

UNIVERSAL BANKING : AN INTERNATIONAL PERSPECTIVEPart I : INTRODUCTION

The banking system was first developed in its modern form<sup>1</sup> 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.<sup>1A</sup> 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, differences of opinion behind the evolution of banking system in this direction.<sup>2</sup> 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.<sup>3</sup> 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<sup>has</sup> 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<sup>have</sup> 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.<sup>4</sup> 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.<sup>5</sup> No outside agency was required to supply either long-term capital or entrepreneurship because the entrepreneur himself was the source of both.<sup>6</sup> 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 <sup>who</sup> 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.<sup>6A</sup> 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 :<sup>7</sup>

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

ii) <sup>In</sup> Backward countries industrialization stresses on bigness of both plant and enterprise in comparison to the advanced countries where industrialization started ~~more~~ earlier than the backward countries . Thus it requires to make large investment programme for industrialization in backward countries to purchase machinery of improved technology <sup>in order</sup> 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 countries 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 <sup>the</sup> 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 <sup>the</sup> 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 <sup>the</sup> cases 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.<sup>8</sup> 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, <sup>the French</sup> ~~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.<sup>9</sup> 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.<sup>10</sup>

But it was the <sup>construction of</sup> rail-roads, 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.<sup>11</sup> 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 tons<sup>12</sup> 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 rise in population. In 1871 the total population strength in Germany was 41 millions which rose to 68 millions in 1915.<sup>13</sup> The rapid growth in population also helped in getting the expanded market for industrial goods in Germany.

Germany as an area <sup>which is</sup> 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 Gerschenkron<sup>14</sup> ;

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
1881-1913	-	3.8

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.<sup>15</sup> 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%).<sup>16</sup>

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.<sup>17</sup> 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

Sub-period before 1914	Annual growth rate
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. <sup>17A</sup> Through land reform, <sup>the</sup> government allowed the peasants to hold less area of land than had been assigned to them before the reform. <sup>It</sup> was a positive step in the field of industrialization. The inadequacy of land holding compelled them to sale their land like their counterpart in the west and use 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, <sup>the</sup> 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, <sup>the</sup> share of U.S.A. was lower than <sup>that of</sup> U.K. But U.S.A.'s share was well ahead of Germany's 13.2%.<sup>18</sup> 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 areas<sup>19</sup> 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.<sup>19A</sup> So, it was <sup>a</sup>parallel to <sup>the</sup>German style of universal banking system. Considering this point <sup>the</sup>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<sup>it</sup> 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 (~~1918~~) lowered the required reserves on time deposits than on demand deposits. The effect was to give banks a strong incentive<sup>s</sup> to raise the ratio of time deposits over demand deposits.<sup>20</sup> 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.<sup>21</sup> In the absence of availability of experienced persons those who were familiar with western method,<sup>the</sup> 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.<sup>22</sup> Foreign food and foreign machinery were also imported by the government and distributed among the prefectural 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 <sup>the</sup> government of Japan had keen interest in foreign trade. It purchased raw materials <sup>from</sup> in domestic market to sell them abroad and used that sale proceeds to finance the imports. During the sixties of the 19th century <sup>the</sup> postal and telegraph system was introduced and steamship and railways were built up and these were financed by the Japanese government <sup>by</sup> 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 <sup>the</sup> government of Japan was bound to take financial assistance from Mitsui and other merchants who were <sup>the</sup> government's chief supporters. In 1868 <sup>the</sup> government's expenditure was 25 million yen while <sup>the</sup> government's revenue from ordinary sources was not more than 3.7 million yen.<sup>23</sup>

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.<sup>24</sup>

### 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.<sup>25</sup> On the other hand, credit Banks (universal bank) were free from banking regulation which helped them to take general and elastic programme.<sup>26</sup> 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 <sup>the</sup> 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.<sup>27</sup> Similarly, section 2 of the statute of the Duetch Bank (1870) stated, "the purpose of the bank is to carry on banking transactions of every description...."<sup>28</sup>

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.<sup>29</sup> According to this Act, one single firm was allowed to get credit from a bank a maximum <sup>of</sup> 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.<sup>30</sup> 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.<sup>31</sup> 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.<sup>32</sup> On account of the vigorous objection from the industrialists the government of Japan was compelled to withdraw this restriction in 1895.<sup>33</sup> 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.<sup>34</sup> 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."<sup>35</sup> In these circumstances it was felt <sup>important</sup> to reorganise <sup>the</sup> banking regulation. Thus a new banking law was introduced in 1928 to replace the outdated and clearly inadequate 1890 ordinance. <sup>Some of the</sup> 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

reserve.<sup>36</sup> The new banking regulation did not claim any revolutionary change in <sup>the</sup> 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.<sup>37</sup> 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.<sup>38</sup>

