General Insurance Business (Nationalisation) Act, 1972, Insurance Regulatory and Development Authority (IRDA) Act, 1999, Consumer Protection Act,1986 and other related Acts.

Types of Insurance



With liberalization, the insurance sector felt the need of reforms that would enable the government sector companies to face the challenges posted by the private and foreign insurance companies and also improve the sectoral performance. Malhotra Committee, headed by former Finance Secretary and RBI Governor R.N. Malhotra was formed in 1993 to suggest insurance sector reforms which were initiated in 1993. The task entrusted to the committee was to appraise the current state of the Indian insurance industry and recommend steps regarding its future journey that would work in tandem and compliment the financial sector reforms.

The following were the Key Recommendations of Malhotra Committee:

1. Structure

- The stake of the government in the insurance companies should be reduced to 50 per cent.
- The government should take over the holdings of GIC and its subsidiaries to enable them to act as independent corporations.
- Greater liberty should be given to the insurance companies for operation.

2. Competition

- Private companies with a minimum paid up capital of ₹1billion should be permitted to enter the industry.
- Both life and general insurance products should not be dealt by a single entity of a company.
- Foreign companies may be permitted to enter the industry in partnership with the domestic companies. Postal Life Insurance should be allowed to operate in the rural areas of the country.
- Only one State Level Life Insurance Company should be allowed to operate in each state.

3. Regulatory Body

- The Insurance Act should be amended from time to time.
- An Insurance Regulatory body should be established.
- Controller of Insurance should be made independent of any governing body.

4. Investments

- Mandatory investments of LIC Life Fund in government securities should be reduced from 75 per cent to 50 per cent.
- GIC and its subsidiaries should not hold more than 5 per cent in any company.
- LIC of India should pay interest on delays in payments beyond 30 days.
- Insurance companies must devise unit linked pension plans.
- Application of latest technology tools and application should be implemented in this industry.

In addition, Malhotra Committee also powerfully recommended the establishment of an independent regulatory body — The Insurance Regulatory and Development Authority (IRDA) with the objective of providing more autonomy to insurance companies. This measure would help them to prove their performance and also act as independent companies with economic interests.

11.2.6 Liberalization of Insurance Sector

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Liberalization of the insurance sector in India was initiated in March 2000 when the Insurance Regulatory and Development Authority (IRDA) Bill was passed. The bill lifted all entry barriers for private players. Moreover, the foreign insurance players were allowed to enter the market, albeit with some limits on direct foreign ownership. After years of debate, the Indian government increased the Foreign Direct Investment (FDI) limit in insurance companies to 74 per cent against the current 49 per cent. An announcement in this regard has been made in the recent Union Budget 2020-21. The opening up of the insurance sector has led to rapid growth of the sector. Currently, the Indian insurance industry has 58 insurance operators, out of which 24 are life insurance companies and 34 are non-life insurance companies in the market. The Indian life insurance market has large untapped pools which measure up to almost 80 per cent. The health insurance and non-life insurance market holds more potential and is more inviting as the market continues to be well below international standards. The liberalization and the reforms backed up by robust regulatory framework, positive business environment and economic growth, threw open the Indian insurance sector to competition in 2000 and it has continued to evolve since then. All the growth factors are well-placed today for the sector to develop into one of the fastest growing financial services markets in the world. The demand is boosted due to the rising income levels, higher awareness and varied needs of the increasingly sophisticated consumers that have compelled the players to come-up with customized products.

11.3 LIFE INSURANCE CORPORATION OF INDIA (LIC)

Let us study about the vision, mission, objectives, functions and role of LIC.

11.3.1 Vision and Mission

Vision

"A trans-nationally competitive financial conglomerate of significance to societies and Pride of India."

Mission

Its mission to ensure and improve the quality of life of the general public by providing financial security through the medium of financial products and services promising decent returns and contributing towards economic prosperity of the country.

11.3.2 Objectives of Life Insurance Corporation

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The following are the objectives of LIC of India.

i. The life insurance service should reach the rural areas along with the social and backwards areas with the objective of increasing the customer base and ensuring the reach of insurance across the country.
ii. Motivate people to invest in insurance-linked savings by making them attractive.
iii. Bear in mind, in the investment of funds, the primary obligation to its policyholders, whose money it holds in trust, without forgetting about the interest of the community as a whole. It must ensure to use the funds with the sole objective of furthering the economic prosperity of the country and its people.
iv. It must conduct business in the most judicious manner and with the full realization that the moneys belong to the policyholders.
v. It should act as trustee of the insured public in their individual and collective capacities.
vi. It should be capable enough of meeting the changing needs of the general public in terms of the dynamic socio-economic environment.
vii. It should ensure that the employees of the Corporation are working in their best capacity and delivering excellent service to the country and its people.
viii. Promote amongst all agents and employees of the Corporation a sense of participation, pride and job satisfaction through discharge of their duties with dedication towards achievement of the objectives of the Corporation.

11.3.3 Functions and Role of the Life Insurance Corporation of India

As per Chapter III, Section 6 of the Life Insurance Corporation Act, 1956 the functions of Life Insurance Corporation of India, which also defines its role are the following:

(1) Subject to the rules, if any, made by the Central Government in this behalf, it shall be the general duty of the Corporation to carry on life insurance business, whether in or outside India, and the Corporation shall so exercise its powers under this Act as to secure that life insurance business is developed to the best advantage of the community.

(2) Without prejudice to the generality of the provisions contained in sub-section (1) but subject to the other provisions contained in this Act, the Corporation shall have power-

  (a) to carry on capital redemption business, annuity certain business or reinsurance business in so far as such reinsurance business appertains to life insurance business.

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(b) subject to the rules, if any, made by the Central Government in this behalf, to invest the funds of the Corporation in such manner as the Corporation may think fit and to take all such steps as may be necessary or expedient for the protection or realisation of any investment; including the taking over of and administering and property offered as security for the investment until a suitable opportunity arises for its disposal;

(c) to acquire, hold and dispose of any property for the purpose of its business.

(d) to transfer the whole or any part of the life insurance business carried on outside India to any other person or persons, if in the interests of the Corporation it is expedient so to do.

(e) to advance or lend money upon the security of any movable or immovable property or otherwise;

(f) to borrow or raise any money in such manner and upon such security, as the Corporation may think fit;

(g) to carry on either by itself or through any subsidiary any other business in any case where such other business was being carried on by a subsidiary of any insurer whose controlled business has been transferred to and vested in the Corporation under Act;

(h) to carry on any other business which may seem to the Corporation to be capable of being conveniently carried on in connection with its business and calculated directly or indirectly to render profitable the business of the Corporation;

(i) to do all such things as may be incidental or conducive to the proper exercise of any of the powers of the Corporation.

(3) In the discharge of any of its functions, the Corporation shall act so far as may be on business principles.

Check Your Progress

1. Name the first insurance company established in India.
2. When was life insurance in India nationalized?
3. What task was entrusted to the Malhotra Committee formed in 1993?

11.4 THE GENERAL INSURANCE CORPORATION OF INDIA (GIC)

The General Insurance Corporation (GIC) was constituted by the Government of India in 1972. With effect from 1 January 1973 the erstwhile 107 Indian and foreign insurance companies who were operating in the country prior to nationalisation, were grouped into four operating companies, namely,

i. National Insurance Company Limited
ii. New India Assurance Company Limited
iii. Oriental Insurance Company Limited
iv. United Insurance Company Limited

With head offices at Kolkata, Mumbai, New Delhi and Chennai, respectively GIC which was the holding company of the four public sector general insurance companies has since been delinked from the later and has been approved as the 'Indian Reinsurer' since 3rd November 2000. All the four entities are government companies registered under the Companies Act.

11.4.1 Brief History of General Insurance

The nationalization of the general insurance sector in India was executed through the implementation of the General Insurance Business (Nationalisation) Act, 1972 (GIBNA). Through nationalisation, the Government of India (GOI) acquired the shares of 55 Indian insurance companies in addition to the undertakings of 52 insurers carrying on general insurance business.

The General Insurance Corporation of India (GIC) was established in accordance of Section 9(1) of GIBNA and was incorporated on 22 November 1972 under the Companies Act, 1956 as a private company limited by shares. With the inception of GIC, GOI transferred all the shares it held of the general insurance companies to GIC.

GIC was formed for the purpose of supervising, controlling and carrying general insurance business in India.

Following the overhauling of the Indian insurance sector through mergers, the following four companies were left as fully owned subsidiary companies of GIC:

- National Insurance Company Limited
- The New India Assurance Company Limited
- The Oriental Insurance Company Limited
- United India Insurance Company Limited

The next phase of reforms in the insurance sector happened on 19th April 2000 with the implementation of the Insurance Regulatory and Development Authority Act, 1999 (IRDAA). The IRDA Act introduced certain amendments to GIBNA and the Insurance Act, 1938. Among the amendments made, exclusive privilege of GIC and its subsidiaries carrying on general insurance in India as per provisions of GIBNA was removed.

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In November 2000, GIC was renotified as the Indian Reinsurer. It marked the end of its supervisory role over the above named four subsidiaries.

With the General Insurance Business (Nationalisation) Amendment Act 2002 (40 of 2002) coming into force from 21 March 2003; GIC ceased to be a holding company of its subsidiaries. The ownership of the four erstwhile subsidiary companies and also of the General Insurance Corporation of India was vested with the Government of India.

11.4.2 Regulatory Framework

The functioning of GIC has to be within the regulations of the following major Acts:

- IRDAI Obligatory Cessions Gazette
- The Companies Act, 2013
- Insurance Act, 1938
- General Insurance Business (Nationalisation) Act, 1972
- General Insurance Business (Nationalisation) Amendment Act. 2002
- Insurance Regulatory and Development Authority Act, 1999
- Memorandum Articles of Association

11.4.3 Subsidiaries of GIC

1. GIC Re South Africa Ltd

GIC Re South Africa Ltd is a completely owned subsidiary of GIC Re. It was set-up by acquiring South African composite reinsurer Saxum Re in 2014 to fulfil the Reinsurance needs of the African continent, especially South Africa. The major objective of the company is underwriting business from the entire African continent except Egypt and Libya.

2. GIC Perestrakhovanie LLC, Russia

Russia is a 100 per cent subsidiary of GIC Re which was set-up on 14 November 2018 and got the license to transact reinsurance business on 30 January 2020. The primary focus of GIC Perestrakhovanie LLC is to underwrite business in all classes of reinsurance in areas such as Russia and former Soviet Union countries, namely, Armenia, Azerbaijan, Belarus, Georgia, Kazakhstan, Kyrgyzstan, Moldova, Tajikistan, Turkmenistan, Ukraine and Uzbekistan.

3. GIC Re, India, Corporate Member Ltd

As part of its involvement in global business scenario, GIC Re has been providing capacity to Lloyd's syndicates through quota share capital gearing treaties since

2011. As a capacity provider, since GIC Re was required to have its own Corporate Membership at Lloyd's, GIC Re took over I-CAT CCM TEN Ltd, an existing Corporate Member company, in December 2013 and renamed it as GIC Re, India, Corporate Member Ltd, which is registered as a private limited company in the UK and 100 per cent owned subsidiary of GIC Re. The acquisition has the authorization of the Ministry and IRDA.

4. GIC Housing Finance

GIC Housing Finance Limited (GICHFL) was integrated as 'GIC GrihVitta Limited' on 12 December 1989. It was renamed through a fresh Certificate of Incorporation issued on 16 November 1993. GICHFL's primary objective is that of granting housing loans to individuals and to persons/entities engaged in the construction of houses/flats for residential purposes.

GICHFL is promoted by the General Insurance Corporation of India and its former subsidiaries namely, National Insurance Company Limited, The New India Assurance Company Limited, The Oriental Insurance Company Limited and United India Insurance Company Limited.

11.4.4 Vision, Mission and Core Values of GIC

Vision

Its vision is to be a pioneer in global reinsurance and risk solution provider.

Mission

- Building long-term mutually beneficial collaboration with business partners.
- Conducting business in a fair and just manner
- Application of 'state-of-art' technology, processes including enterprise risk management and creative solutions.
- Developing and retaining highly motivated professional team of employees.
- Focus on earning profit and enhancing the financial position as per the global scenario.

Core Values

- Trust and mutual respect
- Professional excellence
- Integrity and Transparency
- Commitment
- Responsive Service

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11.4.5 Objectives of General Insurance Corporation of India

Objective of the GIC

- To execute the general insurance business other than promoting life insurance products and services.
- To aid and motivate the subsidiaries to conduct the insurance business and
- To assist the subsidiaries in executing the investment strategies in an efficient manner.

11.4.6 Role and Functions of GIC

- Executing any part of the general insurance, if it is desirable to do so.
- Assisting and advising the acquiring companies in matters of devising the standards of conduct and sound practice in general insurance business.
- Rendering efficient services to policy holders of general insurance.
- Advising the acquiring companies in area of expenditure including the payment of commission and other expenses.
- Advising the acquiring companies in matters of investment.
- Issuing directives to the acquiring companies in relation to the conduct of general insurance business.

Issuing directions and encouraging competition among the acquiring companies in order to render their services more efficiently.

11.4.7 GIC's Business Activities

GIC's business activities can be categorized under Domestic, International and Overseas Offices.

