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# INFRASTRUCTURE DEVELOPMENT IN RURAL INDIA THROUGH ADEQUATE FINANCING

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It is been evident from various researches that adequate infrastructure is the major factor which is required for advancement of any country. Inadequate infrastructure development in India is a major constraint for sustainable economic growth. Though the country is growing in economic terms, it is still way behind in terms of infrastructure development. Hence, this paper deals with status of infrastructure development in India and the major financial bodies that are engaged in providing funds to infrastructure sector. The paper also examines the issues related to infrastructure financing primarily from the view of Indian banking sector perspective. It also discusses the initiatives taken by Reserve bank of India in developing adequate infrastructure financing system in the country. The paper concludes that infrastructure development helps in maintaining a sustainable economic growth. However, financing of infrastructure remained a constraint for developing countries like India as many investors find such countries highly exposed to risk. Moreover, need for large investments, requirement of long development period, slow returns are some of the common issues which further raise the issue of infrastructure financing. Hence, there is a need for a policy with much greater clarity so that it may help in building up confidence in investors in bringing their finances to the country. Also, there is need to widen the investor base and to build up new vibrant market for financing infrastructure projects. Hypothesis: Adequate financing through banks on Infrastructure projects has positive effect on economic growth in Rural India.

**Keywords:** Gross Domestic Product (GDP), International Monetary Fund (IMF).

## INTRODUCTION

India is one of the fastest growing countries in the world. The country recorded 5.9% growth in Gross Domestic Product (GDP) for Q3FY14 as compared to the previous year. According to International Monetary Fund (IMF), the country in 2016-17 is likely to report GDP growth rate at

6.5%. However, this is still not enough as large number of country's population is living below poverty line. India occupies the second most populated country in the world with poverty averaging to 21.9% in FY12. Thus, it is important for India to grow in a sustainable way and take forward its growth performance to reduce poverty

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levels in the country. This can be only achieved if India will continue to grow and emerge as one of the major contributors in global market. And, therefore, to achieve this objective it is necessary to give importance to various factors like employment, economic policies, infrastructure etc. Among these, 'development of infrastructure' is one of the most important factors the country should consider the most.

The economic growth and development of infrastructure has a very close relationship. On one hand, it is through infrastructure development a country could achieve economic growth and at the same time, it is economic growth which provides country more demand for infrastructure. Therefore, it is important to develop an adequate infrastructure for developing countries like India to give more importance to infrastructure development with adequate infrastructure investments.

Though there are many benefits related to infrastructure development it still remains a difficult job for any country. Need for large investments, long commencement period, slow returns are some of the commonly faced problems which give rise to the issue of infrastructure financing.

### Statement of the Problem

Infrastructure development is quite inadequate in India. Though the country is growing in economic terms, it is still way behind in terms of infrastructure development. Hence, this paper deals with status of infrastructure development in India, the issues related to infrastructure financing primarily from Indian banking sector and role of Reserve Bank of India towards regulatory measures.

### Objective

1. To determine the status of infrastructure development.
2. To understand the issues related to infrastructure financing
3. To give necessary suggestions with regards to facilitate more funds to the infrastructure sector

