UNIT 10 NON-BANK FINANCIAL INTERMEDIATION—AN OVERVIEW

Structure

10.0 OBJECTIVES

After studying this unit, you should be able to:

- explain the meaning of financial intermediation
- describe the role of non-bank financial intermediaries
- identify various types of non-bank financial intermediaries in India
- describe the importance and role of Life Insurance Corporation of India, Gederal Insurance Companies and Unit Trust of India as non-banking financial intermediaries.

10.1 INTRODUCTION

In the previous block you have studied the theory and practice of commercial banking. You have also learnt about the role of various banking institutions particularly the commercial banks and the central bank in the economic development of a country.

In this unit you will study the role of various non-bank financial instilutions including the Life Insurance Corporation of India, General Insurance Companies and the Unit Trust of India. Before taking up a detailed discussion of these institutions, it is necessary to know the meaning of financial intermediation and the manner in which non-bank financial intermediaries differ from the financial intermediaries, viz., commercial banks.

10.2 NON-BANK FINANCIAL INTERMEDIATION

10.2.1 What is Nan-bank Financial Intermediation?

Financial intermediation is the modern term used for 'Financial Institutions'. The financial intermediaries act as mediators to bring together the savers and users of capital. They mobilise money from the savers by selling securities to them, and lend the same to the borrowers. Broadly, the term financial intermediaries can be applied to a variety of institutions, some of which are listed below:

- Commercial Banks
- Insurance Companies
- Provident Fund Organisations

- Investment Companies.
- Special Financial Companies
- Share Brokers and Dealers
- Hire Purchase Finance Companies
- Chit Fund Companies

Of these institutions, the commercial banks come under the category of bank financial intermediaries, since they mobilise money from the public and pay them on demand. They lend money to individuals as well as business firms mainly on short-term basis. Generally, commercial banks do not directly participate or undertake promotional activities for the development of business or industry.

On the other hand, the non-bank financial institutions, acting as financial intermediaries, mobilise savings from the public and lend the same to business firms. All the other institutions specified above, other than commercial banks, are non-bank financial intermediaries.

The following are the differences between the bank and non-bank financial intermediaries.

1) The banking institutions mobilise demand deposits and other deposits from the public and pay the same on demand to the customers. Non-bank financial institutions generally pay back the money taken from the public only after a specified time.
2) The banking institutions generally provide loans to individuals as well as business firms mainly on short-term basis. Non-banking financial institutions lend funds mainly on term basis to business firms only. They also subscribe for the shares and debentures of industrial concerns.
3) The commercial banks do not directly participate in the promotional activities in general. The non-bank institutions, on the other hand, undertake many promotional activities for the rapid industrial development of the country.
4) All the banking institutions in the country are in the organised sector. The Banking Companies (Regulation) Act, 1949 is applicable to all banking institutions. The non-bank financial intermediaries, on the other hand, come under the categories of both organised and un-organised sectors.

10.2.2 Role of Non-bank Financial Intermediaries

The non-bank financial institutions acting as intermediaries play a crucial role in bringing together the savers and the borrowers. The intermediation process of these institutions helps the individuals to invest their funds safely and enables business firms to borrow funds without problems.

For instance, an automobile manufacturing firm wants to borrow Rs. 100 crore. In the absence of financial intermediaries it has to seek out individuals who would lend that amount, which is a very difficult problem. In the same way assume that you have a sum of Rs. 1,000 to lend. How would you, as an individual, find a borrower who needs an amount of Rs. 1,000 only. It is in this context that the financial institutions come into the picture. They solve the problem by providing benefit to all'the parties involved. They serve as intermediaries between the savers (by pooling' their funds) and the users (by lending them the money thus pooled). In addition to this the pooling of funds provides certain administrative economies of scale.

Acting as intermediaries, the non-bank financial institutions help the individuals, business firms and the nation as a whole in the following ways:

1) The non-bank financial institutions help the individual investors by providing them triple benefits viz., low risk, steady return and capital appreciation.
2) They help the business firms in securing funds at reasonable cost and in time. They take the risk of mobilising savings from numerous small investors. The business firms are, thus, relieved of the problem of approaching small investors scattered throughout the country.
3) The non-bank financial institutions also help the different sectors of the economy according to the priorities fixed by the Government from time to time.
4) By providing financial help on softer terms to the enterprises set up in backward areas, these institutions help in correcting regional imbalances in the country.
5) When the programmes of rapid industrialisation get bogged down due to the inadequacy of finance. these non-bank financial institutions render valuable

assistance in the form of loans, underwriting services or direct subscription of shares and debentures.

6) They provide technical, financial and managerial assistance to entrepreneurs. These institutions undertake various promotional activities such as the formation of project ideas, conducting viability studies, the implementation of the projects, etc. Thus, financial institutions play a very crucial role in accelerating the pace of industrial development.

