CHAPTER - I:

HISTORICAL REVIEW OF THE BANKING POLICIES, PRACTICES AND APPROACHES TO THE SMALL INDUSTRIAL SECTOR

This Chapter takes a historical review of the changes in the banking policies, practices and priorities before and after nationalisation of commercial banks with reference to the financial assistance extended to the Small Entrepreneurs owning Small Scale Industries.

Small scale industrial units play an important role in the economic development of a Country, whether it is an advanced country like the U.S.A., Britain or Japan or a developing country like India.

Small scale industrial units have occupied a significant place in the economy of India, the reason being that these Small Scale Industrial units generate employment for millions of people and can be set up in the rural and semi urban areas for mobilising the local resources and removing the regional imbalances. They also help increase the wealth of the poor people, thus increasing their standard of living.

Even before nationalisation of the 14 major commercial banks small scale sector's growth was remarkable. In 1965-66, the small scale sector accounted for Rs.1349 crores of the national income as against Rs.1207 crores of the large industries. In
terms of employment provided, the role of small scale sector was even more impressive, employing as it did 5.7 million out of a total of 8.9 million industrial workers (excluding the household sector)\(^1\).

In the United States also there are approximately 5.5 million businesses which compose the so called "visible" population - those with either paid employees or an established place of operation. In addition to these there are some 3 million businesses which operate as part-time activities from non-business locations or have no paid employees. Approximately 95\% of the 5.5 million "visible" businesses are considered small by the United States Small Business Administration. These businesses employ about 40\% of the civilian labour force. Of all businesses, 66\% have annual gross sales of less than $1,00,000 and 71\% employ fewer than 10 people. Thus we can see that small businesses make up an important segment of the American business complex.\(^2\)

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After the nationalisation of the 14 major commercial banks in India, there was tremendous progress in financing the small scale sector as it was treated as a priority sector and special attention was given by the Government in its Five Year Plans to develop the small scale industrial sector by all means. The progress made by the public sector banks in extending credit to the small scale industrial sector can be seen from the figures given below.  

<table>
<thead>
<tr>
<th>No. of small scale industrial units</th>
<th>Amount Outstanding</th>
<th>December 1979</th>
</tr>
</thead>
<tbody>
<tr>
<td>50850</td>
<td>251.07</td>
<td>655609</td>
</tr>
<tr>
<td></td>
<td></td>
<td>2322.54</td>
</tr>
</tbody>
</table>

It is estimated that more than 40% of the total industrial output is contributed by the small scale sector. Therefore the small scale sector should be encouraged under the self-employment scheme, tiny sector and the small industries proper. For this they should be provided liberal finance, technical training, raw materials and infrastructural facilities including marketing of products. A study made of Punjab reveals Rs.1 lakh of investment in fixed assets provides employment to 15 workers in the small scale sector as against 3 workers

in the large scale sector. Therefore, it is better to encourage the establishment of small scale industries which are employment intensive.

PROBLEMS OF SMALL SCALE INDUSTRIAL UNITS:

The small entrepreneurs have to face many problems in running their small scale units. The problems which are generally faced are:

1. Lack of adequate supplies of raw materials.
2. Lack of trained labour.
3. Lack of finance.
4. Lack of technical knowledge.
5. Lack of marketing facilities.

The problems faced by the small entrepreneurs are more or less the same even in the foreign countries. A study of small entrepreneurs and entrepreneurial development programmes in Malaysia revealed the following operational problems of small enterprises.

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OPERATIONAL PROBLEMS OF SMALL ENTERPRISES:

<table>
<thead>
<tr>
<th>Problem</th>
<th>No. of firms</th>
<th>Percentage</th>
</tr>
</thead>
<tbody>
<tr>
<td>Capital</td>
<td>64</td>
<td>28.1</td>
</tr>
<tr>
<td>Land/Building</td>
<td>56</td>
<td>24.7</td>
</tr>
<tr>
<td>Labour</td>
<td>40</td>
<td>17.6</td>
</tr>
<tr>
<td>Marketing</td>
<td>15</td>
<td>6.6</td>
</tr>
<tr>
<td>Competition</td>
<td>13</td>
<td>5.7</td>
</tr>
<tr>
<td>Other</td>
<td>39</td>
<td>17.2</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>227</strong></td>
<td><strong>100.0</strong></td>
</tr>
</tbody>
</table>

The study revealed that 95% of the small scale units had one problem or the other.5

The Banker's Attitude: -

The banker is expected to act according to the changing circumstances and help to solve the various problems of the small entrepreneurs, not only the financial but also in the other areas which are connected.

with the business, i.e. production, marketing, accounting etc. In short, the banker is required to adapt himself according to the changing circumstances. Banker should develop appropriate attitudes with a view to functioning as leaders of the community.

