CHAPTER 6

THE CHANGING STRUCTURE OF INDUSTRIAL FINANCE IN JORDAN AND INDIA

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6.1 INTRODUCTION :

Industrial finance forms a crucial part of industrial economics. The sources of finance and its effective utilization play a complementary role pertaining to the overall economic development of a country. Various authors have described "Industrial finance as the life blood of industry which acts as a prerequisite for mobilising real resources to organise production and marketing".

Industrial finance forms a very vital aspect of industrial economics, the existence of which revolves around two principles :

- Firstly the source from where the finance is sought, and
- Secondly how efficiently can it be utilized.

The financial behaviour of an economy can be judged by its varied financial instruments that play a key role in actual practice.

Broadly speaking industrial finance means "the provision of funds needed by an industry irrespective of the period for which they are made available".(1) However, the task of procuring an adequate supply of industrial finance has many sides to the picture. The job of evolving a regular supply of industrial finance primarily depends upon the overall savings generated in an economy. The savings once generated need to be effectively channelled into profit-seeking investments.

Public policy measures have a direct effect on industrial finance in several ways. Taking the example of India, the most significant can be cited as government purchase of shares, loans by the financial institutions like State Financial Corporations (SFCs), Industrial Finance Corporation of India (IFCI), Industrial Development Bank of India (IDBI), Industrial Credit and Investment Corporation of India (ICICI), Unit Trust of India (UTI), Life Insurance Corporation of India (LIC), etc., arrangement of finance from domestic and foreign institutions, and loans granted by the commercial banks to industrial sectors.

Hence financial needs can be fulfilled depending on the type of production, various aspects of payments involved and type of loans required i.e., short term, medium term or long term.(2)

This chapter primarily deals with the comparison of the many facts of industrial finance involved both in India and Jordan. A comparative study would help significantly in understanding the role of various financial institutions in providing finance to industry in Jordan.

To understand the concept more clearly and to judge the differences in the structure of industrial finance in India and Jordan, this chapter has been divided into two parts - the first part elucidating the sources of industrial finance in India which mainly covers commercial banks and six financial institutions viz. SFCs, IFCI, IDBI, ICICI, UTI and LIC; and the second part includes the sources of industrial finance in Jordan which mainly covers commercial banks and Industrial Development Bank of Jordan (IDBJ), the main financial institutions providing finance to industry.

Part A

6.2 INDUSTRIAL FINANCE IN INDIA

Over the past few decades, the Planning Commission in India has given priority to the industrial growth because it has been realised that the economic development of the country is not possible without adequate industrial growth. As finance is the most important input, the importance of industrial finance has increased and the involvement of the government and the other financial institutions in providing short-term, medium-term and long-term finance to industry has significantly increased.

Ever since the independence and specifically after the second five year plan (1956-1961), there has been a change in the structure and pattern of industrial finance. Not only this, there has been a non-ending increase in competition in all the markets of the world, with India not very far behind. The growth of industrial finance has definitely been the most significant post-independence event.

As we know that organised sector primarily needs two types of finance - Fixed capital / block capital and floating / short term capital. Long term capital fulfills the massive loans required for the establishment or sizable expansion or moderanisation of the industry, whereas short term capital or the floating capital is required for the smooth and regular functioning of the industrial unit. Whether it is a long-term or medium term or short-term requirement, the industrial units have to depend on commercial banks and/or other financial institutions, apart from raising funds from the general public.

According to the National Planning Commission of India, finance cannot be segregated from Industrial Management as both are inter- dependent. Striving for profit-seeking opportunities is a necessary step for industrial finance subsequently after which the finance evolved can be activated for necessary deals.(3)

Careful examination of the various sources of finance would help to analyse the industry's financial condition in India. These sources can be classified into following categories -

(1) Internal finance mainly consisting of retained earnings.

(2) External finance raised through sale of shares, debentures; by accepting public deposits; through commercial banks, and from other financial institutions mainly providing finance to industry.

Internal finance is ideally raised by the company itself and is utilized as short term credit. Once a company has the ability to retain a part of its profit as capital, its dependancy on external sources declines to a large extent.

External funds too are utilized on a short term credit basis, used in the form of bank loans, trade credits, etc. Fixed deposits with companies has gained ground in India and has become a very easily accessible means of financing in all short term, medium term and long term credit.

As regards long-term capital, finance is generally obtained as shares, bonds and debentures and also loans. The active financial participaters are the Industrial Development Bank of India, Industrial Finance Corporation of India, Industrial Credit and Investment Corporation of India, State Financial Corporations, and so on.[4] Along with this, Unit Trust of India and Life Insurance Corporation of India also play an important role in providing finance to industry. All these institutions are discussed in detail in the latter section of the chapter.

With a rising complexity in the working of financial institutions of India, industrial finance has very much come into the limelight. The government of India in its post-independence economic declarations has emphasised the need for allocating powers in the hands of such finanical agencies which would not only concentrate on enhancing the economic strength of the country but at the same time ensure equitable distribution of wealth. This concept has been validated with the assurance of similar economic strategies for both the public and private sectors. There has been the nationalization of private banks and Life Insurance, along with the establishment of special financial institutions that are solely responsible for channeling the available resources to various sectors, primarily industries.

The principle financial intermediaries entrusted with the task of facilitating the need of finance by industries and business can be listed as -

(1) Commercial Banks

(2) Specialized Credit Institutions

(3) Corporations such as the UTI and LIC.

(4) Indian Capital Market

6.2.1 Commercial Banks :

From the time of their establishment, commercial Banks have followed the stringent financial policy of confining themselves to forwarding short term self liquidating transactions. Their assets lie in the highest form of liquidity. Such a bank can be called "truely liquid" only if it ensures the involvement of lesser risk as well as the convertability of assets. As a rule, commercial banks run on the basic principle of deposit banking in which the money received as deposit is subsequently channeled to industry and commerce. Investment banking runs on the principle of profitable sale of shares and debentures purchased by investors.

Commercial banks being important elements of the Indian financial structure over the past few decades, increasing attention has been paid on their role as financers of private industries and commerce.

Indian banking has come a long way having undergone major evolutionary changes from unsound and uneconomic banking during the post-independence era to the restoration of a unified, consolidated and compact banking system with a highly mechanised machinery today. Therefore transforming the age old idea of limiting the role of banks to fulfill temporary financial needs, today commercial banks have become a part and parcel of industrial financing. The commercial banks also undertake the task of evolving newer concepts of financing such as term lending, underwriting of issues and corporate securities.

The pre-independence picture of banks depict the continuation of the age old conventional practice of self liquidating short term credit. Commercial banks were considered as the only financial intermediaries for granting loans to business houses.

There was a total lack of new industrial entrepreneurs due to the restricted role played by banks and absence of long term financing facilities by financial intermediaries. Hence growth of the industrial sectors was highly restricted as they primarily depended on their internal savings. Any incoming profitable opportunities could not be substantiated due to lack of financial aid.[(5)]

The post Nationalization period of banking can be viewed in a number of ways. An ardent attempt was made via government policies to ensure total segregation of such institutions from individual concerns as well as to promote certain roles in both the public and private sectors that may run parallel to each other and as rightly stated "to be viewed as a part of a single mechanism". Various financial mechanisms have now been handled by a number of public authorities. There was also the nationalization of private institutions which included RBI (1948) as well as LIC (1956).

The relationship between a planned economy as well as its financial system has been interestingly dealt with by E. Nevin, who says that 'The financial instruments of a planned economy should be complementary to the policies laid down by the government'

The financial resources should have a specific pattern of allocation and distribution of maximum benefits are to be derived from the acquisition of credit. This can be possible only if the government has an upper hand on both credit and finance.

Policies of development have altered the concept of industrial finance in India. There has been a greater awareness of institutional financing facilities as well as the increasing hold of public authorities on the financial system of the country. This has in turn helped to erase the age-old managing agency system.[6]

It is generally believed that the first important event that has gone into providing the necessary direction for setting up a public sector banking system in the under previledged areas of India has been the nationalization of 14 major commercial banks in the midst of economic instability in the late 1960's.

Undoubtely there has been an affinity on the part of the commercial banks in a developing economy as that of India to concentrate its working on the urban areas and flourishing sectors of the country.

However, the Indian economy is framed in such a manner that it expects equitable distribution of wealth and social equality among people. Today the stringent financial theory of banking has been left far behind and commercial banks have entered new fields of term lending and underwriting.

The commercial banks in India have adopted the American model of term lending in which these banks recognise short and medium term loans. This procedure of term lending was adopted in the aftermath of the world war II in order to overcome the severe financial depression prevailing in the country.

There are two important factors which encouraged the role of banks in medium term lending. These included - emphasis laid on industrialization in the second five year plan (1956-1961) and the incresing demand from small scale industries for finance. The plan clearly brought out the ability of the country to set up greater economic facilities for rapid expansion of industries along with an industrialization boom. This necessecitated the need for medium term financing.

A formal scheme of term loans was forwarded by the Government of India in 1958 and the Refinance Corporation for Industry (RCI) was the special institution created for this purpose. The entire task of term lending was given to RCI so much so that banks continued to contribute in their own way by behaving as promotional distributors.

The rules laid down for fulfilling the eligibility criteria for giving loans to industries ranged from 3 - 7 years and the lower and the upper limits of loans was restricted to Rs.5 lakhs and Rs. 2.4 crores. However, after the establishment of IDBI, the lower limit has been raised to Rs.100 lakhs for refinance.

The total advances sanctioned and disbursed by commercial banks between 1975-76 and 1989-90 to industry is shown in Table No. 6.1.

Table 6.1

Total Advances Disbursed by Scheduled Commercial Banks to Industry

YEARS	LOANS DISBURSED	
	Amount (in Crores)	Percentage of total Industrial Finance
1975-76	5713	48.9
1980-81	12220	49.1
1985-86	23970	42.7
1986-87	31386	46.0
1987-88	33243	46.6
1988-89	41655	47.3
1989-90	50846	48.8

Source : Report on Currency and Finance, 1976 till 1990, Volume I, Economic Review

Table 6.1 gives a relative picture of credit advances by scheduled commercial banks to industries in India between 1976 and 1990. The total credit given by these commercial banks was Rs.5,713 crores in 1975-76, amounting to 48.9 percent of the total credit given to industry. The total amount of credit given increased to Rs.50,846 crores in 1989-90, which is 48.8% of the total credit given by commercial banks. It means that share of commercial banks has remained more or less the same during the period under study. The percentage of credit extended to the industrial sector has been slightly lower than 50 percent of the total bank credit disbursed, with an overall average of 47% during the period under study i.e., 1978 to 1990. The total credit given by commercial banks increased from 48.9% in 1975-76 to 49.1% in 1980-81 which was record of all time high during the period under study. This was because of substantially higher rates of growth than the preceeding year in aggregate deposits, non-food credit and cash in hand, and balances with the RBI being the major highlights of banking trends in 1980-81. But its share declined to 42.7% in the year 1985-86. Since then, the share of scheduled commercial banks in the total credit to industry has been continuously increasing. It increased to 46.0% in 1986-87, 46.6% in 1987-88, 47.3% in 1988-89 and to 48.8% in the year 1989-90. These data reveal one thing that the contribution of commercial banks in terms of total credit to industry has remained significant since 1975-76 and therefore the role of commercial banks in bringing the industrial growth cannot be ignored.

In recent years, there has been a substantial growth and diversification in the Indian financial system. There has been a gradual introduction of liberalisation in the banking industry which has helped in imparting a greater flexibility to its operations.

6.2.2 Specialized Credit Institutions :

On analysing the functioning of the specialized credit institutions, it can be well explained that they work as bridge to fill the gap between normal financial activities. Such institutions have played a highly participatory role in enhancing the day to day working of the modern financial system of India. According to Prof. L.C. Gupta these institutions have been appropriately termed as 'development banks' primarily because of the availment of quick finance to innumerable upcoming industries and development projects.

The specialized credit institutions have well assisted in providing finance in fixed assets, thus widening the channels of real investments.

In India, it has been observed that the small scale and medium scale industries require maximum financial assistance. A very important factor that helped in compelling the government of India to set up specialized credit institutions was the lack of proper supply of finance to all the segments of industrial sector of the economy.

The smaller companies which have a paid up capital of below Rs.25 lakhs were regarded as small scale companies. Such companies faced difficulties with respect to obtaining loans, as for such small issues, much interest is not shown by the public. However, with the rapid growth in the industrial sector, the problem of industrial financing has assumed great importance.

