Chapter I

OBJECTIVES AND METHODOLOGY

In the modern economy, banking is a potent instrument for the economic pace-progress. The overall economic development of the country depends on rendering and making the capital active and productive but not mere augmenting the capital. "No nation can afford to live without active capital." ¹ In other words, the effective operations of banking industry will improve the quality of economic life of the people. "Bank is, in the most of world, the nerve centre of economics and finance of a nation; and the barometer of its economic prosperity." ² Banks in Germany and Japan which had close ties with the industrial and agricultural sectors were an important element in the rapid development of these countries. It was perhaps this forced the great economist, Schumpeter to refer to "credit as a phenomenon of development". ³ Credit is, thus, useful feature and phenomenon of banking system. Judicious flow of credit arrests the economic constraints. The quantum,


the composition, the direction and distribution of credit are of paramount importance in the context of economic growth and development. The erstwhile Finance Minister, Morarji Desai has rightly observed "banking, when properly organised, aids and facilitates the growth of trade and industry and hence of the national economy". Therefore, it is being realised that bank is a major instrument in achieving the socio-economic goals of the nation. The banking industry has been recognised as an effective measure in the Plans that it is more suited to the programmes of development, making the processes of savings and their utilisation to the productive ends. David has rightly remarked:"the innovator looked at the banker for credit he needed to carryout his plans... Ultimately it is the banker who provided the basic fuel (credit) for economic growth". The saving ratio which was only about 10 per cent of national income in 1950-51, has reached a level of about 23 per cent. This large increase in savings was made possible by the fact that the benefit of wide spread institutional development of banking system. The bank, is, therefore, a 'key change' facilitating the attainment of socio-economic aims of country. Indian banking system, to-day, has sheer economic status.

5. David, R., Creative Management in Banking, 1965, p.34.
The banking industry, in the past, did not meet the emerging needs of economy and, in fact, essentially trade-oriented and served a very selective clientele of the industry. The business operations of the banking industry were thus characterised as: Finance follows where industry leads. This has given birth to widening the imbalances and aggravating the unemployment problem. The credit system, as part of effort at planning within the framework of democracy, was needed what is called 'socialisation of credit'. An idea was mooted to introduce social control over commercial banks. Accordingly, social control was imposed on commercial banks in mid-1967, with the objective of wider spread of bank credit and engulfing the sectoral as well as regional imbalances. Experience in social control showed that though the intention was good, progress was inadequate, still a hang-over from the past. The concept of social control was halfway house turned into unsatisfactory. Nationalisation of 14 major banks in July, 1969, followed by six more in 1980 was considered an essential, in order to gain control over the commanding heights of the economy and utilise the banking system as an effective instrument of economic development.
To mention the speech of Smt. Indira Gandhi, made in the Lok Sabha, is appropriate here. She said: "Our sole consideration has been to accelerate development and thus make a significant impact on the problems of poverty and unemployment; and to bring about progressive reduction in disparities between the rich and the poor sections of our people and between relatively advanced and backward areas of our country". The underlying objective of nationalisation of commercial banks was to gear up banking machinery for an equilitarian society and quickening of economic progress. In other words they should become effective instruments of development, policy and planning. The supply of essential credit input to agriculture, industrial growth with a marked emphasis on the growth of small scale and medium scale industries, and balanced regional development were the aims of national economic planning. Nationalisation of commercial banks was, indeed, the most indispensable call of the day. However, everything will depend upon how the commercial banks operate, what supporting policies and measures are adopted and how vigorously they are implemented.