10.2.3 Types of *Non-bank Financial Intermediaries*

On the basis of the functions they perform, these non-bank financial institutions are classified broadly into the following three categories :

1) Investment Trusts : These institutions are also known as investment banks. They mobilise the savings of scattered masses and channelise them to productive uses. They invest their excess money in various securities in addition to the provision of long-term loans. They also undertake merchant banking activities including underwriting of securities. This type of institutions include the Life Insurance Corporation of India. (LIC), General Insurance Corporation of India (GICI) and the Unit Trust of India (UTI).

2) Development **Banks** : These institutions are also known as special Financial Institutions. They provide long-term financial assistance to industrial undertaking in various forms. Since they also undertake many promotional functions, they are known as development banks. These institutions include Industrial Finance Corporation of India (IFCI). Industrial Credit and Investment Corporation of India (ICICI) and Industrial Development Bank of India (IDBI) at national level while the State Financial Corporations (SFCs) and State Industrial Development Corporations (SIDCs) exist at the State level.

3) Other Institutions : Generally some institutions do not provide financial assistance. They mainly undertake promotional activities and provide various services to entrepreneurs. These institutions include National Small Industries Development Corporation (NSIC), State Small Industries Development Corporations (SSIDCs) and Technical Consultancy Organisations (TCOs).

.We first discuss the role of investment trusts in this unit, followed by all India level term-lending'financial institutions'in Unit 11 and state level term-lending financial institutions in Unit 12.

Check Your **Progress A**

1) Non-bank institutions are broadly of three kinds. What are they?

....

....

2) Which of the following statements are True and which are False ?
   i) Financial intermediaries bring together the demanders and suppliers of capital.
   ii) Non-bank institutions lend money to individuals and business firms.
   iii) Banking institutions provide funds mainly on long-term basis, while non-banking institutions look after the short-term loans.
   iv) To entrepreneurs in backward areas the non-bank institutions provide financial help at easy terms.
   v) State Small Industries Development Corporations mainly provide consultancy and other such services to the entrepreneurs.

10.3 LIFE INSURANCE CORPORATION OF INDIA (LIC)

The Life Insurance Corporation of India (LIC) was constituted under the LIC Act, 1956 as a wholly-owned gavernment corporation by nationalising 244 private companies operating from 97 centres in India. The main objective behind the establishment of this corporation was to carry on the business of life insurance to the best advantage of the community and to channelise the funds into investment in accardance with plan priorities.

Objectives

The following are the specific objectives of the corporation:

1) Spreading the gospel of life insurance as far and wide as possible, reaching out beyond the more advanced urban areas into the previously neglected rural areas;
2) Affording life insurance protection to every eligible man and woman in the country through insurance schemes suited to different sections of the community;
3) Mobilising public savings or effectively for nation building activities;
4) Providing complete security and prompt and efficient service to the policy-holders at economical rates.
5) Conducting its business with the utmost economy and with the full realisation, that the money belongs to the policy-holders, investing the funds in such a way as to secure maximum yield consistent with the safety of capital;
6) Developing a dynamic and vigorous organisation under a management conducted in a spirit of trusteeship.

Resources

When the LIC was nationalised, an initial capital of Rs. 50 crore was provided by the Government of India. Premiums paid by the policy holders are the principal source of funds of the LIC. Besides, the LIC receives interest, dividends, repayments and redemptions which add upto its investible resources.

Investment **Policy**

The Corporation is essentially an investment institution. Its investment policy has been designed taking into account the cardinal principles of safety of the principal amount. Diversification of funds in terms of various types of securities, number and types of enterprises, maturity and regions. The corporation is supposed to function on business principles and its investment policy is guided by the consideration of the interest of its policy-holders unless it is in the larger interest of the country..

The pattern of investment policy of the LIC until recently was governed by Section 27A of the Insurance Act, 1938 which was amended in April 1975. The following are the general guidelines relating to the investment policy of LIC:

1) The keynote of the corporation's investment policy is that it should invest its funds in such a manner as to safeguard and promote, to the maximum extent possible, the interest of the policy holders. The larger interest of the. country should not however be ignored.
2) Investment should be dispersed over different classes of securities, industries and regions. The Corporation's policy has been not to acquire more than 30% of the outstanding equity shares of a company.
3) The corporation should act purely as an investor. It should not assume the role of an operator or speculator in order to take advantage of temporary fluctuations in the market prices of securities.
4) The Corporation should underwrite security issues after a careful investigation of the project from financial, economic, technical, managerial and social angles.
5) The Corporation should review its investment portfolio from time to time and make such changes in its composition as may be warranted under the circumstances.
6) The Corporation should not acquire control of or participate in the management of any concern in which it has an interest as an investor, unless exceptional circumstances warrant such participation.

Investment Pattern

The'aggregate investible funds of LIC, comprising life insurance business and capital redemption insurance business increased from Rs. 17,318 crore in 1988 to Rs. 20,428 crore as at the end of March, 1989. Thus, in the year 1988-89 it recorded a rise of 18%. compared to 15.7% and 14.1% in the preceding two years.