Irving Pfeffer states the five most common problems with small business loans. They are:

(i) insufficient equity
(ii) quality and depth of management
(iii) poor historical earnings record
(iv) time and expense involved
(v) high mortality rate of small businesses

HISTORY OF INDIAN BANKING

In India banking was known from ancient times. But it was developed after the East India Company came to India and started business which required banking facilities. Thereafter the three Presidency Banks were estab-


blished under the Charter of the East India Company, one each in Bombay, Bengal and Madras. In 1920, these three Presidency Banks were amalgamated and the Imperial Bank of India was formed which was again nationalised in 1955 & was named as the State Bank of India.

The Swadeshi movement was instrumental in setting up various joint stock banks which were formed with Indian capital and also managed by the Indians. Out of the 14 banks which were nationalised on 19th July 1969, the oldest bank dates back to as far as 1895 when the Punjab National Bank Ltd. was formed, followed by the Bank of India Ltd., 1906, the Bank of Baroda Ltd. 1908 & the Central Bank of India Ltd., 1911.

Banking in India was then concentrated mainly in the big cities like Bombay, Calcutta & Madras. The banks did not invest their money for the small businessmen, but only dealt with the big business houses. Thus the small borrowers' requirements were solely met by the 'Savkars' and 'Money lenders' who charged very high rates of interest.

Before independence small scale industries in India occupied an almost insignificant place in the national economy. There were very few modern small scale enterprises and the small industries sector consisted mostly of un-
organised units including household units engaged in the manufacture of arts & crafts with the aid of simple hand tools. The Central Government started taking active interest in the development of small scale industries during the IIInd world war. In 1947 a conference on Industrial Development was held. The conference stressed the necessity of organised development in the field of small scale industries and in pursuance of its recommendations the Cottage Industries Board was set up as an advisory body. The importance of small scale industries was also underlined in the Industrial policy dated the 6th April, 1948.

In order to mobilise the resources from the rural areas and extend credit to the masses, the Govt. of India in 1955 nationalised the Imperial Bank and formed the State Bank of India under the State Bank of India Act 1955. The object of forming the State Bank of India was to open more branches in district and taluka levels so that the masses derived benefit from the banks. By 1968 about 60% of the total branches opened by the S.B.I. & its subsidiaries were in the rural & semi-urban areas which catered to the needs of the semi urban & rural populace.

THE POST INDEPENDENCE POLICY:

Though the commercial banks grew much in number, strength and stability after Independence, attention was not given to the priority sectors which included Agriculture, Small Scale Industries and Small borrowers and exporters. The banks only met the credit requirements of the big and medium industrial concerns. The reason for this was that the commercial banks were under the obligation of the big concerns who had vested interest in the banks as regards the ownership and control. Commercial banks and other credit institutions had, due to several historical reasons, shown a marked reluctance in the past to finance small scale industries and small borrowers. 9

Commercial banking was rather 'security' oriented than 'risk' oriented. Thus the social objectives of the Government of India as per the five year plans were not fulfilled by the banks by not extending credit facilities to the poorer sections of the society and reducing the concentration of economic power in the hands of a few. The banks did not like to change their policies and keep pace with the changing requirements of the society. These shortcomings of the banks led the political leaders think

9. Loans to small industries and small borrowers - Sudarshan Lal, - Navrang (New Delhi), 1976. page (i).
about bringing social control over the banks which was possible only through nationalisation of the banking industry. In 1968, the Banking Laws (Amendment) Act was passed which came into effect from February 1, 1969. The main objective of this Act was to have a proper and systematic working of the banks and eliminate the concentration of economic powers in the hands of a few as also put a check on the misuse of bank’s credit.

