Letter of Transmission[1]

S.K. GOYAL, M.A., Ph.D

New Delhi
23rd October, 1967

Dear Shri Chandrashekhar:

I have great pleasure in forwarding the Report of our Team on Banking Institutions and Indian Economy. May I, however, make it clear that the Team members have signed this Report in their personal capacity and therefore the views expressed are personal and not those of the institutions in which they are employed.

I would like to thank you, on behalf of the Team for providing us the opportunity to come together and study such an important problem of the Indian economy.

With best wishes,

Yours sincerely,
Sd/-
(S.K. Goyal)

Shri Chandrashekhar
Secretary
Congress Party in Parliament
24-25 Parliament House
New Delhi - 1

[1] For a copy of the letter from Shri Chandrashekhar see Appendix-I.

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Part One

BANKING IN INDIA - STRUCTURE AND TRENDS

Introduction

In recent years India's national economy has developed certain serious economic maladies. in the first instance the economy has become heavily dependant on foreign aid. The proportion of foreign aid in the Plan Development Programme has been continuously rising since the First Five Year Plan. Since the prospects of the availability of foreign aid in the last two or three years have become very uncertain and rather dim, there has been a slack in the levels of economic activity and employment in the country.

Secondly, there has been the paradox of inflationary recession having come in the economy and tending to become all pervasive. The chief characteristic of the recession is that, while on the one hand there are large unutilised industrial capacities in the economic system, the supply of raw materials and other components for production of final goods is extremely deficient. The decline of agricultural production explains only a part of this phenomena, while another part will have to be ascribed to the general shortages in the economy which have been generated as a result of the growing inter-sectoral imbalances caused by the functioning of the financial institutions and the economic system in a particular manner.

The most curious aspect of the present situation is that the price level of industrial and agricultural goods continues to be very high despite the slack in demand. Obviously, the financial system of the country seems to have acquired such characteristics that it is able to sustain a prolonged holding of goods in the economy without leading to the adjustments of the price level with the existing state of demand and supply.

The role of bank credit in the situation is obviously an important factor to be examined in so far as it helps to create the present situation as well as to maintain it for a long period.

In addition, due to various political and economic reasons, both national and international, the perspective of long term development of the economy is tending to get blurred. The commitment to long term programmes of plan development has tended to become weak in recent years and greater attention is being given to measures of policy which seek to attain economic stability rather than economic growth. In this context too, it has become necessary to examine the role that the banking system of the country has played so far in promoting the long term growth of the economy as well as in creating conditions in which further growth of industry and agriculture has been halted in recent years.

With this background in our mind, we have examined in this Report the structure and functioning of our banking system and drawn necessary conclusions regarding its reorganisation, which in our opinion are vital for accelerating further growth of the economy and the achievement of broader social objectives.

The magnitude of the bank deposits in 1965 was only 15 per cent of the National Income (at current prices). The corresponding figure for 1951 was 9 per cent. In money terms, the bank deposits have grown on an average at the rate of nearly 16 per cent i.e. from rs. 908.47 crores in 1951 to Rs. 3073.36 crores in 1965.

This fact indicates two things. One, that the bank deposits in India represent a significant part of the Nation's disposable resources. And secondly, the growth of bank deposits has been nearly five times the rate of growth of the National Income. With each successive year of planning in India, the banks have been accumulating larger and larger financial resources of the society. On the assumption that the past trends would continue it can be safely projected that banks would very soon acquire command over the bulk of the nation's financial resources.

Declining Number of Banks

The Banking institutions in India can be broadly grouped under two categories viz., (i) scheduled, and (ii) non-scheduled. Since 1951 there has been a significant decline in the number of these institutions. From a total of 566 banks (of both categories) in 1951, the number had come down to only 109 in 1965. The reduction in the number of non-scheduled banks has been phenomenal -- from 473 to mere 33; and the scheduled banks from 92 in 1951 to 76 in 1965. As is only natural, with reduction in numbers on the one side and growth in banking deposits on the other, it has led to larger concentration within the banking sector.

Scheduled and Non-Scheduled Banks

Out of the total bank deposits of Rs. 3183.20 crores in 1965, the non-scheduled banks, which numbered 33, held deposits worth rs. 24.15 crores only. Similarly, the significance of non-scheduled banking has been very little in terms of advances and other operations. Past experience provides support to the idea that small financial institutions have little place in a developing society. These do not enjoy confidence of the public in general; nor do these institutions have the resources to organise such facilities which can be easily provided by the large sized national financial institutions. Therefore, for the purpose of our discussion, the non=scheduled banks have very little significance.

The scheduled banks are 76 and these can be grouped under (i) the Public Sector; and (ii) the Private Sector. The former comprises of the State Bank of India and seven of its subsidiaries[2] Out of the remaining 68 scheduled banks 15 banks are of foreign origin.

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2. The subsidiaries to State Bank of India are: (i) The State Bank of Bikaner & Jaipur; (ii) The State Bank of Hyderabad; (iii) The State Bank of Indore; (iv) The State Bank of Mysore; (v) The State Bank of Mysore; (v) The State Bank of Patiala; (vi) The State Bank of Saurashtra; and (vii) The State Bank of Travancore.

This leaves the private sector Indian banks as 53 only.

Foreign Banks

The total number of scheduled Bank offices at the end of 1965, were 6,133 only. The following Table gives details of the State-wise Bank Offices.

Table - I

Showing State-wise Break-up of Bank Offices in India

S. No.	States	No. of Offices in Each State				% of Offices in Each State		
		S.B.I. and Sub.	O.I.S.B.	F.B.	Total	S.B.I. and Sub.	O.I.S.B.	Foreign Banks
	1	2	3	4	5	6	7	8
1.	Andhra Pradesh	205	217	2	424	10.7	5.6	2.2
2.	Assam	34	24	1	59	1.8	0.6	1.1
3.	Bihar	93	120	-	213	4.8	3.1	-
4.	Gujarat	155	329	1	485	8.1	8.4	1.1
5.	Jammu & Kashmir	2	12	1	15	0.1	0.3	1.1
6.	Kerala	126	257	4	387	6.6	6.6	4.3
7.	Madhya Pradesh	134	104	-	238	7.0	2.7	-
8.	Madras	161	679	10	850	8.4	17.4	10.9
9.	Maharashtra	199	587	23	809	10.4	15.1	25.0
10.	Mysore	137	429	1	567	7.1	11.0	1.1
11.	Nagaland	2	-	-	2	0.1	-	-
12.	Orissa	49	20	-	69	2.6	0.5	-
13.	Punjab	143	232	4	379	7.4	6.0	4.3
14.	Rajasthan	125	119	-	244	6.5	3.1	-
15.	Uttar Pradesh	213	325	2	540	11.0	8.3	2.2
16.	West Bengal	94	229	25	354	4.9	5.9	27.2
17.	Union Territories	48	209	18	275	2.5	5.4	19.5
18.	Total	1920	3892	92	5904	100.0	100.0	100.0

S.B.I. : State Bank of India and Subsidiaries.
O.I.S.B. : Other Indian Scheduled Commercial Banks
F.B. : Foreign Banks.

It would be seen that out of the 92 offices of the foreign banks, 75 offices were located in four States of the country i.e.e Maharashtra, 23; West Bengal, 25; Delhi, 17; and Madras 10. Punjab and Kerala had 4 offices each. States like Bihar, Madhya Pradesh and Orissa did not have even a single branch of foreign banks. It is, therefore, obvious that the foreign banks have generally confined themselves to centres of international trade. Also it is by no coincidence that the majority of the foreign bank offices have been at the seaports of the country, except Delhi, for obvious reasons.

Concentration of Banking Operations - State-wise

In the case of Indian scheduled commercial banks it can be seen that bank offices are concentrated in a few States only. For instance, large number of the offices are located in five States viz., Maharashtra, Madras, Gujarat, Mysore and West Bengal. The five States' combined total of bank offices was 3065 out of the total of 5,812. States like Jammu and Kashmir, Bihar, Orissa and Madhya Pradesh had a significantly smaller share in the national total. However, two States, namely Kerala and Mysore, are exceptions. Otherwise, the bank offices have been mainly located in the comparatively well-off States of the country.

Another way of studying the special distribution of banking activity is to have a look at the distribution of bank offices according to the population of urban centres. The following table shows the number of offices in centres of varying population. (See Table-II showing Distribution of Bank Offices according to Population Centres)

Table - II

Showing Distribution of Bank Offices According to Population of the Locations

		Number of Offices as on December 31, 1965						
S. No.	Population Range	Foreign Banks	State Bank & Sub.	Other Indian Scheduled Banks	Total	% of Col. 2	% of Col. 3	% of Col. 4
	1	2	3	4	5	6	7	8
1.	Unclassified	-	74	42	116	3.8	1.0	2.0
2.	Less than 5,000	-	104	117	221	5.4	3.0	3.8
3.	5,000 to 10,000	1	289	258	548	15.0	6.6	9.4
4.	10,000 to 25,000	1	620	625	1246	32.3	16.0	21.4
5.	25,000 to 50,000	3	315	510	828	16.4	13.1	14.2
6.	50,000 to 1 lakh	-	161	486	647	8.4	12.5	11.1
7.	1 lakh to 5 lakh	11	192	849	1052	10.0	21.8	18.1
8.	5 lakh to 10 lakh	5	58	230	293	3.0	5.9	5.5
9.	10 lakh and above	71	107	775	953	5.6	19.9	16.4
10.	Total	92	1920	3892	5812	100.0	100.0	100.0

Source: R.B.I. - Statistical Tables Relating to Banks in India, 1966.

From this it is evident that the banking activity has been mainly confined to urban centres. For instance, nearly two-thirds of the bank offices are located in centres having population of more than 1 lakh. On the other hand only 15 per cent of bank offices were located in towns with population of 10,000 and lesser.

In both the above tables if one compares the degree of spatial concentration of banking activity, as represented by the offices, one notices that the degree of dispersion is comparatively higher in the case of the State Bank of India and its subsidiaries. Comparatively the State Bank offices are more evenly distributed than that of the private commercial banks. Similarly, a large percentage of the State Bank offices are located in smaller towns as compared to the private banks. Nearly one-fifth of the private banks are in big cities whereas the corresponding percentage for the State Bank is only 5.6. There is clear indication that the State Bank offices are opened in such areas where the private banks hesitate. It could happen only because the State Bank had followed a different policy as regards the opening of offices, from that of the other banks.

However, the overall picture of banking in India is that of uneven distribution. It becomes further clear from the State-wise break up of banking offices the deposits and bank credit in relation to population. From the following table it would be seen that the most highly developed States, from banking view point, are Madras, Mysore, Kerala and Gujarat. The worst in order are: Orissa, J&K, Bihar and Assam. In the first category of State a bank office exists for every 50,000 persons whereas in the worst an office is for more than 2 lakh persons. (See Table-III showing Distribution of Bank Offices, Deposits and Bank Credit in Different States, 1965).

Table - III
Showing Distribution of Bank Offices, Deposits and Bank Credit in Different States (1966)

S.No.	States	000 person per Office	Per capita Deposits	Per Capita Bank Credits	Credit Deposit Ratio
	1	2	3	4	5
1.	Andhra Pradesh	90	30.0	17.5	58.0
2.	Assam	227	22.7	9.1	40.0
3.	Bihar	234	19.3	6.9	36.0
4.	Gujarat	47	103.7	57.7	56.0
5.	Jammu & Kashmir	246	43.7	3.4	78.0
6.	Kerala	48	51.1	31.0	61.0
7.	Madhya Pradesh	148	21.9	14.9	68.0
8.	Madras	41	57.5	60.8	106.0
9.	Maharashtra	53	184.8	152.1	82.0
10.	Mysore	45	57.4	39.5	69.0
11.	Nagaland	-	-	-	-
12.	Orissa	273	9.3	4.6	50.0
13.	Punjab	59	78.9	33.6	43.0
14.	Rajasthan	91	23.2	12.1	52.0
15.	Uttar Pradesh	145	28.8	12.7	44.0
16.	West Bengal	112	115.8	123.1	106.0
17.	All India Average	80	64.2	44.6	67.0

Source: R.B.I. - Statistical Tables Relating to Banks in India, December, 1966.

Per Capita Deposits in States

From column 3 of table III it is also clear that per capita deposits are the highest in these States which have larger number of offices. For instance, the four States (after excluding two States, namely, West Bengal and Maharashtra where the higher per capita deposits can be explained because of the high quantum of demand deposits of the industrial and business enterprises) with the higher per-capita deposits are those which had larger banking offices.

Looked from the per capita bank credit angle it would be seen that except for the four States (namely), Maharashtra, West Bengal, Madras and Gujarat) the per capita credit in 12 States was lower than the national per capita average of Rs. 44.6. In Maharashtra the per capita credit was Rs. 152.1; West Bengal Rs. 123.1; Madras Rs. 60.8 and in Gujarat Rs. 57.7. On the other hand, the per capita bank credit was as low as Rs. 3.4 in Jammu and Kashmir; Rs. 4.6 in Orissa; Rs. 6.9 in Bihar and Rs. 9.1 in Assam. In the rest of the States the figure varied from Rs. 12.0 to nearly Rs. 40.0.

Credit-Deposit Ratio

It is of interest to see the credit-deposit ratio in States. It is only in the case of two States, West Bengal and Madras, that the ratio is more than 100 showing that the Bank credit is 6 per cent more than the deposits. In the case of the rest of the States the ratio is less than 100. In five States the ratio is less than 50 with Jammu and Kashmir having the ratio as low as 7.8.

Bank Investments

It needs to be mentioned here that credit-deposit ratio does not represent the true picture. It is so because out of the total deposits the investments accounted for nearly 935.16 crores in 1965. Nearly four-fifths of the bank investments were held in the form of securities of the Central and State Governments. Investments, other than in the Government securities, were of the order of Rs. 159.97.

From this it would be seen that investments account for nearly 30.7 of the total deposits. Therefore, credit-deposit ratio should take into account the spatial investment pattern as well. In the absence of more details on State-wise bank investments, for the purpose of understanding real credit policies, one may deplete the deposits of each State, on an average, by the percentage of investments to deposits. For instance, one can take it that each State has to share its bank deposits with the Central and State Governments by a certain ratio. For the year 1965 one may spread the bank investments of Rs. 935.16 crores equally over all states.

Table - IV

Showing Pattern of Investments of the Scheduled Bank (March 1965)

S.No.	Source of investment	Amount	Percentage
	1	2	3
1.	Government Securities	755.12	80.7
	a) Central	562.69	60.2
	b) States	191.20	20.4
	c) Others	1.23	0.1
2.	Domestic Investments	159.97	17.1
	a) Trustee Securities	114.53	12.2
	b) Shares of Joint Stock Companies	25.04	2.7
	c) Real Estate	10.21	1.1
3.	Foreign Investments	20.7	2.1
4.	Total	935.16	100.0

Source: R.B.I. - Statistical Tables Relating to Banks in India, December 1966.

Movement of Resources

Table - V shows Statewise bank deposits and credit as on March 31, 1965. Column 3 gives the adjusted deposits as is shown in columns 4 and 5. From these columns it emerges that out of the 16 States of the country only three States are such which draw more bank credit than their deposits. It can be seen that through the institution of banking nearly 345 crores of rupees are channelized for purposes of business and industrial activity from the other States and made available to West Bengal, Maharashtra and Madras. The situation can also be described as one in which the commercial banking institutions act as instruments of mobilizing saving from the other States of the country for supporting investments and other economic activity in the three States which are already well developed.

Viewed from another angle the banks act as instruments to ensure flow of financial resources from under-developed areas to the industrially advanced ones. If one looks at the pattern of advances and deposits, according to the centres of population, one finds relatively much higher concentration of advances in cities. The advance/deposits ratio for large cities works out to be as high as 91.3 whereas the ratio is 39.2 in the case of small centres.

Table V

Showing Variation in Bank Deposits and Credit (State-wise)

S.No.	States	Deposit in Crores	Credit in Crores	Deposits after accounting for invest-ment (In Crores)	Excess Deposits	Excess Credit
	1	2	3	4	5	
1.	Andhra Pradesh	114.3	66.8	79.2	+12.4	-
2.	Assam	30.4	12.2	21.0	+8.8	-
3.	Bihar	-96.6	34.6	66.9	+32.3	-
4.	Gujarat	235.3	130.9	163.1	+32.2	-
5.	Jammu & Kashmir	16.1	1.3	11.1	+9.8	-
6.	Kerala	94.3	57.2	65.3	+8.1	-
7.	Madhya Pradesh	77.3	52.6	53.6	+1.0	-
8.	Madras	202.4	214.0	140.3	-	73.7
9.	Maharashtra	795.5	655.0	551.3	-	103.7
10.	Mysore	146.3	100.6	101.5	+0.9	-
11.	Nagaland	-	-	-	-	-
12.	Orissa	17.6	8.7	12.2	+3.5	-
13.	Punjab	175.7	74.1	121.8	+47.7	-
14.	Rajasthan	51.3	26.9	35.6	+8.8	-
15.	Uttar Pradesh	225.9	99.3	156.5	+57.2	-
16.	West Bengal	453.0	481.4	313.9	-	167.5
17.	All India	3049.2	2116.4	2116.4	+344.9	344.9

Source: R.B.I.: -- Statistical Tables Relating to Banks in India, December, 1966.