Total outstanding investments of LIC (in Government and other approved securities, infrastructure facilities, assistance to industry, housing etc.) in March, 1989 aggregated to Rs. 18,702.3 crore, recording an increase of 17.2% over, that in the previous year. In March 1989 LIC's investments in Government and other approved securities and its direct assistance to industry constituted 49.2% and 13.2% of LIC's total investments.

The Corporation is authorised to assist the public sector undertakings and public limited companies by way of investment in their securities. The LIC subscribes to the share capital of companies, both preference and equity and also to bonds and debentures. It underwrites shares and debenrures but it does not guarantee deferred payments or loans as in the case of other financial institutions.

As shown in Table 10.1, LIC's direct assistance, to industry hy way of loans and underwriting direct subscriptions to shares and debentures sharply rose from Rs. 362.7 crore in 1987-88 to Rs. 660.2 crore in 1988-89. Sanctions by way of term loans increased from Rs. 127.2 crore in 1987-88 to Rs. 325.7 crore in 1988-89. Assistance sanctioned by way of underwriting/direct subscriptions increased by 42% during 1988-89 as against a decline of 20.6% registered in the previous year. Disbursement of direct assistance to industry, which had registered a decline (Rs. 342.3 crore) in the previous year, recorded an increase (Rs. 442 crore) during.1988-89.

Table 10.1 Assistance Sanctioned and Disbursed

(Rs. in crores)

Year	Sanctions	Growth Rate %	Disburse-ments	Growth Rate %
1964-65	15.0	—	11.5	—
1970-71	17.8	—	8.1	—
1971-72	23.1	29.8	5.3	(-) 34.6
1972-73	20.1	(-) 13.0	14.0	164.1
1973-74	25.9	28.9	20.0	42.9
1974-75	43.8	69.1	54.1	170.5
1975-76	61.0	39.3	27.5	(-) 49.2
1976-77	57.1	(-) 6.4	38.9	41.5
1977-78	52.7	(-) 7.7	42.8	10.0
1978-79	65.5	24.3	31.7	(-) 25.9
1979-80	80.0	22.1	70.9	123.7
1980-81	70.0	(-) 12.5	65.5	(-) 7.5
1981-82	165.5	136.4	135.9	107.2
1982-83	136.5	(-) 17.5	86.6	(-) 36.3
1983-84	166.8	22.2	140.9	62.7
1984-85	219.9	31.8	161.5	14.6
1985-86	383.6	74.4	261.9	62.2
1986-87	363.8	(-) 5.2	389.8	48.8
1987-88	362.7	(-) 0.3	342.3	(-) 12.2
1988-89	660.2	82.0	442.0	29.1
Cumulative upto March 1989	3067.7		2413.6	

Source: IDBI, Report on Development Banking in India 1988-89

Aggregated assistance sanctioned by LIC; upto March 1989, totalled to Rs. 3,067.7 crore comprising term loans of Rs. 1,370.9 crore (44.7%) and underwritingldirect subscriptions of Rs. 1,696.8 crore (55.3%). Likewise, term loans and. underwritingldirect subscriptions constituted 45.2% and 54.8% respectively of the cumulative assistance disbursed upto March, 1989.

The chemicals and chemical product industry accounted for the highest share of 33.1% of direct assistance-sanctioned to industries, followed by basic metals (25.6%), textiles (14.4%) and machinery (9.7%). Assistance to chemicals and Chemical products, which was around Rs. 75 crore during the last three years, shot up to Rs. 218.6 crore during the year 1988-89, recording a growth of nearly three times. Among other major industries, assistance to basic metals increased by over two times and to textiles by nearly three times.

Assistance to machinery and electrical machinery increased by 51.7% and 51.5% respectively while assistance to the electricity generation industry witnessed a marginal decline of 0.4% as compared to the previous year. A little over two-thirds of the cumulative sanctions upto March, 1989, was accounted for by five industries viz., chemicals and chemical products (20.5%), machinery (15.7%), textiles (14%), basic metals (11.1%) and electricity generation (8.1%).

Now let us see the state-wise direct assistance given by LIC. Kerala State recorded maximum growth of 26 times in assistance sanctioned and its share increased from 0.08% in 1987-88 to 1.2% during 1988-89. Rajasthan and Madhya Pradesh registered appreciable increase of about 15 and 11 times respectively in assistance sanctioned and their respective shares increased'to 5.7% and 10.2% during 1988-89 from 0.7% and 1.7% in 1987-88. Assistance to Goa rose by four times; while assistance to Assam and Orissa almost doubled. Andhra Pradesh received maximum assistance sanctioned by LIC at Rs. 184 crore followed by Gujarat (Rs. 166.2 crore) their respective shares increasing to 27.9% and 25.2% in 1988-89. Thus, sanctions to these two states alone constituted more than half the total assistance sanctioned by LIC during 1988-89.