**IMPACT OF NATIONALISATION OF THE 14 MAJOR BANKS:**

The commercial banks had already started following the social objectives of the Government before nationalisation. In order to ensure that the commercial banks acted as per the Government’s policy and attained the social objectives, the Government of India on July 19, 1969 nationalised the 14 major Indian Commercial Banks with deposits of Rs.50 crores or more by an ordinance which became law by the Banking Companies (Acquisition and Transfer of Undertakings) Act, 1969. The main objectives of nationalisation were as follows:

1. To mobilise deposits from rural and semi-urban areas also throughout the country and not only from the big cities and towns.

2. To extend banking facilities in the rural areas which are unbanked or under banked.
3. To extend credit facilities to hitherto neglected sectors viz. Agriculture and Small Scale Industries for promoting their rapid and balanced growth.

4. To encourage new entrepreneurs for the development in the backward areas.

5. To provide better service to the public.

The main object of nationalisation was to bring about a rapid growth in the priority sectors which were the neglected sectors hitherto. The definition of priority sectors as given by the National Credit Council, (established in 1968) consist of Agriculture, Small Scale Industries and Exports. But the concept of priority sector was further extended after nationalisation and they now include besides Agriculture, Small Scale Industries and Exports, Road Transport Operators, Water Transport Operators, Small Businessmen, Professionals, Retail Traders, Self-employed Persons as well as Education. The policies and practices of lending to the priority sectors have also undergone changes after nationalisation. The security oriented approach of lending has since been replaced by the purpose-oriented approach and now more stress is given on the purpose of the loan rather than on other conventional factors viz. the financial standing of the borrowers, repaying capacity, and securities offered.
But lending money to inexperienced small business people without supervision is often equivalent to pouring it down the drain; what these people need is first supervision and advice and capital only secondarily. A combination of financial and managerial assistance not only helps prevent waste of scarce capital but it is also perhaps the best means of ensuring that managerial performance will improve.  

The progress made by the nationalised banks as regards lending to the priority sector since nationalisation can be judged from the following Table Nos.1, 2, 3 & 4 given hereunder:

(a) Table No.1 shows the number of units and Amount outstanding as of June 1969, June 1976, June 1979 and December 1979.

(b) Table No.2 shows Bankwise amounts given to the priority sector between the period December 1969 & December 1979 as also the Annual Growth Rate percentage during 1969-79.

(c) Table No.3 shows the progress made by the 14 Nationalised Banks as regards the Branches opened by them during the period December 1969 to December 1979 as also the Annual Growth Rate percentage during the period from 1969 to 1979.

(d) Table No.4 shows the Advances to priority sector by the Nationalised Banks from June 1969 to December 1978.

Nationalisation of Banks has helped in the development of small scale industries in the rural and backward areas and has provided employment to the rural population which has checked over-population in the urban areas. The economic disparities between various States and regions have also been reduced by spreading the Small Scale Industries evenly, thereby promoting the economic growth of the area which in turn adds to the Indian economy as a whole.

The priorities in banking have been changing according to changing priorities of the Government. All this is dependent on the various policies and programmes formulated by the Central and State Governments in developing and encouraging the Small Scale Industries. The development programmes include:

1. Allocation of maximum funds for the Small Scale Industries from the Union and State Budgets.
2. Providing various types of incentives and financial assistance.
3. Setting up of the various agencies for meeting the requirements of the Small Scale Industries.
4. Reservation of more and more items of manufacture
   for the Small Scale Industries Sector.
5. Providing more credit from banks by introducing suitable
   policies.

The new industrial policy was formed by the Government in 1977 which envisages effective promotion of Small Scale Industries in rural and semi-urban areas. A new category called the "tiny sector" was also introduced for the first time by which the smallest units would get preferential treatment in their promotional and developmental activities. The units in the "tiny sector" include those units with an investment in machinery up to Rs.1 lakh and situated in towns with a population of less than 50,000 according to the 1971 census figures and villages.

Under the revised definition which came into effect from 1st May 1975, "Ancilliary industries" have been re-defined. Those units whose investment in fixed assets in plant and machinery not exceeding Rs.15 lakhs and which are engaged in :

(a) the manufacture of parts, components, sub-assemblies, toolings or intermediaries or (b) rendering of services; and supplying or rendering or proposing to supply or render 50% of their production of the total services as
the case may be to other units for the production of other articles, provided that no such undertaking shall be a subsidiary of, or owned or controlled by any other undertaking.