1. Domestic

Being the sole reinsurer in the domestic reinsurance market, GIC Re provides reinsurance to the direct general insurance companies in the Indian market. GIC Re receives statutory cession of 5 per cent on each and every policy subject to certain limits. It leads many of domestic companies' treaty programmes and facultative placements. GIC Re's capacity for each class of business on Treaty and Facultative basis for domestic business is provided in the following table:

Class	Capacity
Property	INR 15000 million. Any one risk
Energy	USD 150 million per risk
Marine	Hull - \$ 125 million. any one vessel
	Cargo \$ 125 million. Any one policy/sending
Engineering	INR 15000 million. Sum Insured

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Miscellaneous	INR 2500 million. Sum Insured
Liability	INR 2500 million per occurrence
Spares	INR 250 million.
Health	INR 2500 million.
Agriculture/Weather	INR 4,000 crores on Sum Insured/PML basis.
Insurance (Domestic)	INR 35 Crores (Facultative)
Motor & Workmen Compensation	INR 100 Crores (Treaty)

Aviation

	Hull	Liability
Airlines	US $ 35 Mln	US $ 200Mln
General Aviation	US$ 30 Mln	US$ 200 Mln
Treaty - Proportional	US $ 4Mln in any one Treaty	
Treaty- NonProportional	US$ 12 Mln Any One Programme	

2. International

GIC Re has spread its wings to develop as an active reinsurance solutions partner for the Afro-Asian region and is currently leading the reinsurance programmes of several insurance companies in the SAARC countries, South East Asia, Middle East and Africa. In pursuit of providing quality service, easy accessibility and customised reinsurance solutions, GIC has opened liaison/ representative/ branch / subsidiary offices in UK, Russia, UAE, Malaysia, South Africa and Brazil. It also offers an offshore branch in GIFT City, Gujarat. GIC provides following capacities for Treaty and Facultative business on risk emanating from the international market based on merits of the business:

Property

Type	On PML Basis	Sum Assured
Facultative	US $ 20 million	US $ 50 million
Treaty	US $ 4 million	US $ 10 million

Marine Hull, Cargo & Offshore Energy (per risk)

Type	Cargo	Hull	Energy
Facultative	$ 20 million	$ 20 million	$ 150 million
Treaty	$ 20 million	$ 20 million	$ 20 million

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Aviation

	Hull	Liability
Airlines	**US** $ 17 Mln	**US** $ 150 Mln
General Aviation Int (other than SAARC)	US$ 7.5 Mln	US$ 75 Mln
General Aviation SAARC	**US** $ 30 Mln	**US** $ 200 Mln
Treaty- Proportional	US$ 4 Mln Any One Treaty	
Treaty Non-Proportional	**US** $ 12 Mln any one programme	

Liability

Type	Limit of Liability basis (Claims made basis covers)
Facultative	US $ 10 million
Treaty Proportional	US $ 6 million
Non-Proportional	US $ 8 million

Miscellaneous

Type	Miscellaneous	S I Basis
Facultative	US $ 20 million	US $ 50 million
Treaty	US $ 4 million	US $ 10 million

Motor (S I)

Type	Motor
Facultative	US $ 5 million
Treaty	US $ 10 million

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Life

Type	Capacity offered
Proportional	250 million/ US \$ 5 million per person
Non-proportional	750 million / US \$ 15 million per treaty

Agriculture/Weather Insurance

Type	Capacity offered
Agriculture/Weather Insurance (Foreign)	USD 50 mln on Sum Insured basis and USD 25 mln on PML basis

3. Overseas Offices

GIS has the following overseas offices:

- GIC Re - Dubai Branch
- GIC Re- Malaysia Branch
- GIC Re - UK, London Branch
- GIC of India- Dubai Branch

Classes of Reinsurance Business	Types
Property	Treaty
Casualty	Facultative
Marine	
Energy	

The areas of operation in the middle-east region cover Bahrain, Cyprus, Iran, Iraq, Jordan, Kuwait, Lebanon, Oman, Palestine, Qatar, Saudi Arabia, Syria, United Arab Emirates, Yemen, Algeria, Egypt, Libya, Morocco, Sudan and Tunisia.

Check Your Progress

4. When was the General Insurance Corporation (GIC) established in India?
5. Name the major Acts which regulate the functioning of GIC.

11.5 THE ROLE OF INSURANCE IN INDUSTRIAL DEVELOPMENT

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The growth and development of the insurance sector in our country in the past few decades has significantly contributed to industrial development as well. The expansion of the insurance sector has been able to mobilize savings of the general public towards economic growth by opening various avenues of investment for the general public. The insurance sector has led to economic development by providing insurance cover to greater section of the population and business enterprises throughout the country.

Moreover, liberalization of the Indian economy opened opportunities for the insurance sector as well. Indian witnessed the entry of new players in the insurance sector leading to general of employment. The growth of GDP of the country effectively contributes to the expansion of trade and commerce as well. Every bank which provides loan needs to check the insurance cover of the assets being purchased.

The insurance industry provides financial stability to the economy by insuring the losses and risks involved in the purchase of assets, goods or setting up of industries and business houses.

11.6 ANSWERS TO CHECK YOUR PROGRESS QUESTIONS

1. Oriental Life Insurance Company was the first insurance company established in India.
2. Life insurance in India was nationalized on the 19th of January 1956.
3. Malhotra Committee, headed by former Finance Secretary and RBI Governor R.N. Malhotra was formed in 1993 to suggest insurance sector reforms. The task entrusted to the committee was to appraise the current state of the Indian insurance industry and recommend steps regarding its future journey that would work in tandem and compliment the financial sector reforms.
4. The General Insurance Corporation (GIC) was constituted by the Government of India in 1972.
5. The functioning of GIC has to be within the regulations of the following major Acts:
   - IRDAI Obligatory Cessions Gazette
   - The Companies Act, 2013
   - Insurance Act, 1938

- General Insurance Business (Nationalisation) Act, 1972
- General Insurance Business (Nationalisation) Amendment Act. 2002
- Insurance Regulatory and Development Authority Act, 1999
- Memorandum Articles of Association

NOTES

11.7 SUMMARY

- The term 'insurance' has different facets and can be differently defined, both financially and legally. The financial aspect focuses on the funding for ensuring financial security against a probable mishap whereas the legal aspect deals with provisions relating to a legally enforceable contract.
- From the legal aspect, insurance may be referred to as a contract between two parties during which one party accepts to take guarantee of any financial loss suffered by other party, in consideration of a sum of money, on the happening of a specified event; for example, fire, accident or death.
- The modern concept of life insurance came to India from England in 1818. The first life insurance company on Indian soil, namely, Oriental Life Insurance Company was started in Kolkata (then Calcutta) by the Europeans.
- The first two decades of the twentieth century witnessed four-fold increase in the insurance business. The fleet of 44 companies with total business-in-force of ₹22.44 crore rose to 176 companies with total business-in-force of ₹298 crore in 1938.
- Satellite Sampark offices were launched in many cities with the objective of providing easy access to its policyholders. Smaller and leaner in size, the satellite offices are closer to the customer and are more accessible.
- The insurance sector happens to be one of the booming sectors of the Indian economy and is growing at the rate of 15-20 per cent per annum. Along with the banking industry, it contributes to about 7 per cent of the country's GDP.
- With liberalization, the insurance sector felt the need of reforms that would enable the government sector companies to face the challenges posted by the private and foreign insurance companies and also improve the sectoral performance.
- Liberalization of the insurance sector in India was initiated in March 2000 when the Insurance Regulatory and Development Authority (IRDA) Bill was passed. The bill lifted all entry barriers for private players.
- The liberalization and the reforms backed up by robust regulatory framework, positive business environment and economic growth, threw open the Indian insurance sector to competition in 2000 and it has continued to evolve since then.

- The General Insurance Corporation (GIC) was constituted by the Government of India in 1972.
- With head offices at Kolkata, Mumbai, New Delhi and Chennai, respectively GIC which was the holding company of the four public sector general insurance companies has since been delinked from the later and has been approved as the 'Indian Reinsurer' since 3rd November 2000. All the four entities are government companies registered under the Companies Act.
- The General Insurance Corporation of India (GIC) was established in accordance of Section 9(1) of GIBNA and was incorporated on 22 November 1972 under the Companies Act, 1956 as a private company limited by shares. With the inception of GIC, GOI transferred all the shares it held of the general insurance companies to GIC.
- With the General Insurance Business (Nationalisation) Amendment Act 2002 (40 of 2002) coming into force from 21 March 2003; GIC ceased to be a holding company of its subsidiaries. The ownership of the four erstwhile subsidiary companies and also of the General Insurance Corporation of India was vested with the Government of India.
- GIC's business activities can be categorized under Domestic, International, Overseas Offices, Training / Risk Rating Systems and MGA.

11.8 KEY WORDS

- **Insurance:** It is a transfer of risk from the individual to the group and there is a sharing (pooling) of losses on some equitable basis such that unexpected losses can be guaranteed.
- **Satellite Sampark offices:** These were launched by LIC in many cities of the country with the objective of providing easy access to its policyholders. Smaller and leaner in size, the satellite offices are closer to the customer and are more accessible.
- **Foreign Direct Investment (FDI):** It is an investment made by a company or an individual in one country into business interests located in another country. FDI significantly contributes to the economic growth of a country.

11.9 SELF ASSESSMENT QUESTIONS AND EXERCISES

Short-Answer Questions

1. Define 'insurance' from the financial and legal perspective.
2. Write a short note on the nature of insurance.

3. List the various types of insurance.
4. Mention the impact of liberalization on the Indian insurance sector.
5. Briefly mention the history of general insurance in India.
6. What is the role of GIC?

Long-Answer Questions

1. Discuss the history of insurance in India.
2. Examine the key recommendations of Malhotra Committee constituted in 1993.
3. Explain the functions and role of the Life Insurance Corporation of India.
4. Describe the vision, mission and objectives of GIC.
5. Explain the business activities of GIC.

11.10 FURTHER READINGS

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NOTES

BLOCK - IV
CRISIL AND CARE

UNIT 12 CREDIT RATING AGENCIES IN INDIA: CREDIT RATING INFORMATION SERVICES OF INDIA LIMITED (CRISIL)

Structure

12.0 Introduction
12.1 Objectives
12.2 Credit Rating Agencies
  12.2.1 Benefits of Credit Rating
  12.2.2 Rating Methodology
12.3 Credit Rating Agencies in India
12.4 Credit Rating Information Services of India Limited (CRISIL)
  12.4.1 Vision, Mission and Core Values
  12.4.2 Chronological timeline of CRISIL
  12.4.3 CRISIL's Rating Process
  12.4.4 CRISIL Credit Rating Scales
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12.5 Answers to Check Your Progress Questions
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12.0 INTRODUCTION

Credit rating is the assessment of the borrower's credit quality. It performs the function of credit risk evaluation reflecting the borrower's capability to repay the debt as per the terms of the issue. Credit rating is merely an indicator of the current opinion of the relative capacity of a borrowing entity to meet its debt obligations within a specified time period and with particular reference to the debt instrument being rated. Credit rating serves as a valuable input in the decision-making process of the various investors and regulators. The primary objective of rating is to provide guidance to investors / creditors in determining a credit risk associated with a debt instrument.

Credit Rating Information Services of India (CRISIL) happens to be the pioneer in India's credit rating business, as it was the first credit rating agency to be established in India. With time, CRISIL has expanded the rating process to various industrial sectors and has also tied-up with global rating agencies like S&P, which has not only improved its operational efficiency but also enabled the agency to operate in foreign countries. The unit focusses on the benefits of credit ratings to different concerned parties and also the factors assessed during the rating process.

12.1 OBJECTIVES

After going through this unit, you will be able to:

- Describe the concept of credit rating
- Identify the variables assessed during the credit rating process
- Explain the inception and progress of CRISIL
- Discuss the probable shortcomings that may affect the fairness of a credit rating

12.2 CREDIT RATING AGENCIES

A **credit rating agency** (**CRA)**, which is also referred to as a **ratings service,** is a company that assigns credit ratings. This agency assesses the entity's creditworthiness or rate a debtor's ability to pay back debt by timely repayment of the principal and interest and the probability of default. An agency usually rates the creditworthiness of issuers of debt obligations, of debt instruments, and in some cases, of the servicers of the underlying debt, but not of individual consumers.

The financial instruments that are rated by the rating agencies vary across the spectrum from government bonds, corporate bonds, Certificate of Deposits, municipal bonds, preferred stock, to collateralized securities, such as mortgage-backed securities and collateralized debt obligations.

CRISIL can boast to be the pioneer in the rating services in India, as the very activity of rating debt instruments started with the incorporation of the Credit Rating Information Services of India Ltd. (CRISIL) in 1987, which later started rating companies in 1987-88.

CRISIL was promoted by the leading financial institutions such as ICICI and Unit Trust of India (UTI) and it established its headquarters in Mumbai. India became the first country among the developing countries of that period to boast of setting up a credit rating agency. Gradually, CRISIL got associated with a globally renowned rating agency— Standard and Poor's (S&P) in 1996 and carved a niche for itself on the global rating platform.

It is to be noted that after the establishment of CRISIL, the second rating agency to be established in India was ICRA in 1991. ICRA was promoted by the Industrial Finance Corporation of India (IFCI) and other esteemed financial institutions and banks. ICRA has been associated with Moody's Investors Services which is a globally renowned rating agency.

In the year 1993 another well-known credit rating agency was established in India known as CARE—it stands for Credit Analysis and Research Limited. Another rating agency Onicra Credit Rating Agency of India Limited was established in 1993. Furthermore, Duff and Phelps Credit Rating (India) Private Ltd. (DCR) was set-up in 1996. However, it is now known as Fitch Ratings India Private Limited.

In 2005 SME Rating Agency of India Limited (SMERA) was established. This rating agency was a collaboration of SIDBI, Dun & Bradstreet Information Services (D&B), Credit Information Bureau of India Limited (CIBIL), and 11 other significant banks in the country. The distinguishing of this rating agency is that it focusses solely on the SME sector of the country. Another rating agency Brickwork Ratings (BWR) was established in 2007 with its headquarters in Bangalore.

However, it is worth noting that CRISIL (Standard & Poor), ICRA (Moody's), CARE and Fitch, and Brickwork Ratings are recognized by SEBI.

12.2.1 Benefits of Credit Rating

A. for Investors

- It enables investors to get superior information at low cost.
- It helps investors to take investment decisions.
- It encourages common man to invest his savings in corporate securities and get high returns.

B. for Corporate Borrowers

- It facilitates companies with good rating to enter the capital market.
- It is used as a marketing tool.
- It facilitates foreign collaborations.

C. for Government

- It helps in channelizing public savings for productive uses.
- It facilitates formulation of public policy guidelines on institutional investments.
- It facilitates investor's protection without putting that burden on the government.

12.2.2 Rating Methodology

In India, the rating exercise begins at the behest of the company. A rating is applicable to a specific debt obligation of the company and is not an evaluation of the entire performance of the company as a whole. The emphasis of evaluation is entirely on the ability of the company to meet its financial obligation in within the stipulated period.

The rating of an instrument needs a thorough analysis of the parameters that impact the credit worthiness of the issuer. The methodology comprises an analysis of the past performance of the company and an evaluation of its future prospects, which involves judgement of the company's competitive position and evaluation of its management and strategies.

