

UNIVERSAL BANKING IN INDIA : ITS RETROSPECT AND PROSPECT

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PREFACE

The commercial banking was developed in India in the 19th century after the prototype banking model which was characterised with the mobilization of deposit and sanction of working capital loan. The familiarities of pioneer Indian banks who hailed from the British community with that system might explain to some extent why India assumed that particular type of banking. But a more important explanation was that never being worried about India's economic development, Britain was interested only in her import-export trade which was required to be financed by the banking system through short-term loans.

There were, however, some nationalist countries in the contemporary world like Germany, Japan etc. where the banking system the so-called universal banks used to provide term finances also in conjunction with working capital.

In the absence of any term financing institution, however, India gave birth to the managing agency system which nurtured her industrial development over the countries. These managing agents had so monopolised the industrial sector that they, on the one hand, prevented the diffusion of entrepreneurship among a wider spectrum, and earned, on the other, high rates of return from investment in a very limited number of industries. The resultant narrow bases of both entrepreneurship and industrial structure were not, however, considered conducive to further industrial development and were sought to be

rectified by the independent India by reducing the importance of the managing agency system in the country. The herculean task thereby, bestowed upon the Indian planners particularly, during post-independence era to tackle the economic stagnation for attaining the objectives like accelerated rate of industrial growth which needed introduction of term financing institutions in India.

In such circumstances, the Government of India established a series of development finance institutions (DFIs) in the post-independence era. Simultaneously with the establishment of development finance institutions, however, India also sought to introduce term-financing in the existing commercial banking network so as to herald an era of universal banking in the country. Commercial bank's move to this new dimension was also endorsed by a number of committee.

We thus find two term financing institutions namely commercial banks and development finance institutions in term lending sinario in India after independence. Such a development may be appreciated only if these institutions are found complementary to each other or they are almost equally competent in term financing. On the other hand, if we find only of them more competent than the other, there remains no reason for the continuation of the system. In this connection mention may be made that development finance institutions have shown their inefficiency in a number of third world countries as an

industrial financier which is revealed in a number of studies conducted by the World Bank. So, it is opined in these studies either closure of development finance institutions or merger with the commercial banks.

In this study we will examine the reasons which were responsible for the genesis of universal banking in India, their growth and role as an industrial financier and their viability in industrial financing. To encounter the objectives, appropriate hypothesis have been tested by both financial and statistical tools.

On completion of the present research investigation, I take the opportunity to express my deep sense of gratitude and indebtedness to my revered guide Dr. Indrajit Ray, Department of Commerce, University of North Bengal for his valuable guidance and sustained interest at all stages of this research work. Despite his busy schedule of work, he always took keen interest all along and spared considerable time for me often sacrificing his extremely limited leisure period. It is needless to say that without his apt guidance the present study would not have seen the light of the day. He will remain a constant source of inspiration to me throughout my life.

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I am equally beholden and enriched by writings and ideas of many authors in this disciplines of study and the bibliography attached at the end of the thesis bears testimony of the same.

I am very much thankful to Dr. Saha, Director, Reserve Bank of India Library, Calcutta, for his keen interest he has shown in my work and for kind words of encouragement.

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C O N T E N T S

	Pages
List of Tables	viii
List of Annexures	xi
INTRODUCTORY :	xii
Chapter I : Universal Banking ; an International Perspective	1
Chapter II : Trend of Universal Banking in India Before Independence	55
Chapter III : Trend of Universal Banking in India After Independence.	101
Chapter IV : Assessment of Universal Banking ; a Theoretical Framework and Model Specification	134
Chapter V : Cost Efficiency of Universal Banking in India : Evidences from Cross Section data.	150
Chapter VI : Summary of Observations and Policy Implications.	167
Select Bibliography.	186

: : : : :

List of Tables

	Pages
1.1 Economic Backwardness and Sources of Capital Supply	4
1.2 Industrial Growth Rate in Italy During the Period 1891-1913.	9
1.3 Industrial Growth Rate in Russia During the Period 1885-1913.	10
1.4 Group of Bank Deposits (including Current A/C balance)	20
1.5 Deposits and Current Account Balances as Percentage of Total Working Funds	23
1.6 The Relative Importance of Long-Term Deposits in City and Country Banks in Japan.	24
1.7 Reporting Member Banks in U.S.A. Net Demand and Time Deposits.	26
1.8 Reporting Member Banks in New York City, Net Demand and Time Deposits.	27
1.9 Securities as Percentage of Total Assets of German Universal Banks.	31
1.10 Growth of Universal Banks in Japan	33
1.11 Universal Banks Credit to Industries in Japan	34
1.12 Securities Held by Four 'Big' Universal Banks in Japan	35
1.13 Growth of Universal Banks in U.S.A.	36
1.14 Loans and Investments of All Member Banks	37
1.15 Net Profits as a Percentage of Capital Funds of Insured Commercial Banks in United States of America.	40
1.16 Addition to and Deduction from Net operating Earnings of Insured Commercial Banks.	44
1.17 Security Profits and Losses. All Insured Commercial Banks.	49

	<u>Pages</u>
1.18 Percentage of Net Profit on Paid up Capital and surplus of universal banks in Japan	43
1.19 Percentage of Net Profit on Paid up Capital and Reserve of British Banks	44
1.20 Expenses as % of Gross Profit of German Universal Banks	45
1.21 Yearly Dividend Rate of German Universal Banks	46
2.1 Joint Stock Companies in India in 1914	56
2.2 Paid up Capital and Reserves of Indian Joint Stock Banks	63
2.3 Trend of Time Liabilities of Joint Stock Banks	65
2.4 Growth of Universal Banks in India Before Independence	67
2.5 Capital and Reserve, Deposit and Cash Balances of the Principal Universal Banks	72
2.6 Proportion of Cash Balance to Deposits of Indian Banks	73

	Pages
2.7 Some Swadeshi Enterprises and Their Service Life.	81
3.1 Amount of Capital Outflow from India on the Eve of Independence .	91
3.2 Level of Repatriated Public Debt	91
3.3 Proportion of IFC Financing to ^{the} Total External Long Term Financing of the Public Ltd. Companies.	93
3.4 Population Group-wise Distribution of Commercial Bank offices .	95
3.5 Commercial Banks (Capital and Reserves) .	103
3.6 Deposit Trend of Scheduled Commercial Banks .	104
3.7 Trend in Time deposits and its ^{influence} on Term Lending to the industry by Scheduled Commercial Banks.	107
3.8 Industrywise Distribution of Term-loan from Scheduled Commercial Banks .	109
3.9 Banks and their Relative Shares of Underwriting of Corporate Shares.	114
3.10 Investment in Shares and Debentures of Joint Stock Companies by Scheduled Commercial Banks .	116
5.1 Deposit Level of Sample Branches,	143
5.2 Total Expenditure and their Components .	145
5.3 Working Capital and Term Loans	147
5.4 Product Specific and 'Overall' Scale Economies ,	155
5.5 Simple Co-relation Co-efficient between the Firm Size and Scale Economies ,	158
5.6 Scope Economies.	161

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List of Annexures

- 2.1 Balance-sheet of the People's Bank of Punjab, 30th June, 1910.
- 2.2 Balance-sheet of the Specie Bank Ltd., 30th June, 1908.
- 2.3 Balance-sheet of the Specie Bank Ltd., 30th June, 1910.
- 2.4 Balance-sheet of the Bengal National Bank Ltd., 30th June, 1910.
- 2.5 Balance-sheet of the Amritsar Bank Ltd.
- 3.1 Financing of Project Cost During 1966-1982.
- 3.2 Financing of Projects by Companies which issued capital by Prospectus.
- 5.1 Research Survey on Term Financing by Commercial Banks in Siliguri Region.

INTRODUCTORY

The idea of adopting universal banking must be new to most of the developing countries which today maintain well-graded, stratified and specialised financial structures. The evolution of universal banking system indebt to the conservative outlook of the commercial banking practice which avoids long-term financing and consequently to the growing need to fill the demand supply gap in long-term capital requirement. To meet this vital requirement government in many countries emerged as a promoter of specialised Development Finance Institutions (DFIs). As per the studies completed by the World Bank, DFIs in third world countries have shown their inefficiency taking part in their rapid economic development process.

There are three approaches to the universal banking. One lies in commercial banking sector with large deposit base taking up additional development banking functions; the second in development banking sector taking up additional commercial banking functions and the third in acquisition of or merger/ amalgamation with one set of institutions by the other.

As for India is concerned, by the turn of this century particularly during the Swadeshi movement period adopting first approach to the universal banking, commercial banks did development banking here along with the commercial banking functions to meet the need for short as well as long-term capital requirement of the Swadeshi enterprises. But those banks failed

within a short period of their inception.

After independence, Government of India put the point of rapid industrialization on the top of its economic agenda. For getting industrial capital a number of Development Finance Institutions (DFIs) were established by the government on the one hand and on the other, existing commercial banks were encouraged to do their functioning following the principle of universal banking which opened an era of banking activities to the new dimension in India.

In international perspective a number of studies have been devoted on universal banking of Germany, Austria, Japan, United States of America. These studies include "Economic Backwardness in Historical Perspective", "Joint Stock Banking in Germany", "Functional and Structural Aspects of the German Universal Banking System", "Banking and Finance in Germany", "Financial System of Japan", "A Monetary History of the United States (1867-1960)", "Banking and Industrialization in Austria - Hungary". These studies have concentrated their investigation on the causes behind the genesis of universal banking, growth aspect of universal banking in those countries, strength of their relationship with the industries and how far this banking was viable in their functioning.

In respect of India, a scanty of study has been reported on universal banking. In some books and government reports like "Industrial Finance in India", "Indian Financial System",

"The Changing Structure of Industrial Finance in India", "Narashimham Committee (1991)", "Indian Central Banking Enquiry Committee (1991)", we find discussion on universal banking. So far as academic investigation in this field is concerned, we may refer a little number of studies. They are the "Commercial Banks and Industrial Finance-Term-Lending and Underwriting" where commercial banks role as a provider of term-loan under the refinance scheme along with their participation in corporate shares and debentures have been investigated. Another study namely "Universal Banking System : A case for Adoption in Developing Countries" focusses on the conservative outlook of the commercial banks which avoided long-term financing and growing need for such finances to the industrial sector has helped to introduce universal banking in underdeveloped countries. One more study titled "Cost Efficiency of Universal Banking in India : An Analysis of Scale and Scope Economics" has found evidences from time-series data that there exist substantial scale economics among Indian nationalised banks to do universal banking. The same hypothesis can be examined on the basis of cross section field survey data.

These studies have not extensively examined the genesis of universal banking in India both in pre and post independence period, their growth and role as an industrial financier is not yet investigated and also viability aspect of universal banking within the commercial banking set up has not yet been tested in

Indian context taking cross section field survey data.

Objective of the Study

In the absence of term financing institutions before independence, managing agencies used to provide industrial term-loan to the industries in India. Their objective was to prevent diffusion of entrepreneurship in one hand and on the other earned high rates of return on investments. In addition to that absence of the enrich stock market, conservative outlook of the non-banking institutions like insurance companies and apathy of the imperialist government towards industrial financing were creating barrier on the path of industrial development. After the independence, the industrial policy resolution which was announced from time to time spelt out faster growth of industries in every part of the country. Consequently, industrial financing became major issue. Government promoted a number of Development Finance Institutions (DFIs) and at the same time started to encourage the existing commercial banks to provide term-loan (development banking activities) along with commercial banking activities. Thus we find two parallel institutions in term-lending scenario in India. One is Development Finance Institutions (DFIs) and other is commercial banks. Such a development may be appreciated only if these two institutions are found complementary to each other or they are almost equally competent in term of

financing. On the other hand if we find either of them more competent than the other, there is no reason for the continuation of the system.

It should be noted in this context that there are two versions about the relative competence of commercial banks and Development Finance Institutions (DFIs) in term-lending. Mention may be made that a number of studies devoted by the World Bank on third world countries reveal that DFIs has shown their inefficiency as an industrial financier. So, it is opined in those studies either closure of Development Finance Institutions (DFIs) or merger with the commercial banks. In this background, the proposed study aims to progress with the answer of the following research questions :

1. In international perspective whether the universal banks are successful or not ? If yes, what are the characteristics of those successful universal banks ? Whether those characteristics of successful universal banks applicable to Indian context or not ?

2. Does the universal banking exist in commercial banks in India ? If yes, whether this banking is a successful one or not ? Is there any example of unsuccessful universal banks in Indian context ? If yes, what are the reasons behind their failure ? Whether these reasons still remain with the universal banks in India or not ? We will investigate these points in our study.

3. What are the efficiency levels of commercial banks as universal bankers in comparison to the commercial banks with only commercial banking activities ?

Hypotheses

Following null hypothesis are framed to meet the above objectives for the proposed study :

1. Internationally universal banks do not run successfully.
2. In Indian context, commercial banks functioning as universal bank have not enlarged their activities (industrial finance) remarkably ?
3. In relation to objective (3) we intend to frame two sub-hypotheses :
 - (a) There is no scope of introducing long-term financing by the Indian commercial banks.
 - (b) There is little scope of universal banking in commercial banks in India.

Methodology

Both the secondary as well as primary data are used to complete this study. To substantiate the hypothesis whether universal banking in international perspective was unsuccessful or not we have studied the literatures relating to the experience of the similar type of banks in the countries like Germany, Japan and the United States of America. The literatures and official documents what we have consulted in this relation include "Economic Backwardness in Historical Perspective" by Alexander Gerschenkron; "Multipurpose Banking" IMF Staff Paper by Khatkhate, D.R. and K.W.Riechal; "Economic Development in the Third World" by M.P.Todaro; "Why Universal Bank Works" by F.W.Christians; "Industrialization and Foreign Trade" by League of Nations; "A Monetary History of the United States (1867-1960)" by M.Friedman and A.J.Schwartz; "Joint Stock Banking in Germany" by P.B.Wahle; "A Short Economic History of Modern Japan" by G.C.Allen; "Banking in Modern Japan" by Fuji Bank Ltd.; Glass Steagall Act, 1933; Reserve Bank of India Bulletin-1956; "In Defence of Universal Banking" by L.Malhaupt; "The Security Affiliates of National Banks" by W.Nelson Peach; "Economic Report of the President of the United States of America in 1971; "Investment Banking in America" by V.P.Carosso etc.

The hypothesis "Universal banking in Indian context was unsuccessful" substantiated under some sub headings. The

sub headings are genesis of universal banking before independence, their role as an industrial financier and causes of their failure, need for universal banking after independence, regulatory framework and role as an universal banker. To make eye to eye analysis of the genesis of universal banking before independence the literature which we have consulted include "The Evolution of the State Bank of India" by Anya Kumar Bagchi; "Parliamentary Papers (1860)" — House of Commons; "Indian Currency and Finance" by J.M.Keynes; "Industrial Finance in India" by S.K.Basu; Indian Central Banking Enquiry Committee (1931); Summary of Capital and List of Shareholders Made upto 31 January, 1896 - The Abbion Jute Mills Ltd., Calcutta; Calcutta Review (1937); The Indian Insurance Act, (1938), Section 27(1); "Study on Managing Agency System" by The Economic and Scientific Research Association; Indian Industrial Commission (1916-18); "The Managing Agency System — In Retrospect and Prospect by S.K. Basu; "Organisation and Finance of Industries in India" by D.R.Samant and M.A.Mulky; "Banking and Industrial Finance in India" by N.G.Das.

To verify the role played by the universal banks in pre-independence period as an industrial financier as well as the causes behind their failure, we needed data relating to the pioneer universal banks functioned like the Peoples Bank of Punjab, The Credit Bank, The Specie Bank, The Lahore Bank, The Hindusthan Bank, The Bengal National Bank, The Tata Industrial Bank Ltd., The Calcutta Industrial Bank, The Indian

Industrial Bank, The Indian Industrial Bank, The Mysore Industrial Bank, The Industrial Bank of Western India, The Karnani Industrial Bank, The Raikat Industrial Bank and the Laxmi Industrial Bank. These banks tryed their level best to fill the gap of industrial finances in this country before independence. After covering a short survival period almost all of them compelled to close their doors. In this relation we have collected data from the official documents of the concerned banks and also we have consulted some research oriented books and journals. They are the Indian Industrial Commission (1916-18), The Indian Central Banking Enquiry Committee (1931), The External Capital Committee (1924), Prospectus of Calcutta Industrial Bank and Tata Industrial Bank (1919), Liquidator's Report of the Bank of Burma Ltd. (1911), Balance Sheet of Tata Industrial Bank (1918), Balance Sheet of Indian Industrial Bank (1921), various issues of 'Capital', Economic Backwardness in Historical Perspective by Alexander Gerschenkron, Modern Banking in India by S.K.Muranyan, Industrial Finance in India by S.K.Basu, Joint Stock Banking in India by D.S.Savarkar, Swadeshi Enterprises in Bengal (1900-1920) by Amit Bhattacharya and genesis of Development Finance Institutions in India by Tarun Bandyopadhyay and Indrajit Ray. So far as need for universal Banking after independence is concerned, we required data relating to the outflow of British Capital from India on the eve of independence which was the primary barrier of industrialization in

post independence period. To substantiate this point a number of literatures have been consulted. They are the 'India's Balance of Payment' by A.K. Banerjee; 'Foreign Investment in India' by M. Kidron; 'Planning and Economic Policy in India' by D.R. Gadgil; 'Decentralised Planning - The Karnataka Experiment' by Dr. Abdul Aziz; 'Planning Commission' by Government of India; 'Financial Intermediaries' by M.S. Joshi; 'Development Financing Institutions and Multipurpose Banking' by P. Mistry; 'Functioning of Public Sector Banks' - Report of the Committee by Reserve Bank of India; 'Report of the Industrial Licensing Committee' by S. Dutt and 'Indian Banking Since Independence' by Kalipada Deb.

So far as the question of banking regulation and opinion of the expert committee on universal banking is concerned, Section 6(a) of the Banking Regulation Act, 1949; Indian Companies Act, 1913; Opinion of the IMF Mission headed by Barnstain (1953); Shroff Committee Report (1954); Appraisal of Term-Loan (Report of the Working Group on appraisal of Application of Term Loans) by Reserve Bank of India; 'Banks and Medium-term Credit to Industry' by B.K. Madan; Narasimham Committee (1992) Report are helpful in getting answer of the above question. In order to explain the point of Universal bank's role as an industrial financier we have collected data relating to the demand and time deposits in consultation of various issues of Reserve Bank of India Bulletin, Trend and Progress of Banking - Supplement to the Reserve Bank of India

Bulletin, Basic Statistical Return - Supplementary to the Reserve Bank of India. In addition to that we have consulted Shroff Committee Report (1954); 'Commercial Banks and Industrial Finance - Term-Lending and Underwriting' — M.Y.Khan and Preeti Singh; 'Report of the Working Group on State Financial Corporation' by Reserve Bank of India.

The hypotheses relating to the efficiency of commercial banks for providing term-finances, both in absolute sense and relative to DFI's will be investigated from the view point of economics of scale and scope. In this study we have estimated two types of cost relationships for measuring scale and scope efficiency. They are the conventional translog cost function and hybrid translog cost relationship. To develop new model and to collect relevant data in favour of examining the efficiency of universal banking within the set up of commercial bank we have collected data in consultation of a number of articles published in the journal at both the national and international level. They are the "Cost Efficiency of Universal Banking in India : An Analysis of Scale and Scope Economics" by Indrajit Ray; "Scale Efficiency in Indian Commercial Banking : An Econometric Investigation" by Ray Indrajit and Sumita Sanyal; "Competitive Viability in Banking : Scale, Scope and Product Mix Economics" by Berger, A.N., G.A. Hanweek and D.B. Humphre; "Branching Restrictions and Banking Cases" by Bino, M.J., Eakin, B.K.; etc.

Thus, the proposed study will be essentially based on historical and analytical methods. In fact, historical method would help to explain the background of the origin of the universal banking system whereas the analytical part would explain the course of its operation. In other words, for the meaningful completion of such studies, references should be made to both primary and secondary source-materials. The above presentation would clearly indicate that all the relevant documents and other primary source materials will be thoroughly examined along with the findings already made, though from different perspectives, by other scholars. As because efficiency of universal banking in India's respect is investigated by Dr. Indrajit Ray at firm level taking time series data, this study will examine same hypothesis at plant level taking cross section field survey data. Question may come why we have used plant level data instead of firm level data ? Answer will be that an exclusive plant-level model can yield more powerful conclusion than what a single variable in the firm-level model can. Note that a joint study conducted by Sumita Sanyal and Dr. Indrajit Ray reveals that the plant -level scale economics have been sought to be measured by incorporating a 'branching' variable in the cross section model at the firm level and drew a powerful conclusion.

Considering all these points we will collect cross section field survey data (at plant level) from the schedule commercial bank branches in the district of Darjeeling , West Bengal where banking business is showing trend of gradual increase , to measure efficiency of universal banking .

Scope of the Study

Capital formation in accelerate pace is one of the fundamental requirements of most of the industrializing economies. For capital formation it needs to rely chiefly on the capacity of the financial system to garner up term deposits and to transfer them into productive capital. The performance of such a vital function can be achieved with greater when there is a prudent combination of development banking and commercial banking. In the liberalised economic environment like ours capital formation has also got its vital importance in response to her rapid industrialization process which was started just after independence through a series of five years plan. In this circumstances commercial banks were getting encouragement from different corners to take part in long-term financing to the industries along with their short -term financing activities. In 1951 one IMF Mission headed by Mr. Bernstein visited India. Opinion of the commission was in favour of the commercial bank's participation in universal banking. To investigate into the matter of commercial bank's functioning adopting principles of universal Banking, Reserve Bank of India appointed a committee under the chairmanship of A.D.Shroff which is popularly known as Shroff Committee. The Committee's suggestion was not different from the opinion expressed by the IMF Mission. Naturally question comes why commercial banks are the favourable choice of the expert committees in doing universal banking in India ?

The commercial banks in India are in a suitable position in doing universal banking with their rapid growth of deposits which they mobilize through their vast branch network covering both the rural as well as urban areas. On the other hand Development Finance Institutions are mainly dependent on government for their resources. In addition to this, the branches of Development Finance Institutions are located only in the big town areas. Thus scope of universal banking within the set up of commercial bank is not less important.

On the other hand if unused capacity of the commercial banks is used for development banking purpose it will be undoubtedly a cost saving device in one hand and on the other it will be helpful to our industries to get all types of financial assistances in time from the same institution. Commercial banks in Japan, Germany and the United States of America are the examples to this end. As because, capital formation is the emerging needs of the liberalized Indian economy, government aims at the restoration of a prudent, viable, efficient and internationally competitive banking system here. Aims of the Government can be fulfilled when there is a prudent fusion of commercial banking with development banking within the commercial banking set up.

Very recently Development finance institutions in India like IDBI, ICICI have opened their deposit mobilizing wing. Object behind this step taken by the Development finance institutions is to accept the principle of universal banking. It indicates that the scope of universal banking on Indian soil is expanding in response to her open market economy.

Sampling Procedure

There are sixty one branches of different commercial banks in the study area of Darjeeling district. Instead of sampling such a thin set of population, we have initially sought enumerate census, and have accordingly approached all of them with a structured questionnaire. As because security scam of Harshed Meheta was fresh in mind of the bank official at that time, it was not possible in most of the cases to derive all relevant informations only through questionnaire, so attempt has been made to collect informations through direct and personal interview of the branch managers. Out of sixty one bank branches, twenty branches responded fully and eleven responded partially. The sample set covering one-third of the population was thus fairly representative in character and showed a high degree of randomness in view of no preconceived design in sample selection. Requisite data were collected for three consecutive years so that the estimations could be repeated to ensure temporal stability of result.

Analysis of Data

The data collected from the survey have been analysed in a number of ways. The generated data are presented in a tabular form to gather an initial impression about the scope of universal banking and the nature of scale economics among the sample branches. In our study we will estimate the

conventional translog and hybrid translog cost functions with two sets of independent variables : (X_1, X_2, W) and (X_1, X_2) . X_1 indicates commercial banking activities (aggregate of various types of deposit and short-term loans), X_2 indicates development banking activities (term-loan sanctioned to the industrial sector) and W indicates average salary and wages per employee. As because conventional translog cost function is not always suitable to measure scope economics, we will adopt hybrid translog cost relationship to measure the same. In certain case estimation of both the conventional and hybrid translog cost function with wage rate give insignificant value of F statistics. So, our attempt will be to estimate alternative relationship where wage rate (W) will be excluded.

Limitation of the Study

This study does not include investment in corporate shares and debentures by the sampling branches as development banking activities by the commercial banks. Because such practices are absent among the sample banks. Further, being unable to guess the significance of such research study, some of the bank official raised queries on the purpose of the study. However, with great deal of persuasion the present researcher could establish cordial term with bank officials and could collect the required data.

Chapter Scheme

This thesis begins with the international perspective on universal banking followed by pre-independence experience and post-independence experience of universal banking, model specification for assessing the efficiency of universal banking, empirical result analysis and summary and policy implications.

Organisation of materials in the above mentioned chapters is as follows :

First chapter starts with a brief discussion of genesis of universal banking in three countries namely Germany, Japan and the United States of America where universal banking achieved a rapid progress and highlighted how banking regulatory framework helped the universal banks in those countries to work in this new dimension. The feasibility aspect of universal banking is studied taking into account the trend of time deposits - the principal means of long-term ends. After studying the feasibility aspect, role of universal banking in the economic development of the countries is discussed. Finally, viability aspect is studied taking into consideration the return on capital fund and the trend of dividend declared by the universal banks. In Indian context, the need for universal banking before independence, feasibility aspect from the view point of the trend of time deposits, role as an industrial financier and finally causes of their failure are

discussed in Chapter II. Following the same style, universal banking in post-independence era is discussed in Chapter III under the headings given below :-

- i) Need for universal banking after independence.
- ii) Regulatory frame work and opinion of the expert committee in relation to the universal banking within the commercial banking set up.
- iii) Feasibility aspect from the view point of increasing trend of time deposits with the commercial banks.
- iv) Role of universal bank as an industrial financier.