Apart from the increase in the investment ceiling, the new definition for ancillaries involves changes in the following important respects:

i. Units producing intermediates will now be recognised as ancillaries

ii. Units providing servicing facilities e.g. sand blasting, machining, pressure cleaning, grinding etc. will be recognised as ancillary

iii. The concept of 'parent unit' will now include small scale industries also. Thus one small industry can function as an ancillary to another.

iv. A unit to be recognised as an ancillary should supply or propose to supply at least 50% of its production to one or more parent units.

The Industrial Policy of 1977 expected the Industrial Development Bank of India to co-ordinate, guide and monitor the entire credit facilities offered by the other Institutions to the Small Scale Industries by creating separate wings in the public sector banks.
It is interesting to see the changes in the definition of small scale industry since 1955 as given below:

(a) Definition in 1955 - 'An unit employing less than 50 persons using power & less than 100 persons without the use of power with capital assets not exceeding Rs.5.00 lakhs'

(b) Definition in 1960 - The ceiling on investment in fixed assets was raised to Rs.10.00 lakhs in case of Ancilliary Industries, while the criteria of number of persons employed was deleted.

(c) Definition in 1966 - The ceiling of Rs.5.00 lakhs in case of small scale industries was raised to Rs.7.50 lakhs. Investment in plant and machinery at original purchase price was considered and investment in land and building was not to be taken into account for determining the ceiling limit.

(d) Definition in 1975 - The ceiling of Rs.7.50 lakhs of investment in plant and machinery was enhanced to Rs.10.00 lakhs in case of small scale industries and in case of Ancilliary Industries engaged in certain
types of manufacture/serving etc. the limit was increased to Rs.15 lakhs (as already explained in the preceding paras)

(e) Definition in 1977 - The new Industrial Policy of the Government introduced for the first time the 'Tiny Sector' which include those units with an investment in machinery up to Rs.1 lakh and situated in towns with a population of less than 50,000 according to the 1971 census figures and villages.

(f) Definition in 1980 - The limits of investment in plant and machinery were increased from Rs.1 lakh to Rs.2 lakhs for tiny units (located in villages & towns with population not exceeding 50,000) from Rs.10 lakhs to Rs.20 lakhs for Small Scale Industrial units and from Rs.15 lakhs to Rs.25 lakhs for Ancilliary units.

Thus the banks had to adapt to the changes in the Government's policies and priorities from time to time to cater to the needs of the small entrepreneurs who run the small scale units.

The New Industrial Policy of the Government of India, 1977 has enlarged the list of products reserved for exclusive development in the small scale sector from 180 items to 807 items.

For the purpose of the present study, the definition of small scale industrial units as given in 1975 is taken into account, i.e. the ceiling of investment in plant and machinery up to Rs.10 lakhs.
Apart from the regular functions which the Reserve Bank of India performs as performed by the Central Banks in every country, it has also to perform several other functions which are in the context of an underdeveloped economy.

In an underdeveloped country like ours, the central bank's policy should not be restricted only to the management and regulation of currency and credit, stabilization of price level, acting as an agency of clearance and settlement of claims of member banks, acting as the agent of the Government and lending to the member banks as lender of the last resort. It should also play an important role in developing the economy and improve the living standards of the poor people in our country. Thus the monetary policy of the Reserve Bank has to perform the task of facilitating the rapid economic growth with stability in the economy. The Reserve Bank of India has to play a dynamic role not only in the development of agriculture, industry, trade and commerce by extending financial assistance, but also in the development of a sound banking system in our country by promoting the development of banks by an organised and systematic branch expansion policy.
The need for appropriate adjustment in the monetary policy of our country, to suit the economic development is what is expected of the Reserve Bank of India in the Five Year Plans. Thus Reserve Bank of India has to perform two functions:

i) to provide necessary finance to the private sector through the banking channels for the economic development, and

ii) to control the inflation generated in the economy due to tremendous investment in development expenditure.

The monetary policy of the Reserve Bank of India is that of providing adequate finance for rapid economic growth and at the same time maintaining price stability.