Assistance sanctioned to Bihar and Tamil Nadu declined in 1988-89 compared with 1987-88. Since from the inception, Maharashtra accounted for the highest share in sanctions (22.2%), followed by Gujarat (17%), Andhra Pradesh (10.4%), and Tamil Nadu (8.5%). Similarly, in 1988-89 in cumulative disbursements also Maharashtra secured the first position with 20.7%, followed by Gujarat (15.7%), Andhra Pradesh (12%), Tamil Nadu (8.6%) and West Bengal (8.4%).

LIC's assistance to backward areas has not been substantial and it does not also grant loans on concessional terms. It, however, participates in extending assistance to such units on normal terms. LIC's sanctions to backward areas rose from Rs. 37.3 crore in 1987-88 to Rs. 71.6 crore in 1988-89. Of backward areas in total sanctions marginally improved to 10.8% during 1988-89 from 10.4% in 1987-88. Orissa, which had not received any assistance for its backward areas in 1987-88, was sanctioned Rs. 5.3 crore in 1988-89. Maharashtra received the maximum assistance of Rs. 22 crore, accounting for 30.7% share in the total assistance sanctioned to backward areas during 1988-89, followed by Gujarat (17.2%) and Tamil Nadu (11.2%).

If we analyse the sector-wise assistance, the Corporation invested major portion of its resources in public sector. The investment in public sector increased from Rs. 9,064 crore in 1986 to Rs. 14.032 crore in 1989 consisting of 80.9% of total invested funds. The investment in private corporate sector including joint sector accounted for 11.9% followed by cooperative sector 7.2%.

Evaluation **of** the Investment Policy

The LIC has achieved a major breakthrough in mobilising the savings of the people and building up a big reservoir for financing socio-economic schemes of national importance and the needs of public and private sector undertakings. The bulk of the corporation's investment is in the government securities and loans to socially oriented schemes and projects. Only a small proportion has gone to the financing of joint stock companies. Obviously, the public sector has claimed more than three-fourths of the Corporation's total assistance: while the balance (one-fourth) was shared by other sectors.

There has not been any significant diversification of the corporation's investment portfolio among different industries and regions. It has not extended its assistance to agricultural sector which is considered to be the backbone of Indian economy. A more realistic approach on the part of the LIC in investing its funds for industrial and agricultural sectors will help the country for a balanced economic growth in future.

The Corporation has been playing a pivotal role in the capital market since its formation. Although only a small share of the funds is used for financing the needs of private sector enterprises, the magnitude of the Corporation's resources is such that even this small proportion constitutes one of the largest single sources of industrial finance in the country.

In spite of its achievements, the investment policy of the Corporation has been the subject of controversy. It is said that LIC's contribution to the new industrial ventures is very limited. There is no doubt that the funds at the disposal of the Corporation arc the hard earned savings of the common man. So the corporation is not in a position take the risk of investing its funds in new industrial ventures. However, the LIC can help them by forming underwriting consortiums with other credit institutions and by purchasing liberally the securities, shares and debentures of other financial institutions. It is said that the LIC has not played any significant role in social development projects like housing, drainage, water supply and other basic amenities.

Thus, the LIC occupies a unique position among the various financial institutions that constitute the Indian Capital Market. Because of its handling huge funds, the decisions of the Life Insurance Corporation exercise a decisive influence on the capital market, whether they relate to government bonds, industrial securities, or real estate.

10.4 GENERAL INSURANCE COMPANIES

The Government of India nationalised general insurance companies in India by taking over 107 general insurance companies. For managing these companies, it established General Insurance Corporation of India in 1973. The General Insurance Corporation of India (GICI) is a holding company having the following four subsidiaries.

1) National Insurance Company Ltd.
2) New India Assurance Company Ltd.
3) Oriental Fire and General Insurance Company Ltd.
4) United India Insurance Company Ltd.

Management

Management of the Corporation is vested in the hands of Board of Directors consisting of one Chairman and nine Directors including two Managing Directors. The registered office of the Corporation is located in Bombay.

Investment Policy

The main objective of the GICI's investment policy is to invest funds in socially oriented sectors of the economy. Such investments include Central and State Government securities, bonds, and debentures of public sector undertakings and also loans on soft terms to State Governments and other agencies engaged in housing and urban development. In addition to this the Corporation helps the industrial units by providing direct and indirect assistance.

GICI's investments in 1989 amounted to Rs. 3,409 crore. The investments in shares, debentures and term loans of companies went up in absolute terms to Rs. 1,115 crore registering a growth of 16.2% over the previous year. Study Table 10.2 carefully for the data relating to the financial assistance sanctions and disbursements by GICI and its subsidiaries.

As shown in Table 10.2, assistance sanctiqned by GICI and its four subsidiaries during the year 1988-89 to the industrial sector by way of term loans, underwriting/direct subscriptions to shares/debentures firm allotments and rights issue of sharesldebentures aggregated to Rs. 123 crore, recording an increase of 24.7% over the previous year.