In Chapter IV universal banking literatures are reviewed and models developed for assessing viability of universal banking in India. And finally in Chapter V results of the models developed in Chapter IV are discussed.

CHAPTER I

UNIVERSAL BANKING : AN INTERNATIONAL PERSPECTIVE

Part I : INTRODUCTION

The banking system was first developed in its modern form¹ in United Kingdom as an institution of accepting private deposit and of providing short-term capital. But this Anglo-Saxon banking system could not retain its style down the centuries world-over. The first blow fell on it with the establishment of Credit Mobilier in France in 1852 which started providing long-term loans and yeomanry services to industrial enterprises in contrary to the Anglo-Saxon banking principles. This practice snowballed subsequently in the german banking system, and it flashed so extensively then as to go now under the name of German style of banking. The interaction between these alternative forms of banking practices gave birth to universal banking in the world scenario. It is a combination of Anglo-Saxon and industrial banking in that both deposit mobilisation and short-term financing on the one hand, and consultative services and long-term financing on the other are practiced under this form of banking.^{1A} A salient feature of universal banking is that a direct and close link exists between the bank and the borrowing unit which is maintained through current accounts. The meaning of current account differs from country to country but in almost all, credit limits are sanctioned on the basis of certain securities and borrowers then use these limits when needed for short-term as well as long-term purposes. Following Germany, this form of banking practices was introduced in Japan and the United States of America.

There are, however, different~~e~~ of opinion behind the evolution of banking system in this direction.² A widely acceptable hypothesis in this field has been put forward by Alexander Gerschenkron who explains the causes behind the departure from commercial banking to universal banking in a country by the degree of its industrialization relative to that in Britain.³ The cause of the emergence of universal banking having thus been studied at length the present chapter seeks to critically analyse the feasibility and viability of universal banking in world perspective. The study has been conducted in respect to three countries, Germany, Japan and the United States of America where the universal banking ~~has~~ achieved a rapid progress.

It starts with a brief discussion of universal banking development in those countries in part II and sketches a description of its regulatory framework in part III. The question of feasibility of universal banking is studied in part IV. The investigation is based here in the main on the extent of their time deposits - the principal means of financing long-term ends. In part V we have analysed the role of universal banking in the economic development of the countries under study. Part VI delves into the viability aspect of universal banking. It studies in particular the return on capital fund and the trend of dividend declared by the universal banks. These are followed by a summary of observation in part VII.

Part II : CROSS COUNTRY GENESIS OF UNIVERSAL BANKING

The idea of adopting universal banking is not new to most of the developed and developing countries in the world. According to Alexander Gerschenkron, these institutions were first established during the nineteenth century in some less-developed countries in Europe under inspiration from the Saint-Simonian philosophy of nationalism for attaining the state of industrial development in Britain.⁴ He substantiates this hypothesis on the strength of his evidence that universal banking evolves in a country where industrialization has a time distance from its birth place in England. When England started to industrialize with relatively small scale enterprises she required little capital and specialised entrepreneurship. Long-term capital requirements of them were fulfilled by their own sources or ploughing back of profit.⁵ No outside agency was required to supply either long-term capital or entrepreneurship because the entrepreneur himself was the source of both.⁶ It was one reason among many which impelled the commercial banks in England to emphasise short-term lending. Industrialization in England was an outgrowth of commercialization that evolved high turn over of capital. Naturally, therefore, the commercial culture dominated the functions of banks, which emerged to meet the needs of expanding industry. Apart from this, the more adventurous section in England^{W.H.} was seeking new avenue to make more profit by employing their surplus fund, came forward to invest in the industries. As a result, no support from outside agency was

called for. When moderately backward countries like Germany started industrialization, technology and markets were more complex than the period when Britain started her industrialization process and average size of plants required for production were also needed to be larger to remain in competition with Britain. So, moderately developed countries required larger amount of block capital to purchase heavy plant and machinery.^{6A} To fulfil this requirement universal banks evolved there as a prime source of capital as well as entrepreneurship. The relationship between the industrial units and the sources of their capital supply was expressed by Gerschenkron as follows :

Table 1.1

Economic Backwardness and Sources of Capital Supply

Stage	Advanced Area	Area of Moderate Backwardness	Area of Extreme Backwardness
I	Factory	Banks	State
II	-	Factory	Banks
III	-	-	Factory

Source : Gerschenkron, A. Economic Backwardness in Historical Perspective, p.355.

Gerschenkron identifies three typical cases for the supply of initial capital and entrepreneurial services to the industries. In advanced region entrepreneurs' own savings are the source of initial capital for their industries. In extremely backward regions the state functions as a supplier of initial industrial capital whereas in moderately backward region banks are the prime source of initial industrial capital.

To measure the degree of economic backwardness of a country in respect to England Gerschendron specifies six characteristics which are given below :⁷

i) The country experiences a discontinuous, sudden, great spurt proceeding to a relatively high rate of growth of manufacturing output.

In
ii) Backward countries industrialization stresses on bigness of both plant and enterprise in comparison to the advanced countries where industrialization started earlier than the backward countries . Thus it requires to make large investment programme for industrialization in backward countries to purchase machinery of improved technology ^{in order} to remain in competition with the developed countries.

iii) The more backward a country's economy, the greater is the stress upon producer goods as against consumer goods. As a late comer the backward countries emphasize upon the machine-making industries which ultimately help to produce consumer goods.

iv) The more backward a country's economy, the heavier is the pressure upon the levels of consumption of the population.

The more backward a country's economy, the greater is the part played by special institutional factor to increase supply of capital to the nascent industries and entrepreneurial guidance. Note that in extremely backward countries ^{the} state takes initiative to supply capital to the nascent industries.

vi) The more backward a country, the less likely is its agriculture to play any active role by offering to the growing industries the advantages of an expanding industrial market based, in turn, on the raising productivity of agricultural labour.

Considering ^{the} above characteristics we will proceed to examine the genesis of universal banking in different countries of the world. Gerschenkron applied his hypothesis to Italy and Bulgaria - with inconclusive result. But it was more accurate in ^{the} case of United Kingdom, Germany and Russia in particular.

The industrial scene in Germany during the first half of the 19th century was not so impressive in comparison to other developed countries like United Kingdom, France etc. for various reasons.⁸ One of the main reason was political non-unification among the 38 sovereign states in Germany. In the absence of such unification in Germany industrial growth was stagnated and also the need for an unified market was badly felt. During 1790-1815, ^{the French} occupation did land reforms in Germany through abolition of feudal restriction and dissolution of guild system. On account of these reforms far reaching results were seen in the traditional corporate society. Since 1815 Germany was proceeding step by step in the field of industrialization.⁹ The manufacturing sector particularly textile industries were growing in response to foreign demand and the elimination of tariff barriers in 1834. By the end of 1840 a few iron, steel, engineering and machine making industries were set up.¹⁰

construction of

But it was the rail-roads, ^{which} which really made possible Germany's modern industrial development faster. By the end of 1846 more than 2000 miles of railways were opened in Germany which fostered the heavy industries providing easy transport facilities.¹¹ Thus the production of pig iron in 1850 was 5,29,000 tons whereas in France pig iron production was 8,98,000 tons. But in 1875 pig iron production in Germany rose to an impressive quantity of 20 lakh tons whereas production of pig iron in France was only 14 lakh tons¹² which fits the Gerschenkron hypothesis that more backward a country's economy, heavier is the pressure upon raw material of machine-making industry rather than production of consumer goods to remain in competition with the developed countries. One of the reasons for this dramatic improvement in production was availability of cheap labour supply due to raise in population. In 1871 the total population strength in Germany was 41 millions which rose to 68 millions in 1915.¹³ The rapid growth in population also helped in getting the expanded market for industrial goods in Germany.

Germany as an area ^{which is} of moderately backward, had fewer potential entrepreneurs and less availability of liquid capital for its industries. To solve this problem, banking evolved there as a paragon of the type of the universal bank which became the prime source of capital and entrepreneurship. According to Gerschenkron¹⁴:

The inadequacy in the numbers of available entrepreneurs could be remedied or substituted for by increasing the size of plant and enterprise above what otherwise would have been an optional size. In

Germany, the various incompetencies of the individual entrepreneurs were offset by the device of splitting the entrepreneurial function : the German investment banks - a powerful invention, comparable in economic effect to that of the steam engine - were in their capital - supplying functions a substitute for the insufficiency of the previously created wealth willingly placed at the disposal of the entrepreneurs. But they were also a substitute for entrepreneurial deficiencies. From their central vantage points of control, the banks participated actively in shaping the major - and sometimes even not so major - decisions of individual enterprises. It was they who very often mapped out a firm's paths of growth, conceived far-sighted plans, decided on major technological and locational innovations, and arranged for mergers and capital increases."

Italy during the decades following its political non-unification was very backward in relation to England. To understand the speed of industrialization in Italy before 1914 Gerschenkron considered four sub-periods.

Table 1.2

Industrial Growth Rate in Italy During the period 1891-1913

Sub-periods before 1914	Remarks	Growth Rate
1881-1888	Moderate Growth	4.6
1888-1896	Stagnation	0.3
1896-1908	Very rapid growth	6.7
1908-1913	Reduced rate of growth	2.4
<u>1881-1913</u>	-	<u>3.8</u>

Source : Gerschenkron, A., Economic Backwardness in Historical Perspective, p.76.

From the table 1.2 it is clear to us that there was a great leap in industrial development in Italy between the period 1896-1908. This period was featured with a rapid increase of producers' goods in total output. The statistics computed by Gerschenkron revealed that the share of producers goods which was 43 per cent of total output in 1908 increased to 47 per cent in the year 1913.¹⁵ The more belated the big industrial spurt, the stronger it is likely to be when it comes. The rate of industrial growth in Italy during the period 1896-1908 was 6.7 per cent which was lower than Russia (8.3%) but more than Germany (5.5%).¹⁶

It may be mentioned in this connection that Italian Government's participation in and contribution to the big industrial spurt certainly fell far short of what might have been expected in other countries like Russia. Direct and indirect tariff imposed on industrial raw materials or on the elements of production hampered industrialization in Italy.¹⁷ In these circumstances the big banks in Italy played an important role for industrial development after 1895. As in Germany, the universal banks in Italy not only supplied capital to the nascent industries but also provided them entrepreneurial guidances and took part in the decision making functions of the related concerns.

In Russia, which was even more backward than Germany, the big spurt of industrialization took place in 1890. To understand the annual growth rate in industrial sector in Russia before 1913

The following table may be considered :

Table 1.3

Industrial growth Rate in Russia During the Period 1885-1913

<u>Sub-period before 1914</u>	<u>Annual growth rate</u>
1885-1889	6.1%
1889-1899	8.3%
1900-1906	1.45%
1907-1913	6.25%

Source : Gerschenkron, A., Economic Backwardness in Historical Perspective, p.183.

From the Table 1.3 it seems that the period 1889-1899 was characterised as the period of highest industrial growth in Russia, government policy in favour of industrialization in Russia was not less important. Through land reform, ^{17A} the government allowed the peasants to hold less area of land than had been assigned to them before the reform. ^{It} was a positive step in the field of industrialization. The inadequacy of land holding compelled them to sell their land like their counterpart in the west and used the proceeds for establishing themselves outside agriculture. In such a way their dependence on agriculture was minimised gradually and the peasants who left countryside created a large reservoir of labour supply to the nascent industry.

According to Gerschenkron Russia was an extremely backward country. When industrialization started there technology and

markets were more complex. Large scale plants were necessary to compete with the developed and moderately backward countries. To meet the need for huge amount of investment of block capital in setting up of industries, ^{the} government of Russia came forward. It not only provided industrial capital but also acted as entrepreneurs to set up industries.

Let us take up the case of U.S.A. How far this country satisfies the hypothesis of Gerschenkron regarding the origin of universal banking ? The answer would seem to be that it was not but there were certain parallels. On the eve of the civil war the United States of America was well ahead of its nearest continental European rivals, and it was gaining rapidly on its acknowledged industrial leader. In 1870 United Kingdom's share in global manufacturing output was 31.8% and the United States of America's share was 23.3%. Because of civil war effect, ^{the} share of U.S.A. ^{that of} was lower than U.K. But U.S.A.'s share was well ahead of Germany's 13.2%.¹⁸ Thus according to Gerschenkron U.S.A. falls under the category of underdeveloped economy.

In England original accumulation of profit and retained earnings played a decisive role in industrial financing in the first industrial revolution. But the role played by the bank could not be ignored. Pressnell study rightly revealed that during the period 1750 to 1844 funds in England were transferred from the rural areas to the industrial areas¹⁹ which was obviously used as industrial capital. So, there was an obvious parallel between

the English development and the development of the National Bank Reserve System in the United States of America after the civil war. In this sense United States fits the English pattern and Gerschenkron might give similar levels of economic advancement in the two countries.

But this does not exhaust the similarities between American and European financial development. By the end of nineteenth century American banks stationed at the pivotal points where the banking system and the capital market were connected and employed financial resources to rearrange the structure of American industry.^{19A} So, it was ^aparallel to ^{the}German style of universal banking system. Considering this point ^{the}United States could not be regarded as relatively backward country according to Gerschenkron. Because the United States was not at that time beginning to industrialize, it had already made notable industrial development.

In these circumstances rapid increase in time deposits compel the banks to seek new avenue for its employment. When bank pays interest at higher rate on time deposits in comparison to demand deposits, people get attraction to keep their savings in time deposits account instead of demand deposits. Developmental expenditures in a country that have been undertaken have been able to create increments in the savings of people which are bound to seek suitable accommodation through banks. From regulatory point of view also if central bank in a country allows the commercial banks to maintain lesser percentage of time deposits with the central

bank as statutory reserve^{it} will certainly increase capacity of the commercial banks to do universal banking. Let us see how far this hypothesis fits for U.S.A. and Japan.

In U.S.A. commercial banks were functioning informally as universal banks since the beginning of this century although the National Bank Act (1863) prohibited the banks to participate in the long-term financing. Later on, the Federal Reserve Act (1913)²⁰ lowered the required reserves on time deposits than on demand deposits. The effect was to give banks a strong incentives to raise the ratio of time deposits over demand deposits. Banks increased the differential between interest paid on the two kinds of deposits and offered services in connection with time deposits designed to assimilate than to demand deposits. In this way a tendency developed in the minds of the depositors to transfer their funds from current a/cs to time deposits accounts. Banks frequently not only allowed such a transfer but also encouraged their customers in favour of such a transfer so that they could take advantages of lower reserves to obtain a larger basis for credit expansion towards universal banking.

Let us turn to Japan. In Japan restoration government realised that economic backwardness of the country might make her a easy spoil of western power. Without rapid industrialization as per restoration government independence of Japan was in jeopardy.²¹ In the absence of availability of experienced persons those who were familiar with western method, ^{the} government of Japan took positive

action to bring industrial experts from western countries to help its industrial development. In 1875 according to official statistics 527 foreign experts were employed in different sectors of Japanese economy.²² Foreign food and foreign machinery were also imported by the government and distributed among the perfectual authorities who used them as models for the producers in their locality. Similarly, agricultural experimental stations were set up to assist in the adaptation of foreign crops to Japanese condition. During this time^{the} government of Japan had keen interest in foreign trade. It purchased raw materials ^{from} in domestic market to sell them abroad and used that sale proceeds to finance the imports. During the sixties of the 19th century postal and telegraph system was introduced and steamship and railways were built ^{up} and these were financed by the Japanese government raising loan from England. Some rich merchant families also came forward to set up a large number of manufacturing establishment by purchasing machinery from western countries. Difficulty arose for the government in regard to meet expenditure in relation to the setting up of large scale enterprises from its revenue earnings. To solve this problem ^{the} government of Japan was bound to take financial assistance from Mitsui and other merchants who were ^{the} government's chief supporters. In 1868 ^{the} government's expenditure was 25 million yen while ^{the} government's revenue from ordinary sources was not more than 3.7 million yen.²³

In Japan most of the large scale enterprises which were either in the hands of the government or in the hands of the great family scarcely made any public issue of shares. In these

circumstances Japanese public used to keep their savings preferably in fixed deposits at the ordinary banks and these resources were invested by the banks in industrial concerns both for the short as well as long term purposes.²⁴

Part III : Regulation

In the last part we pointed out how the countries under the direction of universal banking made a departure from specialised system. There were certain strong economic impulses which worked in favour of the choice of universal banking system. Banking regulation was one of the factor which favoured the banks to work in this direction. In this background subject matter of this part is to highlight the universal banking regulation operated in different countries of the world.

In addition to credit banks (which were known as universal banks), there were some special type of banks in Germany to serve special purposes. The special type of banks included Noten Banken, Joint Stock Mortgage Bank, Royal Sea Trading Copy and Co-operative Credit Society. Each bank had its own banking Act.²⁵ On the other hand, credit Banks (universal bank) were free from banking regulation which helped them to take general and elastic programme.²⁶ It was the common practice of the credit Banks (universal banks) in Germany to give industrial credit out of all proposition, for example, against

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security of assets or against earning power or prospect of the firm. In addition to ^{the} sanction of industrial loan, German credit banks took part in company promotion and worked as underwriter of the Corporate shares. In the absence of banking Act, every credit Bank (universal bank) had its own statute to conduct business. The Statute (Article 111K) of the Bank Fur Handel Und Industries which was written following the statute of the 'credit Mobilier' of France empowered it to do promotional activities and to help^{ed} the new companies by underwriting their shares and debentures.²⁷ Similarly, section 2 of the statute of the Duetche Bank (1870) stated, "the purpose of the bank is to carry on banking transactions of every description...."²⁸

Banking crisis in 1931 insisted Hitler to appoint a Banking Enquiry Committee. The report of the Committee was published in November, 1934 which is known as German Bank Act, 1934.²⁹ According to this Act, one single firm was allowed to get credit from a bank a maximum ^{of} 5 per cent of the bank's capital. The banks were directed to inform the commissioner of bank when total debt to a single firm exceeded 1 million Reichs marks within a period of one month.³⁰ There was an exception to this rule. One firm must get bank credit twice the legal percentage if all partners or managing directors of the bank expressly agreed, but the information relating to credits in excess of the legal percentage must be communicated to the Commissioner of bank so that the authorities would be kept informed of the kind of enterprise to credits of more than average size were allotted and of the form in which they were given.³¹ The law added

that investment in real estate and permanent participation in shares of all client companies must not exceed the banks capital.

The ordinary banks of Japan which were controlled by the Ordinary Bank Ordinance, 1890 had a persistent tendency on their part to accommodate industries with short as well as long term financial assistances. This ordinance limited the volume of loan to a single customer upto 10 per cent of the banks paid up capital and reserves.³² On account of the vigorous objection from the industrialists the government of Japan was compelled to withdraw this restriction in 1895.³³ As a result, the Zaibatsu firm transformed their finance department into bank which helped them to get easy finance from their own banks.

After the World War I, the economy of Japan slipped into recession, a serious slump prolonged by the devastating Kanto Earth Quake of 1923. As the decade progressed and the situation was worsening, banking practices was deteriorating, speculative advances were increasing and the need for major financial adjustment became acute.³⁴ As a result, a number of banks were also failed. Manchester Guardian had described the Japanese finance "as half a century behind the times and unsuited to the modern industrial world."³⁵ In these circumstances it was felt ^{important} to reorganise ^{the} banking regulation. Thus a new banking law was introduced in 1928 to replace the outdated and clearly inadequate 1890 ordinance. Some of the striking features of the new banking regulation were that it did not set any legal standard for the concentration of loans on a single client, minimum cash

18

reserve.³⁶ The new banking regulation did not claim any revolutionary change in ^{the} Japanese banking system. This law allowed the 'Ordinary' banks which were known as universal banks to continue their policies of long term lending, aggressive credit extension, heavy investment in corporate equities and close relations to industry.³⁷ In 1942 banking law in Japan was modified and the functions of the banks were still broadened to include participation in industrial as well as commercial finance.³⁸

Commercial banks in U.S.A. were controlled by the National Bank Act (1863) till 1913. This Act imposed some restriction chiefly referred to the maximum amount loanable to a single borrower and on real estate loan. The banks were not allowed to lend more than 10 per cent of their capital and surplus to a single customer directly or indirectly. But the Federal Reserve Act (1913) granted limited permission regarding mortgage loan to the National banks which was an important step towards universal banking by the commercial banks in U.S.A. According to this Act the banks were allowed to provide/loan^a maximum 25 per cent of their capital and surplus against^{the} security of marketable non-perishable commodities. The State Bank competing with the National banking institutions could lend large sum on real estate. State Bank Act permitted the banks to lend an amount equal to 25 per cent of their paid up capital and surplus or $\frac{1}{3}$ rd of time deposit whichever is higher against the security of improved and unencumbered farm bonds within a distance of one hundred miles from the office of the lending bank. Note that loan given in this way must not exceed 50 per cent ^{of the} estimated value

of land kept as security and term of loan must not run for the period ^{of} more than 5 years.³⁹ On account of the strict limitation imposed by the National Bank Act (1863) on national banks, many of them merged with the State bank. Later on, the McFadden Act (1927) gave the banks more liberal power of lending on real estate security. According to this Act, the banks were allowed to invest in the securities of a single company which must not exceed 25 per cent value of the banks paid up capital and ~~reserves~~. The Act liberalised the restriction on the grant of real estate mortgage loan permitting banks to provide 50 per cent of their saving deposits in this connection, provided maximum limit of this loan must not exceed 25 per cent value of the paid up capital and reserves of the Bank.⁴⁰ The Banking crisis ^{of} in 1931 compelled the Government of U.S.A. to pass a Bank Act which is known as Glass-Steagal Act (1933). This Act separated commercial banking from investment banking. Section 20 of the Act provided that "after one year from the date of enactment of this Act, no member bank shall affiliate.... with any corporation, association, business trust or other similar organisation, public scale or distribution at whole scale or retail or through syndicate participation of stocks, bonds, debentures notes or other securities."⁴¹

Banking Amendment Act (1935) again liberalised the real estate loan. According to this Act, loans for the period of three years or less, the amount of loan given was not permitted to exceed more than sixty per cent value of the real estate kept as security.

If however, amortization was required within a period not exceeding twenty years, the amount of loan was not allowed to exceed seventyfive per cent value of the real estate offered as security. Banks were permitted to underwrite single issue upto twenty percent of the total issue or not more than \$ 10,00,000 so long as this did not exceed than per cent value of their unimpaired capital and surplus. A bank's aggregate underwriting was not allowed to exceed at any one time, two hundred per cent of its unimpaired capital and surplus.⁴²

Part IV : FEASIBILITY

Having discussed the regulation of universal banks with particular reference to industrial finance in the previous part of this chapter, we would proceed to examine the availability of fund of the universal banks for industrial finance in different countries of the world. The banks in different countries which had confined their operation only in short-term lending, departed to a surprising extent to the universal banking. The reasons for this remarkable fusion of banking functions in countries where they were so carefully segregated were not far to seek. In some countries tremendous increase in time deposits with the banks⁴³ or in some countries channelling the public savings to promote industries as a trustworthy organisation the universal bank came into existence.⁴⁴

In Germany, the resources of the banks during their earlier stage were confined only to their paid up capital and reserves. But later on, the deposit resources were the prime source of their working fund.

Table 1.4

Group of Bank Deposits (including current A/C balance)

(Million marks)

Dec. 31st	All Credit Bank	9 Berlin banks
1889	1392.18	743.67
1891	1281.38	633.92
1893	1321.50	653.66
1885	1769.38	1016.46
1887	2069.07	1143.90
1889	2837.58	1612.80
1901	3028.05	1726.36
1903	3014.81	1699.13
1905	3709.55	2214.52
1907	5298.40	3212.54
1909	8112.71	4173.28
1911	9413.08	4969.30
1913	9641.54	5148.63

Source : P.B.Whale, Joint Stock Banking in Germany, p.23.

The deposit entrusted to the banks increased very rapidly, vide Table 1.4. In 1889 total deposits of all credit banks was 1.392.18 million marks, which raised to 9641.58 million marks in 1913. ^{We find} Similar tune of increase we find in the case of 9 Berlin banks.

One result of this increase in deposits was that although the capital of the banks was repeatedly raised by

large amounts (that of the Deutsche Bank grew from 15 millions in 1870 to 200 millions in 1913), it declined as a proportion of the total working fund at their disposal vide Table 1.5. According to the table all banks share of deposits and current account balance in total working fund was 58.8 per cent in 1895^{and} raised to 84.5 per cent in 1912. Similarly,⁹ Berlin banks' lowest share was 51 per cent in 1895 and the highest share was 87.5 per cent in 1908. These imply that by the turn of the century universal banks' main source of finance was deposits.

Table 1.5

Deposits and Current Account balances as percentage of Total working funds (not including acceptance liabilities)

(in percentage)

Year	All banks	9 Berlin banks
1895	58.8%	51.0%
1905	66.2%	69.1%
1906	67.8%	71.2%
1907	67.7%	70.2%
1908	69.0%	87.6%
1909	70.6%	73.2%
1910	72.2%	75.3%
1911	71.5%	74.8%
1912	84.5%	74.9%
1913	72.0%	75.9%

Source : P.B.Whale, Joint Stock Banking in Germany, p.24.

Similarly the disproportionate growth in time deposits in the Japanese Commercial banking sector in comparison to demand deposit helped them to accept the principle of universal banking as is evident from the following table :

Table 1.6

The Relative Importance of Long-Term Deposits in
City and Country Banks in Japan (1930-57)

(Billion yen)

Year end	C i t y B a n k		C o u n t r y B a n k	
	Time & Saving deposit	Percentage of total deposit	Time & Saving deposit	Percentage of Total deposit
1930	2	60.4	3	54.1
1940	7	52.0	6	50.4
1945	19	29.3	15	38.4
1947	17	13.1	14	17.2
1949	112	23.8	74	30.6
1951	282	32.9	199	42.1
1953	595	39.1	435	48.6
1955	1001	41.6	588	55.5
1957	1582	44.2	1009	58.4

Source : The Modern Japanese Banking System - Hubert F.Schiffer,
p.195.