The Reserve Bank of India gives special treatment to certain priority sectors, e.g. the Small Scale industries. The commercial banks are allowed to borrow additional amount at the Bank Rate depending upon their lending to small scale industries.

The rate at which the Reserve Bank of India gives accommodation to the Commercial Banks by acting as the lender of the last resort is of much significance. With
the help of the Bank Rate, the Reserve Bank of India influences the cost and availability of credit to the commercial banks.

Table No. 6 shows the Changes in Monetary Policy of the Reserve Bank of India from 1969 to 1982. The frequent changes introduced by Reserve Bank of India in the criteria for lending and Deposits indicate how since nationalisation, commercial banks have to carry on their operations against the constraints created by changing Reserve Bank of India's policy. The efficacy of commercial banks in the provision of credit to the Small Scale Sector is bound to be either adversely or favourably affected. Therefore, the role played by commercial banks in the provision of credit to the Small Scale Sector must be assessed in the context of changes in the Reserve Bank of India's monetary policy and changing priorities of the Government.

Two charts I and II show the lending rates and composite Term Loans to the Small Scale Sector.
The Indian Banking system was not an organised sector before independence and even at the time of Independence, it continued the old traditions. It was only when the Banking Regulations Act, 1949 was passed that some discipline was brought in and stability in the system was introduced.

There was a change in the pattern of flow of credit and credit creation was linked with monetary stability. The policies and practices of the commercial banks were not in conformity with the socialistic objectives and priorities of the Government for the economic development of India. At the same time, the monetary authorities became strict and brought control over the activities of the banks to play a significant role in the economy for developmental planning.

With a view to bringing control over the activities of the commercial banks, and to ensure flow of funds to the needy sectors of the economy, the Government thought of nationalising the major banks in India. It was after the nationalisation that the national objectives could be turned into various policies by the Government.
The Government could now plan for regionwise and state-wise allocation of the resources mobilised by the banks and channelise the same to the needy sections of the society. The idea of Priority Sector also came into being which included fields like Agriculture, Small Scale industries, exports etc. But the formulation of various policies made by the Government were not free from political pressures and other sections of the society who dominated the socio-economic activities of our country.

In a developing country like ours it is difficult to frame the credit policy which will bring about better balance between the total demand and total supply since there is always an inflationary trend in the economy due to rising incomes which is again due to Government’s heavy capital investments for the various developmental programmes.

The policy of credit creation is also to be executed with utmost care in anticipation of increased production and mobilization of the savings by the public.

The creation of credit is possible only when the banking system develops in the whole country and ensures that the credit flows in the desired channels.
The last two decades have witnessed substantial growth of the small scale industries in India. It is estimated that during 1979-80, the number of small scale units in the country have crossed the 7.5 lakh mark (of which the registered units number at about 3.23. lakhs) with the value of production exceeding Rs.15,000 crores. Export contribution from this sector is estimated at Rs.900 crores. This sector provides employment to about 60 lakh persons.

The Union Government initiated many programmes during the Third Plan period for improving the status of the existing small scale industries as also to promote small scale industries in the rural and semi-urban areas. It also thought of modernisation of the certain selected industries on a large scale. The promotion of ancilliary industries was also given a push and a separate treatment was thought to be provided to such units in various forms.

While the Industrial policy resolution, 1956 aimed at improving the competitive strength of the small scale industries, the Industrial Policy of 1977 stressed the need for subsidy and regulation as the basic requirements of the Policy.

It was after Independence that the Government's policy towards cottage and small scale industries showed a remarkable change. The industrial policies of 1948, 1956, 1973 and 1977 played a significant role in the developmental programmes of rapid industrialization. The Industrial Policy of 1977 envisaged elimination of unemployment by increasing the industrial production of the small scale and cottage industries. Since then small scale industries are playing an important role in our economy. The 1977 policy reserved about 504 items for the exclusive production by the small scale sector.

The 1st Five Year Plan earmarked Rs.49 crores for the development of village and small industries. The 2nd Five Year Plan aimed at development of village and small industries for which Rs.175 crores were spent during the Plan period. The Third Plan envisaged Rs.264 crores for the development of village and small industries. Though the 4th Plan envisaged a total outlay of Rs.293 crores for the development of village and small industries, while the actual expenditure incurred was to the time of Rs.250 crores. During the 5th Plan period a little over 360 crores were spent for village and small industries.
During the Sixth Plan period i.e. 1980-85, the total outlay is to the extent of Rs. 923 crores for the village and small scale industries.