The revolutionary change and the dramatic transformation that have taken place in the history of Indian banking since nationalisation speak of the banking system's dynamic response to the challenging tasks, set before it. "The post nationalisation period has witnessed a complete reorientation of Indian banking from 'class banking' to 'mass banking'". 7

The contribution of the banking to the national goals in the post-nationalisation period is quite commandable in (i) branch expansion from 8262 in 1969 to 60,000 resulting in the per branch population served from 74,000 to 14,000 despite the fact the population itself has grown by several times in the intervening period, (ii) deposits mobilisation Rs.1,64,402 crores, (iii) credit deployment Rs.98,699 crores by March 9, 1990. 8 The commandable progress of Indian banking is nothing short of phenomenal progress of banking in any country in the World. In fact, the banking sector is closely involved in the economic development of the nation and in implementing a number of welfare-oriented programmes. In other words, banking sector is trying to identify itself more close to the socio-economic objectives of nation. The


8. "Bank Deposits Aggregate to Rs.1,64,000 Crores", The Hindu, Bangalore; April 4, 1990, p.13.
Banker, London has focussed on Asia's top 200 banks on their performance in 1987 and ensembled in Asia's circuit. It stated "India had one in top five, seven in top fifty and seventeen in top hundred". Banking is, thus, a distinct activity in Indian economy.

THE PROBLEM

The progress of Indian Banking industry since nationalisation is tremendous in branch network particularly in rural areas, besides deposits and credit. Still much is to do. And still a long way to go in softening the incidence of poverty and unemployment. Issues like changing banking scenario to rural areas, credit for gainful employment, aid to agricultural sector as well as weaker sections of the society etc., are requisites in socio-economic development which are to be studied. The new phase of banking is characterised by increasing qualitative aspects like customers services, build up of quality loan assets, operational efficiency, employee productivity etc., which call for identification of fresh priorities and greater attention towards improving the impact of banks' policies and programmes. It is under this context necessary to evaluate whether nationalisation of commercial banks is a pyrrhic victory, what is gained

and what is lost. And it is high time to appraise the present operational performance of the commercial banks, on which appropriate revamping measures would be initiated. Examining the performance of the commercial banks since nationalisation would certainly aid in decision-making to meet the future demands.

REVIEW OF LITERATURE

Review of earlier studies done by the individuals as well as institutions would help to scientific investigation. In other words, review of literature enriches with critical and reflecting approach in carrying out investigation. The review of literature, thus, gives an insight with which a scientific policy can be built up. Some of the studies in line to the present study are reviewed hereunder.

The effective functioning of banking industry largely depends upon the size and composition of clients. To mention the statement of an orthodox banker is appropriate here. "Our clients are larger merchants and big industrialists. They approach us with their demand for larger loans and advances and in return give us larger business. If we transfer our limited resources to small industry, agriculture etc., how can we increase our deposits, advances? And how
can we survive?"  

Branch expansion is a prerequisite factor for better functioning and thereby better performance of banking industry. In other words, branch mobilises funds from surplus areas and utilises them in those areas where they are needed. The underlying aim is to act an intermediate agent. Banking industry has made a commendable progress in extending the frontiers of banking both geographically and functionally. Patel, the then Finance Minister has said: "To-day the banking system reaches out over a far wider area and covers a much larger segment of population that it did barely a few years ago. The progress, of course, has been some what uneven; and while regional disparities in banking development have been narrowed to some extent, a lot remains to do".  

Raghupathy has also reported "the country calls for much more than has been achieved particularly in respect of sectoral and geographical areas, and population groups.... If the objectives are not fully achieved the fault does not lie entirely with the bankers but lies in our not being able to integrate all powerful instruments of development into an efficient system".  

10. Gopal, K., Perspectives in Indian Banking, Bombay; Popular Prakasan, 1977, pp.64-65.  
Though tremendous progress in terms of branch expansion, deposit mobilisation and advances has recorded, the trend has been in favour of urban areas, leaving the larger rural masses out of the reach of banking services. This was a serious thinking which to be recast and remodelled to meet the growing challenges. The Raj Committee which examined the branch expansion since nationalisation stated that "the progress in respect of branch expansion would still seem to fall short of the requirements of the country". Regarding the concentration of banking operations in the hands of rich people, Sharma stated: "one has to admit that every industrialist's family has been actively associated with the flotation and running of a bank in India. The intimate association of Tatas with Central Bank, Birlas and Goenkas with United Commercial Bank, Sahujains with Punjab National Bank, Singhanias with Hindustan Commercial Bank and a large number of Parsis and Gujarathis with Bank of India and Bank of Baroda, is well known". "The banking system continues to show a bias in favour of richer sections", is the opinion expressed by Tiwari on Indian banking system.

