INTERNATIONALISATION OF INDIAN BUSINESS
—Role of Financial Institutions

R. C. SHAH

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Published by

THE A. D. SHROFF MEMORIAL TRUST
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(ii) Organising one or more memorial lectures annually on subjects which were of interest to the late Mr. A. D. Shroff, namely, banking, insurance, and industrial finance, the subjects to be chosen in rotation, and the lectures to be delivered by persons eminent in these fields.

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INTRODUCTION

The A. D. Shroff Memorial Trust arranges every year a public lecture to be delivered by distinguished speakers —by turn, on Banking, Insurance and Industrial Finance. These were the fields in which the late A. D. Shroff contributed so much to the country. The Trust has had eminent authorities to deliver the lectures on the three subjects which are of crucial importance to the economic well-being of the country.

In April 1983 we were fortunate to have Mr. R. C. Shah, Chairman of EXIM Bank and a distinguished banker, to deliver a lecture on "Internationalisation of Indian Business: Role of Financial Institutions". With his vast experience in the field of banking, he has dealt with the subject with keen insight and has made a number of most useful and pragmatic suggestions. The booklet would be of great value to policy-makers and those entrusted with the affairs of financial institutions in the country today.

The Board of Trustees has pleasure in publishing the text.

Bombay,
June 28, 1983.

N. A. PALKHIVALA
Chairman

A. D. SHROFF

(1899 - 1965)

A. D. Shroff's achievements in the field of business, industry and finance were many and varied. A large number of enterprises owe their origin and development to him. As an economist, his predictions have proved right over the years. Through the Forum of Free Enterprise, which he founded in 1956, as a non-political, educative organisation, he sought to educate the public on economic affairs. It was his firm conviction that a well-informed citizenry is the foundation of an enduring democracy.

George Woods, former President of the World Bank, paid the following tributes to A. D. Shroff :

> "In every age and in every society men must express anew their faith in the infinite possibilities of the human individual when he has freedom to develop his creative talents. For this is in large part how the message of freedom is passed from generation to generation. A. D. Shroff spoke eloquently in a great tradition, and thanks to him we can be sure that other great men of India will continue to speak this message in the unknown context of our future problems."

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INTERNATIONALISATION OF INDIAN BUSINESS — ROLE OF FINANCIAL INSTITUTIONS*

R. C. SHAH

Transition from A Closed Economy

India has grown as an open society. It has, however, until recent times, been a relatively closed economy. Having made these two statements, I propose to elaborate more in support of the second statement than the first. In an open society, members have the freedom to rise socially and occupy places of other members. This leads to a movement towards competition and striving for excellence. In the course of past three decades, we have witnessed this phenomenon occurring and enlarging. Open society is not my brief this evening. Hence, I should want to move to the second statement that India has been a relatively closed economy for good part of the past three decades. This has an important bearing with internationalisation of Indian business, which is my major theme, this evening.

Consider the ratio of imports to GNP and share of manufactured imports in total utilisation of manufactured goods. Both ratios have been lower than most developing countries and even compared to some

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*Text of the Annual Public Lecture delivered under the auspices of the A. D. Shroff Memorial Trust by the eminent banker, Mr. R. C. Shah, Chairman & Managing Director of EXIM Bank, in Bombay on 8th April 1983.

industrialised countries. This seeks to indicate the extent of self-sufficiency the country has achieved. This is the result of import-substitution policy followed for over three decades.

Import substitution has followed a dynamic path inasmuch as no sooner self-sufficiency was reached in one commodity, endeavour has been to achieve self-sufficiency in others. The First Plan sought to eliminate imports of consumer goods and the decade following 1956 witnessed an emphasis on the production of capital goods. This enabled Indian industry move up the technological ladder and altered the profile of the country's import basket. Whilst this has helped the growth of a diversified industrial structure, with strong sub-sectors that have competitive advantages in overseas markets, it has also led to a high cost production economy through sheltered markets. Suffice it to say, at this stage, that the policy of import substitution has contributed to a shift in the pattern of industrial production. Thus, consumer, intermediate and capital goods now contribute one-third each of value added.