CREDIT SQUEEZE - PROS AND CONS:

Apart from the impact of changing Reserve Bank of India's policies and of the changes in overall economic policy made by the Government, the banking system as a whole has to face severe criticism from the various sectors whenever such radical changes as 'Credit Squeeze' of 1974 and 1981 are imposed on the banking sector.

The country had witnessed spiraling of prices during the whole of 1973 and up to September 1974. The Reserve Bank of India took a series of steps to raise the cost of bank credit and to reduce the volume of purchasing power in the hands of the public. The Reserve Bank of India's object of 'dear money' policy was to check the inflationary trend in the economy. The steps taken by Reserve Bank of India in this regard were:

1) Rise in the Bank Rate
2) Stepping up of minimum lending rates
3) Rise in deposit interest rates
4) Net liquidity ratio.
In addition to the above, the Reserve Bank of India also advised the commercial banks to review their lending policies as regards the big accounts.

The impact of credit squeeze had a positive effect on the economy which was evident from the fact that the general price level started declining from the end of September 1974.

Credit Control Measures of 1977
by the Reserve Bank of India:

The Reserve Bank of India adopted stricter measures since 1977 to control credit expansion and to have a check on inflation. Some of the measures taken were:

1. The Reserve Bank of India became strict with the commercial banks in maintaining the Cash Reserve Ratio and an additional cash reserve of 10% on the incremental deposits was required to be maintained by the banks.

2. The margin on all types of advances was raised by 10% (except in certain categories of advances viz. Agriculture, Small Scale Industries and exports) against inventories and book debts.
(3) Banks were advised to scrutinise all the big accounts whose limits exceeded Rs.50 lakhs to ensure that the advances were related with the actual output.

The above measures had certain positive bearings on the reduction of prices. Hence the Reserve Bank of India abolished the interest tax and advised the commercial banks to reduce the maximum lending rates. The rates on deposits were also reduced.

THE PRESENT CREDIT SQUEEZE OF 1981 :-

Again in the last quarter of 1981 the Reserve Bank of India tightened its measures and brought stricter controls over the banks by raising the 'Cash Reserve Ratio' and the 'Statutory liquidity Ratio'. The Cash Reserve Ratio was raised from 6 percent to 8 percent over the last year, thus impounding over Rs.800 crores. Then the Statutory Liquidity Ratio was raised from 34% to 35% which impounded a further Rs.400 crores.

STIFF PENALTIES :-

The banks were required to pay heavy penalties for even a marginal shortfall on the Cash Reserve Ratio and lost all interest payments on their cash deposits with the
Reserve Bank of India. The banks were also required to pay penal interest @ 3 percent to 5 percent on their borrowings.

EFFECT OF CREDIT SQUEEZE ON PRODUCTION AND EMPLOYMENT - (A GENERAL REVIEW)

I. ENGINEERING INDUSTRY:

The big industries like the Tata Engineering and Locomotive Company (TELCO), Ashok Leyland and most of the others are hard hit by the credit squeeze. About 30-50% production is curtailed by these big industries. Due to the prolonged strike of the textile workers in Bombay there has set in a recessionary trend in the economy. About Rs.33 crores worth of machinery is lying idle as the mill owners do not have money to take delivery. Thus the prices have reportedly reduced by 20%.

Since the farmers are not having money to purchase the fertilisers, the fertiliser companies are holding about 70% of their stocks in hand. Hence they have to reduce their prices by 15-20%.
II. ELECTRICAL AND ELECTRONICS INDUSTRY:

It has been observed that the prices for electrical and electronics goods has also been reduced since there is lack of demand for T.V. sets, Refrigerators, Fans, etc.

III. CHEMICAL INDUSTRY:

The chemical industries also face the same problems of piling stocks as that of Engineering industries. About 120 crores of caustic soda remains unsold. Prices are therefore reduced considerably to sell the stocks.

IV. PAPER INDUSTRY:

The paper mills are running at 2/3rd of their capacity. The prices of their products have dropped by about 10%.