The banking industry after nationalisation has entered into many areas which would have been considered as unbanked by the private sector banks. Thingalaiah is of the opinion the progress of the Indian banking system is unique in many respects. But considering the needs of Indian economy and its population, he said: "banks have still a long way to go".16 "The banking system touches and should touch the lives of millions by inspiring the national priorities and objectives".17 The policy of branch expansion is to cover deficit areas mainly of rural country on rational approach. Commenting on branch expansion, Upadhaya has observed: "Except opening more than 60 per cent of total branches in the rural areas, not much progress has been made by the rural branches with regard to deposit mobilisation".18

Referring to the Indian banking progress achieved it has been nothing that of phenomenal, Narasimham says "banking anywhere in the World, has not the Indian type of explosion of branches from around 8,000 in 1969 to over

to 60,000 in the short span of 20 years. And I believe that this was a very major factor in helping the Indian economy to register an impressive increase in its saving ratio.¹⁹ In promoting Indian economy and its population, banking has still a task before it to accomplish. "And the banks should not feel complacement of what had been achieved so far but expect more in 21st century"²⁰ is the opinion of Reddy, C.R. The country wide survey conducted by the National Institute of Bank Management has revealed, "there are still untapped sectors in the country. Banking is largely a habit of literate Indian and the market strategies so far have not fully exploited the potential of illiterate - non-bank savers. And many in the urban areas still do not know about banking business".²¹ Following a series of steps, Eduardo Faliro, the Minister of Staff for Finance says "the customers service in banks had improved. But we are not satisfied and are trying to do better".²²

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Credit has been channelled to various sectors of the economy due to the existence of multi-agency approach. It is believable fact that due to stronghold of money lenders in the rural areas, the rural credit agencies are not covered the rural people widely and deeply. "Though the amount of credit to rural areas has increased by nearly 80 times, only 14 per cent of the rural households were so far covered". On regional imbalances in banking development, Chandrasekhar Rao has stated, "the bank branches in southern region alone have achieved the national target of 60 per cent both in the rural and semi-urban areas. Banks in the central and western regions have attained the target only in the rural areas. In the northeastern region banks have come close to achieving the target in the rural areas. The northern and eastern regions lagged behind the target both in the rural and semi-urban areas".

Though found better recommendations in the above studies for effective functioning of Indian banking industry, they lack indepth analysis on sectoral and geographical credit pattern, deposit mobilisation and rural and urban dichotomy. These made the author select the problem "Progress and Performance of Banking" for investigation.

OBJECTIVE OF STUDY

The specific objectives of present study are:

1. To study the progress and performance of banking in branch expansion, deposit mobilisation and credit deployment.

2. To examine the geographical and sectoral bank credit.

3. To analyse the credit-deposit ratio.

4. To suggest remedial measures for healthy growth of banking industry.

SCOPE AND METHODOLOGY

The Indian banking sector is a major instrument and is as important as important financial institutions with vast investment capacity. In other words, the banking sector has major instrument that governed the savings of the people and made them available for deployment both for industrial and rural sectors. The banking sector which was primarily oligarchic giving credit; and receiving credit was a matter of privilege without the democratic aspirations. The credit system was democratised as a part of planning effort within the frame work of democracy. This is termed as ‘socialisation of credit’. Keeping in view the bank's role in economic improvement with social
aims, the present study covers (1) branch expansion, (2) deposit mobilisation, (3) credit deployment, (4) credit-deposit ratio, (5) regional banking analysis and (6) priority sector credit for analysis.

To highlight the objectives that have taken in the present study, data was compiled. A period of two decades starting from 1969-70 to 1988-89 was taken in the study and the analyses were studied at three points namely 1969, 1979 and 1989. The urban and rural classification is taken to study the rural - urban dichotomy.