There is a relationship between a country's development strategy and trade related issues. Criticism on India's development strategy has not been wanting. Be that as it may, it is supportable to argue that the development strategy so far followed has brought the economy to consider itself at a level of self-sufficiency, at a given level of technology. This also sets a base from which internationalisation of Indian business is possible. It is in this context that I have sought to

dwell, briefly, on some effects of national development policy, that have a bearing on our ability to internationalise Indian business.

At this stage of my presentation I should like to embark on a two-stage effort. The first stage involves projection of related data to support internationalisation of business that has already occurred and is occurring. The second stage involves an analysis of trends in Indian business internationalisation. Hope is that this effort will lead to intensive thought and work in the area of internationalisation of Indian business. In this context, this presentation is really a stage in 'work in progress'.

The related data, I have in view, comprise joint ventures abroad promoted by Indian business houses, project exports, and the growth of Indian bank branches abroad. Two features are common in respect of these three major forms reflected in current state of internationalisation of Indian business. First feature relates to the international dimension that Indian business had added to its business. Second feature is one of Indian technology that runs through joint ventures abroad, project and consultancy exports and Indian banks abroad.

Joint Ventures

It might be of some interest to outline the concept underlining joint ventures before looking at the achievements. The concept is about twelve years old in the Indian case. It was accepted as an export promotion strategy and hence found a place in the Export

Policy Resolution of 1970. From the national point of view, the concept springs from the need to play a part in international trade. From the international point of view, the concept responds to the need for inter-regional and intra-regional co-operation among the developing countries. I made bold to state, at the outset, that over the past three decades, India has built up expertise in intermediate technology which bears appropriateness of character for many developing economies. This places Indian business as an appropriate partner in the industrialisation efforts of developing countries. Joint ventures offer a medium for such partnership.

For India, joint ventures can contribute several advantages. First, through India's supply of capital goods and technology, a country image of beneficial value can be built up. Second, repeat orders for Indian goods can be created through joint ventures. Third, successful joint ventures can earn for India foreign exchange through dividends, technical fees and the like.

Joint ventures abroad is a form of overseas investment by India, in partnership with partners in host countries. Initial policy, that lasted till 1980, providing for Indian minority shareholding with equity contribution exclusively in the form of capital goods export has undergone some change. It is now possible for majority Indian equity participation and for some cash remittances.

Table I presents data on a number of approvals for joint ventures granted by the Indian Government,

Table II provides information on the regional pattern joint ventures have assumed. Table III highlights earnings from joint ventures.

TABLE I

Approvals of Joint Venture Proposals

Year	Number of approvals	Ventures in operation	Ventures abandoned/ not imple-mented	% of 4 to 2
Upto 1970	106	22	84	79
1971	18	5	13	72
1972	23	6	16	69
1973	15	6	9	60
1974	31	15	14	45
1975	34	15	17	50
1976	34	13	16	47
1977	49	19	16	33
1978	35	9	8	23
1979	28	6	2	8
1980 (Jan.-Aug.)	26	1	—	—
Total	399*	117	195	49

* As on end August 1980, out of 399 approvals, 87 Joint Ventures were under implementation.

Source : Indian Investment Centre.

TABLE II

Region-wise Investment in Indian Joint Ventures (Actual and proposed) (As on end August 1980)

(Rs. '000)

Region/Country	In operation		Under implementation	
	No. of JVs	Actual Indian Equity	No. of JVs	Approved Indian Equity
S.E. Asia				
1. Malaysia	29	124354	8	21421
2. Indonesia	10	62074	8	126773
3. Thailand	5	15377	4	64215
4. Singapore	9	11065	4	14200
5. Philippines	2	4498	2	8874
6. Fiji	1	1122	—	—
7. Hong Kong	1	258	2	375
8. Tonga	—	—	1	—
Sub-Total	57	218748	29	235858
South Asia				
1. Sri Lanka	3	893	5	39689
2. Nepal	1	1462	6	44878
3. Bangladesh	—	—	1	1800
Sub-Total	4	2355	12	86367
West Asia				
1. U.A.E.	9	4499	5	8395
2. Oman	3	1184	2	21966
3. Saudi Arabia	2	1040	5	11907
4. Iran	1	710	—	—
5. Kuwait	1	147	—	—
6. Bahrain	1	110	—	—
7. Qatar	—	—	1	431
Sub-Total	17	7690	13	42699