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. <sup>38A</sup> According to this Act the banks were allowed to provide <sup>a</sup> <sup>as</sup> loan <sup>of</sup> maximum 25 per cent of their capital and surplus against <sup>the</sup> 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 lands 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 <sup>of the</sup> estimated value

of land kept as security and term of loan must not run for the period <sup>of</sup> more than 5 years.<sup>39</sup> 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.<sup>40</sup> ~~The~~ Banking crisis <sup>of</sup> 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."<sup>41</sup>

Banking Amendment Act (1935) again liberalised the real estate loan. According to this Act, <sup>in</sup> 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 ten 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.<sup>42</sup>

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 ~~were~~ <sup>had</sup> 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 banks<sup>40</sup> or in some countries channelling the public savings to promote industries as a trustworthy organisation the universal bank came into existence.<sup>41</sup>

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. <sup>We find</sup> 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 <sup>and</sup> 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 <sup>the</sup> share of time and saving deposits was more than 50% but after the war particularly in 1947 it fell <sup>down</sup> 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 fund<sup>45</sup> 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 <sup>the</sup> public sentiment was effective behind the rapid increase in deposits with the banks in Japan. On account of underdeveloped capital market in Japan in Meije period, the public clearly preferred to keep their money in the relatively secured financial institutions especially banks.<sup>46</sup>

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. <sup>also</sup> 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 <sup>in</sup> 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	3,633	6839
1930(Sept.)	13,542	7489
% increase	33%	127%

Source : Phillips, C.A., Aernanus, 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 <sup>in</sup> time deposits four times than of demand deposits. Similarly, the growth rate <sup>in</sup> time deposits was faster than that of the demand deposits.

The Comparative growth <sup>in</sup> time deposits in the reporting member banks <sup>in</sup> 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, <sup>in U.S.A.</sup> 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 Schaaffhausenscher 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 Creditbank. 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.<sup>47</sup> 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.<sup>48</sup> 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.<sup>49</sup> By this means they sought to strengthen their connection with the undertakings and to gain more influence on their policy and more insight into its execution.<sup>49A</sup> 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<sup>or</sup> when the banks realised to maintain price of shares, they used to buy own issues.<sup>498</sup> 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."<sup>50</sup> 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 trend<sup>in</sup> 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 gesells chaft	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 and 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.<sup>51</sup>

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 Ronro Comerong, 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 <sup>financial</sup> 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 Meije 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.<sup>52</sup> 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	M i t s u i			M i t s u b i s h i			Yasuda
	S/A	I/A	I/S	S/A	I/A	I/S	S/A
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	0.29	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. Cameron 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 <sup>the</sup> 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.<sup>53</sup> 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 <sup>the</sup> exchange banks ordinary banks also entered into the stock market on a very large scale.<sup>53A</sup> 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. Metsubishi	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, <sup>that</sup> 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 <sup>this trend</sup> 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.<sup>54</sup> The booming security market led most of the commercial banks to form security affiliates.<sup>55</sup>

They engaged in security underwriting, holding of securities for control purposes and various other activities.<sup>56</sup> By 1929 commercial banks and their security affiliates had equalled private investment banks in terms of volume of securities underwritten.<sup>57</sup> During the period 1921-28 Commercial banks investment in Corporate shares increased from 14%<sup>to 19% of the</sup> 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 \$11,277 million in 1921 increased to \$22,897<sup>million</sup> 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 <sup>the</sup> non-financial corporations which caused a long slide of gross national product from \$ 103 billion in 1921 to \$ 55 billion in 1929.<sup>58</sup> 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.<sup>59</sup> 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.<sup>60</sup>

## 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 notwithstanding 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."<sup>61</sup> 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, <sup>a</sup> moderate rate of return was noticed till 1960. This was the cause of prohibition imposed on the universal banking after <sup>the</sup> depression by banking Act of 1933 and <sup>the</sup> permission <sup>given</sup> 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, and Additions to Reserves	Net Credits(+) or Debits (-)
1935	\$ 432.5	\$ 628.1	\$ - 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<sup>out</sup> of the ten years<sup>Period</sup> 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 decreases. Similarly, security holdings are sold when demand for loans increase. 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<sup>earned</sup> 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 <sup>the</sup> 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 (1+2+3)	Profit % 5 of 4
	1	2	3		
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 6.8
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 <sup>the</sup> 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 <sup>of</sup> only 8%.

In Germany we <sup>also</sup> find a noticeable change <sup>in</sup> 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 Bankverein	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
Mitteldeutsche credit bank	30.0	33.3	35.0	39.0	39.6	39.5	33.6	36.6
Average	30.0	33.3	34.0	34.5	36.5	37.5	36.3	37.1

Source : Whale, 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.<sup>62</sup>

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
Discontogese -llschaft	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 Handelsgese llschaft	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 <sup>to</sup> 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.

## 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 <sup>in</sup> 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.

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