CHAPTER I

INTRODUCTORY
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Nationalisation of the fourteen major commercial banks in July 1969 consolidated social control of the banking system. It was a step towards keeping control over the "commanding heights of the economy". The following decade has witnessed a change in the Anglo-Saxon tradition of banking, a change in the structure, approach, emphasis and style of functioning of the major components of the banking structure in India. There has been a geographical and functional diversification of the banking system for meeting the credit needs of the priority sectors and generating growth in the poor socio-economic classes.

Nationalisation was not, however, entirely a novel experiment, although it looked so due to its revolutionary thrust and potentials for terminating strangle-hold of poverty. The Imperial Bank was nationalised, twenty years before, on the recommendation of the Rural Credit Enquiry Committee and renamed the State Bank of India. The State Bank of India Act, 1955, specified three distinct objectives of acquisition: (a) to take over cash work from non-banking treasuries and sub-treasuries, (b) to provide vastly extended remittance facilities for co-operative and other banks and (c) to provide the credit requirements of co-operative marketing and processing societies and small-scale industries.

1. Prime Minister, Indira Gandhi's broadcast address to the nation on 19th July, 1969.
The State Bank of India came into existence to discharge these responsibilities and with a quarter of total deposits, supplemented the operations of the Reserve Bank of India in providing credit facilities to rural institutions and small scale industries etc. In short, it became a lender of immediate resort.

The nationalisation of the fourteen major commercial banks was also undertaken to imbue these institutions with a social purpose. This was sought to be achieved by consolidating social control so as to remove concentration of banking ownership, provide adequate credit for agriculture, small industry and exports and encourage growth of new classes of entrepreneurs.

The State Bank of India, which had already one foot in agriculture through its connection with co-operative movement, opened the gateway to the rural households. By taking a lead in reaching out to the rural poor and urban slum dwellers, it has become the torch bearer of a new banking culture in the country.

The Lead Bank Scheme introduced by the Reserve Bank of India in December 1969, soon after nationalization, is a landmark in the history of India's banking development. It marks evolution of 'area approach' to the preparation of plan programme and development of banking and credit structure. In the first phase, the scheme aimed at identifying potential
potential centres for bank operations and opening of bank branches there. The spurt in bank offices and the rural branches within five years of time show that considerable success has been achieved with respect to this objective. The second phase began in 1974 with the objective of preparing District Credit Plans with bankable Schemes for specific area development. Credit Plans were prepared for 375 districts before the end of the year 1978. It is also a remarkable achievement because formulation of a regional plan requires survey of physical endowments, socio-economic characteristics, input-output linkages and credit needs and projecting the credit gap to be met by the banking and co-operative institutions in the plan period.

Two Study Groups of Reserve Bank reviewed the working of the Lead Bank Scheme in Maharashtra and Gujrat in 1975. The combined Report of the two States stressed the importance of collective action by the banks and other agencies for district development and expediting preparation and implementation of technologically feasible and economically viable schemes.

The first District Credit Plan was launched in 1976. Credit Plan is an apparatus of collective action with the Lead Bank acting as the trend setter to mobilise surplus and channelise credit to the priority sectors, notably for integrated rural development.
It was also in the same year that the Government of India established Regional Rural Banks to provide a sound rural base to the banking structure. A step from rural branches to rural banks marks a further commitment of the public authorities to rural development.

Thus there are now three categories of public-sector banks: (a) The State Bank of India with its subsidiaries; (b) the nationalised banks and (c) regional rural banks. These commercial banks along with private sector and co-operative banks constitute the organised banking structure of the Indian economy.

Bank Nationalisation, Lead Bank Scheme and Credit Plan have sought to free the major segment of the banking structure from the age-old allignment with the trade and commerce, their urban nexus and metropolitan base and a dominant profit motive by forcing them to evolve a social purpose, a long-run perspective and to reorient their activities towards weaker sectors of the economy. The sectoral and spatial redistribution of credit is a temporal phenomenon of the seventies. Attempt is made to formulate specific banking schemes for the backward classes and establish Special Development Agencies like Command Area Development Authority (CADA) and District Rural Development Agency (DRDA) for providing subsidy and technology to the rural target groups. These steps are being taken to foster growth in them and thus minimise vertical disparity. The formulation of anti-poverty
policy schemes like Antyodaya or ERDF (Economic Rehabilitation of the Rural Poor) by different State Governments and DIR (Differential Interest) Scheme by Reserve Bank of India also aim at neutralising interpersonal inequalities in line with the national plan strategy of growth with redistribution.