V. OTHER INDUSTRIES:

The other industries also have to face problems of low demand and excess stock. Discounts are therefore offered to boost up sales e.g. the Tyre companies are offering bigger discounts to the dealers, the big industries are contemplating for four-day week workings, while the automobile ancillaries are also doing badly in particular.
THE OVERALL SCENE :-

The combined effect of credit squeeze and slump in demand has affected the industries roughly between 25 and 40 percent. Thus the industrial growth may be to the extent of 4% only in 1982 as compared to 8% in 1981.

Eminent industrialists have pointed out that recession is inevitable. According to them there are three factors which are responsible for the current problems. They are -

(a) liberal import policy
(b) reduced Government spending in key areas, and
(c) undisguised drop in demand.

Though the businessmen think that credit squeeze is the main reason for the present situation, many others feel that credit is not the only factor for the present crisis and problems.

EFFECT ON BANKS :-

The banks were worst hit by the credit squeeze than the industries because heavy penalties were imposed on them if they failed to meet the Reserve Bank of India's

requirements. Banks have not witnessed such a terrible crisis in the history of Indian banking was the opinion of a chief executive of a nationalised bank.

It was found that the basic banking morality was lowered when the banks in order to attract deposits started paying commission to the big depositors, especially the public sector bodies as inducement to shift their deposit accounts to the banks.

**ILLEGAL METHODS** :-

International banks were also trapped in the credit squeeze who resorted to other illegal means. The prospective borrowers were asked to bring in matching deposits if they required any loan. Hence the borrower caught hold of someone who had invested his money elsewhere and produced him before the bank. A deal was then struck between the borrower and the depositor for mutual benefits. The depositor would shift his money to the bank on which the bank would give a part as a loan to the borrower. The borrower would agree to pay the depositor in cash additional interest over and above the interest paid by the bank on regular deposit accounts to the depositor.
THE PRESENT SITUATION :-

With the Reserve Bank of India's decision to reduce the cash reserve ratio from 8 to 7.25%, there is some relief in the default position of the banks from April 8, 1982. But still the position of deposits is not encouraging, as there is meagre growth in deposits. The reason being that the depositors are investing their money in the private money market where the rate of interest is anything between 24 and 36 percent, whereas the banks offer maximum of 10% interest only.

CONCLUSION :-

Thus from the above, we can conclude that credit squeeze has both the effects - positive and negative. The positive effect can be seen from the fact that the prices of products have been considerably reduced and that there is a check on the galloping inflation which if had continued for some more period would have crippled our entire economy.

The negative aspect is that the industries in order to tide over the situation have started recession in their industries, thus resulting into mass scale unemployment. Industrial output has come down to 4% only due
to the credit squeeze, while on the other hand 1982 being the year of 'Productivity' maximum growth rate is expected.

The industries have learnt not to rely exclusively on the bank's credit facilities but to generate surplus from within to meet such difficult situations. Thus financial discipline which was lacking in the industries have been introduced.

The banks have also checked their credit portfolio and have learnt a lesson to obey the Reserve Bank of India directives of maintaining the Cash Reserve Ratio and the Liquidity Ratio.

THE SITUATION IN PUNE :-

In Pune a large number of small scale industries depend on the big industries for their survival. These units have limited capital and have to depend upon the big industries as they get orders from them for supply of various types of machinery parts. A recent report stated that about 3,000 Small Scale Industrial Units in and around Pune contribute to the extent of Rs.10 crores annually for the industrial growth. All these units are feeling the pinch of credit squeeze since their payments by the big industries are delayed beyond the normal period of a month or two. This has resulted into laying off workers by the small units.
About 10 Small Scale Industrial units have already been closed down it is reported.

The Medium and Big industries when contacted about the present situation agreed that recession was round the corner as a result of credit squeeze and if nothing is done to remedy the situation a severe crisis may soon overtake the industries.

Kirloskar Oil Engines had laid off the workers for one day a week and has made five day a week for the workers, as the tractors are not bought by the farmers as planned by the manufacturers.

The TELCO trucks are also not moving as earlier. The same trucks were sold at a premium and there was a long waiting period prior to the credit squeeze. Now they are available immediately as there are no buyers.

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