It is evident from the Table 1.6 that before World War II, share of time and saving deposits was more than 50% but after the war particularly in 1947 it fell ^{down} to an average of

15% and again increased to an average of 51% in 1957. The early postwar inflation, which made it unprofitable for the public to keep their money with the bank was responsible for this change. Another striking feature ~~that~~ we notice from the above table is that there was rapid increase in time and demand deposits from 1951. The reason behind this increasing trend in deposit was that the Article 8 of the Japanese Banking Act (1951) empowered every bank in Japan to transfer 10% of its earning to reserve fund⁴⁵ instead of creating statutory reserve on time and demand deposits. As a result banks were showing their keen interest to attract more time deposits from the public which they could use for medium and long-term investment purpose.

Not only the banking regulation but also ^{the} public sentiment was effective behind the rapid increase in deposits with the banks in Japan. On account of underdeveloped capital market in Japan in Meiji period, the public clearly preferred to keep their money in the relatively secured financial institutions especially banks.⁴⁶

Increasing resources of commercial banks compelled them to branch out in the investment field not only in the case of Germany, Japan but also in that of United States of America. Just after the war period the growth in deposits was encouraging in the commercial banks in U.S.A. But from 1922 we find a disproportionate growth in time deposits in the banking sector in U.S.A. (vide table 1-7). Like Japanese banking law, the banking

regulation in U.S.A. ^{also} favoured the member banks by lowering reserve requirement on time deposits which encouraged the banks to attract more time deposits for long-term investment purpose.

The Following table shows the comparative growth ⁱⁿ net demand and time deposits of the reporting member banks in U.S.A. from 1921 to 1929.

Table 1.7

Reporting Member Banks in U.S.A.

Net Demand and Time Deposits

(in million of dollars)

December	Net demand deposits	Time deposits
1921	10,247	3009
1922	11,146	3720
1923	11,127	4083
1924	13,184	4855
1925	13,173	5357
1926	13,032	5768
1927	13,872	6419
1928	13,399	6842
1929	3633	6839
1930(Sept.)	13,542	7489
% increase	33%	127%

Source : Phillips, C.A., Aemanus, T.F., Nelson, R.W. 1937 ~ Banking and the Business Cycles - A study of the great depression in the United States, p.97.

From December, 1921 to October, 1929, the increase in net demand deposits in the reporting member banks was roughly 33% while the increase in their time deposits was 127% or an average annual percentage increase ⁱⁿ time deposits four times than of demand deposits. Similarly, the growth rate ⁱⁿ time deposits was faster than that of the demand deposits.

The Comparative growth ⁱⁿ time deposits in the reporting member banks ⁱⁿ New York City was even more rapid, as shown in the following table :

Table 1.8
Reporting Member Banks in New York City,
Net Demand and Time Deposits

(in million of dollars)

December	Net demand deposit	Time deposit
1921	4219	290
1922	4325	539
1923	4234	609
1924	5372	814
1925	5204	792
1926	5094	902
1927	5570	1034
1928	5305	1198
1929 (October)	5561	1258
Per cent increase	32%	333%

Source : Phillips, C.A., Acmanus, T.F., Nelson, R.W. 1937 - Banking and the Business Cycles, p.97.

In the above table the increase in time deposits was 333 per cent while net demand deposits was only 32 per cent during the period 1921 to 1929. The above tables (1.7 and 1.8) imply that banks^{in U.S.A.} were in a favourable position to follow universal banking with the rapid increase in time deposits.

Part V : GROWTH OF UNIVERSAL BANKING

From the above discussion it is clear that there was a historic landslide in commercial banking practices. The favourable banking regulation and the resources of the commercial banks of the concerned countries favoured them to go through the activities of long-term financing along with short-term financing. But this new innovation has not emerged in all the countries of the world at the same period and same speed. In this context, we will now examine the growth of universal banking in a number of countries like Germany, Japan and U.S.A.

In Germany universal banking has started with the establishment of the Schaffhausen'scher Bankverein Cologne, the first Joint Stock Bank in 1848. In 1853 The Bank Fur Handel Und Industrie was established with the distinct object of taking an interest in setting up of industry following the model of 'Credit Mobilier' of France. Following the Bank Fur Handel Und Industrie a number of other banks were established during the period 1848-70. Of these, the more important were The Disconto Gesellschaft, The Berliner Handels Gesellschaft and The Mitteldeutsche Credit Bank. In Germany universal banking

opened a new Chapter when Deutsche Bank and Commerz Bank were established in 1870 to finance foreign trade. They were largely unaffected by the company failures in Germany during the international crisis of 1873. After 1876 they gradually became universal bank with an extensive deposit business and close links to German industry. They were rapidly growing along with new line in subsequent years with the establishment of nine Berlin banks.

In Germany universal banking business had its beginning with the opening of current account with its customers.⁴⁷ The extent to which the customer would be indebted to the bank, maximum period for which the indebtedness might be outstanding, the purpose for which advances required, were mentioned in the current account agreement. The amount thus obtained from the current account helped the concerned undertakings to meet their need of working as well as long-term capital requirements.⁴⁸ It was common practice in Germany that the universal banks obtained representation through the persons of their own directors on the supervisory boards of the Companies which were their customers.⁴⁹ By this means they seeked to strengthen their connection with the undertakings and to gain more influence on their policy and more insight into its execution.^{49A} In the course of promotional activities, the universal banks in Germany took over all the shares of the concerned companies in their own name and sold the same to the investing public. In order to minimise this risk borne by a

single bank and to lead the investing public to purchase share of a company it was very common for several banks to come together to form a Konsortium. Lasting participation in share capital of a Company was not the policy of the German banks. But in some circumstances, when the issue of share capital of related corporations proved unsuccessful, the banks were pushed to hold shares for long time^{49B} when the banks realised to maintain price of shares, they used to buy own issues.⁵⁰ Indeed, it changed the very ethos of banking. As Gerschenkron has put it : "A German bank accompanied an industrial enterprise from the cradle to the grave, from establishment to liquidation, throughout all the vicissitudes of its existence."⁵⁰ Following table gives the average percentage of securities to total assets of the leading German universal banks during the period 1913-1928.

Table 1.9.

Before World War I development banking activities of the German banks were in a remarkable position. After the war we find decreasing trendⁱⁿ in the development banking within the German joint stock banking set ups. As compared with figures of 1913, the decrease in the relative size of long term investments as shown by the proportion of own securities and syndicate participations to total assets is strikingly significant from the above table.

Since the war of 1914 they had far less long term capital locked up in industry than was the case in the days

Table 1.9

Securities as Percentage of Total Assets of
German Universal Banks

	1913	1914	1915	1916	1917	1918	1922	1924	1926	1927	1928
Deutsche Bank	13.3	10.6	8.9	6.5	5.0	3.9	.23	9.0	3.6	4.0	3.3
Dresdner Bank	8.8	11.1	10.3	6.9	5.9	5.9	.08	15.2	4.0	3.6	3.0
Disconto gesellschaft	16.6	22.9	17.2	15.0	9.8	8.4	.45	28.3	8.4	7.4	6.6
Darmstädter Bank	10.9	11.0	10.3	7.9	5.7	5.6	NA	17.2	3.6	3.8	3.2
Berliner Handelsge sellschaft	19.1	20.8	19.2	18.3	14.9	18.0	1.2	22.4	4.5	5.2	5.1
Commuz. u. Disconto bank	11.16	14.2	12.7	7.4	4.8	7.2	.23	10.6	2.6	20.9	5.1
National Bank	17.3	16.3	13.9	10.2	7.6	7.6	7.7	NA	NA	-	-
Mittel-deutsche credit-bank	10.6	7.8	7.9	6.7	3.3	4.2	.25	14.1	1.6	0.8	-
Eight Berlin Bank	13.0	13.9	11.8	9.1	6.6	6.2	.23	16.6	4.3	3.2	3.9
Average	13.41	14.28	12.46	9.77	7.06	7.45	2.67	16.67	4.07	3.76	4.31

Source : Whale, P.B., Joint Stock Banking in Germany, p.202,
p.223 and p.275.

before it. A careful perusal of the balance sheets during that period showed startling increase of short-term loans of the German banks. The short-term loans of German banks increased from 19,608 million RM in 1913 to 27,926 million RM in 1930 while the long-term loans declined from 26,424 million RM in 1913 to 15,824 million RM in 1930.

Universal banking in Japan dates from the 1876s when traditional houses like Mitsui were allowed to establish joint stock banks with the initial capital of 2 million yen. Following Mitsui Bank several other mercantile houses like Tokugawa Era Mitsui established banks with capital ranging from 2,00,000 to 5,00,000 million yen.

At the next stage of universal banking growth in Japan, National Bank came into existence to take part in promotional activities of companies. Although the National Bank had the right to note issue, the sources of deposits and the lending behaviour were like the Mitsui and other universal banks. During the prewar period lending behaviour of most of the Japanese banks was unsound as they were engaged in speculative business, made extensive loan to the directors and frequently concentrated their lending on one customer.⁵¹

The Bank Act of 1890 empowered the private commercial banks and the quasi banks to merge with ordinary banks and later on in 1899 National banks joined with them. The ordinary banks were noted universal banks in Japan. Between 1888 and 1901 the

number of ordinary bank rose almost six fold, loans increased six fold and deposits increased almost seven and a half times.

Table 1.10

Growth of Universal Banks in Japan (Million yen)

Year	Head Office	Deposits in mill. yen	Loans & advances mill.yen	Year	Head Office	Deposits in mill. yen	Loans & advances mill.yen
1888	346	58.9	99.6	1904	1708	605.3	720.7
1890	351	58.9	117.0	1905	1697	692.5	796.4
1892	402	88.2	117.0	1906	1670	1033.7	1111.7
1894	833	116.2	170.0	1907	1658	944.3	1113.2
1895	925	159.3	245.1	1908	1635	938.0	1098.1
1897	1281	262.3	435.1	1909	1617	1054.4	1123.4
1898	1948	288.8	441.1	1910	1604	1185.7	1249.9
1899	1561	392.3	573.1	1911	1603	1256.24	1393.5
1900	1802	436.8	653.2				
1901	1867	450.2	628.4				
1902	1841	536.7	687.4				
1903	1754	566.2	715.3				

Source : Hugh, T.P., 1967. "Japan, 1868-1914" in Ron Cameron, et al., (ed.) Banking in the Early Stage of Industrialisation, p.264.

In 1895 the government of Japan removed some restrictions on the banks which encouraged the Zaibatsu family based industries to transform their finance department into bank to provide all types of financial assistance to their firms. As a result, Mitsubishi and Somitomo two renowned universal banks were established in 1895.

The other universal banks which came into being were Yasuda and Dai-ichi Bank.

In Japan there was a persistent tendency among the universal banks to accommodate industries with extensive loans. Banks were generally aggressive in their credit practices and tended to extend loan beyond their financial capacity during the Meiji period. The term 'overloan' has been widely used in studies of Japanese banking to refer to the condition where financial institutions have allowed advances exceeding deposits.⁵² The Extent of loan provided by the universal banks to the industries in Japan is presented in the following Table.

Table 1.11

Universal Bank's Credit to industries in Japan

Year	Mitsui			Mitsubishi			Yasuda S/A
	S/A	I/A	I/S	S/A	I/A	I/S	
1896F	0.18	0.24	0.57	0.02	0.32	0.74	0.70
1896L	0.21	0.18	0.50	0.05	0.26	0.75	0.28
1897F	0.29	0.16	0.43	0.02	0.24	0.32	0.28
1897L	0.19	0.13	0.32	0.02	0.14	0.19	0.28
1902F	0.25	0.14	0.34	0.06	0.13	0.16	0.25
1902L	0.23	0.15	0.33	0.06	0.20	0.24	0.22
1904F	0.19	0.21	0.40	0.09	0.17	0.20	0.24
1904L	0.18	0.24	0.47	0.08	0.20	0.25	0.20
1905F	0.17	0.24	0.46	0.07	0.14	0.17	0.20
1905L	0.16	0.21	0.42	0.07	0.10	0.10	0.22

Notes : F and L following year indicate first and last six months of the year.

S stands for securities of firms

A for total assets

I/S stands for short-term loans

I stands for long-term loans

Source : Yamamura, K. 1972 "Japan 1868-1930" in R.Camerons et al. (ed.) Banking & Economic Development, p.177.

Three banks which are mentioned in the Table 1.11 were reckoned for their participation in long-term industrial financing. Consulting the above table we find that the banks involved themselves remarkably in long-term financing. To do so ^{the} banks were not facing any problem of liquidity as Bank of Japan came forward with financial accommodation by discounting bill or providing direct loan during the Meiji regime.⁵³ Gradually many new banks became sympathetic to this new innovation. For example, exchange banks leaving their normal path of operation entangled themselves in heavy long-term investment in industry. Following ^{the} exchange banks ordinary banks also entered into the stock market on a very large scale.^{53A} The balance sheet of four out of the 'big five' universal banks in Japan disclosed a remarkable increase of their security holdings during the period 1927-34.

Table 1.12
Securities Held by Four 'Big' Universal Banks of Japan

(in thousand of yens)

	1927	1928	1929	1930	1931	1932	1933	1934
1. Mitsubishi	233	322	360	337	285	350	345	411
2. Mitsui	-	211	233	215	272	182	280	353
3. Sumitomo	174	236	233	242	248	261	326	358
4. Dai-ichi	-	248	285	269	304	-	376	408

Source : The Statist, International Banking Section, Nov.14, 1931, pp.764-65, also Nov.12, 1932, pp.73-74.

The universal banks in United States of America also showed a remarkable growth since the mid of nineteenth century.

Dual banking system consisting of National Bank and State banks, was considered as universal banks in U.S.A. It is evident from the Table 1.13, the number of universal banks increased some eight times during the period 1850-90 and this trend continued till 1927. After 1927 the universal banks were showing downward trend and ^{this trend} continued till banking crisis in 1931.

Table 1.13
Growth of universal Banks in U.S.A.

Year	National Bank	State Bank	Total	Year	National Bank	State Bank	Total
1850	-	830	830	1932	6011	805	6816
1860	-	1579	1579	1937	5260	1081	6341
1870	1612	2612	1873	1942	5081	1598	6679
1880	2076	1051	3127	1947	5005	1918	6923
1917	7600	53	7653	1952	4909	1889	6798
1922	8240	1648	9892	1957	4620	1773	6393
1927	7759	1275	9034				

Source : Banking and Monetary Statistics (Board of Governors of the Federal Reserve System, Washington DC 1943), pp.20-23, for 1917-37; Federal Reserve Bulletin (May, 1948), p.535, (December, 1953), p.1347; (October, 1958), p.1183.

The universal banks in U.S.A. had persistent tendency to investment in corporate securities. In 1920 there was a rapid growth of security offerings by the American Corporations. New securities offered by the Corporations rose from \$2788 million in 1920 to \$9377 million in 1929.⁵⁴ The booming security market led most of the commercial banks to form security affiliates.⁵⁵

They engaged in security underwriting, holding of securities for control purposes and various other activities.⁵⁶ By 1929 commercial banks and their security affiliates had equalled private investment banks in terms of volume of securities underwritten.⁵⁷ During the period 1921-28 Commercial banks investment in Corporate shares increased from 14%^{to 19%.} of total investment. Whereas short-term loans decreased from 53% in 1921 to 36% in 1928. A more complete presentation of the nature of the universal banking activities performed by all the member banks during the period 1921-29 are presented in the table.

Table 1.14
Loans and Investments of All Member Banks
(in million of dollars)

Year	Invest- ment	Loans on security	Loans of urban real estate	Total	All other banks	Total loans & Investments
1921	6002	4400	875	11,277	12,844	24,121
1922	7017	4500	1100	12,617	11,565	24,182
1923	7757	4950	1350	11,057	12,450	26,507
1924	7963	5350	1575	14,888	12,279	27,167
1925	8863	6718	1875	17,456	12,062	29,518
1926	9123	7321	2161	18,605	12,579	31,184
1927	9818	8156	1449	20,423	12,533	32,756
1928	10,758	9068	2624	22,450	12,611	35,061
1929	10,052	10095	2750	22,897	12,814	35,711
Increase	4,050	5,695	1875	11,620	-30	11,590
% increase	67%	129%	214%			48%

Source : Phillips, C.A., Acmanus, T.F., Nelson, R.W., 1937,
Banking and The Business Cycle, p.105.

The Above table shows that long term investment which was \$ 11,2777 million in 1921 increased to \$ 22,897^{million} in 1929 implies an increase of more than 100%. On the other, short-term loans decreased to a remarkable extent during the same period.

The great depression of 1930 hit the Commercial banks even more than ^{the} non-financial corporations which caused a long slide of gross national product from \$ 103 billion in 1921 to \$ 55 billion in 1929.⁵⁸ After World War II, when the American economy recovered from the depression, the commercial banks again became an important financier of non-financial corporation. During the Period 1966-74 industrial loans supplied by the Commercial banks were 22% of the external funds used by the non-financial corporations.⁵⁹ One study reported that during the period 1946-60 commercial banks trust department's net purchase of corporate securities equalled about three fourth of the value of bank credit extended to business firms.⁶⁰

Part VI : VIABILITY OF UNIVERSAL BANKING

From the growth of universal banking in different countries of the world as mentioned in the last part of this Chapter we may say that the drift of commercial banks in universal banking field is not without its advantages to industry. The history of Germany gives us ample scope to say how the commercial banks carried on industrial financing without serious risks and not without success. The overwhelming importance of German banks

was expressed by Deutsch-Oekonomist thus : "Any one who observes impartially the development of the German banking system and the policy of the guiding minds must see that, without the vigorous and, in some ways, daring initiative of the banks, the present proud edifice of the German national economy could not have been created in so relatively short a time."⁶¹ In the booming security market since 1920 investment banks in United States of America only took part of underwriting of securities to a limited extent. In that circumstance , the Commercial bank came forward to help the non-financial undertaking by underwriting securities through their security affiliates.

This sort of developmental banking activities favoured the commercial banks in U.S.A. to produce moderate rate of return on paid up capital and reserves.

From the Table 1.15 we find that the lowest rate of return on capital was 3.35% in 1935. But after that^d moderate rate of return was noticed till 1960. This was the cause of prohibition imposed on the universal banking after ^{the} depression by banking Act of 1933 and ^{the} given permission^h to do so according to the banking amendment Act of 1935.

Table 1.15

Net profits as a percentage of Capital funds of insured
Commercial Banks in United States of America

Year	%	Year	%	Year	%	Year	%	Year	%
1935	3.35	1940	6.08	1945	10.87	1950	8.51	1955	7.90
1936	8.35	1941	6.72	1946	10.01	1951	7.82	1956	7.82
1937	5.97	1942	6.34	1947	8.20	1952	8.07	1957	8.30
1938	4.68	1943	8.82	1948	7.49	1953	7.93	1958	9.60
1939	5.99	1944	9.78	1949	7.98	1954	9.50	1959	7.94
								1960	10.03

Source : The American Bankers Association
The Commercial Banking Industry, p.328.

The extent to which net profit of insured banks have been affected by incomes and expenditures is shown in Table-1.16.

Table 1.16

Addition to and Deduction from Net Operating
Earnings of Insured Commercial Banks (1935-60)

(Amount in Million)

Year	Transfer from Reserves, Recoveries, & Security Profile	Losses, Charge off, Net Credits(+) and Additions to Reserves	Net Debits (-)
1935	S 432.5	S 628.1	S - 195.6
1936	585.1	501.7	+ 83.4
1937	308.9	395.1	- 86.2
1938	329.2	454.5	- 125.3
1939	381.2	438.2	- 57.0
1940	349.1	386.0	- 36.9
1941	324.5	334.0	- 9.5
1942	222.8	271.1	+ 62.4
1944	361.7	265.9	+ 105.8
1945	509.3	264.1	+ 245.2
1946	408.6	283.2	+ 125.4
1947	262.0	294.3	- 32.3
1948	266.4	485.8	- 219.4
1949	231.1	379.0	- 147.9
1950	245.5	366.9	- 121.4
1951	169.2	395.7	- 226.5
1952	144.1	362.4	- 218.3
1953	152.4	448.3	- 295.9
1954	631.5	552.6	- 78.9
1955	239.6	707.2	- 467.6
1956	250.2	993.5	- 473.3
1957	198.8	757.4	- 559.0
1958	864.1	783.2	+ 84.9
1959	329.9	1362.5	-1032.6
1960	579.8	948.4	- 403.6

Source : Federal Deposit Insurance, p.329.

In consulting the above tables (1.15, 1.16) we see that the items of income and expenditure affect the net profit of banks of a particular year to a substantial extent. But these have had limited effect upon the ratio of net profits to capital funds for the whole period.

In U.S.A. Internal Revenue Code authorised commercial banks to deduct net capital losses like falling security prices from taxable income. In Table 1.17 we see that security losses have substantially exceeded profits on security sold.

Table 1.17

Security Profits and Losses. All Insured Commercial Banks (1951-60)

(Million Dollar)

Year	Profits on securities sold or Redeemed	Losses on securities charged against Earnings	Losses on securities charged to Revenue A/C	Net Profit (+) or Losses (-) on Securities
1951	56.6	83.8	17.7	- 44.9
1952	33.8	97.5	25.6	- 89.3
1953	38.9	156.9	38.5	- 156.5
1954	416.5	66.7	15.8	+ 334.0
1955	57.1	221.2	68.1	- 232.2
1956	31.2	317.4	95.5	- 381.7
1957	64.4	237.5	74.5	- 247.6
1958	681.6	93.7	19.7	+ 568.2
1960	329.3	219.8	47.7	+ 61.8

Source : The Commercial Banking Industry (1962)
 - American Bankers Association, p.330.

It is evident from the above table that in seven years ^{out} of the ten years, ^{Period} between 1951 to 1960 losses incurred exceeded profits.

But in two recession years 1954 and 1958, large profits were realised on securities sold.

Over the long run, commercial banks must expect to incur substantial net loss on securities as they adapt to the changing needs of the economy. Holding of securities is expanded in period of recession when the demand for loans decreased. Similarly, security holdings are sold when demand for loans increased. Due to these cyclical increases in loans requirement banks may suffer loss on security investment. But skillful investment portfolio management may lessen such type of risk to some extent.

Statistics reveal that six leading universal banks in Japan earned remarkable rate of return on Capital as is evidenced from the table given below :

Table 1.18

Percentage of net profit on paid up capital and surplus of universal Banks in Japan (1936)

(in thousand yen)

Name of Bank	Paid up Capital 1	Reserves 2	Total 3	Profit 4	% 4 of 3
Mitsui	60,000	52,000	1,12,000	26,246	23.43
Mitsubishi	62,500	46,000	1,08,500	23,100	21.29
Dai-ichi	57,500	68,500	1,26,000	16,808	13.33
Sumitomo	50,000	36,500	86,500	18,132	20.95
Saswa	72,000	25,510	97,510	10,714	10.98
Yasuda	92,750	66,500	1,59,250	18,020	11.31
			Average -	16,88	

Source : Sarasas, P., Money & Banking in Japan, p. 203.

If we make a comparative study of this performance with those of five leading English deposit banks, we find that Japanese universal banking is superior to English banking in respect to return on Capital.

Table 1.19

Percentage of net profit on paid up Capital and Reserves of British Banks (1938)

(in £)

Name of Bank	Capital	Reserve	Carry over	Total	Profit %	
	1	2	3	(1+2+3)	5 of 4	
West minister	9,320,000	9,320,000	527,000	19,167,000	1,557,000	8.1
Barelays	15,858,000	10,750,000	528,000	27,136,000	1,926,000	7.1
National Provincial	9,479,000	8,500,000	574,000	18,553,000	1,873,000	9.8
Lloyds	15,810,000	9,500,000	527,000	25,837,000	1,763,000	6.6
Midland	15,159,000	42,410,000	628,000	28,197,000	2,492,000	8.8
				Average		8.0

Source : Balogh, T. 1950, Studies in Financial Organisation, p.106.

Comparing the above tables it is noticeable that ^{the} average rate of return on paid up capital of six leading Japanese universal banks was 16.88% in 1935 while in 1938 five leading English deposit banks showed an average rate of return on capital ^{of} only 8%.

In Germany ^{also} we find a noticeable change ⁱⁿ the relationship between gross profits and business expenses of the universal banks.

Table 1.20

Expenses as % of gross profit of German universal Banks

Name of Bank	1906	1907	1908	1909	1910	1911	1912	1913
DeutscheBank	36.0	27.5	28.0	40.8	42.5	43.9	36.7	35.4
Dresdner Bank	28.0	30.7	33.0	33.9	34.4	36.6	38.3	38.2
Discontogesell -schaft	29.0	30.5	30.0	30.6	33.1	34.2	35.6	36.4
Darmstädter	37.0	42.7	42.0	43.0	47.9	49.3	42.8	46.0
Schaaffhausen Bankvereen	16.0	18.4	21.0	23.7	25.0	25.6	31.8	35.4
Berliner Handelsgesells chaft	15.0	18.1	20.0	17.3	19.5	19.0	21.1	23.3
Commerz-U. Discon to bank	36.0	41.8	46.0	45.4	47.1	48.1	47.1	46.9
National bank	22.0	27.9	28.0	28.8	28.0	46.2	30.9	33.8
Mitteldent sche credit bank	30.0	33.3	35.0	39.0	39.8	39.5	33.6	36.6
Average	30.0	33.3	34.0	34.5	36.5	37.5	36.3	37.1

Source : Whaley, P.B., 1930. Joint Stock Banking in Germany, p.174.

It is evident from the table that there was a general tendency for the expenses to become relatively higher. There were some reasons to think that the declining trend of gross profit was due to the creation of secret reserves out of undisclosed profits.⁶² To prove its accuracy we can consider Table 1.21.