These attempts notwithstanding, the nationalised banks have come under serious criticisms. It has been pointed out that performance of these financial institutions has lagged behind the national policy objectives. More specifically, I.J.N. Seshadri has shown that public-sector banks do not measure up to the private-sector commercial banks in terms of commercial profitability, capital adequacy and operational efficiency. It has also been observed that pattern of distribution of benefits of public facilities like irrigation and banking service has been regressive in character. The large and middle class farmers are alleged to have been the principal beneficiaries of bank nationalisation because of their easy access to these institutions. It is for these reasons that we make a case study to find out the impact of commercial bank finance on rural development.

1.1 Literature Survey

Among the earlier research works, the studies conducted by Reserve Bank of India viz. All India Rural Credit

2. I.J.N. Seshadri (Economic Research Division, Birla Institute of Scientific Research), Banks Since Nationalisation, Allied, New Delhi, pp. 40-51, 1961
Survey\(^3\) (1951-52), Rural Credit Follow-up Survey (Annual) Reports\(^4\) from 1956 to 1959 and its evaluation by Dantwala\(^5\) are important contributions to the assessment of the extent of indebtedness of rural cultivating and non-cultivating households, the credit gap in agriculture and the need for enhancing institutional credit in this sector. These studies revealed the dominant position enjoyed by the moneylender in the rural credit market.

Imperfect knowledge of and lack of ability to contact existing institutional source of credit are in Srinivasan's views\(^6\) (1954) the main reasons behind the communication gap between banks and rural households.

The role of commercial banks and other financial institutions in meeting rural credit needs was further examined by the All India Rural Debt and Investment Survey\(^7\) (1961-62) by estimating asset-groupwise loans per rural household (also per cultivating and non-cultivating household). Issues relating to development of adequate market structure to support the farm credit framework, modus operandi of extending loan to agriculture, innovations in financial operation and

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3. All India Rural Credit Survey Report, Reserve Bank of India, Bombay, 1954.
4. Rural Credit Follow-up Survey (Annual) Reports 1956-1959, Reserve Bank of India, Bombay.
ways of increasing institutional credit to agriculture were discussed in an important Seminar organised by Reserve Bank in December 1969.6

The formulation of area approach9 to the problem of rural credit (1969) and institution of Lead Bank Scheme10 (1969) as an apparatus of area planning have deepened social commitment of the banks and co-operative institutions in India to rural reconstruction. The Banking Commission Report (1972) has probed deep into the problem of co-ordination between commercial and co-operative banks on three aspects viz. (a) geographical coverage, (b) loan policies and procedure and (c) resources and organisational aspects.11

There has been academic contribution in the field of capital formation in agriculture related to institutional credit. C.H. Shah and Tara Shukla12 (1956, 1971) have analysed the


need for increasing and stabilising the value of farmer's margin of production over subsistence requirements of his family so that he may invest still more in production and thus add to the value of the assets which he can present against a loan from the institutional source and employ it for productive purposes. Samuel Paul (1970) has measured investment surplus in agriculture through cost-benefit analysis of farm credit items like tractors, deep and shallow tube wells etc.

Capital formation and productivity of agriculture are closely linked with the repayment issue. Dandekar (1956) has pointed out the methods of social coercion and monopoly power exercised by the village money-lender visavis the rural borrowers which ensured repayment. Jakhade and Gadgil (1970) have examined production and repayment capacity oriented lending for farm investment.

Economists have attempted to construct econometric models of banking in India. G.S. Gupta's prototype model (1972) has two simultaneous equations covering demand for and


supply of credit. Khusro and Sidharthan\(^1\) (1972) improved upon it by incorporating deposit aspect into the picture.

Overseas scholars, Dalisay\(^2\) (1964), Wise\(^3\) (1964), Chavoenvirhia\(^4\) (1965), Oluwasanami\(^5\) (1965) and Nisbet\(^6\) (1967) have worked on structure of rural credit and agricultural credit needs in relation to economic development in Philippines, Georgia (U.S.A), Thailand, Nigeria and Chile respectively.

Three studies deal with inter-regional variations in the growth of banking in India. Donald Hester\(^7\) (1964) was perhaps the first economist who made an empirical study of operation of Indian banks touching the regional dimensions.


\(^{19}\) J.O. Wise, "Commercial Bank Loans to Georgia Farmers", College of Agriculture, University of Georgia, U.S.A. 1964.


The second study is by Reserve Bank of India (1969) which constructed and applied composite index of the degree of development of agriculture to 300 districts for arriving at conclusions about gaps in banking facilities. Subhas K. Basu (1979) has meticulously analysed the determinants of inter-district disparity in outstanding agricultural credit and deposits made out of savings from already increased productivity in agriculture.

1.2 This Study

This Study seeks to make a micro level, in-depth analysis of commercial banks' finances for rural development of Sambalpur district. While the previous empirical exercises rest their core findings on inter-district variations on secondary (official) sources, this study proposes to touch the grass root level by conducting a Sample Survey and seeks to do so for exploring the more ticklish problem of intra-regional disparity in bank finances within Sambalpur district which is a planning and administrative region.