The following are some of the most important credit institutions fulfilling the needs of industrial finance in India -

(A) State Financial Corporation (SFC) :

The contemplation for the setting up of separate financial corporation in various states by the government was made during the establishment of the IFC which was primarily set up with the aim of fulfilling the requirements of public limited companies, however excluding the small scale and medium sized industries whose financial requirements were highly diversified.(7)

It was from August 1st, 1952 that the State Financial Corporation Act came into play in order to satisfy the credit requirements of all the small and medium scale industries located in various states and union territories. These institutions have proved to complement the activities of the Industrial Finance Corporation.(8) In accordance with the State Financial Corporation Amendment Act, 1985; the corporation provides assistance to those industrial corporations whose paid up capital does not exceed Rs.3 crores. Assistance is forwared mainly via loans, underwriting of shares, bonds and debentures.

Till the late 1960's, concentration was more in providing assistance to the medium scale industries. However, this trend has now been diverted towards the small scale industries. Today the State Financial Corporations have formulated several schemes that cover all fields of industry such as agrobased industries, textiles, food processing, mining, quarrying, paper products, engineering and manufacture of machines.

Presently 18 SFCs are operating in the respective states and union territories. There is also a greater dependance on the IDBI refinance facilities as the finance raised by SFC through bonds and debentures have not kept pace with the rapid growth in the operation of this corporation. Its operational policies also keep into consideration the development of backward regions and promotion of new entrepreneurs.

State Financial Corporations cater to the financial needs of small and medium scale enterprises. They have particularly been of use to small industries in order to assist the rural artisans and the new technician entrepreneurs. With their overgrowing and diversified activities, the SFCs have come to occupy an eminent position in the institutional set up for industrial development in the country.

The total advances sanctioned and disbursed by State Financial Corporations between 1975 and 1976 and 1989-90 to industry are shown in Table No. 6.2.

Table 6.2

Total Advances Sanctioned and Disbursed by State Financial Corporations to Industry

YEARS	LOANS SANCTIONED		LOANS DISBURSED	
	Amount (in Crores)	Percentage of total Industrial Finance	Amount (in Crores)	Percentage of total Industrial Finance
1975-76	162.3	26.8	99.4	24.7
1980-81	383.2	16.9	249.0	17.7
1985-86	1008.7	17.2	607.2	14.3
1986-87	1244.5	17.2	784.1	15.3
1987-88	1352.2	15.8	933.6	14.8
1988-89	1468.6	9.7	1048.0	11.0
1989-90	1561.6	9.1	1154.3	10.8
Compound Growth Rate per annum				
1976-90		16.2		17.7

Source : RBI report on Currency and Finance, pp.97

The table no. 6.2 gives an analysis of the operational efficiency of State Financial Corporations between 1976 and 1990, the period under study. This table shows the amount of loans sanctioned and disbursed by the SFCs at the end of March every year. Till about 1970, the operations of SFCs grew at a rather slow pace but after 1970, there was a rapid growth in their operations. This pace of growth was sustained even in the 1980s. This can be seen from the data given in the table.

The total loans sanctioned increased from Rs.162.3 crores in 1975-76 to Rs.383.2 crores in the year 1980-81, which shows an increase of Rs.220.9 crores. Since then, the total loans scantioned has continuously increased and had reached the level of Rs.1561.6

crores in 1989-90. But the growth performance of the SFCs however showed variations during the different years. On the other hand, the loans disbursed by SFCs rose from Rs.99.4 crores in 1975-76 to Rs.249.0 crores in 1980-81 and further to Rs.1154.3 crores in 1989-90.

Although the total amount of loans sanctioned and disbursed has increased in absolute terms during the period under study, but the relative growth rate was not favourable. We can see from the table that the total share of SFCs in terms of loans sanctioned has reduced continuously from 26.8% in 1975-76 to 9.1% in 1989-90, barring a slight growth between 1980-81 and 1985-86 i.e., an increase of 0.03%. On the other hand, even the total share in terms of loans disbursed has continuously fallen from 24.7% in 1975-76 to 10.8% in 1989-90, barring a slight increase between 1985 and 1986 and 1986-87 i.e., 1%. The compound growth rate per annum during the period under study has been 16.2% and 17.7% as related to loans sanctioned and disbursed.

Thus, it can be infered that the finance given by SFCs to industry has increased in absolute terms between 1975 and 1976 and 1989-90, but it has increased at a diminishing rate. It implies that performance of SFCs in terms of percentage has shown a downward trend in the total amount of loans sanctioned and disbursed to industry.

(B) <u>Industrial Finance Corporation of India</u> (IFCI) :

Industrial Finance Corporation was the first long term financial institution set up in India which initiated the provision of long term financial assistance to large scale industries and some small scale industries.

The importance of industrial finance in the economic development of a country lies in the fact that for the setting up of new units, arrangement of finance is the greatest necessity without which significant advancement cannot be sought in any field. The first step was initiated by the government with the development of the Industrial Finance Corporation (IFC) in 1948 with an authorized capital of Rs.10 crores. This was the first institution that assured long term loans for the public. The role of Industrial Finance Corporation has been tremendous in assisting varied consumer industries such as sugar and cotton, textiles, cement, fertilizers, etc. The Industrial Finance Corporation has provided financial assistance on a national level.

The Industrial Finance Corporation could not have served the regional industries at the state level primarily because the establishment of such a body requires restricted areas of growth and familiarity with respect to the industrial areas of that region.[9]

The Industrial Finance Corporation readily provides assistance to areas located in the lesser developed regions of the country, projects aimed at exploring new areas of technology, agricultural based projects and various other projects that may assist in gaining foreign exchange.[10]

The corporation behavioural principles with regard to the disbursement of financial assistance depend largely upon newer entrepreneurs, industry, commerce and many technologies entering the business world for the first time. The corporation's major source of financial assistance includes borrowings from the central government and RBI, sales of investments, repayment of loans as retained earnings as well as its own capital.

This corporation has build up vast reserves and accepts deposits from the public as well as the state government. The corporation works with the aim of including all the technical, economical and financial aspects of any project. Working principles of the Industrial Financial Corporation are more business oriented. The corporation is more involved in various other promotional activities such as underwriting of issues, as well as the availment of foreign loans. It has now established itself as a developmental institution rather than an a mere lending institution.

The amount of loans sanctioned and disbursed by IFCI during the period under study, is shown in Table No.6.3.

Table 6.3
Total Advances Sanctioned and Disbursed by Industrial Finance Corporation of India to Industry

YEARS	LOANS SANCTIONED		LOANS DISBURSED	
	Amount (in Crores)	Percentage of total Industrial Finance	Amount (in Crores)	Percentage of total Industrial Finance
1975-76	51.3	8.5	34.7	8.6
1980-81	211.7	9.3	108.7	7.7
1985-86	489.8	8.4	403.9	9.5
1986-87	798.0	11.0	451.6	8.8
1987-88	1025.1	12.0	660.1	10.5
1988-89	1897.4	12.5	1004.7	10.5
1989-90	2272.2	13.2	1127.7	10.6
Compound Growth Rate per annum				
1976-90		28.7		26.1

Source : (1) IDBI annual report 1984.
(2) Report on Currency and Finance from 1976-1991.
(3) Includes guarantees.

The table no. 6.3 gives an industry wise distribution of loans sanctioned and disbursed to various sectors by Industrial Finance Corporation of India between 1976 and 1990, the period under study. This data relates to the total financial assistance sanctioned to industries of high national priority such as cotton textile, fertilizer industry, cement, paper industry and machinery. The IFCI also participated in the soft loan scheme for modernisation of selected industries such as cement, sugar, cotton textile, and certain other industries.

The total loans sanctioned increased from Rs.51.3 crores in 1975-76 to Rs.2272.2 crores in the year 1989-90. This indicates not only the growth in overall investment activities in the economy but also the growing reliance of the industrial sector on institutional assistance. On the other hand, the loans disbursed by IFCI rose from Rs.34.7 crores in 1975-76 to Rs.1127.7 crores in 1989-90.

Along with increase in the total amount of loans sanctioned and disbursed by IFCI, it has shown a favourable trend in relative terms also. We can see from the table that the total share of IFCI in terms of loans sanctioned has continuously increased from 8.5% in 1975-76 to 13.2% in 1989-90, barring a slight fall between 1980-81 and 1985-86 i.e., a fall of 0.09%. On the other hand, even the total share in terms of loans disbursed has continuously increased from 8.6% in 1975-76 to 10.6% in 1989-90, barring a slight fall between 1975-76 and 1980-81 i.e., 0.9%; and 1985-86 and 1986-87 i.e., 0.7%. The compound growth rate per annum during the period under study has been 28.7% and 26.1% as related to loans sanctioned and disbursed.

Thus, it can be infered that the finance given by IFCI to industry has increased in absolute as well as relative terms between 1975 and 1976 and 1989-90.

(C) Industrial Credit and Investment Corporation of India (ICICI) :

Another specialised institution set up with the solitary aim of supporting industries requiring capital for a longer duration, was the ICICI which was set up on Jan. 5th, 1955 with its head quarter in Bombay. However, the most important task imparted to this corporation was to arrange easily available foreign credit to upcoming industries. This was the institution that set up prospects for the introduction of sophisticated foreign technology.

The objectives of this corporation, in short, include the promotion of activities of the private sector, its greater participation in industrial investments, disbursement of long and medium term loans, and underwriting of issues.

This corporation also gives advice on various technical matters. Through its participation in the underwriting of issues as well as in the capital market, it has made itself eligible enough, not only assisting industries with long and medium term loans, but also with risk capital. One of the noteworthy functions of the corporation has been its immense success in the promotion of private foreign capital in India. All in all, the ICICI has assisted greatly in expanding the capital market of India. With its role as a financial assistant and in cooperation with other financial institutions such IFCI, SBI, LIC, SFCs and commercial banks, the ICICI has come a long way in establishing itself as one of the prominent industrial financial institutions of India.

The ICICI is also one of the members of the consortium of the financial institutions under the soft loan scheme, providing finance on concessional basis to companies with limited liabilities, to enable them to overcome the backlog what so ever in modernization, replacement and renovation of their plant and equipments.

As described earlier, most of the undertakings of the ICICI are done with foreign currencies, the main source being the world bank and foreign commercial banks. This corporation has been working on the footmarks of the capital market of India with concentrated attention being paid to entrepreneurship and a risk taking business finance. This corporation has been working with the ardent participation of the government of India as well the IDBI.[11]

Underwriting of issues also became an important task for the ICICI, more so because it was neglected by the IFCI inspite of being one of its major goals. The period between 1967 and 1973 showed the ICICI as the only underwriter of issues. In corporate issues, it assisted 18% of the total issues underwritten. Again as time proceeded, with the participation of other institutions in this matter, the issues underwritten by ICICI declined to 8.2% during 1971-75.

After 1975, the IDBI had a much stronger hold on the underwriting of corporate issues. However, the ICICI still continues to underwrite fixed interest security. The role of ICICI in underwriting, has been termed as 'Selective and of a conservative character'.[12]

The Industrial Credit and Investment Corporation of India in association with the Unit Trust of India (UTI) has provided financial assistance to many companies like

Credit Rating Information Services of India Ltd. (CRIS), Technology Development and Information Company of India Ltd. (TDICI), with the aim of initiating technological development oriented activities, upgradation of technology as well as provision of technological information. In order to meet the currency components of its clients, ICICI has raised loans from the World Bank, Indo-German Joint ventures, Swedish Export Credit Corporation and other international commercial markets.

The operations of ICICI have shown a sizeable growth in terms of loans sanctioned and disbursed over the fifteen years of this study, which is shown in Table No. 6.4.

Table 6.4
Total Advances Sanctioned and Disbursed by Industrial Credit and Investment Corporation of India to Industry

YEARS	LOANS SANCTIONED		LOANS DISBURSED	
	Amount (in Crores)	Percentage of total Industrial Finance	Amount (in Crores)	Percentage of total Industrial Finance
1975-76	78.5	12.9	61.1	15.2
1980-81	310.5	13.6	175.0	15.5
1985-86	554.4	9.5	397.7	9.4
1986-87	1118.3	15.5	695.5	13.6
1987-88	1283.4	15.0	771.2	12.3
1988-89	2048.2	13.5	1083.5	11.3
1989-90	2927.8	17.8	1355.1	12.7
Compound Growth Rate per annum				
1976-90		27.2		22.9

Source : RBI Report on Currency and Finance 1976-91.