Table 1.21
Yearly Dividend Rate of German Universal Banks

Name of Bank	1906	1907	1908	1909	1910	1911	1912	1913
Deutsche	12.0	12.0	12.0	12.5	12.5	12.5	12.5	12.5
Dresdner	8.5	7.0	7.5	8.5	8.5	8.5	8.5	8.5
Discontogesellschaft	9.0	9.0	9.0	9.5	10.0	10.0	10.0	10.0
Darmstädter	8.0	6.0	6.0	6.5	6.5	6.5	6.5	6.5
Schaaffhausen Bankverein	8.5	7.0	7.0	7.5	7.5	7.5	5.0	3.0
Berliner Handelsgesellschaft	9.0	9.0	9.0	9.0	9.0	9.5	9.5	9.5
Commerz-U. Disconto Bank	6.5	5.5	5.5	6.0	6.0	6.0	7.0	6.0
National Bank	7.5	6.0	6.0	6.5	7.0	7.0	7.0	6.0
Mitteldeutsche Credit-Bank	6.5	6.5	6.5	6.0	6.5	6.5	6.5	6.5
Average	8.8	7.9	8.0	8.5	8.7	8.7	8.5	8.0

Source : Whale, P.B., 1930, Joint Stock Banking in Germany, p.176.

From the table it has been shown that the dividends tended on the whole rather to increase than to decrease; and certainly became steadier from year to year. It is also clear from the table that the newer banks like Deutsche and Dresdner, showed the most marked increase in dividends. The proportion of net profit set to reserves tended rather to decline; but this was probably offset by additions to secret reserves.^{63.}

Part VII : Conclusion

According to Alexander Gerschenkron's hypothesis, the universal banks were set up in those countries where industrialisation started much later than in England. This hypothesis was not equally applicable in all the underdeveloped countries of the world. There were some countries like Japan, United States of America where rapid increase ⁱⁿ time deposits created pressure on the commercial banks to take shelter under the shed of universal banking while in the countries like Germany universal banking evolved there following the hypothesis of Gerschenkron. This system recommended on strong economic ground of efficiency, savings mobilization, resources allocation and system flexibility. In these course of actions, banking regulation of the concerned countries, managerial efficiency in the banks, risk bearing tendency of the commercial banks to provide long-term loans, entrepreneurial service to the industries, direct participation in corporate shares and debentures along with short-term loan, eagerness of the industrialists to get both short as well as long-term finance from the commercial banks had converted universal banking as a successful financial system.

Notes and References

1. Different countries had their own style of indigenous banking prior to the period of industrial revolution for a brief review of some of them vide World Development Report, (1989), pp.47-49.
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Chapter II

UNIVERSAL BANKING IN INDIA BEFORE INDEPENDENCE

Part I : INTRODUCTION :

In ^{the} last chapter we ^{have} examined that the Universal Banks in Germany, Japan and U.S.A. proved themselves as an important provider of financial assistances to the industrial ventures. We also investigated that favourable regulatory framework of bank and rapid increase ⁱⁿ time deposits helped them in the concerned countries to accept universal banking.

In ^{the} Indian context we find that financial system before independence was constituted mainly of banking system and managing agency system. While the latter arranged for block capital requirement of the industries, the former used to provide only working capital. Some stray attempts by 'Swadeshi' banks to practise universal banking ^{have} failed in bud. In this background the organisation of this chapter is as follows :

The need for universal banking before independence is the subject-matter of Part II. After studying the need for universal banking we ^{have} examined the sources of financing in Part III. Part IV concentrates ^{on} the growth of Universal banking in India before independence while bank failures

are interpreted in Part V. The last part of this Chapter delves with a summary and conclusion.

Part II: Need for term-financing before Independence

Industrial term-financing in India had its peculiarities of its own during the British regime. Her economy was conspicuous by the absence of development banks as in France, Universal banks as in Germany and issue markets as in England for meeting industries capital need. In the absence of industrial banking in modern line backed by the government managing agencies and indigenous banks like Marwaries, Multanies and Chettis were the century old tradition among the Indian community to cater to the financial requirements of industries. In these circumstances, first victorian style of joint stock bank namely The Bank of Bengal came into existence in the year 1809.¹ The Object of Victorian style of banking was only to accumulate working capital needs of industry.² Following the bank of Bengal, the other joint stock banks which opened their doors on Indian soil included Union Bank (1829), Bank of Bombay (1840), Bank of Madras (1843), Calcutta City Banking Corporation (1863), Oriental Bank, Central Bank of India (1911) etc. These banks were modelled on the principle of providing only short-term loan following the Victorian style of banking. The reasons behind adopting that banking principle were that the joint stock banks which were registered in England were legally bound to follow victorian style of banking in India.³ In case of others, which were registered in India, absence of banking Act of the land insisted them to follow the banking line of Great Britain.⁴

But unlike the British experience, the stock market was very weak institutions in India before independence.⁵ Investing public in India were less interested to invest their savings in shares of industry. Perhaps speculation was considered as an attractive field of investment for most of the Indians at that time.⁶ S.K.Basu's study reveals that one Calcutta based jute mill namely Albion Jute Mills Company Ltd. published its list of shareholders on 31st January, 1896 which included only one name of Indian who purchased only 25 ordinary and 25 preference shares out of a total of 6000 ordinary and 5000 preference shares of Rs.100 each.⁷ Even those who were in search of other avenues of investment, preferred riskless government securities, municipal and port-trust bonds and postal cash certificate instead of industrial shares and debentures.⁸ This impeded the free flow of savings to industrial investments.

Insurance companies may also, act as a source of industrial finance. They in fact played an important role in this regard in the countries like Japan, Germany and U.S.A.⁹ But their attitude was very passive in India in so far as the industrial financing was concerned. Most lucrative field of investment of the insurance companies was also riskless government and semi-government securities. Statistics reveal that during the period 1921-36 seventy per cent of insurance companies asset was blocked in government or semi-government securities whereas only four per cent was blocked in corporate shares.¹⁰

The Insurance Act was not less responsible for such an insignificant amount of industrial investment by the insurance companies in India at that time. Section 27(1) of the Act had compelled the insurance companies to invest fiftyfive per cent of their liabilities to holders of life insurance policies in government and government-approved securities¹⁴ and whatever little scope was available for providing industrial finance has been later on curtailed by the Insurance Amendment Act, 1950 which rigidly controlled the investments of insurance companies.

The only means of industrial finance prior to independence was the managing agents. Mainly three types of functions like promoting industrial concerns, providing them financial assistances and managing them for a long period were performed by the managing agencies.¹⁵ Reference of these functions were reflected in the statement made by Hon'ble Mr. W.A.Ironside, partner of the Messrs Bird & Company, a leading managing agent in Calcutta. He pointed out, "The managing agency system has been, and is, to my mind, a considerable factor in many successful ventures in this part of India at any rate. Powerful firms, by reason of their large stake in enterprises, often protected to languishing or difficult scheme from premature liquidation...."¹⁶

British nationals were at the helm of the pioneer managing agencies in India. Managing agencies controlled by the British nationals were able to accumulate their capital both within the Indian territory and from abroad on the strength of their

reputation in international as well as national market which helped them to open out a number of new production-lines in India.¹⁴ One section of ^{the} British capitalists who were residing in England considering prospect of those industries in India came forward to invest their savings either in the reputed British controlled managing agencies or through London Stock Exchange without taking direct part in India's development process. To understand the inflow of fund from foreign capital market through managing agencies or directly through London Stock Exchange in India following table will focus light on industrywise investment in Joint Stock Companies registered in India and elsewhere (mainly in England) :

Table 21

Joint Stock Companies in India 1914

	Registered in India		Registered Elsewhere (mainly in England)	
	No.	Paid-up-Capital (in lakh Rs.)	No.	Paid-up-Capital (in lakh Rs.)
Bank & Finance	436	780.1	13	2,455.1
Trading & Manufacturing	754	1133.0	113	11,423.9
Tea & Other Plantations	237	473.5	118	1,873.9
Coal & Mining	140	609.5	6	13.9
Cotton Mills	205	1,670.7	3	40.00
Jute mills	34	761.1	9	242.9
Others	674	2,536.2	147	13,026.1
Total	2480	8,024.1	479	29,077.3

Note : Conversion at Rs.10 = £ 1.

Source : Statistical Abstract for British India,
1914-15 to 1923-24, Government of India,
Calcutta, 1925, pp.558-59.

Following implications we may draw from the Table 2.1:

1. Nearabout eighty per cent of the total paid up capital of the Joint Stock Companies in 1914 derived from abroad mainly from England and remaining twenty per cent realised within the Indian territory. It is evident that compared to Rs.60.7 lakhs for an average foreign company, the paid up capital was Rs.3.3 lakhs for an average rupee company.
2. Dilating industrywise analysis it can be observed that foreign companies in comparison to rupee companies were much ahead in the fielding of Banking & Finance, Trade and Manufacturing, Tea and other Companies capturing 76 per cent, 91 per cent and 80 per cent paid-up capital in the respective fields. It indicates that British community in India was interested in selective number of industries.
3. Although rupee companies were ahead in coal mining and textile industries, they were dominated by the British national in India.
4. Big Joint-Stock Companies listed their shares in the London Stock Exchange instead of Indian stock market.
5. High inflow of capital from abroad indicates that the investing public in Britain were interested to take part in the industrial development process of India through British managing agents. Note that they did never extend financial assistance to the indigenous industries which were suffering from dearth of capital before World War I.

Sometimes, British managing agents strategically kept the Indian entrepreneurs away the industrial sector through interlocking of industries.¹⁵ The managing agencies which were involved in Tea and Jute industries for example, extended their field of operation to coal, engineering and transport industries. Object behind this type of activities were that the former used to provide secured market for the latter and the latter used to provide cheaper goods and service inputs to the former. All these functions were done by the giant managing agents to create entry barriers for the Indian entrepreneurs.

But Indian entrepreneurs found it a formidable task to mobilize funds for industrial ventures. They usually belonged to small and medium scale industries.¹⁶ Their problems of long-term industrial finance was not only confined to raising of initial capital by means of selling shares but also to find the requisite funds to develop and carry on the business. It was very difficult for them even to arrange for working capital. In the emergency period they had to run to the indigenous bankers to get working capital loan paying interest as high as 36 per cent.¹⁶ In case of small collieries this rate varied between 36 per cent to 84 per cent.¹⁷ Thus the problem of industrial finance in India was not only limited to the provision of long term capital alone. The insufficiency of working capital and the high cost of such as is available were an important element in the problem of industrial finance in India before independence.

Even though the banks used to provide little capital to

the industries, it was their policy to recover that financed amount at any cost which caused sometimes premature death of the financed units. The spinning and Weaving Mills of Bezwada for example, received loan from Imperial (at present State Bank of India) Bank. As soon as its fortune became low, the mills had to find the money for repaying the bank loan which caused their liquidation on June 6, 1929.¹⁸ This conservative outlook of the joint stock banks was not responsive to opportunities for industrial investment and was clearly incapable of sustaining a high rate of industrial growth, particularly the growth of new and innovating enterprise.

Government interest was also not moving to that direction. They introduced securities in the market in 1917. The rate of interest was 1 to $1\frac{1}{2}$ per cent higher than the interest rate offered by the banks on deposits.¹⁹ This type of practices adversely affected the bank's deposit position. From 1925 to 1930 government borrowing from the market through selling securities was Rs.140 crores whereas the levels of bank deposit remained stationary during that same period.²⁰ Government apathy of this kind had failed to gear up the impetus towards development of financial system.

By the turn of the 20th century, nationalist movement known as 'Swadeshi Movement' started in India²¹ and that movement featured the joint-stock banks to commence long-term industrial financing culture. These two events speak in favour of the Gerschenkron hypothesis, inner meaning of which is nationalist

sentiment leads to the formation of universal banking in underdeveloped countries like Germany. While describing the formative stage of universal bank in India before independence under the title 'Swadeshi' bank, S.K. Basu indeed anticipated the Gerschenkron hypothesis. He observed, "The whole country was swayed by the new spirit of 'Swadeshi' and there was a widespread drive to foster the indigenous industries. A rapid development of joint stock banking took place about that time. The new joint stock banks undertook various types of business and developed an unmistakable tendency to provide long-term finance to industry."²² The prospectus issued by the 'Swadeshi' banks in relation to finance and to assist the development of 'Swadeshi' industries (new indigenous and industrial and agricultural concerns) gives an impression that nationalist sentiment encouraged the growth of 'Swadeshi' banks even after the World War I. Their prospectus even cited examples of Japan and Germany to eulogize the image of universal banks as a nation builder.

The imperialist government also realised the need for universal bank in India before independence. For example, the report of the Indian Industrial Commission (1916-18) stated, "It appears to follow that an industrial bank with a sufficient large capital to ensure its safe working must, at any rate, for some time, combine ordinary banking business with its industrial activities to enable it to obtain a return on its capital."²³ To minimise the risk of providing long-term loan the commission opined to draw a distinction between industrial finance and ordinary banking

business. Share and debenture capital and time deposits were only advised to use for long-term purpose but ^{never for} short-term deposits never. It would be of great benefit from the point of view of the concerns as well as of the banks, if the latter would try to replace such permanent advances by a debenture issue. The bank should underwrite such debentures and also be the trustee, and sell them to their depositors. They should try not only to replace their own advances by debentures, but also prevail upon the companies to replace the public deposits, if they have any, by debentures. This will help to put industrial finance on more scientific lines.²⁵

Part III : Feasibility of Universal Banking During Pre-Independence period.

Last part considered that the need for universal banking during the pre-independence period was an important factor for rapid industrialization. In this connection, this part will examine to what extent it was feasible for the joint stock banks to take part in universal banking.

In India industries were facing problem for insufficiency of short as well long-term capital before independence. The

joint stock banks which were noted as an institutional financial intermediaries, confined their activities only to provide short-term loans from the short-term deposits following the orthodox theory of banking. This orthodox arrangement set forth in favour of ^{ed} delimiting the banking institutions in the field of industrial finances.

If we examine the structure of liabilities of the joint stock banks, we find that liabilities consists of not only short term deposits but also long term deposits, and capital and reserves which can be profitably utilized for long term industrial financing.

CAPITAL AND RESERVES :

In case of the trading concerns, capital is utilized for financing the purchases of fixed assets. But in the banks whose primary function is to serve as a cushion or insurance fund is to absorb losses that may occur. So it is very important for the joint stock banks to utilize capital and surpluses for the purpose for which other short-term liabilities are unsuitable.

Table 2.3 portrays that total paid up capital of the joint stock banks was Rs.82.12 lakhs in 1900 rose to Rs.799.49 lakhs in 1934. It was an increase of 8.74 times during the period of 31 years. Similarly, reserves increased 9.2 times during the same period. One striking feature of the table is that capital of these banks had been increasing rapidly since 1907. The overall

raise of paid up capital and reserves was ten times from 1900 to 1934 which impressed the joint stock banks to divert their activities towards long-term industrial financing.

Table 2.²

Paid up Capital and Reserve of the Indian Joint Stock Banks
(1900-1934)

(Rs. in 1,000)

Year	Reporting Banks	Paid up Capital	Reserves	Total
1900	9	82, 12	45, 60	1, 27, 72
1905	9	84, 57	77, 82	1, 62, 39
1907	20	2, 29, 61	63, 27	2, 92, 88
1909	15	2, 66, 07	87, 97	3, 54, 04
1911	18	2, 85, 60	1, 26, 54	4, 12, 14
1913	18	2, 31, 33	1, 32, 94	3, 64, 27
1915	21	2, 69, 13	1, 57, 02	4, 26, 15
1917	18	3, 03, 70	1, 62, 99	4, 66, 69
1919	21	5, 43, 22	2, 32, 24	7, 75, 46
1921	28	9, 42, 23	2, 76, 06	12, 18, 29
1923	26	6, 86, 03	2, 85, 40	9, 71, 43
1925	28	6, 72, 97	3, 86, 62	10, 59, 59
1927	29	6, 88, 70	4, 19, 35	11, 08, 05
1929	33	7, 86, 97	3, 66, 54	11, 53, 51
1931	32	7, 77, 32	4, 28, 14	12, 05, 46
1933	34	7, 63, 70	4, 84, 51	12, 48, 21
1934	36	7, 99, 49	4, 65, 92	12, 65, 41

Source : The Statistical Tables Relating to Banks in India
(various issues)

On the basis of the classification of demand and time deposits, it is evident from Table 2.2, ^{that} time deposits were showing rapid increase. During the period 1915 to 1934 the ratio of time deposits to the total deposit although declined in some of the years, rose as much as 66% in 1928 as against 32% in 1915 which indicated ^{the} lions share of the bank deposits belonged to time deposits. Time deposits increased between 1915 and 1921 by about 1046% and in 1934 amounted to Rs. 37, 37, 01, 000 or 968% more than that of 1915. Although the growth rate of time deposits was fluctuating after 1921, it showed remarkable growth from 1915 to 1921.

Table 2.3

Trend in Time Liabilities of Joint Stock Banks (1915-1934)
(Rs. in 1,000)

Year	Time Deposits	Per cent Growth over Preceeding year	Total Deposits	Percentage share in (4) of (2)
1915	3, 86, 06	-	1, 19, 309	.32
1916	1, 52, 053	293.8	2, 43, 214	.62
1917	1, 56, 299	2.7	2, 71, 631	.57
1918	2, 17, 105	38.9	3, 79, 121	.57
1919	2, 75, 899	27.0	5, 92, 058	.46
1920	3, 44, 415	24.8	6, 92, 562	.49
1921	44, 23, 06	28.4	75, 80, 08	.58
1922	36, 17, 52	(-) 18.2	60, 61, 62	.59
1923	26, 40, 51	(-) 27.0	43, 58, 53	.60
1924	32, 69, 38	23.8	51, 37, 36	.63
1925	32, 69, 47	0.002	51, 90, 88	.62
1926	35, 02, 82	7.1	57, 29, 01	.61
1927	36, 57, 35	4.4	56, 75, 44	.64
1928	40, 13, 19	9.7	60, 64, 61	.66
1929	37, 45, 09	(-) 6.6	58, 25, 22	.64
1930	34, 98, 08	(-) 6.5	59, 17, 70	.59
1931	35, 49, 89	1.4	57, 24, 69	.62
1932	38, 43, 63	8.2	67, 74, 03	.56
1933	38, 27, 25	(-) 0.4	67, 82, 46	.56
1934	37, 37, 01	(-) 2.3	72, 68, 32	.51

Source : The Statistical Tables Relating to Banks in India
(Various issues).

From the above table it is clear to us that the share of time deposits was more than sixty percent of total deposits in nine years out of twenty years and it was more than fifty percent in another eight years. Thus the trend of paid up capital and reserves and the changes in the character of the fixed deposits were in favour of the argument that the banks were in a suitable position to undertake long-term industrial finance along with short-term without disturbing their liquidity position. The External Capital Committee also in its report dated 16th September, 1925 stated, "India possesses a vast store of dormant capital awaiting for development and in order to make this available capital for investment, banking facilities must be increased and extended."²⁶

Part IV : Growth of Universal Bank and Their Role as an Industrial Financier

The nationalist sentiment of Indian public during the Swadeshi movement and boom of the post World War I period opened avenue for setting up of a huge number of industries which demanded sufficient amount of institutional industrial finance. In response to that demand a number of universal banks were set up. Most of those banks were large enough and were in a feasible position to do industrial financing. In this connection we will investigate in this part of the growth of universal bank along with their role as an industrial financier before independence.

A cursory glance at the following table would reveal that there had been a marked growth of universal banks in India in terms of number and paid up capital before independence.

Table 2.⁴

Growth of Universal Banks in India Before Independence

Year 1	No. of Banks 2	Paid up Capital (Rs.) 3	Average Size (Rs.) 4 = $\frac{3}{7}$ 5
1900-1905	2	30,62,500	15,31,250
1906-1910	6	95,31,281	15,88,546
1911-1915	1	8,00,000	8,00,000
1916-1920	5	3,63,55,670	72,71,134
1921-1924	3	63,48,000	21,16,000

Source : 'Capital' (various issues)

The initial incident which emerges from ^{the} study of the Table 2.⁴ is the pre-banking crisis and post banking crisis boom in universal banking and the unsteady increases in the total paid up capital of universal banks during the period 1900-24. Before banking crisis of 1913 a large number of Swadeshi enterprises were set up and to finance these enterprises a large number of universal banks were established under the name of 'Swadeshi' bank. In second phase some more universal banks came into existence under the title 'industrial bank' during the post world war I industrial boom period. Before banking crises average size of the universal bank varied from Rs.15 lakhs to Rs.16 lakhs but after the banking crisis this size varied from Rs.21 lakhs to Rs.73 lakhs, vide

Table 2.5. That means after the banking crisis average size of the bank was larger than before.

Between the period 1900 and 1905 two universal banks namely People's Bank of Punjab and Bank of Burma Ltd. were established in 1901 and 1904 respectively. Between 1906 and 1910 there was a great outburst of universal banking activity which received its impetus from Swadeshi movement in 1905 led to the foundation of the Indian Specie Bank ^{Act.} in 1906. The other universal banks which opened their offices during the period 1906-1910 were the Lahore Bank Ltd. (1906), The Hindusthan Bank (1906), The Bengal National Bank Ltd. (1907), The Credit Bank of India (1909), and The People's Industrial Bank Ltd. Thus, the first Chapter of the universal banking came to an end.

During the banking crisis period (1911-15) only one universal bank namely the New People's Bank of India (1914) was set up. At the end of the banking crisis eight more universal banks were established. Among these the name of the Tata Industrial Bank was important. Following Tata Industrial Bank, seven more universal banks under the name 'industrial bank' came into existence. They were The Calcutta Industrial Bank (1919), The Indian Industrial Bank (1919), The Mysore Industrial Bank (1920), The Industrial Bank of Western India (1919), The Karmani Industrial Bank (1921), The Raikat Industrial Bank (1922), and The Laxmi Industrial Bank (1923).

The People's Bank of Punjab (1901) started its industrial financing activities with an initial registered capital of Rs. 35

lakhs.²⁷ There is evidence that the bank made large advances of Rs.90 lakhs to various industrial concerns on the security of machinery and building which indicates the virginity of the functioning of the bank.²⁸ In addition to that the bank accommodated long term financial requirement to the Punjab Spinning and Weaving Mills Co.Ltd. by 20.20 lakhs, The Lahore Spinning and Weaving Mills Co,Ltd. by Rs.7.5 lakhs, The Pioneer Investment Co.Ltd., Lahore by Rs.8.5 lakhs, and The Surat People's Spinning and Weaving Mills by Rs.4.5 lakhs.²⁹ Direct subscription to debenture was also not negligible. People's Bank subscribed to debentures in the Lahore Spinning and Weaving Mills by Rs.1 lakh.^{29A} Thus the culture of industrial financing by 'Swadeshi' banks had begun in India for the first time before independence.

Following the People's Bank of Punjab a number of banks came up in the field of industrial financing. Among these, bank of Burma (1904) was the first European controlled mixed bank in India. This bank was established with an object of providing industrial capital to the Mower and Company and other Companies in which Mower and Company was the managing agent.³⁰ There is evidence that the bank advanced Rs.45.58 lakhs to Mower and Company of which Rs.12.44 lakhs was for short period.³¹ Sanction of loan to Mower and Company against mortgage of other companies share has not less important. Bank of Burma sanctioned loan of Rs.6.12 lakhs to Mower and Company against security of 61250 shares of Irrawaddy Petroleum Syndicate.³²

According to liquidators report the bank advanced money

to Mower and Company amounting to Rs. 7,88,750 against the security of 70,875 shares of Molla Oil Company. There is evidence that Bank of Burma provided long term loan, among others to Burma Petroleum Co. and Burma Investment Ltd., and also underwrote shares of Mower and Company, a reputed managing agency firm.³³

This emerging sector was dominated by, apart from the above, the Indian Specie Bank (1906), and the Credit Bank of India (1909) with paid up capital of Rs.70.50 lakhs and Rs.10.90 lakhs respectively.³⁴ It was the common practice of the Indian Specie Bank to advance loan against security of pearls.³⁵ From liquidators report of the bank we know that the bank advanced Rs.64 lakhs on the security of pearls. Following the German style universal banking model Indian Specie Bank and Credit Bank of India mobilized private deposits which stood at Rs.270 lakhs and Rs.50.10 lakhs respectively in the early 1910s and they regularly carried out various long-term industrial financing activities.³⁶ In addition to these there were some less important banks like The Hindusthan Bank, The Lahore Bank, the Doaba Bank, the Industrial Bank which provided long term industrial loan to ginning factory, flour mills, leather factory.³⁷

After the World War I once more long-term financing to industry was noticed among the Swadeshi Banks. Tata Industrial Bank (1917) was the forerunner at that stage.³⁸ Following the Tata Industrial Bank, some more 'Swadeshi' banks were in the

picture. They were the Calcutta Industrial Bank (1919). The Indian Industrial Bank (1921), The Raikat Industrial Bank(1922), The Laxmi Industrial Bank (1923), The Mysore Industrial Bank(1920).³⁹ Paid up capital of these banks varied from Rs.1 lakh to Rs.6 lakhs. Object of these banks was to arrange long-term finance to the indigenous industrial units in a war broken economy following German style of ^{universal} banking system.⁴⁰ As for instance, Tata Industrial Bank granted a loan of Rs.75,79,529 to various industrial units both for short-term and long-term purpose which was by no means a small amount.⁴¹ To perform this kind of activities the trend of fixed and current deposits was also encouraging which rose from Rs.2,28,00,000 in 1918 to Rs.3,25,00,924 in 1922.⁴² The balance sheet of lucian Industrial Bank which was published on 31st December, 1922 revealed that its investment structure was Rs.49,669 in 6% war bonds and Rs.26,610 in limited companies shares and stocks⁴³ while the balance sheet of the Calcutta Industrial Bank dated 31st December, 1921 showed that Rs.24,500 was invested in shares of public Company.⁴⁴ In addition to these the Calcutta Industrial Bank, the Industrial Bank of Western India and the Karnani Industrial Bank were, however, provided industrial loan upto Rs.70.59 lakhs, Rs.40.00 lakhs and Rs.60.00 lakhs respectively.⁴⁵

IV. Bank failure

Although the existing 'Swadeshi' banks rendered a good deal of services to the industry, yet there were occasional banking crisis in Pre-independence period. At long ago Keynes had

pointed out that unstable equilibrium of deposits foreboded crisis.⁴⁶ In 'Swadeshi' banks we also noticed instability in deposits. To prove into the Keynes forecasting in 'Swadeshi' banks let us examine the following table :

Table 2·5

Capital & Reserve, and Deposits of Principal 'Swadeshi' banks

(in lakhs of Rs.)