### Methodology

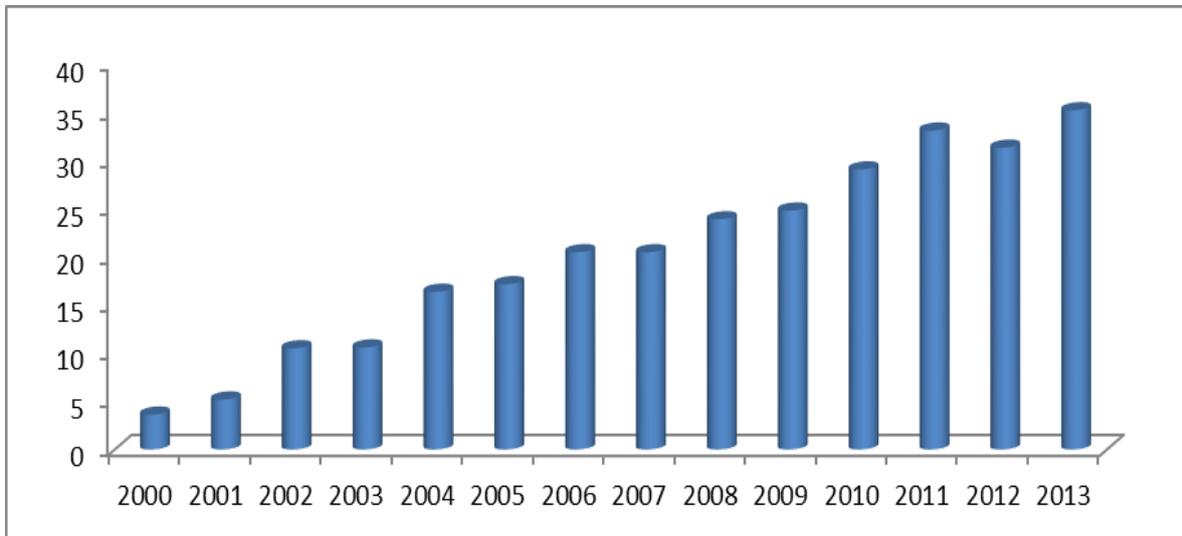
The study is primarily based on secondary data. Publications of Reserve Bank of India (RBI), Journals, Magazines, newspapers, online websites and various reports relating to infrastructure and infrastructure financing formed some of the secondary sources of data for the present study. Simple percentage has been used as a statistical tool. The study is confined to India only.

### Major Sources to Infrastructure Sector Finance

The major institutions involved in providing financing to the infrastructure Sector are banks, Non Banking Financial Corporation (NBFCs) and External Commercial borrowing.

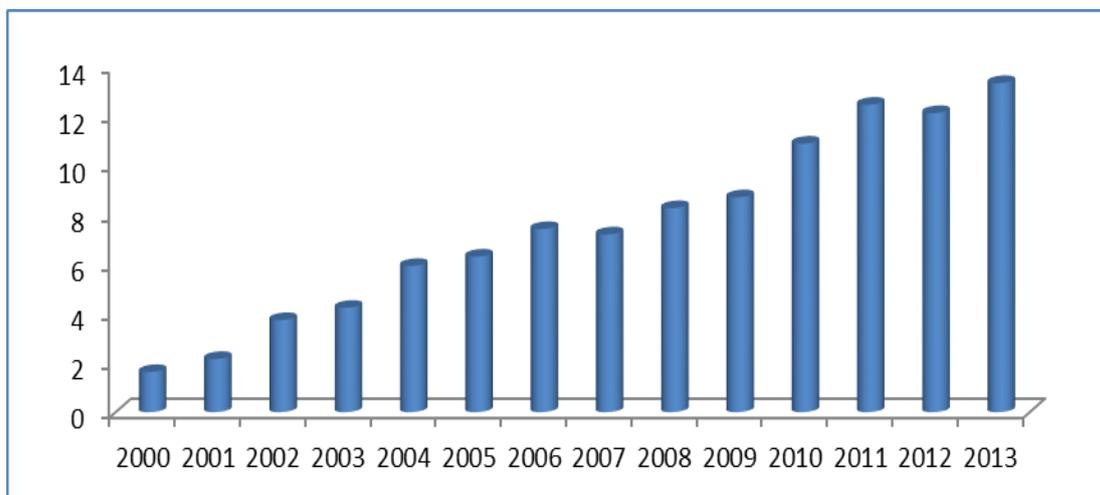
**Banks:** Infrastructure framed 35% of share of total credit industry in FY13 which is highest in a decade as shown in Chart 2. Therefore, in order to fulfil such credit requirements both Private and Public banks act as the major source of finance for the sector. It can be inferred from the Chart 1 that there is major involvement of banks in providing credit for infrastructure projects. In FY13 total bank credit accounts to infrastructure stood around 14%, which was only 1.63% share in FY01. The sector recorded a Compounded Average Growth Rate (CAGR) of 30.8% during the period FY08 - FY13.