The table no. 6.4 shows the amount of loans sanctioned and disbursed to industry by Industrial Credit and Investment Corporation of India between 1976 and 1990. The net financial assistance sanctioned during 1975-76 amounted to Rs.78.5 crores which rose to Rs.2927.8 crores in 1989-90, whereas the total disbursement increased from Rs.61.1 crores in 1975-76 to a significantly high figure of Rs. 1355.1 crores in 1989-90. In case of loans sanctioned as well as loans disbursed, the amount of assistance has increased.

The percentage data reveals that the total share of ICICI in terms of loans sanctioned has increased from 12.9% in 1975-76 to 17.8% in 1989-90, but it had reduced significantly between 1980 and 1981 and 1985-86 i.e., from 13.6% to 9.5%. On the other hand, the total share in terms of loans disbursed has been reduced from 15.2% in 1975-76 to 12.7% in 1989-90. Even during different years, it has shown inconsistent trend. The compound growth rate per annum during the period under study has been 27.2% and 22.9% as relate to loans sanctioned and disbursed.

This implies that although the finance sanctioned by ICICI to industry has increased in absolute as well as relative terms between 1975-76 and 1989-90, but the amount of loans disbursed has significantly gone down during the period under study.

(D) <u>Industrial Development Bank of India</u> (IDBI) :

It has been found that competition, management, versatility, skills and efficiency and many other factors are duly important over and above finance for the systematic working of any development bank.

The incompetence of commercial banks with respect to the fulfilment of medium & long term loans of industries has been dealt with earlier in this chapter. Disbursement of long term loans involves a greater risk on the part of the institution, whereas short term investment result in greater liquidity and faster revival of capital, this being conventionally followed by all commercial banks.

These development banks have proved to be very supportive to the capital market, and have been correctly defined as the backbone of the financial system in India. Overall economic development has been a major cause of concern, where the development banks assisted by the IDBI have taken balanced steps to promote the economy, specially in the remote and lesser developed regions of India.

The IDBI has been considered as the apex institution for assisting term finance to the industrial sector. This development bank has many important functions to perform. The primary source of finance of all development banks like IDBI has been the government of India, RBI and foreign sources i.e., Industrial Finance Corporation of India (IFCI) and International Development Association (IDA) in the form of bonds/debentures and borrowings.

This arrangement of banks has facilitated industries to take loans on a highly assured and cheap basis so that more and more industries depend on these development banks for financial assistance with the extension of a low rate of interest. This property has raised the debt-equity ratios tremendously as well as the capital intensity in industries. Concessions of the development banks may be cited as, ready availability of term finance, with an added advantage of an enormous subsidisation by the public financial institutions as well as the evolvement of industrial enterprises.

These development banks have certainly not overlooked the promotional and consultancy aspect of banks which occupies an equal position along with the term lending role of industries.

Industrial potential services have been carried out in order to segregate the industrial potentials of areas.(13)

Prior to the establishment of the IDBI, the IFCI and ICICI were working as development banks but could not achieve those goals with which they were established in terms of quality, magnitude and overall economic services. There was a lack of integration and co-ordination amongst these institutions which were so diverse in nature. According to V.V. Bhatt, there was the need of "an institution that could co-ordinate and maintain cordial relationships with other institutions. Establishment of such a working relationship could greatly facilitate a rational financial system. Moreover the establishment of such a centrally run institution would help greatly in promoting a diversified process of industrialization".

As such the IDBI was set up in July 1964. The following year, it was declared as the principle financial institution of the country which was shown by the fact that its initial link with the RBI was stopped from Feb. 1975. This delinking was also necessary in order that the RBI may concentrate on its central banking functions. Numerous duties performed by the RBI were subsequently transferred to the IDBI, the government of India then having to consult the IDBI instead of the RBI with the task of consolidation of the resources of financial institutions. The IDBI has also maintained immense flexibility with regard to the conduction of other additional duties and developmental projects. The IDBI has also extended its roots to the lesser developed regions of the country and newer areas of technology and research. The IDBI has assisted in providing a link between the industrial arena of the country with the upcoming industries. According to M.Y. Khan "The role of IDBI in the field of development banking may be comparable to the role of RBI in commercial banking".

As discussed earlier, the financial assistance provided directly to the industrial sectors are in the form of underwriting, loans, guarantees and development funds. Such loans given may range between 10 to 12 years. The Development Assistance Funds has been one of the noteworthy characteristics of these development banks. This fund was evolved for those industries which experience great investment pressures. However, the working of such industries being worthwhile in some way, financial assistance becomes the need of the country. The provision of funds to such industries needs the prior approval of the government of India.

Another function of the IDBI is that of marketing and industrial surveys research. Such surveys are conducted on a regular basis which has helped in promoting and developing industrialization in India.[14]

The complementary part played by the IDBI with respect to industrial financing in India can be precisely stated as : "The IDBI has not only fulfilled its role as a financer of new real investment and as gap fillers of the numerous categories of finance with that of industries but has also fulfilled a heavier responsibility of probing into any problems facing the medium and long term financing of industry which has helped in promoting future development planning. It has successfully behaved as an apex institution and an autonomous institution with the RBI".[15]

Table 6.5
Total Advances Sanctioned and Disbursed by Industrial Development Bank of India to Industry

YEARS	LOANS SANCTIONED		LOANS DISBURSED	
	Amount (in Crores)	Percentage of total Industrial Finance	Amount (in Crores)	Percentage of total Industrial Finance
1975-76	245.4	40.5	174.9	43.4
1980-81	1257.7	55.3	758.5	53.9
1985-86	2537.1	43.3	2075.7	49.0
1986-87	3097.9	42.9	2232.6	43.7
1987-88	3351.5	39.1	2672.7	42.5
1988-89	6940.5	45.7	4716.2	49.3
1989-90	8124.1	47.3	5070.7	47.6
Compound Growth Rate per annum				
1976-90		26.2		25.1

Source : Reports on Currency and Finance, 1975-1991.

The table no. 6.5 shows the total financial assistance sanctioned and disbursed to industry by Industrial Development Bank of India between 1976 and 1990. The available data clearly indicates that over the period under study, the IDBI has provided maximum financial assistance to industry in comparision with other lending institutions. The IDBI has recorded an impressive performance in its operations with the total effective sanctions going up from Rs.245.4 crores in 1975-76 to Rs.8124.1 crores in 1989-90, experiencing a growth rate of 26.2% over the period under study. On the other hand, the total disbursement increased from Rs.174.9 crores in 1975-76 to a significantly high figure of Rs.5070.7 crores in 1989-90, showing a growth rate of 25.1% during 1976 to 1990. In terms of loans sanctioned as well as loans disbursed, the amount of financial assistance has increased considerably.

The total financial assistance sanctioned doubled between 1985-86 and 1988-89 and experienced the highest growth rate of 107% over the preceeding years, whereas disbursements by IDBI experienced the highest growth rate of 76.4%.

The percentage data reveals that the total share of IDBI in terms of loans sanctioned has increased from already considerably high figure of 40.5% in 1975-76 to 47.3% in 1989-90, but this increase was not consistent. On the other hand, the total share in terms of loans disbursed has also increased from 43.4% in 1975-76 to 47.6% in 1989-90, but the trend has been inconsistent.

This implies that the finance sanctioned and disbursed by IDBI to industry has been maximum in absolute as well as relative terms between 1975-76 and 1989-90.

6.2.3 Corporations Such as the UTI and LIC :

(A) Unit Trust of India (UTI) :

The UTI is an investment institution established on the 1st of Feb., 1964 under the UTI Act, 1963 with the sole aim of providing the small investor a share in India's economy and its industrial progress, keeping into consideration the involvement of minimum risk. These investors invest in corporate securities, the trust offering several advantages such as liquidity, diversification of investment and professional management.

The UTI is considered as a pure non-banking financial intermediary that raises funds from the public, directly or indirectly. "A Unit is a pro-rata share in a large but diversified portfolio of corporate securities which is essentially managed by the trust".[16] This unit capital has been raised over the years by selling units to the general public.

The establishment of the UTI was the result of initial capital of Rs.50 million being made available by the RBI and jointly by the SBI and its subsidiaries. Today the UTI is an associated institution of the IDBI with the passing of the UTI Act of 1976 which started the delinking of IDBI from the RBI.

The UTI maintains its investments in, income securities which include short-term deposits, bonds as well as ordinary shares that may guarantee a steady flow of income. The exemption of tax on its income is a step to maintain a balance between the direct as well as indirect holders of corporate securities through the UTI.

Keeping into consideration the objectives of the UTI, there has been the introduction of a number of schemes by which the trust savings are channeled into profitable ventures as well as for the security of its investors. Investments of the UTI in companies have to follow certain rules and regulations. "Investment in any one company should not exceed 5% of UTI's invertible founds or 15% of the securities issued".

Another notable feature with regard to the operation to the UTI is its growing participation in the under-writing of new issues that is in the nature of the firm committment to invest upto the amount undersecurity. This is done with respect to the active co-ordination of all the Indian financial institutions.

With the amendment of the UTI Act of April 1986, UTI now grants term loans, rediscounts bills, does hire purchase financing, allowes equipment leasing along with the provision of housing and construction finance.[17] The operational policies of the UTI with regard to the international financial market is in the form of selling overseas funds and units to the non-resident Indians.

The growth of UTI business in terms of advances sanctioned and disbursed is shown in Table No. 6.6.

Table 6.6
Total Advances Sanctioned and Disbursed by Unit Trust of India to Industry

YEARS	LOANS SANCTIONED		LOANS DISBURSED	
	Amount (in Crores)	Percentage of total Industrial Finance	Amount (in Crores)	Percentage of total Industrial Finance
1975-76	7.1	1.2	5.2	1.3
1980-81	40.4	1.8	51.0	3.6
1985-86	887.1	5.1	485.7	11.5
1986-87	465.0	6.4	417.6	8.2
1987-88	1024.9	12.0	749.1	11.9
1988-89	1973.1	13.0	1091.3	11.4
1989-90	1495.6	8.7	1280.5	12.0
Compound Growth Rate per annum				
1976-90		42.8		44.3

Source : (1) IDBI Annual Reports 1984 pp. 53
(2) Report on Currency and Finance, 1978-91.
(3) Including guarantees.

The table no. 6.6 shows the total financial assistance sanctioned and disbursed to industry by the Unit Trust of India between 1976 and 1990 and thereby occupying a strong position in the Indian market. The available data reflects the present position of UTI and the rapid progress made with respect to financial assistance over the period under study. The UTI has recorded an impressive performance which can be judged from its financial position. The total loans sanctioned went up from just Rs.7.1 crores in 1975-76 to as high as Rs.1495.6 crores in 1989-90, experiencing a growth rate of 42.8% over the period under study. On the other hand, the total disbursement increased from Rs.5.2 crores in 1975-76 to a significantly high figure of Rs.1280.5 crores in 1989-90, showing a growth rate of 44.3% during 1976 to 1990. In terms of loans sanctioned as well as loans disbursed, the amount of financial assistance has increased considerably.

The percentage data reveals that the total share of UTI in terms of loans sanctioned has continuously increased from a relatively low figure of 1.2% in 1975-76 to 13.0% in 1988-89, but it got reduced to 8.7% in 1989-90. On the other hand, the total share in terms of loans disbursed has also increased from 1.3% in 1975-76 to 12.0% in 1989-90, but the trend showed varied fluctuations.

Various factors can be cited for the rapid growth of UTI in terms of financial growth. These factors are attractive offers introduced under various schemes, an immense diversification of its network, introduction of newer strategies as well as a number of tax benefits offered from time to time. The massive increase in UTI's holding is also the consequence of its holdings in a large number of companies. A systematic analysis of the assistance given by UTI reflects a vast improvement in its working. In short, we can say that the finance sanctioned and disbursed by UTI to industry has been significant in absolute as well as relative terms between 1975 and 1976 and 1989-90.

(B) Life Insurance Corporation of India (LIC) :

The functioning of the Life Insurance Corporation took root when it took over the life insurance business of 244 private companies and the declared LIC as a wholly owned government corporation under the LIC Act 1956. In accordance with this act, the life insurance business of all these companies was nationalized and a single monolithic organization, the LIC was set up.

In the field of insurance, the LIC enjoys a monopoly so much so that whatever business is conducted by the post and telegraph department is relatively negligible and declining.(18) 'Life Insurance' as such is a very important from of long-term contractual savings which promotes saving and results in rapid mobilisation.

The LIC was established with an initial capital of Rs.50 million being provided by the government of India. The major sources of funds of the LIC include premiums paid by policy holders, interests, dividends as well as repayments. These funds collected are then invested in a number of income-producing sectors. A 'life fund' is a fund which is collected out of the excess premiums and income collected from investments. This surplus collected is partly assigned to the policy holders and the rest is used for adding upto the reserves.