	1908	1909	1910	1911	1912
Capital & Reserves	81.62	78.00	72.11	83.19	85.38
Deposits	197.71	150.00	438.67	388.07	238.50
Total Resources	279.33	228.00	530.78	471.26	323.88
Cash Balance	19.14	14.44	5.59	15.26	NA
Percentage of Cash Balance to Deposits(%)	9.68	9.62	1.03	3.93	NA

Source : Various issues of 'Capital'.

Table 2·5 shows that deposits mobilized by the 'Swadeshi' banks was Rs.197.71 lakhs in 1908 and came down to Rs.150.00 lakhs in 1909 and again it had gone up to Rs.438.67 lakhs in 1910 and since then it had come down to Rs.388.07 lakhs and Rs.238.50 lakhs in 1911 and 1912 respectively. Such an unstable deposit position in 'Swadeshi' banks testifies Keynes forecasting of banking crisis.

It was the policy of the 'Swadeshi' banks to attract more deposits than of retaining adequate cash reserves which was one of the major cause of bank failure in 1913.⁴⁷ The statistics mentioned in the above table indicate that cash position of the 'Swadeshi' Banks was deteriorating year after year. Percentage of

cash balance to deposit which was 9.68 per cent in 1908 declined to 3.93 per cent in 1911. If we compare the percentage of cash balance to deposit of the 'Swadeshi' banks with presidency and other joint stock banks we find a very small proportion of cash to deposits ratio maintained by the 'Swadeshi' banks or (Universal Banks).

Table 2.6

Proportion of Cash Balance to Deposit of Indian Banks

	1908	1909	1910	1911	Average
'Swadeshi' banks (Universal Banks)	9.68	9.62	1.03	3.93	6.06
Indian Joint Stock Banks	27.00	23.00	21.00	16.00	21.75
Presidency Banks	33.00	33.00	31.00	35.00	33.00

Source : Cash balances of 'Swadeshi' banks from 'Capital' and cash balances of Presidency Banks and Joint Stock banks from 'Memorandum of Banking' - Indian Industrial Commission (1916-18).

Table 2.6 reveals that cash balances of Indian Joint Stock Banks and Presidency Banks since 1908 onwards were more favourable than the 'Swadeshi' banks. Considering average cash position of three types of banks as mentioned in the above table we find that 'Swadeshi' bank's position was only 6.06 per cent while the Indian Joint Stock bank's and Presidency bank's position were 21.75 per cent and 33 per cent respectively. Again if we compare the percentage of cash reserve position of 'Swadeshi' banks with other countries banks, even then 'Swadeshi' bank's position was the lowest. For example, when cash reserve position

of U.S. Member Banks was 9.5 per cent, The London clearing Banks position was 11.5 per cent, Swiss Private Banks position was 8.0 per cent, Chartered Bank of Canada's position was 11.00 per cent⁴⁸ then 'Swadeshi' bank's position was only 6.06 per cent.

It was the common practice of the 'Swadeshi' banks to mobilize more deposit at any cost than of providing loan to viable industrial units. While providing evidences before the Indian Industrial Commission (1916-18) Rai Bahadur Damodar Das pointed out that normal rate of interest paid by the 'Swadeshi' Banks was 6 per cent. It was 2 per cent higher than the rate offered by the Presidency Banks for deposit mobilization.⁴⁹ If the depositors were minor, widow or orphan the rate was as high as 8 per cent.⁵⁰ There could be no objection to offer such a high rate of interest, if the funds so attracted were wisely used for more lucrative business. On the eve of the liquidation of the Bank of Burma it was found that the bank advanced one-third of its working capital against worthless security to a firm in which banks directors had their vested interest.⁵¹ Rai Bahadur Damodar Das's evidence before the Indian Industrial Commission reveals that directors of the Bank of Hindusthan borrowed from the bank either for themselves or for their friends without any security.⁵² Similarly we may cite the examples of Rangpore Bank which provided substantial assistances to Rangpore Tobacco Company,⁵³ Noaba Bank to Amritswar General and Flour Mills and Phagwara Company,⁵⁴ Tata Industrial Bank to Tata Iron and Steel Company.⁵⁵ In all these cases the respective bank directors had their personal interest.

Another ¹backmark against the universal banks was that their activities were not reflecting the nationalist morale of their promoters. Some banks were involved in speculative business which in no way helped country's economic development and could never come under the definition of universal banking. For example, The Indian Specie Bank was deeply involved in the pearls and 'badly' business.⁵⁶ The Amritswar Bank granted a loan of Rs.1.5 million to speculative business namely the Upper India Real Estate Company.⁵⁷ The Hindusthan Bank provided loan to a theatre group and Punjab Bros. Company, a speculative shop.⁵⁸ Investment pattern of these banks does not prove the development seeking nationalist thrust of their promoters and testifies against the hypothesis of Gerschenkron, inner meaning of which is that ^{the} nourishing of heavy industries is the main object of industrial financing.⁵⁹ In addition to these, history of the several universal banks spell out the various incidents of malpractices. We may cite the example of People's Bank which made false entry of Rs.4 lakhs in the accounts of the Ganges Flour Mills,⁶⁰ and paid dividend out of capital which was a criminal offence.⁶¹ Similarly making of fictitious entry was common practices in the Indian Specie Bank also.⁶²

The shareholders of the banks also failed to realise their responsibility. They were concerned about their dividends only and remained indifferent to the proper conduct to the business which gave rise to the malpractices. In the case of Hindusthan Bank it was found that the director was not able to declare dividend if he could show Rs.6000 as salary per annum. So, fraudulently he credited

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Rs. 6,000 to the bank and debited the same to his son.⁶³ As soon as the annual balance sheet passed and the dividend was declared, he reversed the entry.⁶³ The actual offence was ensuring balance sheet for cheating the public. In Germany it was the policy of the bank to publish annual Balance Sheet and Profit and Loss Account in the newspaper after approving the same in the shareholders' meeting.⁶⁴ The object of this type of practices by the bank was to inform the public about the performance of the banks. The universal banks in India were not following this type of banking practices. The banks were set up only to satisfy a transitory caprice and not to satisfy trading requirement of the public. A glaring example in this connection was the Rangpore Bank. This bank was set up by the directors of the Rangpore Tobacco Company to get finance at a cheap rate. The Rangpore Bank sanctioned loan to this company which was not earning any profit at all.⁶⁵

Mismanagement, due to inexperience in banking affairs, was the cause of the bank failures. In this connection, we may quote the remarks of the official committee of Lahore, "The evidence produced before us insisted on the want of business knowledge and inexperience in company promoters, managers and staff as a primary cause of failure. There were few competent manager whether of banks or of industrial concerns. Consequently egregious blunders were committed and some of the so called dishonesty seems to us very like ignorance, much of it was due to anxiety

to cloak losses."⁶⁶ The men at the head of the banking institutions were no doubt energetic. But most of them were not fit for the direction of a banking business. The persons who were successful in other walk of life were placed in the banking institutions.⁶⁷ Non-availability of entrepreneur who had experience in banking business was the inevitable cause to place personnel from other sectors to the banking sector. In the petition for bailment of Jaffar Joosab, manager of the Credit Bank of India, it was stated that the directors, appointed him in his present job knowing his ignorance on banking and accountancy. According to the advice of the directors he gave up his lucrative insurance business to take up the management of the bank. Most surprising thing was that the bank manager was not familiar with the meaning of the bills of exchange. Even when anybody asked him to account Rs.5 lakhs out of total amount of Rs.7 lakhs as shown in current account, he made following confession, "That was made up of mere paper entires; mystery taught me this is window dressing and said it was not illegal and many banks are doing it The account and Balance Sheets were prepared by my staff under instruction from the auditor."⁶⁸ Similarly, Lala Doulat Rai, one medically unfit person who compulsorily retired from civil nazir profession at the age of 45 years was appointed as manager of the Hindusthan Bank.⁶⁹

These types of problems were faced not only by the Indian banks, during the early years of banking, joint Stock

Banks in different countries of the world were facing similar types of problems. Gilbert mentioned that in ^{the} absence of practical experienced personnels, the English banking system also suffered.⁷⁰ Other countries ^{which} learnt from the experience of English banking system ^{also} invited the expert persons to train their countrymen. Japan also did not lag behind in inviting the foreign expert. The President of the National Bank of Japan remarked "Again the Japanese are very grateful for the valuable services of Mr. Alexander Allan Shand, now a director of the Paris Bank, London, who came to Japan at the invitation of the issue department in 1872, acted as adviser in banking to that department, wrote valuable books on banking, instructed young Japanese in that line and thus paved the way for the development of banking business in the country."⁷¹

The failure of so many banks is, no doubt, a serious blow to the industrial development of the country and for some time to come the course and extent of investments may be affected, but in the long run the present loss may prove to have been most beneficial. On the report of working of companies in the Punjab in 1914 -15 the Registrar said, "The removal of a number of rubbish and dishonest concerns will clear the way for the growth of sounder companies under more able management and hedged round by the more stringent provisions of the new Act."⁷² Indeed the Registrar was perfectly right in his views that weak spot in the field of Indian banking was removed by the crisis of 1913 and

subsequent years. Failure of banks was unavoidable in their early years and all countries of the world more or less have experienced this. For example, in England not less than 1229 banks ~~have~~ failed during the crisis of 1726-28 and U.S.A. experienced not less than 517 National Bank failures during the period 1865-1911.⁷³

There was a good deal of destructive criticism passed against the Indians that they were incapable of managing banking business of the modern type.⁷⁴ In response to this criticism it may be mentioned that among the banks which ~~have~~ failed on Indian soil, all were not under the management of the Indians. There were some banks, which ~~have~~ failed,^{that were} managed by the Europeans. For example, The Bank of Burma had failed in 1911⁷⁵ or again the Alliance Bank of Simla which came to the grief in 1923.⁷⁶ Punjab Provincial Industries Committee rightly observed, "The survival of the Punjab National Bank showed that a purely Indian directorate and staff were capable of steering a bank through circumstances trying as ever any financial institution had to face."⁷⁷

The Swadeshi movement in and after 1905 began to have important consequence on the development of Swadeshi enterprises. These enterprises were set up at ~~the~~ time when India was under the domination of British colonial Government whose intention was to keep India far from industrial sector. "Commodities like Jute, coal and tea were monopolised by the

British, while the export market of hides and skins was dominated by Germany. The Bengali bourgeoisie of the late 19th and early 20th centuries entered into areas where foreign interests were both firmly entrenched, or nominally present.⁷⁸" The fields where competition was present included shipping, cotton fabrics, medicines, perfumes, soaps, cigarettes, pottery, match, lock and key, iron-safes, leather goods etc. On the other hand, competition was nominal in the field of hair oil, bidi, Zarda, Khaini, pencil, mustard oil etc. There is, no doubt, that the colonial Government imposed a lot of obstacles against the Indian to set up and run industries like shipping, cotton fabrics, cigarettes etc. The weakness of the new bourgeoisie was also manifest in other ways. "As indigenous technology lagged far behind western scientific advancement, machinery had to be imported. Machines for cotton mills, cigarette factories, match factories, steam-driven ships and others had to be either directly imported or bought from foreigners. Then, there was the dependence on foreign experts who, most of the time, did not want to teach Indian workers the method of manufacture."⁷⁹ Sometimes, the Indian entrepreneurs also failed to understand the importance of expert hand in an industry. Rai Bahadur Damudar Das cited an example before The Indian Industrial Commission (1916-18) that Ambala Glass Factory employed an Australian expert in the concern. The director thought it was useless to pay a high salary to that person. So, he was dismissed from the job. As a result, the concern could not work without an expert and within a short

period it went into liquidation.⁸⁰ Similarly, in the Krishna Mill in Bombay the managing agent did cut its relation with the concern on account of the lack of right manager.⁸¹ On account of the causes like apathy of Imperialist Government, cut-throat competition with the British concern, mismanagement within the concerns compelled most of the ^{indigenous} concerns to go into liquidation. In regard to the Swadeshi enterprises Amit Bhattacharya said, "There were success and failures, and there is no denying ^{of} the fact that the latter was more numerous than the former."⁸² From the following table ^{an} idea relating to the life span of the Swadeshi enterprises can be gathered :

Table 2.7

Some Swadeshi Enterprises and Their Service Life

Name of the Enterprise	Date of Registration	Date of Liquidation
1. The National Spinning Co .Ltd.	1905	1909
2. The Calcutta Weaving Co.Ltd.	1905	Within a short period of its registration.
3. Indian Spinning & Weaving Co.Ltd.	1905	1909
4. The Oriental Hosiery Mfg. Co.Ltd.	1893	With a short period of its operation
5. Bengal Hosiery Co.Ltd.	1907	1918
6. Kamala Mills Ltd.	1906	1915

Source : Swadeshi Enterprises in Bengal (1900-1920) - Amit Bhattacharyya.

The Above table shows that a number of swadeshi enterprises were set up in India before independence in response to the swadeshi movement but they were short lived. There were so many reasons behind that early disastrous position of the swadeshi enterprises. Among others non-availability of industrial capital was important.⁸³ Then British government was showing apathy towards the swadeshi enterprises in regard to industrial capital. So, rapid expansion of swadeshi enterprises gave birth to the swadeshi banks (universal banks) and swadeshi banks came forward to finance^d them without evaluating their prosperity. As a result with the liquidation of weak swadeshi financed enterprises, the banks also fell into a disastrous position. For example we may mention the name of Hindus^{than} Bank. This bank financed 21 branches of the Punjab Bros. Ltd. without evaluating their prosperity. Later on Hindus^{-than} Bank compelled to close its doors on account of the liquidation of those units.⁸⁴

Conclusion

Alongside the emergence of swadeshi movement and a great outburst of indigenous industries by the turn of this century,

there was a growing realisation of the need to integrate ^{universal} banking (combination of development banking with commercial banking) with rapid industrial development process. In response to this need 'Swadeshi' Banks were established adopting ^{universal} banking principle to provide industrial finances to indigenous industries against fierce competition from orthodox banking of British Capitalists. Quantitatively speaking, magnitude of such financing was too small to alter the basic structure of Indian banking vis-a-vis industrial financing. Their activities were also against the principle of ^{universal} banking which compelled them to face disastrous situation. Registrar of Companies comment in his report on working of Companies in Punjab in 1914-15 reveals "The removal of a number of rubbish and dishonest concerns will clear the way for the growth of sounder companies under more able management and hedged round by the more stringent provisions of the new Act." Indeed the Registrar was perfectly right in his views that weak spot in the field of Indian banking was removed by the crisis of 1913 and subsequent years. Thus the pre-independence period experience of ^{universal} banking by 'Swadeshi' banks helped government of independent India to place ^{universal} banking by the commercial banks at the top of its economic agenda.

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Chapter III

TREND OF UNIVERSAL BANKING IN INDIA

AFTER INDEPENDENCE

Part I : INTRODUCTION

It is clear from the last Chapter that ^{the} nationalist sentiment of Indian public was active behind the growth of Universal banks in India before independence. Unfortunately they were not successful in their venture on account of their wrong way of practicing universal banking. After independence in 1947 the question of universal banking through our commercial banks became a topic of discussion among our statesmen and industrialists to built up our industrial economy through a series of five year plans. One group strongly criticised the transplantation of universal banking on Indian soil,¹ while another group expressed their opinion boldly in favour of the universal banking, remembering its successful operation in Germany, Japan, America etc.²

In this background the object of this Chapter is to investigate the part played by the commercial banks in India in industrial term-lending and underwriting capital issues in corporate enterprises. While Part II of the Chapter is devoted to the need for universal banking in India after independence, Part III delineates the banking regulation and the opinion of

the expert committees in relation to the universal banking in India, Part IV deals with the feasibility aspects and Part V concerns with the critical analysis of term-lending by the Indian commercial banks to industry. ^{The} Subject-matter of Part VI is the underwriting aspects. The investment holding of corporate shares and debentures by the commercial banks are the concern of the Part VII. These are followed by conclusion in Part VIII.

Part II : NEED FOR UNIVERSAL BANKING AFTER INDEPENDENCE

Intensified freedom movement during the thirties gave a signal to the repatriation of British Capital from India. No official figure is available on the volume of repatriation. But some studies which were reported in this regard by Lord Kindersley and B.R.Shenoy respectively indicated the repatriation of British capital from India was £ 20 million and £ 17 million during the period 1931-35³. On the other hand, Mr. Kidron's study recorded it at a lower figure of Rs.20 million during 1931-32 and 1936-37.⁴ A detailed estimation was made in this regard by A.K. Banerjee who showed that the gross capital inflow abruptly dropped since 1934-35 in the face of its accelerated outflow since 1931-32. The result of this trend^{is} showed in the following table :

Table 3.1

Amount of Capital Outflow from India on the Eve of Independence
(Rs. in million)

Year	Net Amount of Capital Outflow
1935-36	51.70
1936-37	174.10
1937-38	37.0
1938-39	64.50

Source : Banerjee, A.K., 1963, India's Balance of Payment,
 pp. 195, 210-23.

The Government account was a burning example, which revealed the greatest incidence of capital repatriation. From the following table an idea may be gathered in relation to the repatriation of capital in government accounts.

Table 3.2

Level of Repatriated Public Debt

(Rs. in million)

Year	Repatriated Amount
1935-36	231.60
1936-37	251.00
1937-38	68.40
1938-39	29.40
1939-45	4252.27

Source : Banerjee, A.K. 1963. India's Balance of Payment,
 p. 192; p. 240.

The above table reveals that there was an overall shortage of capital on account of the massive repatriation of British capital just before the independence which caused a primary barrier to industrialization in post-independent India.

After independence, in 1947, the Government of India started to build up its staggering industrial economy through a series of five year plans. The first industrial policy which was announced in 1948, aimed at initiating a mixed economy with an overall responsibility of the government for the planned development of industries. But in actual practice that policy created a considerable amount of confusion and uncertainty with regard to the role of government sector and non-government sector including foreign interest in the industrialization process of the country.⁵ Again the second Industrial Policy Resolution which was declared on 30th April, 1956 during the second five year plan period (1956-61) had further broadened^{ed} the scope of rapid industrialization with particular emphasis on the heavy industries and on the other Co-ordination with a planned expansion of large scale consumer goods and cottage and small scale industries.⁶

It was absolutely necessary that along with the plan for industrial development there should be a simultaneous plan for sound development of its financial machinery in the public sector for short as well as long-term capital.^{6A} In response to the these requirements government stepped forward to re-shape and re-model its financial organisation of the economy and established

a series of development finance institutions. The first step in this connection was to set up of the "The Industrial Finance Corporation of India" in 1948.⁷ During the early years of its operation, disbursement of loan both in absolute amount as well as in proportionate figure was satisfactory. But after 1953-54 both the absolute as well as proportionate figure was in decreasing trend. If we take the aggregate picture of eight years under review as shown in Table 3.3, we find that IFC provided only 11.57% of the total external long-term funds for the whole sector of public limited companies.

Table 3.3

^{the}
Proportion of IFC Financing to Total External
Long Term Financing of the Public Ltd. Companies

(Amount in lakhs of Rs.)

Year 1	Total External Long Term funds for the whole Sector of Public Limited Companies 2	Loans Availed from IFC 3	Percentage of 3 to 2 4
1951-52	1398	178.38	12.76
1952-53	780	249.76 *19.56	32.02
1953-54	2025	281.86	13.92
1954-55	1797	164.31	9.14
1955-56	3358.50	220.23	6.56
1956-57	6012.99	977.50 *10.44	16.26
1957-58	9854.55	833.35	8.46
1958-59	6348.05	747.71	11.78
Total	31,574.09	3653.10	* 11.57

* Average

Source : Joshi, M.S. 1965. Financial Intermediaries in India, p. 164.

On examination of the above table 3.3 we find that IFC's share in total external long-term funds for the whole sector of public Ltd. Company from 1951-54 was on an average 19.56 per cent and from 1954-59 average rate came down to 10.44 per cent.

In regard to participation in Corporate share Capital IFC was very shy. Although section 23 of the Industrial Finance Corporation Act, empowered it to undertake equity capital financing, yet this has not been attempted in actual practice because of its compulsion to dispose of any share within a period of seven years. Moreover, the Industrial Finance Corporation of India caters primarily to the needs of large scale undertakings : its clientele are also restricted to the public & limited companies. 7A

The Gandhian Philosophy and later on the second five year plan (1956-61) stressed their importance on the promotion, development and dispersal of small scale industries especially in backward areas and small towns of the country. To provide them financial assistance the government of India placed on the statute book a State Financial Corporation Act in 1951.⁸ Since their inception and till today policies were not adopted by the Corporation ^{for} ~~the~~ branch expansion in the rural areas. In addition to that the rules for sanctioning loans are so rigid that many applicants consider it difficult to accept them. These sorts of complexity have caused less accessibility on the part of the entrepreneurs to get financial assistance from SFC.

Establishment of direct contact with the domestic public for deposit mobilization is functionally imperative for the viability and dynamic growth of a financial system. As a conservative, specialised institutions, DFI's face strong functional and institutional barriers to accepting deposits from the public though in some countries these institutions have been able to perform deposit-taking functions confined mostly to large institutional or personal long-term savings.⁹

On the other hand, statistics reveal that liberal branch licencing policy which was adopted after 1956¹⁰ permitted the commercial banks to open branches in rural as well as in urban areas and they had done accordingly.

The following table focusses light on the above point :

Table 3.4

Population Group-wise Distribution of Commercial Bank Offices

Year	Rural	Semi-urban	Urban	Metropolitan	Total
Dec.31, 1955	276 (9.7)	1447 (50.06)	1,135 (39.7)	-	2,885 (100.00)
Dec.31, 1968	1,507 (20.2)	3,096 (41.5)	2,860 (38.3)	-	7,463 (100.00)
June 30, 1973	5,561 (36.2)	4,723 (30.6)	2,573 (18.7)	2,505 (16.3)	5,362 (100.00)
June 30, 1978	11,802 (42.1)	7,586 (27.1)	4,452 (16.2)	4,086 (14.6)	28,016 (100.00)
June 30, 1983	22,678 (53.9)	9,036 (21.5)	5,577 (13.2)	4,788 (11.4)	42,079 (100.00)
March 31, 1986	29,633 (55.8)	10,594 (20.0)	7,589 (14.3)	5,269 (9.9)	53,085 (100.00)

Source : Deb, K. 1988, Indian Banking Since Independence, p. 52.

From the table 3.4 rapid progress of opening branches in rural areas is evident. The Total number of branches which was 2885 in December, 1955 increased to 53,085 on March 31, 1986. This progress in opening the new rural branches is, indeed, significant. In rural areas the number of branches which was only 276 on 31st December, 1955 reached to 29,633 on March 31, 1986. In terms of percentage it was only 9.7% in 1955 but in 1986 it reached to 55.8%. Trend of branch expansion in semi-urban, urban and Metropolitan region was also not negligible.

It is interesting to note that lack of fund and branch network in the rural as well as ⁱⁿ urban areas countering the development finance institutions in one hand and commercial banks on the other have been seeking new avenue with their widespread branch network both in rural and urban areas and vast amount of time deposits.

The

In these circumstances Reserve Bank of India came forward to insist commercial banks providing necessary banking regulation to take part in universal banking for the development of India's industrial economy.

Part III : BANKING REGULATION AND OPINION OF EXPERT COMMITTEE

Until 1936 the Joint Stock Banks in India were governed by the general provision of the Indian Companies Act, 1913. Only

the sections 136 and 259 of the Act, respectively dealt with the rules for preparing balance sheet and procedures to be registered with limited liability. No provisions were laid down in regard to the nature of banking business, their management system etc. which pushed them to a disastrous position. The Bombay Provincial Enquiry Committee rightly observed that the bank failure in 1913 was ^{result of} the incorporation of Indian banks under the provisions of Indian Companies Act.¹¹ As a result a departure was made in 1936. Considering peculiar nature of banking business a special Chapter was added in the Indian Companies (Amendment) Act 1936. Part X-A of the Act aimed at the protection of depositors, restrictions of banking transactions, proper reserve fund maintenance, restrictions on granting loan to the officers of the banks, directors, auditors etc.

World War II witnessed the mushroom growth of small and weak banks in India indulging in speculative activities and thereby endangering the trust money of the public. So, special banking legislations became essential as the Companies Act was not adequate in regulating specialised activities of a concern like bank. Thus, the banking Companies Act, 1949 (now the Banking regulation Act) was passed in India and came into force on March 16, 1949. Section 6(a) of the Banking regulation Act empowered the banks in addition to the normal course of business, they could do, "underwriting and dealing in stock, funds, shares, debentures, debenture stock bonds, obligations, securities and

investments of all kinds; the purchasing and selling of bonds scrips or other forms of securities on behalf of constituents and others...". In regard to the permanent participation of the banks in Corporate shares and debentures section 6 (d) states, "the effecting, insuring, guaranteeing, underwriting, participating in managing, carrying out of any issue, public or private, of state, municipal or other loans or of shares, stock, debentures or debenture stock of any company, corporation or association and the lending of money for the purpose of any such issue." These provisions were remained valid upto the modification on 1.4.1989.

The official approach in regard to the universal banking has been cautious. Because the public in India could not forget the tragedy of bank failure which took place before a few years. In these circumstances, an IMF mission, headed by Bernstein who visited India in 1953, expressed its dissatisfaction regarding inadequate industrial finance here and suggested commercial banks to change their outlook and to start long-term industrial financing.¹² To investigate^{into} the matter The Reserve Bank of India appointed a Committee under the Chairmanship of Mr. A.D.Shroff. This Committee expressed its view somewhat equivocally as followed¹³; "In general, banks appear to be of the opinion that, with their present resources, they can not make advances to industries on a long term basis. It has been suggested that commercial banks would be prepared to undertake, to a certain extent, long-term finance of industries provided,

in case of need, they can obtain loans from the Reserve Bank of India against such advances. The Committee has examined the issue and is of the opinion that, in the general interest of the credit structure of the country, it does not appear to be desirable to encourage a tendency on the part of the banks to lean on the Reserve Bank for providing liquidity against these advances which they make on their own judgement and initiative. The committee is definitely of the opinion that commercial banking practice has proved sufficiently helpful in providing finance to industries within the limits of the resources available today to banks in India. This practice, however, does not preclude - and has not precluded - advances of a medium or long-term character provided individual banks are satisfied in their own judgement that such advances are for moderate amounts in consonance with ordinary banking prudence and are also consistent with the maintenance of liquidity."