The primary factors that are measured while rating a financial instrument are the following:

1. Business Analysis

- o It analyses the industry risk by judging parameters such as government policies, nature of competition and so forth.
- o It analyses the market position of the company within the industry by judging parameters such as market share, competitive advantage and so forth.
- o It analyses the operating efficiency of the company by judging parameters such as advantage of location, factors such as labour and cost.
- o It analyses legal position of the company by judging parameters such as terms of prospectus, trustees and their relationship.

2. Financial Analysis

- o It analyses the accounting quality of the company by judging parameters such as valuation of inventory and statement of profit & loss.
- o It analyses the future earning prospects of the company by judging parameters such as profitability ratios and so forth.
- o It analyses adequacy of cash flows by judging parameters such as working capital management and sustainability of cash flows.
- o It analyses the financial flexibility by judging parameters such as the ability to raise funds and financial plans.

3. Management Evaluation

- o This involves evaluating the past performance of the company.
- o It evaluates the alternate action plans of the company to confront any kind of challenging business situation.
- o It analyses the mission, vision and objectives of the company.

4. Fundamental Analysis

- o This analyses includes judging the capital adequacy of the company through an assessment of its net worth.
- o It evaluates the asset quality of the company by judging parameters such as quality of credit-risk management and systems for monitoring credit.
- o It evaluates liquidity management of the company by judging parameters such as capital structure and cash management.
- o It analyses the financial position of the company in the market.
- o It analyses interest and the adaptability of the company while being exposed to changes in interest rate and hedging.

12.3 CREDIT RATING AGENCIES IN INDIA

The various credit rating agencies in India are as follows:

1. CRISIL

CRISIL began operating in India in 1987. The company has established offices in eight countries of the world including India. However, its headquarters is in Mumbai.

The company provides services such as ratings, analytics, solutions and research with a very good track record of innovation and growth. It is to be noted that Standard and Poor's is the primary shareholder of CRISIL.

2. ICRA

ICRA was the second rating agency in India and was established in 1991. It is a public limited company with its head office in New Delhi. Moody's is the primary shareholder of ICRA.

3. CARE

CARE was the third Indian rating agency to come up in the year 1993. It has its head office in Mumbai and it happens to be India's second largest credit rating agency. It is one of the five partners of international rating agency called ARC Ratings.

Conclusion

The ratings assigned by these credit rating agencies after extensive analysis provide a potential investor with valuable insights regarding imminent risk associated with the related debt instruments and also its creditworthiness. This actually simplifies investment related decision-making.

CRAs registered with SEBI

Name of the CRA	Year of Commencement of Operations
CRISIL	1988
ICRA	1991
CARE	1993
FITCH INDIA	1996
SMERA	2005
BRICKWORKS	2008

12.4 CREDIT RATING INFORMATION SERVICES OF INDIA LIMITED (CRISIL)

The Credit Rating Information Services of India Limited (CRISIL) is the first rating agency in India and was established in 1987 by the Industrial Credit and Investment Corporation of India Limited (ICICI) and Unit Trust of India (UTI).

The main focus areas of CRISIL are ratings and risk assessment, research and advisory. CRISIL is a leading credit rating agency and the only credit rating agency in India which delivers sectoral specialization. CRISIL provides rating and risk assessment services to manufacturing companies, banks, Non-banking financial companies, financial institutions, housing finance companies, municipal bodies and companies in the infrastructure sector. It also rates long-term instruments such as debentures, bonds, preference shares, structured obligations, fixed deposits, commercial papers and short-term deposits.

It makes credit assessments of various institutions such as state governments and subsidiaries and joint ventures of multinationals. It also delivers ratings of financial force to insurance companies. CRISIL has devised several structured ratings for MNCs based on guarantees and letters of comfort from the parent companies and standby letter of credit arrangements from bankers. CRISIL's its rating provides direction to the investors with regards to certainty of timely payment of interest and principal on a particular debt instrument.

12.4.1 Vision, Mission and Core Values

Vision

The company desires to be a pioneer in providing innovative analyses on a global platform.

Mission

Its mission is to provide valuable perspective, insights and effective resolutions so that the business markets can function with greater flexibility.

Core Values

- *Integrity:* The company is absolutely trustworthy in its actions and thinking. It offers analyses and solutions which are unique, reliable and unbiased.
- *Excellence*: The company always aims towards excellence while delivering solutions and analyses so that accurate decisions can be taken which reduce the hazards as well. *Accountability:* The company is fully responsible for its actions and takes complete onus for the solutions and opinions provided to its clients.
- *Teamwork:* The company believes in the spirit of teamwork. Hence, it ensures that every member of the team works together in designing the solutions and adding value to the whole experience.
- *Respect:* The company treats all the associated entities namely, stakeholders, customers and colleagues with equal trust and respect.

12.4.2 Chronological timeline of CRISIL

- *1987: Incorporation of CRISIL*

  CRISIL, India's first credit rating agency, promoted by the erstwhile ICICI Ltd along with UTI and other financial institutions, was incorporated in the year 1987.
- *1990: CRISIL launches CRISILCARD*

  'CRISILCARD Service', aimed at providing information and analytical opinion on India's corporate entities was launched by CRISIL.
- *1992: CRISIL sets footprint globally*

  CRISIL offers technical assistance and training to help set-up Malaysian Rating Corporation Berhad (MARC), and Israeli securities rating company S&P MAALOT.
- *1993: CRISIL goes public*

  CRISIL's IPO got an overwhelming response when it got oversubscribed by 2.47 times even when its 20,00,000 shares were sold at a premium of ₹40 per share.
- *1995: CRISIL500 Equity Index is launched*

  CRISIL500 Equity Index, designed to help investors track stock price movements, developed by CRISIL in partnership with National Stock Exchange of India Ltd. (NSEIL), was launched.
- *1996: Business alliance with S&P*

  With an eye on improving the skill set, CRISIL enters into a strategic alliance with Standard & Poor's (S&P) Ratings Group.

- *1997: S&P acquires 9.68 per cent stake in CRISIL*

  S&P acquires a 9.68 per cent stake in CRISIL on 8 May 8 1997. CRISIL gets an image makeover through the alliance with S&P which happens to be the world's leading rating agency and it adds a new dimension to CRISIL's methodologies. CRISIL gets a global exposure through S&P's rating processes.

- *1998: CRISIL sets up IISL*

  CRISIL sets up India Index Services Ltd (IISL), a joint venture with NSEIL. It provided a variety of indices and index related services and products to India's capital markets.

- *1999: RAM becomes banking industry standard*

  CRISIL's Risk Assessment Model (RAM) which focuses on banks' risk management practices becomes the banking industry standard. RAM's amplified regulatory focus acts as a personalized credit rating model for the banks.

- *2000: CRISIL acquires INFAC*

  On 15th March, CRISIL acquires the brand INFAC of Information Products and Research Services (India) Pvt. Ltd. Given INFAC's proficiency in financial research, CRISIL's research business was strengthened and made it India's leading provider of integrated research.

- *2000: CRISIL Composite Performance Ranking)CRISIL-CPR) launched*

  CRISIL Composite Performance Ranking (CRISIL-CPR) was launched by CRISIL to provide performance evaluation standards and investment decision support to mutual fund houses, distributors and investors.

- *2001: Global Data Services set-up*

  CRISIL sets up its first subsidiary, Global Data Services of India Ltd. that worked on standardising various financial data published for analytical purpose.

- *2002: CRISIL MarketWire is launched*

  MarketWire - providing real-time financial news was aimed to provide assistance to clients to make pricing and investment related decisions.

- *2002: CCER is set-up*

  The Centre for Economic Research (CCER) was set-up to apply economic principles to live business situations. This would help to study the market response to real life business environment.

- *2003: Integrated risk management solutions by CRISIL*

  With the aim to provide integrated risk management solutions and advisories, CRISIL sets up a group solely focusing on investment and risk management services.
- *2003: CRISIL acquires EconoMatters*

  The first overseas acquisition done by CRISIL; it acquires EconoMatters Ltd (later the Gas Strategies Group), a London-based company providing natural gas related consulting, information and training, and conference-organizing services.
- *2004: CRISIL invests in CariCRIS*

  CRISIL expands globally with an equity investment in the world's first regional rating agency, the Caribbean Information and Credit Rating Services Limited (CariCRIS).
- *2005: S&P acquires majority stake in CRISIL*

  Majority stake of CRISIL acquired by S&P.
- *2005: CRISIL acquired Irevna*

  The acquisition of Irevna, a leading global equity research and analytics company, marked CRISIL's second overseas acquisition. In the process, CRISIL added equity research to its working portfolio.
- *2005: CRISIL SME Ratings is launched*

  CRISIL, in order to serve the small and medium enterprises, launches Small and Medium Enterprise (SME) Ratings.
- *2006: CRISIL launches IPO grading*

  IPO grading services launched by CRISIL that provide investors with independent, dependable, and stable assessments of new public issues.
- *2007: CRISIL assigns first BLR*

  CRISIL assigns India's first Bank Loan Rating under the Reserve Bank of India's Basel-II related regulations.
- *2008: CRISIL Complexity Levels is launched*

  CRISIL launches Complexity Levels, an initiative to strengthen India's capital markets by providing greater transparency to investors.
- *2007: Real Estate Awards is launched*

  CRISIL's foray into other sectors continued with the launching of Real Estate Awards in association with CNBC AWAAZ. The award honours India's exemplary developers and builders.
- *2008: CRISIL's revenue crosses ₹ 5 bn*

  CRISIL's revenue crosses ₹5 billion in 2008.

- *2009: Irevna continues to dominate the research and analytical arena.*

  Irevna tops the global ranking as the No. 1 Investment Research and Analytics Outsourcing Firm by *The Black Book of Outsourcing*.
- *2009: CRISIL captured half of BLR market*

  Around half of India's bank loan rating market share is captured by CRISIL.
- *2009: CRISIL IER is launched*

  Independent Equity Research (IER) is launched by CRISIL.
- *2010: CRISIL moves to new HO*

  CRISIL has a new, corporate head office 'The CRISIL House', a state-of-the-art, green buildingat Powai, Mumbai.
- *2010: CRISIL assigns 15,000 SME ratings*

  CRISIL's ratings for Small and Medium Enterprises crosses the 15,000 mark.
- *2010: CREST is launched*

  CRISIL makes its presence in the real estate sector by launching CRISIL Real Estate Star Ratings.
- *2011: CRISIL Education Gradings is launched*

  CRISIL's sectoral involvement gets expanded with the launching of Education Grading, beginning with business schools.
- *2010: CRISIL acquires Pipal*

  CRISIL acquires Pipal Research through which it strengthens its position in the KPO industry.
- *2011: CRISIL Solar Grading's is launched*

  CRISIL ventures into Solar grading's.
- *2011: Gold and Gilt Index is launched*

  CRISIL launches Gold and Gilt Index.
- *2011: GR&A wins NASSCOM award*

  The relentless progress is acknowledged with CRISIL Global Research & Analytics winning the NASSCOM Exemplary Talent Practices Award.
- *2012: CRISIL acquires Coalition*

  In pursuit of entering into analysing and grading investment banks, CRISIL acquires UK-based Coalition, a company providing high-end analytics to global investment banks.
- *2012: CRISIL launches Pragati series*

  CRISIL focuses on investor education and conducts 'Pragati', a series of financial awareness workshop that transforms the lives of 1000 rural citizens.

- *2013: CRISIL Inclusix is launched*

  CRISIL launches 'CRISIL Inclusix', a comprehensive financial inclusion index which provides accurate measure of the extent of financial inclusion in more than 632 districts of the country.

- *2013: CRISIL Foundation is launched*

  CRISIL launches CRISIL Foundation, a platform to serve its twin goals of increasing financial awareness and conservation of the environment.

- *2014: CRISIL rates first commercial mortgage backed security*

  India's first Commercial Mortgage Backed Securities are rated by CRISIL.

- *2013: CRISIL releases 'State of the Nation' report*

  CRISIL releases its first 'State of the Nation' report, a comprehensive analytical report that offers a holistic view of India's economic state.

- *2014: CRISIL Chair of Financial Markets' instituted at IIM A*

  MoU signed between CRISIL and Indian Institute of Management, Ahmedabad (IIM-A) to set-up a 'CRISIL Chair of Financial Markets' at the institute.

- *2014: Fund Management ratings launched*

  CRISIL ratings bring mutual funds within its research domain by introducing Fund Management Capability Ratings.

  2015: CRISIL RE is launched

  To contribute socially, CRISIL RE, a programme focusing on environment conservation through employee volunteering is launched.

- *2015: CRISIL rates partially guaranteed debenture*

  CRISIL for the first time issues rating for an innovative partially guaranteed debenture issue of a passive infrastructure 'Special Purpose Vehicle'.

- *2016: CRISIL launches the first hybrid issuance ratings*

  For the first time, hybrid issuance ratings in the insurance sector is launched by CRISIL.

- *2016: 10th batch of CCAP launched*

  Continuing its association with the academic sector, CRISIL partners with the Narsee Monjee Institute of Management Studies (NMIMS) to launch the 10th batch of Certified Analyst Programme (CCAP).

- *2016: CRISIL features in the list of the top 100 Best companies in India for women*

  CRISIL finds place in the list of the 'Top 100 Best companies in India for Women' published by Avtar Group and Working Mother Publication.

- *2016: CRISIL launches CSR Year Book*

  The first CRISIL CSR Year Book, an annual publication providing account of CSR activities and spending by CRISIL in compliance with Section 135 on CSR in the new Companies Act, 2013 is launched.

- *2016: CRISIL launches first Infrastructure Rating*

  First Infrastructure Rating on the 'Expected Loss' scale launched by CRISIL.

- *2016: CRISIL Foundation selected for RBI scheme*

  CRISIL Foundation is selected by the Reserve Bank of India to receive financial assistance under its Depositor Education & Awareness Fund Scheme.

- *2017: CRISIL launches SMART (an innovative financial research platform)*

  CRISIL launches SMART, an innovative financial research platform that supports research analysts to perform certain tasks and optimize decision-making for many others.

- *2017: CRISIL launches 'smefirst'*

  Looking to provide SMEs easy access to ratings and other related activities, CRISIL launches an online platform 'smefirst'.

- *2017: CRISIL buys stake in CARE*

  CRISIL turns its eyes towards its competitors and buys 8.9 per cent stake in CARE Ratings.

- *2017: CRISIL launches InfraInvex*

  India's first infrastructure investability index is launched by CRISIL.

