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Development Banking in India

Preeti Bansal[1], Vipin Kumar[2]
vipinbnsl007@gmail.com

Abstract: Development Banking is form of financial intermediation that provides financing to high priority investment projects. This paper focuses on the meaning of Development Banks, their functions, difference between Development Bank and Commercial bank along with their critical evaluation. Table is used to show the financial assistance sanctioned and disbursed by Development Banks, taken from the site of RBI-respective financial institution.

The meaning of Development banking is different for different people, for different places, and also for different times. This only goes to show that development banking has evolved since it was first conceptualized as an 'instrument of development'. However, in its original form and in its broadest definition, it is a type of financial intermediation to help the country reach a higher and sustainable level of development. On the wider context, the desired level of development includes the whole spectrum of socio-economic progress. Development banking therefore can also be defined as a form of financial intermediation that provides financing to high priority investment projects in a developing economy. Both definitions imply that the purpose of development banking is to bring the country to a higher level of development.

Introduction and definition of development bank

A development bank is a 'bank' established for the purpose of 'financing development'. Development banks are specialized financial institutions which provide medium and long term finance to enterprises. These banks perform twin functions of providing medium and long term finance to entrepreneurs and performing various promotional roles conductive to economic development. The financial assistance is sanctioned to promote and develop important sectors like agriculture, industry, import-export, housing and allied activities. They do term lending, investment in securities and other activities.

Development banks are those financial institutions whose prime goal is to finance the primary (basic) needs of the society. Such funding results in to growth and development of social and economic sectors of the nation.

Rationale in setting up Development bank

The need for development banks stemmed from the following reasons. First, India needed an "instrument" to accelerate long-term Investment to achieve rapid growth and create employment. Second, to achieve a higher degree of efficiency and in pursuit of Employment objectives, a policy decision was taken to rely on the private sector as engine of growth. Third, the then existing financial sectors in India were dominated by commercial banks which were contented with short-term banking activities and were either not willing nor not in a position to support national priorities of long-term investment in the real sectors. Finally, it was generally felt that there was a clear case of market failure, requiring national government to intervene in the financial markets. The common underlying principle however is that long-term resource allocation should be done by business-oriented financial institutions vis-à-vis direct allocation by the government.

Difference between development bank and commercial bank

1. Commercial bank lend for short term requirements of trade and industry primarily for working capital purposes, the development banks lend for medium and long periods, mainly for the purpose of investment in fixed assets for the establishment, diversification, modernization etc. of industrial units.
2. Developments banks as compared to commercial banks not only provide finance for the establishment of industrial units, but maintain close liaison with them, guiding, supervising and advising the entrepreneurs throughout the period of loans.
3. A development bank is created as an instrument of economic development while a commercial bank is created by business opportunities.

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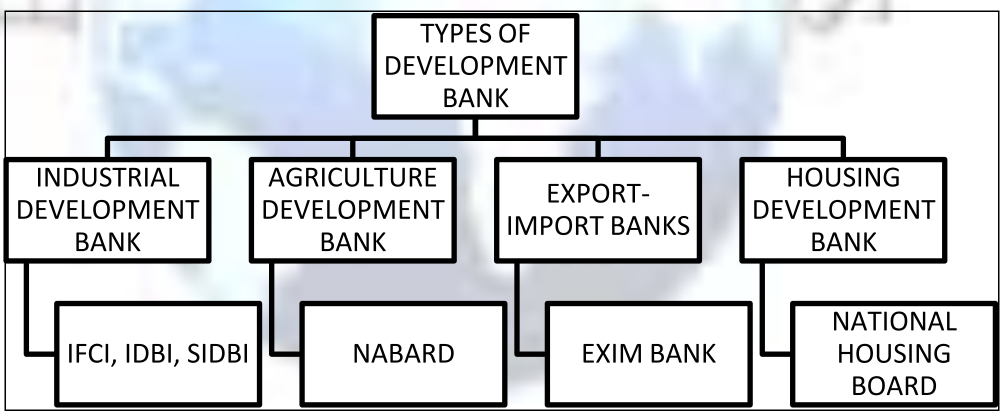
4. A development bank is supposed to be pro-active as it should take an active role to promote projects and to develop institutions (entrepreneurs). The projects chosen are those that are consistent with the economic development priorities. A commercial bank is known to be reactive to business opportunities. It requires bankability only after the entrepreneur's decision has been made; it waits for the idea to culminate into a funding requirement
5. A development bank is dependent on concessionary, long-term funds, e.g. pension funds, funds from multilateral financial institutions like the World Bank, Asian Development Bank, etc. It has traditionally limited access to domestic or commercial funds. A commercial bank has a strong deposit base and its corporate borrowers are also depositors. They can match its commercial borrowing against its own short-term loans.

