Industrial Structure, Financial Liberalization & Industrial Finance in India: An Assessment

Santosh Kumar Das

The study explores the emerging relationship between the industrial and financial structures; and its implications on industrial finance. The dynamic interaction between the two sectors has been examined by analysing whether financial liberalisation succeeded in removing financial constraints on industrial sector. We found that not only financial liberalization has not succeeded in removing financial constraints for industrial development in India, but also it underlines growing asymmetries between the financial and industrial sectors. The financial structure that emerged in the post reform period is not aligned as per the diverse needs of the industrial sector. It failed to create a market based approach to the long term financial needs of the industry.

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Introduction

The critical role that finance plays in the process of industrial development received considerable attention with the seminal work of Greschenkron (1962) who, while explaining the process of industrialization in Europe in a historical context, highlighted that the banks did play critical role in the process of industrialization. Since then, financial policy as an instrument of industrialization has been designed world over to achieve faster rates of industries.

Absence of availability and access to affordable finance has been identified as one of the key holding blocks in the path of industrial development in India (Bhattacharjee & Chakrabarti, 2013; Khanna, 2013; Das, 2015). It was perceived that the underdeveloped financial sector due to state control was the primary reason behind unavailability of adequate financial resources for industrial sector. Financial liberalization was argued to be appropriate policy measure which will be instrumental to India's industrialization. It was expected that following reforms in the financial sector, a developed financial sector will be able to fulfil the financial needs of the industrial sector.

Following financial reforms, the structure of the Indian financial system has undergone significant transformation. Though it still continues to be primarily a bank driven financial system, there have been attempts to establish a vibrant mechanism for resource mobilization and allocation. This change in approach had serious implications for industrial finance. While with liberalization and opening up new sources of finance emerged; however, the earlier existing public financial institutions like the Development Finance Institutions (DFIs) were converted into universal banking due to insufficient government funding (Ray, 2015). While the universal banking (commercial banks) system provided only working capital, the term loans that was earlier recognized as key in reducing the financial constraints of the firms significantly went down. Even the working capital provided by the universal banking system is not sufficient enough to meet the growing credit demand of the Indian industries.

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With the deregulation of directed credit program, the flow of bank credit to industrial sector went through restructuring with dilution of priority sector lending program. The structure of the newly emerged financial system following financial liberalization while brought new opportunities in terms of access to finance for a few industries, which are large in nature and registered with the stock exchanges; on other side reduced the access to finance to several Small and Medium Enterprises (SMEs). The SMEs were highly dependent on the DFIs as one of the key accessible sources of finance, which are no longer available to them (currently there are few operational DFIs). While the large firms now could borrow from both internal and external sources with low interest cost, the SMEs are increasingly faced with financial constraints. While there has been diversification of the sources of industrial financing in India (even if it is not sufficient), still the size and the location of the firm / industry play a determining role when it comes to accessing finance. Therefore, as the current financial system excludes many firms from accessing finance, is not adequate for many (industry as a whole). In this scenario, a few firms / industries have access to different sources of finance both internally and externally; on the other hand, a large number of firms (including new firms) do not have access to any form of finance. Against this backdrop, this paper has attempted to study the impact of financial liberalization on industrial development in India by analyzing the relationship between the structures of the financial and industrial sectors. It has been studied by analyzing whether financial liberalization has succeeded in removing credit constraint on the Indian industry.

Structure of Industrial Sector

The industrial sector in India is diverse in terms of location, size and the type of ownership. As per the Sixth All India Economic Census, in terms of number of establishments by broad economic activity, the total number of establishments in the manufacturing sector was 10329822 which is 17.66 percent of the total number of establishments in the country. Out of the total number of

Table 1 Region & Location- wise Spread of Establishments in Manufacturing Sector: 2013-14

State/UT	Rural		Urban		Total	
	Number	% share in Total Number of Establi-shments	Number	% share in Total Number of Establi-shments	Number	Share (%)
Jammu & Kashmir	81071	0.78	37814	0.37	118885	1.15
Himachal Pradesh	63089	0.61	9007	0.09	72096	0.70
Punjab	140926	1.36	164343	1.59	305269	2.96
Chandigarh	155	0.00	6377	0.06	6532	0.06
Uttarakhand	32636	0.32	23307	0.23	55943	0.54
Haryana	80790	0.78	95991	0.93	176781	1.71
Delhi	1397	0.01	154553	1.50	155950	1.51
Rajasthan	264718	2.56	211231	2.04	475949	4.61
Uttar Pradesh	597306	5.78	544097	5.27	1141403	11.05
Bihar	230698	2.23	81964	0.79	312662	3.03
Sikkim	917	0.01	474	0.00	1391	0.01
Arunachal Pradesh	1420	0.01	1009	0.01	2429	0.02
Nagaland	7773	0.08	2231	0.02	10004	0.10
Manipur	45483	0.44	24145	0.23	69628	0.67
Mizoram	1784	0.02	3118	0.03	4902	0.05
Tripura	24884	0.24	12163	0.12	37047	0.36
Meghalaya	7212	0.07	2701	0.03	9913	0.10
Assam	155959	1.51	55210	0.53	211169	2.04
West Bengal	865186	8.38	599658	5.81	1464844	14.18
Jharkhand	64359	0.62	66243	0.64	130602	1.26
Odisha	327016	3.17	61690	0.60	388706	3.76
Chhattisgarh	50411	0.49	39970	0.39	90381	0.87
Madhya Pradesh	264124	2.56	214305	2.07	478429	4.63
Gujarat	138112	1.34	366396	3.55	504508	4.88
Daman & Diu	318	0.00	1811	0.02	2129	0.02
D & N Haveli	696	0.01	1586	0.02	2282	0.02
Maharashtra	373584	3.62	546888	5.29	920472	8.91
Karnataka	322876	3.13	271721	2.63	594597	5.76
Goa	4249	0.04	6919	0.07	11168	0.11
Lakshadweep	142	0.00	514	0.00	656	0.01
Kerala	263491	2.55	268316	2.60	531807	5.15
Tamil Nadu	357961	3.47	576246	5.58	934207	9.04
Puducherry	2374	0.02	6136	0.06	8510	0.08
A & N islands	985	0.01	799	0.01	1784	0.02
Telangana	256249	2.48	177673	1.72	433922	4.20
Andhra Pradesh	412519	3.99	250346	2.42	662865	6.42
Total	5442870	52.69	4886952	47.31	10329822	100

Source: Calculations based on Sixth All India Economic Census data.

establishments, 5442870 (52.69 percent) are located in the rural areas and the rest 4886952 (47.31 percent) are in the urban areas (Table 1).