- *2017: SIDBI & CRISIL sign MoU to launch CriSidEx*

  CRISIL enters into a MoU with Small Industries Development Bank of India (SIDBI) to launch India's first MSME Sentiment index named CriSidEx

- *2018: CRISIL launches FPI index*

  CRISIL launched India's first index to benchmark performance of investments of foreign portfolio investors (FPI) in the fixed-income market, in both rupee and dollar versions.

- *2018: CRISIL, SIDBI launch India's first MSE sentiment index*

  CriSidEx, India's first sentiment index for Micro and Small Enterprises (MSEs) developed jointly by CRISIL and SIDBI is launched by the then Finance minister Shri Arun Jaitley.

- *2018: CRISIL launches WE-Check for women entrepreneurs*

  CRISIL in association with NITI Aayog, launched'WE-Check', a digital verification and assessment service exclusively for women entrepreneurs.

12.4.3 CRISIL's Rating Process

The rating process adopted by CRISIL is the following:

1. Request of the company: The first step of the rating process begins by receiving the request of the company desiring of having its issue obligations under proposed instrument rated by CRISIL.
2. Assignment to analytical team: Once the request has been received, in the second stage, CRISIL hands over the task to an analytical team responsible for executing the rating assignment.
3. Obtaining and processing data: The analytical team in charge of executing the rating assignment primarily obtains data from the company employees by interacting with them. After obtaining the requisite data, it is then processed and compiled together.
4. Findings presentation: The findings of the team are presented to the Rating Committee (which consists of some directors not connected with any CRISIL shareholder) which then decides on the rating.
5. Communication of decision: A this stage, the decision of the Rating Committee is conveyed to the client company with the clause that the company still can provide additional information for reconsideration of rating grade assigned to this instrument. In case, the company has nothing to produce as an additional fact, then rating grade is formally confirmed to the company by CRISIL.
6. Monitoring of change of rating: Last but not the least, once the company decides to use the rating, CRISIL is obliged to monitor the rating, over the entire life of the instrument. However, it is to be noted that CRISIL has the right to alter the rating influenced by new developments. Also, CRISIL needs to make the changed rating public.

12.4.4 CRISIL Credit Rating Scales

The credit ratings provided by CRISIL for financial institutions and various debt instruments are categorized under the following seven categories:

1. Long-term instruments

   The ratings that CRISIL assigns for the various long-term financial instruments having a maturity period of more than one year include bonds, debentures and loans varies from 'CRISIL AAA' to 'CRISIL D'. The entire range of ratings is displayed in the table below:

Rating	Meaning
CRISIL AAA	Highest safety [a rating that signifies that instruments have the highest level of safety with respect to timely servicing of financial obligations. Such instruments carry lowest credit risk.]

CRISIL AA	A high degree of safety [a rating that signifies that instruments have the high level of safety with respect to timely servicing of financial obligations. Such instruments carry very low credit risk.]
CRISIL A	An adequate degree of safety [a rating that signifies that instruments have adequate level of safety with respect to timely servicing of financial obligations. Such instruments carry low credit risk.]
CRISIL BBB	A moderate degree of safety [a rating that signifies that instruments have moderate level of safety with respect to timely servicing of financial obligations. Such instruments carry moderate credit risk.]
CRISIL BB	A moderate risk of default [a rating that signifies that instruments have moderate risk of default with respect to timely servicing of financial obligations.]
CRISIL B	High risk of default[a rating that signifies that instruments have the high risk of default with respect to timely servicing of financial obligations.]
CRISIL C	Very high risk of default [a rating that signifies that instruments have very high risk of default with respect to timely servicing of financial obligations.]
CRISIL D	Instruments in default [these instruments are already in default or soon to be in default.]

2. Short-term instruments

   The short-term instruments for which CRISIL assigns ratings have a maturity period of less than one year and include commercial papers, short-term debentures and short-term loans. The ratings vary from 'CRISIL A1' to 'CRISIL D' and are as follows:

Rating	**Meaning**
CRISIL A1	Very strong degree of safety regarding timely payment of financial obligations. Such instruments carry lowest credit risk.
CRISIL A2	Strong degree of safety regarding timely payment of financial obligations. Such instruments carry low credit risk.
CRISIL A3	Moderate degree of safety regarding timely payment of financial obligations. Such instruments carry higher credit risk as compared to the above two.]
CRISIL A4	Minimal degree of safety regarding timely payment of financial obligations. They carry very high credit risk and are susceptible to default.]
CRISIL D	In default or expected to default on maturity.

3. Long-term Structured Finance Scale

   The ratings assigned by CRISIL are the same as that of long-term instruments, except for the fact that (SO) is added to the general ratings assigned in the case of long-term instruments. Thus, the ratings assigned to long-term structured finance scale reads as CRISIL AAA (SO) for highest safety, CRISIL AA (SO) for high safety, CRISIL A (SO) for adequate safety, CRISIL BBB (SO) for moderate safety, CRISIL BB (SO) for moderate risk, CRISIL B (SO) for high risk, CRISIL C (SO) for very high risk and CRISIL D (SO) for default.

4. Short-term Structured Finance Scale

   Similar to the ratings of long-term structured finance scale, the short-term structured finance scale are assigned CRISIL A1 (SO) for very strong degree of safety, CRISIL A2 (SO) for strong degree of safety, CRISIL A3 (SO) for moderate degree of safety, CRISIL A4 (SO) for minimal degree of safety, and CRISIL D (SO) for default.

5. Long-Term Credit Enhancement (CE)

Rating	**Description**
CRISILAAA(CE)	Instruments have highest degree of safety which also means that they have lowest credit risk.
CRISILAA(CE)	Instruments have high degree of safety which also means that they carry very low credit risk.
CRISIL A(CE)	Instruments have adequate degree of safety which also means that they have low credit risk.
CRISIL BBB(CE)	Instruments may be considered to have moderate degree of safety.
CRISILBB(CE)	Instruments may be considered to have moderate risk of default.
CRISIL B(CE)	Instruments may be considered to have high risk of default.
CRISIL C(CE)	Instruments carry very high risk of default.

6. Short-Term Credit Enhancement (CE)

   The short-term credit enhancements are on the same lines of long-term ones and likewise, the ratings are CRISIL A1 (CE) for very strong degree of safety / lowest credit risk, CRISIL A2 (CE) for strong degree of safety / low credit risk, CRISIL A3 (CE) for moderate degree of safety / higher credit risk than the above two, CRISIL A4 (CE) for minimal degree of safety / very high credit risk and CRISIL D (CE) for most likely default.

7. Fixed Deposit Scale

Rating	**Description**
FAAA (“F Triple A) Highest safety	Indication that safety with respect to timely payment of principal and interest is very strong
FAA (“F Double A) High safety	Indication that safety with respect to timely payment of principal and interest is strong but less as compared to the above.

FA Adequate safety	Indication that safety with respect to timely payment of principal and interest is satisfactory but may get adversely affected by environmental issues.
FB Inadequate safety	Indication of inadequate safety.
FCHigh risk	Indication that repayment of principal and interest is doubtful. Most likely to get heavily affected by adverse economic conditions leading to reduction in ability and willingness to repay.
FDDefault	Either default or expected to default.
MMNot meaningful	Have certain factors associated with them which makes the instruments meaningless e.g. reconstruction / reorganization of the issuer, likely liquidation, facing dispute in the court of law/ statutory authority.

8. Corporate Credit Scale

Rating	**Description**
CCR AAA ("CCR Triple A")	Indicates highest degree of strength with respect to honouring debt obligations.
CCR AA("CCR Double A")	Indicates high degree of strength with respect to honouring debt obligations.
CCR A	Indicates adequate degree of strength with respect to honouring debt obligations.
CCR BBB	Indicates moderate degree of strength with respect to honouring debt obligations.
CCR BB	Indicates inadequate degree of strength with respect to honouring debt obligations.
CCR B	Indicates high risk and vulnerability with respect to honouring debt obligations.
CCR C	Indicates substantial risk and very high vulnerability with respect to honouring debt obligations.
CCR D	Indicates partial or total default for the debt obligations.
CCR SD	Indicates that the entity defaulted on selective debt obligation but is likely to meet other remaining debt obligations.

12.4.5 Shortcomings of Credit Ratings

Even though the ratings are an indication of the entity's strength regarding repayment of debt obligations, still the investors are sceptical at times to be confident about the ratings. The lack of belief in the ratings is due to the following reasons:

1. **Biased rating and misrepresentations**: Ratings in most of the cases are influenced by the weight of the persons associated with the instrument or

company. This results in the ratings being biased. Also, many a times, companies deliberately do not disclose lower ratings while raising funds from the market so that an investor either himself has to make effort to know the rating or has to invest without taking into account the hazardous nature of the instrument.

2. **Static study:** Since the rating methodology takes into account the past and current data, it may be considered to be a static study and the ratings are just predictions which may or may not materialize depending upon the environmental changes. Hence, as the future is uncertain and full of risk, the relevance of the ratings get diluted due to the likely impact of the uncertainties that may affect the environment.
3. **Concealment of material information**: It is very likely that companies will conceal and not reveal information's that might adversely affect the ratings. The ratings in such a scenario are unreliable.
4. **Rating does not assure guarantee for soundness of company**: Ratings are never a certificate of guarantee for creditworthiness of an instrument or any entity.
5. **Human bias**: Ratings suffer from human bias when investigating members have personal weaknesses towards the company.
6. **Reflection of temporary adverse conditions:** Short-time hostile economic and environmental conditions might pull down the ratings, although that is hardly the realistic conclusion as the company is likely to recover during normal times. Thus, low ratings during adverse conditions are not the true reflection of the strength of the company and also do not reflect the true performance of the concerned instrument. However, in reality, it still affects the company's reputation through downgraded ratings.
7. **Difference in rating of two agencies**: There are differences in the rating assigned by two different rating agencies for the same instrument. Such differences happen because of judgmental differences on qualitative issues. This ultimately creates confusion among the investors.

Check Your Progress

1. When was Credit Rating Information Services of India Limited established in India?
2. Name some of the credit rating agencies established in India.
3. What are the main focus areas of CRISIL?
4. Mention one shortcoming of credit ratings.

12.5 ANSWERS TO CHECK YOUR PROGRESS QUESTIONS

1. Credit Rating Information Services of India Limited was established in India in the year 1987.
2. Some of the credit rating agencies established in India are the following:
   - Investment Information and Credit Rating Agency (ICRA)
   - Credit Analysis and Research Limited (CARE)
   - Onicra Credit Rating Agency of India Limited
   - SME Rating Agency of India Limited (SMERA)
   - Brickwork Ratings (BWR)
3. The main focus areas of CRISIL are ratings and risk assessment, research and advisory. CRISIL is a leading credit rating agency and the only credit rating agency in India which delivers sectoral specialization. CRISIL provides rating and risk assessment services to manufacturing companies, banks, Non-banking financial companies, financial institutions, housing finance companies, municipal bodies and companies in the infrastructure sector.
4. Ratings in most of the cases are influenced by the weight of the persons associated with the instrument or company. This results in the ratings being biased. Also, many a times, companies deliberately do not disclose lower ratings while raising funds from the market so that an investor either himself has to make effort to know the rating or has to invest without taking into account the hazardous nature of the instrument.

12.6 SUMMARY

- A credit rating agency (CRA), which is also referred to as a ratings service, is a company that assigns credit ratings.
- The financial instruments that are rated by the rating agencies vary across the spectrum from government bonds, corporate bonds, Certificate of Deposits, municipal bonds, preferred stock, to collateralized securities, such as mortgage-backed securities and collateralized debt obligations.
- CARE was the third Indian rating agency to come up in the year 1993. It has its head office in Mumbai and it happens to be India's second largest credit rating agency. It is one of the five partners of international rating agency called ARC Ratings.
- CRISIL, India's first credit rating agency, promoted by the erstwhile ICICI Ltd along with UTI and other financial institutions, was incorporated in the year 1987.

- The ratings that CRISIL assigns for the various long-term financial instruments having a maturity period of more than one year include bonds, debentures and loans varies from 'CRISIL AAA' to 'CRISIL D'.
- Even though the ratings are an indication of the entity's strength regarding repayment of debt obligations, still the investors are sceptical at times to be confident about the ratings.

12.7 KEY WORDS

- **Hedging:** It is a strategy that tries to limit risks in financial assets.
- **Credit-risk Management:** It is understood as the process of identifying and analyzing risk factors, measuring the level of risk, thereby selecting measures to manage credit activities to limit and eliminate risks in the credit process.
- **CRISILCARD Service:** This service launched by CRISIL is aimed at providing information and analytical opinion on India's corporate entities.
- **FPI Index:** CRISIL launched India's first index to benchmark performance of investments of foreign portfolio investors (FPI) in the fixed-income market, in both rupee and dollar versions.

12.8 SELF ASSESSMENT QUESTIONS AND EXERCISES

Short-Answer Questions

1. What is the main function of a credit rating agency?
2. Write a short note on the establishment of CRISIL in India.
3. Briefly mention the vision, mission and core values of CRISIL.
4. What are the major shortcomings of credit ratings?

Long-Answer Questions

1. Discuss the benefits of credit rating.
2. Explain the primary factors that are measured while rating a financial instrument.
3. Describe CRISIL's rating process.
4. Examine the credit ratings provided by CRISIL for financial institutions and various debt instruments.

12.9 FURTHER READINGS

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UNIT 13 ICRA LIMITED

NOTES

Structure

13.0 Introduction
13.1 Objectives
13.2 Investment Information and Credit Rating Agency of India Limited (ICRA Limited)
  13.2.1 Mission
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13.0 INTRODUCTION

ICRA Group is one of the most respected credit rating agencies not only in India but also in Sri Lanka and Nepal where it operated through its subsidiaries ICRA Lanka and ICRA Nepal. The rating methodology adopted by all the three are similar and are strengthened by technical assistance provided by the largest shareholder Moody's Investors Service, which is an international credit rating agency.

This unit discusses about the credit rating methodologies adopted by the parent company ICRA Limited and also its two Asian subsidiaries and also the ratings assigned to various instruments.

13.1 OBJECTIVES

After going through this unit, you will be able to:

- Explain the functioning of ICRA
- Discuss ICRA's rating methodology
- Examine ICRA's ratings of select sectors
- Discuss about the ICRA Group
- State about ICRA's overseas subsidiaries in Sri Lanka and Nepal

13.2 INVESTMENT INFORMATION AND CREDIT RATING AGENCY OF INDIA LIMITED (ICRA LIMITED)

ICRA Limited (formerly Investment Information and Credit Rating Agency of India Limited) was established in 1991 jointly sponsored by the Industrial Finance Corporation of India (IFCI) and other financial institutions and banks as an independent and professional investment information and credit rating agency.