The Commercial banks and co-operative institutions finance rural development through District Credit Plan. Yet


a careful scanning of the literature does not yield evidence of any worthwhile work having been done in this field. The present study makes a modest attempt to fill this gap by exploring this new field of regional credit planning.

This study seeks to empirically analyse productivity aspect of rural credit disbursed by commercial banks which previous studies did not touch upon. Basu deals with productivity variables like percent of irrigated area and intensity of cultivation which have a bearing on productivity. But like others, he operates with secondary data and as such is constrained to examine the linkages between bank credit and rural productivity.

Another novel feature of this study is to formulate a simple methodology for estimating crop loan needs of the district by regressing crop loan on household income which can be projected the rural population. It also examines the degree of dependence of other types of agricultural loan on household income.

It also re-examines the distribution aspect of bank finances by attempting an income class classification of the rural loanees and regressing bank credit on the land size as well as on the land concentration ratio separately.
1.3 Objectives

This study has the following objectives:

1. To find out the level and pattern of rural finance, both deposit mobilisation and loan operations, by the commercial banks, particularly the nationalised institutions, operating in the Sambalpur district during Credit Plan period.

2. To study the inter-regional variation of rural financing in the region.

3. To examine productivity, viability and overdues aspects of rural credit disbursed by commercial banks.

4. To determine the pattern of distribution of bank credit among different income groups of the region.

1.4 Hypotheses

The study seeks to establish the following hypotheses for empirical testing:

Hypothesis 1. Rural Credit extended by commercial banks operating in Sambalpur district has significant bearing on productivity in both the sub-regions.

Hypothesis 2. Crop Loan is not linearly dependent upon
(I) size of irrigated land under cultivation.
and
(II) the level of initial household income in R1 or R2.
Hypothesis 3. Inter-regional variation in the levels of Bullock loan is satisfactorily explained in linear form by variation in the levels of household income.

Hypothesis 4. There is significant co-relation between the quantum of loan under (i) Cow (ii) goat and (iii) dug-well schemes and the income status of the loanee.

Hypothesis 5. Bank credit to scheduled caste and scheduled tribe, the weaker sections of the community is not productively utilised in the rural areas of Sambalpur district.

Hypothesis 6. Large farm houses are the significant beneficiaries of the Credit flow to the agricultural sector.

1.5 Methodology

In Economics, there are three established procedures of study namely, theoretical, historical and empirical methods. An attempt is made to apply these methods to study the role of commercial banks in financing rural development of Sambalpur district. Economic behaviour is conditioned not only by economic factors but also by the socio-cultural and political environment in which the man lives. This Study proposes to use a wider canvas and is therefore inter-disciplinary in nature.

This Study proposes to undertake a sample survey of the rural households of Sambalpur district to elicit primary level information about the role of commercial banks in
financing rural development. It seeks to adopt Stratified Three-Stage Random Sampling Procedure to identify six sample villages (three from irrigated and three from non-irrigated sub-regions) and then proceed to interview twenty respondents from each village. Primary data, so generated, may enable us to record some findings and test relevant hypotheses. The detailed sample procedure and findings are given in Chapter 5 while Chapter 6 is devoted to hypothesis testing.

1.6 Chapters

The first chapter is an Introductory to the rest of the Chapters and contains literature survey, objectives and methodology of study. Chapter 2 is entitled Role of Commercial Banks in Rural Development. It is divided into three sections theory, history and policy. 2.1 is devoted to theoretical conceptualisation of the role of commercial banks in ushering in rural change; 2.2 discusses history of commercial banking in the developed and developing countries and the last section 2.3 describes changing landscape of banking policy in India. Chapter 3 traces Economic Profile of the Region after touching briefly history, culture and geographical setting of Sambalpur district which throws light on the pattern of economic life and the environment. Since banking credit has begun to flow to rural areas and other priority sectors through District Credit Plan, Chapter 4 focusses on Commercial Bank Finances for Rural Development through Credit Plan. It discusses the
methodology of plan formulation, estimation of rural credit needs, fixation of targets and constraints of plan fulfilment. A Sample Survey is conducted in the rural areas of Sambalpur district to study the extent and pattern of commercial bank finances, estimate correlation between household income and credit needs, elicit information about productivity and viability of rural credit to formulate and test relevant hypotheses. Methodology of the survey and findings are incorporated in Chapter 5. The title of this Chapter is Sample Survey I - Methodology and Findings. Chapter 6 is captioned Sample Survey II - Testing of Hypotheses. Comparing between theoretical postulations about the role of commercial banks in bringing about all-round, integrated rural development of a region and the actual performance of the banks in Sambalpur district available from official records and monitored through on-field assessment, some conclusions are reached and suggestions offered in Chapter 7 entitled Conclusion.