The share of establishments employing more than 100 workers does not even add up to 1 percent of the total manufacturing establishments.

More than 93 percent of the total manufacturing establishments are small in size (Table 2). About 5 percent of the manufacturing establishments are employing more than 6 people and not more than 9 people. The number of large establishments are relatively less in the manufacturing sector. The share of establishments employing more than 100 workers does not even add up to 1 percent of the total manufacturing establishments. Establishments employing more than 5 workers tend to locate in the urban areas, where as smaller establishments, having 1-5 workers are predominantly located in the rural areas. More than 50 percent of the establishments, having employment size between 1 and 5 are located in rural areas, and 42.65 percent of the small establishments are located in the urban areas. With the increase in the size of the establishments in terms of employment size, for relatively large proportion of the manufacturing establishments, the urban areas are the preferred locations of their operation.

Table 2 Distribution of Establishments by Size of Employment in Manufacturing Sector: 2013-14

Employment Size	Rural		Urban		Total	
	Number of Establishments	% share of Total Number of Establishments	Number of ments	% share of Total Number of Establishments	Number of Establishments	% share
1-5	5208109	50.42	4405891	42.65	9614000	93.07
6-9	152709	1.48	356359	3.45	509068	4.93
10-14	30292	0.29	45583	0.44	75875	0.73
15-19	10157	0.10	20724	0.20	30881	0.30
20-24	8023	0.08	12477	0.12	20500	0.20
25-29	4074	0.04	7958	0.08	12032	0.12
30-99	20979	0.20	29071	0.28	50050	0.48
100-199	4869	0.05	4941	0.05	9810	0.09
200-499	2582	0.02	2742	0.03	5324	0.05
500 or more	1076	0.01	1206	0.01	2282	0.02
All Classes	5442870	52.69	4886952	47.31	10329822	100

Source: Calculation based on Sixth All India Economic Census data.

The distribution of establishments in the manufacturing sector by type of ownership suggests that about 95 percent of the establishments are owned by private proprietors (Table 3). While less than 1 percent of the total manufacturing establishments are owned by the government, the rest of the establishments are owned by private entities in different forms. These private entities included private partnership (0.88 percent), private company (0.41 percent), private self-help group (0.13 percent), Private co-operative (0.08 percent), and private not-profit institutions (0.09 percent).

Table 3 Distribution of Establishments in Manufacturing Sector by Type of Ownership: 2013-14

Type of Ownership	Number of Establishments	% share
Govt./PSUs	83483	0.81
Private-Proprietary	9774315	94.62
Private-Partnership	91076	0.88
Private -Company	42809	0.41
Private-Self Help Group	13632	0.13
Private-Cooperative	8432	0.08
Private-Non- Profit Institution	9764	0.09
Private – Others	306311	2.97
Total	10329822	100

Source: Calculation based on Sixth All India Economic Census data.

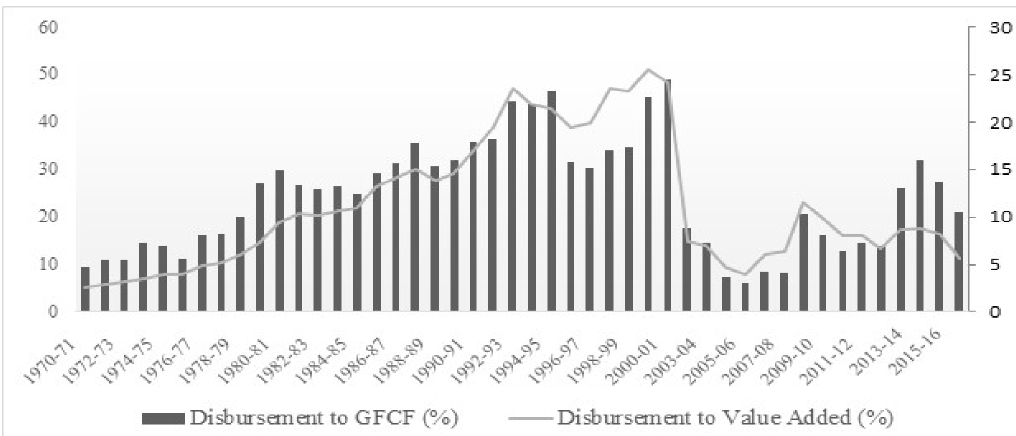
Financial Structure in Post Liberalization Period

The financial liberalization brought several major changes in the institutional structure of the financial sector in India. These include increased share of private and foreign banks even the public sector banks continue to dominate, greater importance of the financial markets, greater integration with the global financial markets. From an industrial financing perspective, on the one side, the primacy of the existing Developmental Financial Institutions (DFIs) declined substantially. On the other, market-based financing gained importance with greater envisaged role of capital market as provider of finance for industry.

Decline of DFIs

During the early years of Independence, the DFIs played a critical role as providers of long term finance at all India level, and also term lending institutions of the states operating within the states (Nayyar, 2015). During this period several term lending institutions, at national and regional (state) level were established. The importance of these specialized term lending institutions remained intact through the period of bank nationalization till the first decade into the post liberalization period (Fig. 1). The share of total disbursement by DFIs in the Gross Fixed Capital Formation (GFCF) of the manufacturing sector reached almost 50 per cent in 2000-01. Between 1970-71 and 1994-95, disbursement by the DFIs increased from 10 percent to close to 50 percent. The important role that the DFIs played during this period is evident from another indicator, which is disbursement by the DFIs as a percentage of value added in manufacturing sector. Data shows that the ratio of DFIs disbursement to value added in the manufacturing sector in percentage terms went up rapidly from 2.6 per cent in 1970-71 to 25.6 per cent in 1999-00. Subsequently, it declined substantially in the later years with the demise of development banking. Several DFIs were converted into universal commercial banks.