With time, ICRA has progressed from ICRA to ICRA Group of Companies and is known as Group ICRA today. ICRA's shares are listed on both, the Bombay Stock Exchange and the National Stock Exchange. It is a public limited company.

As of today, ICRA is an associate of the international rating agency Moody's Investors Service which happens to be ICRA's largest shareholder. Moody's involvement in the processes is supported by a Technical Services Agreement, which requires Moody's to provide technical support to ICRA. Moody's allows ICRA to access its global research base which helps ICRA to enhance its research capabilities. Under the agreement, Moody's provides enrichment programmes to ICRA employees, including access to the financial markets and related courses that are offered as part of the E-Learning software licensed by Moody's from intuition, and provision of financial writing training seminars to the designated ICRA employees.

13.2.1 Mission

To be at the forefront of enhancing market efficiency as the most respected rating and analytical services firm by:

- Serving our customers with high standards integrity, intellectual rigour and independence.
- Maintaining high ethical standards, with sound governance practices and being socially responsible.
- Creating a stimulating, inclusive and transparent environment for our employees.

ICRA's services are designed to fulfill the following objectives:

- Disseminate information and guidance to institutional and individual investors/ creditors;
- Educate and increase the ability of borrowers/issuers to access the money and the capital market for tapping a larger volume of resources from a wider range of the investing public;
- Assist the regulators in promoting transparency in the financial markets;
- Provide intermediaries with a tool to improve efficiency in the funds raising process.

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13.2.2 Business of ICRA

Investment Information and Credit Rating Agency of India Ltd. (ICRA)'s primary business is that of a full-service credit rating agency but it also offers Consulting services, IT-based services, Information services, and Outsourcing services. To provide additional services, in addition to ICRA Ltd., Group ICRA has three wholly-owned subsidiaries which together form the ICRA Group of Companies (Group ICRA).

The subsidiaries are:

- ICRA Management Consulting Services Limited (IMaCS)
- ICRA Techno Analytics Limited (ICTEAS)
- ICRA Online Limited (ICRON)

ICRA being an early entrant in the credit rating business, it is one of the most experienced and followed rating agency in India. ICRA rates rupee-dominated debt instruments issued by manufacturing companies, commercial banks, NBFCs, financial institutions, public sector undertaking and municipalities etc. In addition, ICRA also rates structured obligations and also rates structured obligations and sector specific debt obligations such as instruments issued by power, telecom and infrastructure companies. The other services offered include credit risk rating of debt mutual funds, an Independent Credit Evaluation of the residual debt in entities under the RBI's framework for resolution of stressed assets and rating of security received issued by Asset Reconstruction Companies as required by RBI.

The various services offered are discussed at length hereunder:

1. Corporate Debt Ratings

The ratings assigned by ICRA are a symbolic indicator of ICRA's current opinion on the concerned corporate entity's capability to meet the debt obligation timely with reference to the instrument rated. The information and clarifications obtained from the entity and from other sources form the basis of such ratings. The professional approaches followed by ICRA ensure a reliable, consistent and unbiased rating. On the basis of the rating, investors assign weightage to the risk factor and take investment decisions accordingly. ICRA rates long term medium-term and short term debt instruments for the following issuers:

- Manufacturing entities
- Banks and Financial Institutions
- Infrastructure sector corporates
- Service sector companies
- Municipality and other local authorities
- State Governments
- NBFCs
- SMEs

2. Financial Sector ratings

ICRA's financial sector debt ratings cover entries like banks and financial institutions, NBFCs and HFCs. Even though the functions they perform are similar in nature, there is a marked difference in terms of the volume of work, services and products offered, product delivery, regulatory requirements and internal control systems. Moreover, there is significant difference in the risk profiles as their borrowing capability and sources differ. Their borrowings include term loans, debentures, public deposits, working capital demand loan, and cash credit from banks, commercial paper, etc.

3. Structured Finance Ratings

ICRA structured finance ratings (SFRs) are opinion regarding the possibility of instrument being able to honour its debt obligations in accordance with the terms. An SFR is different from a corporate credit rating in the sense that in case of a SFR, the assessment is based on the risks associated with the individual components of the structured instrument. The components that have a bearing on the rating include legal risk, credit quality of the underlying asset and the various features of the structure. The ratings assigned to SFRs carry a suffix of SO (for structured obligation) along with symbols used credit ratings. SFRs are based on an assessment of the expected loss on the rating instrument under various possible scenarios. The expected loss is calculated by multiplying the probability of default and severity of loss as and when the default occurs. The difference between SFR and Credit Rating is that a SFR it is based on the strength of the underlying assets and structure.

The research methodology applied for SFRs is different from that of a normal credit rating. It is based on ICRA's understanding of the asset class, the structure and the legal aspects associated with them.

- **Asset Backed Securitisation (ABS)**

ABS refers to the securitisation of a diversified collection of financial assets which includes automobile and commercial vehicle loans, consumer durable loans or any non-financial class of assets that can be directly related and separated from the operations of the issuer and also that the risk of loss can be measured.

- **Mortgage Backed Securitisation (MBS)**

The housing loans are considered to be underlying assets in this category.

- **Collateral Debt Obligation (CDO)**

The underlying assets that are considered here include corporate loans, bonds, any debt securities including structured debt.

- **Future Flow Statement (FFT)**

FFTs involve identification of the future cash flows and earmarking them for the purpose of meeting the debt obligations. The specific sources that are identified include property tax revenues of municipal corporations, power receivables of bulk consumers and property lease rentals.

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4. Infrastructure Sector Ratings

Infrastructure sector ratings consist of ratings related to debt programmes of issues in the power, roads, telecommunications and other such infrastructure related sectors. Considering the fact that such infrastructural projects require huge funding and also long gestation period, and mounting inability and reluctance of the government, both at the centre and state level, to fund such projects, the private sector involvement has increased and they have enhanced their importance as the principal infrastructure developers. Increased private participation and relevance has made ICRA believe that ratings in this sector will increasingly gain importance both from the issues and the investors' perspective. The rating process involves assessment of the viability of the project in light of political, legal and regulatory environment affecting the sector.

13.2.3 ICRA's Rating Process

ICRA initiates its rating process after receiving a formal request from the potential issuer. The rating assignment is taken up by a rating team comprising of two analysts who possess requisite skills and have expertise required to evaluate the business of the issuer. The issuer is asked for specific information that covers all the aspects which ICRA deem necessary to evaluate a business. Simultaneously, information is also collected from ICRA's own research division. There are interactions with the issuer's management to discuss various aspects like planning, outlook, competitive position and funding policies.

In the case of manufacturing companies, plant visits are arranged to get a better understanding of the manufacturing process, production facilities and evaluate the technical acumen of the personnel involved in the production line. All these are done to form an opinion with regard to the variables that influence level, quality and cost of production and also evaluate the progress of the project. On the basis of analysis done after evaluating and assessing all the information collected, a rating report is prepared and presented to the Rating Committee. The Rating Committee has the final say on the ratings to be assigned. The signed rating is then shared with the issuers to the management for acceptance. In the case of non-acceptance of any rating, confidentiality is maintained and the non-accepted rating is not disclosed.

The issuer has the right to appeal for a review against the non-accepted rating. Review is done when new inputs are provided by the issuer. Such new information is presented to the Rating Committee, which may take it into consideration and revise the rating, if they deem it necessary. The rating is generally reviewed once a year, if it is not necessitated due to any urgency.

13.2.4 ICRA's Rating Methodology

The rating methodology takes into account all the relevant factors affecting future cash generation. The factors so assessed include industry characteristics, market share, operational efficiency, management quality, commitment to new projects and the funding policy of the issuer. Past financial statements are deeply analysed to understand the real business dynamics. Sensitivity analysis is taken up to estimate future cash generations that gives an idea about its probable ability to meet the debt obligation.

Select Sectoral Rating Methodology

(i) Airports: ICRA's risk assessment for Indian airports, both greenfield and brownfield, is based on the following factors:

1. Business Risk Drivers
   - (a) Contractual agreements
   - (b) Construction risk
   - (c) Funding risk
   - (d) Scale of operations, traffic trends and volatility
   - (e) Revenue risk
   - (f) Operating risk
   - (g) Transaction structure risk
   - (h) Counterparty credit risk
   - (i) Force majeure risk
2. Industry risk drivers
   - (a) Traffic risk
   - (b) Regulatory risk
3. Financial risk drivers
   - (a) Profitability
   - (b) Leverage and debt coverage indicators
   - (c) CapEx plans
   - (d) Liquidity and financial flexibility
   - (e) Foreign currency-related risks
   - (f) Tenure mismatches, and risks relating to interest rates and refinancing
   - (g) Contingent liabilities and off-balance sheet exposures
4. Management Quality and Corporate Governance
5. Parentage

(ii) Banks

The factors assessed while doing credit analysis are:

1. *Business Risk Analysis*
   - (a) Operating Environment
   - (b) Regulatory Environment

(c) Franchise
(d) Management, Governance, Information Systems and Strategy

(e) Risk Management

2. *Financial Risk Analysis*
   (a) Asset Quality
   (b) Diversity of Funding and Liquidity
   (c) Profitability, Earnings Stability and Prospects
   (d) Capital Adequacy and Management

(iii) Corporate Credit Rating

The various aspects covered in the process of assigning rating to the corporates are the following:

1. *Industry Risk*
   (a) Growth Prospects
   (b) Cyclicality
   (c) Competitive Intensity
   (d) Regulatory Risk
2. *Business Risk*
   (a) Scale and Market Share
   (b) Competitive Position
   (c) Diversification
   (d) Operating Efficiency
   (e) Quality of Assets
   (f) Project Risks
3. *Financial Risk*
   (a) Profitability
   (b) Leverage
   (c) Coverage
   (d) Liquidity
   (e) Cash Flows
4. *Management Risk*
   (a) Quality of Management
   (b) Financial Policies
   (c) Governance Structure and Practices

(iv) Housing Finance Companies

In addition to providing housing loans, the HFCs also offer products like loan against property (both residential and commercial), builder, construction finance or project loans, lease rental discounting and personal and insurance loans.

The risk assessment is done on the basis of the following factors:

1. *Business Risk*
   (a) Business Profile
   (b) Operating Environment
2. *Financial Risk*
   a) Profitability
   b) Liquidity
   c) Capital Adequacy
   d) Asset Quality

(v) Financial Ratio Analysis of Entities in the Non-Financial Sector

The ratios that are analysed for assigning the ratings are:

1. *Profitability Ratios*
   a) Operating Profit Margin
   b) Net Profit Margin
   c) Return on Capital Employed (RoCE)
2. *Leverage Ratios*
   a) Gearing Ratio
   b) Total Indebtedness Ratio
   c) Debt to Profit Ratio
   d) Accruals to Debt Ratio
3. *Coverage Ratios*
   a) Interest Coverage Ratio
   b) Debt Service Coverage Ratio
4. *Liquidity Ratios*
   a) Current Ratio
   b) Working Capital Cycle
   c) Working Capital Intensity

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(vi) Rating of Commercial Papers

The key factors that ICRA analyses in the process of assigning ratings to Commercial Papers includes the following:

1. *Industrial Risk*
    a) Existing and expected demand-supply situation
    b) Intensity of competition
    c) Vulnerability to imports
    d) Regulatory risks
    e) Outlook for user industries
    f) Working capital intensity of the business
    g) Overall prospects and outlook for the industry
2. *Issuer's Competitive Position*
    a) Scale of operations
    b) Vintage of technology used
    c) Capital cost position
    d) Location advantage in terms of proximity to raw material sources as well as markets
    e) Operating efficiencies (yields, rejection rates, energy consumption, etc.)
    f) Market position as reflected in trends in market share, ability to command premium pricing, distribution network, and relationship with key customers
3. *Financial Risk*
    a) Operating Profitability
    b) Gearing
    c) Debt Service Coverage Ratios
    d) Working Capital Intensity
    e) Accounting Quality
    f) Contingent liabilities/Off-balance sheet exposures
4. *Liquidity and Financial Flexibility*
    a) The availability of unutilized working capital limits or lines of credit with the issuer from banks/financial institutions. Typically, issuers that are assigned A1+/A1 ratings for Commercial Papers by ICRA are generally expected to have unutilized limits to fully cover the size of Commercial Paper programme.

b) The quality and nature of the issuer's current assets.

c) The support/commitment available to the issuer from promoters/ group entities.

d) Other sources of financial flexibility for the issuer like liquid investments.

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13.2.5 ICRA's Rating Scale

- **ICRA's Long-Term Rating Scale**

Rating	Meaning
[ICRA]AAA	Highest degree of safety / lowest credit risk
[ICRA]AA	High degree of safety / very low credit risk
[ICRA]A	Adequate degree of safety / low credit risk
[ICRA]BBB	Moderate degree of safety / moderate credit risk
[ICRA]BB	Moderate risk of default
[ICRA]B	High risk of default
[ICRA]C	Very high risk of default
[ICRA]D	In default or expected to be in default soon

- **ICRA's Medium-Term Rating Scale (only for Public Deposits)**

Rating	Meaning
MAAA	Highest credit quality / lowest credit risk
MAA	High credit quality / low credit risk
MA	Adequate credit quality / average credit risk
MB	Inadequate credit quality / high credit risk
MC	Risk-prone credit quality / very high credit risk
MD	Lowest credit quality / very low prospects of recovery

- **ICRA's Short-Term Rating Scale**

Rating	Meaning
[ICRA]A1	Very strong degree of safety / lowest credit risk
[ICRA]A2	Strong degree of safety / low credit risk
[ICRA]A3	Moderate degree of safety / higher credit risk
[ICRA]A4	Minimal degree of safety / very high credit risk
[ICRA]D	Default or expected to be in default

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- **ICRA's Issuer Rating Scale**

An Issuer Rating is an opinion on the general creditworthiness of the rated issuer and is not specific to any particular debt instrument.