The committee, however, advocated¹⁴ that "Even with the present resources available to banks they should endeavour in an indirect manner to make increased finance available to the private industrial sector by (a) adding to their investments in shares and debentures of first class industrial concerns where they are satisfied regarding their transferability and marketability, (b) making larger advances to approved parties against such shares and debentures and (c) subscribing to a greater extent to the shares and bonds of the Industrial Finance Corporation of India and the State Financial Corporations."

The views expressed in the report by the committee did not favour the commercial banks any radical departure from the existing lending practices to the universal banking. To reconsider the possibility of universal banking by the commercial banks was necessary very soon in the climate of the enlarged programme of industrial development in the second five year plan (1956-61).¹⁵ This appears to have been the most important consideration behind the Government's decision, taken ⁱⁿ about 1956, to bring the commercial banks into the field of medium-term lending.¹⁶ The second consideration of the Government decision was to spread out institutional credit facilities all over the country so that the small scale industries and the medium sized industries would be financially helpful. But the machinery of the State Financial Corporations lacked local contacts apart from its ~~mm~~ slow movement. It was thought that the problem could be solved if the bank took greater part in the financing of small and medium sized business. As Dr. Madan put it¹⁷ : "The problem is, on the one hand, to persuade the larger banks to widen the range of their activities to cater to the needs of this [medium- and small-scale] sector of industry to a limited extent and subject to adequate safeguards, and, on the other hand, to protect the smaller banks from the hazards of industrial lending. Any extension of such lending should in the first instance, be confined to the largest banks."

It is gratifying to note that a working group of the Reserve Bank of India (1962) recommended the adoption to a limited

extent by the big commercial banks of the practice of formal term-lending.¹⁸ Government policy has also started to favour the banks in this connection. In 1957 State Bank of India Act 1955 was amended. According to the amendment State Bank was allowed to extent loans and advances to industries for^a period ranging between 6 months and 7 years.¹⁹ On December 23, 1967, a bill was introduced in the Lok Sabha to amend the State Bank of India Act, 1955. The amendment enabled the State Bank of India to grant term-loans for approved purposes for any period upto fifteen years. A nine member Narasimham Committee on the financial system going into the various problems affecting the commercial banking sector brought out a report which recommends banks' participation to provide long-term finance to industry along with short-term finance in the course of its lending operations.²⁰

Part IV : FEASIBILITY

At first sight it may appear that term-lending by the commercial banks does not satisfy the canon of liquidity which may be the major consideration in all bank loan operation. The reason behind this argument is that a large part of the banks' liability consists of demand liability which can be claimed by the depositors at any time. According to sound banking policy commercial banks are to distribute assets in such a way which helps to shift the same into cash in time of needs.

We mentioned earlier that the commercial banks were seeking new avenues to use their vast amount of deposits profitably. As a first step of their venture to this direction, they like their counterparts in U.S.A. proceeded to follow the practice of rolling over a substantial part of their advances. That is to say, while most of the credit is formally made on a demand basis, a fair portion of this demand credit is in effect allowed to run for a considerable periods either through not being recalled, or if recalled through immediate or early renewals.²¹ Thus Indian banks have been making available informal medium term loans without disturbing its liquidity.

But still the commercial banks have been facing tremendous problems of fund when their owned resources (paid up capital and Reserves) and time deposits are showing quick rise over the years.

Paid up capital and reserves form a very small percentage of the total resources of banks. However, they are important because they form only that fixed part of the resources of the banks which may be utilized for the purposes for which other term liabilities are unsuitable.

Table 3.5
Commercial Banks
(Capital and Reserves)

Year	Paid up Capital	Reserves	(Rs. in crores)
			Total
1953	41.1	34.2	75.3
1962	40.2	40.8	81.0
1975	52.61	158.69	211.29
1980	106.77	426.75	533.52
1983			809.00

Source : Reserve Bank of India Bulletin

(relevant issues)

From Table 3.5 we find that capital and reserve of commercial banks in India increased from Rs.75.3 crores in 1953 to Rs.809 crores in 1983, an increase of about 11 times during the period of 28 years. Paid up capital, however, showed very little increase from Rs.41.1 crores to Rs.106.77 crores during the period 1953-80. On the other hand, reserves accounted for almost all the increase, mainly due to the statutory provisions (reserves increased from Rs.34.2 crores to Rs.426.76 crores, more than 12 times increase).

On the other hand, deposits which were considered ^{as} main source of fund for a banking Company played an important role in ^{21A} industrial financing. Table 3.6 clearsthe above point.

Table 3.6
Deposit Trend of Scheduled Commercial Banks
(1948-91)

(Rs. in crores)

Year	Demand Deposit	Time Deposits	Total
1948	606.0	279.0	885.0
1953	500.4	363.0	863.0
1956	629.3	495.8	1,125.1
1957	674.0	672.7	1,346.6
1958	664.0	898.3	1,562.2
1959	683.0	1,132.5	1,815.5
1963	1,000.4	1,252.6	2,253.0
1966	1,426.86	1,522.97	2,949.8
1970	2,329.00	2,946.00	5,275.0
1972	3,126.00	3,979.00	7,105.0
1973	3,958.00	5,207.00	9,165.0
1976	6,106.18	9,071.44	15,177.62
1979	11,050.00	17,621.00	28,671.00
1982	8,290.0	32,259.0	40,549.00
1985	15,039.0	62,036.0	77,075.0
1986	16,841.00	74,613.0	91,454.0
1987	19,283.0	88,515.0	10,7898.0
1988	21,329.0	103,905.00	12,5234.0
1989	23,342.0	116,808.0	140,150.0
1990	28,856.0	138,103.0	166,959.0
1991	33,193.0	159,349.0	192,542.0

Sources : Reserve Bank of India Bulletin (various issues),
Trend and Progress of Banking (various issues).

From Table 3.6 we note a remarkable change in composition of deposits of banks in India for the period 1948 to 1991. In 1948 demand deposits were 68% of the total deposits, ^{and} the remaining 32% was in the form of time deposits. Since then, over a decade, we find a continuous change in the formation of the deposit liabilities of banks; the rate of growth of demand deposits slowly decreased whereas that of the time deposits marked a continuous rise. It was steep during the years from 1957 to 1959 and at the end of the 1991. The position was completely altered when demand and time deposits stood in a proportion of 17.3% and 82.7% respectively.

The changes in the character of both the owned resources and time liabilities of the banks was in favour of the argument that the banks should increasingly participate in the field of long-term financing.^{21B} Table 3.6 reveals that major portion of the growth in time deposits, however, took place after 1957. Between 1958 and 1991, that is over a period of 34 years, there was more than 177 fold rise in time deposits as against only 2.41 times in the preceding ten years. So, the commercial banks in India were in a favourable position to take part in term-lending in large scale.

Part V : TERM LENDING BY THE COMMERCIAL BANKS

The initial response of the commercial banks to universal banking was not encouraging. It is crystal clear from the fact that at the end of^{the} busy season of 1961-62 the total amount of term-loan provided by the commercial banks to the industry was Rs. 79 crores which constituted about 14% of the commercial advances.²² In 1967^{the} total amount of medium term loan extended by the commercial banks to the industry was Rs. 226 crores. It was 13% of^{the} total advances to industry and 81% of the total medium term loan provided by the commercial banks to the various sectors.²³ This disappointing response in the initial years was attributed to the fact that webbed to the orthodox financial theory. The banks were too tradition bound to respond quickly to the financial innovation introduced through the universal banking.

Gradually, the magnitude of industrial term loans provided by the commercial banks was showing a healthy trend with the sharp rise of term-deposits as is evident from the Table 3.7 :

Table 3.7

Trend in Time Deposits and its Impact on Term Lending
to the Industry by Scheduled Commercial Banks

(Rs. in crores)

Year	<u>Time Deposits</u>		Term-loan to the Industry	P.C.Growth over preceding year
	Amount	P.C.Growth over preceding year		
1972	3,979	-	282.52	-
1973	5,207	30.86	336.81	19.21
1974	5,830	11.96	459.50	36.42
1975	6,864	17.73	583.90	27.07
1976	9,079	32.26	610.10	4.48
1977	10,623	17.00	754.17	23.61
1978	13,344	25.61	934.63	23.92
1979	17,621	32.05	1,273.16	36.22
1980	22,822	29.51	1,591.59	25.01
1981	30,298	32.75	2,000.38	25.71
1982	32,259	6.47	2,156.34	7.79
1983	43,838	35.89	2,849.06	32.09
1984	52,425	19.58	3,075.87	7.96
1985	58,113	10.84	3,795.26	23.38
1986	71,585	23.18	4,117.40	8.48
1987	85,692	19.70	4,214.59	2.36
1988	103,905	21.34	6,130.90	45.46
1989	116,808	12.41	6,906.53	12.65
1990	138,103	18.23	7,695.31	11.42

Sources : 1. Time Deposits from RBI Bulletin (various issues)
 2. Term-loan to Industries from Basic Statistical
 Return, RBI (various issues).

From the analysis of the table 3.7 we find that time deposits rose from Rs.3,979 crores in 1972 to Rs.138,103 crores in 1990 and ^{the} growth rate varied between 6.47 per cent to 35.89 per cent. This increasing trend of time deposits inspired the commercial banks to extend term loans to the industry. On examination of the Table 3.7, ^{it} reveals that in 1973, 1974, 1975, 1976, 1985 and 1990 term loans and time deposits showed reversal direction. But from 1977 to 1984 and 1986 to 1989 similar trend was noticeable between term loans and time deposits. In addition to that, out of eighteen years Period, seven years growth in industrial term loans was more than the growth in time deposits. It implies that commercial banks were showing interest in industrial term loans with the increasing trend of time deposits.

Table 3.8

Industrywise Distribution of Term-loan from Scheduled Commercial Banks.

(1972-90)

(Rs. in lakhs)

Sl. No. Industry	1972-81	1982-90	Total
1. Food-manufacturing & Processing	919.94 (9.9)	8504.21 (17.86)	9424.15 (16.26)
2. Chemicals & Chemical Products	1425.79 (13.8)	5129.23 (10.77)	6555.02 (11.31)
3. Textile	1376.76 (13.32)	4381.54 (9.20)	5758.30 (9.94)
4. Engineering	1214.21 (11.75)	4916.39 (10.33)	6130.60 (10.56)
5. Basic Metal & Metal Products	1119.62 (10.83)	4697.44 (9.87)	5817.06 (10.03)
6. Beverage & Tobacco	2781.13 (2.69)	6477.1 (1.36)	9258.4 (1.60)
7. Mining & Quarrying	1304.4 (1.26)	5472.5 (1.15)	6776.9 (1.17)
8. Paper, Paper Products	763.23 (7.39)	3095.01 (6.50)	3858.24 (6.66)
9. Leather and Leather Products	755.6 (.73)	457.78 (.96)	533.34 (.92)
10. Rubber & Rubber Products	256.91 (2.54)	901.29 (1.89)	1158.20 (2.00)
11. Manufacturing of Basic minerals	112.13 (1.08)	277.43 (.58)	389.56 (.67)
12. Cement	116.87 (1.13)	1672.52 (3.52)	1789.39 (3.09)
13. Vehicles & Vehicle Products	1214.21 (11.75)	4916.39 (10.33)	6130.60 (10.58)
14. Other Industries	650.80 (6.30)	4295.22 (9.02)	4946.02 (8.54)
15. Electricity	446.37 (4.32)	1905.60 (4.00)	2351.97 (4.07)
16. Construction	229.44 (2.22)	1267.46 (2.66)	1496.90 (2.58)
Total	10330.41 (100.00)	47612.47 (100.00)	57942.88 (100.00)

Source : Basic Statistical Return Reserve Bank of India,

Note : Figures in parenthesis represent percentage of shares.

It would be interesting to examine in detail the term-loans given to individual industries during the period 1972-90. This focuses on the importance of a particular industry as far as term loans are concerned. Table 3.8 detailed the data relating to industry-wise term-loans given by the banks. The industries mentioned in the table 3.8 are grouped as "traditional industries" and "non-traditional industries".²⁴ Food manufacturing and processing, Textile are considered as traditional industries and remaining industries (SL.2, 4, 5, 6, 7, 8, 9, 10, 11, 12, 13, 15 and 16) are considered under the heading non-traditional industries. The basis of this classification is that ^{the} sustained effort started to develop the latter category of industries comparatively recently.

It is evident from the table that traditional industries' share of term loans from the commercial banks was only 22.22 per cent and non-traditional industries share was 71.49 per cent during the period 1972-81. During the next nine years from 1982-90 traditional industries' share reached to 27.06 per cent and non-traditional industries' share came down to 63.92 per cent. On the other hand, in regard to industrial term loan commercial banks devotion to non-traditional sector was more than 65 per cent while traditional sector's share was more than 26 per cent during the period of 19 years from 1972-90. It implies that commercial banks are extending their term-loan activities to a large extent to those sectors which have recently started.

Part VI : BANKS AND UNDERWRITING OF CAPITAL ISSUES IN INDIA

Commercial banks' entry into the field of underwriting new issues of industrial securities is a significant development in the field of financial assistance to industry. Long before it was suggested by the Indian Central Banking Enquiry Committee (1931) that the larger banks should participate in underwriting operation.²⁵ The Committee's suggestion was not materialized. Because necessary lead was not forthcoming from the larger banks. Later on, The Shroff Committee which was appointed by the Reserve Bank of India in 1953 repeated the same suggestion.²⁶

"The Committee feels that the indirect participation by banks in long term industrial finance would be considerably facilitated if the leading banks in India, in co-operation with insurance companies, could form a consortium or syndicate for underwriting such a consortium could appropriately function under the leadership of the largest joint stock bank in the country, namely the Imperial Bank of India."

Although the Committee's suggestion regarding the formation of consortium was not implemented finally, some banks using their own discretion, entered the field to provide underwriting support to industrial enterprises to sell their shares in the market.^{26 A}

The role of commercial banks in underwriting of capital issues can be presented both in terms of the amount and the number of issues underwritten and their relative shares in total underwriting. During the second five-year plan period (1956-61) the total amount underwritten was Rs.8.20 crores and yearly average amount was Rs.1.64 crores ($Rs.8.20 \div 5$).²⁷ This was the period when commercial banks started to involve themselves in this type of activities for the first time. During this period commercial banks' share was almost one-third.

During the next five year plan period (1961-66) the total amount underwritten by the commercial banks was Rs.12.75 crores and yearly average amount was Rs.2.55 crores ($Rs.12.75 \div 5$). Their underwriting in terms of number ranged between two-fifth and one-third in different years comprising the period.²⁸

During the early years of commercial banks' involvement in underwriting activities was more encouraging than the DFIs and other financial organisations collectively. After 1965 commercial banks' share in underwriting operation showed a declining trend. A more important factor causing decline in the share of banks in this sphere was the emergence of a broad based and diversified underwriting organisation mainly as a result of the participation of the Industrial Development Bank of India (IDBI) and the investment institutions notably Life Insurance Corporation of India (LIC) and Unit Trust of India

(UTI).²⁸ Table 3.9 reveals that in 1967 banks share in underwriting participation was only 10.3 per cent as against 24.09 per cent for LIC, 12.4 per cent for IFC, 15.92 per cent for ICICI, and 30.82 per cent for IDBI and UTI for 6.46 per cent. If we compare bank with DFIs and investment institutions collectively as mentioned in the Table 3.9, we find that ^{the} later group maintained its lead over the former group both in terms of amount and the proportion to total institutional underwriting. During this period there was a great depression in the stock market. And as a conservative institution commercial banks did very little of underwriting. During the period from 1966 to 1983 only in two years namely in 1969 and 1971 banks' share in the underwriting of corporate shares was less than 10 per cent, if we make a comparative study between the banks and other underwriting institutions as mentioned in the table 3.9.

Banks' share was more than 20 per cent in the years namely 1968, 1976, 1978, 1979, 1980 and 1981. That means bank's share in underwriting operation was gradually increasing since 1975. One point which strikes our mind in this connection is that in 1968, 1976, 1979 and 1980 banks claimed second position while in 1978 bank's position was first.

Table 3.9

Banks and their Relative Shares of Underwriting of
Corporate Share.
(Rs. in lakhs)

Year	Bank	LIC	IFC	ICICI	IDBI	UTI	Total
1966-67	136.6 (10.3)	319.5 (24.09)	164.5 (12.4)	211.1 (15.92)	408.7 (30.32)	85.7 (6.46)	1326.1 (100.0)
1967-68	267.5 (20.01)	462.2 (34.58)	75.5 (5.65)	257.9 (19.3)	61.5 (4.60)	212.0 (15.86)	1336.6 (100.0)
1968-69	88.0 (7.96)	366.4 (33.11)	128.8 (11.65)	173.3 (15.66)	93.1 (8.42)	256.7 (23.20)	1106.3 (100.0)
1969-70	122.7 (14.01)	221.0 (25.24)	45.5 (5.20)	210.0 (23.98)	102.5 (11.70)	174.0 (19.87)	875.7 (100.0)
1970-71	84.7 (5.80)	270.0 (18.51)	128.9 (8.84)	358.0 (24.55)	442.4 (30.34)	174.5 (11.86)	1458.5 (100.0)
1973-74	181.2 (11.13)	184.6 (11.34)	213.49 (13.11)	292.61 (17.97)	578.28 (35.52)	177.77 (10.93)	1627.98 (100.0)
1975-76	743.14 (24.86)	438.49 (14.67)	332.6 (11.13)	512.75 (17.16)	787.94 (26.34)	174.25 (5.84)	2988.27 (100.0)
1977-78	1052.16 (3.37)	341.5 (9.87)	465.25 (13.43)	615.94 (17.78)	927.03 (26.76)	62.0 (1.79)	3463.88 (100.00)
1978-79	478.12 (21.37)	80.0 (3.58)	444.88 (19.89)	315.2 (16.33)	815.68 (36.46)	53.0 (2.37)	2236.88 (100.0)
1979-80	612.1 (24.18)	125.25 (4.95)	409.55 (16.18)	468.75 (18.52)	759.18 (29.99)	156.5 (6.18)	2531.34 (100.0)
1980-81	487.59 (20.89)	96.5 (4.14)	415.31 (17.80)	491.07 (21.05)	829.95 (35.57)	13.0 (0.55)	2333.42 (100.0)
1982-83	739.0 (15.35)	86.0 (1.79)	988.0 (20.52)	1009.0 (20.95)	1981.0 (41.14)	12.0 (0.25)	4815.0 (100.0)

Source : Company News and Notes (various issues)

Notes : Figures in parenthesis represent percentage of shares.

Part VII : INVESTMENT HOLDINGS OF CORPORATE SECURITIES

The Commercial banks provide long-term finance to industry through direct subscription to the shares and debentures of joint stock companies. Their holdings of such securities, partly as a result of underwriting commitments have, however, been relatively of small magnitude. Data shown in the Table 3.10 reveals that at the end of 1951 banks' holding in corporate shares and debentures were Rs.12.7 crores, which comprised Rs.8.7 crores of shares and Rs.4.0 crores of debentures. After five years at the end of 1956, the aggregate amount reached to Rs.11.2 crores which indicate a slight decline in security investment by the banks. Again after five years, scheduled commercial banks' holding in corporate shares and debentures totalled Rs.18.1 crores which comprised of Rs.11.4 crores in the form of shares and Rs.6.7 crores in debentures. Since 1961 we notice an increasing trend in corporate investment by the commercial banks till 1990. But the period 1979 to 1981 was exceptional when declining trend in security investment was noticeable. Banks' investment in corporate shares and debentures which was Rs.12.8 crores in 1949 increased to Rs.1862.86 crores in 1990 which indicated an increase of more than 145 times. From the Table 3.10 we find that from 1949 to 1961 investment in shares by the commercial banks was more than debentures. The higher investment in corporate shares was due to the fact that the listed equities of non-government public limited companies were pre-dominated

Table 3.10

Investment in Shares and Debentures of Joint Stock Companies by Scheduled Commercial Banks

(1949-90)

(Rs. in lakhs)

As at 31st December	Shares	Shares & Debentures	Debentures	Total
1949	-	12.8	-	12.8
1950		14.4		14.4
1951	8.7		4.0	12.7
1952	7.4		3.6	11.0
1953	7.3		3.8	11.1
1954	6.9		4.4	11.3
1955	7.7		4.2	11.9
1956	7.3		3.9	11.2
1957	7.2		4.0	11.2
1958	9.3		6.1	15.4
1959	15.1		8.7	23.8
1960	NA		NA	NA
1961 March	11.4		6.7	18.1
1962 March		19.0		19.0
1963 March		21.8		21.8
1971		40.0		40.0
1972		45.0		45.0
1976	27.35		65.32	120.02
1977	29.23		107.63	136.86
1978	35.11		92.15	127.26
1979	44.03		71.19	115.22
1980	43.55		69.98	112.53
1981	46.20		67.72	113.92
1982	41.28		81.76	123.04
1983	42.71		98.01	140.72
1984	47.23		126.91	174.14
1985	48.54		129.43	177.97
1986	42.11		141.60	183.71
1989	160.83		1157.42	1318.25
1990	224.14		1638.72	1862.86

Sources : Figures for 1949-61 (Dec.) are from RBI Annual Report on Trend and Progress of Banking in India and the balance from RBI Bulletin.

in the capital market during that period. Calculation based on the information given in Reserve Bank of India bulletin (1967) reveals that equity capital constituted 77.1 per cent, Preference Share Capital 14.5 per cent and debentures constituted only 8.4 per cent of the total capital employed by the all non-government public limited companies. From 1976 to 1990 debentures were making lead over the shares. This change came as to the regular payment of interest was confirmed and if the Company failed to pay interest, the bank had ^{the} right to foreclose and realize its capital from debenture investment.

Part VIII : CONCLUSION

A unified and compact banking system was developed in India during the post 1951 period with sufficient strength and stability as a result of vigorous official measure. This type of growing realisation was felt due to integrate banking operations and policies with planning priorities. Apart from the bank credit to the industry, a significant development since the mid-fifties relates to the diversification of the range and type of bank financing of industry. Another diversification in Indian banking was ^{the} underwriting of corporate shares and debentures. They also extended their financial assistance to private industry through direct subscription to shares and debentures.

The diversified form of financing by the commercial banks is an indication of their interest to move towards universal banking. Quantitatively speaking, initial response to the magnitude of such financing was not as encouraging to alter the basic structure of banking vis-a-vis industrial financing. They continued to pursue the prototype line of providing short-term industrial credit against rapidly-turned-over assets. None of the excursions in the new directions can be said to have materially altered the basic structure of Indian banking till the later half of the sixties. The developments in the post nationalised period necessitating a more equitable distribution of bank finance to sectors and areas, have of course, affected the basic structure. Industrial term loan which was Rs.282.52 crores in 1972 rose to Rs.7695.31 in 1990. It was undoubtedly a significant rise. One striking feature during the period 1972-90 was that non-traditional sectors share of term loan from the commercial banks was more than the traditional sector. The banks were less successful in the field of underwriting, albeit their good performance in the beginning. Their term assistance through equity participation was, however, less satisfactory.

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Chapter IV

ASSESSMENT OF UNIVERSAL BANKING : A THEORETICAL FRAMEWORK AND MODEL SPECIFICATION

Part I : INTRODUCTION

We will consider in this chapter a suitable methodology for the performance appraisal of universal banks within the commercial banking set up. To do so, we first review in Part II previous studies on this subject particularly in respect of methodological framework. Part III will review the econometric studies which have so far been reported on scale and scope economies in financial institutions. In Part IV, however, we will develop and calibrate a suitable econometric model which can be used to assess the performance of commercial banks, both in absolute and relative senses in term financing business.

Part II : REVIEW OF UNIVERSAL BANKING LITERATURE

A number of studies have been reported on universal banking in different countries. A substantial volume of the literature have, however, been devoted to a hypothesis concerning the raison-de-etre of universal banking. The debate has presumably originated from the investigation why, disobeying the lead of Great Britain for the adoption of orthodox type of banking, different countries adopted universal

banking in their development processes.

The pioneer study on the above issue was made by Alexander Gerschenkron who hypothesised that the countries like Germany, Italy etc. where industrialization were initiated much later than the period of industrial revolution in Great Britain, adopted universal banking.¹ He reasoned that the need for an arrangement of voluminous investment of fund to support large scale industries at the initial stage of development itself compete with the already industrialized countries like England compelled them to introduce such institutions. Gerschenkron tested this hypothesis for the banking systems of Germany, Russia, England, Austria, Belgium, Spain and Italy.

Cameron Rondo sought to re-examine the Gerschenkron hypothesis in his edited work on 'Banking in the Early stage of Industrialization'. In that edited work Olga Crisp studies the nature of banking in Russia,² Hugh T. Patrick on that in Japan³ and Richard Tilly on that in Germany.⁴ The hypothesis was however, again taken up by Cameron Rondo in his another edited work 'Bank and Economic Development'. This volume was contributed by Richard Sylla on United States of America,⁵ Cohen on Italy,⁶ Kozo Yamamura on Japan⁷ and George D. Green on Louisiana.⁸ Rondo's work apart, two more studies exclusively analysed the Gerschenkron hypothesis. Those were Banking and Industrialization in Austria-Hungary by

Richard L. Rudolf⁹ and Banking and Finance in West Germany by Francke Herman and Michael Hudson¹⁰ and the Economic development of France and Germany by John M. Clapham.¹¹ These authors did not, however, see eye to eye in regard to the strength of the Gerschenkron hypothesis to explain the emergence of universal banking in the international scenario.