Table 10.2 : Assistance Sanctioned and Disbursed

(Rs. in crores)

Year	Sanctions	Growth Rate %	Disburse-ments	Growth Rate %
1980-81	30.8	—	44.0	—
1981-82	50.1	62.7	33.7	(-) 23.4
1982-83	92.7	85.0	44.7	32.6
1983-84	108.5	17.0	84.5	89.0
1984-85	144.1	32.8	110.5	30.8
1985-86	153.0	6.2	107.3	(-) 2.9
1986-87	153.3	0.2	131.6	22.6
1987-88	98.3	(-) 35.9	103.5	(-) 21.4
1988-89	122.6	24.7	115.4	11.5
Cumulative upto March 1989	1097.3	—	857.9	

Source: IDBI, Report on Development Banking in India 1988-89

Industry-wise, fertiliser industry was the largest recipient of GICI's sanctions during the year, followed by textiles and machinery industries.

The analysis of GIC's state-wise assistance reveals that Maharashtra received major share during 1988-89 followed by Gujarat and Tamil Nadu. While coming to assistance to backward areas, in view of its primary concern for maintaining a sound and profitable investment portfolio, GIC has generally. refrained from participating in the grant of concessional assistance to backward areas.

On the whole GIC and its four subsidiaries are helping the nation in building a very. good base for the provision of general insurance facilities. While doing so it has been assisting the industrial sector financially in different ways. But it would be socially desirable if in future the GIC take more interest in providing finance for industries located in backward areas as instead of concentrating on the units located in industrially developed areas.

Check Your **Progress B**

1) In 1988-89 the LIC's share of investment to private corporate sector including the joint sector, the public sector and the cooperative sector were :
   i) private sector ....
   ii) public sector ....
   iii) cooperative sector. ....
2) State whether the following statements are **True** or **False.**
   i) The LIC is a holding company.
   ii) The LIC should invest in securities with an aim to speculate.
   iii) The interest, dividends, repayments and redemptions received by the LIC are a part of its investible resources.
   iv) The LIC must do a detailed scrutiny before underwriting a security issue.
   v) The LIC has treated both public and the private sector equally in its investment policy.

10.5 UNIT TRUST OF INDIA (UTI)

The Unit Trusts are quite popular in the western countries and they have made far greater progress than even genuine investment companies. This is particularly on account of certain advantages which the unit trusts enjoy over other forms of intermediation. The notable advantages of the unit trusts are:

1) Diversified portfolio or pooling of risks
2) Professional management
3) High degree of liquidity

A small investor on his own cannot avert risk if he directly makes investment in the shares and debentures of companies. With small resources to invest, he cannot have diversified portfolio. However, by making investment in the shares of unit trusts, risk is averted due to their investment policy. The unit trusts as a policy do not make concentrated investments in a few companies whatever be their financial position. In addition, they have the advantage of professional management. The redemption feature of units ensures high degree of liquidity. It is in fact this advantage which induces a large number of small savers to make investment in units.

Establishment of UTI : The importance of unit trusts in mobilising savings of small savers in India was recognised as early as 1931 by the Indian Central Banking Enquiry Committee. The need for setting up these trusts was stressed once again by the Shroff Committee in 1954. However, it was only in 1964 that the Unit Tryst of India was set up under the UTI Act, 1963. The UTI is an investment institution which offers the small investor a share in the India's industrial growth and productive investment with a minimum risk and reasonable returns.

The **Unit** Trust of India (UTI) is not a development bank. As the name itself suggests it is an investment trust. It falls in the category of financial institutions which collect savings of other economic units and lend them to those who wish to make productive use of them. Unit trust is comparable to Mutual Funds in the USA.

Objectives of UTI : The primary objective of UTI is to encourage and mobilise savings of the community. It channelises them into productive corporate investments so as to promote the growth and diversification of the country's economy. Specifically, the objectives of the Trust are the following:

i) It mobilises the savings of the community and channelises them into productive investment. By promising savers the triple benefits of safety, liquidity and profitability of their investments, the Trust encourages individuals to save.
ii) It gives every one a chance to indirectly own shares and securities in a large number of select companies and enables the investors to share in the widening prosperity consequent on industrial growth.

Resources

Initial Capital : The initial capital of the UTI was statutorily fixed at Rs. 5 crore. It was to be contributed by the Reserve Bank of India (Rs. 2.5 crore), the Life insurance Corporation of India (Rs. 0.75 crore), the State Rank of India and its subsidiaries (Rs. *0.75* crore) and other financial institutions including banks (Rs. 1.0 crore). In 1976 the initial capital held by the Reserve Bank of India was transferred to the IDBI and thus the UTI became an associate institution of the latter.