TABLE II—(*Contd.*)

(Rs. '000)

Region/Country	In operation		Under implementation	
	No. of JVs	Actual Indian Equity	No. of JVs	Approved Indian Equity
Africa				
1. Kenya	10	94095	4	5025
2. Nigeria	5	12688	8	120974
3. Mauritius	7	10231	1	1340
4. Uganda	1	2807	—	—
5. Zambia	1	1906	1	3000
6. Liberia	—	—	1	6800
7. Seychelles	—	—	1	6750
8. Libya	—	—	1	1000
9. Botswana	—	—	1	500
Sub-Total	24	121727	18	145389
Europe, America and Australia				
1. U.K.	5	177	4	578
2. France	1	262	—	—
3. West Germany	1	3800	1	430
4. Netherlands	1	375	—	—
5. Switzerland	—	—	1	45
6. Greece	—	—	1	8874
7. Cyprus	—	—	1	2926
8. Yugoslavia	—	—	1	19200
9. Canada	1	838	—	—
10. U.S.A.	5	483	6	26995
11. Australia	1	685	—	—
Sub-Total	15	6620	15	59048
Grand Total	117	357140	87	569361

Source : Indian Investment Centre.

TABLE III

Earnings from Joint Ventures

(in Rs. three zeroes omitted)

Year	Exports towards equity	Dividends	Other repatriations	Additional exports
Upto 1970	30200	4300	4200	39200
1970-71	6200	500	1100	4400
1971-72	12300	1000	1300	10100
1972-73	12800	1700	1600	13300
1973-74	21800	2500	2200	42100
1974-75	23900	3400	2900	73600
1975-76	30100	2600	13000	97800
1976-77	34200	3900	12900	104700
1977-78	24500	5300	19600	157900
1978-79	17300	5400	21800	151400
1979-80	28800	5500	27000	163600
1980-81	13700	N.A.	N.A.	3600
Total	255800	36100	107600	861700

Source : EXIM Bank of India compilation.

A study of data reveals several interesting features. First, concentration of Indian joint ventures has been in English-speaking areas and mostly in neighbouring countries of South East Asia and Africa. Second, size of units has been rather small. This is especially evident when you consider that in 1978-79, sixty units accounted for sales turnover of only Rupees 2.92 billion. Low scale of operations tend to keep the production cost high and leads to low profitability. Third,

textiles, paper and pulp, engineering and palm oil processing accounted for nearly eighty per cent of investment in joint ventures. Fourth, the Indian business houses that are front runners in joint ventures are the Birla group of companies, the Tata group, the J.K. group, the Thapar group, Shahibag enterprises, the Sarabhai group, the Kirloskar group. These groups are large, diversified industrial houses within India. In recent times, other large enterprises have been entering the field.

Data appears to suggest that exports towards equity made upto 1981, amounted to Rs. 256 million. This appears to have been recouped through cumulative dividends of about Rs. 40 million, other repatriations of about Rs. 110 million and additional exports of about Rs. 860 million. In other words, there has been net inflow into the country of Rs. 754 million. It is nevertheless true that there is growing sickness amongst Indian joint ventures abroad. I have to offer four comments on the causes. First, in many cases, choice of the local partner has been inappropriate. Wherever the local partner has been one of local importance and financially strong, joint ventures are able to weather difficult economic patches. It has to be recognised that the local partner provides the bridge between the Indian company and host country environment. Such a partner has to have considerable image and capacity of influence in host country. Wherever this has been present, joint ventures have done well. Second, Indian companies generally take up production of products abroad without much product adaptation to reflect needs of host countries. It is con-

ceivable that where Indian joint ventures have been able to mix Indian technology with some foreign technology, the result has been more marketable. Third, the lack of a brand name is a severe handicap in foreign markets. Many joint ventures are set up on the assumption that protection by way of tariff and import restrictions would be made available by the host country. When this does not occur, or such protection is withdrawn, in the absence of brand name for their products and presumably, international quality, products of such joint ventures are unable to sell against international competition. Fourth, most joint ventures begin on a thin funds base. Soon enough, they are cash starved and at best raise long term debt to meet the situation. The interest burden assumes disproportionate proportion in total cost and often causes cost overruns in project implementation. The resultant debt, premature repatriation of technical fees, royalties, etc., also contribute to cash starvation in projects.