The importance of the LIC as a financial intermediary has grown over the years with respect to its efforts to mobilize savings, its volume of funds and magnitude of total investments. The LIC is an ardent investor of funds in government securities. In accordance with the investment policy of LIC, not less than 75% of the funds have to be invested in central government and state government securities.

The funds of the LIC are made available directly to the private sector through investment in shares and debentures and in the form of long term and short term loans. Investments policies of the LIC ensure avoidance of any speculative or high capital gain promises, the major principle of its investment policy being security of funds.

The investment pattern of LIC during the period under study indicates that the most important avenue of its investments, is the government followed by housing and mortgage loans, loans to power corporations, corporate securities and policy holders. The data related to loans sanctioned and disbursed is shown in Table No. 6.7.

Table 6.7
Total Advances Sanctioned and Disbursed by Life Insurance Corporation of India to Industry

YEARS	LOANS SANCTIONED		LOANS DISBURSED	
	Amount (in Crores)	Percentage of total Industrial Finance	Amount (in Crores)	Percentage of total Industrial Finance
1975-76	61.0	10.1	27.4	6.8
1980-81	69.9	3.1	64.5	4.6
1985-86	383.7	6.5	261.9	6.3
1986-87	504.8	7.0	530.7	10.4
1987-88	524.1	6.1	505.6	8.0
1988-89	845.1	5.6	626.9	6.5
1989-90	793.4	4.6	670.4	6.3
Compound Growth Rate per annum				
1976-90		42.8		44.3

Source : (1) RBI Reports 1983
(2) RBI report on Currency and Finance 1975-90
(3) Includes guarantees

The table no. 6.7 reflects the present position of LIC and the its progress with respect to financial assistance during 1975-76 to 1989-90. The total loans sanctioned went up from just Rs.61.0 crores in 1975-76 to Rs.793.4 crores in 1989-90, which shows a compounded growth rate of 18.6% over the period under study. On the other hand, the total disbursement increased from Rs.27.4 crores in 1975-76 to Rs.670.4 crores in 1989-90, showing a compounded growth rate of 23.7% during the period under study. In terms of loans sanctioned as well as loans disbursed, there has been a spurt in the financial assistance given during the last few years.

The percentage data reveals that the total share of LIC in terms of loans sanctioned has diminished from a relatively high figure of 10.1% in 1975-76 to 4.6% in 1989-90. On the other hand, the total share in terms of loans disbursed has remained more or less the same. The total amount disbursed has been reduced from 6.8% in 1975-76 to 6.3% in 1989-90.

These data reveal that the share of LIC in the total finance given to industry is low in comparison with other financial institutions and has not shown any significant change during the period under study i.e., 1975-76 to 1989-90.

The relative performance of different financial institutions in providing finance to industry can be judged from their respective shares and the fluctuations in terms percentages. It has been found that the the share of IDBI in terms of loans sanctioned is maximum, followed by ICICI, IFCI, SFCs, UTI and LIC respectively. Not only this, there is a vast gap between maximum and minimum share. Even in terms of total loans disbursed, the IDBI stands at first position, followed by ICICI, UTI, SFCs, IFCI and LIC respectively. This relative position is shown in table no. 6.8.

Table 6.8
Percentage of Assistance Sanctioned and Disbursed out of the Total Assistance by Six Financial Institutions during 1975-76 to 1989-90.

YEAR	AMOUNT SANCTIONED						AMOUNT DISBURSED					
	SFC	IFCI	IDBI	ICICI	UTI	LIC	SFC	IFCI	IDBI	ICICI	UTI	LIC
1975-76	26.8	8.5	40.5	12.9	1.2	10.1	24.7	8.6	43.4	15.2	1.3	6.8
1980-81	16.9	9.3	55.3	13.6	1.8	3.1	17.7	7.7	53.9	12.5	3.6	4.6
1985-86	17.2	8.4	43.3	9.5	15.1	6.5	14.3	9.5	49.0	9.4	11.5	6.3
1986-87	17.2	11.0	42.9	15.5	6.4	7.0	15.3	8.8	43.7	13.6	8.2	10.4
1987-88	15.8	12.0	39.1	15.0	12.0	6.1	14.8	10.5	42.5	12.3	11.9	8.0
1988-89	9.7	12.5	45.7	13.5	13.0	5.6	11.0	10.5	49.3	11.3	11.4	6.5
1989-90	9.1	13.2	47.3	17.1	8.7	4.6	10.8	10.6	47.6	12.7	12.0	6.3

The above table shows the relative performance of all the six financial institutions in providing finance to industry. It can be seen from the table that the total loans sanctioned by IDBI were 40.5% in 1975-76, which increased to 47.5% in the year 1989-90, whereas SFCs sanctioned 26.8% of the total financial assistance given by all the six institutions but this figure got reduced to just 9.1% in 1989-90. It can also be seen that the share of other institutions also increased in terms of percentage during the period under study but it nowhere reached near the relative figure of IDBI.

In the same manner, the total amount of loans disbursed by different financial institutions shows that IDBI is a leading financial institution, which fulfills 47.6% of the total credit requirements among the six important financial institutions. The share of other institutions has ranged between approximately 6% to 13%, far behind the share of

IDBI. Thus, it implies that IDBI has been the major source of industrial finance since 1975-76 and has grown in absolute as well as relative terms.

6.2.4 Industrial Finance in the Indian Capital Market :

An efficient capital market is an essential pre-requisite of economic development because capital market is mainly linked with long term finance. It comprises of a series of channels with which savings of the community are distributed to numerous industrial and commercial undertakings. An upcoming capital market is dependent on a number of factors for its development and efficacy of work like, availability and proper channelization of savings, regularity of investments, mobilization of savings and systematic organisation of the concerned institutions. The investment institutions, saving banks, specialized financial institutions as well as stock exchanges, all form a part and parcel of the capital market.

The capital market works on a demand and supply basis, that is, demand from various borrowers such as central and state governments, local authorities, agriculture, industry and various other sectors, and supply of funds to the capital market through various channels. A large part of the funds are mainly raised directly from individual investors through equity capital.

The growth of a capital market is dependent upon the quantum of available savings that in turn determine the extent of industrial investment. A well developed capital market does not restrict itself to the investors, instead takes greater risks by participating in newer ventures, such as underwriting of issues which facilitate raising of capital by new enterprises as well as expansion in the network of the specialized financial agencies which form an eminent part of the capital market.

It is obvious that the structure of the capital market varies from country to country. In U.K. and U.S.A., rapid industrialization, modernized agriculture and trade necessitated the need for long term capital to industry. Today, specialized institutions in these countries are responsible for the collection of savings from individuals and corporations for channelizing them into newer industrial undertakings.

- **Institutional Structure of Indian Capital Market :**

On viewing the capital market of underdeveloped countries or developing countries like India where the indigenous 'Moneylender' is also the banker of the village, a country with heterogeneous population, most of the rural investment has no access to the wider public or any external source. However, with the entry of Indian enterpreneures into industry, in order to satisfy the larger capital needs, insurance companies arose. The main purpose of the Indian money market was to supply short term capital needs to firms, the long term finance being met with through internal sources and a security market which could meet the requirements of only a few firms.

As rapid industrialization set in, the need for professional promoters, underwriting agencies as well as the need for financial intermediaries was emphasized. With regard to the underwriting of issues in India, tremendous progress has been made through the specialized institutions like ICICI, UTI, LIC, IDBI and IFC. According to the structural framework of the capital market, it can be segmented into demand and supply of long term funds, with a linkage provided by the various financial intermediaries cited above. With the process of industrial growth, the development of the capital market in India showed several features. Analysis of capital market during the time period of this study, that is, from 1975 and 1976, clearly indicates the rapid progress made by the market from an early stage of its development. The need for it originally arose out of the requirements of foreign investors who transacted business within the country, also due to the need for the modernized capital market of today, as a consequence of the entry of Indian entrepreneurs into industry. During the mid seventies, general sluggishness accompanied by strong under currents of revival were the main features. Support extended by the term lending institutions to the corporate sector was also higher. The private sector of the market also appeared to have improved tremendously. However in 1975-76, the recovery proved to be short lived, as prices declined in 1976 mainly due to the persistence of recessionary conditions in certain textile industries. Moreover, the LIC and UTI provided selective support to the industries and other enterprises. However, the banks occupied a fairly comfortable position, the market operations being highly facilitated by the banks. Another important feature of the market during the seventies was the flotation of new issues by non government public limited companies through shares and debentures. The trend of revival of the capital market was reflected by a series of measures undertaken by the government such as flexibility with respect to the bonus issues and the accessibility of foreign equity capital in the Indian market during the early eightees.

The late eightees saw the capital market witnessing erratic movements in its equity prices. However, with the continuation of pragmatic policies by the government, growing institutional support, a comfortable investment climate was created by the end of the 1980 era. Activities in the primary and secondary markets reached new heights with the announcement of new liberalisation policies by the government.

This part of chapter necessarily focuses on the developments undergone in the Indian capital market between 1975-76 and 1989-90, a systematic analysis of its functions being depicted in the following pages ahead.

The market sentiments were inspired by an overall progress made in the economy accompanied by a good monsoon and the announcement of new industrial policies. The early 1980's also saw an increase in the equity prices with an annual industrial growth rate of 8-9%. During 1985-86, the capital market was further boosted but suffered a setback after presentation of the union budget for 1986-87.

The new capital issues through prospectus and rights by non-government public limited companies during 1976 -1990 is shown in table no. 6.9A.

A look at the table depicts the distribution of new capital issues through prospectus and rights by the non-government public limited companies. The continuation of the pragmatic policy initiatives by the government, encouraging corporate issues coupled with institutional support, improved the investment climate. The new capital issues were in the form of equity shares, preference shares as well as debentures. The number of new capital issues through prospectus rose from 93 in 1975-76 to 188 in 1989-90. Whereas number of issues through rights soared from 24 to 216 in 1989-90. Equity shares occupied a major portion of the issues uptil 1987-1988 subsequently after which debentures through prospectus and rights exhibited a sharper rise. This has been clearly indicated in the table where the share of debentures issues through prespectus soared from Rs.183-7 crores (26.2%) in 1987-88 to Rs.854.5 crores (55.4%) in 1988-89.

This increase could be attributed to the increase in the ceiling rate of interest on secured public debentures. According to data compiled by the RBI, the new capital issues increased from Rs.46.8 crores in 1975-76 to Rs.1543.7 crores in 1988-89 finally doubling to Rs.3145.9 crores in 1990. The bulk of rise was primarily owing to a spate of equity issues till 1986-87, and as mentioned earlier, a significant rise of debentures from 87 onwards till 1990. Rise in equity issues reflected the private corporate sector's quick response in an environment of favourable investment climate. In 1985-86 an over-whelming proportion of equity issues during the year were accounted for by new companies. During the greater part of 1986-87, the market witnessed an erratic movement in equity prices which was partly a corrective measure adopted by the government in response to the disproportionately increased buoyancy experienced in 1985-86. The share of equity shares declining from Rs.7921.1 in 1986-87 to Rs.510.5 crores in 1987-88 that is by 35.5% whereas debentures declined from Rs.479 crores to Rs.183.7 crores in 1987-88 or by 61.6% the total amount experiencing a downward trend to Rs.700.9 crores in 1987-88 from Rs.1271.3 crores in the proceeding year.

Issues through rights showed a similar trend. The total amount of these issues totalled upto Rs.3290.7 crores in 1990. Preference shares occupied a very small proportion of the total issues both as prospectus and rights.

The suggishnesh and slackening of equity prices staged a recovery by the end of 1988, following the announcement of various tax concessions to the industrial sector. The capital issued by way of rights at Rs.1591.5 in 1989 doubled to Rs.3290.7 crores in 1990.