Unit **Capital** : The main source of the funds of the UTI is the unit capital which is raised from the sale of units to public under various schemes. The bulk of the funds obtained in this form are under the Unit Scheme, 1964 and Capital Gains Units Scheme, 1983. These two schemes presently account for more than two-thirds of the collections from the sale of units. The Unit Scheme, 1964 was the first scheme to be introduced by the UTI and has always been popular with the investors. The units sold under this scheme are of the face value of Rs. 10 each. However their market price is periodically determined and is higher than the face value. The basis for determining the market price of units under this scheme is the market valuation of the aggregate investments of the UTI over the previous period. The purchase price is kept lower than the sale price and between the two there has been always a margin of **30** paise or more.

Investment Policy : The investment policy of the UTI attempts to strike a balance between security of principal and return on capital. From the point of view of the security of capital, the securities in which investments are made must be of proven soundness and should be easily marketable. This implies that in the choice of securities safe andliquid securities should be preferred. Often these securities also ensure reasonable return on capital together with fair prospects of capital appreciation.

The UTI is not constrained like the LIC and banks to invest a certain proportion of its funds in government and other approved securities. It has the freedom to decide where it wants to invest its funds. However there are certain guidelines in this regard which suggest that the investment by the UTI in any one company should not exceed 5% of its (the UTI's) total investible funds or 15% of the value of the securities issued and outstanding of such a company. Moreover, investment in the initial issues of securities of new industrial undertakings should in any case be less than 5% of the UTI's total investible fund. The purpose of laying down these guiding principles for making investment by the UTI is to ensure that there is a reasonable amount of diversification of the investment portfolio.

Advantages to the Unit Molders

The investors derive the following advantages by investing in the units of Unit Trust of India.

1) Safety **of Investment** : The investment made in the units of UTI is quite safe. The UTI reinvests this money in wide range of securities covering risk and return. Hence the investors are assured safety for their investment.
2) Steady and Reasonable return on **Investment** : As per the statutory guidelines, the UTI has to distribute not less than 90% of its total income among the unit holders. It means that the unit holders are assured of a steady and reasonable rate of return on their investment.
3) Liquidity: The unit holders can easily convert their units into cash. The UTI repurchases the units anytime at the prices fixed by it. Further, the unit holders can transfer their units to third parties or can get loan from banks by putting units as security.

Working of UTI

The establishment of the UTI in 1964 may be said to be an important landmark in the development-of capital market in India. The Trust played a crucial role for increasing activity in new issues market and for the development of the secondary market for industrial securities in the country.

For the last 25 years, the UTI introduced many new schemes for channeling the savings of the people into productive sectors. The Trust so far introduced 22 schemes. All these schemes received tremendous response from public. Study Table 10.3 carefully for the highlights of the UTI's performance during the last five years.

Table 10.3 : Unit Trust of India – Growth in Perspective

(Rs. in crores)

Indicators	1984-85	1985-86	1986-87	1987-88	1988-89
1) Sales under all Schemes	756.19	891.75	1261.06	2059.42	3855.01
2) Unit Capital	1757.30	2586.39	3726.11	5449.58	8905.11
3) Unit-holding Accounts (in lakhs)	17.01	20.38	29.79	38.56	48.56
4) Investible Funds	2209.61	3218.34	4563.68	6738.81	11834.65
5) Reserves and Provisions	299.87	445.08	567.18	940.72	2075.10
6) Gross Income	257.05	389.97	524.58	840.90	1687.02
7) Gross Expenditure	11.77	15.39	22.21	41.36	64.03
8) Income Distribution	214.92	316.79	427.86	682.68	1246.46
9) Sanctions	357.30	696.60	465.00	1024.80	1973.10
10) Disbursements	236.20	528.90	417.60	749.20	1091.20

Source : Annual Report of UTI, 1988-89.

It can be observed from the table that the sale of units by UTI under all schemes scaled a new peak (Rs. 3,701 crore) during 1988-89 recording significant growth of 79.7% over the previous years (Rs. 2,059 crore). The UTI added 9:2 lakh unit holder accounts in 1988-89 as compared to 8.9 lakh in the previous year, reflecting the growing.popularity of-its schemes,.The total number of unit holder accounts as at the end of June, 1989 was 47.8 fakh.

Investible funds: The total investible funds of UTI as on June 30, 1989 crossed Rs. 10,000 crore-mark for the first time, increasing to Rs. 10,859 crore from Rs. 6,739 crore as at the end of June, 1988 and registered an increase of 61.1%. Investments in the corporate sector in terms of equity/preference shares and term loans registered significant growth rates of 87.1% and 93.4% respectively. The trust invested a major portion of its income in the privately placed debentures (Rs. 1,790 crore).

Industry-wise and state-wise assistance : As shown in Table 10.4 the miscellaneous industry continued to be a largest recipient of UTI's assistance in 1988-89. The industry accounted for the highest share of Rs. 1,114 crore of the total cumulative assistance of Rs. 5,203 crore since the inception of UTI upto the end of March, 1989. The other industries which received assistance from the trust include machinery (Rs. 828 crore), basic metals (Rs. 329 crore), electricity generation (Rs. 458 crore) and services (Rs. 643 crore).