This analysis suggests some policy as well as practice changes. In the area of policy designs, six suggestions appear to be in order. First, before a joint venture is approved, commercial viability and adequate financing arrangements should be allowed for. Where cash injection is required, export of Indian capital goods may not be the answer. Second, in approving a joint venture proposal, it should be reckoned that additional equity contribution in cash might be necessary and a margin needs to be provided for, *ab initio*. This will avoid costly delays caused by sanctions from several agencies at a later stage. Third, fiscal incentives appear necessary in order that earnings from joint

ventures are increasingly repatriated to India. What might be lost in exchequer revenue could well be made up by increased accrual in foreign exchange. Fourth, flexibility needs to be provided such that dividends, royalty, etc., can be ploughed back into a joint venture until it comes out of gestation period. Fifth, joint ventures that have turned sick, need to be rehabilitated through a consortium effort of Indian banks and industry. Sixth, best personnel is not allocated by Indian companies to their joint ventures. This leads to poor management and increase in mortality prospects of joint ventures. In the area of practice, Indian companies could profit by improved product and country identification, without working on the assumption of availability of protected markets in host countries.

Whilst there is recognition that joint ventures represent outposts of Indian technology abroad, there does seem to be a need for more will to lay down the investment required to make such outposts successful. Experience suggests that Indian joint ventures can become a spring board for transnationalisation of Indian business.

Project Exports

Joint ventures constitute one group of technology export. The other group is export of projects. This refers to export of industrial plants including related services involved in design, installation and commissioning. Such exports are also described as turnkey plant exports. I propose to address three questions here. What has been the size of project exports. What has been the direction of such exports. What has been

the industrywise distribution of project exports. The cumulative value of export of capital goods and industrial projects between 1973 to 1981 is in the region of Rs. 16 billion. Major share of projects has been accounted by electricity generation, followed by electricity distribution. It would appear that power generation has been a successful area for the public sector. Major share of power distribution projects has been with private sector companies. Cement, sugar, machine tools, textile, paper and pulp are other areas where India has been able to make turnkey project exports. In terms of destination of industrial projects, the pattern is interesting to observe — Middle East accounts for the major share of power related projects. In general, project exports have gone to oil economies in Middle East, followed by South-East Asia and Africa.

Export of capital goods and project exports is a phenomenon of 1970's. Such exports have grown in 1981 to account for nearly forty per cent of total engineering exports. This achievement is largely the result of India's expertise and availability of skilled workers in what is known as intermediate technology. Prospects of growth in exports of capital goods and industrial projects appear bright. It must, however, be stated that such prospects will not automatically materialise unless conscious and disciplined steps are adopted to seize opportunities. One estimate has been that by 1990, India would be able to reach project and capital goods export level of Rs. 160 billion. Another area of expansion has been construction contracts overseas. Total value of such contracts, in 1981, was in the region of Rs. 35 billion. Geographical concentra-

tion of these contracts has been in oil economies in Middle East.

I shall now dwell on some features of construction contracts and project exports. Construction contracts are characterised by very small export of goods from India. They do involve export of skilled and unskilled manpower, which is a source of foreign exchange earnings through increased remittances. Construction equipment and materials need to be bought from developed countries. Whilst this is a source of weakness in value of such contracts to India, it can also be recognised as an opportunity for India. The opportunity lies in Indian upgradation of construction equipment to meet needs of construction projects abroad. Similarly, it should be possible to produce construction materials, to an extent for overseas projects contracted. Again, in the case of project exports, about twenty per cent of equipment has to be acquired abroad. Project exports, however, carry a considerable value through supply of Indian equipment. If project exports are to contribute more foreign exchange earnings for India, quantum of foreign equipment will need to be reduced. Whilst in the case of joint ventures, Indian equity contribution is through supply of Indian capital goods, the character of construction contracts and project exports is somewhat different. Moreover, the financial pattern, organizational skills and type of personnel required for project exports are also of a different order compared to joint ventures. What is common between them is that joint ventures as well as project exports represent export of Indian technology and stand for internationalisation of Indian business. Such exports form a base for further internationalisation of Indian business.