Fig. 1 Total Disbursement of DFIs in Manufacturing Sector: 1970-2017



Source: Nayyar (2015) & estimated from ASI Annual Results

Declining Presence of Government Owned Banks

One of the critical outcomes of the liberalization policy was the decline of govt. owned banks in India. During the period from bank nationalization till liberalization, the public sector banks played a critical role in encouraging local entrepreneurship by disbursing verities of loans. Not only these banks did provide working capital to the industrial sector, they also provided financial support to small scale industries, rural industrialization, handicraft sector etc. With liberalization, the basic objective of the PSBs also went through a revision that had far reaching implications. Profitability became the primary criteria of evaluating the performance of a bank. With change in objectivity, the PSBs abandoned their developmental role. The decline of public sector banking and the emergence of private banking can be seen from the two key indicators – decline in the branches or offices of the PSBs and decline in the asset share of the PSBs. Not only the PSBs witnessed relative decline in their

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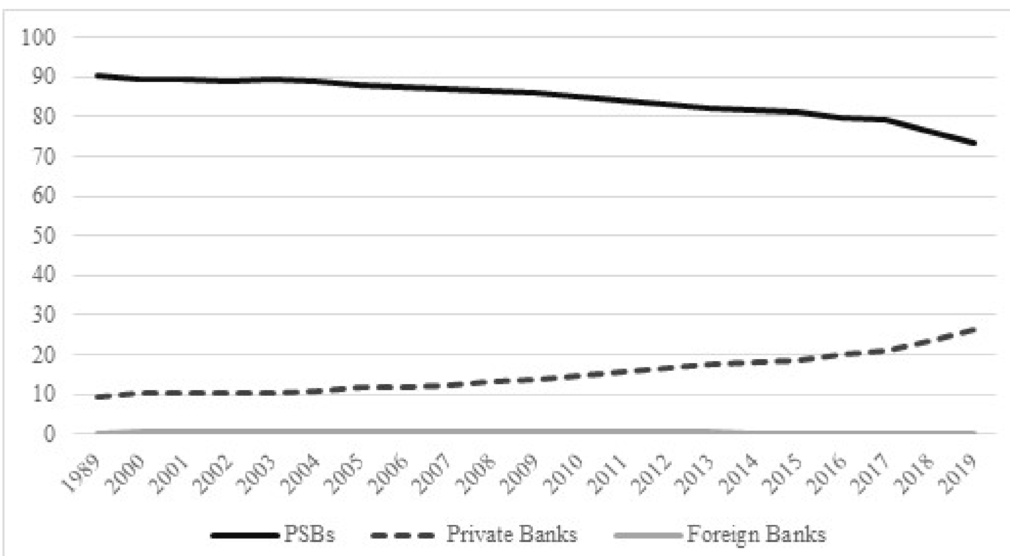
role as providers of finance, subsequently, government ownership in these banks also declined substantially. Though, PSBs still continue to constitute largest share in terms of geographical reach and asset, there has however been a paradigm shift in terms of nature of banking in India.

With the liberalization, the presence of private banks increased. There has been a corresponding increase in the number of bank branches or offices as well. Foreign banks have not been able to expand the way private banks have expanded their offices or branches (Fig. 2). Though it is still the PSBs which dominate the banking operation with their vast branch network, the private banks have expanded substantially. As of March 2019, out of total number of functioning offices of the SCBs, the PSBs accounted for 73.6 per cent, followed by private banks (26 per cent) and foreign banks (0.21 per cent). There has been a decline in the branch share of PSBs from about 90 per cent in 1989 to 73.6 per cent in 2019. During the same time period, the private banks significantly expanded their operations. This is evident from the fact that the branch shares of private banks went up from about 9.4 per cent in 1989 to about 26 per cent in 2019.

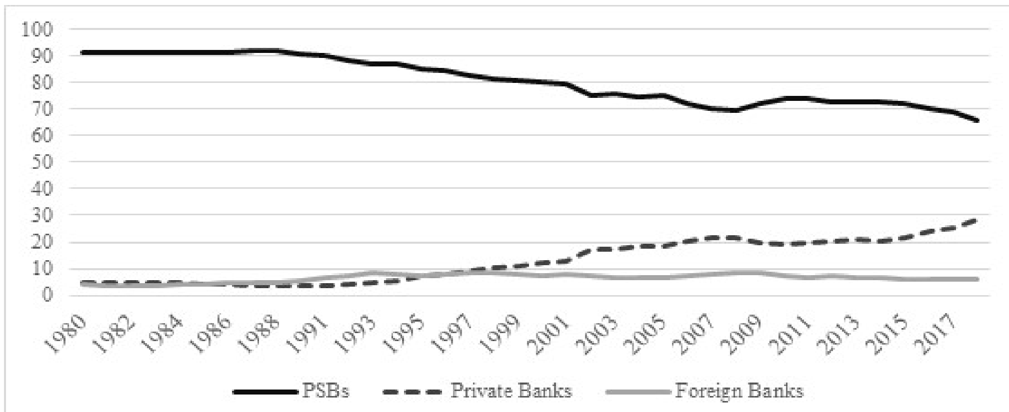
Fig. 2 Distribution of Functioning Offices of Commercial Banks (%)



Source: Calculation based on RBI data.

A very similar story emerges from the analysis of asset distribution among different bank groups (Fig. 3). The asset shares of PSBs declined from 91 per cent in 1980 to 65.8 per cent in 2019. On the other side, the asset shares of the private banks increased substantially from 5 per cent to 28.1 per cent during the above time period. While the private banks did expand their asset share considerably, their foreign counterparts however did not expand the way private banks did. There was a dip in the asset share of foreign banks from the peak of 8.5 per cent in 2009 to 5.7 per cent in 2019.

