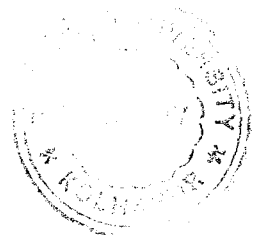


# **CHAPTER - I**

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## **INTRODUCTION**



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## CHAPTER - I

### INTRODUCTION

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#### 1.1 INTRODUCTION:

Finance is the lifeblood of industry. Without finance, industry cannot work. But most of the developing and under-developed countries of the world are facing the crisis of adequate medium-term and long-term industrial finance. Various countries have come up with various sources of industrial finance. In India, after the Second World War, Government established many financial corporations for the purpose of providing industrial finance to various industries. 'Karnataka State Financial Corporation' is one of them, which provides medium-term and long-term loans to industries. To solve the problem of industrial finance, Government established development corporations named 'Development Banks'.

The development banks have been playing a significant role in the field of industrial development of the country. After the Second World War, there was a strong demand of finance to industries for the purpose of modernization, reconstruction, expansion and diversification, establishment of new industrial projects and balanced industrial development. During the Five-Year Plans, the Government gave emphasis on the development of industries and on the financial institutions which provide industrial finance to the industries.

The small-scale industry occupies a key position in the structure of the country. The promotion of small-scale industry springs mainly from the fact that it has a large employment potential and ensures diffusion of economic power and better distribution of national income, so essential to achieve the egalitarian objectives of establishing a Socialistic Welfare State.

Small-scale industries, conceived and developed as an integral part of the total industrial structure of a country, help in the achievement of not only the purely economic objectives, but also certain socio-economic goals of economic planning. These industries create employment opportunities on a large scale at a relatively small cost, meet a substantial part of the increased demand for consumer goods and facilitate the mobilization of resources of capital and skills, which might otherwise remain inadequately utilized.

The sector also enjoys another advantage of easy dispersal. As the units do not require massive infrastructural facilities as in the case of large units, it is possible to reduce the regional imbalance by systematic dispersal. Therefore, in economic jargon, the term 'small-scale industries' boils down to the diffusion of income and wealth through the dispersed and decentralized development.

The State of Karnataka is endowed with abundant forest and mineral resources and offers great opportunities

for industrial development. The slogan 'Industrialise or Perish' made popular by Sir M.Visvesvaraya, has inspired the setting up of many prestigious industries in the State for nearly half a century. Carrying on that great tradition, the State is now offering special concessions and incentives for industrial investment and entrepreneurship through specialized agencies like the Karnataka State Industrial Investment and Development Corporation.

Karataka is well-suited for a number of agro-and mineral-based industries. In order to prevent concentration in and around the city of Bangalore and to attract entrepreneurship in other areas of the State where infrastructure has been and is being developed, special treatment is being provided in the backward areas of the State.

The basic industrial infrastructure is available in Karnataka and the State has traditionally enjoyed industrial peace. And thus, there is the unique climate in most parts of the State, cool and salubrious and surprisingly free from the rigours of either summer or winter.

Karnataka State Financial Corporation, which, prior to November 1973, was known as Mysore State Financial Corporation, was established on March 30, 1959, that is to say, on the last but one day of the financial year 1959-60. Although the State Financial Corporations Act came into effect as far

back as August 1, 1952, the then Government of Mysore established the Corporation several years later. In the Reserve Bank's Report on Currency and Finance for the year 1955-56, it was stated that "Mysore Government have also decided to set up a Financial Corporation". However, this event happened four years later. It has not been possible to find out the reasons for the delay in the establishment of the Corporation.

During its existence for the last 30 years, the Karnataka State Financial Corporation has grown by leaps and bounds. The Corporation has spread its activities in all the districts of the State. Now the Corporation has branch offices in every district headquarters. The branches are empowered to consider loan applications upto Rs.8.0 lakhs from local entrepreneurs. The main emphasis in extending delegation of power to the branch offices is to assist more and more small and tiny sector projects.

Karnataka State Financial Corporation has been playing a pivotal role in supplying industrial finance. So, an attempt is made in the present study to analyse and to study the industrial finance of Karnataka State Financial Corporation during the period from 1986-87 to 1988-89.