Rating	Meaning
[ICRA]AAA (earlier denoted as IrAAA)	Highest degree of safety / lowest credit risk
[ICRA]AA(earlier denoted as IrAA)	High degree of safety / very low credit risk
[ICRA]A (earlier denoted as IrA)	Adequate degree of safety / low credit risk
[ICRA]BBB (earlier denoted as IrBBB)	Moderate degree of safety / moderate credit risk
[ICRA]BB(earlier denoted as IrBB)	Moderate risk of default
[ICRA]B(earlier denoted as IrB)	High risk of default
[ICRA]C(earlier denoted as IrC)	Very high risk of default
[ICRA]D ((earlier denoted as IrD)	In default or expected to be in default soon

- **ICRA's Rating Scale for Instruments supported by Explicit Credit Enhancement**

Long-term (instruments with a maturity period of over one year)

Rating	Meaning
[ICRA]AAA(CE)	Highest degree of safety / lowest credit risk
[ICRA]AA(CE)	High degree of safety / very low credit risk
[ICRA]A(CE)	Adequate degree of safety / low credit risk
[ICRA]BBB(CE)	Moderate degree of safety / moderate credit risk
[ICRA]BB(CE)	Moderate risk of default
[ICRA]B(CE)	High risk of default
[ICRA]C(CE)	Very high likelihood of default
[ICRA]D(CE)	In default or expected to be in default soon

- **ICRA's Short-Term Credit Enhanced Instruments**

Rating	Meaning
[ICRA]A1(CE)	Very strong degree of safety / lowest credit risk
[ICRA]A2(CE)	Strong degree of safety / low credit risk
[ICRA]A3(CE)	Moderate degree of safety / higher credit risk
[ICRA]A4(CE)	Minimal degree of safety / very high credit risk
[ICRA]D(CE)	Default or expected to be in default

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- **ICRA's Structured Finance Rating (Long term)**

Rating	Meaning
[ICRA]AAAmfs	Highest degree of safety
[ICRA]AAmfs	High degree of safety
[ICRA]Amfs	Adequate degree of safety / low credit risk
[ICRA]BBBmfs	Moderate degree of safety / moderate credit risk
[ICRA]BBmfs	Moderate risk of default
[ICRA]Bmfs	High risk of default
[ICRA]Cmfs	Very high risk of default
[ICRA]Dmfs	In default or expected to be in default soon

- **ICRA's Long-Term Debt Fund Credit Risk Rating Scale**

Rating	Meaning
[ICRA]A1mfs	Very strong degree of safety
[ICRA]A2mfs	Strong degree of safety
[ICRA]A3mfs	Moderate degree of safety
[ICRA]A4mfs	Minimal degree of safety

13.3 ICRA GROUP

Fig 13.1 *ICRA Group*

13.3.1 ICRA Analytics Ltd

ICRA Analytics Ltd (formerly known as ICRA Online Ltd), is a wholly-owned subsidiary of ICRA Ltd. It provides solutions, analytics and digital platforms for risk management, market data, consulting, grading services and knowledge services.

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ICRA Analytics Ltd. is the amalgamated entity of ICRA Online Ltd. (ICRON) and ICRA Management Consulting Services Ltd. (IMaCS), both wholly-owned subsidiaries of ICRA Ltd.

The services provided by ICRA Analytics Ltd. include the following:

- *Risk Management advice and solutions* to Banks, NBFCs, Housing Finance Companies, Development Finance Institutions and Corporates in India, Asia and Africa.
- *Market Data research, content and analytics* to Fund Managers across Mutual Funds, Pension Funds, AIFs and Insurance as well as to Investors and Intermediaries comprising Corporate Treasuries, Brokerages, Wealth Managers and Independent Financial Advisors in India and global markets.
- *Financial and Risk Advisory as well as technical assistance* to Corporates, Energy Sector entities, Electricity Regulatory Bodies, Government Organizations, Multi-Lateral Agencies and Industry Associations in India.
- *Knowledge Services in the area of Automated Data Management, GAAP & IFRS Accounting Support, Financial Statement Analysis, Modelling, Research and IT Services* to companies in India and global markets.
- *Grading Services that ensure independent, objective, and regular evaluation* for Energy Service Companies (ESCO), Solar Power, Vendor / Dealer Due Diligence and Ministry of Power.
- *Risk Management services*
  i. Internal Rating Software for banks with Basel II compliant models
  ii. Credit Risk Modelling
  iii. Expected Credit Loss computation
  iv. Operational Risk Management software
  v. Industry Risk Score
  vi. Red Flag Reports
- *Market Data*
  i. Daily pricing of active ISINs through Security Level Valuation
  ii. Indices
  iii. Rating Tracker
  iv. Performance data & research of live MF schemes
  v. Portfolio tracking & analysis
  vi. Investor Education Collateral

- *Consulting*
    - i. Energy & Renewables
    - ii. Financial & Risk Advisory
    - iii. Tariff assistance
    - iv. Social sector
- v. Design & monitoring
    - vi. Program management
    - vii. Technical assistance
- *Knowledge Services*
    - i. Automated data management
    - ii. GAAP & IFRS accounting support and analysis
    - iii. Research
    - iv. IT services

13.3.2 ICRA Lanka

ICRA Lanka Limited (ICRA Lanka) is a Credit Rating Agency licensed by the Securities and Exchange Commission of Sri Lanka (SEC). ICRA Lanka is a fully owned subsidiary of ICRA Limited (ICRA) of India. The company was granted license by the SEC in May 2011.

ICRA Lanka is also supported by a Technical Services agreement with ICRA, wherein the parent company provides operational support and resources. ICRA Lanka follows the same methodology as that of ICRA. Currently, the rating committee of ICRA Lanka is composed of senior executives from ICRA.

Rating Methodology of ICRA Lanka

The rating methodologies adopted by ICRA Lanka are more or less on the same lines that of its parent firm ICRA.

The Issuer Rating Methodology revolves around assessing factors that may be broadly categorized under the heads— business risk and financial risk. Under the business risk category, the issues analysed are industry risk, competitive position and management quality, whereas the factors analysed under financial risk are financial position, profitability, capital structure and financial flexibility.

For Corporate Credit Rating, in addition to the above mentioned factors, ICRA Lanka also analyses new project risk under business risk category and future cash flow adequacy under financial risk.

Similarly, the rating methodology for NBFCs which provide services like vehicle loans, equipment loans, personal loans, micro credit, loans against property, loans against shares, and corporate loans is performed by assessing the business and financial risk factors that are already mentioned earlier.

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One of the crucial financial instrument for which rating is assigned is mutual funds. ICRA Lanka's rating approach for mutual funds include using information related to prospectus and related documents, debt fund portfolio data, including periodic investor reports and public filings, Industry surveys, studies, and special reports, and internal documents describing the AMC's structure, investment philosophy, decision making process, and performance track record.

While assigning rating to general insurance companies, ICRA Lanka's business analysis covers factors like industry analysis, regulatory environment, ownership, management and strategic focus, operating strengths and business franchise, underwriting and reinsurance strategy. The financial analysis studies factors like capitalization, profitability, liquidity, investment risk, and asset/liability management.

13.3.3 ICRA Nepal

ICRA Nepal Limited (ICRA Nepal), the first Credit Rating Agency in Nepal, is a Subsidiary of ICRA Limited (ICRA) of India and was incorporated on 11 November 2011. It was granted license by the Securities Board of Nepal (SEBON) on 3rd October 2012. ICRA Nepal is supported by ICRA Limited through a Technical Support Services Agreement through which it helps in such areas as rating process and methodologies, analytical software, research, training, and technical & analytical skill augmentation.

ICRA Nepal's Rating Methodology

ICRA Nepal's rating methodology is also very much similar to the process adopted by its parent company ICRA and the process adopted by ICRA Lanka.

One of the rating assignments that we have not yet discussed above in the case of both ICRA and ICRA Lanka is fund management rating quality. The key parameters and factors that are re-assessed to assign a rating are the following:

- Ownership
- Organizational Structure and Management Quality
- Governance Structure and Fiduciary Responsibility
- Transparency and Investor Service
- Investment Performance
- Financial Soundness

In the case of IPO ratings, ICRA Nepal considers factors like industry prospects, market position, operating efficiency, risk and prospects of new projects, current financial position and future prospects, the management quality, the corporate governance practices, and compliance and litigation history.

Check Your Progress

1. When was ICRA Limited established in India?
2. What are the different kinds of services provided by Investment Information and Credit Rating Agency of India Limited?
3. Define Asset Backed Securitisation (ABS).
4. What is the rating methodology adopted by ICRA?
5. What is ICRA Lanka's rating approach for mutual funds?

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13.4 ANSWERS TO CHECK YOUR PROGRESS QUESTIONS

1. ICRA Limited (formerly Investment Information and Credit Rating Agency of India Limited) was established in 1991 jointly sponsored by the Industrial Finance Corporation of India (IFCI) and other financial institutions and banks as an independent and professional investment information and credit rating agency.
2. ICRA's primary business is that of a full-service credit rating agency but it also offers Consulting services, IT-based services, Information services, and Outsourcing services.
3. ABS refers to the securitisation of a diversified collection of financial assets which includes automobile and commercial vehicle loans, consumer durable loans or any non-financial class of assets that can be directly related and separated from the operations of the issuer and also that the risk of loss can be measured.
4. The rating methodology adopted by ICRA takes into account all the relevant factors affecting future cash generation. The factors so assessed include industry characteristics, market share, operational efficiency, management quality, commitment to new projects and the funding policy of the issuer. Past financial statements are deeply analysed to understand the real business dynamics. Sensitivity analysis is taken up to estimate future cash generations that gives an idea about its probable ability to meet the debt obligation.
5. ICRA Lanka's rating approach for mutual funds include using information related to prospectus and related documents, debt fund portfolio data, including periodic investor reports and public filings, Industry surveys, studies, and special reports, and internal documents describing the AMC's structure, investment philosophy, decision making process, and performance track record.

13.5 SUMMARY

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- ICRA Limited (formerly Investment Information and Credit Rating Agency of India Limited) was established in 1991 jointly sponsored by the Industrial Finance Corporation of India (IFCI) and other financial institutions and banks as an independent and professional investment information and credit rating agency.
- Investment Information and Credit Rating Agency of India Ltd. (ICRA)'s primary business is that of a full-service credit rating agency but it also offers Consulting services, IT-based services, Information services, and Outsourcing services.
- ICRA being an early entrant in the credit rating business, it is one of the most experienced and followed rating agency in India. ICRA rates rupee-dominated debt instruments issued by manufacturing companies, commercial banks, NBFCs, financial institutions, public sector undertaking and municipalities etc.
- ICRA structured finance ratings (SFRs) are opinion regarding the possibility of instrument being able to honour its debt obligations in accordance with the terms.
- ICRA initiates its rating process after receiving a formal request from the potential issuer. The rating assignment is taken up by a rating team comprising of two analysts who possess requisite skills and have expertise required to evaluate the business of the issuer.
- The rating methodology takes into account all the relevant factors affecting future cash generation. The factors so assessed include industry characteristics, market share, operational efficiency, management quality, commitment to new projects and the funding policy of the issuer.
- ICRA Analytics Ltd (formerly known as ICRA Online Ltd), is a wholly-owned subsidiary of ICRA Ltd. It provides solutions, analytics and digital platforms for risk management, market data, consulting, grading services and knowledge services.
- ICRA Lanka Limited (ICRA Lanka) is a Credit Rating Agency licensed by the Securities and Exchange Commission of Sri Lanka (SEC). ICRA Lanka is a fully owned subsidiary of ICRA Limited (ICRA) of India. The company was granted license by the SEC in May 2011.
- The rating methodologies adopted by ICRA Lanka are more or less on the same lines that of its parent firm ICRA.
- ICRA Nepal Limited (ICRA Nepal), the first Credit Rating Agency in Nepal, is a Subsidiary of ICRA Limited (ICRA) of India and was incorporated on 11 November 2011.

- ICRA Nepal's rating methodology is also very much similar to the process adopted by its parent company ICRA and the process adopted by ICRA Lanka.

13.6 KEY WORDS

- **Public Listed Company:** It is a form of business organization that operates as a distinct legal entity from its owners. It is formed and owned by shareholders.
- **Moody's Investors Service:** It is a leading provider of credit ratings, research, and risk analysis. Moody's through its expertise contributes in ensuring transparency across the financial markets; thus, protecting the integrity of credit.
- **Infrastructure Sector Ratings:** These consist of ratings related to debt programmes of issues in the power, roads, telecommunications and other such infrastructure related sectors.
- **Force Majeure:** It is a clause that is included in contracts to remove liability for natural and inevitable calamities. It also covers human actions, such as armed conflict.
- **Interest Coverage Ratio:** It is a ratio which helps to decide whether the company will be able to pay interest within the stipulated period.

13.7 SELF ASSESSMENT QUESTIONS AND EXERCISES

Short-Answer Questions

1. State the mission and objectives of ICRA.
2. How is structured finance rating different from a corporate credit rating?
3. Write a short note on ICRA's Rating Process.

Long-Answer Questions

1. Explain the various services offered by ICRA.
2. Examine the significant implications of ICRA's Rating Scale.
3. Discuss the services provided by ICRA Analytics Ltd.
4. What is rating methodology adopted by ICRA Nepal and Lanka?

13.8 FURTHER READINGS

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UNIT 14 CREDIT ANALYSIS AND RESEARCH LIMITED (CARE)

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Structure

14.0 Introduction
14.1 Objectives
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14.0 INTRODUCTION

Credit Analysis and Research Ltd (CARE Ratings) is a serving rating organization that offers a wide scope of rating and reviewing/gradingservices financial instruments across sectors. CARE is acknowledged by the Government of India (GoI), Securities and Exchange Board of India (SEBI), and Reserve Bank of India (RBI).The organization does rating of the debt obligations like Commercial Papers, Debentures, Fixed Deposits and Bonds across various sectors that include Industrial Companies, Service Organizations, Infrastructure Companies, Banks, Financial Institutions (FIs), Non-Banking Finance Companies (NBFCs), Public Sector Undertakings (PSUs), State Government Undertakings, Local and Municipal Corporations, Structured Finance dealings, Securitization Transactions, SMEs, SSI and Micro Finance Institutions. The organization's credit rating is an assessment on the general capacity and readiness of a guarantor/issuer to make periodic repayments on the related dent obligation over its lifetime. In this unit, you will study about the various sectors, factors and the methodology adopted for rating/grading purpose.