Fig. 3 Asset Share of Indian Scheduled Commercial Banks (%)



Source: Calculations based on RBI data.

Declining Rural Bank Branches

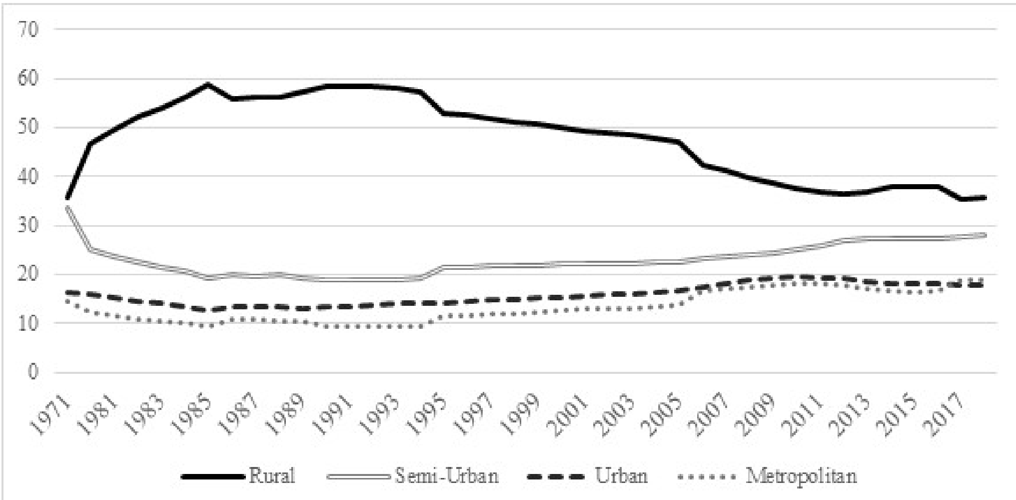
In the post reform period, the share of rural bank branches has declined substantially from about 58.5 percent in 1991 to about 35.6 percent in 2018. On the other hand, the share of semi urban, urban and metropolitan areas has increased during the same time period (Fig. 4). With growing presence of private banks and entry of foreign banks in the post liberalization period, there has been increase in the number of bank branches or offices in the urban and metropolitan areas as it has been their preferred area of operation. With changed framework of banking and its operation, where profitability is supposedly the primary objective; banks prefer to locate considering their business assessment. This however is likely to adversely impact the less developed regions in terms of access to bank credit for starting any new economic activity.

In the post liberalization period, there has been increase in the number of bank branches or offices in the urban and metropolitan areas as it has been their preferred area of operation.

Changing Structure of Bank Lending

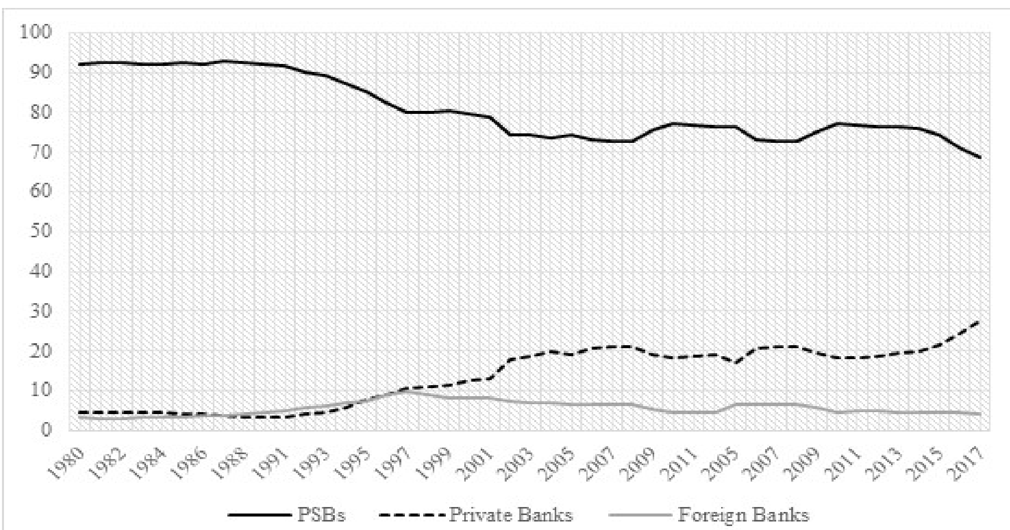
The decline of the public sector banking and credit planning has resulted in decline in credit share of the PSBs, as well as restructuring of the composition of bank lending in India. The distribution of disbursement of credit among different bank groups shows that the credit share of PSBs has declined from more than 90 per cent in 1980 to 68.5 per cent in 2017. On the other hand, the private banks have gained substantially during the same period (Fig. 5), from 2 percent to 27.4 percent between 1980 and 2017.

Fig. 4 Distribution of Bank Branches in India (%)



Source: RBI. Statistical Tables Relating to Banks in India, various issues.

Fig. 5 Credit Share by Bank Ownership of Scheduled Commercial Banks in India (%)



Source: Calculations based on RBI data.