Table 6.9

New Capital Issues through Prospectus and Rights by Non-government Public Limited companies during 1976- 90

Year	Issues through Prospectus (A)					Issues through Rights (B)					Grand Total		Distribution between			
	No. of Issues	Equity Shares	Prefer-ence Shares	Deben-tures	Total Amount 3+4+5	No. of Issues	Equity Shares	Prefer-ence Shares	Deben-tures	Total Amount 8+9+10	No. of Issues	Amount	No. of Issues of New Comp.	Amount	No. of Issues of Existing Comp.	Amoun t
1	2	3	4	5	6	7	8	9	10	11	12	13	14	15	16	17
1975-76	93	41.1 (87.8)	4.7 (10.0)	1.0 (2.2)	46.8 (100)	24	6.6 (71.0)	0.4 (4.3)	2.3 (24.7)	9.3 (100)	117	56.1 (100)	66	35.5 (62.9)	51	20.8 (37.1)
1980-81	311	255.2 (64.9)	2.0 (0.5)	136.1 (34.6)	393.3 (100)	86	27.9 (31.0)	0.0 (0.0)	26.0 (69.0)	89.9 (100)	397	483.3 (100)	254	209.4 (43.3)	143	273.9 (56.7)
1985-86	614	687.1 (88.4)	1.6 (0.2)	88.3 (11.4)	777.0 (100)	120	56.8 (7.9)	0.3 (0.0)	666.4 (92.1)	723.5 (100)	734	1500.5 (100)	547	732.0 (48.8)	187	768 4 (51.2)
1986-87	414	792.1 (62.3)	0.2 (0.0)	479.0 (37.7)	1271.3 (100)	115	84.7 (7.3)	0 6 (0.1)	1077.6 (92.6)	1162 9 (100)	529	2434.2 (100)	279	678.1 (27.9)	250	1756.1 (72.1)
1987-88	140	510.5 (72.8)	6.7 (1.0)	183.7 (26.2)	700.9 (100)	83	586.2 (55.2)	0.2 (0.0)	475.2 (44.8)	1061.6 (100)	223	1762.5 (100)	87	340 6 (19.3)	136	1421 9 (80 7)
1988-89	191	687.4 (44.5)	1.8 (0.1)	854.5 (55.4)	1543.7 (100)	146	319.6 (20.1)	1.5 (0.1)	1270.4 (79.8)	1591.5 (100)	337.	3135.2 (100)	131	1791.2 (48.0)	206	1944.0. (52 0)
1989-90	188	735.3 (23.4)	5.4 (0.2)	2405.2 (76.4)	3145.9 (100)	216	470.9 (14.3)	2.5 (0.1)	2817.3 (85.6)	3290.7 (100)	404	6436.6 (100)	105	625.3 (9.7)	299	5811.3 (90.3)
Compound Growth Rate (percentage per annum)																
1976-90		**21.20**	**0.4**	**68.03**	**32.38**		**32.91**	**12.99**	**60.64**	**47.88**		**37.18**		**21.12**		**45.57**

Note : 1. Data exclude capital issues by term-lending institutions and exclude bonus issues.
2. Figures in brackets indicate percentages to totals.

Source : Report on Currency and Finance.

Part B

6.3 INDUSTRIAL FINANCE IN JORDAN

Historically, the growth of any nation can be ascertained from a structural shift in the economic pattern. This shift can be in the terms of shift from rural economy to urban economy or from agriculture to industry. It was as early as 1950s that Jordan, like many other developing nations, started promoting industrialization in the country because its growth was restricted due to heavy dependence on import of consumer goods. So it was realized that the development of Jordan is not possible without industrial growth. Keeping this view in mind, the government thought of giving more finance for the growth of the industrial sector.

The investigation of theoretical studies and implication of the importance of a strong financial system for an incoming economy has been a recent phenomenon.(1)

On observing the financial development of developed countries, two distinct patterns of financial intermediation can be segregated - one is, the institution which has a direct hand in financing and promoting industrial development, as seen in the case of Germany. And the second institution is one which caters to the needs of rapid industrilization by merely responding to the emerging demand made for its services. An appropriate example in this case is that of England. Jordan has followed the pattern of financing directly to industrial sector for promoting industrial development.

This particular evolution pattern of financial intermediaries is in response to the varying development needs of the country.(2)

It has been found that the English financial system became well adjusted to the special needs of its economy and thereby facilitated real economic growth. Countries vary considerably with respect to their culture, social, political and economic circumstances which in turn impose a number of requirements and responsibilities on their financial system. The financial system plays a crucial role in promoting the required infrastructural changes in an economy.

Hence, in continuation with the realization of this fact, many developing countries have given top priority to the development of financial institutions, which in turn, largely influences real economic growth. The works of classical writers like Gurley, Shaw, Goldsmith and Cameron reveal the most prominent studies done in this field of economic literature.(3) It is a strongly held fact that growth in the economic sectors of a country is largely responsible for inducing financial development.(4)

A very important function of the financial system is the provision of entrepreneureal talent as well as the financing of technical and industrial innovation. This function has a developmental impact which stimulates economic growth indirectly.(5)

The financial system in Jordan has passed through several stages of development since the establishment of the kingdom. According to major statistical estimates, economic growth experienced in Jordan aftermath the 1967 Middle East war, was considered to be one of the most significant "success stories" concerning the lesser developed countries of the world, the only hinderance being limited available economic resources. During 1970s, the industrial sector's annual contribution to the GDP increased from 11.2% in 1973 to 18.8% in 1980.

The industrial sector started attracting a tremendous amount of private investment, with nearly three-quarters of the investment being carried out by the private sector. However, this investment by the private entrepreneurs experienced a shortfall during the early eighties with the overall growth of the industrial sector declining to 4.9%. With the formulation of the third five-year development plan of 1986-90, a great deal of expansion was seen with the expansion in the industrial production due to the growth of major industries.

6.3.1 Sources of Finance in Jordan :

Historical evidence and theoretical analysis suggests that the financial system can play an active promotional role in initiating and manipulating the course of economic development. The industrial sector of Jordan has access to financing through various channels which include :

Commercial Banks, Industrial Development Bank of Jordan (IDBJ), Finance companies, and other non-banking institutions such as insurance companies, the postal saving fund, and other SCIs are responsible for activities related to the manufacturing sector. Moreover, industry in Jordan also has the access to the Arab and Foreign financing institutions, a few of which are Islamic Development Bank, and Kuwait Fund for Arab Economic Development (KFAEB).

The principle financial intermediaries entrusted with the task of facilitating the need of finance by industries and business can be listed as -

(1) Commercial Banks

(2) Specialized Credit Institutions

6.3.1.1 Commercial Banks :

Development of Commercial banks began with the opening of a branch in Amman called the Ottoman Bank in 1925, primarily being a British entity. It was in absence of an adequate central banking structure that the role played by this bank was that of a fiscal agent of the government[6].

The Central Bank of Jordan being an autonomous public institution, is endowed with the power to control as well as regulate the credit creation capacity of the commercial banks. It was only by the early seventies that steps were taken by the commercial banks to allocate a much larger percentage of their loans to various industrial activities of the country.

The activities of Commercial Banks can best be analysed with reference to their balance sheets which reveal their efficiency as specialized financial intermediaries in the mobilization of funds as well as channeling them into appropriate uses.

A look at the post independent era uptil 1959 reveals that these banks were free to conduct business without the regulation of any banking law. Concomitantly, the establishment of the first law i.e., law No. 4 in 1959 coincided with the creation of an independant monetary authority called the Central Bank of Jordan.[7]

However, effective banking control did not start until 1966, the Temporary Banking law No. 94 giving the Central bank of Jordan a total control over the banks with a stronger control on their investment behaviour and composition of their liquid assets.[8]

The sources of funds as well as the capital / reserves of banks has been elaborately analyzed, in the chapter on the 'Role of commercial banks' which significantly indicates that the role of commercial bank in the task of economic development can be best judged by their ability to mobilize the community's savings. The nature of these banks can also be seen with respect to the very insignificant low share of borrowings from the Central bank.

- **The Traditional Commercial Banking Theory :**

Jordan followed the British banking policy, as a result, the commercial banks confined themselves to the traditional approach of extending short term loans to industries. This traditional practice was adopted because of insecurity realized by banks in "term lending" i.e., medium and long term loans which had maturities over one year. This was distinct from short-term lending which is usually extended for a period upto one year. No doubt, such an orthrodox banking practice of borrowing limited amount and even lending limited amount was well practised and appreciated in British banks. However, during the early 1933, the great economic depression of USA indicated the fact that such a system of lending can not ensure liquidity.[(9)]

The fallacy of this theory has earlier been shown by Joseph Schumpeter when he stated that, "The short term character of bank credit is indeed one of the fictions of banking theory and rests on the prejudices, that banks essentially lend their depositors money whereas their essential function lies in the creation of money, not in acting as intermediaries between borrowers and depositors".[(10)]

This term lending technique also found a positive response in many developing countries. The need for medium comprehensive development programme being strongly emphasised by the commercial banks itself in countries like India, where "the need for participation by the commercial banks in more comprehensive term lending was stressed by the country's Central Bank, with the Commercial Banking system displaying an increasing interest in term lending business".[11]

The next question that needs to be asked is whether commercial banks in Jordan were justified in confining their credit extension to short term loans or undertake term lending. It is undoubtedly true that allocation of short term loans, adequately suited the economic environment during the colonial era where very little emphasis was given to industrialization which needed long term loans. In turn, the lending scenario changed a great deal with the post independence era, as the building up of the required capital demanded long-term financing. Today, it is a well known fact that banks in Jordan extend loans and advances even of a medium term nature especially to sectors of trade and commerce.

The demands for term lending in Jordan are fulfilled by the special credit institutions such as the Industrial Development Bank (IDB) in case of manufacturing and the Agriculture Credit Corporation (ACC) in case of agriculture. With the increasing demand for long term credit and to participate in meeting part of demands, commercial banks have contributed effectively to the economy of the country.

Bank deposits are of a relatively stable nature, because the assets of the commercial banks have been considerably influenced by its deposit structure. Moreover, time deposits depicting a greater stability, banks can rely upon extending medium and long term loans without endangering their liquidity.[12]

This fact does not imply that short term lending is no longer relevant, instead it still assumes paramount importance with respect to various economical and financial activities. In comparison with the medium term lending of IDB, the interest rate charged by commercial banks on its loans was 9% during the mid 1976, which was 8% in case of Industrial Development Bank of Jordan. The IDB loans have a longer maturity than commercial banks loans to industry. However, the commercial banks loans are mobilized in such a manner that it promotes sources of credit on a continuous basis.[13]

Various government policies have also been introduced in the financial sector to boost the financial market and thereby benefiting industrial sector. During the mid 1980s, the government's credit and monetary policies aimed at fixing regulated interest rates and mobilization of credit to fruitful enterprises.

A very important element of the government policy wsa to promote the allocation of finance by commercial banks to the private sector. For this, the Central Bank of Jordan rediscounted all syndicated loans of commercial banks. It is important to note here that earlier to this, the Central bank legislation in Jordan forbided the Central bank of Jordan in providing rediscounting facility to commercial banks for any financial instrument with maturity exceeding nine months.[14]

Hence, for encouraging term lending and enabling the Central bank of Jordan to secure bank liquidity by rediscounting long term financial instruments, it was essential to amend this act.

A major distinguishing feature of commercial banking in developing country like Jordan now-a-days is the increasing importance of the relative share of the manufacturing sector in the total bank credit. However, this was not the case with Jordan where the sectoral distribution of bank credit was not consistent. In Jordan, more emphasis was being given to diversifying the national economy. Between 1964 and 1976, commercial banks in Jordan were heavily geared to finance the foreign trade sector, which claimed a bulk of their credit.

Jordan gave priority to promote internal agriculture and manufacturing activities in accordance with comprehensive development programmes. This inconsistency in the allocation of credit reflected the inappropriate adaptation of the commercial banks to the changing needs of their economy, along with the failure of the monetary authority to sufficiently influence the allocation of bank credit in favour of developmental activities.

However, it can be seen from the following table that after 1976-78, commercial banks started participating actively in development and started planned operations along the lines laid down in economic development strategies with the pursuance of specific central banking innovations.

All this necessitated the flow of bank resources towards priority sectors thereby promoting the required structural change in the economy of the country. The survey of the distribution of credit facilities to the three major economic sectors viz. industry & mining, construction & general trade and commerce, reveals the varying trends.

The percentage share of commercial banks in providing credit to different sectors and the credit given to industry and mining, in particular, is shown in the table no. 6.10.

Table 6.10

The Percentage Share of Commercial Bank Credit to Industry and Mining in the Total Commercial Bank Credit during 1976-1990.