Suffice it to mention at this stage that Indian experience in construction contracts and project exports can be more successful and advantageous to the country when a consortium approach in bidding is adopted, increased expertise is developed in costing when bids are made, and enlarged use of Indian equipment, materials enter into projects. There is also a need for greater rigour of tests before a company is allowed to undertake a project overseas. Its track record and financial viability are both important. Otherwise, enormous financial losses can occur for the country as penalties for delayed implementation of projects can be considerable. In order that public profit and private gain converge, project exporters will need to accept greater financial as well as organisational discipline. Experience in this regard, of the past decade, has been uneven. It, however, serves to provide a powerful spring board for predictable success in this decade.

Indian Banks Abroad

I have so far discussed the growth of joint ventures, project exports that reflect internationalisation of Indian business. These are illustrations in production area. In the area of services, hotels, airlines, shipping, insurance and banking, constitute a major grouping. I propose to concentrate on the growth of Indian banks' representation overseas as the third feature of internationalisation of Indian business. No developing country has an international banking network that India has developed over the past three decades.

Table IV presents data on the geographical distribution of Indian bank offices abroad. As at the end of June 1982, twelve Indian banks had 137 offices spanning 25 foreign countries. In this context it could be said that many Indian banks operate transnationally. A bank that conducts banking operations in many different countries and national systems alone could make a claim to being transnational. In this specific sense, three Indian banks could be described as transnational viz. State Bank of India, Bank of Baroda and Bank of India. It is of some interest to note the geographical spread of these banks between offshore centres, developed countries and developing countries:

	Offshore Centres	Developed Countries	Developing Countries	Total
State Bank of India	4	15	4	23
Bank of Baroda	2	17	38	57
Bank of India	2	20	2	24

It is evident that barring offices in developed countries, there has not been congruent networks of Indian bank branches in developing countries. Motivation for expansion abroad as well as pattern of business in the case of these three banks have been somewhat different. Growth of Bank of Baroda and Bank of India branches largely occurred in the late 1950s. This growth occurred where ethnic group provided business opportunities. The character of business has been retail. In the 1970s, Indian banks followed the direc-

TABLE

Offices of Indian Scheduled

(as at end

Country	State Bank of India	Central Bank of India	Bank of India	Bank of Baroda	United Commercial Bank
	1	2	3	4	5
1. Bahamas	1	—	—	1	—
2. Bahrain	1	—	—	1	—
3. Bangladesh	1	—	—	—	—
4. Belgium	—	—	—	1	—
5. Cayman Islands	1	—	1	—	—
6. Channel Islands	—	—	1	—	—
7. Fiji Islands	—	—	—	11	—
8. France	1	—	1	—	—
9. Guyana	—	—	—	2	—
10. Hong Kong	1	—	2	—	4
11. Japan	1	—	2	—	—
12. Kenya	—	—	2	7	—
13. Maldive Islands	1	—	—	—	—
14. Mauritius	—	—	—	6	—
15. Oman	—	—	—	3	—
16. Panama	1	—	—	—	—
17. Seychelles	—	—	—	1	—
18. Singapore	1	—	1	—	3
19. South Korea	—	—	—	—	—
20. Sri Lanka	2	—	—	—	—
21. Thailand	—	—	—	—	—
22. United Arab Emirates	—	—	—	8	—
23. United Kingdom	6	3	12	15	2
24. United States of America	4	—	2	1	—
25. West Germany	1	—	—	—	—
Total :	23	3	24	57	9

Source : Department of Banking Operations & Development, RBI.