The increase in private bank lending and reduction in the share of PSBs in total bank lending has resulted in restructuring in the composition of the bank lending at both broad sectoral and sub sector levels. The biggest loser in terms of distribution of bank credit has been the industrial sector (Fig. 6). The credit share of industrial sector (large, medium and small) in total bank credit has declined substantially from 57 percent in 1980 to 33.4 percent in 2019. The decline was

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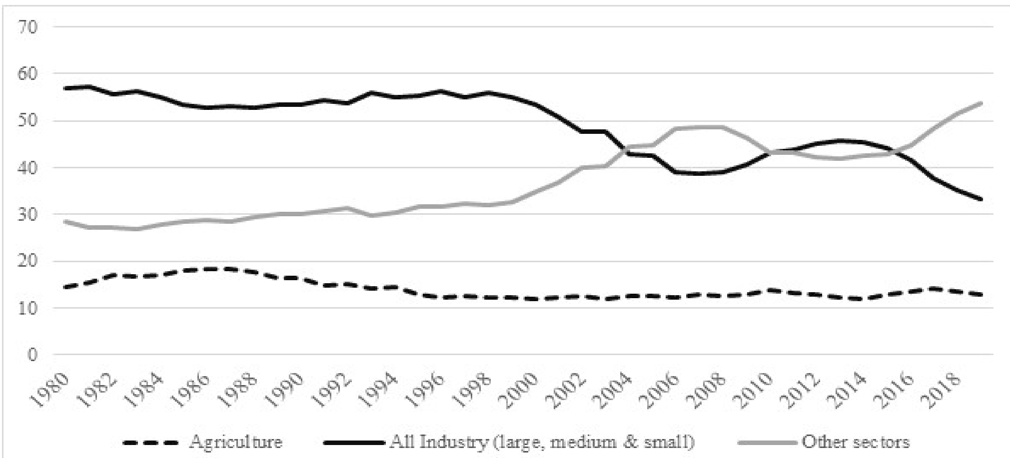
much faster during the later years of liberalization (2000s). Credit to agriculture sector too declined, however there has been significant increase in bank lending in other sector that includes services sector and personal loans.

Fig. 6- Bank Credit to Broad Sectors (%)



Source: Calculations based on RBI data.

Recent data shows that bank lending to service sector and personal loans constitute more than 50 percent of the total bank lending in India (Table 4). Lending to these sectors is following an upward trend. Data also shows that with in the industrial sector, there has been substantial decline in lending to the medium segment industries. While lending to all segments has declined, however the decline is fast in case of the medium industries. Lending to medium industries as percentage of total bank credit decline from 5 percent in 2008 to 2.12 percent in 2019.

Greater Role of Global Finance

Financial liberalization has facilitated greater role for global finance in India. During the later years of financial liberalization (2000s), there has been significant flow of financial resources into India, both in the form of foreign investment and borrowings. While the benefit and the volume of real inflow of foreign investment both in the form of foreign direct investment (FDI) and foreign portfolio investment (FPI) is subject to debate, there has been substantial inflow of gross foreign investment into India (Table 5). The flow of foreign investment is substantially high during the post crisis period, largely due to portfolio investment. Similarly, flow of foreign borrowings into India has increased substantially in the form of external commercial borrowings (ECBs) and short-term credit.

Table 4 Sectoral Deployment of Bank Credit (percent)

Year	Agriculture & Allied Activities	Industry (Micro & Small, Medium and Large)	*Large*	*Medium*	*Micro & Small*	Services	Personal Loans
2008	12.49	38.93	*27.89*	*5.03*	*6.02*	24.91	23.67
2009	13.02	40.53	*29.33*	*4.69*	*6.50*	24.84	21.62
2010	13.68	43.15	*31.99*	*4.36*	*6.79*	23.91	19.27
2011	13.11	43.75	*34.84*	*3.18*	*5.73*	24.38	18.76
2012	12.74	45.16	*36.74*	*2.91*	*5.52*	23.85	18.25
2013	12.11	45.80	*37.40*	*2.56*	*5.84*	23.65	18.43
2014	12.04	45.51	*36.97*	*2.24*	*6.30*	24.19	18.26
2015	12.76	44.27	*35.87*	*2.07*	*6.33*	23.54	19.43
2016	13.49	41.71	*34.28*	*1.75*	*5.67*	23.54	21.27
2017	13.99	37.77	*31.08*	*1.48*	*5.21*	25.40	22.84
2018	13.40	35.11	28.91	1.35	4.85	26.67	24.82
2019	12.87	33.43	*27.84*	*1.23*	*4.35*	27.98	25.72

Source: Calculations based on RBI data.

Industrial Finance after Financial Liberalization: Emerging Features

The access to and availability of adequate industrial credit or financial resources is critical for industrial development. We elaborate to what extent financial liberalization has helped in improving the access and availability of credit or finance.

Declining Share of Industrial Credit

The declining share of bank credit to the industrial sector is one of the key emerging features or outcomes of the liberalization exercise. Contrary to the expectation, the share of industrial sector in total bank non-food credit declined during the later years of liberalization (Fig. 7). The bank credit to the industrial sector declined from about 57 percent in 1980 to about 35 percent in 2018. The decline was faster between 1997 and 2008. The decline is much faster for the small industry sector (SSI) relative to the large sector.

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Insufficient Fund Mobilization by Stock Market

The stock market is an important source of finance for the industrial sector. Companies raise resources by issuing IPOs and debentures. Data suggests that mobilization of funds through the stock market is not adequate from the perspective of industrial financing. After an initial surge, the equity market has not performed as per the expectation (Table 6). The new issues in terms of number was relatively high between 1993 and 1997. The IPOs declined substantially

Table 5 Flow of Financial Resources to India (US$ million)