YEAR	CONSTRUC-TION	GENERAL COMMERCE & TRADE	INDUSTRY AND MINING	TOTAL FACILITIES	SHARE OF COMMERCIAL BANKS CREDIT TO INDUSTRY
(1)	(2)	(3)	(4)	(5)	(6)
1976	50.0	81.6	22.1	207.1	10.7
1977	65.8	81.4	26.8	244.0	11.0
1978	100.0	100.5	38.3	332.8	11.5
1979	151.0	134.2	60.5	465.1	13.0
1980	180.8	167.0	73.1	563.9	13.0
1981	201.0	225.8	89.2	721.3	12.4
1982	216.8	284.9	112.6	887.2	12.7
1983	271.3	276.7	138.9	1030.9	13.5
1984	324.0	296.1	169.8	1184.8	14.3
1985	331.6	308.5	189.3	1274.4	14.9
1986	353.7	338.7	221.0	1395.4	15.8
1987	358.2	363.7	220.7	1513.0	14.6
1988	374.5	402.5	221.5	1634.0	13.6
1989	399.1	391.5	239.0	1729.2	13.8
1990	422.7	407.8	236.9	1863.5	12.7
Compound growth rate in percentage per annum					
1976-80	29.31	15.39	27.02	22.18	
1981-85	10.53	6.44	16.24	12.05	
1986-90	4.97	3.78	1.39	5.95	

Source : Monthly and yearly statistical series IDBJ annual reports 1976-1990.

To understand the trend, the explanation of the table is carried out in three phases - the first phase includes the period between 1976 and 1980, second phase covers the period between 1981 and 1985 and the third phase explains the changes between 1986 and 1990.

On analysing the first phase i.e, 1976-80, we can observe that the total credit facilities given by commercial banks increased from 207.1 million JD in 1976 to 563.9 million JD in 1980, thus showing a rise of 356.8 million JD. Among all the sectors, general trade and commerce occupied a major bulk of total credit, increasing from 81.6 million JD in 1976 to 167 million JD in 1980. However, on studying these figures in terms of percentage, the share of these sectors in the total credit declined from 39.4% in 1976 to 29.6% in 1980, showing that the relative share of the industry and construction sectors had increased at the expense of the trade sector. This is also reflected in the higher share of credit allocated to construction sector in comparison with the commerce sector in the year 1980. The total credit given to construction sector rose from 50 million JD in 1976 to 180.8 million JD in 1980, which is almost four times higher. The share of this sector in the total credit increased from 24.1% in 1976 to 32% in 1980.

If we look at the figures of total credit secured by industry, we can say that the share of industry was marginal in comparison with other sectors. The industry and mining sector received just 22.1 million JD in 1976, which increased to just 73.1 million JD in 1980. It means that although the percentage share of industry has increased from 10.7% in 1976 to 13% in 1980 but it is not significant. It means that during the phase of the study, the commercial banks did not provide enough finance to industry, which is a crucial factor of slow growth of industrial sector in Jordan.

The period between 1981and 1985 i.e., second phase also showed the same trend in terms of total credit given to different sectors, but in terms of percentages, the industry received more share in comparison with other sectors. Not only this, it can also be seen that the percentage share of other sectors declined whereas share of industry increased. The total credit facilities given by commercial banks to different sectors increased from563.9 million JD in 1980 to 721.3 million JD in 1981, showing a rise of over 27.9% over the 1980 level, which further increased to 1274.4 million JD in 1985.

It can be observed from the table that the largest portion of the credit went to the commerce and trade sector, resulting in a slight increase in its relative sectoral importance as credit recipient at the end of 1981. The total credit facilities received by commerce and trade sector increased from 225.8 million JD in 1981 to 308.5 million JD in 1985, but in terms of percentage share, it was found that it declined from 31.3% in 1981 to 24.2% in 1985. Similar is the case for construction sector, which received 201 million JD in 1981 and subsequently increased to 331.6 million JD in 1985 but in terms of percentage, its share has declined from 27.8% to 26% during the second phase. On the other hand, the industrial sector shows a rise of 180.1 million JD from 89.2 million JD in 1981 to 189.3 million JD in 1985, its percentage share rising from 12.4% in 1981 to 14.9% in 1985. This trend shows a positive change in favour of industry as far as credit facilities are concerned.

So it can be said that during the second phase, the credit development facilities were in line with the government objectives. Commercial banks continued to extend medium and long term loans through syndicated loans and corporate bonds issued on behalf of public share holding companies. These figures also reflect the success of the monetary policy in controlling credit and the drop in the demand for credit facilities financing trade, in response to a sluggish trade activities.

The third phase i.e., 1986-90 shows a decline in the credit facilities extended to industrial sector in terms of percentage. Although the total amount of credit extended to industrial sector rose in absolute terms, but there was a decline in terms of percentage. The table shows that the credit facilities received by the industrial sector increased from 221 million JD in 1986 to 236.9 million JD in 1990, a insignificant rise of 15.9 million JD. If we compare the percentage change, it can be seen that the share of industrial sector in getting credit facilities declined from 15.8% in 1986 to 12.7% in 1990.

The table also shows fluctuations in percentage share of industrial sector which increased from 10.7% to 13% during the first phase i.e., 1976-80; declined from 13% in 1980 to 12.4% in 1981; again increased from 12.4% to 14.9% during the second phase i.e., 1981-1985; but the share declined to 15.8% in 1986 to 12.7% in 1990 i.e., third phase. This shows that the third phase shows decline in share of credit received by industry from commercial banks.

Not only this, even the compound growth rate shows an overall decline in total percentage and sectoral distribution. The compound growth which was 22.18% during the first phase, declined to 12.05% during the second phase and further declined to just 5.95% during the third phase.

Thus, it can be seen that the sectoral breakdown of credit facilities did not show any significant changes over the whole period of study. It means that although the credit facilities provided to different sectors increased in absolute terms but the industry received the minimum share.

6.3.1.2 Specialized Credit Institutions :

Smooth and efficient operation of the economic system pre-supposes the existence of an organized and integrated financial structure. The primary function of financial institutions in the monetary economy is to provide necessary funds to finance the production process. Hence, it becomes crucial that adequate resources are diverted into those investment areas which contribute most effectively to economic development.

Monetary and fiscal developments in Jordan have on the whole been appropriate to set the pace of economic development in the country. Much emphasis is laid on the development of Jordan's basic economic sectors namely agriculture, industry, mining, manufacturing and housing in Jordan's national development plans. A serious hinderance primarily to the industrial sector has been the inability of market forces to attract adequate finance for this sector, thereby creating financial gaps in Jordan's economy. Commercial banks operations were mainly oriented to short-term credit which was found to be inadequate to meet the growing needs of the private sector.

The Five year plan of 1976-1980 emphasised the role of specialized credit institutions towards restructuring the economy through rapid industrialization. The plan expected that the SCIs will play a "more active role in identifying new investment prospects and increase the resources of SCI by attracting time deposits and issuing bonds at competitive rates of interest.(15)

The bias of banks towards the foreign trade sector could never be totally controlled by the Currency Board System. The first fifteen years of the post independence era witnessed the pursuance of a similar type of monetary policy, as a result the above mentioned credit gap remained unaltered. The first attack on the unsatisfactory role played by these financial institutions in the past was made in the Seven Years Developmental Plan (1964-70). The key sectors were segregated out as being largely inhibited by as shortage of private capital.[16]

It has been realized that the SCIs have an eminent role to play in the economic and social development of the country. Presently, there are six specialized credit institutions serving various sectors of the economy that work as channels for the effective mobilization of savings and their productive utilization in long term domestic investments. All these institutions were established with the active co-operation of the government in recognizing the need for them.[17]

These institutions can be listed as :

1. Municipal and village loans fund
2. Industrial Development Bank
3. Housing Corporation
4. Agricultural Credit Corporation
5. Jordan Cooperative Organization, and
6. Housing Bank.

All the six SCIs have proven to be essential tools for provision of direct financial and entrepreneurial assistance with a view to achieving Jordan's sectoral development objectives.

Here the focus of this discussion will be the Industrial Development Bank of Jordan only which caters to the needs of long term financing of industrial establishments and entrepreneurs of Jordan.

(A) The Industrial Development Bank of Jordan (IDBJ)

The apparent need for the establishment of a specialized credit institution which would help in providing medium and long term loans to industry was fulfilled with the setting up of the Industrial Loan Fund, a government department attached to the Jordan Development Board. The inability of this institution to fulfill this aim, due to limited availability of resources, prompted the government to set up the Industrial Development Bank(IDB) in July 1965 with an authorized capital of 3 million JD made up of 1,110,000 ordinary shares and 1,890,000 preference shares holding a nominal value of JD.

The four major objectives of the Industrial Development Bank as defined by the IDB law no. 27 of 1965 can be stated as :

1. Encouragement, activation, expansion, development and renewal of industrial projects.
2. Encouragement of small local industries through the establishment of co-operative societies and their support through technical assistance and loans.
3. Encouragement of financing of industrial projects from internal or external sources whether public, private or international.
4. Increasing work opportunities in Jordan by aiding in the industrialization of the country.

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4. Agricultural Credit Corporation
5. Jordan Cooperative Organization, and
6. Housing Bank.

All the six SCIs have proven to be essential tools for provision of direct financial and entrepreneurial assistance with a view to achieving Jordan's sectoral development objectives.

Since its establishment in 1965, the IDB has been giving numerous loans to the industrial and tourism sector in the range of JD 1000-21000, for a period of 3-15 years. The IDB now operates with the legislative framework provided by the Permanent law no. 5 of 1972.

In accordance with this law, the Bank is empowered to offer banking services as well as other promotional functions related to industrial development. The bank has also been empowered to help industrial companies raise capital by issuing guarantees for loans obtained by them from other financial sources and also by underwriting shares and debentures. The development of a flexible capital market is also a primary objective of the law.

The Industrial Development Bank has also been authorized to supply both debt and equity capital, debt capital assuming much more importance. A look at the interest rates of the IDB also indicates an element of subsidy, particularly low interest (4%) loans from the Central Bank of Jordan. However, the role of the IDB is essentially that of a financial institution rather than a fiscal one.[18]

Moreover, in order to cater to the needs of the small borrowers who were excluded from the IDB loan applications as well as the administrative procedures, the Small Industries and Handicrafts Loan Fund was established in 1975 within the IDB. These loans involved a lessor degree of formality as compared to the application of ordinary IDB loans which were lengthy and required careful monitoring.

The financing of any industrial project need to comply with the following three principles :

1. The project must be economically feasible.
2. The project must be technically sound.
3. The project must have efficient management at all levels.

These principles form the basis of the investment policy of the IDBJ.[19]

As mentioned earlier, the formalities related to ordinary IDBJ loans are fairly time consuming and certainly does not end by merely issuing the loan. Once the loan has been granted, it is the duty of the IDBJ staff to carefully monitor the project in order to ensure its proper execution. Loans are disbursed as and when required by the customers. Re-payment rates are therefore comparatively good and differs from project to project spreading between the span of 5-15 years along with a grace period granted for construction during which only interest is accepted.

The IDBJ also gives due weightage to the provision of technical assistance which forms an important part of its task.

The next question that may be asked is how far has the IDBJ progressed in achieving its goals and set targets which were assigned to it at the time of its establishment in the country ?

An attempt to answer these questions will be made in the following pages which give a numerical distribution of loans disbursed to various industrial sectors and their respective compound growth rates.

- **Need For Specialised Manufacturing Credit**

The industrial and manufacturing sector was found in its embryonic stage when independence was achieved by the kingdom in 1946. The three decades till 1976 saw this sector diversify at a fairly rapid rate with the establishment of some basic industrial projects that catered to the needs of the domestic market. The three year plan of 1973 and five year plan of 1976 both had an influential role to play in its expansion. This development pattern of the industrial sector was seriously abrupted on many instances such as the continuous political instability prevailing in the country as a consequence of the 1967 war and 1970 civil disturbances. The high degree of uncertainty was also reflected in the people's attitude to invest in highly liquid assets. This was aggravated by the minor contribution made by the commercial banks towards the industrial sector which confined itself to short term loans for well established companies. The medium and small scale industries were left far behind. It was with this deficiency of financial system in mind, that the government of Jordan Created a specialised credit institution called IDB for fulfilling the long term needs for medium and small scale industries.

The total number and amount of loans advanced by the Industrial Development Bank of Jordan have been explained in the table no. 6.11.