14.1 OBJECTIVES

After going through this unit, you will be able to:

- Discuss the various sectors for which the rating exercise is conducted

- Identify the factors assessed during the rating exercise
- Learn about the rating methodology adopted by CARE

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14.2 CREDIT ANALYSIS AND RESEARCH LIMITED (CARE)

Credit Analysis and Research Ltd. (CARE) was established in 1993 and is the second biggest rating office (regarding rating pay) in the nation. The organization offers a wide scope of rating and evaluation of administration across different instruments and businesses. Apart from giving rating administrations to monetary area, foundation area, corporates, public money and MSMEs, CARE is likewise occupied with rating IPOs, instructive organizations, shipyards, and so forth. The organization has, as of late, started its valuation benefits and began offering valuation of debt instruments and market connected debentures. Being settled in Mumbai (Maharashtra), CARE has topographical presence in Republic of Maldives, Brazil, Malaysia, Portugal and South Africa.

14.2.1 Vision, Mission and Values

Vision: 'To be a respected company that provides best - in its field - quality and value services.'

Mission

- To offer a range of high-quality services to all the stakeholders in the capital market
- To build a pre-eminent position for the organization in India in securities analysis, research and information services and to be an international credit rating agency
- To earn customer satisfaction and investor confidence through fairness and professional excellence
- To remain deeply committed to our internal and external stakeholders
- To apply the best possible tools and techniques for securities analysis aimed to ensure efficiency and top quality
- To ensure globally comparable quality standards in our rating, research and information services

Values:

- Integrity and Transparency: Commitment to be ethical, sincere and open in our dealings
- Pursuit of Excellence: Committed to strive relentlessly to constantly improve ourselves
- Fairness: Treat clients, employees and other stakeholders fairly

- Independence: Unbiased and fearless in expressing our opinion
- Thoroughness: Rigorous analysis and research on every assignment that we take

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14.3 CARE'S ROLE

14.3.1 Corporate Ratings

CARE attempts rating exercise dependent on data given by the organization, in-house information base and information from different sources that CARE thinks about is reliable.

- *Debt Ratings*

  CARE carries out credit rating for various debt instruments which includes both medium-term and long-term debt instruments like debentures, bonds (including convertible bonds) and FDs, and also commercial papers, inter-corporate deposits and certificates of deposit that are short-term debt and deposit obligations.

  The essential focal point of the rating exercise is to analyse future cash generating capacity and their sufficiency to meet obligation commitments later on. The investigation in this manner endeavours to decide the essentials of the business and the probabilities of progress in these basics, which could influence the creditworthiness and reliability of the borrower.

  The insightful system of CARE's evaluating philosophy is segregated into two related fragments. While one of them manages the operational attributes, the second takes care of the monetary qualities. Other than quantitative components, subjective perspectives like appraisal of the management's

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abilities assume a significant part in showing up at the rating for an instrument. The overall significance of subjective and quantitative segments of the investigation differs with the type of guarantor.

(i) Manufacturing entities

CARE's rating methodology for manufacturing concerns begins with the assessment of the economy/industry of which the firm is a part of, which is trailed by the evaluation of the business hazard factors exclusive to the concerned firm. It is then followed by an appraisal of the monetary and risk factors associated with the project along with the qualitative superiority of the management. Evaluating liquidity and monetary adaptability of the issuer acquires substantial significance while reaching at the short-term ratings in addition to the credit examination of a guarantor.

(ii) Banks, NBFCs and Financial Institutions

To draw the rating of Banks, NBFCs and Financial Institutions, CARE assesses the sector to which the firm belongs. This is followed by the appraisal of the business basics of the establishment utilizing the 'CRAMELS' model which represents:

C - Capital adequacy

R - Resource raising ability

A - Asset quality

M - Management quality

E - Earnings quality

L - Liquidity

S - Systems

CARE has likewise evolved rating philosophies explicit for different areas. These methodologies endeavour to bring up variables, far beyond those referenced in the broader aspect which is thought of while examining organizations linked to a particular sector.

- *Bank Loan Ratings (BLR)*

BLRs is used by banks to determine risk weights for their loan exposures, in line with the Reserve Bank of India's (RBI's) guidelines for implementation of the New Capital Adequacy Framework under Basel II framework. CARE rates all type of fund-based and non-fund based facilities sanctioned by banks. This would include cash credit, working capital demand loans, Letter of Credit, Bank guarantees, Bill discounting, Project loans, loans for general corporate purposes, etc.

- **Issuer Ratings**

CARE's Issuer Rating is an explicit appraisal of the credit hazard of the specific issuer. While the extent of CARE's Issuer Rating is like long-term instrument evaluations, the fundamental distinction between Issuer Rating and different appraisals is that Issuer Rating is not for a specific instrument but oriented towards an issuer.

- **Corporate Governance Rating**

  SEBI rules (Credit Rating Agencies) Regulations,1999 (Amendment) dated 30th May 2018 forbids a Credit Rating Agency from doing any non-rating action. As per the guidelines, Corporate Governance Ratings will be completed via CARE Advisory Research and Training Ltd. (CART).

- **Recovery Rating**

  Securitization and Reconstruction of Financial Assets and Enforcement of Security Interest (SARFAESI) Act was sanctioned to encourage banks to recuperate their non-performing resources without the mediation of the court. The Act empowers three elective strategies for the recuperation of non-performing assets, in particular securitization, asset reconstruction and requirement of security without the court's intervention. This encourages the mitigation of long-awaited legal issues with respect to recovery of NPAs and includes proficient mastery via including securitization companies (SCs)/ Asset Reconstruction Companies (ARCs) in the recuperation cycle. Security Receipts (SRs) are instruments given under 'The SARFAESI Act' by SCs/ ARCs (against the assimilated financial resources) after obtaining resources for Qualified Institutional Buyers (QIBs).

14.3.2 Monetary Sector Ratings

The appraisal factors that CARE uses to rank financial organizations like Banks, Insurance, NBFCs and instruments like Capital Protection Oriented Schemes, Securitization, Housing Finance etc., consists of variety of risks like business, legal, and monetary risks and the executive vulnerabilities.

1. Banks

The methodology of bank rating is described below:

The factors that are used for the rating purpose can be categorized as (A) quantitative and (B) qualitative factors.

A. Quantitative Factors

   (i) Capital Adequacy

   Capital adequacy is a proportion of how much the bank's capital is accessible to retain potential misfortunes. It likewise demonstrates the capacity of the bank to embrace extra business. CARE inspects the similarity of the bank to the administrative rules on capital ampleness proportion. Higher extent of Tier I (center capital) in the general capital is seen well. Further, the 'stressed capital adequacy' which is a result of anticipated loss of capital due to issues like:

- Extra cushioning for NPAs
- Likely losses to be incurred due to restructuring of assets
- Expected losses from various weak assets

(ii) Asset Quality

Asset Quality survey starts with the assessment of the bank's credit hazard structure. The general asset quality is surveyed by assessing the area by area advance and assurance introductions. The bank's insight of advance misfortunes and discount/arrangements are deliberated upon cautiously. The level of assets is grouped into standard, unacceptable, suspicious or misfortune and the history of recuperations of the bank is inspected intently. The diversification of the portfolio and its presentation to distressed businesses/regions is assessed to show up at the degree of weak assets. The exposure of the rearranged assets ensures that banks are additionally considered to show up at the possible NPAs of the bank.

(iii) Resources

Asset base of the bank is dissected regarding cost and structure. Deposits are the center financing wellspring of a bank. Extent of low-cost deposits within the total deposit and retail and wholesale deposit is analysed. The rate of growth of deposits as well as their rollover rates is likewise examined. Normal and incremental cost of the deposits is inspected with regards to the current interest rate scenario. The ability of the bank to raise extra assets at modest rates is fundamentally analysed.

(iv) Liquidity

Absence of liquidity can prompt a bank's disappointment, while, solid liquidity can help even a generally frail organization to remain strong even during troublesome occasions. CARE assesses the inside and outside bases of assets to meet the bank's prerequisites. The liquidity hazard is assessed by analysing the Assets Liabilities Management (ALM) profile, renewal rates of deposits, the mix of liquid assets in the total assets and how much the core assets (those that are generally illiquid) are supported by center liabilities. The short duration external funding as a refinance facility from RBI and the inter-bank borrowing limits accessible alongside CRR and SLR are significant cradles of liquidity reserves.

(v) Earnings Quality

CARE dissects the constituents of banks' income structure by isolating them into those generation and fund related activities. Principal earnings are distinguished by not including non-recurring revenue from the total revenue. Every business territory that adds to the core revenue is evaluated for uncertainty and risk in addition to its profit possibilities and development rate.

B. Qualitative Factors

(i) Ownership

It is important to make an assessment of the ownership arrangement and shareholder backing. With respect to public sector banks, the readiness of the public authority to help the bank is a significant thought.

(ii) Management Quality

The structure of the board, transition of CEOs and the internal structure of the bank— all are taken into consideration. The bank's essential goals and activities with regards to assets accessible, its capacity to distinguish openings and history in overseeing difficult circumstances are taken as markers of managerial capability.

(iii) Risk Management

The management's opinion about risk and its management is assessed. The evaluation of credit risk management is done by scrutinizing the evaluation, observing and recuperation frameworks and the prudential loan giving standards of the bank. The bank's balance sheet is inspected with respect to interest rate sensitiveness and risks involved with exchange rate fluctuations. Financing cost hazard emerges due to contrasting development of resources and liabilities and jumble between the skimming and fixed rate resources and liabilities.

(iv) Compliance with statutory requirements

CARE inspects the history of the bank to ensure that they follow the SLR/CRR criteria and priority segment loaning standards as indicated by the RBI.

(v) Accounting Quality

Rating depends vigorously on evaluated information. Guidelines for income acknowledgment, provisioning and valuation of investments are inspected. Appropriate acclimations of the figures reported made for consistency of assessment and significant understanding.

(vi) Size and Market Presence

The asset base and the networking of the bank's branches may have a say on the bank's competitive status. While both big and small banks have effectively existed together in India, in the ever evolving banking scenario, the individualistic approach and area specific focus of the smaller banks against the size and operational advantages of the bigger banks would be deliberately analyzed to comprehend the plan of action of each bank.

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2. Credit Quality Ratings

CARE's asset credit quality appraisals are views on the general credit nature of explicit Debt Mutual Fund plans. The appraisals catch the asset's total exposure to default threat.

CARE uses the following qualitative factors to arrive at the rating:

(i) Quality of the Management

CARE's asset credit quality appraisals depend on assessment of the asset's speculative methodology and portfolio credit threat. It additionally includes assessment of credit nature of individual assets, spread of the portfolio, quality of the management and operational arrangements. CARE utilizes the idea of credit scores that are associated with specific securities, according to credit scoring grid created by CARE.

(ii) Operations & Risk Management Systems

CARE analyses Management Information and Risk Management frameworks in different operational regions. Frameworks for regular checking of the portfolio and the exchanges with the custodian and record holders are analysed. The bookkeeping frameworks, divulgence levels and the administrative compliance record of the AMC and the policies to make sure that the said compliance is followed are additionally examined. The nature of trading and back office frameworks, control frameworks for separation of trading and back office activities is additionally inspected.

(iii) Continuous Review, Surveillance and Withdrawal of Rating

CARE continuously audits the already rated funds to sustain the ratings it has given. All things considered, month to month reports of the asset are analysed and thorough yearly assessment of the fund is also done. While the asset needs to keep up the credit score in line with the benchmark reserve scores in a specific month, CARE gives one month to the AMC to realign the score if the fund score breaks the benchmark. In case, the fund fails to improve during the permitted period, CARE would think about changing the rating assessment. Finally, the rating would be withdrawn on appeal made by the AMC with the notification time of one year.

3. Insurance Ratings

The share in the Indian insurance industry is roughly around 70 per cent that of life insurance and the balance 30 per cent by non-life coverage organizations. CARE's Issuer Rating for Insurance companies is a verdict on the basis of assessment done on the life and non-life insurance business, its financial ability and its capacity to respect the commitments made to the insured. The verdict on the commitments and ability to meet the obligations is not explicit to any particular insurance scheme.

The credit risk appraisal of an insurance agency starts by breaking down the different threats (the executives, industry, business, financial threat) at an independent level. CARE's investigation of issuer rating starts with a survey of the economy and the business in which the insurance agency works. The structure of the insurance guidelines and the company's competitive situation in the market is also examined. All this is followed by the 'RAMELS' system to evaluate the monetary strength of the respective insurance agency. Prior to doling out a rating, not a single factor but every contributing factor is considered in combination.

- *R (Risks Underwritten)*: The viability of an association's guaranteeing strength is brought out by its experience in the business, level of diversification in risks guaranteed and the overall development in business volumes. The factors that are assessed include market share, geographical coverage, diversity of risks guaranteed, pricing policy, expertise in the field of underwriting, competitive edge over its competitors, innovative products, claims coverage and its ability to tackle hefty risks arising due to catastrophes. A quantitative and subjective appraisal of the above components is completed by investigating the patterns of insurance premium collection, reinsurance surrendered, experience in managing claims and costs incurred on reinsurance business over a period of five years and above. Aside from the above mentioned, CARE also measures the existing as well as probable guaranteeing capability by studying the company's operating leverage.
- *A (Asset Quality)*: Ability to honour claims by the insurer could be hampered by future misfortunes that its investment portfolio might face. In regard of insurance companies, the quality of the asset to a large extent influences not only the revenue generation prospect but also has an immediate bearing on the insurance provider's capacity to arrange for immediate liquidity.The factors that the insurance provider assesses include diversification of portfolio, creditworthiness of the investments, level of NPAs and its acknowledgment standards, sufficiency of provisioning and liquidity of the portfolio.
- *M (Management)*: The quality of the management is a significant subjective viewpoint, which can have a considerable effect on an organization's performance. Back up plans should have the option to exhibit that they have developing and beneficial business. In this specific situation, CARE investigates the administration's objectives, mission, theory and so on and surveys the corporate methodology set down to accomplish the expressed objectives. CARE examines the operational

targets given out to singular groups or divisions to comprehend their importance by the general corporate technique which has an immediate bearing on key operational aspects.This includes a phase wherein CARE's group attempts conversations with key officers to comprehend the insurance agencies' points of view on the systems and plans intended to counter the environmental issues. Hence, experience and expertise of the executives to hold over times of emergency is perceived as an ideal trait.