Year	Foreign Investment			Foreign Borrowings			
	Foreign Investment	*FDI*	*FPI*	Loans	*External Assistance*	*ECBs*	*Short Term Credit*
1990-91	113	*107*	*6*	9432	*3397*	*4282*	*1753*
1991-92	151	*147*	*4*	9419	*4367*	*3152*	*1900*
1992-93	589	*345*	*244*	8671	*3302*	*1179*	*4190*
1993-94	4609	*651*	*3958*	9970	*3475*	*3015*	*3480*
1994-95	5763	*1351*	*4402*	10930	*3193*	*4249*	*3488*
1995-96	5644	*2174*	*3456*	11331	*2933*	*4261*	*4137*
1996-97	7825	*2864*	*4953*	17720	*3056*	*7579*	*7085*
1997-98	9266	*3596*	*5573*	17301	*2885*	*7382*	*7034*
1998-99	5892	*2518*	*3225*	14771	*2726*	*7231*	*4814*
1999-00	12240	*2170*	*9951*	13060	*3074*	*3207*	*6779*
2000-01	17720	*4101*	*13619*	23806	*2941*	*9621*	*11244*
2001-02	15488	*6229*	*9259*	11601	*3352*	*2687*	*5562*
2002-03	14001	*5168*	*8833*	11568	*2878*	*3514*	*5176*
2003-04	32682	*4464*	*28218*	19667	*3350*	*5228*	*11089*
2004-05	46934	*6087*	*40847*	30287	*3809*	*9084*	*17394*
2005-06	77298	*9178*	*68120*	39479	*3631*	*14343*	*21505*
2006-07	133210	*23590*	*109620*	54642	*3767*	*20883*	*29992*
2007-08	271121	*37322*	*233800*	82192	*4240*	*30293*	*47658*
2008-09	171660.2	*43005.9*	*128654*	62216.87	*5230.2*	*15221.9*	*41764.8*
2009-10	198652.7	*38484.1*	*160169*	74163.46	*5896.95*	*15002.7*	*53263.9*
2010-11	292561.2	*38609*	*253952*	108780.7	*7881.86*	*24123.1*	*76775.7*
2011-12	234617.7	*49007.4*	*185610*	140990.5	*5645.9*	*32590.3*	*102754*
2012-13	215026.9	*39786.2*	*175241*	155085.3	*4734.68*	*27616.5*	*122734*
2013-14	246766	*43582.3*	*203184*	134836.2	*4659.19*	*30059.8*	*100117*
2014-15	308556.5	*51795.7*	*256761*	123354.9	*5779.67*	*27846.5*	*89728.7*
2015-16	276433	*59878.2*	*216555*	120322.9	*6123.3*	*24156.7*	*90042.9*
2016-17	310522.4	*70784.3*	*239738*	120532.1	*6494.79*	*22584.5*	*91452.9*
2017-18	359545.6	*64461.4*	*295084*	147111	*7718.01*	*38879.1*	*100514*

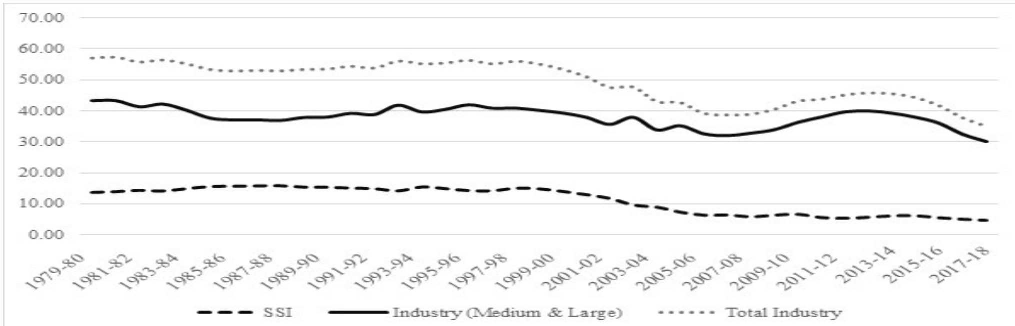
Source: RBI Handbook of Statistics on Indian Economy.

The IPOs declined substantially after initial years of liberalization.

after initial years of liberalization. Subsequent events of Asian financial crisis and global financial crisis did adversely impact the performance of the stock market. The volume of new issues in terms of value suggests that equity market cannot be seen as a stable source of funds for industry in India.

Another dimension of the capital that was raised from the primary market is

Fig. 7 Bank Credit to Industrial Sector (% to Non-Food Credit)



Source: RBI Handbook of Statistics on Indian Economy.

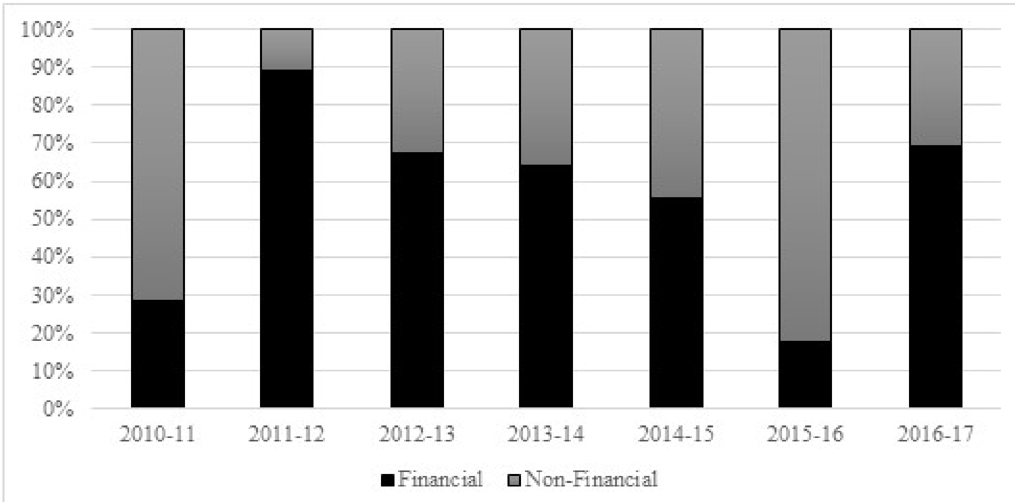
Table 6 Capital Issued By Non-government Public Limited Companies

	Total		New	
Year	No. of Issues	Volume (Rs. Billion)	No. of Issues	Volume (Rs. Billion)
1970	113	0.7	51	0.3
1980	237	1.6	141	0.6
1990-91	364	43.1	86	7.4
1991-92	514	61.9	94	9.4
1992-93	1040	198	188	33.1
1993-94	1133	193.3	244	55.8
1994-95	1678	264.2	368	64.6
1995-96	1663	160	577	31.2
1996-97	838	104.1	367	22.7
1997-98	102	31.4	27	6.8
1998-99	48	50.1	7	0.6
1999-00	79	51.5	10	2.2
2000-01	139	58.2	111	23.1
2001-02	19	56.9	4	0.9
2002-03	9	18.8	3	2.1
2003-04	38	37.2	9	13.8
2004-05	54	130.8	22	47.8
2005-06	131	211.5	77	102.6
2006-07	117	306	72	256.6
2007-08	115	636.4	80	370.9
2008-09	46	161.7	21	20.3
2009-10	71	279.8	36	144.8
2010-11	76	274.6	49	161.5
2011-12	63	156.8	33	57.8
2012-13	54	161	32	49.4
2013-14	70	116.8	38	12.4
2014-15	86	170.6	46	30.4
2015-16	96	267.2	73	142.6
2016-17	237	845.3	104	280.6
2017-18	221	729.5	192	465.9

Source: Calculated from RBI data.

that most of it went to the financial companies (Figure 8). The financial companies have a dominant share in the capital raised from the primary market.