Another factor which needs to be kept in mind is that the nature of deposits also varies from centre to centre. However, broadly speaking, fixed and saving deposits from higher percentage of the deposits in smaller centres whereas in larger cities (as is also true of industrially developed states) the deposits are more of the nature of demand deposits. Viewed in this light the flow of funds from under-developed states may appear to be even more significant. Similarly, it would be seen that banks help to mobilize saving from smaller population centres to larger ones[3].

From the above account it may be said that banking institutions in India have not been uniformly developed in all States. Also there is an evidence that bank offices have

3. For an analysis of the deposits and advances in cities and smaller centres, See: Kanvinde, D.J. State Bank of India, Monthly Review, July, 1967, pp. 234-246.

been mainly operating in thickly populated centres. In this regard, a better spatial dispersion of the State Bank of India is well recognised than of the other commercial banks. The disparities in level of growth of banking is indicated by number of offices, and the magnitudes of bank deposits and credit. Another interesting feature of the Indian banks operation is their impact on the flow of financial surpluses from different states to only three states of the country. As can be expected from the above pattern of the growth of banking in this country, an evidence to the fact exists that banks act as instruments of mobilizing savings from smaller centres for providing credit in the urban and industrial centres of the country.

Paid-up Capital and Deposits Ratios

Another important feature of the Indian banking system is the extremely low ratio between the paid-up capital and the bank deposits. Initially the banks were established with very little paid-up capital and the situation continues to be so. For instance, the paid-up capital of most of the banks have been around one to two crores. The total paid-up capital of all the Indian Scheduled Banks (numbering 61) stood at Rs. 44.36 crores only. However, because of the continued persuasion on the Reserve Bank the banks have built up some reserves. The total equity capital of the scheduled Banks was Rs. 61.78 crores in 1951 and it rose to Rs. 93.25 crores in 1965. The rise in the amount has been mainly due to the building up of Reserves. The rise in paid-up capital and reserves has been by about 50 per cent only whereas the bank deposits have grown by nearly 238 per cent. As a result the ratio of paid-up capital and reserves to Deposits has gone down from 9.7 per cent in 1951 to 3.4 per cent in 1955.

Table - VI

Showing Paid-up Capital and Deposits Ratio in the Indian banks -- 1965

S.No.	Name of the Bank	Paid-up Capital and Reserves (Cr)	Deposits (Crores)	Ratio (Col. 2/3)
	1	2	3	4
1.	Bank of Baroda	2.0	185.91	1.07
2.	Bank of India	4.0	235.72	1.69
3.	Central Bank of India	4.7	306.04	1.53
4.	Punjab National Bank	2.0	232.96	0.86
5.	United Commercial Bank	2.8	141.15	1.98
6.	Five Banks (1 to 5)	15.5	1101.78	1.48
7.	State Bank of India (and its Subsidiaries)	10.63	881.47	1.20
8.	All Scheduled Banks	44.4	2814.66	1.57

Source: R.B.I. - Statistical Tables Relating to Banks in India, December, 1966.

The paid-up capital Deposit ratio for the overall banking sector is low in itself but if one looks at the ratio in the individual banking companies, one would notice that the same is extremely low in the case of the bigger banks of the country. How important this ratio is, needs to be underlined because it is the paid-up capital the ownership of which determines controlling authority over the banks. The following table shows paid-up capital to Deposits ratio of the important banks in the country.

Ownership of Bank Shares

The quantum of paid-up capital or its relationship with deposits is not in itself of much significance as the implications of the pattern of the ownership of the bank shares which form the paid-up capital. Take the case of the Central Bank of India. The paid-up capital is Rs. 4.70 crores. According to the information provided in the balance sheet of the Bank, the bank had 12.6 lakhs shares held by 24,800 share-holders. nearly 92 per cent of the share-holders held less than 100 shares each. Another 5 per cent held shares between 100-200 each and 2 per cent held shares between 200-500. It was only one per cent of the share-holders who held more than 500 shares, individually. From another point of view 49 per cent of the shares were held by 3 per cent of the share-holders and 36 per cent shares were owned by one per cent of the share-holders.

The pattern of ownership is widely dispersed. If one were to have details regarding the spatial distribution of bank shareowners, one would find that a large part of the shares are held by small isolated individuals scattered throughout the country. On the other hand a fraction of the share-holders own a big block of shares. The wide dispersion of share-holders helps to strengthen the control of a small section of the share-holders in the banks. In a company in which all share-holders could be present at its General Meetings, the group which wishes to carry majority would require 51 per cent votes. But if the share-holders are scattered all over the country an interest group can enjoy control over the company with even much lesser votes. Because of the wide distance and lack of interest by an average share-holder, control over the banks is exercised by a small group. Even keeping the numbers aside, one needs an investment of Rs. 1.0 crore only to obtain control over a bank with paid-up capital of Rs. 2.0 crores. It is through this mechanism that control over each banking institution has come to rest with a group of persons or a few families.

It is in this regard that the Governor, Reserve Bank of India, said:

> "One of the structural features of Indian banking is this concentration of power which, in some cases, is enormous in relation to the capital actually employed. From time to time we come across cases in which a family or group has a controlling interest in a bank and it has become a major task of inspection to prevent the exercise of this interest in undesirable ways".

Ownership and Control of Banks

On account of the scatteredness of the share-holdings of private commercial banks as well as the limited amount of paid-up capital in relation to the total deposits, it is necessary to examine the ownership and control of private commercial banks in India. Here, it is necessary to distinguish between the persons who own shares in the banking companies and those who put their deposits in the banks. As we have seen the ratio of paid-up capital of the total number of deposits is extremely low. Consequently, the depositors have much higher stakes in the successful operations of private commercial banks, financially speaking, than the owners of share capital. Nevertheless, it is found, as already indicated above, that the ownership and control of the total finances of the banking system rests with very small number of persons who are able to determine the patterns of allocation and investment of bank finance according to their own individual interest and convenience.

With the present system of private ownership of banks,the security enjoyed by the depositors is considerably weakened since it rests on the ability and competence of those who control the allocation and investment of bank finances. But from the point of view of social justice and of encouragement of the confidence of depositors in the banking system, it is necessary that they should be ensured a complete security for their deposits with the banks which can be done only if the banking system was to be nationalised and the ownership of banks was to rest in the Government. This is because the first claim on the resources of a bank in case of its failure would be that of depositors and not of the owners of share capital, and this would be best ensured by a nationalised banking system.

While under any law the private banking institutions can go bankrupt, there is nothing like a phenomenon called government going bankrupt. Hence the interests of the depositors cannot be admittedly secured beyond any doubt whereas in case of private banking, insecurity can never be ruled out.

If ownership alone is to be the criterion it stands to reason to state that the depositors whose deposits are infinitely far greater in proportion to the total paid-up capital should be considered the legitimate owners of the banks rather than the market shareholders, and an ordinary depositor, in fact, exercises greater control over government and governmental activities than he can ever do in the case of private bank.

Thus even from the point of view of exercise and control in the case of nationalised institution, the depositor will not be an invisible owner but an active participant in the exercise of control.

Ownership of Deposits

The total number of bank accounts stood at 1.02 crores in 1965. Out of this fixed deposit accounts were nearly 19 lakhs and the saving deposits nearly 67 lakhs. The number of current accounts were around 16 lakhs. The following table provides break-up of the accounts and deposits.

Table - VII

Showing Distribution of Accounts and Deposits

S.No.	Category	Accounts	Deposits Cr.	Accounts %	Deposits %
1.	Demand Deposits	16,32,000	835.7	15.9	30.8
2.	Savings Deposits	67,28,000	581.7	65.7	21.4
3.	Fixed DEposits	18,74,000	1296.5	18.3	47.7
4.	Total	1,02,34,000	2,713.9	100.0	100.0

It would be seen that nearly 31% of the deposits are demand deposits held by nearly 16% of the accounts. The savings accounts from nearly two-thirds of the total bank accounts.

For the purpose of the study of the ownership pattern of the bank deposit in clientele can be grouped under three broad heads: (i) Personal and partnerships; (ii) Government, public sector and cooperatives; and (iii) corporate sector. (See Table-VIII).

Table - VIII
Showing Ownership Pattern of Demand, Savings and Fixed Deposits under Three Categories

S. No.	Category	Personal and Partnership		Govt. and Cooperative		Corporate Sector	
		000 Accts.	Cr. Amount	000 Accts.	Cr. Amount	000 Accts.	Cr. Amount
	1	2	3	4	5	6	7
1.	Demand Deposits	1,529	468.9	41	185.7	63	181.1
2.	Savings Deposits	6,728	581.7	-	-	-	-
3.	Fixed Deposits	1,855	929.9	10	218.0	9	148.5
4.	Total	10,112	1,980.5	51	403.7	72	329.6

Out of the total demand deposits of Rs. 835.7 crores, nearly 24% belonged to the corporate sector. In the case of savings accounts the entire deposits of Rs. 581.7 crores belonged to personal accounts. Similarly, about three fourths of the fixed deposits were that of personal and partnership accounts. If one looks at the savings and fixed deposits collectively, one would see that out of the total deposits less than eight per cent of the deposits (amount) belonged to the corporate sector. For the purpose of our discussion one can combine the ownership category of personal and partnerships with the Government and cooperatives. The ownership pattern of bank deposits indicates that practically nine-tenths of the bank deposits belong to a large number of small depositors or Government institutions and cooperatives.

Industry and Banks

However, the control over banks is enjoyed by the corporate sector only. This is evident from three sets of statistics. One, the close relationship between the corporate sector and the Bank Directors; two, the nature of credit policies as pursued by banking institutions; and three, the extent to which the Directors of the banking companies have taken loans from the banks.

Inter-locking

The extent of inter-locking between leading banks and other companies a study was conducted in the Company Law Department by Shri R.K. Nigam. According to the Survey of Directorships of the twenty leading banking companies, a total of 188 persons served as Directors on the boards of these 20 banks. The 188 bank directors held 1452 directorships of other companies also. The total number of companies under these directors were 1100. This excludes non-profit making organisations. (See Table IX).

Table - IX
Structure of Demand, Savings and Time Deposits

S. No.	Deposits	Limited Companies		Govt., Quasi-Govt. & Coops		Personal and Partnerships	
		Accts. in 000	Amounts in crores	Accts. in 000	Amounts in crores	Accts. in 000	Amounts in crores
	1	2	3	4	5	6	7
I.	**Demand Deposits**						
	(i) Industry	18	64.6	1	38.4	64	25.3
	(ii) Trading	30	46.1	1	7.8	588	158.2
	(iii) Financial	8	54.9	-	2.6	-	2.3
	(iv) Others	9	15.5	39	136.9	877	282.1
	Total (I)	63	181.1	41	185.7	1529	468.9
II.	**Savings Deposits**						
III.	**Time Deposits**						
	(i) Industry	3	73.8	1	31.8	3	9.7
	(ii) Trading	3	38.6	-	12.2	56	36.6
	(iii) Financial	1	6.7	-	5.9	-	0.4
	(iv) Others	2	29.4	9	168.1	1796	883.2
	Total (III)	9	148.5	10	218.0	1855	929.9
	Grand Total	72	329.6	51	403.7	10112	1980.5

Source: R.B.I.: Statistical Tables Relating to Banks in India, December, 1966.

A detailed study of the directorships held by the directors of the five leading banks reveals that through common directors these five banks are connected with 33 insurance companies, 6 financial companies and 25 investment trusts. Further, these banks were connected to 584 manufacturing and other companies and 26 trading companies and 15 associations not for profit. (See Table X).

The close relationship between the private corporate sector and the banking institutions was also underlined by the Mahalanobis Committee Report. It had specially noted that "The dominance of industrial directors on the boards of the commercial banks is seen to be much greater in the case of the first eight banks, in whose case they numbered 59 out of 77 or nearly 77 per cent of the total".

Financial Accommodation to Directors

A very natural corollary of the close relationship between the banks and the industrial enterprises is the advantage that these industrialists enjoy for the purpose of credit accommodation to their own concerns. Due to obvious reasons a bank director is in a better position to obtain credit from his bank. The debt due to the bank directors or their companies was nearly Rs. 55.8 crores in 1954. But the amount had risen to Rs. 290.0 crores by 1965. The debt due reflects only the amount due at the end of the year. The bank loans given to the directors and their companies in the same year stood at Rs. 317.4 crores.

The figures given above should only be taken as broad indications of the financial accommodation that the bank directors obtain directly from their own banks. But the advantages enjoyed by the bank directors and the ease with which they can secure bank credit, is not fully reflected in these figures. There is no doubt that the director of a bank commands a special status and reputation and thereby his association helps the companies to secure easy credit from practically any banking institution. Moreover, the phenomena of `back scratching' and its implications cannot be assessed through these figures.

Back Scratching

Supposing `X' is the director of `A' bank and `Y' that of `B' bank. With mutual understanding, bank `B' can lend loans to `X' and in return `Y' can obtain similar financial accommodation from `A'. In this way both banks have not lent to their own directors; and yet bank credit has been made available to both the bank directors. This phenomena is a well known one in the financial circles. It would be no surprise if the total bank credit advanced, directly or indirectly, to bank directors works out to be around Rs. 600 crores to Rs. 700 crores. Thus out of the aggregate bank credit, a few industrial houses would be claiming a large chunk.

Table - X

Showing Distribution of Directorships Held by the Directors of the Leading Five Banks

S.No.	Name of the Bank	Number of Directors	Number of Directorships held	Directorships held in: Insurance	Financial Companies	Investment Trusts	Manufac-turing & Other Cos.	Trading Companies	Associations not for profit
	1	2	3	4	5	6	7	8	9
1.	Bank of India	11	174	10	1	8	146	9	-
2.	Central Bank of India	10	108	4	1	3	94	4	2
3.	Bank of Baroda	12	196	9	-	9	162	7	11
4.	United Commercial Bank	13	144	6	2	4	127	3	2
5.	Punjab National Bank	9	65	4	2	1	55	3	-
	Total	55	689	33	6	25	584	26	15

Source: Nigam, R.K.,: Company News and Notes, October, 1, 1963, pp. 62-74.

The figures of bank credit to their directors also suffer from another serious limitation. According to the Bank Companies Act, no bank director can hold directorship of another bank and there is also a limit beyond which no individual can hold company directorships. These legal provisions are very easily set aside if one has his wife alive; and the situation is most convenient if one is lucky enough to have a large number of children or relations. In India, therefore, it poses no problem to keep oneself within the legal limits and yet operationally continue as one would if there were no legal restrictions.

Thus the quantum of bank loans, shown against the directors and their companies in the above Statements, is only the direct and a clear one -- for which returns have been filed to the Reserve Bank. But the extent of `back scratching' can only be known through a study of the manner in which the bank credit in India has been shared by individuals, the banking magnets and the few big industrial and business houses to which the directors belong.

Lion's Share in Bank Loans

An indication of the gross underestimation of the Bank loans to the Directors and their companies is revealed by a compilation of the data regarding the bank loans and advances for the year 1966. The total bank credit for this year stood at nearly Rs. 2432 crores. This amount was shared by nearly 9 lakh accounts. A break-up of the bank loans and advances for this year indicates that out of this Rs. 1800 crores were lent to nearly four thousand accounts only. It has also been brought out that in June 196, 572 borrowers in the entire banking system were extended nearly Rs. 1400 crores out of the bank credit of nearly Rs. 1800 crores given for industrial and commercial purposes to the big borrowers. This means that nearly two-thirds of the total bank credit was obtained under less than six-hundred accounts in the country which formed a fraction of the total borrowers.

If the five to six hundred accounts were to be identified by industrial and business houses one would find that the number of borrowers are in fact only four or five and also those only who enjoy control over the largest banks of the country. Thus the figure of Rs. 292 crores as debt due from the Bank directors and their Companies reflects less than one fourth of the financial consideration that has been actually shown to the Banks[4].

Another indicator of the phenomena of `back scratching' is evident from the extent of mutual accommodation of the Big houses while appointing Directors over the Bank Management Boards. Even a cursory glance at the composition of the Boards of Directors of the five largest banks would show that the bank managements are closely interlinked with one another through different members of the same family holding Directorships in three or four, out of the five largest banks. For instance, the four member of one family held on Bank Directorship each in the Punjab National Bank, the United Commercial Bank,

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4. The Minister for Planning, Shri Asoka Mehta while delivering convocation Address at Saugar on 4th Feb., 1996 said: "Broadly speaking about 650 accounts in this country constitute roughly two-thirds of the total advances of the banking system".

the bank of India and the Bank of Baroda. Similarly, the Birlas held directorships on two Banks, viz., the Bank of Baroda and the United Commercial Bank. Apart from the interlinks through family members the close links within the banking sector have often been seen through the non-family group-members also. Another interesting feature of the Bank Directorships is that there are very few changes in the composition of the Bank Directors overtime. In a rare case where a Bank Director did not continue for another term, it is not abnormal that the same individual was accommodated in one of the other Banks or some other companies[5]. The hold of a family on a Bank is unfortunate and it creates problem of its own but when a group of families control all the major Banks jointly very serious implications are bound to follow.