- *E (Earnings)*: Beneficial activities are fundamental for insurance agencies to work as a going concern. CARE's estimation of income revolves around the insurance company's capacity to effectively interpret its strategies and competitive edge into growth opportunities and maintain overall revenues and profit. CARE investigates the productivity of the underwriting and investment aspects independently.
- *L (Liquidity)*: While examining insurance provider's liquidity, CARE would fundamentally look at the Asset Liability Management (ALM) profile of the guarantor. CARE would likewise analyse the effect of pressure tests on the ALM to comprehend its ability to endure shocks in case of an unanticipated loss of certainty, untimely and abrupt disasters or wide changes in the security markets.

NBFC Ratings

CARE's evaluations are an assessment on the relative capacity and readiness of an insurer to make ideal installments on the particular obligation commitments over the life of the instrument. Moreover, CARE has built up an extensive strategy for credit rating of financial instruments offered by NBFCs.

The beginning stage in arriving at a rating choice is a point by point audit of key proportions of monetary execution and soundness like capital adequacy, asset quality, resources, liquidity, quality of earning and a qualitative analysis of issues like ownership, management quality, risk management, compliance with the regulatory authorities, market share and presence, and accounting quality.

Housing Finance Ratings

Housing is a critical factor for development and advancement of the economy. Housing and financing of its related business in India have seen colossal development throughout the long-term. A portion of the variables that have prompted this development are –tax rebate to borrowers, increment in disposable income, alterations in the age profile of the house seekers, simple accessibility of advances, smaller family units and urbanization, and so forth.

14.3.3 Public Finance Ratings

CARE has a comprehensive system for the evaluation of the credit nature of states and nearby bodies.

1. State Government Entities

CARE ratings have rated around twelve state governments. These appraisals include those for the public space, for example, evaluations of state government ensured borrowings by State Electricity Boards, Irrigation Corporations and Road Development Corporations and one-time credit evaluations attempted at the particular solicitation of investors and business houses that had put up infrastructure projects in various states.

The state government's credit quality assessment is done by CARE on the basis of two broad aspects, namely, financial risk and economic risk.

Financial Risk: CARE assesses numerous economic and financial pointers fundamental in understanding the exhibition, possibilities and henceforth reliability of the state government.

(i) Revenue Performance: The assessment of the performance of the state government's revenue collection and generation is done by evaluating factors like the proportion of own tax revenues and non-own tax revenues in the total revenue generated, the state's share in the central government's tax collection.

(ii) Expenditure Management: While appraising expenditure management, CARE's procedure attempts to evaluate the viability of outlay control systems and productivity in the utilization of state assets. CARE rates those governments favourably whose consumption is in line with accessible assets. Specific consideration is paid to the creation of use, which is categorized as developmental and non-developmental.

(iii) Revenue Deficit: CARE is worried about the pattern and the degree of income deficit as it not just mirrors the nature of the management of state government funds but also possibly has the potential to raise forthcoming debt requirement of the state government. CARE opines that the size and pattern in the income shortage is a preferable indicator for measuring financial stress as compared to Gross Fiscal Deficit.

(iv) Debt Profile: CARE's debt profile analysis covers parameters like Debt/GSDP Ratio, Liabilities/GSDP Ratio, previous record of debt release, history of meeting liabilities, debt/revenue collections, pattern of the weighted average cost of debt and the pattern of debt composition.

(v) Liquidity Support: CARE concludes that the state government's failure to maintain the minimum balance with the RBI and its inability to use liquidity support offered by the RBI as a testimony for poor liquidity management.

Economic Risk: Economic risk evaluation is done to identify the economic strength and related weaknesses. While doing so, the following parameters are worked upon:

(i) Economic structure: CARE's analysis of the strength of the economic structure are based on factors like social and economic infrastructure, the growth in the annual GDP, business growth and quality of personnel and financial policies the structure of the investment policies. CARE believes that a state's tax prospective is considerably enhanced by a robust secondary and tertiary sector performance and it also gives a hint of the extent of stability in regular flow of revenues.

(ii) Demographics and Social infrastructure: CARE investigates the conventional demographic indicators, for example, per-capita income, level of poverty, extent of urbanization, literacy rates, rate of employment and so on since it accepts favourable socio-economic altogether to improve a state's development potential while simultaneously eliminating hard budgetary limitations of high allocations for social consumption.

(iii) Economic infrastructure: On the economic infrastructure front, CARE's assessment revolves around irrigation, transport, power and communication among others as it believes that proper economic structure is essential for economic growth.

(iv) Banking: CARE's assessment is that the accessibility of good financial framework empowers the preparation and development of reserve funds and investment inside the state and the availability of credit to encourage monetary movement.

(v) Agriculture: The agricultural output and its growth is assessed by CARE on the basis of factors like total amount of crops cultivated, area under irrigation, firm inputs used and agricultural productivity.

(vi) Political risk: Political stability and risk is a critical factor and is shown up after assessing the strength of the state government, perspectives of major ideological groups on significant issues, financial conditions, lawfulness and nature of the organization. The political link between the central and state governments is additionally considered as this may affect allocation and disbursement of funds from the central government in infrastructural projects and tasks taken up by the Public Sector Units, Railways, and National Highways etc., which may boost the state's economic surge.

2. Urban Local Bodies

CARE's credit rating of local civic bodies revolves around parameters like (i) *economic base* that include factors like nature of local economy, employment and income pattern of the neighbourhood, and indicators of development and accessibility of municipal services; (ii) *legal set-up* that includes issues like borrowing power and the limit, unresolved disagreements, authority to impose charges on clients, exact control over sources of revenue with a thought about the political ramifications of tax and client charge increase, mechanism for enforcing collection and curb on operations; (iii) *administrative issues* like organizational structure, responsibility sharing between the administrative and political wings, excellence and stability of management, extent of allocation, billing of tax, collection and prosecution machinery, previous performance in project implementation, extent of free hand enjoyed, MIS, and industrial relations; (iv) *prevailing practices in accounting* and the quality of the audits held; (v) *debt factors* like the structure of the existing debt burden, interest coverage ratio and debt service coverage ratio, assurances/inconvenienceson cash flows, dependency on short-term debt, alternatives existing to moneylenders, in the case of repayment default, as per the Act; (vi) *financial indicators* like budgetary and arranging measures, tax regime and past trends, movements in tax rates, recovery of costs from various municipal services, ability to bear financial shocks, revenue surplus/deficit, degree of financial assistance provided by the State, operating and collection competence, sources and distribution of capital expenditure, quantity of borrowings, if any, from non-governmental sources and the level of compliance with regard to borrowings enforced by such financiers; (vii) *project viability* like a project being constituted and act as a special purpose vehicle (SPV), source and application of funds in the concerned project, projected inflows and outflows during the life of the instrument, trend of revenue generation from the venture and scope of salvaging cost, promised financial assistance and other credit enhancement actions.

14.3.4 Infrastructure Sector Ratings

CARE's infrastructure sector rating envelops the appraisals allocated to debt projects of guarantors in the streets, broadcast communications and other such foundation related areas. CARE assesses financial reasonability of the task being financed, legitimate risk, legally binding system, credit improvement instrument and so on while allotting ISR.

1. Road Projects

   CARE looks at the expansive boundaries of the project undertaken as per the point by point project report presented by the contractor. The significant zones covered are the following:

   - The basic nature of the project like whether it is a by-pass or lane expansion, qualitative improvement of the road, bridge construction etc.
   - Who are the financers for the project?
   - What is the location?
   - What is the usual traffic demand and expected revenue generation as per the proposed toll pricing?
   - Project schedule.

NOTES

- Engineering Procurement and Construction (EPC) Contractor and terms and conditions of the contract.
- Operation & Maintenance (O & M) agency and the related contract.
- What is the impact on the environment and social life?
- The conditions listed in the Concession Agreement (CA), if any.
- Land acquiring status.
- The ability of the Engineering, Procurement and Construction (EPC) contractor, in light of specialized and monetary strength and experience.
- Insurance provisions.
- Capital structure and leverage.
- Earning possibilities.
- Debt Service Coverage Ratio (DSCR).

2. Power Projects

   The continuous liberalization measure has made the private sector more interested in the power sector. Power projects are capital intensive and for financing them, public funding is essential. CARE has built up a rating approach for debt issues of Power Producers (PPs). The factors that are considered during the rating process include the following:

   - The basic nature of the project like whether it is hydel, thermal, nuclear, wind, solar or any other non-conventional project.
   - What is the generation capacity?
   - Whereabouts of the promoters.
   - The location of the project viz. whether in the plains, hills, remote areas etc.
   - Requirement of fuel for operations and the availability of such fuel.
   - Infrastructural necessities to be developed by the power company.
   - Power distribution network.
   - Technical knowhow, and
   - Project schedule.
   - Available option for fuel supply.
   - Adaptability of the plant to utilize substitute fuels.
   - The regularity and quantum of rainfall in the catchment area and its impact on productivity in the case of hydro-electric project.

3. Ports

   India has 7,517-km long coastline with 13 significant ports and 187 minor ports, which handle greater part of India’s global exchange. The essential duty of improvement and the management of significant ports lies with the Central Government. These ports are represented by the Major Port Trusts Act, 1963. The non-significant ports are officially under the state government and are ruled by the Indian Ports Act, 1908.

CARE inspects wide-ranging factors related to the project on the basis of the project report forwarded by the client. The significant regions covered are the following:

- Location of the port
- Ease of operations with respect to draft, siltation, warehousing and departure facilities
- Ease of approachability to the port
- Contracts regarding loading / unloading of cargo
- Credibility of the client and other parties involved in implementing the project
- Financial arrangements
- Financial cushion in the case of time and cost overrun
- Regulatory clearance necessary for execution of the plans
- International trade policies formulated and followed by the government
- Patterns in global and local cargo routes and movements
- Revenue generation from various cargo types
- Adaptability and ability of the port to shift to different cargo types
- EXIM trends in the region
- Political uncertainty and risk
- Environmental guidelines
- Payback period of the project
- Extent of risk exposure to currency rate fluctuations
- Vulnerability to natural calamities and weather hazards
- Technology involved

Check Your Progress

1. What was the main objective of the Securitization and Reconstruction of Financial Assets and Enforcement of Security Interest (SARFAESI) Act?
2. Mention the essential values of CARE.
3. How does CARE draw the rating of Banks, NBFCs and Financial Institutions?

14.4 ANSWERS TO CHECK YOUR PROGRESS QUESTIONS

NOTES

1. Securitization and Reconstruction of Financial Assets and Enforcement of Security Interest (SARFAESI) Act was sanctioned to encourage banks to recuperate their non-performing resources without the mediation of the court. The Act empowers three elective strategies for the recuperation of non-performing assets, in particular securitization, asset reconstruction and requirement of security without the court's intervention.
2. The essential values of CARE are the following:
   - Integrity and Transparency: Commitment to be ethical, sincere and open in our dealings
   - Pursuit of Excellence: Committed to strive relentlessly to constantly improve ourselves
   - Fairness: Treat clients, employees and other stakeholders fairly
   - Independence: Unbiased and fearless in expressing our opinion
   - Thoroughness: Rigorous analysis and research on every assignment that we take
3. To draw the rating of Banks, NBFCs and Financial Institutions, CARE assesses the sector to which the firm belongs. This is followed by the appraisal of the business basics of the establishment utilizing the 'CRAMELS' model which represents:

   C - Capital adequacy

   R - Resource raising ability

   A - Asset quality

   M - Management quality

   E - Earnings quality

   L - Liquidity

   S - Systems

14.5 SUMMARY

- Credit Analysis and Research Ltd. (CARE) was established in 1993 and is the second biggest rating office (regarding rating pay) in the nation. The organization offers a wide scope of rating and evaluation of administration across different instruments and businesses.
- CARE attempts rating exercise dependent on data given by the organization, in-house information base and information from different sources that CARE thinks about is reliable.

- BLRs is used by banks to determine risk weights for their loan exposures, in line with the Reserve Bank of India's (RBI's) guidelines for implementation of the New Capital Adequacy Framework under Basel II framework.
- Securitization and Reconstruction of Financial Assets and Enforcement of Security Interest (SARFAESI) Act was sanctioned to encourage banks to recuperate their non-performing resources without the mediation of the court.
- Asset Quality survey starts with the assessment of the bank's credit hazard structure. The general asset quality is surveyed by assessing the area by area advance and assurance introductions.
- CARE dissects the constituents of banks' income structure by isolating them into those generation and fund related activities. Principal earnings are distinguished by not including non-recurring revenue from the total revenue.
- CARE continuously audits the already rated funds to sustain the ratings it has given. All things considered, month to month reports of the asset are analysed and thorough yearly assessment of the fund is also done.
- The share in the Indian insurance industry is roughly around 70 per cent that of life insurance and the balance 30 per cent by non-life coverage organizations.
- CARE's infrastructure sector rating envelops the appraisals allocated to debt projects of guarantors in the streets, broadcast communications and other such foundation related areas.
- The continuous liberalization measure has made the private sector more interested in the power sector. Power projects are capital intensive and for financing them, public funding is essential. CARE has built up a rating approach for debt issues of Power Producers (PPs).

14.6 KEY WORDS

- **Issuer Rating:** It is not for a specific instrument but oriented towards an issuer.
- **Capital Protection Oriented Schemes:** These are closed-ended hybrid mutual fund schemes with a clear focus on debt to achieve capital protection.
- **Per Capita Income (PCI):** It measures the average income earned per person in a given area, in a particular year. It is calculated by dividing the area's total income by its total population.
- **Bank Loan Ratings (BLR):** It is used by banks to determine risk weights for their loan exposures, in line with the Reserve Bank of India's (RBI's) guidelines for implementation of the New Capital Adequacy Framework under Basel II framework.

14.7 SELF ASSESSMENT QUESTIONS AND EXERCISES

NOTES

Short-Answer Questions

1. Write a short note on the vision and mission of CARE.
2. How is debt rating carried out for manufacturing units and financial institutions by CARE?
3. Briefly mention the 'RAMELS' system adopted to evaluate the monetary strength of the respective insurance agency.

Long-Answer Questions

1. Discuss the methodology adopted for monetary sector ratings by CARE.
2. Explain the procedure for conducting credit quality ratings by CARE.
3. 'CARE has a comprehensive system for the evaluation of the credit nature of states and nearby bodies.' Explain the statement.
4. Discuss the steps involved in carrying out infrastructure credit ratings by CARE.

14.8 FURTHER READINGS

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