Fig. 8 Capital Raised from Primary Market by Financial Vs Non-Financial Companies



Source: SEBI

Weak Domestic Bond Market

In a market driven financial system, the corporate bond market plays a critical role by providing long term finance to industry. In India, it was expected that market reform policies will lead to the creation of a vibrant domestic bond market. However, data suggests that the size of the corporate debt market in India is quite small (Table 7). Even the size of India's corporate debt market is smaller than several other developing economies like Brazil and China. And, it is too small in comparison to the markets of the advanced industrialized countries with dominance of banks like in Germany and Japan. Recent data suggest that the size of India's corporate bond market is as small as US$ 26.2 billion, vis-à-vis Brazil's US$ 214.8 billion and China's US$ 3024 billion.

Unequal Access: Distribution of Investible Funds

Bank credit and capital market are seen as the major sources of finance for the industrial sector in India. Data suggests, both forms of finance are not equally accessible to firms across regions and sectors, also in terms of location. Unequal distribution of credit and investible funds across different sectors and regions, and location are the dominant features of the financial system in the post liberalization period. The metropolitan area is the preferred destination for credit flow,

The metropolitan area is the preferred destination for credit flow, followed by urban and semi urban areas.

Table 7 Status of Bond Market (Amount Outstanding) as on December 2018 (US$ Billion)

Country	Government	Financial Institutions	Corporate issues	Total
Brazil	1469.3	564.1	214.8	2248.3
Canada	1278.2	1352.3	449.4	3079.9
China	4819.3	4853.4	3024	12696.7
France	2263	1607.9	676.2	4547.1
Germany	1812.9	1542.3	192.2	3547.4
India	857.6	19.2	26.2	905.7
Japan	9199.5	2608.8	688.2	12496.6
South Korea	626.1	672.1	589	1887.2
UK	2634.7	2597.5	510.8	5747.8
US	18680.4	16120.7	6283.9	41301.1

Source: Bank for International Settlement (BIS): Debt Securities Statistics.

followed by urban and semi urban areas. The flow of credit to metropolitan areas increased significantly from about 37 percent in 1990 to about 62 percent in 2017. Other locations – urban, semi urban and rural have witnessed reduced credit share over years, especially during the post liberalization period. It is abundantly clear that increasingly credit has been consolidated around the metropolitan region, thereby suggesting greater economic activity around it. This phenomenon suggest that lesser credit is available for the rural and semi rural areas, thereby squeezing the economic potentials of the region. From industrial finance perspective, while the above pattern of credit does look promising for firms and new industrial activities located in metropolitan areas, however, it gives a discouraging picture to the firms located or potential firms to be located in the rural and semi urban areas. It also deprives entrepreneurs, small industries and handicraft industries from having access to bank credit either for their expansion or a new start-up.

Recent data suggest that in 2018, the rural areas received only 1.9 percent of the total bank credit disbursed to the industrial sector in India (Table 8). Other areas like the Semi Urban and Urban areas have also recorded reduction in industrial credit share. On the other side, industrial credit has consolidated in favor of the metropolitan areas with about 79 percent share in industrial credit. Data suggest that there is increasing consolidation in favor of metropolitan areas and on the other side, parallel marginalization of the rural, semi urban areas.

Table 8 Population Group wise Bank Credit to Industrial Sector in India (%)

Population Group	2011	2012	2013	2014	2015	2016	2017	2018
Rural	3.9	2.6	2.5	1.6	1.8	1.9	1.9	1.9
Semi Urban	6.4	5.8	6.8	4.9	5.1	5.8	5.2	5.2
Urban	18.9	16.9	16.5	14.8	14.7	14.0	13.6	13.6
Metropolitan	70.8	74.7	74.1	78.7	78.4	78.3	79.3	79.3
Total	100	100	100	100	100	100	100	100

Source: RBI Basic Statistical Returns of Scheduled Commercial Banks in India, various issues

The regional distribution of bank credit suggest that it is concentrated in three regions – Western, Southern and the Northern (Table 9). These three regions received more than 80 percent of the bank credit in 2018. Regions which received lesser credit included the North-Eastern region, Eastern and Central regions.

Table 9 Region Wise Distribution of Bank Credit in India (%)

Region	2011	2012	2013	2014	2015	2016	2017	2018
Northern Region	23.42	23.39	23.28	23.17	23.94	22.91	22.76	22.82
North-eastern Region	0.77	0.77	0.76	0.75	0.8	0.87	0.96	1.02
Eastern Region	7.78	7.72	7.63	7.52	7.83	7.67	7.70	7.61
Central Region	7.04	7.1	7.39	7.67	8.49	8.66	8.80	8.94
Western Region	34.06	33.92	33.75	34.15	31.57	32.43	32.05	30.85
Southern Region	26.92	27.11	27.19	26.73	27.37	27.46	27.73	28.76
All India	100	100	100	100	100	100	100	100

Source: RBI Basic Statistical Returns of Scheduled Commercial Banks in India, various issues.