Bank Credit For Industry and Commerce

Thirdly,the close links between industry and banking institutions are also indicated in the pattern of bank advances. For instance, out of the bank credit of Rs. 2097.7 crores for the year 1965, an amount of Rs. 1287.3 crores was extended for industrial purposes and another Rs. 536.8 crores for commerce. In other words, nearly 87 per cent of the bank credit was utilised for purposes of industry and commerce. Since 1950, the beginning of the Indian planning era and the time from when onward the banking business in India started growing at a fast rate, the pattern of bank loans has changed in such a manner that larger and larger share of the total bank credit is being directed to support industrial and commercial activities. For instance, in the year 1953 (September) the total loans for industrial purposes stood at Rs. 182.39 crores only against the sum of Rs. 1287.3 crores in 1965. This is an increase of 6 to 7 times whereas the total bank advances had increased by a little over 4 times only. As a result one notices that the industrial loans which comprised nearly 36.4 of the bank credit in 1953 accounted for 61.5 per cent in 1965. The trend in bank loans extended for agricultural purposes was absolutely to the contrary. In 1953 (September) agricultural loans stood at Rs. 19.01 crores whereas the amount was Rs. 3.9 crores only for the year 1965. Not only the amount of absolute loan for agriculture had come down to one fourth of what it was in 1953 but more significant is the fact that the share of the agricultural loans in total bank credit declined from 3.8 per cent to its nearly one-twentieth i.e. 0.2 per cent only.

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5. This becomes unavoidable as no one can hold Directorships in two Banks: and also holding of very large member of Directorships of companies does not find favour with Government.

Table - XI

Showing Debts due by Companies or Firms in which Directors of the Bank are Interested

(Rs. in crores)

Year	All Banks	Scheduled Banks	S.B.I.	Other Indian Banks	Foreign Banks	Non-Scheduled Banks	Five Banks
1	2	3	4	5	6	7	8
1954	-	55.83	18.31	31.83	5.69	-	-
1955	52.35	51.19	15.13	31.04	6.80	1.16	-
1956	66.50	65.63	20.85	36.76	8.02	6.87	-
1957	103.14	102.41	39.44	54.20	8.95	0.73	-
1958	109.57	108.99	51.03	50.57	7.39	0.59	-
1959	110.13	109.52	43.79	56.60	9.67	0.61	-
1960	142.13	141.96	63.17	68.11	10.70	0.15	-
1961	156.30	155.92	67.81	72.92	14.19	0.38	51.96
1962	183.68	183.47	72.81	96.81	13.85	0.21	73.90
1964	228.57	228.35	29.43	111.89	13.39	0.22	-
1965	290.90	290.87	126.36	135.07	13.89	0.90	-

Source: R.B.I.: Statistics Tables Relating to Banks in India, 1955 to 1965.

Bank Credit and Plan Priorities

From the above account it is obvious that the bank credit in India is being increasingly directed for industrial and commercial activities in the country; and out of the industrial loans a lion's share is claimed by a few industrial Houses. Further, the tendency of increasing dominance of few houses in bank credit is on the increase. One can safely make a generalization that the banks have become instruments of mobilizing community savings for the growth of a few big industrial houses. We will deal with this aspect a little later but the point to be emphasised here is that normally one would expect that the pattern of Bank loans would reflect the Plan priorities not only in its distribution to individual sectors but more so in conformity with the Plan priority industries and other social considerations. one is not sure if it was so. On the contrary it appears that bank credit has been used for a number of such industries which had the least priority under the Plans and only those few who have, due to some historical reasons, come to enjoy control over the banking institutions.

It needs to be said that the financing of industries in general and that of big industrial units is not the same thing as the `Big Industrial Houses'. Within the broad category of loans for `industrial purposes', it is often observed, that not only the resources are directed to non-priority industries but also to industries which are surely contrary to the broad social objectives -- other than `concentration of economic power'. Therefore, while considering the fact that bank loans are increasingly used for industrial purposes one must distinguish between the desirable and the undesirable industries.

Concentration in Consumer Goods Industries

Since we have said above that there can be certain industries which may run contrary to the overall national and social objectives, we may explain this a little further with reference to the consumer goods industries. It is well known that there has been a clear but recent tendency in the industrial consumer goods production to have large scale production units.

On the one hand, concentration of production in consumer goods industries leads to discourage the growth of small scale industries, and on the other, it reduces opportunities of employment since large scale production is more mechanized. Very obviously such concentration in production and industrialisation runs contrary to the social objective of ensuring maximum employment opportunities in the economy. The process is not complete here. More relevant question to be asked is whether the price charged from the consumer is higher than what could be for a similar product of small scale enterprises and in view of the advantages of economies of scale, which are available to large scale production units and what happens to the difference between the price paid by the consumer and the actual cost of production of a big industrial unit. If the pricing policy of these units was a deliberate one and was used for the purpose of mopping away surpluses in the economy, or for ploughing back the surplus resources raised in this manner, there could be some justification for such concentration in production of consumer goods. But unfortunately, surpluses obtained by this type of concentration of production in consumer goods industries do not get invested for expansion or establishment of other essential or priority industries. A very little of this price differential is ploughed back. It happens so because large enterprises have to maintain huge sales organisations. As a result the administrative and supervisory costs of distribution of these products involves 30 to 40 per cent of the gross sales. In the case of small enterprises the sales costs are very limited. Thus, what is gained by way of economies of large scale production is lost in supporting a huge administrative and distributive system by the big industrial units.

From our preceding discussion, it is evident that the private commercial banking system in our country suffers from serious structural maladies. These have thwarted a purposeful use of bank credit in the Indian economy along desired lines. On the contrary banks have led to the creation of conditions in which economic results are contrary to our planning priorities have followed.

Moreover, it has been reported that a recent official document on social control over banking contains a detailed study of India's banking system in which the following conclusions have been reached by the author:

(1) The private commercial banks have failed to attract deposits of the rural masses in spite of the fact that the rural depositor is more than willing to

take to banking habits once he comes into contact with the organised banking sector.

(2) The private commercial banks have mainly acted to drain away deposits from rural and semi-urban centres by means of fixing a low rate of interest on such disbursements.

(3) Private commercial banks have contributed an extremely small proportion of bank credit to small industry and agriculture despite the fact that 40 per cent of India's industrial production comes from small industry and 45 per cent of total national income from agriculture.

(4) There is no basis in the arguments usually given by the private banks for their failure to help small scale industry and agriculture.

(5) The new entrepreneurs whose main capital is their technical and managerial skill have been denied bank credit facilities almost completely.

(6) The use of bank credit is exclusive and highly concentrated which have led to many undesirable social consequences and conferred the benefits of public savings upon only a few persons and industrialists. Private commercial banks, by their credit policies, have added, abetted and supported social desirable activities.

(7) The support and attitudes of commercial banks in favour of certain industrial houses have vitally added to their capacity and influence to raise internal capital and secure foreign collaboration. (This has been clearly pointed out in the report of Dr. Hazari).

(8) The private commercial banks have not been guided in their credit policies and practices by any positive social objectives and the major commercial banks have been highly selective and exclusive in their credit policies.

Since the above conclusions are admittedly true, we do not wish to burden this document by presenting an analysis which would lead to the same conclusions. Hence we have deliberately avoided to include a discussion of this aspect and take the above conclusions for granted for our purpose.

Part Two

PLAN OBJECTIVES

Introduction

The basic objective of planning in India is to unleash a process of development which will raise standards of living, help to create new economic opportunities for the vast masses of the country, and lead towards the establishment of a "Socialist Society". The planning problem is basically that of utilizing more effectively the potential resources available to the community. However, the economic system of a country at a given time is the product of its broader social environments, the socio-economic institutional arrangements,values of the people and the operational goods of the State objective of plan efforts in India has been to bring about the necessary changes in the functioning of the economic system by introducing the required institutional and other reforms. It is in this context that one has to consider the question of management and control of the banking set-up which is undoubtedly a strategic institution in any economy. How can the achievement of national objectives be facilitated by introducing a change in the control and management of the banking institutions? This is a question which can be more fruitfully discussed only when the national objectives have been identified in a precise manner. With this purpose in mind an effort has been made in the following pages to identify the major objectives before the Indian economy and explain some of the recent trends in these.

I. Economic Growth

Very few objectives are amenable to as many interpretations as the expression `economic growth'. It can be measured in many ways; and each has its own purpose. Generally, however, economic growth is equated with the growth rate of national income. But rate of growth, whether it is measured in terms of national income or in terms of *per capita* incomes, not an objective in itself. All attempts at improvement of growth rates are mere means of achieving the basic objective of ameliorating the living conditions of the Indian population. Even at the cost of a little deviation from our main discussion, it would be necessary to underline that a mere talk about the achievement of higher rate of national income growth has no meaning unless it was ensured that the benefits of growth are shared by the largest numbers of the Indian people.

Therefore it is essential that the process of economic growth is also accompanied with efforts at reduction of disparities in the incomes and the wealth levels. Viewed from this angle the yardstick of economic growth is not only the growth rate of the national or *per capita* incomes but also the extent of improvements in the average living standards of the large sections of the population. It follows from this that economic growth in a country like India must necessarily be accompanied by a reduction of disparities in levels of income and wealth - or at least to ensure that these do not get aggravated.

Income Disparities

The Government's policies at reducing disparities in income levels were expected to be two pronged. Firstly, to follow such fiscal monetary and regulatory policies which would not allow the gap in income levels to widen; and secondly, to undertake upon itself the direct responsibility to provide basic amenities to the weaker sections of the community. This would have involved the pursuance of a well worked out incomes and wage policy. However, we have yet to evolve such a policy. Consequently alongwith the evolving of appropriate policies to correct imbalances it is equally, and perhaps more, important to pay attention to reform the economic system and establish such institutional arrangements which would allow the fullest utilisation of the community's resources as also would ensure against the like possibilities of exploitation by a few of the many.

For instance, the progress of land reforms has not been uniform in the States. One must admit that the programme has made significant changes in the countryside. But the progress of these efforts would have been more impressive if only due attention was given to the understanding of the purposes for which land were being suggested. Moreover, while pursuing reforms in the countryside a logical step was to evolve the corresponding policies for urban property. In the present situation one can rightly ask "why should the reforms be confined to agricultural sector alone? Why should there be a ceiling on land holdings when in the urban centres there was no ceilings on holding of property or number of houses? This has been mentioned to point out that the approach to incomes & wage policy has to be applied throughout and not confined to a part of the economy.

How far the disparities in incomes had worsened during the first decade of planning in India was brought out by the Mahalanobis Committee Report. Speaking about the urban and industrial sector it was categoric that the inequalities had grown, the reasons given were:

(a) The operation of the economic system with its criteria of credit-worthiness and security of lending and investment tends to support the large established enterprise against the small and struggling entrepreneur. The large companies and bigger enterprises have an easier access to the capital market as banks, life insurance companies, and trusts; besides individuals have a preference for investing in shares of large companies.

(b) The Government's policy during the Plan period has been responsible for the growth of the private sector and in the process specially of big companies. In addition to affording a protected market and necessary overhead facilities and maintaining a budget policy with a middle inflationary bias favourable to industry, the Government has been permitting the growth of private industry by extensive tax incentives.

(c) One of the factors accounting for an increase in economic power of the large groups in recent years have been the larger flow of foreign investment and technical know how through joint ventures.

Concentration of economic power is not objected to on non-economic considerations alone. To some extent, and in certain cases, concentration may be justified on functional grounds but the Report observes, "concentration of economic power in Private sector is more than what could be justified on functional grounds".

These observations have to be seen in the context of the Directive Principles of the Indian Constitution, one of which read, "In the economic sphere the State is to direct its policy in a manner as to secure the distribution of ownership and control of material resources of the community to subserve the common good and ensure that the operation of economic system does not result in the concentration of wealth and means of production".

In brief the objective of economic growth is not an end in itself. The basic purpose of growth in national income and per capita incomes is the improvement of living standards of the masses. Thus if there was growth in the economy accompanied by widening of the gulf between the few and the large many this cannot be considered as economic growth. Moreover, one is not sure if there can be sustained growth in any economy if the disparities do not get reduced. Even from the purely economic angle disparities are least conducive to a continuous sustained growth of any economy. As economy which has concentration of economic power is also the one which is most liable to severe fluctuations, depressions, recessions and booms. Thus, it is imperative to realize that economic growth which does not reduce disparities is neither socially desirable nor economically sound development in the long run - leave apart the political implications of such developments.

II Balanced Growth: Inter-Sectoral

Another objective in the process of planning is that of ensuring balanced growth in the economy. The concept of balanced growth can be interpreted in three ways. One, it may be interpreted to mean a balance between the rates of growth of different sectors of the economy. It does not, however, mean equal rate of growth of all sectors. For instance, for obtaining a 5 per cent rate of overall growth a few sectors may grow at the rate of 10 to 15 per cent; whereas in certain others the growth may be around 3 to 4 per cent only. The essential meaning of a balanced growth would be to ensure that the inter-sectoral balances were not disturbed since excess or lower production in one sector would lead to a number of bottlenecks which would stand in the way of a smooth and sustained rate of economic growth. To ensure this the government would have to use taxation, credit and other regulatory measures to support or discourage production in a matter that the supplies of various inputs are available in the required quantum. This is a function which cannot be left to the operations of the market forces. In some measure one is afraid that our past experience has not been a very happy one in this respect. At many a point of time shortages had created bottlenecks for production. Especially a number of plan priority industries which should have been developed had lagged behind whereas in a number of non plan industries the growth has been phenomenal.

Inter-regional

Balanced growth can also be referred to the ensuring of reductions in the inter-regional disparities over space. However, the situation that is obtained in the country to-day presents a picture of considerable disparities in levels of growth - from one State to another. (See Table I). To some extent the inter-state disparities are corrected by central Investments but unfortunately the private sector growth has tended to negate the trends towards spatial balances.

One can measure the level of economic activity in States in many ways. But no single indicator would reveal the real inter-State disparities. A broad indicator of a States level of development is provided in the State *per-capita* income estimates. (See column 2 of Table I). However, a more important indicator of the differences in levels of growth of the States would be in the study of the share of each State in the national productive capital in factory establishments. It would be seen that the two States, namely, West Bengal and Maharashtra claimed nearly two-fifths of the national productive capital in the private sector. The State of Rajasthan was the least industrialised having only one per cent share in this capital. (See column 3 of the Table I). To some extent the existence of varying shares in productive capital may be explained by the differences in State potentials. But, surely enough one cannot argue that the existing distribution of national productive capital in the private sector reflects nothing but spatial differences in potentials. For instance, from all accounts it seems clear that States like Mysore, Kerala, Andhra Pradesh and others do have considerable scope for the establishment of industries. This has also been indicated by the techno-economic surveys of the States. The real reason for development of only a few States lies in the manner in which the Indian economic system operates and is also to some extent due to historical and political factors. It would be noticed that the two States which claim two-fifths of the national productive capital in factory establishments are the States which were initially developed as centres of Commerce and Trade. And due to a variety of reasons growth of industries has followed the same spatial pattern as that of commerce and trade. One would not, however, argue that there have been deliberate attempts at developing only the States of Maharashtra and West Bengal whereas no efforts were made towards industrialization by the other States.

Table - I

Showing Indicators of Economic Activity in States in India

S. No.	States	Per capita income (Rs.) (1961-61)	% share in the Nations Productive capital in Factory Establish-ments 1963	% of Central Investment 1965-66	% of total villages Electrified 1965-66	Length of Roads per 100 K.M. 1965-66	Per Capita Bank Deposits (Rs.) 1965
1.	Andhra Pradesh	287.0	5	4.5	20	17	30.0
2.	Assam	333.3	2	2.6	1	4	22.7
3.	Bihar	220.7	13	16.0	6	14	19.3
4.	Gujarat	393.4	8	3.0	9	13	103.7
5.	Jammu & Kashmir	289.0	-	-	10	4	43.7
6.	Kerala	314.9	2	2.3	39	43	51.1
7.	Madhya Pradesh	285.3	9	20.5	2	10	21.9
8.	Madras	334.1	7	7.0	7	38	57.5
9.	Maharashtra	468.5	20	3.7	11	15	184.8
10.	Mysore	304.7	3	1.4	15	28	57.4
11.	Nagaland	-	-	-	-	-	-
12.	Orissa	276.2	7	16.5	1	9	9.3
13.	Punjab	451.3	3	1.1	25	17	78.9
14.	Rajasthan	267.4	1	0.5	4	8	23.2
15.	Uttar Pradesh	297.3	5	6.4	9	14	28.8
16.	West Bengal	464.6	20	14.5	5	30	115.8
17.	All States	334.5	100	100.0	10	17	64.2

Source: Col. 2 - National Council of Applied Economic Research.
Col. 3 - Annual Survey of Industries.
Col. 4 - Planning Commission.
Col. 5 - Planning Commission.
Col. 6 - Planning Commission.
Col. 7 - Reserve Bank of India Ltd.