IV

Commercial Banks outside India

of June 1982)

Indian Overseas Bank	Indian Bank	Syndicate Bank	Punjab National Bank	Bharat Overseas Bank Ltd.	Punjab & Sind Bank	Union Bank of India	Total
6	7	8	9	10	11	12	13
—	—	—	—	—	—	—	2
—	—	—	—	—	—	—	2
—	—	—	—	—	—	—	1
—	—	—	—	—	—	—	1
—	—	—	—	—	—	—	2
—	—	—	—	—	—	—	1
—	—	—	—	—	—	—	11
—	—	—	—	—	—	—	2
—	—	—	—	—	—	—	2
7	—	—	—	—	—	—	14
—	—	—	—	—	—	—	3
—	—	—	—	—	—	—	9
—	—	—	—	—	—	—	1
—	—	—	—	—	—	—	6
—	—	—	—	—	—	—	3
—	—	—	—	—	—	—	1
—	—	—	—	—	—	—	1
1	1	—	—	—	—	—	7
1	—	—	—	—	—	—	1
2	2	—	—	—	—	—	6
—	—	—	—	1	—	—	1
—	—	—	—	—	—	—	8
—	—	1	3	—	1	1	44
—	—	—	—	—	—	—	7
—	—	—	—	—	—	—	1
1	3	1	3	1	1	1	137

tion of India's foreign trade. State Bank of India appears to have more actively predicted its growth of overseas branches on this trend. In both cases, Indian banks have had to set up branches in offshore centres and international money centres to cater to needs of branches in developed and developing countries. Past three decades' experience of overseas branches has been successful both in terms of profits remitted into India and resources mobilised abroad.

It cannot, however, be claimed that the international dimension that Indian banks have acquired has invested them with the true character of transnational banks. Following are some observations on the working of Indian banks overseas. First, unlike transnational banks, Indian banks overseas have been very largely bypassed in the recycling process of petro dollars. Given the thin capital base of the parent banks, overseas branches of Indian banks have not been able to attract petro dollars. Second, they have had to continue addressing retail business in host countries and servicing business emanating from India. By and large, given resources base, home office technology and expertise, they have followed a low risk, low yield strategy. This has prevented banks from developing specialisation. Major developments in international business like merchant banking, wholesale banking, leasing, fiduciary operations, money and capital market operations, have eluded Indian bank branches overseas. Third, overseas branches of Indian banks have not been a force in the promotion of Indian exports.

If Indian banks overseas have largely remained outside the centre stage of international banking as well

as Indian exports, the reasons are twofold. First set of reasons is traceable to the institutional set-up, skills and home market structure. A second reason is the form of overseas representation Indian banks have adopted, viz., branch form. Branches are an extension abroad of the parent bank. Hence, a general claim on a branch is a claim on the bank. Recent experience has shown that the opposite is also true. In other words, a claim on the Indian parent by a foreign importer can be pursued against the Bank's foreign branch if the latter and the foreign importer are domiciled in the same country. I propose to return to the theme of a possible reorganisation of Indian banks abroad, in a short while.

India as an Exporter of Technology

At this stage, it might be useful to draw together the major strands of my presentation so far. I have sought to convey that internationalisation of Indian business has taken three major forms, covering production and banking services. Joint ventures abroad and shift in our export basket from engineering products to projects are examples of internationalisation of Indian production area. Growth of Indian bank branches overseas represent internationalisation of banking services.

Joint ventures and project exports represent technology exports by India. Capacity to achieve this trend is traceable to the import substitution regime and emphasis on growth of heavy industry from the beginning of India's Plan period. Before we move on to some advantages that India has in technology exports, it could be useful to enumerate the motivation of busi-

ness houses to adopt an overseas dimension through joint ventures and project exports. We observe the following features in the case of project exports. A major stimulus appears to have flowed from slow domestic growth, resultant excess capacity. It is observable that when demand has been slack domestically, exports have tended to increase. A related reason is utilization of domestic capacity built up with skilled manpower. Controls on corporate growth and slow growth in domestic market appear to have led large business houses to establish joint ventures abroad. A smaller reason appears to be that by setting up abroad, freer access to foreign technology may be facilitated. In due course, such access to foreign technology could provide a feedback to the domestic operations of business houses setting up abroad. In brief, growth rate of domestic market, controls and availability of incentives have made for a curious mixture providing for export of Indian technology.