Functions of development bank

1. Development bank promote and develop SSI.SIDBI provide direct project finance and equipment finance to small scale industrial units
2. Development banks finance the development of housing sector in India. National Housing Board refinances bank and financial institutions that provide credit to housing sector.
3. Development banks facilitate the development of large scale industries in India. These banks provide merchant banking services such as preparing project reports, doing feasibility studies, advising on location of projects and so on.
4. Development bank NABARD helps the development of agriculture sector and rural India.
5. Development bank- EXIM BANK enhance the foreign trade of India by providing medium and long term loan to exporter and importer.
6. Development bank help to review (cure) sick industrial units. IIBI is main credit and reconstruction institution for revival of sick industries. It facilitates modernization, reconstruction and diversification of sick units by providing credit and other services.
7. Development bank encourages the development of Indian entrepreneurs. NABARD, SFCs etc, provide training to entrepreneurs in developing leadership and business management skills.
8. Development bank promotes economic activities in backward areas of the country. They provide finance for started companies in backward areas.
9. Development banks contribute in growth of capital market. They invest in equity shares and debentures of various listed companies in India.



A) **Industrial development Bank**

Various Industrial Development Bank like IFCI, IDBI, ICICI, SIDBI etc. provide medium and long term finance to industries. IFCI was the first Industrial development institution established in 1948.

B) **Agriculture development bank**

NABARD was established in 1982 with a view to strengthen the agriculture finance.

C) **Export-Import Development Bank**

To provide financial facilities to export-import trade, EXIM BANK was established in January 1982.

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D) **Housing Development Bank-**

NATIONAL HOUSING BANK is the apex institute of housing finance with the objective to develop and finance housing activity.

FINANCIAL ASSISTANCE SANCTIONED AND DISBURSED BY ALL INDIA FINANCIAL INSTITUTIONS					
(Rs. Crore)					
	2007-08	**2008-09**	**2009-10**	**2010-11**	**2011-12 P**
1	**2**	**3**	**4**	**5**	**6**
1. Industrial Finance Corporation of India Ltd					
(i) Sanctioned	2550.5	4014.9	7007.2	12259.9	4467.1
(ii) Disbursed	2280.1	3311.5	6045.4	8399.6	5949.6
2. Industrial Development Bank of India					
(i) Sanctioned	Na	Na	na	na	na
(ii) Disbursed	Na	Na	na	na	na
3. Small Industries Development Bank of India					
(i) Sanctioned	16146.3	29216.7	35545.2	42213.7	43339.6
(ii) Disbursed	15099.3	28317.8	31941.9	38795.9	41812.4
4. EXIM Bank					
(i) Sanctioned	35006.4	35246.9	40193.8	51014.8	47167.8
(ii) Disbursed	29199.7	29964.2	33636.1	35576.8	38406.2
5. National Bank for Agriculture and Rural Development					
(i) Sanctioned	44572.3	54218.8	53566.9	68336.1	86231.1
(ii) Disbursed	38244.7	49965.7	49132.5	59949.0	79330.5

Source: Reserve Bank of Indis-Respective Financial Institutions. na: Not available.

Achievements of development banks

1. Since their inception the development banks have supplied adequate invisible funds for the development of industries.
2. The development banks have emerged as the most important underwriting institutions in the primary market.
3. The rigorous scrutiny by the development banks prior to sanctioning assistance to industries has improved the quality of industrial projects.
4. These development banks have prompted the development not only large scale industries but also of small scale industries.
5. The development banks have also lacked the problem of industrial sickness
6. The development bank has solved the problem of regional imbalances by promoting industries in backward areas.

Shortcomings of development bank

1. The development banks prefer to give loans to the already established units. It hampers the growth of new industries in the countries.
2. The development banks do show much interest in underwriting, even though this is extremely important from the viewpoint of economic growth.
3. The development bank has failed to solve the problem of industrial sickness.

Apart these development banks could not tackle the problem of unbalanced regional growth. The interest of small units in the way of financial assistance is also ignored by development banks. Lack of own capital resources incapacitates these institutes to achieve their objectives.

Suggestions for improving the working of development banks

The Development Banks should be allowed more autonomy in their working. Only Competent professional persons should be appointed as the chief executives of development banks. The development banks should have the sole responsibility in loan sanctions. The development banks should borrow from the capital market at market related rates. Development banks should be globally competitive. They should adopt internationally accepted norms, and restore capital adequacy.

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Conclusion

Development banks in the country have significantly, contributed to the process of industrialization. As a result of the establishment of specialized financial institution many shortcomings of the industrial finance organization of the country have been removed. In the absence of these institutes, rapid industrialization would never have been possible. These institutes have not only given financial assistance to the industries, but have also facilitated the establishment of new industries. Technical assistance has been provided to the industries. Special efforts have been made to spread the industries in the backward regions of the countries.

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