In our opinion the main reason for this unbalanced growth of regions in the country has been the functioning of our economic system which contributes towards the growth of such areas which are already better developed against those which are poorer. A similar pattern of distribution was noticed regarding the growth of banking institutions. Part One of this study indicates as to how the operations of the banking system in India have led to movement of nearly Rs. 390 crores from the poorer States to the three States, namely, Maharashtra, West Bengal and Madras. Since banking set-up is an important and potent part of the economic system it is no surprise that the operation of the overall economic system has helped the growth of certain States at a faster rate than the others. While the strategic institutions are allowed to operate as they do now, there can be little hope for inter-regional balances or for attempts at reductions in the interstate levels of economic activity and growth rates. (See Table I).

To some extent the Central public sector plan investments can attempt to correct such inter-regional imbalances. However, in the initial stages of economic development the location of Central Plan projects has to be more on considerations of immediate economic advantages than other social objectives. Therefore, the central outlay can be used for this purpose in a limited manner only. We would not even for a moment suggest that the plan investments should not be used as an instrument for ensuring greater inter-state balances, wherever it can be done it should be only too welcome. On the other hand it is a well known fact that a large many medium scale industrial units and 'foot loose' industries can be established in places which do not have minerals or other basic materials but have abundance of surplus labour supply -- which is an important resource. The point to be emphasized is that left to the existing economic system as such there can be little hope of development for the depressed areas. It is so because the level of underdevelopment is in itself a great handicap for the poorer States. Therefore, it has to be recognised that a number of institutional reforms are a basic prerequisite to the attainment of spatial balances in the country.

III. Self Reliance and Foreign Exchange

Another objective before the Indian economy is the conservation and enhancement of foreign exchange resources -- both by judicious use of the foreign exchange for purposes of development of strategic and basic industries and also by making every effort at stepping up of exports. The purpose of being careful in the use of foreign exchange is to ensure that the Indian economy reaches a state, as early as possible, from where onwards its normal growth would not remain heavily dependent upon the assistance of the outside world. We are conscious that many a time the interpretation of the objective of `self-reliance' is stretched too far. Some have entertained ideas that self-reliance would mean being self sufficient in all matters-social, economic and political. For them the concept of self-reliance is another form of isolation from the rest of the world. But the purpose, which we have in mind, is a limited one we do not visualize that India can be or it need to be self-sufficient in all respects. We visualize that India's overall trade transactions would get enlarged and India would become an important country from its exports view point as also it would continue to import goods from abroad.

Exports

But the relevant question would be: Why with all the developments in industrial sector has not India become an exporter uptil now? The answer to this lies in three factors, viz, (i) failure of the Indian industrialists to compete in the world market because of their high cost of production (ii) lack of attempts on the part of the Indian exporters to win confidence of the foreign countries by maintenance of better uniform standards of their products, and (iii) absence of any economic pressures and challenges which would force the Indian industrialists to go in search of markets abroad. The three factors are not independent of each other. The basic reason for these has been the existence of seller's market for too long a period accompanied by a variety of subsidies and the pursuance of fiscal and regulatory policies which have discouraged imports and created conditions of an extremely sheltered market for the local industrialists. This question is again closely related to the manner in which the newly established industries were provided conditions for the emergence of monopolies. Many a time licence was given to an industry because it was expected that it would boost up Indian exports. But once the licence was granted, imports of machines and raw material allowed and collaborations arranged, these very industrialists came forward with the plea that the Indian products cannot be exported because they cannot compete in the world market. And therefore, industries which were established with the clear understanding that the bulk of their product would be exported, divert their produce to the home market -- which is only too ready to absorb anything that is available and were no other foreign competitors would be allowed to threaten the monopoly privileges of the so called `national' enterprise.

As far as the lack of efforts at maintaining standards of quality of the industrial products is concerned, this is a hypothetical question in a `sellers market'. Very rightly, as long as there was excess demand to what can be met by the local producers the immediate problem of any rational producer would be to maximise profits by reducing his immediate costs and in this he is only too easily tempted to do his job in a half-baked manner as also charging the highest price that he can. Where does come the question of consumer satisfaction? Or for that matter, where was the threat to his sales? And under these conditions it would be only an idealist or an unintelligent person who would harp on maintenance of quality or reasonable prices. Thus, the question of Indian producers having failed to evolve their standards of quality is only of academic value. The reality of life is too hard to be fully appreciated; and that is that in a monopoly situation the consumer satisfaction or attempts to reduce costs of production remains an unreal question. Similarly, one may ask: Why should the Indian industrialists go abroad for securing new markets when they have the exclusive rights of sales, to their full capacity production, within the economy?

Imports Substitution

On the other hand one has to ask: "Why India imports so many goods both consumer goods and producer goods? One can understand the need to import such commodities which are not produced in sufficient quantity within the country. For instance, foodgrain imports may be justified for short periods. But why have continued food imports? It is not for us to discuss the question of food here; and therefore, much against the temptation to do so we would raise another specific question i.e., "Why do the consumers as well as the producers -- the big as well as the small-prefer imported commodities, from any luxury item like lipsticks to imported cars and machines? Leaving aside the import of machines which are not produced within the country why should even an average man consider imported products as superior to the home made ones. have we as Indians lost all the national pride? The answer to this is not in lack of sentiments but in the lack of faith in the quality of goods produced by the Indian industries. This again brings us to the question of the lack of efforts by the Indian industrialists at maintaining certain uniform standards.

In this respect the responsibility has to be shared equally by the Government as well as by the industrialists. The government's failure has been in not enforcing -- more so where the monopolies exist--the minimum standards for their products. For example, how much deterioration had taken place in a commodity like automobiles--which is used by the most vocal and influential strata of the Indian society--is too well known. We hope the Committee appointed to go into the causes responsible for worsening of the quality of cars would indicate how far the existence of monopolies, and inability of the government to control them, alongwith the prevalence of sellers market has been responsible for this deterioration. The basic point in referring to this to underline that no amount of moral persuasions can prove of any use unless the government took active and continuing interest to impose conditions of quality maintenance and consumer satisfaction. For doing this the government has the obligation to the society, since a large amount of foreign exchange resources were made available to such units by denying the average citizen the rights to import goods from outside. The allotment of foreign exchange to industrial concerns had become possible only when someone else was denied its use. Thus the grant of a licence is not only a social sanction but is also accompanied with a privilege and economic benefit for availing the scarce resources of the society. This sanction was provided by the government; and in return it was an obligation to ensure that the sanction was not used against the broader interests of the society.

A very closely connected question with the low-efficiency of the industrial sector in India has been the fact that the so called industrial entrepreneurs have not made any efforts to achieve specialisation in one type of activity. On the contrary each big industrial house has attempted to enter as many industries as it was capable of. For instance, Dr. R.K. Hazari had pointed out in his Interim Report that the Birlas had entered practically all types of industrial enterprises which included textiles, aluminium, electrical goods, chemicals, cement, a man-made fibre and yarn, heavy engineering, timber products, news print, sugar, vanaspati and so on. Very obviously one industrial house could not have developed specialisation--within such a short period--in all such industries. The diffusion itself is a contra indication that it is impossible to develop expertise on such huge scale. And yet the fact remains that the government did grant licences to the Birlas. The real reason for this lies in their capacity to muster a substantial financial support to all proposals irrespective of the merits. The finance, however, it would be readily agreed have not been out of the savings or profits of these big industrial houses. Basically, the finance become available because each one of the Big Houses in India controls one or two large banking institutions.

In brief, one would say that the objectives of achieving self-reliance are very closely dependent upon the way the industries are managed and the manner in which, these are regulated to become conscious of the necessity of reducing their cost structure as also in maintaining--leave apart improving--the standards of quality to win confidence of the foreign and Indian buyers. It is only then that India can hope to step up her exports and earn foreign exchange which in turn would allow us to accelerate the pace of our movement towards industrialisation and self sufficiency.

In summing up one would say that the three national and plan objective before the nation are: (i) to ensure steady, continuous rate of improvement in the living standards of large many; (ii) to achieve and ensure that economic growth is not accompanied by widening of disparities--inter-state and intro-personal; and (iii) to ensure that the growth of the economy is on such lines which would enable India to reach a stage, as early as possible, from where onwards its growth would not remain heavily dependent upon the foreign assistance.

These three objectives are complementary to one another. The realisation would obviously depend upon the pursuits of such policies which would help to reorganise the present economic structure and develop it along lines which would ensure the fulfilment of these objectives.

Evidently, the financial system of the country, specially the private commercial banking system had to be devoted a great deal of attention from the point of view of realising the above objectives. However, we have seen that while the country has already completed three Five Year Plans, there has been no provision for any type of credit planning in the Indian economy. The Indian plans, while laying down various targets for development programmes have not simultaneously realised the need for allocations of appropriate bank finance for different projects, in the public and private sectors. Since the Government financing of development projects has been confined only to the resources of the State with no efforts at the regulation of bank credit in plan directions, it has often happened that private commercial banks have financed industrial projects which have enjoyed either a low priority in the plans or are outside the plans. Moreover, in extent to which such projects have been financed has been out of all proportion to the needs of the economy or the patterns of demand for these industrial products, which have already emerged in the economic system. In this way, the commercial bank finance has tended to be working against the plan priorities and helping to create imbalances in the growth of the economy from time to time. These aspects of the working of the private commercial banking system have already been documented in a number of Government publication and the First Five Year Plans.

Of course, it is well-known that the banks have financed largely those projects for which licences have been given essentially because the private industrialists have been able to claim the availability of bank finance for financing their projects. Thus licensing of industries and their financing with bank credit have both been enterprised in a vicious circle which have to give help to deflect the course of India's plan development from its expected national priorities, and it is high time that we take necessary steps to break this vicious circle lest it may lead to the end of all plan development of the economy in the future.

Part Three
RESOURCE MOBILIZATION

Three basic truth regarding under-development of countries is the absence of adequate productive capital, -- physical and human. And therefore, all efforts at planning are in essence directed towards the creation of the capital of both types. It is only when the human and physical capital is developed in a harmonious and systematic manner that a country can ensure a rapid sustained and balanced rate of growth. In this effort a country may depend upon foreign capital or mainly rely upon its own capacity to mobilise resources. There is no given rule about the manner of building up national capital. For instance the American development in its early phases was greatly facilitated by the import of human and other capital from the European countries; and the most recent example is that of Israel where foreign capital played a very significant role. On the other hand countries like U.S.S.R. and China have mainly depended upon their own resources.

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How fast an economy can grow is determined by the rate at which the productive capital is built up. And the rate of capital built up is determined by two factors, *viz.* the rate of internal savings and the magnitude and nature of foreign assistance. Whatever may be the extent of foreign assistance the entire cost of growth in any case cannot be borne by the outside world. The two factors are not substitutes for one another. In any case it is necessary to raise corresponding internal physical and financial resources despite all foreign assistance. The situation is simply this: the more efforts a nation is prepared to put in, more countries can be found willing to help. A country which is not prepared to put in her own efforts at development can hardly expect other nations to foot the entire bill of development. In fact, one can even go to the extent of saying that the rate of savings in a community would determine its overall rate of investments and that in turn will determine the rate of economic growth. Therefore, the stepping up of the savings rates is of crucial significance for the growth of a country.

The rate of savings in a country depends upon the extent to which the country is prepared to, willingly or unwillingly, reduce its aggregate consumption. A higher rate of savings would enable higher investments and thereby additional incomes in the subsequent years. Again, the additional incomes generated may be largely saved or go to improve the level of consumption. But greater the willingness on the part of an economy to `tighten the belt' higher would be the rate of capital accumulation. This is what one calls as the sacrifice of the society for its own growth. Normally the, term `savings' indicates voluntary savings of the individuals. But in the context of national savings one has to take account of the voluntary savings of the individuals and other private agencies as also the compulsory savings affected through tax mobilisation for investment and the surpluses of the public enterprises which have been ploughed back for creating additional capital. Under the voluntary saving one may include savings in the form of bank deposits, personal cash hoardings, purchase of shares of the corporate sector and other investments and loans made to the public and private agencies. While compulsory savings would be that part of the public sector and government expenditure which is diverted for productive purposes.

Compulsory Savings

The extent of compulsory savings is very much dependent upon the extent to which governmental agencies can pursue policies of resource mobilization by (i) enhancing the rates of taxation, (ii) widening the coverage of taxable population or (iii) follow such pricing policies in the public enterprises which would yield the requisite surpluses. It need to be recognised at the very beginning in a democratic set up like ours imposition of fresh taxes etc. is not as easy as it could be in a society under some other political system. There are limits within which the government efforts have to be confined. Moreover, the taxation structure cannot be used with as much of intensity as it can be in a developed economy to raise resources. For instance, too high taxation measures can lead to some un-economic efforts e.g., discouragement to new enterprise and incentives. However, it does not mean that under-developed countries always exhaust all revenue collections. For instance, in India it would be only a fool hardy scholar who would argue that the taxable capacity of all sections of the Indian economy have been fully harnessed.

It is, however, true that in underdeveloped economies there are limits beyond which direct taxation cannot be introduced without discouraging the level of investments in the private sector. At the same time if more reliance was placed on indirect taxes the problem comes that of excessive economic sacrifice imposed upon the poorer sections of the community. Thus in an underdeveloped economy the use of direct and indirect taxes has its own limitations. This would, therefore, require a very careful and judicious view, on the part of the Government, regarding the emphasis that it may place on other sources of revenue.

In the field of compulsory savings we would like to make a special mention of the role of public sector enterprises. Fortunately enough it is by now well recognised that the public sector has a special place in the underdeveloped economies. Specially the Public sector enterprises are a necessity in such field where private enterprise does not enter because the magnitude of investments involved are very high, the gestation period is large or the expectations of return on investments are not directly remunerative as against the amounts of investment. Therefore, in such areas the role of public sector enterprises is well appreciated even by the most conservative economists. It is agreed that the public enterprises have a special place in furthering the overall rate of economic growth of a country by providing the economic and social overheads and thereby facilitating the growth of many large private enterprises. For this purpose the public enterprises have to directly enter into the productive system of the economies. It is in this regard that the public enterprises in India have come to occupy a significant role in the development of the country. Thus, the importance of public sector in the development process is not disputed. For example, in the post world war-II period the French economy took over a large part of the national capital under ownership and control.

The controversy arises around the question whether or not the public enterprises should follow similar policies in their functioning as does the private sector. One view is that public sector enterprises should function on no-profit no-loss basis. It is suggested that the attempt should be to help the growth of the private sector by providing all the necessary requisite infrastructure for helping them to overcome such difficulties which individually no private enterprise can meet. In this concept we would like to make it clear that the role of the public enterprises should not be viewed as mere promoters of the private sector. In a developing economy, the public sector enterprises have a very direct role other than what is generally to be the case, in resources mobilization and the direction of development. In the Indian economy the public enterprises should certainly be used as an instrument of resource mobilisation and for providing a sense of direction in the planned process of growth.

There is a difference between the profits of a private enterprise and that of a public sector enterprise. The distinction is that the surpluses of the public sector enterprises become available to the Government and the public agencies and decisions on the use of such resources are directly governed by social and economic considerations of the economy as a whole. The profits of the private enterprises are mainly directed and regulated in a manner which depends on an individuals' opinion about a profitable investment. In a developing society like ours, the surpluses of the public sector should in fact be viewed as Compulsory Savings of the society which would go for further the build up of the national capital--and the capital build-up on the lines which would be in accordance with the plan priorities and overall social objectives.

Voluntary Savings

The Voluntary Savings in a society take various forms. The important organised forms are i) Deposits with the Commercial Banking institutions; ii) Life Insurance Policies; iii) General Insurance; iv) Post Office Savings Deposits; v) Government Bonds and Certificates; vi) Deposits with Cooperatives, and vii) Cash hoardings.

The relative importance of each one of these is broadly indicated in Table II. The

Table has been compiled to indicate a very broad comparison of the different forms of savings in the community. The data is not strictly comparable as it relates to different periods of time as also the types of the data referred to are not identical.

Table - II

Showing a Broad Comparison of the Forms of Voluntary Savings

S.No.	Agency	Remarks	Rs. Crores
	1	2	3
1.	Commercial Banks	Deposits (1965)	3,049.0
2.	Life Insurance Corporation	Investments (1964 March)	763.5
3.	General Insurance	Assets (1963)	90.2
4.	Post Office	Deposits (1965)	555.6
5.	Government Banks & Certificates	Outstanding (1965-66)	449.8
6.	Cooperative Societies	Deposits of Individuals (1964-65)	303.0

Out of the above mentioned organised financial institutions, the Commercial Banks are the most important ones. Also, except for the banks, the other institutions cannot be considered as primarily and wholly the financial agencies. The resources collected by agencies like the Post Offices and Life Insurance Corporation are incidental to their other operations. Therefore, while discussing voluntary savings, one has to place special reliance on banking institutions. it is so because the banks are organised with the basic purpose of mobilising financial resources and for providing credit to the economic functionaries of a society.