**Chart 1: Share of Infrastructure as a Percentage of Total Credit Industry (%)**



Source: RBI, Infrastructure figures include infrastructure related to power, tele-communications, road and ports

**Chart 2: Share of Infrastructure as a Percentage of Total Bank Credit (%)**



Source RBI, Infrastructure figures include infrastructure related to power, tele-communications, road and ports

**NBFC- Infrastructure Finance Company (IFC):**

NBFC-IFC is a company which is engaged in lending and investing in various securities. In Feb 2010, Reserve Bank introduced a new category IFC. IFC will be considered as non depository NBFC should abide with certain guidelines declared by RBI.

**Projected investment in Infrastructure – 12<sup>th</sup> Five Year Plan**

Inadequate infrastructure remained a constraint in Eleventh five year plan. Economic growth and infrastructure development are two sides of the same coin. As it is a fact that for a sustainable economic growth an adequate infrastructure

development plan is essential. Therefore, Government of India in 12<sup>th</sup> five year has planned an investment of Rs. 55 lakh crore. Table 1 shows that infrastructure development which framed 7.40% of GDP in FY13 will increase to 9% of GDP by FY17. This would need more financing from public sector coupled with more rise in investors from private sector. Hence, Government of India in Twelfth five year plan has listed to call private

investment accounting 48% of total investment. Also various measures have been taken by Government of India such as PPP would add to the investment. Attracting more private investors in the market would bring competition and quality in infrastructure projects.

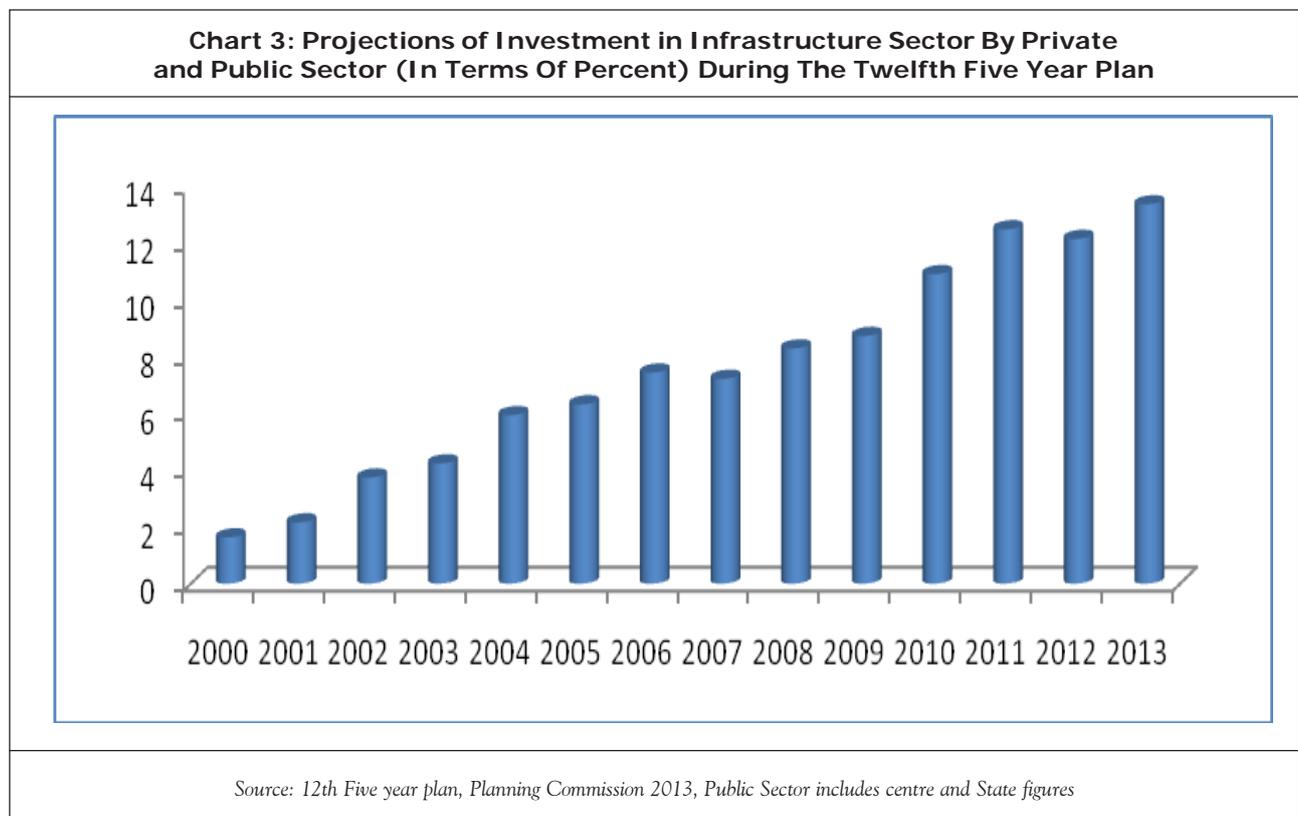
**Structure of Financing in Infrastructure Investment in Twelfth Plan**