Along with unequal distribution of industrial credit across regions and locations, another emerging feature of the liberalization outcome is the consolidation of credit in favor of large loans (Table 10). Recent data shows that about 42 percent of the credit is large loans with credit size Rs. 25 crore and above. While on one hand, credit disbursed to small size loans has declined, except for Rs. 5 -10 lakh and Rs. Rs. 10-25 lakh loans; large size loans have increased on the other. It is also observed that some of the borrowers are moving up the ladder by larger credit size, however, data does suggest there is a consolidation in favor of big-sized loans. It suggests that small firms may find it increasingly difficult to access industrial credit.

Recent data shows that about 42 percent of the credit is large loans with credit size Rs. 25 crore and above.

As we have seen, it is not only distribution of bank credit which has become more unequal across regions and locations, capital raised from stock market too is found to be distributed unequally across sectors. The capital raised from the primary market is consolidated in favor of the banking and financial institutions (Fig. 9). This sector constituted more than 55 percent of the capital raised from primary market in 2017, thereby suggesting lesser volume of capital is available to the productive sector.

Summary & Conclusion

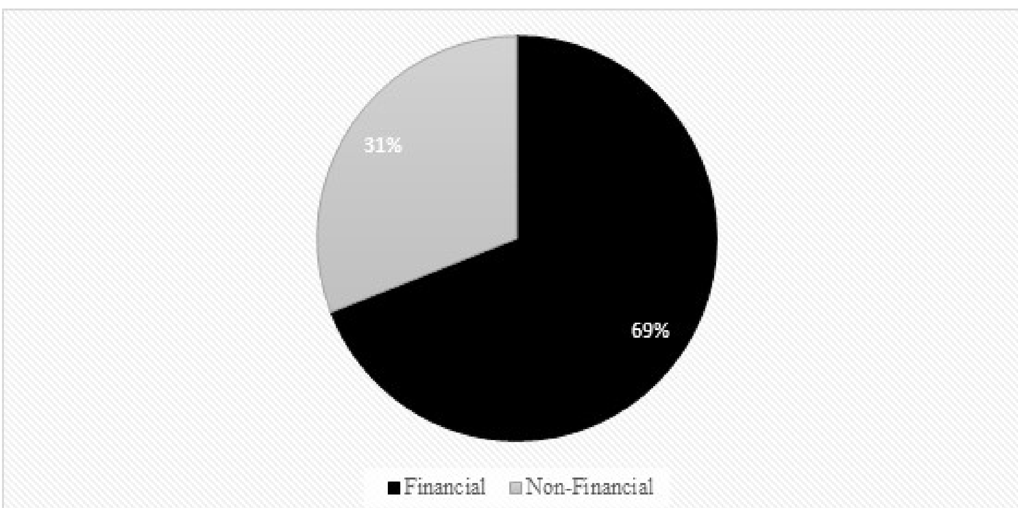
The study aims to explore the impact of financial liberalization on industrial development by analyzing the relationship between the financial structure and industrial structure and what it holds for industrial finance in India. The paper found that the institutions and agencies produced by financial liberalization is not in sync with the financial needs of the industrial sector in India. The structure of the newly emerged financial system

Table 10 Distribution of Credit as per Size (% of Total Credit)

Credit Size	1981	1995	2002	2018
Rs.25,000 and Less	17.8	16.2	5.87	0.50
Above Rs.25,000 and up to Rs.2 Lakh	11^	11.4	13.28	7.83
Above Rs.2 Lakh and up to Rs.5 Lakh	11.9&	5.2	6.66	7.97
Above Rs.5 Lakh and up to Rs.10 Lakh	5.1	3.3	3.47	6.60
Above Rs.10 Lakh and up to Rs.25 Lakh	7.8	4.9	3.77	8.32
Above Rs.25 Lakh and up to Rs.50 Lakh	7.2	5	3.2	6.00
Above Rs.50 Lakh and up to Rs.1 Crore	7.2	6.3	3.54	4.00
Above Rs.1 Crore and up to Rs.4 Crore	9.9	15.2	9.46	6.55
Above Rs.4 Crore and up to Rs.6 Crore	3.8	5.6	3.95	2.28
Above Rs.6 Crore and up to Rs.10 Crore	4.1	6.2	5.67	2.90
Above Rs.10 Crore and up to Rs.25 Crore	14#	20.9#	9.44	5.46
Above Rs.25 Crore			31.69	41.60

Note: # – above Rs 10 Crore; ^ – above Rs 25,000 and up to Rs 1 Lakh; &– above Rs 1 Lakh and up to Rs 5 Lakh
Source: RBI Basic Statistical Returns, various issues.

Fig. 9- Capital Raised from the Primary Market (%)



Source: SEBI Handbook of Statistics on Indian Securities Market, 2017

following financial liberalization while brought new opportunities in terms of access to finance for few industries (large firms); on the other hand, reduced the access to finance for several small and medium enterprises (SMEs). The SMEs were highly dependent on the DFIs as one of the key accessible sources of finance, which is no longer available to them (currently there are few operational DFIs). While the large firms now could borrow from both internal and external sources with low interest cost, the SMEs are increasingly financially constrained.

The post reform financial structure tends to benefit the large firms, thereby making the small and medium ones disadvantaged.

The cost of capital is still very high for small loans vis-a-vis large loans. On one hand, liberalization has not succeeded in addressing the issue of availability and access to affordable finance as argued; on the other side, the post reform financial structure tends to benefit the large firms, thereby making the small and medium ones disadvantaged. The seemingly failure of liberalization in creating a robust corporate debt market also is a cause of concern as it was visualized and argued as a substitution for DFIs as a source of long- term finance. Given the critical role of term finance for industrial development and absence of a robust corporate bond market almost after three decades of reforms, there is a greater role of specialized term lending institutions. In the absence of any robust source for long-term finance, commercial banks are burdened up with the responsibility of funding some of the large industrial projects. It is also a fact that commercial banks are supposed to fund only working capital needs of the industrial sector. Therefore, given the dynamic role the DFIs can potentially paly in industrial development, there should be a rethink in our policy towards DFIs. Globally, the specialized financial institutions have played important role in economic development in general, industrial development in particular.

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