## 1.2 DEVELOPMENT BANKING IN INDIA:

The need of development banks in India was felt very strongly immediately after attainment of Independence, to

fill the gaps in the capital market. The capital market in India was ill-equipped for providing the needs of long-term industrial finance.<sup>1</sup>

Thus, the need of specialized financial institutions to meet the requirements of the finance was recognized as early as 1931. It was also realised that such financial institutions needed to be established both at national and State level. The first development Bank is the Industrial Finance Corporation of India, established in 1948. Its objective was to make long-term credit available to the public limited companies and industrial cooperatives.

The establishment of the financial institutions at the State level was considered almost simultaneously and the Government of India enacted the State Financial Corporations Act, 1951.

The Industrial Development Bank of India, which is the apex development bank of the country, came into existence in 1964, for the industrial finance through different institutions.

#### **1.2.1 Definition and Objectives of the Development Banks:**

A development bank can be defined as:

"An institution established principally or solely to provide long-term financing for industry and

for undertaking development activities for the industry".<sup>2</sup>

In the light of the above definition, development banks have been designed to function as a development agency with special responsibility to:

- (a) undertake investment market research and a survey of techno-economic studies;
- (b) provide technical and administrative assistance for promoting, management and expansion of industry; and
- (c) plan and promote the development of industries to fill vital gaps in the industrial structure.<sup>3</sup>

Thus, the development bank functions to provide long-term finance to industries as well as to promote the industrial development through the activities such as discovery of investment projects, preparation of project reports, technical and managerial services to industries, etc.

#### **1.2.2 Scope of Development Banks:**

A development bank is a financial institution, engaged in providing medium and long-term assistance to business units in the form of loans, underwriting, investment and guarantee operations. There may or may not be complete freedom with regard to operations in all these areas, especially in the matter of underwriting and investment, which carry a larger risk element than the provision of loans.<sup>4</sup>



A development bank is expected to do something more than the provision of capital over the years. A wider role has been envisaged for the institution such as acting as a catalytic agent in promoting development by initiatives and services in other spheres too, such as discovery of investment projects, undertaking the preparation of project reports, provision of technical advice and management services and finally, on some occasions, establishment and management of industrial units. In fact, in a few countries, development banks have also been entrusted with the responsibility of preparing comprehensive economic plans for the country.

There is an important question of the extent to which a development bank can undertake safely what might be regarded as truly promotional role, for beyond a point, there may be a conflict of interests between the promotional role and the financing role of these institutions. The problem can be solved by establishing separate institutions for undertaking promotional activities, leaving the financing part to be undertaken by other institutions. This was the primary motive, for example, for the establishment of the Industrial Development Corporations in most of the States.

### **1.2.3 Distinction between the Development Bank and a Finance Corporation:**

The distinction between the development bank and a

finance corporation or a term-financing institution can also be drawn on the basis of whether or not the institution provides assistance in the form of underwriting and direct investment. If the function is not performed, then the institution is called just a finance corporation or term-lending agency.<sup>5</sup>

Although, generally, development banks are meant to meet the capital requirements of the private sector of an industry, with increasing State participation in industrial growth, the development banks can also act as providers of long-term finance to public sector institutions. On the consideration that a financial institution can do a better job of investment appraisal and surveillance of a project than a Government Department can, the same institution can provide finance to the public and private sectors or separate institutions could be considered for the purpose, even as there should be separate development banks for meeting the needs of specific sectors of the economy such as manufacturing, power development and agricultural development. Even within the same sector, such as manufacturing, one could think of separate institutions for large, medium and small units.

Besides the provision of financial assistance, entrepreneurial guidance, etc., development banks are also expected to play an important role in promoting the saving and investment habits, raising standards of corporate management and acting as watch-dogs of the interests of

investors generally. Provision of management training to prospective entrepreneurs and officials of companies is regarded as yet another function of a development bank.

In short, a development bank is a multi-purpose institution, with a broad developmental outlook that used to be generally associated with commercial banks.

It should be noted that a considerable variety of development banks set up in response to the varying needs of different countries and of different times of the same country.

#### **1.2.4 State Financial Corporation as a Development Bank:**

In 1948, the establishment of the Industrial Finance Corporation of India marked the beginning of the institutionalization process in the country.

In 1951, the State Financial Corporations, as development banks, started their working in different States of the country. Now, along with State Financial Corporations, totally 60 development banks such as National Industrial Corporation of India, Industrial Credit and Investment Corporation of India, State Industrial Development Corporations, Small Scale Industrial Development Corporations, etc., are working in the country. All these development banks are providing finance to industries, after obtaining refinance

from the Industrial Development Bank of India. As important development banks, the State Financial Corporations are providing finance to small and medium scale industries in all the States of the country. Finances upto Rs.80.0 lakhs provided by the State Financial Corporations to the industries are automatically made available as refinance from the Industrial Development Bank of India.