Table 10.4 : Industry-wise Assistance Sanctioned

(Rs. in crores)

Industry	1986-87	1987-88	1988-89	Cumulative up to March, 1989
Textiles	66.7	59.9	90.0	448.0
Miscellaneous	78.1	298.9	387.5	1114.2
Chemicals, Basic Metal's	24.8	66.6	151.4	328.8
Machinery	50.1	29.8	336.3	828.3
Electricity Generation	39.1	150.0	170.3	458.6
Services	20.8	168.6	382.0	642.7
Total	465.0	1024.8	1973.1	5202.9

Source : IDBI, Report on Development Banking in India.

While coming to the state-wise assistance, as shown in Table 10.5, at the end of March, 1989 Maharashtra accounted for the highest share in assistance sanctioned (32.2%); followed by Uttar Pradesh (9.9%), Madhya Pradesh (9.5%), Gujarat (8.8%) and Andhra Pradesh (8.3%).

Table 10.5 : State-wise Assistance Sanctioned

(Rs. in crores)

State	1986-87	1987-88	1988-89	Cumulative up to March, 1989
Andhra Pradesh	10.9	31.1	314.0	432.9
Gujarat	47.9	90.1	137.2	458.4
Madhya Pradesh	1.2	161.2	241.5	492.2
Maharashtra	174.1	322.8	602.2	1675.3
Uttar Pradesh	39.8	134.9	255.1	513.1
Union Territories	24.9	22.8	136.8	244.5
	465.0	1024.8	1973.1	5202.9

Source: IDBI, Report on Development Banking in India, 1988-89.

During the year 1988-89, Public sector received Rs, 1,116 crore (56.6%) followed by Rs. 101 crore by the joint sector, Rs. 75 crore by the cooperative sector and Rs. 681 crore by the private sector.

On the other hand, the purpose wise assistance analysis reveals that the assistance sanctioned by the UTI to new projects registered almost four-fold increase to Rs. 233.4 crore from Rs. 62.7 crore in 1987-88, improving its share in total sanctions from 6.1% to 11.8% in 1988-89. Expansion/diversification schemes, which had received maximum assistance in the previous year, recorded a decline of 9.3% (Rs.416.6 crore) in 1988-89 their share in total sanctions also fell from 44.8% to 21.1%. Share of modernisation rehabilitation acquisition of balancing equipment, which was 10% in 1987-88, declined to 3.3% (Rs. 65 during the year under review).

Though the UTI has shown remarkable progress from year to year for the last 27 years, the performance of the Trust has been criticised due to the following reasons:

1) Bias towards developed states: One of the important criticism on the working of the trust is that it is showing more bias in investing its funds in industrially developed states instead of helping the backward regions. But this argument is not true as the UTI has to invest its funds in industrial securities taking into account safety of unit holders funds followed by the necessity to provide stable return to them.
2) Urban bias: Another criticism is that the Trust is concentrating its activities more in urban areas while the rural masses are denied the advantage of sharing the industrial prosperity of the country. In the recent past the trust is trying to mobilise even rural savings but still there is so much to be done in this respect. There is no denying the fact that the Trust has not been able to provide any savings schemes particularly suited to the needs of different types of investors from rural areas.
3) Conservative investment Policy : The Trust follows a conservative investment policy in deciding investment matters. More than half of its investments are in fixed income-bearing securities which offer very limited scope for capital appreciation, In future the trust needs to show more dynamism in this matter.
4) High maintenance expenditure : The maintenance expenditure of the Trust is increasing many fold from year to year. The expenditure is well over 10% of its income. Considering that the trust distributed 90% of its income among the unit holders, there is little amount left for investment or for adding to its reserves.
5) Return is not high : The rate of dividend given by the trust to its unit holders is not high. No doubt, it has gradually stepped up its dividend rate; but the dividend paid out by the UTI does not compare favourably with the return on equivalent risk investments in other companies. The trust might have attracted more savers if it had promised a competitive dividend rate.

6) **Future of UTI**: At present (31st March, 1989) the Trust has 48.56 lakh unit holders who are spread throughout the length and breadth of the country covering each nook and corner. It is hoped that the trust continues to experience rapid growth and is destined to make an important contribution to the Indian economy and in particular to the capital market. But its success in future depends upon its capacity in mobilising the rural savings and efficient service to the unit holders.

10.6 OTHER NON-BANKING FINANCIAL INSTITUTIONS IN INDIA

In addition to LIC, GIC, UTI there are a number of other non-banking financial institutions in India. They are:

1) Hire purchase finance Companies;
2) Investment Companies;
3) House Finance Companies;
4) Finance Corporations;
5) Mutual benefit Financial Companies; and
6) Chit Fund Companies etc.

These non-banking financial institutions are partly in organised sector and partly in unorganised sector. They may also be divided into non-banking financial companies and non-banking non-financial companies. While the former category includes hire purchase companies, investment companies, finance corporations, etc., the latter category covers all industrial and trading companies including companies which are non-financial and miscellaneous non-banking companies such as Chit Fund companies. These institutions solicit deposits both for short-term and medium-term from the public. Generally these institutions do not accept demand deposits.