It is evident from Chart 3 that the total public sector

**Table 1: Projected Investment in Infrastructure During the Twelfth Five Year Plan (Rs)**  
(in Crore at current prices)

Year	FY13	FY14	FY15	FY16	FY17	Total 12th Plan
GDP	1,01,50,618	1,16,45,987	1,33,58,028	1,53,47,089	1,76,61,485	6,81,63,208
Projected Infrastructure Investment	7,51,012	8,87,454	10,61,316	12,85,573	15,89,308	55,74,663
Infrastructure Investment as percent of GDP	7.40%	7.62%	7.95%	8.38%	9.00%	8.18%

*Source: Planning Commission 2013*

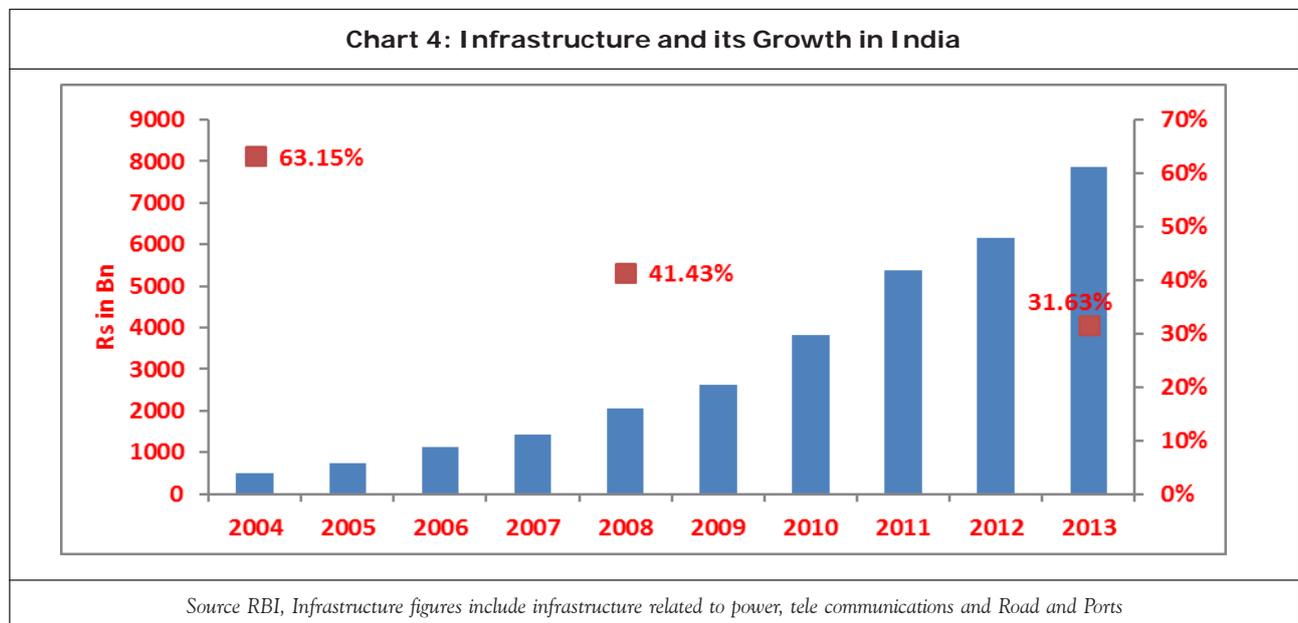


investment in infrastructure projected in the Twelfth five year Plan is 28,90,823 crore contributing 52% of the total investments required. On the other hand, investment made by the private sector is projected to stand at 26,83,840 crore, accounting to 48% of the total investment required during the twelfth five year plan. The private investment includes Public Private Partnership (PPP) projects. In order to promote private investment into this sector, Government has taken initiatives such as development of standardized model concession agreements, regulatory structure for monitoring and