Banking Institutions

The magnitude of resource mobilisation by banking institutions is related to the capacity of these institutions to reach numbers and their success and efficiency in looking after their clientele. For instance, if the banking offices were confirmed to a few centres of the country only, very naturally, the capacity of the banks to mobilise deposits from the public would remain limited to that extent. And if the network of banking offices was extended to all parts of the country and most of the population could reach one or the other bank office conveniently the deposits would be of a larger order. Similarly, if the banking institutions functioned efficiently and made rigorous efforts to provide satisfaction to the savers --irrespective of the fact how big were the deposits of a saver--the banks could still improve their effectiveness in deposit collections. In a developing economy banking institutions have a special role in making people `bank minded'. For a large majority of those who can save opening of an account in a bank would be a new experience. And therefore utmost care would need be taken in seeing to it that the experience is not so unfortunate that an average saver would decide to never visit a bank office again. If a visit to a bank office could be made a pleasant experience the banks would become still better institutions of deposit mobilisation.

This aspect needs to be underlined since very often it is not realised that in underdeveloped economies the savers are not as enlightened as to always bother to look into the economies of returns of their savings. Their values and decisions are dependent upon, at least equally, on considerations other than the interest rates. And one of the important factor is the security of definite and the personalised service and the consideration they would receive from the bank staff. The importance of enhancing savings may not be fully appreciated by an ordinary man. For this one can only say that if the banks can draw out financial surpluses from the community--by way of the deposits--to that extent the buying power in the community gets contracted. And by that magnitude there is a reduction in the aggregate consumption with a corresponding release of physical resources which can be diverted towards the creation of additional national capital. Similarly, by practising selected credit policies the banks can influence the consumption pattern in the society. The banks are important agencies for ensuring greater savings to help economic development.

The capacity and will to save on the part of the savers is not in itself sufficient to ensure deposits. What is equally important is the existence of an institutional framework which makes it convenient to save. One has no measure to assess the level of willingness but it would not be too wrong to presume that everyone, whether rich or poor, would have a desire to save. The degree of will power would, however, vary from one individual to another. In a country which recognises private property and rights to inheritance an average man would undoubtedly like to save. But the real problem is that of impressing upon the savers that the function of saving was also a national obligation and each person must save by habit and in an organised manner.

The task of making `savings' conscious is only possible if there was an institutional framework which would undertake this task vigorously and continuously. And further to this the set up must ensure the necessary physical and organisational conveniences to the savers. It is in this context that one has to evaluate the capacity of the existing financial structure as instruments of enhancing and further mobilization of savings.

In Part One of this study it has been pointed out that the commercial banking in India has remained concentrated in urban centres and also in the comparatively advanced states of the country. It would not be correct to form an impression that banking offices are evenly spread over space within the urban centres or in the comparatively better off States. A study of the spatial distribution of banking offices in these cities would indicate that a very large number of offices were located in the two cities of Bombay and Calcutta whereas the smaller towns and rural areas were as badly neglected as in any other State. Furthermore, a look at the distribution of bank offices in these cities would indicate that more bank offices are located in such areas of the two cities which are trade centres or are inhabited by richer sections of the urban population. Very rarely bank offices are located in areas where the poorer sections of the community live.

From the view point of savings potential it would be appropriate to mention the general belief that the poorer sections in the Indian society have very little savings capacity is completely misplaced. In fact the savings with the lower income groups in the urban centres--which will equal the middle income groups of the rural population--are of a significant order. While the middle income groups enter into a race for consumption of `prestige goods' and become victims of the `demonstration effect' and have lesser savings willingness to save in the lower-income groups are still conservative and do effect savings. Considering the numbers involved even small saving when aggregated would come to a fairly significant order. There is no doubt that dealing with very small amounts and with large numbers of comparatively lesser educated depositors would involve higher costs of administration of these bank offices. The same is true about rural areas. But the benefits of such savings are many times more than the costs of deposit collections. But this approach can only be followed by such institutions which have the proper perspective of their role and are even prepared to bear short term promotional losses in the overall and long term interests of the society.

Rural Banking

For a long time the official view regarding the provision of banking facilities to the rural areas has been that extension of banking facilities to the rural sector should be earmarked for the cooperatives and urban banking should be largely left for the commercial banks. While nationalising the Imperial Bank of India, it also argued that the private commercial banks cannot reach the villages because opening of branches in the rural areas was not a profitable proposition. It was, therefore, suggested that with the nationalisation of the Imperial Bank, the State Bank of India would have special responsibility to provide banking facilities in smaller towns and villages. Thus, the official attitude seems to have been that the State Bank of India and the cooperatives would specialise in rural banking and the private commercial banks would confine their activities to the urban centres.

The implication of this division of areas between the public sector banking (State Bank of India) and the cooperatives *vis-a-vis* the private commercial banks is that the non-profitable banking should be the main responsibility of the public sector institutions whereas the profitable ones should be earmarked for private banking institutions. It is recognised that since rural banking is not a profitable business (and that is why private banks do not attempt this) therefore, the cooperatives and the State Bank of India have to be adequately subsidised for such bank offices which run under loss and were opened with the intention of covering rural area. For this, the Reserve Bank of India meets the deficit of a branch opened by the State Bank of India.

Such an approach would be all right if it was clearly understood that the cooperatives and the public sector banks were not to be judged on the same criteria as the other commercial banking institutions. The public sector banking institutions may, therefore, be judged on different standards than the private ones. But unfortunately it is argued that private banks do not want to go to rural areas because it was not profitable and therefore the public sector (State Bank of India) should undertake the responsibility of entering into the losing business. In the same breath it is also expected that the State Bank should show at least the same profits as other private banks. This really means that the non-profitable propositions are meant for the public sector and the profitable ones for the private sector. And then we turn bank to judge the efficiency on private profit criteria. No logic could be strange than this.

Cooperative Societies

As for the role of co-operatives in rural banking is concerned, it is high time that we understood what the cooperatives can do and what these cannot. We must understand the structural handicaps of the cooperative credit system in an economy like ours. It is only after a proper appreciation of the capacity of the cooperatives that one can decide as to how far the cooperatives can offer a solution to the problem of providing banking facilities in the rural areas.

It should, however, be made clear that we do not doubt the importance and the role that cooperatives in ameliorating the economic and social conditions of the rural areas in general and the farmers in particular. Basically, the cooperatives movement is a sound one and has many a merit. For instance, agricultural, marketing, service, industrial and consumers' cooperatives are of great significance in a developing society like ours. However, the need for opening of bank offices in rural areas is not purely the provision of credit to agriculture. It is more than this. In this respect that we need to understand some of the structural and other inherent limitations of the cooperative credit societies. Also one has to take due note of the present defects in the cooperative movement. No doubt some of the defects in the cooperative credit movement can be set right with appropriate reforms. But, the inherent limitations of this movement for purposes of extending banking facilities to rural areas can hardly be met by such actions. At the same time we visualise that opening of branches of the organised banking institutions in rural areas would help to strengthen the cooperative credit movement in the country side. The existence of organised banking is not a substitute or a rival development to cooperative credit societies. On the other hand, in our view organised banking is a complementary and a pre-requisite for effective functioning of the cooperative credit institutions.

In principle the credit cooperative societies need not necessarily be dependent upon the governmental finance alone. The objective of establishing cooperatives in India, as also anywhere else in the world, is to bring the various economic functionaries together for mutual help. For instance, credit societies, it was expected, would receive deposits from those of their members who had surplus resources, and in turn, these resources would be lent to those who need financial assistance. In this manner, the cooperatives could eliminate the money lenders who discharged this function of receiving deposits and lending credit to the farmers. In this manner the cooperatives could provide a system of mutual help and eliminate the exploitation of the private moneylenders. The cooperatives, viewed from this angle, are an institutional reform where intermediaries are attempted to be eliminated. This is the spirit of cooperative movement. In the initial stages, the Government and other public institutions could provide financial assistance to the cooperatives if the requirements of the members of the cooperatives were more than what the cooperatives could raise from their own members. But unfortunately, in India cooperative credit movement has come to a stay as heavily dependent upon the governmental finance. It is evident from the fact that out of a total working capital of the cooperative credit institutions of Rs. 2101.44 crores in 1963-64, nearly Rs. 500 crores was the share capital and resources. The deposits from its members and other stood at Rs. 303.40 crores only. The rest was provided by the Reserve Bank of India, by the Government and other public institutions. Since the credit cooperating societies have not succeeded in resource mobilisation from their members or otherwise, these have remained instruments of one way flow of finance--from the Government to the members of these cooperatives. Thus the credit cooperatives are in practice only credit distributing agencies. No doubt this is an important function in itself. But this certainly is not banking for rural areas.

The cooperative movement has been heavily subsidised by way of cheap and easy credit by the Reserve Bank of India. Because of this most of the cooperatives were organised by those only who wanted to avail of the governmental financial assistance. Right from the beginning the objective of organising cooperative credit societies was to avail facilities rather than to become a forum to local farmers and other ruralities for mutual help. Secondly, the cooperative societies being each independent of the other has to function in isolation and therefore these societies cannot offer the normal banking facilities which an organised bank can. Due to this handicap, very naturally the depositors prefer to maintain their surplus either with the moneylenders or hoard the amounts in cash with them than handing over the same to a local cooperative credit society which cannot allow similar and easy withdrawal facilities as a private moneylender can. Of course provision of other banking facilities like transfer of funds from one place to another and safe deposit facilities are out of question. Therefore, the depositors are not encouraged to use the cooperative credit societies as institutions where they can deposit their surplus financial resources. Also, because of the advantages offered and the considerable subsidy element, the membership of the cooperatives (which is true about all types of cooperatives) is taken to be closed for others and is confined to a small section of the population of a village. A number of studies conducted by the Reserve Bank of India and other scholars on the working of the cooperative credit societies indicate that majority of the cooperatives can hardly be described as genuine cooperative societies. These are either group organisations or family organisations. A study of the Central Cooperative Banks would also indicate that the control and management of the cooperative finance is generally in the hands of a family or a group of persons and the functioning of the cooperative banks is not much at variance from any other private financial institution.

Even as credit distributing agencies the cooperatives have not made the desired impact. The main reason for this has been the unwillingness on the part of the cooperatives to depart from the credit-worthiness criteria for extending financial accommodation. As a result of this cooperative credit has been availed by those only who could even otherwise raise capital of their own if they chose to do so. A study of the cooperative credit distribution would indicate that a large share of total credit has gone to a fraction of the population comprising of big landlords and so on. This to some is unavoidable in a society whose membership comprises of a heterogeneous group with a few dominating the decisions and functioning of the society. There cannot be any meaningful cooperation between the unequals. The situation can, however, be better dealt with by such organised agencies which are independent of local and vested interest and would function on considerations of merit, not always, and only based on the conventional criteria of credit worthiness of a borrower.

Another structural defect of the cooperatives, mainly dealing with farmers is that a good part of the financial resources remain idle during the year. For instance credit needs of the farmers are the most in the sowing seasons and the pre-harvest periods. The loan recoveries are made after the harvest. Since there is time gap between the sowing and harvesting seasons, during the middle periods the finances of the cooperatives cannot but be idle. However, the requirements of the agricultural trade and processing industries are the most in the post-harvest period. But because of the absence of any institutional mutual arrangements the idle resources of the cooperatives do not become available for the latter purposes. This cannot be helped if the cooperatives remain in isolation of the organised banking structure.

The net result of the division of responsibility between the private commercial banks and the Reserve Bank of India in financing of industry and trade on the one hand and agriculture on the other respectively has been a fragmentation of India's financial system into two water tight compartments. The private commercial banking system operates in unplanned isolation from the needs of the rural sector while the cooperative banking system finances agriculture without any coordination with the needs of the Industrial and urban sectors. The inevitable economic consequence is that there is misallocation of financial resources between the two sectors. This comes about because the funds earmarked for the rural sector remain idle for a major part of the year while the idle funds of the private commercial system during the lean period cannot be utilised for short term financing of the agricultural operations. Inevitably, too much finance is thus tied up merely because the financial system is fragmented into these two broad divisions.

If the private banking system was to be nationalised, it would be possible for the Government to integrate the financial system of the country into one complete whole. This would help to save idle resources of both financing sectors as well as help to coordinate and integrate their financing operations into a system of planned development. Moreover, the skilled personnel of the cooperative financial sector as well as of the private commercial banks can be integrated with one another in order to provide a much large cadre of trained personnel in banking operations of the country.

Such integration of two major financing sectors in the country would also help to curb the flow of financial resources into the unorganised money market which plays havoc with the economy in the present situation of acute scarcities and shortages. Once the two financing sectors, that is the private commercial banks and the cooperative sector are integrated, they would constitute a major source of attraction for all voluntary savings of the community in so far as they would reach out to all the areas of the country from the highest to the lowest range of society, and provide the best security for the deposits of all savers, big or small.

Moreover, in the presence of such a unified financial system the unorganised money market would lose much of its attraction and concealed power to engage any financing operations which will be beyond the purview of the organised financial system. Let us not imagine that the unorganised money market in the country operates entirely outside the banking system. There are strategic points of linkage, between the unorganised money market and the banking system. These linkages would come to full view once the banking system is fully unified under the State control, and it will be easy to keep a watch and regulate the activities of the unorganised money market far more effectively than has been possible hitherto.

Rural Savings Potential

Sometimes one also hears that there was very little surplus resource potential in the rural sector which could be tapped by the Banks. But the facts do not bear testimony of such a belief. For instance, the amount of deposits which the post offices have increased during he last 15 years significantly. We are conscious that the post office bank savings are not a substitute for banking. This is only an indicator of the potential resources which can be mobilised from the lower income strata and the rural communities. In the year 1950-51 the total post office saving bank deposits stood at Rs. 187.28 crores whereas in 1965-66 the figure touched Rs. 641.2 crores. The receipts for the year were Rs. 173 in 1956-57 and the corresponding receipts of the post office saving bank deposits were Rs. 366.27 crores. Similarly, the rate at which small savings have grown as indicated by the number of saving bank accounts with the Commercial banks and also the share of small savings in total bank deposits is an indicator that the small amounts are not really small if only these could be tapped properly.

In Part One it has been seen that the intensity of banking varies from State to State. In some States there is a bank office for more than 2½ lakh population whereas in a few others a bank office exists for less than half lakh of population. The magnitude of *per-capita* bank deposits also varies from one State to another. The highest per capita deposits being nearly Rs. 185 and the lowest being Rs. 9. This variation could be explained to some extent in the differences in per capita incomes in States. But essentially the lower per-capita deposits are because of the absence of banking facilities. This is evident from Table-III in Part One. It would be seen that there was a very high degree of co-relationship between the degree of concentration of banking facilities and the per-capita bank deposits. Those States which have a bank for 40 to 50 thousand people are the States where per capita bank deposits are the largest. We do no believe that what hold true about the States where banking facilities have been extended would not hold true about the States where banking is absent. The non-development of banking in the States has undoubtedly meant lesser deposits mobilisation for the community. And if the national objectives are to enhance savings it is necessary that the banking institutions were more evenly distributed than what these are today.

The savings potential of the rural sector can be appreciated only if one takes into account the level of inequalities in the agricultural sector. Howsoever unfortunate it may be, but one has to recognise the existence of considerable disparities in land holdings--which is the source of incomes--in the rural sector. One can broadly group the agriculturists under two broad categories viz. the ones which would have agricultural produce for the market after meeting their own requirements and those who are just on subsistence level. In numbers the former category in much smaller but the agricultural land with them constitutes a very large part. There are, however, variations from State to State. The agricultural classes which produce for the market have been at a considerable advantage because of the recent rise in prices of foodgrains. This has raised the incomes of the land owning classes in a substantial manner. However, the costs of inputs have remained comparatively lower. The net result of this is the enviable prosperity of the land owning classes of the rural sector. Where would additional incomes thus generated go? One does not wish to argue that all the extra income would be received in the banks; but surely enough a significant part of it can be mobilised if only there was a proper institutional framework. Otherwise one is afraid ready cash has always the temptation of slipping out of the hands for non-essential purposes.

In brief one could say that the lever for growth is the rate of savings an economy can achieve. And the rate of savings in turn is dependent upon the taxation measures and the nature of pricing policies that the public sector enterprises pursue. The view that public sector should not attempt at taking advantage of the market forces for resources mobilisation is wholly misconceived. The public sector profits should be viewed as not only desirable but as necessity. But apart from the compulsory savings the role of voluntary savings is of crucial importance in an under-developed economy. The private banking institutions which operate on profit considerations cannot take up the responsibility of building up a financial and institutional set up to cover the rural and urban areas or reach all sections of the community. As far as the rural banking is concerned the cooperatives alone do not provide the answer. Extension of organised banking for rural areas is a necessary complimentary development to the cooperative movement. Apart from this the function of resource mobilisation can be only undertaken by organised banking institutions.

Part Four

SOCIAL OBJECTIVES AND COMMERCIAL BANKING

Resource mobilisation is one aspect of the banking operations. It has been seen, however, that the growth of the banking institutions has remained confined to the urban centres as also to the new industrially better advanced States of the country. Not only there is concentration of banking offices over space but also the intensity of the banking offices is so distributed that the banks have not made any efforts to reach large majority of the population. As a result its capacity to muster surplus financial resources with the community has remained a limited one. Specially, the present banking system has neglected the poorer sections of the community as also the rural sector.