Apart from probing into the causes for the emergence of universal banks, a number of studies have devoted also to the growth of the universal banking system and its associated advantages and disadvantages in different countries. We may refer in this context the study on Money and Banking in Japan¹², Financial Institutions of Japan by Reserve Bank of India,¹³ and The Modern Japanese Banking System by Hubert F.Schiffer,¹⁴ where the development of universal banking in Japan, the need for such a banking system after the Meiji restoration and the contribution of the Zaibatsu group of financial intermediaries to its development had been discussed. The growth aspects of universal banking had been discussed for Germany in an unpublished work of International Monetary fund (IMF) on "Functional and structural aspects of the German universal banking System by Klaus - Walter Riechel."¹⁵ According to this work German universal banks would keep a close surveillance on the business and continue its proximate association even after profile start accruing and the Company stand steadily on its feet. Similar type of work was done by P.B.Whale focusses light on the evolution, growth and viability of German universal banking.¹⁶

The study on the growth of universal bank in United States of America is no less voluminous. A pioneer work in this field has been done by Milton Friedman and Schwartz, A.J.¹⁷ who had investigated the extent of universal banking by the American commercial banks during the period 1867-1960. They had, however, found that Federal Reserve Act (1913) favoured the universal banking by the commercial banks through lowering required reserves for time deposits than for demand deposits. Similar study was jointly made by C.A.Fillips, T.F.Acmanus and R.W.Nelson¹⁸ who investigated that the proportion of banks assets which represented commercial credit showed decreasing trend in comparison to their investment in capital loans. Harold G.Moulton's work¹⁹ also shows that prior to the organisation of Federal Reserve System commercial banks in U.S.A. followed the principles of universal banking. They used to provide real estate loan although the same was prohibited by the banking regulation. This study reveals that commercial banks share in long term investment were higher than those of the commercial loan. Since 1920 there was a boom in capital market of U.S.A. Many firms started to approach capital market for the first time. As a result banks were losing their traditional lending business to the capital market. To regaining their losing ground of business the commercial banks entered into the capital market which is the subject-matter of study made by White Engene in "Banking innovation in the 1920's ; The Growth of National Banks' Financial Services".²⁰ But all classes of

banks had no direct entrance to the capital market. While the State Bank could engage directly in security business, National banks had to overcome more legal hurdles to diversify their product offerings. To overcome the legal barriers to invest in company securities the National Banks incorporated security affiliates under State Corporate Charter. These aspects of universal banks in USA were studied by Peach W. Nelson in the security affiliates of national banks.²¹

The need for the universal banking system for rapid industrialization was also discussed at length by L. Malhapt in "In Defence of Universal Banks",²² by United Nations Industrial Development Organisation (UNIDO) on Development Finance Institutions and Multipurpose Banking²³ and by F. Wilhelms Christians on "Why Universal Banks Works."²⁴

There is a scanty of literature on Universal Banking in India. In some government reports like that of Shroff Committee²⁵ (1954) and Indian Industrial Commission (1916-18)²⁶ we find discussions on the necessity of universal banking in India to foster her industrial development. A similar study was also made by Reserve Bank of India just before the advent of universal banking culture in India during the post Independence era. The pioneer academic study in this field was "Commercial Banks and Industrial Finance, Term lending and underwriting" by M.Y. Khan and Preeti Singh.²⁷ In their work they have

investigated the fast role played by the commercial banks in India in industrial financing via term loans and underwriting of capital issues by corporate enterprises. Suresh Bedi's work on "Universal Banking System : A Case for adoption in developing countries"²⁸ highlights the universalization of commercial banks's function since the mid-fifties. The other studies made in Indian context are "Banking in India in the Eighties" by Raj Kumar Nigam"²⁹ "The Changing Profile of Indian Banking" by J.N.Saxana,³⁰ "Role of Commercial Banking in a Developing Economy with Special Reference to India" by V.N.Kukku, "Nationalised Banking and Economic Development" by G.D.Khan³² and Corporate Investments, Savings and Borrowings" by L.C.Gupta,^{32A}

A noteworthy study was conducted by Industrial Licensing Policy Enquiry (Dutt) Committee³³ in the field of institutional financing. The study revealed that, out of total assistance sanctioned to the private sector, the S.F.C.'s and SIDCs together provide only 12.2 per cent while three-fourth of the total assistance provided by public financial institution is channelised through institutions which do not deal with small and medium concerns.

Joshi (1965)³⁴ examined the role of the financial intermediaries in providing finance to large scale industries in the private sectors. After analysing the contribution of each important intermediaries

towards industrial development in India, he estimated these intermediaries have participated 17 per cent of investments in various industries against 39 per cent in share capital of public limited companies.

Gupta (1969)³⁵ from the extensive study viewed that, the growth of institutional finance emerged in India due to structural change for industrial financing system with wide change of socio-political situations in India. He attempted to measure overall impact of financial institutions on capital formation in the organised private sector as also on the allocative efficiency of financial system. He observed during first plan financial assistance rendered by special institutions represented only 4.1 per cent of gross fixed investment in private industry which rose to 7.9 per cent in second plan further to 18.1 per cent in the third plan period. He also found that commercial banks remained the most important single agency for financing the private corporate industry and Life Insurance Corporation (LIC) was the single largest purchaser of industrial securities and underwriter of new issues of large and established companies. While investment in industrial securities by Unit Trust of India (UTI) still remain in very narrow range.

Khan (1996)³⁶ analysed the significant development in commercial banks since the mid-fifties related to the widening of

range of banking operations. According to him term lending and underwriting of securities, as forms financing, represented a radical departure from the traditional lending practice of supplying short-term credit for meeting the working capital requirement. In addition to that Professor Khan found the commercial bank's widened range of financial assistance to industry, partly through the purchase of shares and debentures and partly through the lending against such securities.

³⁷ Bandyopadhyay, Tarun and Indrajit Ray (1995) analysed the causes behind the formation of development finance institutions in India before independence. Their investigation shows that nationalist spirit among the people acts behind the genesis of development finance institutions in pre-independence India.

³⁸ Lokanathan (1969) in his lecture delivered under the auspices of A.D.Shroff Memorial Trust observed that, the problems and conditions in respect of industrial finance in India remained more or less the same right upto the end of Second World War and ushered an era in the independent India. Thus 1947 may be taken as a sort of benchmark in dealing with industrial finance.

This point was investigated by A.K. Banerjee (1963), M.Kidron ³⁹ (1965). ⁴⁰ Aziz (1993), ⁴¹ Highlighted his actual experience of decentralised planning in the state of Karnataka and suggested the institutional structure which are necessary to achieve the ends of decentralised governance.

⁴²
Basu (1961) made a comparative analysis of structure, organisation and activities of specialised institutions for industrial finance in Germany, Britain and Japan and suggested for the establishment of suitable machinery to solve hindrances to term-financing in Indian industries.

This review demonstrates only the descriptive assessment of the universal banking within the commercial banking set up without taking resort to the recent advancement in statistical tools and techniques in appraisal.

Part III : Review of Econometric Studies Reported on Scale and Scope Economics in Universal Banks.

⁴³
A recent study has examined the concomitant viability of commercial and development banking activities within India's commercial banking set-up to assess the prospect of universal banking in India. It has followed the following sequence of logic : started with a probe

into the extent of scale economies in the prevailing Indian banking technology to know about the cost implications of a larger volume of activities, it has proceeded to examine the scope of accommodating development banking within the existing output-mix. The concept of cost sub-additivity has been adapted to this end. The study has found evidences from time-series data that there exist substantial scale economies among Indian nationalised commercial banks, and that they are featured with technological sub-additivity. The present study, however, seeks to examine the same hypotheses on the basis of cross section field survey data. The branch-wise sample data enable us to investigate into the existence of scale economies at the plant-level in contrast to the firm-level scale economies studied previously. Moreover, the plant-level scope economies for universal banking can also be examined thereby. Note that the plant-level scale economies have been sought to be measured by incorporating a 'branching' variable in the cross-section model at the firm level.⁴⁴ An exclusive plant-level model can, however, yield more powerful conclusions than what a single variable in the firm-level model can.

Part IV : DEVELOPMENT OF ECONOMETRIC MODEL TO ASSESS
THE PERFORMANCE OF UNIVERSAL BANKING

Thanks to the duality between production and cost functions, the cost behaviour of a firm is often examined for the appraisal of its production efficiency.⁴⁵ Following the

study under reference, we measure the commercial banking activities (x_1) of an organisation by the aggregate of various types of deposit and short-term loans, and its development banking activities (x_2) by term-loans sanctioned to the industrial sector. This study does not incorporate investment in shares and debentures in x_2 since such practices are absent among the sample banks. We model both these variables as arguments though the latter is contested in the literature⁴⁶ and used as a dependent variable also in some studies. Both these variables are, however, measured in rupee terms, and total cost (Tc), having incorporated interest expenses as one of its components at disagreement with the referred study, the exercise follows an intermediation approach to the analysis of bank behaviour.⁴⁷ The wage rate (w) is measured as usual by the average salary and wages per employee.

In line with the recent trend of the literature, we postulate the following conventional translog relationship for the banks' cost behaviour :

$$\begin{aligned} \ln Tc = & \alpha_0 + \alpha_1 \ln x_1 + \alpha_2 \ln x_2 + \alpha_3 \ln w + \alpha_{11} (\ln x_1)^2 + \alpha_{22} (\ln x_2)^2 \\ & + \alpha_{33} (\ln w)^2 + \alpha_{12} \ln x_1 \ln x_2^2 + \alpha_{13} \ln x_1 \ln w + \alpha_{23} \ln x_2 \ln w \end{aligned} \quad \dots \quad (1)$$

Since, as we will shortly discuss, the conventional translog function is not suitable to measure the scope economies, a hybrid translog cost relationship is also adopted here as an alternative. A typical hybrid translog⁴⁸ cost function is of

the following form.⁴⁹

$$\begin{aligned} \ln Tc = & \bar{\alpha}_0 + \bar{\alpha}_1 x_1 + \bar{\alpha}_2 x_2 + \bar{\alpha}_3 \ln w + \bar{\alpha}_{11} (x_1)^2 \\ & + \bar{\alpha}_{22} (x_2)^2 + \bar{\alpha}_{33} (\ln w)^2 + \bar{\alpha}_{12} x_1 x_2 \\ & + \bar{\alpha}_{13} x_1 \ln w + \bar{\alpha}_{23} x_2 \ln w \dots \quad (2) \end{aligned}$$

In certain cases, however, the estimation of conventional and hybrid translog function with the wage rate as one of the arguments leads to insignificant values of F statistics. We attempt, therefore, to estimate the following alternative relationships where wage rate (W) is excluded :

$$\begin{aligned} \ln Tc = & \bar{\alpha}_0 + \bar{\alpha}_1 \ln x_1 + \bar{\alpha}_2 \ln x_2 + \bar{\alpha}_{11} (\ln x_1)^2 + \bar{\alpha}_{22} (\ln x_2)^2 \\ & + \bar{\alpha}_{12} \ln x_1 \ln x_2 \dots \quad (3) \end{aligned}$$

$$\begin{aligned} \ln Tc = & \underline{\alpha}_0 + \underline{\alpha}_1 x_1 + \underline{\alpha}_2 x_2 + \underline{\alpha}_{11} (x_1)^2 + \underline{\alpha}_{22} (x_2)^2 \\ & + \underline{\alpha}_{12} x_1 x_2 \dots \quad (4) \end{aligned}$$

As adumbrated above, the banking technology among the samples is appraised here from the viewpoints of scale and scope economies. The former would entail whether the sample branches contain in themselves adequate excess capacity for the accommodation of any additional activities, and the latter would mop up the technological jointness between commercial and development banking activities. The following constitutes our measure of scale economies (SL) :

$$SL = \frac{\sum_i x_i MC_i}{C} = \sum_i \eta_c x_i \quad \dots \dots \quad (5)$$

which for models 1, 2, 3 and 4 becomes

$$\sum_i \eta_c x_i = \sum_i (\alpha_{i1} + 2 \alpha_{ii} \ln x_i + \alpha_{ij} \ln x_j + \alpha_{i3} \ln w) \quad \dots \dots \quad (6)$$

$$\sum_i \eta_c x_i = \sum_i x_i (\bar{\alpha}_i + 2 \bar{\alpha}_{ii} x_i + \bar{\alpha}_{ij} x_j + \bar{\alpha}_{i3} \ln w) \quad \dots \dots \quad (7)$$

$$\sum_i \eta_c x_i = \sum_i (\bar{\bar{\alpha}}_i + 2 \bar{\bar{\alpha}}_{ii} \ln x_i + \bar{\bar{\alpha}}_{ij} \ln x_j) \quad \dots \dots \quad (8)$$

$$\sum_i \eta_c x_i = \sum_i x_i (\underline{\alpha}_i + 2 \underline{\alpha}_{ii} x_i + \underline{\alpha}_{ij} x_j) \quad \dots \dots \quad (9)$$

respectively. These measures are estimated at the (geometric) mean sample as also at plant levels. If scale economies are found to prevail among sample branches, we proceed to examine the relative strength of development and commercial banking activities in the overall scale economies by dint of the measure, product specific scale economics ($\eta_c x_i$).

The scope economies (SC) are said to prevail when the cost function behaves sub-additively, that is, when total costs resulting from joint production of commercial and development banking are less than the sum-total of costs, resulting from their separate productions :

$$C(x_1) + C(x_2) > C(x_1, x_2)$$

A super-additive cost function :

$$C(x_1) + C(x_2) < C(x_1, x_2)$$

indicates, on the other hand, the prevalence of scope diseconomies. Panzar and Willig, however, measure the same per unit of total cost :

$$sc = \frac{c(x_1) + c(x_2) - c(x_1 x_2)}{c(x_1 x_2)} \dots \quad (10)$$

Scope economies or diseconomies are said to prevail accordingly as

$$sc \geq 0$$

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Chapter V

COST EFFICIENCY OF UNIVERSAL BANKING IN INDIA :

EVIDENCES FROM CROSS SECTION DATA

Part I : INTRODUCTION

We are now equipped to appraise the cost efficiency of universal banking within the commercial banking set up in the district of Darjeeling, West Bengal. To assess its efficiency we have collected data through conducting field survey among the commercial banks in the district. The findings of the survey are presented and interpreted in this chapter with the help of the models developed in the last chapter. This chapter is divided into three parts. Study area and financing to industries are considered in part II, while the subject-matter of part III is related to emperical result analysis. These are followed by conclusion in Part IV.

Part II : STUDY AREA AND FINANCING TO INDUSTRIES

For the purpose of model estimation, cross-section data were collected on the following series : (a) annual operating expenditure under the heads of rent, electricity, stationery and interest expenses (b) wages and salaries along with number of employment, and (c) the level of output in respect of deposits (fixed, saving and current), term loans and working capital loans.

There were 61 branches of different commercial banks in the study area of Darjeeling district.¹ Instead of sampling such a thin set of population, we had initially sought to enumerate census, and had accordingly approached all of them with a structured questionnaire. Out of sixty-one, twenty branches responded fully to what we designed to yield for the model estimations with eleven partial respondents. The sample set covering one-third of the population was thus fairly representative in character, and showed a high degree of randomness in view of no preconceived design in sample selection. The respondents, however, belonged to eight commercial banks, viz., Central Bank of India, State Bank of India, United Commercial Bank, United Bank of India, Indian Bank, Bank of India, Indian Overseas Bank and Allahabad Bank. Requisite data were collected for three consecutive years so that the estimations could be repeated to ensure temporal stability of results.²

The data generated from the survey are presented below in aggregative forms for the economy of space. These are also discussed in a nutshell to gather an initial impression about the scope of universal banking and the nature of scale economies among the sample branches.

Table 5.1

Deposit Level of Sample Branches

(Amount Rs. in crores)

(Account (A/C) in '000)

Year	Fixed Amount	A/C	Saving Amount	A/C	Current Amount	A/C	Total Amount	A/C
1990	54.09 (48.00)	31.42 (17.89)	39.97 (35.47)	144.16 (81.92)	18.62 (16.53)	.40 (.23)	112.68 (100.00)	175.98 (100.00)
1991	73.39 (48.51)	33.97 (18.09)	60.76 (40.17)	153.34 (81.68)	17.11 (11.32)	.43 (.23)	151.26 (100.00)	187.76 (100.00)
1992	83.07 (47.11)	37.00 (18.20)	69.53 (39.44)	165.82 (81.57)	23.70 (13.70)	.46 (.23)	176.30 (100.00)	203.28 (100.00)

Notes : Figures in Parentheses represent percentage

Source : Field Survey.

Bank output is represented, inter alia, by deposits measured in terms of amount or the number of accounts. In the rupee term, fixed deposits shared the highest proportion in total deposits during the study period. It accounted for nearly one-half of the same during 1990-92. The saving deposits were less than 40 per cent and the current deposit, in the neighbourhood of 15 per cent. The lion's share of fixed deposits among the sample banks indicated that they were well in a position to engage in term financing without a stake in liquidity. In terms of the number of accounts, however, a different scenario emerged. The saving accounts had the largest share, viz. around 82 per cent, followed by fixed and current deposits with respective shares at 18 and 23 per cents.

There was, however, some growth, in the amount of aggregate deposits during 1990-92. Its growth rate is worked out at 34 per cent in 1990-91 and 16 per cent in 1991-92. The number of account grew less smartly, at a rate of only 6 per cent in 1990-91 and 8 per cent in 1991-92. Table 5.2 highlights break-up of total expenditure among sample branches.

Table 5.2

Total Expenditure and their Components

(Rs.in Crores)

Year	Wages	Interest	Rent	Stationery	Electricity	Total
1990	2.20 (34.48)	3.78 (59.25)	0.36 (5.64)	0.01 (0.16)	0.03 (0.47)	6.38 (100.00)
1991	2.28 (32.95)	4.23 (61.13)	0.37 (5.35)	0.01 (0.14)	0.03 (0.43)	6.92 (100.00)
1992	2.33 (27.04)	4.96 (57.54)	0.37 (4.29)	0.02 (0.23)	0.94 (10.90)	8.62 (100.00)

Notes : Figures in parenthesis represent percentage

Sources : Field Survey.

Total expenditures are seen to grow from Rs.6.38 crores in 1990 to Rs.6.92 crores in 1991 and again to Rs.8.62 crores in 1992 showing growth rates of 8.46 per cent and 24.56 per cent respectively. Given 34 per cent and 16 per cent growth rates in deposits during the corresponding years, as pointed out above, these growth rates in total expenditures indicate lower average expenditure per unit of deposit. These

are indicative of higher capacity utilization and the prevalence of scale economies among the sample banks.

The component analysis of total expenditures, however, shows that interest payment constituted the highest share in total expenditures (around 60 per cent), followed by wage bills (30-35 per cent) and rent (around 5 per cent). The stationery and electricity constituted 2-5 per cent of total expenditures. Be it noted from the table above that all the components, save interest, showed downward trends during 1990-92 and these were balanced by higher payments of interest. In so far as higher interest payments represent higher deposit mobilisation activities, the compositional change in total expenditure indicates a cost effective development among sample branches.

The employment level remained almost stationary during the period. It was 407 in 1990, 418 in 1991 and 426 in 1992, constituted 19.65%, 20.33% and 20.65% respectively of the managerial cadre, and 80.34%, 79.66% in the clerical and other posts. The average rate of salary is calculated at Rs.0.54 lakhs for 1990, Rs.0.55 lakhs in 1991 and Rs.0.56 lakhs in 1992. The stationary state of employment against a higher output levels is again indicative of scale economies.

Sample banks' assistances towards working capital

and term loans during 1990-92 are furnished in the following table :

Table 5.3
Working Capital and Term Loans
(Rs.in crores)

Year	Working Capital loan	Term loan	Total
1990	15.65	16.27	31.92
1991	19.61	19.85	39.46
1992	21.28	25.63	46.91

Source : Field Survey

Industrial financing by sample branches, however, revealed a striking balance between term loans and working capital loans. The quantum of the former was higher only by 0.62% in 1990, 0.24% in 1991, and 4.35% in 1992 than that of the latter. The sample branches were thus adequately exposed to the principle of universal banking. A preliminary analysis of the survey data thus shows : (1) that a high proportion of fixed deposits made term-financing a feasible business among sample branches, (2) that they did carry out a good deal of such business and (3) that they experienced some degree of scale economies by way of conducting larger deposit mobilisation within a virtually stationary cost structure.

Part III : EMPIRICAL RESULT ANALYSIS

We have estimated the conventional translog and hybrid translog cost functions with two sets of independent variables : (x_1, x_2, w) and (x_1, x_2) . Each of these sets has been estimated for three consecutive years, 1990-92. We have thus twelve estimated relationships denoting TR_{ij} for the conventional translog function and Hy_{ij} for hybrid translog function. The subscript i runs over (1, 2) for the sets of independent variables (x_1, x_2, w) and (x_1, x_2) respectively and with j running over (1, 2, 3) for the years 1990, 1991 and 1992 respectively. We have not presented the estimated values of the parameters and the relevant statistics for the economy of space.

As much as eleven out of twelve estimated relationships have been found to yield F statistic significant at more than 99% level and the rest, namely TR_{12} , at more than 95% level. The R^2 -values for those estimates range over 0.63-0.93. Five models, viz. TR_{12} , Hy_{12} , TR_{22} , Hy_{22} and TR_{32} , have triggered the value of the statistic in the range of 0.63-0.76, two models (TR_{21} and TR_{31}) in the range of 0.84-0.89 and the remaining five above 0.90. Most of the estimated relationships are thus found significant from the statistical viewpoint.

The Durbin-Watson DW statistic calculated for the estimated relationships show on comparison with its tabulated

values with appropriate degrees of freedom that the DW values for six estimates, lie above the upper limit d_u indicating the absence of autocorrelation in those estimations. For the remaining models the observed DW values lie within the indeterminate zone $d_L - d_u$. These relationships (excepting Hy 32), however, involve w and its associated variables. Dissociation of the model from those variables would eliminate the possibilities of autocorrelation.

In regard of estimates for individual parameters, the observed values of t-statistic have been found significant at more than 90% level for as much as fifty out of ninetysix estimates. Only five estimates are insignificant at 60% level, the significant level of other estimates lying within 60-90% point.

This exercise has indicated by large commercial banking (x_1) more significant than the development banking(x_2). The estimated co-efficients for the former have yielded t-statistic significant at more than 80% level in eleven out of twelve models and at more than 90% level in nine models. Those respective levels of significance have been attained by the latter in seven and four models. The squared forms of both of those variables have also been found highly significant in most models. More than 80% significant level has been attained by them in nine and eight models respectively. Their

joint variation represented by the variable $x_1 x_2$ has mostly been found less significant, however. Its observed value of the Student's t has been significant at above 80% point only in five models and above 90% point in only two models. The wage rate has also cut a poor level of significance (less than 80%) in as much as seven models. Its interaction with the variables commercial and development banking, captured by $x_1 x_3$ and $x_2 x_3$ respectively, have also been less satisfactory from the viewpoint of estimated t. Eight models yielded less than 80% significant level for both of them.

The models with and without wage rate as independent variable do not however yield much difference in terms of the number of significant variables. While the former generates 71% co-efficients with significant level above 80%, the latter yields 69% such co-efficients. The co-efficients with significant level at more than 90% are also almost the same, namely 56% and 50% in the respective models. The variation in functional form does not yield a difference in the number of significant co-efficient. Thirtyfour co-efficient are found significant at more than 80% level in both translog and hybrid functional forms. A variation in data set over year, however, leads to difference in this regard. Around twentyfive co-efficient have been significant at more than 80% for the data set of 1991 and 1992 and nineteen such co-efficients for that of 1990.

The overall and product-specific scale economies are calculated from the estimates of different models and are presented in the following table.

Table 5.4

Product specific and 'overall' scale economies

Model	η_{cx_1}	η_{cx_2}	'Overall'
TR 11	0.5464	0.6171	1.1635
TR 12	0.3644	0.5829	0.9473
Hy 11	0.1276	-0.4117	-0.2841
Hy 12	0.1167	0.4475	0.5642
TR 21	0.4387	0.1166	0.5553
TR 22	0.4147	0.2966	0.7113
Hy 21	0.1459	0.1305	0.2764
Hy 22	0.1298	0.2959	0.4257
TR 31	0.1092	0.2578	0.3670
TR 32	0.2332	0.2908	0.5240
Hy 31	0.1021	0.0424	0.1445
Hy 32	0.1399	0.1032	0.2431

There is only one unwanted sign for the estimates of overall scale economies. Almost all of the remaining estimates indicate the existence of substantial scale economies among the sample banks. Barring the models TR 11 and TR 12 which yield constant return to scale, the estimates range over 0.14 - 0.71 implying that an overall scale expansion

would be cost-saving by 29-86% points. The hybrid models are however indicative of higher levels of scale economies than those indicated by the conventional ones.

The scale economy estimates with respect to both commercial banking (η_{cx_1}) and development banking (η_{cx_2}) also confirm the existence of substantial scale economies. The estimates reveal the extent of cost savings by 44-90% for the expansion of commercial banking activities and 39-96% for the augmentation of development banking activities. Although cost saving variations in respect of these activities appear quite insignificant in terms of their range values, a modelwise comparison between them show that the development banking activities are less cost saving for seven models. Out of eleven (abandoning one negative estimated-value) and more cost saving for only two models. The remaining two models, however, indicates both the activities almost similar in this respect. On the strength of these evidences, we conclude that in the present product-mix, expansion of commercial banking activities would be a more judicious choice.

The firm level scale economies, both 'overall' and product specific, are estimated for all the models. Instead of presenting the scale economic values for the economy of space, we present the values of simple correlation co-efficients.

calculated between the size of the firm (defined in terms of deposit level) and the scale economies.