approving PPP projects. These initiatives are likely to bring more investments through PPP in future.

**Issues**

**Gap between Estimated and required funding in Sector:** Gap in funding is one of the major issues which the infrastructure sector is facing. As per the estimates given by Planning Commission for Twelfth five year plan, the funding gap between estimates and required funds is 5,10,470 cr. This frames around 18.4 percent of the estimated requirement of debt.



**Table 2: Projections on Gap in Funding in Sector During 12<sup>th</sup> Five Year Plan**

Sources of funds	Amount (in cr)
Domestic Bank Credit	11,64,646
NBFCs	6,18,462
Pension/Insurance funds	1,50,248
ECBs	3,31,834
Likely Total Debt Resources	22,65,190
Total projected investment	55,74,663
Estimated Requirement of Debt	27,75,641
Gap between Estimates and Likely requirement	5,10,470

Source: Planning Commission

**High Non Performing Assets in Infrastructure**

**Sector:** From the Table 2, it is evident that banks remain the major financiers in infrastructure finance. However, inadequate commercialization of infrastructure projects because of issues pertaining to legal and political environment, the ratio of NPAs to total loans outstanding have raised to 1.45% in FY13 as shown in Table 3. Also the percentage of Gross NPAs and restructured standard advances as to total loans advances in FY13 stood at 17.43% as compared to 4.66% in FY09.

**Role of RBI in Infrastructure Financing**

It is a well known fact that infrastructure development needs huge investment and finances. Therefore, it is necessary to have an adequate flow of funds for a sustainable infrastructure development. The initiatives that have been taken by RBI in order to facilitate free flow of funds for sustainable development of infrastructure in the country are as follows:

**Issue long term Bonds:** RBI has given permission to the banks to issue long term bonds from July 2014. The bonds will have minimum maturity of seven years. This will help in raising

funds for infrastructure projects and housing needs in country. Such instruments have been exempted from Cash Reserve Ratio (CRR)/ Statutory Liquidity Ratio (SLR) maintenance.

**Take out finance:** To meet fund requirements for long term infrastructure projects, banks are allowed to enter into take out financing engagements. Through (Infrastructure Debt Funds) IDFs and other financial institutions (FI) banks can raise debt funds and refinance infrastructure projects. This technique has loosened down the dependence on banks for funds. IDFs should be registered with RBI. The first IDF-NBFC was formed through consortium of Industrial Credit and Investment Corporation of India (ICICI) bank, Bank of Baroda, Citi bank and Life Insurance Corporation (LIC). Currently there are 3 such IDF-NBFCs operating in India. Similarly, IDF formed by way Mutual fund would have to register itself with SEBI.

**Guarantees:** Credit on Infrastructure projects requires availability of finance, regular credit appraisals, and follow ups for free flow of resources. It requires special attention and skills. Such issues are normally faced by banks while

**Table 3: Asset Quality of Infrastructure Loans by Scheduled Commercial Banks**

(Rs. in Bn)

		All Banks				
		Mar-09	Mar-10	Mar-11	Mar-12	Mar-13
Infrastructure	Total Loans Outstanding (Gross)	2618	3816.12	5371.08	6164.4	7860.45
	Total NPAs (Gross)	16.02	22.84	39.1	63.25	114.09
	Gross NPA Ratio (Total NPA/ total Loans Outstanding)	0.61	0.6	0.73	1.03	1.45
Of which	Restructured Standard Advances	105.88	170.23	156.77	690.09	1255.61
	(GNPAs + Rest Std Adv) / Gross Advances	4.66	5.06	3.65	12.22	17.43

Source: RBI magazine

lending finances for infrastructure projects. Therefore, banks can issue guarantees to other lenders or institutions. However, banks still need to fund at least 5% of the total infrastructure project cost and should carry out normal project appraisals and follow ups.