Profit motive of Private Banks

The main reason for this unbalanced growth of banking in the country has been the manner and the criteria of the private sector which determines the operations and the direction of development of these agencies. Because of the smaller amounts, larger number of persons to be dealt with and scattered nature of the villages, the administrative costs of managing banking offices in the rural areas are considerably higher than that of the bank offices which are located in urban centres where the clientele is generally educated, have better incomes and there exist a number of other facilities like better and easy communication. Therefore, opening of bank offices in the rural areas is not a profitable proposition in the immediate sense. This obviously is a limitation of the entire banking system when it is operated in the private sector which seeks to confine its operations in such areas which would yield handsome profits. Therefore, it is no surprise that the bank developments in India have remained confined to urban centres only and yet the fact remains that in the overall interest of economic development and for achievement of other social objectives, it was necessary to extend banking facilities evenly both spatial and from the view point of intensity of coverage in the urban centres.

Banking as Public utility Services

Sometimes it has been suggested that this uneven growth of banking in the country can be improved and set right if only the private banks were enlightened on the necessity of providing banking facilities to the rural areas and were to be under moral pressures by the Reserve Bank of India and the Government. For this it is further suggested that the private commercial banks should be helped, even subsidised, to develop research departments and development wings whose main task would be to locate potential areas where a bank could open its new offices. One wonders if moral pressures can be used to persuade the private sector banking companies to accept *non-profitable* business of extending banking offices in the rural areas. Reliance on such a belief is not only too idealist but also misconceived. As long as the banks are under the control and management of private sector no amount of persuasion can, and would be, effective to follow policies which are against their own economic interests.

On the other hand to expect that in the absence of the private banking institutions being ready to open bank offices in the rural areas, the public sector banking should undertake this job is extremely illogical because this would imply that the profitable areas of banking may be left to be harnessed by the private bankers whereas the public enterprises should run the non-profitable and losing banking business. A more rational view would be that the profits from the banks were not viewed as a very important criteria but the banking institutions were essentially considered as *public utility* services. There perhaps one could even argue that a principle of no-profit-no-loss may be adopted to compensate the deficit incurred by the banks by opening branches in the rural areas from the profits they may earn by banking operations in the urban centres. This obviously would mean the negation of the rights of the private sector to take advantage of their investments in the banking institutions--because no one would like to make investments unless these did offer some scope for direct returns.

Therefore, banking in an under-developed economy which attempts at a continuous balanced rate of growth has to be considered as an institution of resource mobilisation. The criteria of their success should be measured in their capacity to increase deposits and consolidate scattered surplus financial resources in the community, thereby to release demand pressures than to assess their functioning on a very conservative and out-dated criteria of *profits*.

Credit Worthiness

Sometimes one hears an argument that private banks are often in a position to judge the credit worthiness of a small man--who is known to the manager of the bank--is likely to be perhaps a little more flexible than a financial institution which has a set of rules and regulations, handed down by some one from the top and in relation to which if he showed any flexibility, the manager may often be accused of corruption, favouritism and so on. This element of knowing the local man was a very important factor in the development of private banking in countries like United Kingdom.

But how did private banks develop in these countries inspite of the tendency of the banks to prefer to stay in the urban centres? Historically, one would find that in the period of industrial revolution in Great Britain there was a system of `country banks' which were unit banks and did not form a part of branch banking system. Therefore, first of all, the small private banks were subject to directives from above either from the state owned or the private owned enterprises; and secondly `country banks' were allowed to issue currency notes that they had an incentive to work in rural areas. But the right to issue the notes was withdrawn from the commercial banks after britain had reached a stage of take-off. The main advantage with these banks was that the lenders could exercise their judgement regarding the characters of their borrowers and watch their varying fortunes, on day-to-day basis even if the borrowers could not offer good security. In other worlds, the whole problem of dealing with the small man, who have some potential or entrepreneurialability was overcome with the help of the unit banks which were small and enjoyed confidence of the local people.

But the present-day banking is not mere unit banking. From the operational view point it hardly makes any difference whether banking was in the private sector or in the public sector because in branch banking the managers or the bankers can never claim to know the local people so intimately as it was possible for `country bank'. The question of public versus private sector banking comes up only if one considers the basic conflict between the private and the public sector. The banking activity, by its nature, involves a conflict between the small man, the illiterate man, the man who does not have the banking habit and the big man who has banking habit and who has control over the commercial banks. Therefore, the question of nationalisation of banks is really a question of resolving the conflict between the big and the small. What is the social objective? Is it to strengthen the hands of the few who are big or is it to help the common man?

More Controls--Futile

One hears quite often an argument that the apparent conflict between the big and the small can be resolved by regulatory and credit control measures. it is suggested that the Reserve Bank of India has sufficient powers or it can be given more powers to exercise better supervision if the trends in the private banking were not in accordance with the overall social objectives of the country. It has also suggested that some sort of a credit council could lay down broad policies for the private banks. In this manner a great faith is shown in the effectiveness of regulatory and other controls. This is a rather amusing situation because such an argument is advanced by those very persons of the private sector who have the least faith or belief in administrative controls--may these be concerned with any aspect of personal life or otherwise. The persons who show great exuberance regarding the effectiveness of controls, regulatory measures and moral pressures of the Government and the Reserve Bank of India are in fact those persons who do not believe, ideologically speaking, that governmental control can ever prove effective.

However, it would be of interest to see what is meant by the regulatory control and other improvements which have been suggested to direct the functioning of the private banking institutions so that these functions in accordance with the social objectives. The two instruments in the hands of the Reserve Bank of India for regulating the functioning of the private banks are (i) periodic reporting of the banking operations and (ii) periodic inspections.

How far the existing controls are superficial is only too obvious to need any fresh emphasis. The successive failure of the banks like Palai Bank and Travancore National Bank in the recent past are only too fresh to remind that the Reserve Bank of India or any other similar institution cannot supervise the functioning of thousands of bank offices in the country. Moreover, the Reserve Bank of India can at best have once in a year or twice inspect the record of the Commercial Banks and very obviously such an inspection would amount to a postmortem of what has already been done. If the Reserve Bank of India did not approve the operations of a bank it remains in doubt whether it should take any punitive action or impose any fines on the banks because such an action would jeopardise the confidence of the depositors in the concerned bank in particular and banking institutions in general. Therefore, the limitations of the Reserve Bank of India should ensure that banks pursued the Directives it issues from time to time is an extremely difficult task and the net result is that the Reserve Bank of India has failed to achieve the objective for which it was given a number of statutory sanctions.

It will be worthwhile mentioning here that in a country like United States no bank can extend loans to any single concern which are more than 10 per cent of the paid-up capital and reserves of the concerned bank. In other words in the United States there are severe limits for extending credit in large bulk to an individual concern.

Credit Drain--A hindrance to growth

On the other hand the paid-up capital of all the scheduled banks in India is around 44 crores but the Directors of the bank have been shown financial accommodation to the extent of more than Rs. 300 crores. Further as we have mentioned earlier a small fraction of the total borrowers in the country have claimed nearly two-thirds of the total bank credit. Very obviously when the 1/3rds of the bank credit is spared for a handful of industrialists, the rest of the economy cannot but remain starved of the bank credit and to the extent the non-availability of credit does not allow the establishment of new enterprises. There is a positive hindrance to the growth of the economy. In Part One it has been shown that a fraction of the total borrowers had claimed nearly four-fifths of the total bank advances. This needs no further argument to show that presently the banks are being utilised by a small group of industrialists to obtain financial resources for the growth of their own industrial houses. Leave apart any progressive and socialistic concept, let the situation, as it prevails in the country today, be judged on the most conservative policies of those countries who believe in complete capitalism.

Apart from the function of resource mobilisation, the role of the banks in an under-developed economy is also to be viewed in terms of the credit policies that the banks pursue. The close relationship between banking and industries on the one side and banking and commerce on the other side is only too well known to require special emphasis. What role we expect the credit institutions to play in India? In Part II of this Report we have spelled out the three basic social objectives namely (a) achievement of sustained economic growth, (b) a balanced development and (c) self-sufficiency.

The Role of Banks

The role of the banks has to be viewed in this context. The broad social objectives of the Indian society are spelled out in concrete terms in our Five Year Plan documents. Each Five Year Plan has a strategy of development. For instance, during the first Plan greater emphasis was placed on the development of agriculture and irrigation facilities whereas during the second Plan greater emphasis was placed on the development of heavy and basis industries. Thus a Plan document indicates the broad inter-sectoral priorities which need to be pursued for a balanced growth of the economy. One would normally expect that the bank credit was directed in such a manner as to help better implementation of plan priorities. For instance, the banks should give due consideration to the development of agriculture. But we would not like to stretch this point too far because extension of credit to agriculture need not be entirely financed through private commercial banking institutions.

One can understand that the main objective of the private commercial banking institutions is to mobilise resources for the growth of the private sector. Not that one would completely agree with this argument but to keep the area of dispute narrow, let us proceed on the understanding that the main function of the commercial banks was to finance the private industrial sector. If that was so, it would be expected that the bank credit was used for the growth of such industries which were given priorities under the Plans. The rationale for giving an industry a priority in a Plan is derived from the overall national plan strategy. For instance, when we think of the establishment of basic industries,the emphasis on these is placed because in the latter years, it would be possible to grow at a faster rate than if in the initial stages the nation places lesser emphasis on the basic capacity. When the Plans indicate a priority for agriculture, it is necessary to understand that it also means a priority to such industries the output of which would be directed to support the growth of agriculture at a faster rate. For instance, when we place emphasis on agricultural development, industrial sector has the responsibility to provide inputs like fertilisers, pesticides and agricultural implements. Therefore, the nature of industries which are helped with bank credit can be such which would make the implementation of the Plan priorities easier and more effective. Thus even when the banks were used to finance industrial activity one could find that agriculture could be specifically helped in accordance with the plan priorities without bank credit being made available directly to the agricultural sector.

Banks and Industrial Priorities

Similarly bank credit is a very important instrument of influencing investment decisions and locations of the industrial projects. As mentioned in Part II nearly two-fifths of the productive capital in factory establishments in the country is located in only two States of the country. Certainly if the bank credit was used as an instrument of ensuring better spatial balance in development, the banks could have helped in the achievement of the broader social objectives. Also by the use of differential rates of lending, the banks can be used to help the growth of such industries which have a priority in the Plans and discourage those which are non priority industries.

Many a time it has not been fully appreciated that the growth of non Plan industries becomes a great handicap to the process of development. For instance, one often wonders how and wherefrom did the private industries obtain the superior quality steel for mass production of stainless steel utensils. There would be hardly a house which does not have a few stainless steel utensils. Similarly, it is surprising that a large number of household consumer goods of the western type have flooded the Indian markets when these were positively not under any Plan priority. Take the case of Air-Conditioners and Refrigerators which require imported parts and therefore a considerable amount of foreign exchange must have been wasted on the production of such goods. Another case in point is that of the synthetic fibre. We have mentioned these only to underline that the credit mechanism could have been very effectively utilised for discouraging the growth of such industries. The growth of such industries not only wastes foreign exchange and divert other internal raw material but are also instruments of diversion of individual savings. In the same context one would like to refer to the development of certain industries, which were mentioned at the end of Part I, the development of which is certainly against all social objectives.

The bank credit cannot only help rational decision making in the field of investments but also be used to regulate the level of activity in the industrial sector. Proper policies of lending credit for meeting working capital could ensure that those industries receive preference where greater production was otherwise desirable. On the other hand by following proper policies demand for durable use consumer goods like automobiles could be significantly influenced through banking instruments.

The Role of Banks in Trade

The credit institutions, therefore, can play a very important role to regulate and direct the activities of the private sector in the field of industries. Very similar to the objective of regulating industries through credit mechanism one can show that the bank credit can play a strategic role in determining the pattern of commercial activities in the country. By discouraging speculation in such products which are in shortage the banks can manoeuvre price level as also encourage trade where it was desirable to encourage stocks. in this reference one may refer that food problem is one of the constant problems with us which needs to be squarely dealt with. For this it is very necessary that large stocks are built up during the periods when we have bumper foodgrains crops. Very often one hears that after 5 to 10 million tons of foodgrains have to be stored it would be very difficult to find the corresponding financial resources. One does not know why the banking institutions cannot be squarely tapped for ensuring the requisite financial resources for building up of foodgrains stocks. In this manner banking institutions can play a vital role in holding the price line and regulating the private sector trade and commercial operations.

The banking institutions can also play a very important role in ensuring that credit was made available to such entrepreneurs only who have the necessary competence, expertise and capacity to undertake new industries. For instance, just like the World Bank, the banks could insist upon receiving project reports and satisfying themselves regarding the feasibility of investment proposals before granting loans. In this manner the banks could help those who would prove efficient and thereby keep the cost of production lower by helping an industrial house which starts a large number of industrial units each different from the other. This fact is mainly responsible for lower efficiency and high cost of production in the industrial sector of our economy.

One need not rule out the possibility of banks being used as institutions which would ensure that industries pursue certain pricing policies and were managed in the manner in which it was not against the overall interests of the social objectives of the society. In the same manner banking institutions could keep a watch on the operations of the industrial units which were established for the purposes of export promotion or import substitution. The banks could also use their position to ensure better follow-up of the licences which were granted by the Government. Similarly the financial institutions, when properly operated, would ensure that under and over invoicing was not resorted by the private sector, commercial and industrial institutions.

Backing to Investment

Sometimes it has been argued that investment decisions are not influenced by the easy availability of bank credit. Bank credit is made available to only such industries which have been granted the necessary licences by the Government. Therefore, it is argued that banks are the least responsible for encouraging or discouraging plan priority industries. The same argument is put forward regarding concentration of industries and growth of economic power in the hands of a few industrial houses. The argument is an attempt to show the innocence of the banking institutions in matters of helping trends towards concentration of economic power in the country. But this would not stand to reasoning if one was to show that bank credit, though known as short-term credit, can be, and has been, long-term credit as invariably bank credit is rolled over many years. Secondly, the question would arise whether an application which is not supported by a bank guarantee for provision of the necessary financial resources, would ever receive consideration from the Government or any Committee responsible for granting of licences? It is only with the help of the bank credit and the easy availability of financial resources that few industrial houses have been in a position to obtain licences because they only could afford to ensure the required financial resources for the establishment of new industrial units.

Foreign Collaboration

Not only this, the bank guarantees have also ensured easy foreign collaborations on instalments where the home entrepreneurs are not required to undertake very large investments. Why it is that an ordinary man cannot get a licence whereas a big industrial house like Birlas can have many licences? The basic reason is that the Birla House have financial resources drawn from the commercial banks and an ordinary man can never hope to obtain bank loans to the required magnitude. Thirdly, in the Indian industrial structure, inter-company investments are not unknown. A company which has its own resources to meet its working capital can easily invest its working capital into another country if the bank was ready to provide the necessary working capital. In this and in many other manners, the bank credit can be used for investment purposes.

Credit Concentration

Before we come to the question of nationalisation of banks, we would like to indicate the implications of bank advances being used by a few industrial houses. It is a well accepted fact that nearly one per cent of the total borrowers of the country received nearly Rs. 1800 crores during the year 1966 from the commercial banks. The rate of interest per annum for scheduled bank advances has varied from 6 to 10 per cent per annum. The market rate, however, has been between 15 to 16 per cent. Therefore, Rs. 1800 crores have been lent to nearly one per cent of the borrowers at a rate which is two-third of the market rate. Firstly, there is a favoured treatment to these industrial houses because these have been given so much of financial accommodation and secondly the rate of interest charged has been around 8 to 9 per cent. This really means that during the year 1966 these handful of borrowers had obtained an advantage of Rs. 114 crores because of their close communications with the banks. In other words, this is the amount of subsidy which the big business houses received at the cost of the depositors and average man in the country. The amount of special advantage which they have enjoyed during one year would be more than three times the total paid-up capital of all the scheduled banks of the country. This is really shocking situation where one pleads of compensation to the banks when every year they draw 600 per cent *direct returns on their investments in the share capital of the banks.*

Case for Nationalisation

The question of bank nationalisation has to be considered in the light of the above account of the operations of the private banks in the country. Firstly, the present banking system has an inherent limitation in its operations and it cannot provide the necessary banking facilities to rural and the lower income strata of the population. Secondly, the banks have been used for the growth of only a few industrial houses who happened to enjoy control over the banking institutions. Thirdly, the easy credit availability to a few industrial houses has led to the growth of monopolies and helped the process of concentration of economic power in the society. Fourthly, a large number of entrepreneurial ability remains under-employed because the requisite financial resources are denied for their legitimate growth. There is discrimination against those who happen to be competent but unable to satisfy the conservative criteria of credit worthiness. Lastly, the banking institutions as these are, have helped, because of structural reasons, the growth of only a few States and have siphoned away large amounts of resources from the poorer States to the comparatively better industrialised States of the country.

No amount of moral persuasion or minor changes here or there can achieve the social objectives which have been spelled out in Party II of this Report. Further the past experience has shown that regulations and other controls by the Reserve Bank of India cannot prove effective. The basic difference is that of fundamental conflict between the interests of the few and the interests of the many. Under these conditions, there can hardly be any justification for leaving the banking sector in the hands of the few industrial houses. What is necessary is the nationalisation of all commercial banks in the country. Partial nationalisation would neither serve any purpose nor would help to correct the imbalances which have creeped into the working of our economy. We would, however, come to broad policies which must be pursued if the functioning of the nationalised banking has to be more purposive and in the desired directions.