Table 5.5

Simple Co-relation co-efficient between
the firm size and scale economies

Model	Commercial Banking	Development Banking	'Overall'
Hy 11	-0.157	-0.2751	-0.213
Hy 12	0.045	0.204	0.371
TR 11	-0.038	0.685	0.004
TR 12	-0.413	0.564	0.390
Hy 21	-0.938	0.89	0.629
Hy 22	-0.714	0.748	0.378
TR 21	-0.219	0.428	0.185
TR 22	-0.230	0.706	0.467
Hy 31	0.165	-0.367	-0.274
Hy 32	-0.528	0.513	0.366
TR 31	0.639	0.064	0.087
TR 32	-0.135	0.132	-0.070

The values of r are seen negative only in three models, viz. Hy 11, Hy 31 and TR 32, which indicate higher level of scale economies along with the expansion of a branch's scale. But the majority of the models do not corroborate this

proposition. They confirm per contra a lower value of scale economies associated with larger scale. It should be noted that even this majority indications are not strong statistically since r values in almost all the models are found at less than 0.5 mark. A more plausible inference is, therefore, a weak relationship between the size of the bank and economies of scale.

The firmwise results of scale economies specific to development banking are more similar to those for 'overall' scale economies in that all models, barring two, yield positive co-relation co-efficient. Sixty per cent of positive r values are, however, found to lie above 0.5. This indicates a relatively stronger evidence in support of the hypothesis that scale economies gradually disappears along with the expansion of firm size. The Commercial banking activities, however, bear different nature. The firmwise scale economies specific to these activities have revealed a negative co-relation co-efficient with firm size in all but three models. Moreover, three of ten models trigger above 0.5 mark of r .

Table 5.6

Scope economies

Models	$a_1 \times a_2 + a_{12}$	SC_2
Hy 11	-46.8877	127.79
Hy 12	0.0746	1.4732
TR 11	-7.65019	-0.4226
TR 12	0.1290	0.1429
Hy 21	0.4166	6.8904
Hy 22	0.0554	1.3872
TR 21	2.4407	1093.6087
TR 22	0.2004	0.1127
Hy 31	1.4488	62.2814
Hy 32	0.01395	1.2201
TR 31	0.1844	-0.0898
TR 32	0.0634	0.4454

Table 5.6 contains the model-wise results of the verification of sufficient condition of scope economies as also the values of scope economies. Most of the results relating to the former are indicative of non-fulfilment of the sufficient condition by virtue of their positive signs. But the non-fulfilment of sufficient conditions does not necessarily imply that scope economies would not exist. Estimate of the measure of scope economies indeed indicate

by virtue of their positive signs that there is cost complementaries in the prevailing banking technology among our samples. The average cost is therefore, expected to fall if the commercial banks undertake development banking activities along with commercial banking.

Part IV : CONCLUSION

Based on three consecutive years' cross section data for 20 sample branches of various nationalised commercial banks in Darjeeling district, this study has estimated four alternative models of conventional and hybrid translog specifications. Statistically significant on the strength of F-ratio and R²-coefficient, these estimated relationships have indicated certain economic characteristics of Indian commercial banking technology akin to the observation of the study under reference. Both the exercises confirm the prevalence of 'overall' scale economies, and of scale economies specific to the commercial and development banking activities separately. Secondly, the existence of cost complementaries has been indicated among the commercial and development banking activities by both the studies.

But dissimilarities also crop up in a number of fronts. The present study disagrees firstly with the extent of scale economies that the earlier study has observed.

The scale economies are 0.14-0.71% in the present one and 0-0.14% in the earlier one for the 'overall' measure, 0.10- 0.54% and 0.02-0.60% respectively in respect of commercial banking, and 0.04 - 0.61% and 0.39-0.69% respectively in respect of development banking. Secondly, the present study has revealed a fall in the extent of scale economies, specific to development banking activities and a rise in respect of commercial banking activities, just in contrary to the observation of the previous study.

Notes and References :

- 1 Central Bank of India, "Service Area Credit Plan for the District of Darjeeling", (1990), p.26.
- 2 Humphrey, D.B., "Intermediation and Cost Determinants of Large Bank Liability Composition", Journal of Banking and Finance 5 (June, 1981), pp.167-85.

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Chapter VI

SUMMARY OBSERVATIONS AND POLICY IMPLICATIONS

The genesis of universal banking is beautifully brought out by Alexander Gerschenkron. According to Gerschenkron universal bank evolves in a country where industrialization has a time distance from its birthplace in England. Gerschenkron considers three typical cases in his hypothesis. They are advanced region, moderately backward region and extremely backward region. In an advanced and extremely backward region, factory and state respectively take part in industrial financing while in a moderately backward region banks itself take initiative to industrial financing. This hypothesis cannot claim its general application. It can explain the genesis of universal banking in Germany, Italy, Austria. But in the cases like Japan, United States of America this hypothesis fails to claim its application to explain genesis of universal banking. In these countries rapid increase of time deposits, rather than economic backwardness, encouraged the commercial banks to provide long term loan along with short term working capital loan. Much of the contribution that the financial sector can make to growth and development depends upon the legislative and regulatory arrangements devised to guide the activities of financial institutions. The formulation of universal banking regulation also favoured the commercial banks to take part in economic

Growth of the country. In Germany and Japan banking regulations are more liberal than the U.S.A. in favour of universal banking. In U.S.A. although universal banking was being hampered on account of the imposition of strict restriction by the National Banking Act (1863) yet the Federal Reserve Act (1913) and latter on the Mefadden Act (1927) and the medium of holding companies opened the doors for the commercial banks to do universal banking. In United States of America Commercial banks has concentrated largely on term-financing - principally through the form of subscription to equity capital of industries. In the U.S.A. commercial banks had already developed term-loan business in the 1930s; till today it has continued to be an important line of their activities. Similarly, commercial banks in Germany and Japan also ventured into the term-lending activities with the strength of their vast amount of short and long-term deposits. In order to minimise the risk of long-term financing borne by a single bank and to lead the investing public to purchase share of a company it is very common for several banks to come together to form a syndicate in Germany. In Japan also commercial banks may get loan from Bank of Japan against security of long-term investment.

To search for the genesis of universal banking in India before independence, assistances from the contemporary financial machineries like managing agencies, insurance companies etc. were not adequate. The insurance companies which were considered a significant machinery for long-term investment in foreign countries confined their investment activities mainly in government securities. While invest-

in government securities was essential to a certain extent, those concerns could easily cultivate some of our neglected fields of investment like industrial debenture. During the period 1921-36 70 percent workable assets of the insurance companies' in India invested in government port trust and municipal securities. Similarly joint stock banks were also very shy to long-term investment in corporate sector even though time deposits were increasing rapidly. Time deposits which was Rs.386, 08 thousand in 1915 increased to Rs.37, 37, 01 thousand in 1934. Even the small scale industries were facing acute problem for getting working capital loan from the banks given vide evidences before the Indian Industrial Commission. The effect of 'Swadeshi' movement and the World War I gave birth to the nationalist sentiment in the mind of the Indian public. The main object of the 'Swadeshi' movement was to set up Swadeshi enterprises with the help of necessary assistances from the Swadeshi banks. To investigate^{into} the matter of industrial finance, Indian Industrial Commission was set up by the Imperialist government in 1916. Suggestion of the Commission was to establish the industrial bank following the model of German style universal bank. Under such adversities, the domestic entrepreneurs^{came forward to} set up banking institutions on their own with a view to mobilising private deposits for investment in their own concerns.

The universal banks evolved for the first time in pre-independence India particularly at the beginning of the

present century, started with People's Bank in 1901, a chain of such banks were established under the domestic entrepreneurship during ^{the period} 1900-13. Following People's Bank, the pioneer universal banks, which came into existence, were The Bank of Burma, The Indian Specific Bank, The Credit Bank of India, Lahore Bank, The Doaba Bank, The Hindusthan Bank, The ^{Bengal} National Bank, The New People's Bank and The People's Industrial Bank. After the banking crisis of 1913-15 some more universal banks under the title industrial bank came into existence. The lead, given by Tata Industrial Bank in 1917, ^{and} was followed by, among others, The Calcutta Industrial Bank, The Karnani Industrial Bank, The Laksmi Industrial Bank etc. Following ^{the} German model of universal banking, they used to mobilise savings and provide long-term finances. To attract more deposits it was the policy of the banks to pay interest at a rate 2-3 percent higher than the market rate. This explains why these banks used to invest in speculative business.

Unfortunately, almost all the banks had collapsed during the banking crisis of 1913-15. There were a lot of reasons behind this collapse. Deterioration of Cash reserve in relation to deposit was an important cause of bank failure. Among others, financed units were very weak. So that banks were failed along with the liquidation of those ^{weak}/financed units. Mismanagement, investment against worthless security or no

security were also the causes behind bank failure.

The deficiency of capital and entrepreneurship from which indigenous industries were suffering during the pre-independence period became a post-independence phenomena. According to government statistics, ^{the} net amount repatriated from India was Rs. 100.52 billion during the period 1935-45. In these circumstances ~~and the~~ government's eagerness to build up industrial economy of India through a series of five years plan, a chain of DFIs were set up. ~~for~~ But ~~their~~ weak branch network, lack of local contacts and non-availability of sufficient working fund ~~are hampering~~ ^{they} ~~the~~ interest of the industries to get necessary finance in time. On the other hand, commercial banks in India are seeking new avenue with their vast volume of deposits and strong branch network both in rural as well as ^{the} ~~in~~ urban areas. But the problem of liquidity, lack of proper project appraisal machineries, fear of non-recovery of term-loan are creating barriers before the commercial banks to do universal banking, spontaneously although there is ample scope to do so. In these circumstances ~~the~~ IMF mission visited India in 1953 and ~~the~~ Shroff Committee submitted its report in 1954. Both of these two boldly suggested in favour of commercial bank's participation in universal banking. Similarly, section 6 of the Banking Companies Act, 1949 also endorsed the commercial banks to take part in underwriting of corporate shares and

debentures. Purchase of Corporate shares and debentures also have its legal sanction. Considering all these favourable situations commercial banks came forward to take part in universal banking. Industrial term loan which was Rs.282.52 crores in 1972 rose to Rs.7,695.31 crores in 1990. In underwriting activities bank's share was Rs.136.6 lakhs in 1967, it increased to Rs.739.0 lakhs in 1983.

To find out a suitable assessment methodology for our purpose we have reviewed the literature on universal banking. Almost all the studies demonstrate only descriptive analysis to assess viability of universal banking without considering econometric tools and techniques. But a recent study has assessed^{the} performance of universal banking within India's commercial banking set up. This study has shown the strong scale and scope efficiency of universal banking within the commercial banking set up. This study is based on time series data.

The present study, however, seeks to examine the same hypothesis on the basis of cross section field survey data collected from 31 branches of commercial banks in the district of Darjeeling, in West Bengal. This study has estimated four alternative models of conventional and hybrid translog specifications and shows :

- I. that the fixed deposits shared highest proportion in total deposits although the study period. It accounted nearly one-half of the sum during the period 1990-92;
- II. that growth rate of expenditures are 8.62 per cent and 11.40 per cent in 1991 and 1992 respectively, given 34 per cent and 16 per cent growth rate in deposits during the corresponding years. These growth rates in total expenditure indicates lower expenditure per unit of deposit;
- III. that the industrial financing of sample banks reveals a striking balance between the term loans and working capital loan. This may be explained by the backwardness of the region;

Moreover, according to our econometric investigation, this study confirms the 'overall' scale economies and product specific scale economies to the commercial and development banking activities separately. In regard to scope economies this study shows that the existence of cost complementaries among the commercial and development banking activities.

From the above observations, we have drawn the following policy implications :

- (1) To minimise the risk of liquidity in the course of term-lending by the commercial banks, Reserve Bank of India should give advance to the commercial banks against security of term-loan given to the industries like their counterpart in Japan.
- (2) In regard to underwriting and direct participation in corporate shares and debentures commercial banks in India should proceed in co-operation with insurance companies forming a consortium or syndicate. Such a consortium or syndicate participation in corporate shares and debentures is very common among the German universal banks to share risk of liquidity among themselves.
- (3) On the basis of various evaluation criteria, such as efficiency, it is found that India may be benefited more from the adoption of universal banking system, in particular from the exploitation of economies of scale without the inefficiency that often ensues from an increase in the degree of concentration than from adoption of a specialised system.
- (4) To know the overall creditworthiness and paying capacity of a client firm, banks should ask for funds flow statement constructed for a number of years before granting loans.

- (5) Repayment of term-loan will flow in smoothly only if the income of the borrower from the financed units increases as anticipated. So, the commercial banks in India should extend consultative service to the authorities of financed units like their counterpart in Germany.
- (6) There should be a review programme of the progress made in the implementation of the project so that corrective steps, if necessary could be taken well in time. Such a review may be done, in every half year. A review should also be undertaken after the borrowers have committed 75 per cent of the project costs or three months before the scheduled date for completion of the project- whichever is earlier. Such a system would enable the banks to detect the overruns also and to take necessary steps.
- (7) The borrower should provide evidence of insurance on business and on himself sufficient to repay the bank if anything happens to it or him.

Annexure 2.1

Balance-sheet of the People's Banks of Punjab,

30th June, 1910

	Rs.
Liabilities :	
Capital	9, 80, 401.00
Reserve	1, 25, 000.00
Deposits (Fixed, saving and current)	80, 02, 712.00
Security Deposit	59, 599.00
P/F Deposits	31, 066.00
	<hr/>
	91, 98, 778.00
Assets :	
Cash Credit and Loans	75, 39, 672.00
Debentures and Other Investments	4, 18, 625.00
Other Assets	12, 40, 481.00
	<hr/>
	91, 98, 778.00

Source : 'Capital' 1910.

Annexure 2.2

Balance-sheet of the Specie Bank Ltd.

30th June, 1908

	Rs.
Liabilities :	
Capital	74, 57, 400.00
Reserve Call	9, 250.00
Reserve Fund	1, 00, 000.00
Deposits	1, 30, 94, 968.00
Bills for Collection	21, 27, 373.00
Sundries	2, 13, 453.00
Profit & Loss Account	4, 34, 607.00
	<hr/>
	2, 34, 37, 051.00
Assets :	
Credits on Govt. & other Authorised Securities	20, 56, 848.00
Loan on Govt. and other Authorised Securities	1, 19, 84, 332.00
Bills Receivable Discounted	35, 66, 709.00
Overdraft	1, 75, 023.00
Sundries	2, 26, 220.00
Preliminary Charges	12, 607.00
Government Securities	98, 469.00
Bullion	35, 47, 480.00
Cash at Head Office	17, 69, 363.00
	<hr/>
	2, 34, 37, 051.00

Source : 'Capital' 1908.

Annexure 2.3

Balance-sheet of the Specie Bank Ltd.

30th June, 1910.

	Rs.
Liabilities :	
Capital	75, 00, 000.00
Reserve Fund	5, 00, 000.00
Deposits, Bills, Discounted, Acceptance and other sums due by the Bank against Security	3, 39, 27, 283.00
Sundries	3, 66, 756.00
Profit and Loss Account	8, 48, 188.00
	<hr/>
	4, 31, 42, 227.00
Assets :	
Credit on Govt. and Other Authorised	
Security	1, 14, 36, 703.00
Loans on Govt. and Others Authorised Securities	2, 32, 15, 538.00
Bills Receivable Discounted and Purchased	28, 40, 398.00
Overdraft	1, 64, 327.00
Sundries	2, 41, 268.00
Bullion	5, 93, 239.00
Cash	<hr/> 46, 50, 754.00
	4, 31, 42, 227.00

Source : 'Capital' 1910.

Annexures 2.4

Balance-sheet of the Bengal National Bank Ltd.

30th June, 1910

Rs.

Liabilities :

Capital	8, 05, 437.00
Shares Forfeited	13, 376.00
Current, Fixed and Savings Deposit	14, 54, 708.00
	<u>22, 73, 521.00</u>

Assets :

Loans, Cash Credit etc.	
and Overdraft	14, 82, 313.00
Government Securities	
with interest to date	2, 40, 939.00
Other Assets	5, 50, 269.00
	<u>22, 73, 521.00</u>

Source : 'Capital' June, 1910.

Annexure 2.5

Balance-sheet of The Amritsar Bank Ltd.

30th September, 1914.

	Rs.
Liabilities :	
Deposits	25, 58, 804.00
Providend Fund	21, 398.00
Capital	1, 80, 202.00
Unclaimed Dividend	1, 533.00
Surplus	<u>1, 02, 345.00</u>
	<u><u>28, 64, 282.00</u></u>
Assets :	
House Property	2, 875.00
Investment	81, 836.00
(Shares in Lahore Spinning Company)	
Debts due	25, 48, 097.00
Drafts	2, 749.00
Furniture etc.	6, 721.00
Cash and Investment,	<u>2, 22, 004.00</u>
	<u><u>28, 64, 282.00</u></u>

Source : 'Capital' 1915.

Annexure 3.2

Financing of Projects by Companies which Issued Capital
by Prospectus

		1984-85 Rs.crores	Per cent to total cost			
			1984-85	1983-84	1982-83	1981-82
1	2	3	4	5	6	7
1.	Reserves & Surplus	56	6.0	2.8	10.5	5.5
2.	Capital Market					
	(a) Share capital	330	35.7	38.6	24.7	18.9
	(b) Debentures	73	7.9	4.3	21.9	15.2
	Total	403	43.6	42.9	46.6	34.1
3.	Borrowings					
	(a) Financial Institutions	229	24.7	34.7	24.5	29.5
	(b) Banks	52	5.6	5.0	7.8	10.3
	(c) UTI/LIC/GIC	52	5.6	2.1	2.2	2.5
	(d) State Govts/ FI	16	1.7	4.1	2.8	2.6
	(e) Others	95	10.3	6.0	4.1	6.0
	Total	445	48.0	51.9	41.4	59.9
4.	Others	22	2.4	2.4	1.5	0.5
	Total	926	100.0	100.0	100.0	100.0

Source : Company News and Notes, Vol.XXIV, No.3, Sept., 1986.

Financing of Project Cost During 1966-1982.

(Rs. in billion)

Year	Development Finance				Institutions		Com. Banks	Invest. Inst.	Stock Market			Promoters Contra.	Others	Grand Total
	IDBI	IFCI	ICICI	SFCs/SIDCs	Total				Shares	Deb.	Total			
1966	1.70 (11.5)	1.21 (8.2)	0.44 (3.0)	0.48 (3.2)	3.83 (25.9)	NR (1.4)	0.21 (25.3)	3.76 (5.2)	0.77 (30.5)	4.53 (30.5)	NR (30.5)	6.27 (42.2)	14.84 (100)	
1967	0.59 (4.4)	0.57 (4.4)	0.62 (4.7)	0.07 (0.6)	1.85 (14.1)	NR (4.5)	0.59 (30.0)	4.00 (2.8)	0.37 (32.8)	4.37 (32.8)	NR (32.8)	13.56 (48.6)	20.37 (100)	
1968	0.29 (2.7)	0.38 (3.6)	0.48 (4.5)	0.18 (1.7)	13.3 (12.5)	1.35 (12.6)	0.07 (0.7)	2.48 (23.1)	1.35 (22.6)	3.83 (15.7)	NR (15.7)	6.68 (38.5)	13.26 (100)	
1969	0.49 (4.1)	0.28 (2.7)	0.55 (4.5)	0.20 (1.7)	1.52 (13.0)	1.31 (11.0)	0.14 (±.2)	2.84 (23.6)	3.36 (27.7)	6.20 (51.3)	NR (51.3)	4.54 (23.5)	13.71 (100)	
1970	0.19 (1.4)	0.28 (1.9)	0.70 (4.9)	0.22 (1.5)	1.39 (9.7)	1.63 (11.3)	0.05 (0.03)	4.80 (32.2)	0.49 (3.4)	5.29 (35.6)	NR (35.6)	6.41 (43.3)	14.77 (100)	
1971	2.18 (13.1)	0.96 (5.8)	1.16 (7.0)	0.40 (2.4)	4.70 (28.3)	3.18 (19.2)	0.82 (4.9)	5.15 (31.1)	0.26 (1.6)	5.45 (32.7)	NR (32.7)	2.45 (14.9)	16.60 (100)	
1972	1.85 (6.6)	1.20 (4.4)	1.78 (6.4)	0.38 (1.4)	5.21 (18.8)	5.82 (20.8)	0.86 (2.7)	5.36 (19.2)	1.92 (7.0)	7.28 (26.2)	NR (26.2)	8.79 (32.0)	37.96 (100)	
1973	1.92 (8.8)	0.85 (3.9)	1.27 (5.8)	2.42 (11.0)	6.46 (29.5)	4.24 (19.2)	0.43 (2.0)	8.05 (36.4)	0.76 (3.5)	8.81 (39.9)	0.10 (0.5)	1.99 (8.9)	27.03 (100)	
1974	0.99 (9.9)	0.52 (5.2)	0.73 (7.3)	0.57 (5.7)	2.81 (28.1)	2.50 (25.0)	0.15 (1.5)	3.06 (30.6)	0.45 (4.5)	3.51 (35.1)	0.04 (0.4)	1.01 (9.9)	10.02 (100)	
1975	3.52 (13.7)	1.40 (5.4)	1.94 (7.5)	0.99 (3.8)	7.85 (30.4)	4.61 (17.9)	1.45 (5.6)	8.83 (34.3)	0.02 (0.1)	8.85 (34.4)	0.30 (1.2)	27.10 (10.5)	50.16 (100)	
1976	1.32 (8.5)	0.74 (4.7)	1.05 (6.7)	0.89 (5.7)	4.00 (25.6)	2.48 (15.9)	0.69 (4.5)	4.37 (28.1)	0.02 (0.1)	4.39 (28.2)	0.38 (2.4)	3.63 (23.4)	15.57 (100)	
1977	4.52 (13.7)	2.01 (6.1)	2.50 (7.6)	1.37 (4.1)	10.40 (31.5)	5.94 (18.0)	1.57 (6.5)	8.73 (24.5)	0.22 (0.7)	8.95 (25.2)	0.14 (0.4)	5.98 (18.4)	32.98 (100)	
1978	3.46 (14.8)	3.39 (14.6)	1.55 (6.7)	2.22 (9.5)	10.62 (45.6)	1.63 (7.0)	1.20 (5.2)	6.96 (29.9)	0.20 (0.9)	7.16 (30.8)	0.23 (1.0)	2.47 (10.4)	23.31 (100)	
1979	2.71 (11.7)	1.54 (6.6)	2.07 (8.9)	1.77 (7.6)	8.09 (34.8)	2.44 (10.5)	1.31 (5.6)	9.70 (41.7)	0.71 (3.1)	10.41 (44.8)	0.06 (0.2)	9.54 (4.1)	31.85 (100)	
1980	4.24 (10.8)	2.11 (5.4)	2.20 (5.6)	1.76 (4.5)	10.31 (26.3)	1.34 (3.4)	1.17 (2.9)	7.40 (18.8)	6.38 (16.2)	13.78 (35.0)	0.13 (0.3)	126.41 (32.1)	153.14 (100)	
1981	30.28 (20.8)	6.11 (1.2)	6.58 (4.5)	3.84 (2.6)	46.81 (32.1)	28.14 (19.3)	4.40 (3.2)	27.40 (18.9)	22.16 (15.2)	49.56 (34.1)	1.78 (1.2)	15.02 (10.1)	145.71 (100)	
1982	9.86 (11.8)	4.81 (5.7)	5.83 (7.0)	2.36 (2.8)	22.86 (27.3)	6.52 (7.8)	2.03 (2.3)	20.65 (24.7)	18.29 (21.9)	38.94 (46.6)	0.20 (0.2)	132.37 (15.8)	202.92 (100)	

Notes : (i) Figures in brackets represent percentages to total.

(ii) NR - Not reported.

Source: Annual Reports of the Working and Administration of the Companies Act, 1956 (Various issues).

**RESEARCH SURVEY
ON
TERM FINANCING BY COMMERCIAL BANK IN SILIGURI REGION**

(No identity of respondents will be disclosed in the presentation and/or interpretation of data to be supplied).

(Please use / whenever applicable)

A. Operation Statistics :

- | | | | |
|---|---------------|-----------------------------|------|
| 1. What was the levels of deposit ? | (Rs. in lacs) | | |
| | 1990 | 1991 | 1992 |
| i) Fixed - | | | |
| ii) Saving - | | | |
| iii) Current- | | | |
| 2. What are the numbers of account ? | 1990 | 1991 | 1992 |
| i) Fixed deposit | | | |
| ii) Saving deposit | | | |
| iii) Current account | | | |
| 3. What are your annual operating expenditures ? | (in Rs.) | | |
| | 1990 | 1991 | 1992 |
| i) Rent & Rates - | | | |
| ii) Electricity - | | | |
| iii) Stationary - | | | |
| iv) Interest paid- | | | |
| 4. Please furnish the following information regarding employment at present : | <u>Number</u> | <u>Wages & salaries</u> | |
| | | (per month) | |
| i) Managerial - | | | |
| ii) Technical - | | | |
| iii) Non-technical- | | | |

B. Loans :

1. Have you provided term-loans (i.e. investment in fixed assets) during the last three years : Yes/No.
2. If yes please furnish the following information :

Year	Amount of term loan (Rs. in lacs)	No. of beneficiaries (only industry)
1990		
1991		
1992		

3. What is the industry-wise break-up of the amount of term loans ?

Industry	1990	1991	1992	(Rs. in lacs)
Engineering				
Chemical				
Electronics				
Food Products				
Servicing				
Others				

4. To how many entrepreneurs you have provided only term loan and both term loan and working Capital loan ?

Contd...

Year	Term loan	Term loan & working Capital loan
1990		
1991		
1992		

5. How many among your beneficiaries are first-generation entreprenurer ?

Year	1st generation entrepreneurs	Established entrepreneurs
1990		
1991		
1992		

6. Do you state the number of beneficiaries of your working capital loans during the last five years (1988-93) in industries where you assisted term loans in 1992 ?

Engineering
 Chemical
 Electronics
 Food Products
 Servicing
 Others

.....

Contd...

7. What was the scheduled amount of repayment and actual amount of realization of industrial term loans :

(Rs. in lacs)

Year	Scheduled	Actual
1990		
1991		
1992		

8. What sorts of supervision you follow to ensure proper utilisation of term loans :

9. What sort of mortgage you ask for term loans ?

- 1.
 - 2.
 - 3.
 - 4.
-

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