**Relaxations from project delays:** Implementing a large infrastructure project is a complex issue. There are circumstances where the project gets delayed due to unforeseen events. These delays affect the original commencement date of the project. Seeing this issue, RBI has allowed extension beyond original Date of Commencement of Commercial Projects. Certain norms related to extension of original date of commencement have been laid down so as to mitigate the risk of delayed projects on lenders financial position.

**Other measures:** Lenders/banks face a real challenge in order to finance infrastructure projects. Therefore, to encourage banks to lend and increase funds flow for infrastructure development, they are permitted to invest in unrated company bonds. Also RBI has laid down guidelines to raise funds for infrastructure projects through External commercial Borrowing (ECB). The corporate can raise funds upto USD 750 mn during a financial year for implementing an infrastructure project.

### Problems and Suggestions

After having a brief discussion on the current status of infrastructure financing, here are some of the suggestions put forward so as to facilitate more flow of funds to the infrastructure sector.

**Involvement of State and Central Government:** The first and foremost requirement is that the State and Central Government should

increase its participation in developing better quality infrastructure. There is a need of support from State Government in order to frame and maintain supportive and friendly law and order towards issues related to land acquisition, environmental clearances, rehabilitation plans, etc. This will help in facilitating the projects that are undertaken by private sector.

**Priority to Sector:** Infrastructure financing is not considered as primary sector like agriculture, education, housing, etc. Banks have to lend 40 percent to no priority sector.

**Simplify Procedures:** As it is the fact that funding of infrastructure is a major problem, issues like delay in clearance procedures, legal formalities regarding land, etc., further aggravate the issue. Therefore it is necessary to cut down the unnecessary delays especially for mega projects. The simplification of procedures will help in smoothening infrastructure growth. This will bring comfort to the lenders and would facilitate regular financing to the projects.

**Commercially feasible:** Infrastructure projects are mainly financed by banks and other financial institutions. And as it is known that the infrastructure project requires huge finance it is important to make the project commercially feasible for regularity in financing loan. This will in turn bring a sustainable growth in infrastructure without putting financial sector at risk.

**Regular Project Appraisal:** A regular up gradation and follow up is required by the banks so as to check the viability of the project. This would help in mitigating the risk if required.

**Widening investor base:** It is also suggested to widen the investor base by allowing new institutions and investors like insurance

companies, mutual funds, venture capital funds, provident fund etc with reoriented guidelines and regulatory measures and to allow them to invest largely in corporate bonds.

**Bond Market:** An adequate and viable corporate bond market is required as this would reduce the involvement of banks for infrastructure finances and would not burden banks directly or indirectly.

**Tax benefits:** The Government should give more tax benefits so as to attract more investors.

**Develop new markets:** There is a need to develop new markets so as to facilitate infrastructure financing. By creating vibrant corporate bond market we can reduce the dependency on banks. Also feasible G-sec market would help in growing debt market. Provisions for standardizing stamp duties is across the country would too help in a big way.

## CONCLUSION

Development of infrastructure plays a very important role. For developing countries like India, Infrastructure development helps in maintaining a sustainable economic growth. Infrastructure development and economic growth are interrelated. If there is infrastructure development there will be growth in the economy and continued growth in economy would bring more demand for infrastructure. However, financing of infrastructure remained a constraint for developing countries. Countries like India are viewed as highly exposed areas to risk by the investors and therefore it becomes difficult for the country to attract investors. Delay in commencing the projects due to inadequate procedural or legal issue can give rise to risks like fluctuating interest rates, market risk, foreign exchange risk and operational risks. There are times where due to

inadequate planning, the project gets delayed and the cost of infrastructure project increases to such a level where it becomes difficult to get returns. Therefore it is essential to make policy with much greater clarity so that it may build up confidence in investors in bringing their finances to the country. Also there is a need to widen the investor base and to build up new vibrant market for financing infrastructure projects.

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