Table 6.11
Approved Loans Classified by Purpose

Year	Construc -tion	Machi- nery	Raw Mater- ials & Risk Capital	Total Industrial (2+3+4)	Tourism	Grand Total (5+6)	Percentage of total Industrial (5 / 7) x 100
1	2	3	4	5	6	7	8
1976	0.29	2.32	-	2.61	0.91	3.53	74.2
1977	0.83	3.10	-	3.93	0.78	4.71	83.4
1978	0.71	3.17	-	3.88	1.27	5.15	75.3
1979	0.25	3.24	-	3.50	0.30	3.79	92.3
1980	0.55	3.27	1.47	5.29	1.22	6.51	81.3
1981	0.67	4.83	2.02	7.52	0.73	8.25	91.2
1982	1.79	6.23	2.02	10.04	0.27	10.31	97.4
1983	1.29	3.26	3.68	8.23	0.22	8.45	97.4
1984	0.82	2.00	3.31	6.14	0.99	7.13	86.1
1985	1.28	4.21	1.77	7.26	0.22	7.48	97.1
1986	1.06	4.26	2.79	8.11	0.76	8.87	91.4
1987	0.43	4.23	2.82	7.48	0.23	7.71	97.0
1988	0.80	6.05	4.45	11.30	0.10	11.40	99.1
1989	0.58	5.41	6.83	12.82	1.26	14.08	91.1
1990	2.33	6.83	4.17	13.33	1.85	15.18	87.8
Compound growth rate (percentage per annum)							
1976-80	13.65	7.10	-	15.08	6.03	13.02	
1981-85	13.82	-2.71	-2.60	-0.70	-21.32	-1.94	
1986-90	17.06	9.90	8.36	10.44	19.47	11.34	

Source :

(1) Industrial development bank annual reports during 1976-1990.

(2) Raw material started as from January 1980 also, for the years 1989, 1990 the break up is given for Raw Material (revolving) and risk capital in col. 4.

The given table shows the sectoral distribution of loans granted by IDBJ to the industrial and tourism sectors between 1976 and 1990. The total industrial loans approved have been categorised as the construction sector, machinery and raw material along with the involvement of risk capital.

To understand the changes in the role played by IDBJ in providing finance to different sectors of the Jordanian economy, the table can be explained in three phases. Phase I showing the changes during the time period between 1976 and 1980, phase II shows its contribution during 1981-85 and phase III explains the amount of loans advanced by IDBJ during 1986-90.

It can be seen from the table that the bulk of the total specialized credit was extended for purchasing machinery and equipment, followed by the use of loans for factory construction and the remaining percentage of the manufacturing credit being financed for the purchase of raw materials. This type of distribution pattern has been particularly helpful for financing fixed assets, keeping in mind the role of commercial banks as a short term financier of working capital.

During the first phase i.e., 1976-80, the industrial credit constituting credit given for construction, machinery and raw materials and risk capital, increased appreciably a regular interval from 2.61 million JD in 1976 to 5.29 million JD in 1980 but in terms of percentage of the total loans approved, it fluctuated during the same period. During this period, the overall compound growth rate was 13.02% per annum, whereas the compound growth rate with reference to industrial loans granted was 15.08%. This shows a significant and positive change in terms of loans approved in favour of industry.

It can be further expressed that 63.7% of the total loans granted were directed for the purchase of machinery and only 11.1% were approved for the projects related to the construction sector and 18.9% for the tourism sector. An average of 81.3% of the grand total was disbursed to the industrial sector. IDBJ started giving loans for the finance of raw materials and risk capital started only in 1980. The compound growth rate of the loans granted to industrial sector shows a growth of 15.08%, which is higher than the growth rate observed in the construction sector (13.65%) and machinery (7.10%).

During the second phase i.e., 1981-85, there was an overall decline in the total loans granted by the IDBJ to different sectors from 8.25 million JD in 1981 to 7.48

million in JD 1985, indicating a percentage decline of 10.2%. There was also a negative compound growth rate of 1.94% in the grand total during this period.

The total loans granted to the industrial sector in turn also indicated a negative compound growth rate of 0.70%. Among the loans granted to the industrial sector, loans given for the purchase of machinery showed a slight downward trend from 4.83 million JD in 1981 to 4.21 million JD in 1985, indicating a negative compound growth rate of 2.71%, followed by a negative growth rate of 2.60% of the loans granted for the purchase of raw materials. The only sector that showed a positive growth rate was that of the construction sector. The total loans granted to this sector rose from 0.67 JD million in 1981 to 1.28 million JD in 1985, indicating a compound growth rate of 13.82% per annum. However, the total percentage of loans granted to the industrial sector rose from 81.3% in 1980 to 97.1% in 1985. However, figures of 1982 indicate that the IDB loans to industrial projects increased from 7.52 JD million in 1981 to 10.05 JD million in 1982 i.e., by 33.8%. This was due to the fact that during 1982, the ministry of Industry and Trade issued 156 licences for the establishment of various industrial projects. Out of the total licences given, 20 projects were granted total exemption and 28 projects were given partial exemption. The total value of these exemptions amounted to 13.2 million JD. As a consequence, this increased the activities of the remaining projects which were granted a higher value of loans. But the amount of loans approved by IDBJ declined from 10.04 million JD in 1982 to 7.26 million JD in 1985, a reversal which affected the industrial growth.

The third phase i.e., 1986-90 indicate a rapid revival in terms of the total loans disbursed to the industrial sector. Industrial production of major industries increased during this period. The number of industrial projects registered shot up. This increase in the registration of new projects was the result of new government measures to abolish licencing procedures. The total specialized credit allocated to the industrial sector rose from 8.11 million JD in 1986 to 13.33 million JD in 1990, with a compound growth rate of 10.44% per annum. Machinery occupied 51.2% of the approved loans, followed by 17.4% of the construction sector and 31.3% for the purchase of raw materials. Out of the total credit approved, 93.28% of the total credit was received by the industrial sector and the remaining by the tourism sector.

By 1990, the Industries succeeded in boosting exports to neighbouring countries and continued their endeavours to open new channels of export to other countries.

- **The Numbers and Amounts of Approved loans by IDBJ :**

The total number and amount of loans approved by the Industrial Development Bank of Jordan for the years from 1976 to 1990 and their averages are shown in the following table no. 6.12.

Table 6.12

The Numbers and Amounts of Approved loans by IDBJ for the years 1976-1990 and their averages

Year	Number of Loans	Amount (in million JD)	Average Loan amount (in JDs Thousand)
1976	74	3.5	47
1977	61	4.7	77
1978	54	5.1	95
1979	47	3.7	80
1980	56	6.51	100
1981	79	8.25	100
1982	104	10.31	90
1983	98	8.45	86
1984	85	7.12	83
1985	129	7.48	58
1986	95	8.87	93
1987	58	7.71	133
1988	98	11.40	116
1989	116	14.12	122
1990	97	15.18	156
Compound growth rate (percentage per annum)			
	1.82	10.27	

Source : Industrial Development Bank, Annual Report 1976-1990

In terms of finance, the granting of loans has been the bank's largest sector of activity. These specialized loans extended by the IDBJ were very vital for the economic development of the country, as these loans were utilized for the purchase of fixed assets that in turn resulted in industrial expansion.

The given table gives a yearly account of the number and amount of loans approved by the IDBJ for the industrial and tourism sectors. Much discrepancy can be observed with regard to the allocation of loans for various projects, the distribution of loans for the industrial and tourism sectors showing a great deal of variations.

This table reveals that the total number of loans granted in by IDBJ increased from 74 in 1976 to 97 in 1990 i.e., an increase of 23 loans, indicating a compound growth rate of a mere 1.82% per annum. Out of the 74 loans granted in 1976, 65 were to the industrial sector amounting to 2.61 million JD whereas the remaining 9 loans were for the tourism sector having a value of 9.08 million JD, whereby the total amount of loans was 3.52 million in 1976. Although the total number of loans increased during the period under study, but it shows a fluctuating trend. These numbers does not show a single trend i.e., it shows trend in both the directions.

As far as the value of the total amount of loans approved is concerned, it can be seen that it rose from 3.5 million JD in 1976 to 15.18 million JD in 1990, indicating a compound growth rate of 10.27% per annum. Even the amount shows an inequality in approval of loans during the different period of the study.

The critical study shows that in the year 1985 the highest number of loans were granted i.e., 129 amounting to 7.71 million JD, of which 118 loans were for the industrial sector, amounting to 7.26 million JD and the remaining 11 loans were directed towards the tourism sector amounting to 0.22 million JD. Out of the total number of loans approved in 1985, 42 loans were extended to new projects for the manufacture of detergents, fertilizers, insulating materials, fodder, food products and others. The amount of loans granted for financial expansion plans and working capital were 4.4 million JD which is 58.8% of total loans.

On the other hand, in the year 1979, the lowest number of loans were approved i.e., just 47, the total amount of loans granted being 3.7 million JD. Out of these loans, 41 loans amounting to 3.4 million JD were approved for the industrial sector and the remaining 6 projects having a value of 0.3 million JD toward the tourism sector.

During 1990, this bank approved 97 loans, totalling 15.18 million JD, of which 86 loans aggregaring 13.3 million JD were extended to industrial projects and 11 loans of the value of 1.85 million JD were extended to tourism projects.

The total loan applications received during 1990 were 169, covering various fields of industry such as pharmaceuticals, detergents, food, garments etc. Out of these applications, 97 applications were approved by the Board, out of which 18 loans were extended to new projects for manufacturing computers, machines, garments and food products [20].

- **Industrial Development Bank - Equity Investment in Jordan during 1976-1990**

The information regarding equity investment by Industrial Development Bank in Jordan during the period under study is shown in the table no. 6.13.

Table 6.13

Industrial development bank - Equity Investment in Jordan during 1976-1990

(In million JDs)

Year	Equity Investments
1976	0.42
1977	0.53
1978	0.67
1979	0.92
1980	1.49
1981	2.42
1982	2.74
1983	3.01
1984	3.78
1985	3.87
1986	4.17
1987	4.23
1988	4.36
1989	3.49
1990	3.28
Compound growth rate percentage per annum.	
1976-90	14.68

Source : IDBJ annual reports 1976-1990.

In order to strengthen the industrial base of the country, the IDBJ has greatly assisted in the implementation of industrial projects. The given table reflects the position of the bank in terms of its equity investment during different years of the present study. It can be seen from the table that the major portion of the shares in the market were held by the IDBJ. The equity investments of the IDBJ have shown a consistent upward trend over the years. Its total investment in equities which was 0.42 million JD in 1976, rose to 4.36 million JD in 1988, the highest share during the period under study, and subsequently declined to 3.28 million JD in 1990. The compound growth rate per annum of these paid equity investments attained a percentage of 14.68% over the 15 years of study period.

By entering the equity market, the IDBJ has helped to fulfill three purposes.

(1) It has assisted in investing the idle funds to meet the future demands.

(2) It has also provided assistance to the new investors by participating in equity shares.

(3) It has helped in building confidence in other financial agencies and private investors to participate in industrial ventures of new companies[21].

- **Number and Amount of Loans Approved and Cancelled by IDBJ**

It has been seen that IDBJ has been evaluating and analysing different projects on a regular basis, so that the loans granted are not misutilized or used for unprofitable ventures. Keeping the main objective of industrial development in mind, the IDBJ has given approval for many new projects and has also cancelled many approved loans for better financial utilisation and management. The total number and amount of loans approved and cancelled by IDBJ are shown in table no. 6.14.

Table 6.14
Number and Amount of Loans Approved and Cancelled by IDBJ during 1976-90

Year	Number of Loans				Amount of loans (JD million)			
	Approved		Cancelled		Approved		Cancelled	
	New	Existing	New	Existing	New	Exist	New	Exist
1976	40	34	-	2	2.39	1.13	-	0.02
1977	34	27	1	6	3.50	1.19	0.17	0.29
1978	30	24	3	1	2.95	2.18	0.50	0.06
1979	29	18	2	-	2.38	1.41	0.32	-
1980	17	39	2	4	1.36	5.15	0.18	0.12
1981	29	50	1	5	3.15	5.10	0.03	0.65
1982	41	63	-	2	3.58	6.73	-	0.85
1983	28	70	7	1	2.37	6.08	0.26	0.08
1984	29	56	9	8	1.41	5.71	0.24	0.64
1985	42	87	7	3	3.07	4.41	0.38	0.18
1986	27	68	4	-	1.16	7.71	0.22	-
1987	14	44	2	1	0.70	7.01	0.16	0.04
1988	19	79	1	-	2.71	8.69	0.15	-
1989	24	92	5	3	1.63	12.49	0.08	0.34
1990	2	72	-	1	4.23	10.95	-	0.09
Total	**405**	**823**	**44**	**37**	**36.59**	**85.9**	**2.69**	**3.36**

Source : IDBJ Annual Reports 1975-76 till 1989-90.

Giving an account of the number of loans approved and the amount approved by the IDBJ in table no. 6.13, various observations are noteworthy. Out of the total number of loans approved in 1976, 40 loans were granted for new projects which included industries such as footwear, construction materials, wooden doors, windows, etc. The total amount of the new 40 approved loans was 2.39 million JD. And out of the existing 34 approved loans, 2 were cancelled, which amounted to 0.02 million JD out of the total value of 1.13 million JD.