The other non-banking financial institutions are also playing a crucial role in the economic development of the country. They are mobilising good amount of resources both from urban and rural savers. Though statistical data are not available, their contribution for economic development cannot be underestimated.

Owing to the absence of regulating mechanism by the RBI and other government agencies, they are able to exploit innocent public. They offer very high rates of interest and after grabbing good amount of money, they disappear from the scene making the investors to suffer.

It is high time that the RBI and government stopped the exploitation of hard earned sources by bringing these institutions under regulatory framework.

Check Your **Progress** C

1) What are the sources of investible funds of the UTI?

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2) State whether the following statements are True or False:
   i) The UTI is like mutual funds in Western countries.
   ii) The main source of funds of the UTI is the government.
   iii) The UTI tries to choose safe and liquid securities.
   iv) Till 1988-89, the UTI has introduced 12 different schemes.
   v) More than half of the investments of the UTI are in fixed income-bearing securities.

10.7 LET US SUM UP

Financial intermediaries bring together the suppliers and demanders of financial resources. These include commercial banks, investment trusts, insurance companies, share brokers, hire purchase companies, etc. Except commercial banks, all other institutions mentioned above fall under the category of non-bank financial institutions.

Non-bank financial institutions help the individual investors by providing them steady returns with capital appreciation. These institutions provide funds to business and industry in backward areas at softer terms and reasonal cost. Moreover, these non-bank financial institutions also provide technical and managerial consultancy.

The Life Insurance Corporation was constituted under the LIC Act, 1956 as a wholly-owned government organisation. Its main objectives include spreading the message of life insurance to every corner of India, to conduct the business of life insurance to the best advantage of the society and to channelise the accumulated public savings in accordance with the economic policy of the nation. While investing funds the LIC takes into account several considerations like safety of funds, diversification of investment portfolio, time of maturity of the securities, etc.

Since inception the investible funds of the LIC have been continuously growing. During 1988-89 it grew at 18% and stood at Rs. 20,428 crore. Out of its resources, maximum investment flows to the government and other approved securities — its share in the total investment being 49.2% in 1988-89. The chemicals and chemical product industry was sanctioned maximum direct assistance (33.1%) followed by basic metal (14.4%) and textiles (9.7%). During 1988-89, Andhra Pradesh and Gujarat together were sanctioned more than half of the total sanctioned investment.

The LIC has succeeded in mobilising large amounts of savings of the people, but it has not been successful in 'diversifying its investment protfolio, region-wise or industry-wise. Its contribution to new industrial ventures and to the agricultural sector is very limited.

GICI is a holding company with four subsidiaries. It invests funds in socially oriented sectors of the economy which include government securities, and agencies engaged in housing and urban activities. During 1988-89, fertiliser industry was sanctioned maximum funds, followed by textile industry. GICI has not provided any concessional financial assistance to backward areas. However, GICI has helped in building up a good network of general insurance facilities.

The UTI is an investment Trust set up in 1964. Its main objective is to channelise the surplus funds of the community into productive use so as to achieve growth and diversification of Indian economy. The investment policy of the UTI aims at striking a reasonable balance between security. and return on investment. Unlike the LIC and commercial banks, the UTI is not constrained to invest any proportion of its funds in government and other approved securities. The UTI has come up with many schemes over time to tap resources from every segment of society. Its investible funds have crossed Rs. 10,000 crore in 1989, It-has been observed that the UTI has preferred to invest its funds in developed areas. A criticism of the UTI is that a major part of investible funds have flowed into urban areas. For the UTI, there is definitely a need and scope for developing new schemes to mobilise rural savings and to indentify rural industries to get financial assistance. Further there is also scope to reduce expenditure of the UTI and raise dividend to unit holders.

10.8 KEY WORDS

Mutual Fund: A company without issued capital stock owned by those members that do business with it. The profits of a mutual fund (net of reserves) are shared by its members.

10.9 ANSWERS TO CHECK YOUR PROGRESS

A 1) Investment trusts; development banks; Other institutions mainly undertake promotional activities and provide services to entrepreneurs.
2) i) True ii) False iii) False iv) True v) True

B 1) i) 11.9% ii) 80.9% iii) 7.2%
2) i) False ii) False iii) True iv) True v) False vi) True

C 1) Initial capital, unit capital,
2) i) True ii) False iii) True iv) True v) False vi) True.

10.10 TERMINAL QUESTIONS

1) What is a non-bank financial intermediary? What are its features?
2) Discuss the role of the LIC in mobilising savings and helping in the fulfilment of national economic objectives.
3) The UTI has brought professionalism to the non-bank financial intermediation sector in India. Comment.
4) Write a short note on General Insurance Corporation of India.

Note: These questions will help you to understand the unit better. Try to write answers for them. But do not submit your answers to the University for assessment. These are for your practice only.