Claims of Bankers Association Unfounded

In the recent past the Indian Banks Association and, the private banks individually, have been active in creating an impression that nationalisation of banks would be an economic disaster. The Indian Bankers' Association's statement of 10th July, 1967, goes to the extent of saying:

> "... The banks which are the trustees of more than Rs. 3500 crores of deposits from 1.25 depositors mostly representing hard earned savings of small people of moderate means and which are responsible for nearly 100 crores of capital funds belonging to a large body of equally small shareholders cannot meekly submit to pressures that may create a financial panic in the country and jeopardise her economic future. I therefore, wish to send a note of caution that if political or legislative pressures precipitate the issues and force hasty and drastic changes upon banks, *the country may have to pay heavily for it".*

When the attitude of the Bankers Association is that of the issuing warnings to the Government, one does not know if one can discuss the question of bank nationalisation with a cool and calm mind. However, one is surprised at the extraordinary interest which the Association has started showing not only through the press but also otherwise on the question of bank nationalisation. Many claims are made which cannot stand the scrutiny of examination. For instance, the Association claims that banks are owned by small shareholders. In Part I of the note, we have shown how the bank shares of the Central bank of India are controlled by a small fraction of the investors. To repeat, we may mention that from the information published by the Central Bank of India in its Annual Report it is made out that nearly half of the bank shares were held by 3 per cent of the shareholders. The knowledgeable circles, however, believe that the Central Bank of India is perhaps not a representative bank for the study of the distribution of shares. In most of the banks controlling shares are held by one or two business houses. This is indicated in the very little change that takes place in the Board of Directors of these banks as also is obvious from the controlling shares held by a group of persons. Thus the plea of small shareholders does not have much meaning after the controlling shares were held by a small number of persons. In any case the largeness of the shareholders have little meaning if the control and the management of the banks was only with the same and the big industrial houses.

Political Pressurizing

One is surprised that bankers association should issue a warning to the `political or legislative' agencies of the country. What are the political agencies in the country? Very obviously the sovereign body of the Indian Nation is the `Lok Sabha'. Thus the bankers association has directed its warning to the Parliament of the country and said that `the country may have to pay heavily for it'. One does not know what is implied by such a statement. Surely this is not the language of reason or of rationality.

The private banks have been inserting huge advertisements in the national press during the last few months. At the face of it one wonders the provocation for such huge expenditure, out of the public resources. If the banks were running so efficiently and so justly, there was no question of any danger to their functioning whether these were nationalised or these remain in the hands of the private sector. It is admitted that banking is a service. If it were so, as it is so, why should the big industrial houses and those who today control the banks get so agitated? Very obviously one has a reason to doubt if present propaganda and tirade of the private banks is not an attempt to conceal something which is much more anti-social and questionable than what has come to be known to the Parliament and the intelligentsia.

Scare on Depositors--A Myth

Let us take one by one the fears which have been expressed regarding the nationalisation of banks. Firstly, it is argued that nationalization of banks would result in psychological reaction and as a result of the number of depositors with the banks would get declined. Would this be so the basis for such a fear appears to be that the nationalised banks would not enjoy the same degree of confidence from the savers as is enjoyed by the private commercial banks. This argument and `psychological reaction' was argued when the Imperial Bank of India was to be taken over by the State Bank of India. What has happened to the deposits of the State Bank during the 12 years. Has the State bank lost confidence of the savers? This would be indicated by the facts which we can easily cite. Between the period of 1955 and 1965, the deposits of the scheduled banks had risen from Rs. 1071.73 crores to Rs. 2814.66 crores in 1965. This obviously is an increase by less than three times. The deposits with the State Bank of India for the year 1955 stood at Rs. 219.80 crores whereas this stood at Rs. 676.92 crores in 1965. This is more than three times that deposits held in 1955. This would indicate that the argument of adverse `psychological reaction' is only too baseless to require any further discussion.

But more than citing the State Bank of India, one would like to ask as to what is the base of confidence that people have in the banking institutions. This needs be made clear that confidence in the institutional set-up, whether it is banking or otherwise, is derived from the laws of the nation and the trend of the social order. If there was a crisis in the basic structure of an economy the banking institutions have no separate juridical existence. Referring to the fact that the banking institutions have to deal with the finances which have been created by the Reserve Bank of India and the Government, if people's faith in the currency of a country does not exist, or if there is lawlessness in the economy, and the banking institutions provide confidence to the economy? The faith in the banking institution, whether in the private or in the public sector, is provided by an ordered society which is sought to be believed through the rule of law and not through the operations of the few industrial houses. In fact time and again the Government has to introduce legislative measures to ensure that the confidence of the people was built up in the private banking institutions are only too well-known to be referred to indicate that the source of confidence which the private banks enjoy lies with the Government and the Parliament and not with the few capitalists and the self-styled representatives of the people. It is only a few years back that the Government has introduced Insurance in the small deposits with the banks which ensure that small depositors are not made to suffer if a private commercial bank failed. Thus the argument of adverse `psychological reaction' is only worsening the faith and the fear for nationalisation so that small section of the population could continue to exploit the community savings for their personal benefits.

It has also been argued that with the nationalisation of banks, the bank deposits would get reduced. One may ask which is the section of the depositors who would not like to have deposits with the banking institutions. Very obviously the section which maintains current accounts in the banking institutions, comprising of the business and the corporate sector, cannot but help to maintain accounts with the banks because it was an operational necessity for their working. Also it is only through the current accounts that they can obtain credit from the banking institutions. Thus in our discussion regarding the deposits, one must keep the current deposits outside the discussion. In the rest of the deposits, as has been shown in Part I, a large part of the deposits come from small savers. This section of depositors is very directly dependent upon the number of banking offices which are located in the economy. It is very obvious that nationalised banking sector would pursue a vigorous policy to cover the rural areas and the small savers in the urban centres, thereby the quantum of deposits as well as the number of deposits would considerably be enlarged. The same could be said regarding the fixed depositors. One does not see which section is referred to when it was argued that certain type of depositors may withdraw their savings from the nationalised banks.

Credit Needs not Affected by Nationalisation

The main argument put forth by the Private banks is that with the nationalisation of the banks, the private sector would be adversely affected and it would not be able to obtain credit from the nationalised banking institutions. nothing could be more unreal and superficial than this argument. Though Stage Bank of India is not a model enterprise, yet it needs to be mentioned that it is the State Bank of India which has shown accommodation to the private sector in a big manner. Even the ICICI and IFC as well as the LIC are the financial institutions which have been specifically created by the Government to provide finance to the private sector. There is no reason to believe that private sector would not obtain financial accommodation from the nationalised banking institutions. However, one must say that such a fear would be genuine on the part of those who enjoy a privileged position in matters of bank credit not because they have entered priority industries but because of their influence and control over the policies of the private banking institutions. Very certainly, a nationalised banking sector would not be able to allow a favoured treatment to a few only the degree of discrimination against small borrowers would get reduced. Thus the real danger in the nationalisation of banks is not to the industry as such but to a few monopolists and industrial houses who have been receiving an extremely favourable treatment from the private banks which they own or control.

A general charge against the functioning of the private sector is that the policies of the public sector are influenced by political considerations. Without going into the argument further one may only state that all that is `political' is not what is generally made out. There is a difference between the political and personal influence entering into the functioning of the public enterprises. in the case of the functioning of the private banking institutions today the influences `personal' and vested. If the banks were in the public sector, the policies and the management may be under the pressures of the Parliament and the Government. Since the Parliament and the Government are the institutions of the society, the influence of the Parliament cannot be considered as derogatory to the overall interests of the society. Thus even for a moment if one takes the political influence will replace the personal influences, the situation may not be against the social interests and the national objectives. Whereas today the structure of the banking is such that it certainly functions against the broader national objectives, as mentioned in Part II of this Report.

Managerial Talent

Another fear expressed has been that the nationalised banks would not be able to secure the managerial talent required for conducting day-to-day function of the banking institutions. One does not know if such a question need to be posed by those who claim to have better understanding of the banking and private institutions, regarding the question of finding managerial talent immediately after the nationalisation of Banks. With the nationalisation of banks very certainly, the present administrative and managerial staff would remain in employment of the nationalised banks. The only change will take place in the Board of Directors and in this regard, thanks to the close relationship between the industry and the banking, there is no fear of the bank directors going out of job and facing a situation of unemployment if they did not continue on the bank boards. Most of the bank directors hold directorship in industrial companies. Thus the real displacement in personnel would be negligible and no crises would appear after the nationalisation and taking over of the private banking institutions. However, care will have to be taken that special efforts are made to train many more managers and other banking talent which could pursue a vigorous policy of expansion in the rural sectors of the economy. Also the banking institutions would have to develop their own expertise instead of depending upon the normal civil servants, before or after retirement to hold the senior most positions in the nationalised banking sector.

Financial Cost

The total paid-up capital and the reserve of the Indian Scheduled Banks was around Rs. 69.00 crores in 1965 in 1965. Even if the Government chose to take over the entire paid-up capital, which really is not necessary, the cost of compensation would not be significant if one compares the additional deposits of nearly 2,000 crores which would be accompanied by the act of nationalisation. If the differential rate (the market rate and the rate of bank credit) was 6 per cent the whole amount of compensation could be made within a period of one year alone. Moreover, the question of compensation or financial cost is a very minor point in the discussion of bank nationalisation. The financial cost has to be related with the other advantages which he economy would obtain and since nationalisation of banks has a structural role to play in the economy, the financial cost should be the least important consideration in deciding about the question of nationalisation. However, it is not a very significant financial cost because compensation would be liquidated by the profits within a period of 5 to 6.

Foreign Investment

In certain quarters a fear has been expressed that with the nationalisation of banks our foreign trade would be adversely affected. This again is a fear which would not be justified if one conducts an investigation into the nature of imports and export of the country. As far as exports are concerned there should be no reason to believe that our exports would decline and on the import side if the imports of non-essential commodities got to be reduced, which is unfortunately is a remote possibility, it should be most welcome. One can however, see some justification in the argument that private foreign capital may not be coming as easily as it would otherwise. This seems to be the fear. One must state even at the cost of being repetitive that such fears have been expressed all throughout and these are nothing new for students of economics in the country only to cite a few. At the time of the initiation of the planning process it was widely publicised that the growth of the public sector and adoption of planning would take us nearer to the Communist world and with our closer contacts with the socialist countries, the private capital would feel shy of entering the Indian economy. Once again, at the time of the announcement of the Industrial Policy Resolution, these fears were exaggerated. After the resolution of the All India Congress Committee on democratic socialism, it was openly doubted whether any private industrialist would like to invest in this country and the cost of its entering into the Indian economy has not been a light one.

Therefore, it should be made clear that such fears are a stock argument for any rational decision which does not suit a few industrial houses or goes against the ideological convictions of those who have neither faith in their own social order nor have the right of being Indians. How does it matter for a private investor whether the bank was in the private or in the public sector? It was of least importance for his investments and for his profits. As long as he can obtain fairly good degree of returns to his investment he would enter into collaborations and invest directly in the country. The private capital will not come on sentimental reasoning but would be attracted by the economic prospect that we can offer.

Monopoly and Competition

Another argument put forth by the private bankers and the vested interests is that with the nationalisation of banks there would not exist competition in the banking sector. As a result the personalised service to the depositors would disappear. It is further argued that nationalisation would bring in monopoly of the Government in the banking sector. Before posing this question one should ask whether in India today banking is not in the hands of a few industrial houses? Is it not their a virtual monopoly in the private banking sector? This is further indicated by the fact that all the Scheduled Bank representatives have come under a common banner `Indian Bankers Association' to defend the so-called interests of the `Community'. The Banks have been to-day functioning as a monopoly. This point has been amply discussed in Part I and the statistical data clearly indicates that there was a virtual monopoly in the banking sector of the economy. It needs to be mentioned here that a monopoly in the private sector is very much different from the monopoly under the public sector. A public sector monopoly is answerable to the people in general and to the Parliament in particular, whereas the private monopolies are neither responsible nor answerable to any one else than their ownselves. Thus even if there was monopoly of the Government of the Government in the banking sector, it would not be deleterious to social interests as the present monopolistic conditions. However, we would not like to give an impression that the nationalised banking institutions need be negligent regarding providing such services which would attract more depositors and give a sense of personalised attention. Special efforts will have to be made that the nationalised banks pursue such policies. We are dealing with some of the questions in the last part of this Report. By way of indication the broad outlines of the nationalised banking will have to be managed and administered.

Part Five

CONCLUSIONS AND RECOMMENDATIONS

In the foregoing Part of this report, we have dealt with many aspects of the present-day structure of the private banking system and its functional maladies. From our analysis, we arrive at the following conclusions:

1. The private control of commercial banks in a planned economy is an anachronism which has been an obstacle to the achievement of plan objectives in India;
2. The private banks have failed to mobilise the savings of the community, specially of the rural sector, small towns and the lower income groups;
3. The ownership and control of private banks is concentrated in a few hands which militates against the constitutional Directive that the operation of the economic system should not lead to concentration of economic power and widen disparities of income and wealth;
4. The private commercial banks have mainly been instrumental in draining away the deposits from rural and semi-urban areas to large centres off industry and trade, but have not led to balanced regional development of the economy by means of their credit policies;
5. The private commercial banks have failed to contribute to the development of the vital priority sectors of the Indian economy, namely, the small scale and medium industries sector and agricultures;
6. The private commercial banks have failed to promote and encourage the new entrepreneurs, whose main capital is their technical and managerial skill, to set up industries with the help of bank accommodation;
7. The private banks have promoted exclusive use of large deposits by a small group of industrial houses, which as directly helped in the concentration of economic power in their hands;
8. The private commercial banks have abetted and supported socially undesirable activities like hoarding and speculation by violating the rules and regulations laid down by the Reserve Bank of India from time to time;
9. The private commercial banks have failed to be guided by the positive social objectives laid down in the Five Year Plans;
10. The private commercial banks have resorted to policies and practices by means of which the supply of bank credit has been unduly increased in certain crucial periods and diverted bank credit into channels which were contrary to the laid-down priorities in the plans.

11. Easy and cheap availability of credit for a few industrial houses has encouraged the growth of monopolies and in conditions of the "sellers market" in the country the monopolists have not paid any attention to the Plan objectives of achieving `self-reliance' in matters of foreign assistance; and

12. The operations of the private banking institutions have been the basic cause of the lop-sided development of the Indian industrial sector.

On the other hand, in our opinion, the merits of nationalisation of the banking structure would be as follows:

1. The nationalised banking institutions would be in a position to pursue vigorous and continuous expansion programmes of covering the rural, the small towns and other lower income groups in the society for ensuring greater resource mobilisation for the economic development of the country;
2. The nationalised banking would ensure that the credit policies were such which supported plan priority industries and discouraged the trends of investment which were not in conformity with the overall objectives of economic development;
3. Apart from ensuring better economic growth through better implementation of the Plans, it would also be possible to pay special attention to the achievement of the objective of balanced-inter-sectoral and inter-regional-growth in the economy;
4. The nationalisation of private banking would snap the control over the community's resources, which exist in the hands of a few industrial houses of the country. Thereby, it would be possible to reduce concentration of economic power which has its own serious implications in the efficient conduct of the economy;
5. The nationalised banking structure would enable the society to coordinate policies of the various credit institutions in the country in a manner which was necessary for the exploitation of the entrepreneurial and other skills available in the country. In the existing economic system the Reserve Bank of India cannot exercise effective controls for regulating private banking institutions;
6. The nationalisation of the banking institutions would bring about more stability in the functioning of the credit institutions and thereby inspire more confidence from the depositors;
7. Because of the snapping of direct contacts between the few industrial houses and the banking institutions, the discriminations against a large many would come to an end. This will introduce more healthy competition between the entrepreneurs than in the present situation where competition is sought to be between the two unequals--big with all the resources at their command the small denied of any such assistance.

Therefore we are of the opinion that any attempt which seeks merely to impose greater controls on commercial banks, without interfering with the patterns of ownership and control in few hands will not achieve any significant results. The last two decades of the planning period in India have clearly shown that despite comprehensive regulatory control of the Reserve Bank, it has not been possible to regulate and control the activities of the private commercial banks in accordance with the national interests and also the priorities of planned development. The past experience is sufficient to dispel any further hopes regarding the possibility of the present banking system being regulated through controls.

We are also of the opinion that in the present stage of our economic development, partial nationalisation of banks will not meet the needs of the times. It will create many more difficulties than it will solve because the challenges of the present conditions are such which cannot be met without the complete takeover of the banking system.