Technology refers to application of scientific knowledge to the process of production. Indian technology is nowhere close to international frontiers. However, there is relevance of Indian technology in power generation, textile, paper, engineering in the circumstances of developing countries. This relevance is unlikely to continue long unless India upgrades its own technology. For some time, Indian intermediate goods that are needed in early stages of industrialization, involving small to medium scales, could be reproduced by Indian companies in developing countries. Such goods may not replace goods of developed countries but can serve a complementary role. Indian firms can also

purvey know-how in production of equipments that developed countries no longer produce but are needed by developing countries. The fact remains that Indian technology in most areas of production is dated. By import of technology, modernization can occur and enable India to keep up its relevance in project and engineering goods export. It would appear that through concentration on an identified group of products, through firms which have the capacity to absorb technology, India can successfully update its technological and product development for export markets.

Size and Scale

Experience suggests that large size and domestic experience have been contributory factors in successful overseas operations, particularly in project exports and joint ventures. This is not to suggest that the small scale sector does not have a role to play. The small scale sector firms carry improved prospects in addressing export markets through a consortium approach. Size and scale of operations have enormous bearing on capacity needed to meet competition abroad. The small scale sector can also serve as a supply line for those who have the size, scale to cope with export markets. It is recognised that it is difficult to organize project exports from a host of small producers. Hence the need for a meaningful adding up of the forces in small scale sector and medium to large business sector.

Role of Financial Institutions

Financial institutions act as intermediaries between savers and investors. The investment rate has

more than doubled from the early 1950's to 1970's. In this process, the commercial banks and specialised industrial financing institutions have played a major role. In the context of internationalisation of business, I propose to focus on the role of commercial banks, specialized financial institutions and overseas branches of commercial banks. The integrated structure of financial institutions in India is characteristic of a middle income developing country rather than a low income country.

Commercial banks with over 36,000 branches provide a banking network that is comparable with any developed country. These branches represent the arterial system in our financial system. We then have the specialized industrial financial institutions in the form of Industrial Development Bank of India (IDBI), Industrial Finance Corporation of India (IFCI), Industrial Credit and Investment Corporation of India (ICICI) and State Financial Corporations. These institutions have been a response to the rising demand for industrial finance, following the acceleration in the country's industrial programme. Export-Import Bank of India (EXIM BANK) is one of the latest additions to the range of specialized financial institutions.

In June 1958, the Government of India established the Re-Finance Corporation for Industry (RCI). It was designed to provide refinance to commercial banks against term loans granted by them. In September 1964, the IDBI was established by the Government as an apex institution for medium and long term finance to industry and it took over the functions of RCI. In

a sense, what the IDBI is to industrial finance, the EXIM Bank is to export finance. The EXIM Bank, established on January 1, 1982, took over the international financing function of the IDBI and is designed as the apex financing institution for India's foreign trade. This is a response to the change that has occurred in the composition of India's exports and the consequential need to provide the required financial underpinning for export growth.

Shift in Pattern of Exports

India's exports in the 1950's were, preponderantly, primary products. In the 1960's the export basket diversified. Manufactured goods, especially engineering goods, accounted for a major share of total exports. In the 1970's, there has been a shift from export of products to projects. I have attempted to outline the growth of project exports, capital goods exports through joint ventures, and the growth in our ability to complete large value construction contracts abroad, in the early part of my presentation. Estimates are that project exports by 1990 will reach a level of Rs. 160 billion as against estimate of such exports in 1981 at about Rs. 25 billion. In this estimate, made in the Report of the Task Force on Project Exports, construction contracts, capital goods, turnkey contracts as well as service contracts have been subsumed under the description of project exports.

To support estimated rise in project exports, a large financial underpinning would be necessary. Both loans as well as guarantee facilities to exporters would be called for. The EXIM Bank alone would be unable

to meet in entirety fund-based and non-fund based requirements for the estimated growth in project exports. Estimate is that in 1990, to support project exports of Rs. 160 billion, fund based requirement would be in the region of Rs. 38 billion and non-fund based requirement would be in the region of Rs. 47 billion. It is worth noting that the foreign exchange earnings from project exports in 1990 are estimated to be Rs. 78 billion.

Suffice it to say here that the estimated growth in India's project exports is predicated on the investment that is likely to occur in infrastructural, industrial and resources development in Middle East, Asia, Africa. A track record has been established, over the past ten years, by India about its ability and capacity in technology exports. It must, however, be recognised that India's technological capabilities will require considerable upgrading if estimates of project exports are to be achieved. Another key contributory factor that needs recognition is that domestic industrial growth will largely determine growth in India's exports. Hence the relevance of commercial banks, specialised institutions providing industrial finance and the EXIM Bank working in tandem.