### **1.3 SMALL-SCALE INDUSTRIAL SCENARIO IN KARNATAKA STATE:**

The State of Karnataka is full of forest and mineral resources and offers great opportunities for industrial development. There are many large and prestigious industries, which have made name in the State. With all the industrial infrastructure available in the State, it also enjoys the traditional industrial peace and a unique climate to suit all types of industries. This has made the State to be one of the industrially forward States in the country.

A large number of medium scale units are located in the State in the fields of engineering, chemicals, pharmaceuticals, food-processing, textiles, minerals, electricals and electronics, etc.

The Government of Karnataka, through the State Department of Industries and Commerce, is providing all the encouragement and assurance for industrial growth in

the State and especially, for setting up of small-scale industries in the backward and rural areas of the State.

Table 1.1  
Number of small-scale industries  
registered in Karnataka

Year	SSIs registered during the year	Cumulative registration of SSIs
1986-87	11,179	75,526
1987-88	10,530	86,056
1988-89	9,811	95,867

Parappanavar, S.S., "A Study of the Progress of Small Scale Industries in Karnataka State with Special Reference to Karnataka State Financial Corporation, 1990.

Table 1.1 shows that as at the end of the year 1986-87, there were 75,526 small-scale industrial units registered in the State and their number went up to 86,056 units by the end of the year 1987-88, i.e. a little over 10,000 units were registered during the year 1987-88. During the year 1988-89, 9,811 small-scale industrial units were registered and as at the end of the year 1988-89, the total number of the registered small-scale industries in Karnataka State stood at 95,867.

As per the information obtained from the Directorate of Industries and Commerce, the total investment in these small-scale industrial units is nearly Rs.860 crores and the total employment generated by these units is well over 7.0 lakh jobs.

Bangalore Urban District, with 17,854 units, accounts for nearly 19% of the total registered small-scale industries in the State. Mysore district, with 9,129 units (9.5%), stands second and is closely followed by Belgaum District with 8,445 units (8.8%). Other districts, where major number of small-scale units are located, are Dakshina Kannada (7,175 units), Dharwar (7,844 units), Tumkur (5,523 units) and Shimoga (4,106 units).

Karnataka State Financial Corporation is also playing an important role in the establishment of small-scale industries in the State. The details of the Karnataka State Financial Corporation's assistance to the small-scale sector are discussed in Chapter-IV. However, a broad reference to the assistance provided to the small-scale sector is made at this juncture. Out of the total 11,179 small-scale industrial units registered in the State during the year 1986-87, the Karnataka State Financial Corporation has assisted 4,239 units (38%). In the year 1987-88, out of the total 10,530 registered small-scale industrial units, the Karnataka State Financial Corporation assisted 4,232 units (40%); and during the year 1988-89, out of the total 9,811 registered small-scale industrial units, 5,078 units (52%) were assisted by the Karnataka State Financial Corporation.

All these figures clearly indicate the major role played by the Karnataka State Financial Corporation in the

development of the small-scale industries in the State of Karnataka.

#### **1.4 OBJECTIVES OF THE STUDY:**

The main objectives of the present research work are as follows:

- (1) To understand the various schemes introduced by the Karnataka State Financial Corporation from time to time to assist small-scale industries in Karnataka;
- (2) To study and examine the nature and extent of the financial assistance provided by the Karnataka State Financial Corporation to the small scale industries in Karnataka during the period from 1986-87 to 1988-89.

#### **1.5 RESEARCH METHODOLOGY:**

The study is completed by using the secondary data only. Published annual reports and other pamphlets published from time to time by the Karnataka State Financial Corporation are mainly used for the collection of necessary data. In this study, the researcher has also used the descriptive and receive method of research.

#### **1.6 CHAPTER SCHEME:**

This research work is divided into Five Chapters.

**First Chapter** deals with the introduction, stating therein the nature and importance of development banking, financial corporations, small-scale industries in Karnataka and objectives of the study. **Second Chapter** contains a discussion about industrial finance and financial institutions in India. In the **Third Chapter**, the working of the Karnataka State Financial Corporation has been described. The financial assistance provided by the Karnataka State Financial Corporation during the period of three years from 1986-87 to 1988-89 is explained in the **Fourth Chapter** and the important conclusions and suggestions of the study are recorded in the **Fifth Chapter**.



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