Further, while emphasising the need for the nationalisation of the banking system, we would like to make a few suggestions regarding the actual implementation of the policy of nationalisation of banks. These are the following ones:

Credit Policy Guidelines--Working Group

Leaving aside the sins of ommission and commission by the banking system, the basic defects in the working of the credit institutions today in terms of planned development arise because no real policy guidelines have been laid down by the Planning Commission, the Finance Ministry or the Reserve Bank which closely interconnect plan requirements with the grant of bank credit. The Reserve Bank no doubt attempts from time to time to guide the channels of bank credit, but its guidance is much more related to the current economic situation and difficulties than to the requirements of the Five Year Plans. The fact that there is no such clear guidance given--the outlines of such a policy are not even worked out in operational terms by the Planning Commission and the Ministry of Finance--is indicated by the act that the two most important credit institutions in the country which are already in the public sector, the Life Insurance Corporation and the State Bank of India, do not have any policy directions regarding investment and credit which can be said to be in any way closely related to the requirements of development planning as worked out in the Five Year Plans. One of the immediate and crucial tasks, therefore, is to work out what exactly should be the credit policy to be pursued by the financial institutions for the successful implementation of the development plans and for the attainment of the objectives of current economic policy and how should it be laid down by the Planning Commission and the Ministry of Finance. It is also necessary that appropriate instruments to ensure that this policy is carried out in a decentralised way by the banking organisations and their branches should be worked out. The experience of wartime Britain and the planned economies, especially in more recent years, and also that of France, should be studied in this context. One of the essential things to be done immediately would be to set up a competent working party to prepare for the Government outlines of this policy so that the strategy of credit planning can be worked out at the earliest.

Management after Nationalisation

The management of nationalised banks will pose quite a few questions and it will not be possible to meet the challenges by the usual methods of management that have been unfortunately prevalent in the Indian public sector. The bureaucratic domination of public enterprise management and the use of completely unsuitable governmental methods have been the bane of our public enterprises. It is essential that once the Government decides to nationalise banks, clear decisions would have to be taken that a break with the past tradition of bureaucratic and inefficient management will be made at the same time. The intention to do this has of course always been there. When the Imperial Bank was nationalised, the then Finance Minister had indicated that while social and economic objectives would be kept before it by the nationalised bank, its management would largely operate on business principles. With this purpose, he even excluded the nationalised bank from the purview of audit by the Comptroller and Auditor General. While this was certainly useful, it has not led to the kind of business-like management of the State Bank that one would wish for.

Competitive Structure of Nationalised Bank to be Maintained

We may also suggest that the nationalised banks need not all be merged together as was done in the case of the Life Insurance Companies. While a few small banks which are found to be uneconomical may be merged in some way or the other to form more economical and efficient units, the units that are well-organised and economical have to continue to function independently. There is nothing wrong with the different nationalised banks competing with each other and it may even be useful to allow more competition than the Indian Banks Association has usually permitted for the private commercial banks in the past. Such competition would ensure that there was incentive for better service to customers and this may even help in attracting more and more deposits to the banking system. This is an important consideration and we have discussed this in Part Three of this Report.

The maintenance of the nationalised banks as independent units would mean that while the Boards of Directors of the Banks would have to change immediately on nationalisation, the management including the bulk of the top management cadre would continue to be the same. Already the pay structure of employees in different banks has been rationalised through the system of bank employees' awards and the categorisation of banks for that purpose. The problems that were faced by the L.I.C. regarding bringing in one pool employees of different life insurance companies would not therefore create any problem for the nationalised banks.

Boards of Directors

The selection of the nationalised banks' Boards of Directors would be of crucial importance. The tradition of appointing different level bureaucrats on an *ex officio* basis should not be followed in making appointments to these Boards. It is true that there is a tradition against appointing persons who are not under Government control because of the fear that, if they behave irresponsibly, the Government would come into trouble. The underlying assumption of distrust of the non-official citizen is something that needs to be given up as early as possible. This is obviously a heritage from British rule imbibed by the Civil Service and learnt from them, perhaps not quite consciously, by the political leadership. There are a number of sources for recruitment to the new Boards of nationalised banks. For example, experienced officials of the Reserve Bank and the State Bank, well-known professional experts of existing Banks who are not wedded to anti-social and anti-public sector doctrines, professional experts from industry and from the academic world and labour leaders who have some experience of industry should contribute from two-thirds to three-fourths of the Board members. It is, however, necessary to underline that the Directors must be those who have a broader social perspective and have a commitment to the social objectives and are known for their faith in public sector and the philosophy of planning in India.

Employee Cooperation

Unfortunately, the trade unions in India have not always taken a constructive attitude regarding the efficient operations of public sector enterprises, and it would be difficult to expect an over-night change in their attitudes, but it would be useful if an attempt is made right from the beginning to cultivate the bank employees' unions and take them into confidence regarding the post-nationalisation organisation of the banks. While no representatives of the bank employees' unions as such need to be appointed on the Board, the appointment of some prominent trade union leaders on the Boards of nationalised banks, and an attempt by the new managements and by Government to establish an effective system of communication and consultation would help to create a climate where cooperation of employees and their organisation for the efficient functioning of nationalised banks may become available.

Prevent Overcentralisation

One further word of caution is necessary about the management of nationalised banks. Because of parliamentary accountability and the traditional nature of governmental functioning, nationalisation and public ownership especially in India has invariably meant over-centralisation in decision making. This would be suicidal in nationalised banking. A certain part of credit decisions must be left to the local agents of banks and if a feeling is created that the agents have to refer matters all the time to higher authorities, we may not only create public opinion against nationalisation but also make the functioning of trade and small industry difficult. Within the board policies laid down by the Board of Directors and subject to the normal supervision, it should be possible to permit local agents to take decisions regarding grant of credit. This would be treated as obvious--but not in the context of the functioning of the Indian public sector.

It may also be necessary to appoint a working group of accountants, specifically to examine past transactions of banks with a view to finding out how far the private ownership of banks was used to further not only the interest of certain business groups but also to evade public policy and Reserve Bank directives. Such an investigation may also lead to the unearthing of black money and may generally provide a healthy influence for correcting many ills that pervade the Indian economy today.

Credit Policies and Coordination

A word must be said regarding the need for evolving a set of credit policies which would enable the nationalised banks to pursue the social objectives which are placed before the nation. We have already said that a Policy Group should be immediately appointed to work out the necessary guidelines for the nationalised banking. There is, of course, no doubt that the impact of the policies would be periodically reviewed to ensure the necessary modifications in the credit and management policies of the nationalised banking institutions. There would also be need to coordinate the functioning of the other financial institutions like the cooperatives, Life Insurance, General Insurance, Unit Trust, Industrial Credit and Investment Corporation of India and the Industrial Finance Corporation. This is extremely necessary to avoid conflicting and wasteful policies by the various financial institutions.

Annual Credit Reviews

Considering the importance and the strategic role of the banking system in the structure of Indian economy it is necessary to have a comprehensive annual review of the functioning of the various credit institutions in the country and their impact on the furtherance of Plan objectives. Uptil now very little effort has been made in this direction. But one can understand that when banking institutions are not under the direct control of the public sector such a coordination or even a review is next to impossible. We consider, the data on the working of the banking system are an extremely useful indicator of the level and direction of the economic activities in the society. This information should prove of great advantage to the government and the Parliament in evolving of effective, timely and more rational policies in the field of planning.

Part Six

EPILOGUE

In the foregoing Parts of the report we have dealt with the various aspects of banking in the Indian economy. It is clear that the central control and management of the banking institutions cannot be left in the private sector if the plan objectives have to be achieved. However, these conclusions of ours are purely based on economic and social considerations. The case for nationalisation of banks could, however, be also made from the view-point of constitutional and parliamentary angles.

The Indian Constitution has enjoined the Government specific responsibility of taking all such measures which would ensure that the operation of the economic system does not lead to concentration of economic power in the country to the common detriment. in this context we consider that the nationalisation of the private commercial banking is only one of the economic reforms of the economic structure which was long due to curb tendencies towards concentration of economic power and the emergence of monopolies in the productive system of our society.

It is also necessary to take note of the demand often made that in the Indian economy at present considerations for increased production should precede those of social justice and distribution. It is argued that once production rises and capital is accumulated in a few hands, it would not be difficult to take over the large private business and industrial organisations into governmental hands, and which is made out of the point, particularly relating to the private commercial banks that the alternative of nationalisation was always open to the Government.

In this context, we would like to cite Prof. D.R. Gadgil, the present Deputy Chairman of the Planning Commission, who made the observations in the following manner:-

> "That increasing inequality or the heavy and continued concentration of the ownership of the means of production in the hands of a few private capitalists is the only way in which you can speed up production, is far from being universal experience in recent times. It is also very doubtful whether you can continue to concentrate economic and other power in society in the hands of small groups and yet later expect that they will quietly allow you to take it away or even that a state apparatus dominated by such interests will want to reverse current policy".

When the foregoing economic analyses impel us to come to only one conclusion that in the given context of Indian economy, meant to progress towards Socialism, nationalisation of Banks is an inevitable step. However, we should not be understood thereby to mean that either nationalisation of key industries or that of the financial institutions would automatically lead to Socialism. It must be pointed out that nationalisation of key industries and financial institutions had been resorted to by several capitalist countries in the world for the purpose of strengthening and stabilising the institution of capitalism. In this context, we would like to quote late Pandit Jawaharlal Nehru, who made the following observations in the context of the Karachi Resolution of 1931:

> "In the Karachi Resolution it took a step, a very important step in a socialist direction by advocating nationalisation of key industries and services and various other measures to lessen the burden on the poor and increase it on the rich. This was not socialism at all and a capitalist state could easily accept almost everything contained in the resolution".

Care is, therefore, to be taken that nationalisation of banking system does not become merely a measure to strengthen the economic power of the monopolies and the big business in the Indian economy. On the other hand, the nationalised banking system should become an instrument to put an end to anti-social tendency of the growth of a few at the cost of many in the country. It is only then that it would be possible for the Indian economy to achieve rapid economic growth.

Under the Chairmanship of Pandit Nehru, the National Planning Committee set up by the Indian National Congress had recommended regarding the key industries as follows:-

> "All these industries being key industries, their ownership or control should, in accordance with the previous decisions of the National Planning Committee, rest with the State".

This policy had found expression in the Industrial Policy Resolutions of the Government of India in 1948 and 1956. Hence it is beyond any doubt that even long before India became independent, it was decided that the key industries should be under public ownership. It should be realised that "finance" is more basic than even the basic industries as it is the very basis of any economic development. In any type of planning, "finance" acts as a lubricant to the wheels o development and determines the economic whether more directly than any other institution. Hence there is no rationale behind the argument that only key industries must be in the public sector and not the banking institution.

Appendix I

CONGRESS PARTY IN PARLIAMENT

Chandra Shekhar | 24-25 Parliament House
Secretary | New Delhi
12th August, 1967

My dear Dr. Goyal:

You must be aware that for the last few months the question of Bank Nationalization is receiving attention of the Indian people in general and that of the policy making sections in particular. undoubtedly, the question is essentially an economic one though it has direct implications for the social and political aspects of the Indian life as well.

A number of members of our Party in Parliament and outside have expressed their desire to me to get this problem of bank nationalization examined by a group of competent economists who may be in a position to offer their constructive suggestions with an overall perspective of the Indian society and its objective. I have no doubt the question will be also reviewed by the official agencies. And yet the value of an independent group of persons can never be over-emphasized.

It is with this idea that I thought I could approach you for help. I remember nearly four years back you had circulated a paper on the operations of banking institutions which was discussed in a seminar of the staff and research scholars of Delhi School of Economics. Since you have been a scholar of banking alongwith your other interests in the field of planning, I thought you may be kind enough to spare some time for preparing a report for us. I would, however, like to leave it to you to associate two or three other fellow economists who could deal with the question of banking in the light of the demands of the planning process and in that the rural sector in specific. If the report can be a comprehensive document it would provide the necessary perspective for taking a decision on a vital question of the Indian economy.

I hope you would be kind enough to prepare your report by the end of September, 1967. This is a very short notice but I can only hope that you would understand the importance of such a study to allow an enlightened and early discussion on this question.

With regards,

Yours sincerely,
Sd/-

Dr. S.K. Goyal | (CHANDRA SHEKHAR)
IIPA, New Delhi.

Appendix II

CONGRESS PARTY IN PARLIAMENT

Chandra Shekhar | 24, Parliament House
Secretary | New Delhi

Dear Kamarajji,

A few months ago, I had requested some of my economist friends to examine the question of bank nationalisation objectively and dispassionately and prepare a report. They have accordingly made a detailed study of the subject and compiled a report, a copy of which I herewith submit to you.

This study reveals the following among other important conclusions:

(a) The bank deposits have increased from Rs. 908 crores in 1951 to Rs. 3073 crores in 1965 and to Rs. 3500 crores at present. this means an average increase of about 16%. That is the reason why the banks have started having a commanding position over the nation's economy in general and financial resources in particular.

(b) In 1951, there were 566 banks (both scheduled and non-scheduled). In 1965 this number came down to 109. The reduction in the non-scheduled banks has been phenomenal, from 473 to mere 33 and scheduled banks from 92 to 76.

(c) There are 61 Indian scheduled banks today. Through these banks no less than about Rs. 350 crores are mobilised from poorer and backward States and diverted to highly developed States like Maharashtra, West Bengal and Madras, Rajasthan, for example, gets only a mere 1 % of the bank credit. In the 2 States, namely West Bengal and madras, the banks have given more credit than the deposits they have received there.

(d) The total paid-up capital of all the Indian scheduled banks (numbering 61) is Rs. 44.36 crores only. This has increased by building up reserve by about 50 per cent. The deposits on the other hand, have increased by nearly 240 per cent. As a result, the ratio of paid-up capital and reserve to deposits, has gone down from 9.7 per cent in 1951 to 3.4 % in 1965.

(e) 49% of the shares of the Central Bank were held by 3% shareholders and 36% shares were owned by 1 % of the shareholders.

In this connection the Governor of the Reserve Bank once said:-

"One of the structural features of Indian banking is this concentration of power which, in some cases, is enormous in relation to the capital actually employed. From time to time we come across cases in which a family or group has a controlling interest in a bank and it has become a major task of inspection to prevent the exercise of this interest in undesirable ways".

(f) According to the survey of Directorships of 20 leading banking companies a total of 188 persons served as directors on the boards of 20 leading banks. These 188 bank directors held 1452 directorships of other companies also. The total number of companies under these directors were 1100.

(g) Similarly, a detailed study of the directorships held by directors of 5 leading banks reveals that through common directors, these 5 banks are connected with 33 insurance companies, 6 financial companies, 25 investment trusts, 584 manufacturing and other companies and 26 trading companies and 15 non-profit making association.

(h) Debt due to the bank directors or their companies were nearly Rs. 56 crores in December 1954 but this amount rose to Rs. 291 crores in December 1965. The bank loans given to the directors and their companies in the same year stood at Rs. 317.4 crores.

If allowance is made for indirect loans and advances to the bank directors and their concerns this figure is expected to go somewhere between 600 and 700 crores.

(i) The total advances made by the banks in 1966 were Rs. 2,432 crores to about 9 lakhs accounts. Out of these, Rs. 1800 crores were lent to about 4,000 accounts only. It has also been brought out that in 1967, 572 borrowers were extended nearly Rs. 1400 crores out of the bank credit of Rs. 1800 crores even for industrial and commercial purposes.

If five to six hundred accounts were to be identified with industrial and business houses, one may find that number of borrowers were in fact only 4 or 5.

(j) In September 1953, agricultural loans stood at Rs. 19 crores whereas the same was only Rs. 3.9 crores in the year 1965. Not only the amount of absolute loans to agriculture has come down to 1/4th of what it was in 1953, but the more significant point is that the share of the agricultural loans in total bank credit declined from 3.8 per cent to its nearly 1/20th i.e. 0.2 per cent only.

(k) The bank credit has not been utilised for financing the projects according to the Plan priorities but has been invested in low priority projects or even in those which were outside the Plan.

(l) The powers of control in the hands of the Reserve bank for regulating the functions of the private banks are ineffective because the Reserve Bank has to be very cautious in exercising them lest the confidence of the public in banking in general and the concerned bank in particular, may be undermined.

(m) Even in USA, there is a ceiling for paying loans to a single concern. No bank can extend loans to any concern which is more than 10 per cent of the paid-up capital and reserve of the bank concerned.

The banks give credit to the directors and their associates at rates of interest much lower than those prevalent in the market. This benefit alone amounts to more than 100 crores per year. This means that besides the dividend they get on their shares they get a much more substantial benefit through this concession in interest rates.

(n) The deposits with the State Bank of India which were 220 crores in 1955 increased to 677 crores in 1965, that is, more than 3 times. This results the argument that after nationalisation the public deposits will fall.

(o) The private commercial banks have failed to be guided by the positive and social objectives laid down in the Five Year Plans.

(p) Easy and cheap availability of credit for a few industrial houses has encouraged the growth of monopolies and concentration of economic power.

(q) Pandit Jawaharlal Nehru made the following observation in the context of the Karachi resolution in 1931:

"In the Karachi Resolution it took a step, a very important step in a socialist direction by advocating nationalisation of key industries and services and various other measures to lessen the burden on the poor and increase it on the rich. This was not socialism at all and a capitalist sate could easily accept almost everything contained in the resolution".

Banks are key to the key industries. If you wish to nationalise the key industries, you must first nationalise the banks. That is inevitable.

I hope that above points would help the deliberations on this important issue at all levels. I am sending a copy each of this Report to Indira Ji and Morarji Bhai.

With personal regards,

Yours sincerely,

Sd/-

(CHANDRA SHEKHAR)

Shri K Kamaraj

President, AICC

7 Jantar Mantar Road, New Delhi - 1