Export Competitiveness

EXIM Bank would aim to contribute towards India's export competitiveness not merely through provision of rupee finance on deferred repayment terms. Since by virtue of its character of business, its assets should convert into foreign currency earnings it has inherent ability to provide foreign exchange manage-

ment capacity both for customers as well as for financial institutions in the country. I should like to explain this somewhat briefly. EXIM Bank assets largely represent accrual of foreign exchange at a future date. Hence it should be in a position to provide long term forward cover to Indian importers who import goods on long term repayment terms in foreign currency. This should be possible on the basis of building up EXIM Bank's own asset portfolio in multi-currencies as also by accessing the growing international market for long term swaps.

Increasingly, export competitiveness will arise on the basis of financing package that an exporter can offer. In a project export, there are three cost centres. First, the rupee cost; second, the foreign exchange cost; third, cost incurred in host country currency. Profit as well as competitiveness will depend upon the skill with which global sources of financing can be packaged, most competitively.

Indian Bank Branches Abroad

In this function of intermediation in global money, exchange and capital markets, EXIM Bank can lay a firm bridge in terms of operations with Indian bank branches overseas. However, certain handicaps of overseas branches may need to be removed. Five comments appear relevant here. First, Indian bank branches abroad are perceived as India risk by its lenders. Hence ability of such a branch to raise resources, and even make loans will be influenced by the parent bank's capital and reserves. Given the low

capitalisation of Indian banks, the handicap is transmitted to the overseas branch. Second, there is often a conflict between the technology available at the parent bank's headquarters and the technology that an overseas branch needs to utilise, to meet local competition in sophisticated financial markets. Third, overseas branches operate with Indian personnel deputed by parent bank, for a stipulated period of years. This militates against creation of a specialised body of staff that can move from one overseas branch to another, thus taking advantage of related experience. Moreover, motivation for such staff is not improved by extending homogenised scales of pay which reflects concepts that are applicable at home headquarters. Fourth, increasingly, there is disparity in the extent of balance sheet disclosure that is required in India and what may be required in an overseas centre of operations. Five, in the absence of a large number of Indian multinational corporations unlike transnational banks from other countries, it has not been possible for our bank branches to follow the expansion of Indian corporations abroad. In order that our overseas branches can compete with their local counterparts, they would need to be freed from the restraints that the branch form of operations abroad appears to be imposing and seek incorporation, association abroad, which may provide local identity and resultant benefits. Sixth, growth of Indian branches in certain countries can also be limited by the reciprocity rule that most countries follow. In other words, if there are two Indian bank branches in X country overseas, the host country will expect their banks to maintain at least two branches in India.

Some departures from bank branch representation overseas has already occurred. Three Indian banks have joined to set up a deposit taking company in Hong Kong. State Bank of India has set up a subsidiary each in U.S.A. and Canada. It would be worthwhile to examine possibility and lucrative advantages in owning branches overseas through holding companies set up either in India or preferably abroad.

Growth Through Exports

There have been two conflicting views about the relevance of exports to Indian growth, from the 1950's. One view has been that the domestic market in a continental economy that is India, is so large that exports are not essential. The other view has been that exports could be the prime mover in India's industrialisation and growth. Whilst the debate has continued and is likely to continue, I have sought to present data and analysis to evidence that Indian business has achieved a remarkable level of internationalisation through joint ventures and exports. This achievement can hardly be disregarded in our future efforts to augment foreign exchange earnings.

India faces rest of this decade with the prospects of declining reserves, lower concessional borrowing. The high rate of investment that is required can hardly be achieved by raising domestic savings rate, appreciably. Role of external resources is, therefore, very relevant. In this context, exports need to grow rapidly and whatever internationalisation of business has occurred, needs to be strengthened.

Indian business has, in a manner of speaking, reached a bend in the river, in the process of internationalisation. Hope is that a strong economic logic will be provided through policy initiatives in order that India becomes a major player in the world foreign trade.

The A. D. Shroff Memorial Trust has no specific views on these economic problems. This publication is issued for public education, and hence the views expressed are specifically those of the author.