The highest number of new loans were approved in the year 1985, which were 42, having a total value of 3.07 million JD, and the second highest existing loans of 87 were also approved in the same year, its value amounting to 4.41 million JD. It was in the same year, the highest number of new as well as existing loans were cancelled i.e., 9 new loans and 8 existing ones, the total amount being 0.24 million JD and 0.64 million JD respectively. Out of the 198 loans approved in the year 1985, 42 loans were granted for new industrial projects for the manufacturing of paints, insecticide, metal equipments, etc.

But in the year 1990, only 2 new loans were approved and only 1 existing loan was cancelled. The total amount of loan approved for these two projects amounted to 4.23 million JD. On the other hand, the existing 72 loans amounted to 10.95 million JD. During 1990, the amount of one loan cancelled amounted to 0.09 million JD.

If we analyse the complete picture, we find that 405 new loans were approved during the period under study, the total value being 36.59 million JD. Out of the total number of new loans, 44 loans were cancelled amounting to 2.69 million JD i.e., nearly 8%. On the other hand, the existing loans numbered 823, amounted to 85.94 million JD. Out of this number, 37 were cancelled amounted to 3.36 million JD i.e., nearly 4%. It can be inferred from this, that the total number of loans cancelled exceeded the number of existing loans cancelled.

6.3.2 Industrial Finance to Small-Scale Industries and Handicrafts :

For the overall development of a country, the development of small-scale industries cannot be sidelined, particularly in a country like Jordan where such industries occupy an integral part of the economy. A major portion of the manufacturing sector in the kingdom is composed of small-scale industries and handicrafts.

The small and medium scale industries are envisaged to play a very significant role in the Jordanian economy. This sector constitutes the seedlings for future growth into medium and large industries. It is a powerful tool towards rapid decentralised growth and balanced regional development. These industries also provide a sound basis for effectively linking agriculture and allied sectors with industries, for processing of products as well as providing inputs for modernisation of these sectors.

In recognition of its role, the small and medium industries sector, should be treated as a priority sector for the development and due recognition should be given to its role in the five years plans and allocation of resources.

Uptil 1975, the activities of the IDBJ were confined to financing large scale industry and well established enterprises only.(22) For the first time, the small scale Industries and Handicrafts Fund was established in March 1975, with the aim of encouraging the expansion of the existing handicrafts industries through loans extended by the IDBJ. This enabled them to purchase raw materials at concessional rates. In accordance with the Five Year Plan of 1976-80, large scale industries were characterized as high productivity sector and a sound contributor to industrial income. Per capita productivity in these industries was found to be three times in comparison to smaller establishments.

The small scale industries were primarily concentrated in the Amman - Zerga area because of its easy access to the availability of industrial services such as water, electricity and transportation. Moreover, there was also a perceptible shortage of middle level technicians in the existing small scale industries.(23)

The World Bank study has also cited that financial institutions are extremely risk averse and have not helped to promote industrial growth amongst the small scale industries thereby denying them the benefits of institutional support.

Observations made by the Arab Consult Centre also point out that only a few companies have benefitted from public funds, these being the larger establishments.(24)

In accordance with the technical Report of the Regional Development Planning Projects of Jordan, 1988; numerous strategies have been adopted to ensure smooth growth of the small scale and handicraft industries to achieve the objectives. These strategies have the following three components :

(1) Identification of new industrial opportunities in the small and medium scale industries sector through the conduction of industrial potential surveys in the region as well as indepth study at the central level for identifying possibilities in the high technology areas.

(2) Encouragement of the private enterprise to come forward to take up ventures for the success of SMI programmes.

(3) Two other salient components of the strategy relate to provision of essential inputs and consultancy services and streamlining and strengthening institutional infrastructure(25).

The total number of loans and the amount of loans approved by Small Scale Industries and Handicrafts Fund during 1976 - 1990 is shown in table no. 6.15.

Table 6.15

Small Scale Industries and Handicrafts Fund apporved loans by type of activity during 1976-1990

Trade	1976		1978		1980		1982		1984		1986		1988		1990	
	No. of loans	Amount in JD	No. of loans	Amount in JD	No. of loans	Amoun t in JD	No. of loans	Amount in JD	No. of loans	Amount in JD	No. of loans	Amount in JD	No. of loans	Amount in JD	No. of loans	Amount in JD
Buidling materials (Tiles, Bircks, Stone cutting & Quarring	20	35650	24	41800	21	58700	42	128700	30	70300	47	122000	9	27100	10	38800
Carpentry	36	64450	31	69000	21	55200	47	126700	31	81900	49	137100	6	19400	12	34600
Metal working	10	13850	21	45300	19	52900	36	114300	39	92800	63	199200	8	12500	6	35000
Maintenance	2	2300	5	11000	13	39900	35	125800	31	89700	66	202300	6	20500	7	39900
Garments & Knitting	25	25625	13	22300	5	13700	20	69700	11	30100	48	140700	5	11000	14	67200
Printing, Photography	9	15700	7	17000	5	16700	9	33600	12	32100	21	74700	1	3100	8	34800
Food products	2	2100	11	18650	15	50400	20	55000	19	50200	86	291400	21	65800	17	78400
Leather products	5	8250	2	3500	-	-	3	6600	3	9000	5	14500	-	-	3	11000
Others	1	1500	1	1500	3	6500	15	38900	12	35300	19	57400	5	19100	42	259900
Total	110	169425	115	230050	102	294000	227	699300	188	491400	404	1239300	61	178500	119	599600

Source : Industrial Development Bank of Jordan
Annual Reports 1976-1990

On the basis of the recommendations of the three development plans of 1973, to establish a special fund within the IDBJ in 1975, the total number of loans approved by the fund during its two years of operation accounted for 110 amounting to 0.16 million JD by the end of 1976.

Various small scale industries such as building materials, carpentery, maintenance, food and leather products were covered. During 1979, in response to the increase in the cost of setting up small scale industries and handicrafts projects, the IDBJ increased the ceiling on funds loan from 3 thousand JD to 4 thousand JD, of which 1 thousand JD could be allocated for the purchase of raw materials.

In 1980, the Small Scale Industries and Handicrafts Fund received 112 loan applications, of which 102 loans of the total value of 0.29 million JD were approved and 48 of these loans were regionally distributed in Amman and 12 loans in Irbid.

By 1982, the number of loans approved by the fund increased almost two and a half times over 1980, totalling to 227 with an amount of 0.69 million JD. Out of the total number of loans, 42 loans i.e., 18.4% of amounts approved during 1982 were for building material and 47 loans i.e., 18.1% of approved amounts were for carpentry projects, while the rest of the loans were granted for other projects.

The largest number of loans approved by the fund was that of 404 in 1986, its value totalling upto 1.239 million JD. Amman and its suburbs accounted for 47% (190) of the loans whereas the rest of the amount approved was granted to projects located in other areas of the kingdom. 66 such loans were granted for maintenance of the small scale industries whereas 86 loans i.e., 21.2% of the loans were assigned for food products.

The IDBJ continued to direct the fund's policy to achieve more even distribution of small scale and handicraft projects in the kingdom and encouraged the establishment of projects with new ideas.

During 1988, the fund just approved 61 loans totalling 0.178 million JD. It means that the number and amount of loans fell drastically as compared to the figures of 1986. Out of the total loans sanctioned, 36.8% were for food products, followed by 15.2% for building material projects.

During 1990, the bank expanded the funds activities to cover lending to small scale activities in medical services. The number of loans approved rose to 119 and the amount of loans approved was 0.599 million JD. About 29 loans were granted to laboratories and clinics, 17 going to food products and 14 loans to garments and knitting industries.

The compound growth rate per annum of the number as well as amount of loans over the past 15 years was calculated to be 0.525% and 8.79% respectively.

6.3.4 Industrial Finance in the Jordan Capital Market :

One of the most noteworthy developments of the past few decades, following the influx of Arab Cash into the Jordanian economy, has been the ability of Jordanian industries and entrepreneurs to meet their capital requirements in the Amman Capital Market through the syndicated dinar loans and bond issues that have gained recognition since 1978.

Since a domestic capital market commenced operations only in 1978,the industrial firms preferred to raise funds through commercial banks. This made it more convenient for the industrialists to meet their financial needs as well as encourage the public to invest in industrial enterprises. As has been explained earlier in the chapter, the commercial banks inability to raise medium and long term loans facilitated the Amman Financial Market to continue its activities of strengthening the capital market and channeling the savings into appropriate investments.

From an economic development point of view, three areas of functional deficiencies could be identified in the functioning of commercial banks : firstly, strict adherence to the traditional banking practice of confining bank credit only to short term loans; secondly, a distinct sectoral bias towards financing foreign trade transactions; and lastly, maintenance of excessive liquidity in domestic banking(26).

It is here that the specialized credit institutions as well as the Jordanian capital market comes into the limelight. Industrial sectors being deprived of long term loans from the commercial bank started showing their dependence on these institutions.

Today, the AFM is an agency under the government in whom are vested the power of financial and administrative independence. It has come up as an active securities exchange commission with a participatory role being played by the investors. A major breakthrough in the activities of the capital market has been its role for organizing and facilitating trading of securities to the industrial and mining sector companies.

Keeping in mind various factors that are necessary for the overall development of a market, along with fair trading activities, the Jordanian Capital Market has made ardent attempts to establish an adequate investment climate, much stress being laid on the accumulation of savings for upcoming projects, particularly pertaining to the industrial sector. There has been a remarkable increase in the volume of trade at the AFM over the past 15 years which has been clearly depicted in Table No. xxxx of the chapter on Amman Finanacial Market.

The number of shares traded have risen from 2.4 million in 1978 to 136 in 1990, experiencing a compound growth rate of 30.8% per annum. The volume of shares traded also experienced a sharp upward rise amounting to 268.8 million JD in 1990 in comparison to 5.6 million JD in 1976, having a compound growth rate of 29.4% per annum.

The total number and value of shares of industrial and mining companies traded at Amman Financial Market during the period under study is depicted in table no. 6.16.

Table 6.16
Number and value of shares traded in Amman Financial Market

Year	Number of shares (million)	Volume of shares (JD million)
1978	0.9	2.9
1979	2.0	6.8
1980	5.1	17.2
1981	13.9	32.1
1982	14.7	39.8
1983	13.3	20.9
1984	12.4	14.6
1985	9.9	11.8
1986	16.0	18.3
1987	59.3	91.6
1988	64.8	76.4
1989	129.7	240.3
1990	71.0	158.0

Source : Amman Financial Market Statistics, 1978 - 1991.

The table no. 6.16 clearly shows the number of shares of the industrial and mining companies traded at the market. Trading of share is carried out on the Regular Market floor, which may be described as a highly organised and controlled central market, which works in accordance with the rules and regulations laid down by the government. Hence, the Amman Financial Market works on the basis of demand-supply relationship. The industrial sector plays a far more active role in comparison with other sectors such as banking and financial sector, insurance and the services sector; on the market floor.

The number of shares distributed to the industrial sector has shown a regular upward trend from 0.9 million in 1978 to 129.7 million in 1989, however it declined to 71 million in 1990. Value of shares increased from 2.9 million JD in 1978 to 240.3 million JD in 1989 which subsequently declined to 158 million JD in 1990. The number of shares increased by 33.8% per annum between 1978-90. A tangible progress was observed in the market between 1980-81 in which the number of shares traded in the industrial sector rose by 63.3% over the 1980 level and value of shares-rose by 46.4%.

By 1983, the increase in the overall growth of shares was abrupted by a hardly hit economic recession in the Kingdom. The after effects of the recession were observed in the following two years, wherein by 1985 the number of shares traded at the industrial sector declined by 6.5% per annum over the 1981 level.

A major improvement in the industrial activities was reflected in the shares traded in 1987 which rose by 83.3% over 1985 level. Subsequently, the value of shares also showed an upward trend experiencing a growth rate of 87.1% over the figures of 1985.

Improvement in the industrial activities was largely attributed to the interest of the government in the working of these companies as well as the their exemption from exercise and other duties.

Indicators of 1989 reveal that it was this year when the industrial sector occupied the largest number and value of shares, totalling upto 129.7 million and 240.3 million JD respectively, that is, the highest percentage increase of 50% and 68.2% respectively over the previous year. The industrial sector faced its highest level of activity in 1989 at the AFM.

Ironically, this considerable improvement was once again interuppted in 1990 by a severe economic depression that hit the Kingdom in response to the gulf crisis. The number of shares traded in the industrial sector companies declined by 82.6% whereas the value of shares traded resulted in a 52% decline over the indicators of 1989.

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