DATA SOURCE AND COLLECTION

Appraising the performance of banking industry is primarily depend on the valid and reliable data. The required data was compiled from the Banking Statistics, Reports on Trend and Progress of Banking in India, Reports on Currency and Finance and the Bulletins of Reserve Bank of India. Data is also collected from the issues of Pigmy Economic Review.

TOOLS OF ANALYSIS

The underlying objective of drawing scientific inferences lies on the use of scientific tools. To know the progress of banking sector in terms of branch expansion,
deposit mobilisation, credit deployment, priority sector credit, and the relation between credit and deposit, an endeavour has been made to study the statistical techniques. Besides application of statistical techniques, the data has also been classified and arranged in the form of tables. The statistical techniques that are used in the present study are:

Growth Rate: The growth rate (r) is studied to measure the progress of banking industry over a period of two decades. Whether data is increasing or decreasing trend over a period of time, the technique of semi-log trend, \( Y = ab^x \) is studied. This trend equation minimises the square deviation of observed values from the log-arithmetic trend values. The log-linear function of the Least Squares technique may be written as:

\[
\text{Log } Y = \text{log } a + x \text{ log } b
\]

Where,

- \( \text{Log } Y \) represents variable value
- \( \text{Log } a \) represents intercept
- \( \text{Log } b \) represents regression coefficient (slope)
- \( x \) represents time (years)
By solving the simultaneous functions of the equation, the growth rate is obtained thus:

\[(1+r) = \log b\]
\[r = \left(\text{anti log } b-1\right) \times 100\]

Coefficient of Variation: The coefficient of variation indicates how consistent or uniform the bank in achieving progress. It is a relative measure of dispersion and discloses the direction. If the coefficient of variation is less, it is said to be a less dispersion or more uniform. This technique is studied to the aspect of branch expansion, deposit mobilisation and credit deployment. The coefficient of variation is calculated by solving:

\[C.V. = \frac{\Theta}{\bar{x}} \times 100\]

\[\Theta = \sqrt{\frac{\sum x^2}{n}}\]

Where,

\(C.V\) represents coefficient of variation

\(\Theta\) represents standard deviation

\(\bar{x}\) represents arithmetic mean.
Location Quotient: For estimation of the locational imbalances, the location quotient is studied. It is the ratio of ratios. It is determined from dividing the ratio of number of branches in a region to total population in that region dividing by the ratio of number of branches to total population. The location quotient will either be proportionate or more or less than one which would mean that regional average is in balance to or above or below the national average. This technique is also applied to the deposit and credit aspects. Location quotient is written algebraically as:

\[
\begin{align*}
(1) \text{Branches } & \quad L Q_b = \frac{N B \cdot r}{P \cdot r} / \frac{N B}{P} \\
(2) \text{Deposits } & \quad L Q_d = \frac{T D \cdot r}{P \cdot r} / \frac{T D}{P} \\
(3) \text{Credit } & \quad L Q_c = \frac{T C \cdot r}{P \cdot r} / \frac{T C}{P}
\end{align*}
\]

Where,

\begin{align*}
N B & \text{ represents number of branches} \\
T D & \text{ represents total deposits} \\
T C & \text{ represents total credit} \\
P & \text{ represents population} \\
r & \text{ represents region} \\
L Q_b & \text{ represents branch location quotient} \\
L Q_d & \text{ represents deposit location quotient} \\
L Q_c & \text{ represents credit location quotient}
\end{align*}
Elasticity Coefficient:- The elasticity coefficient technique determines the rate of change in relative position over a period of time. It explains the proportionate change in deposits or credit as a result of proportionate change in number of branches. The elasticity coefficient will either be proportionate or greater or lesser than one. If it is proportionate, it would mean the marginal increase in deposit or credit is more than average increase in number of branches. If it is greater or lesser than one, the marginal increase in deposit or credit is more or less than the average increase in number of branches. While the elasticity coefficient is more than one, that region may be called more deposit or credit potential region and the low deposit or credit potential region in case, the elasticity coefficient is less than one. The elasticity coefficient can be expressed as:

(1) Deposits \[ Ed = \frac{\Delta d}{D} / \frac{\Delta b}{B} \]

(2) Credit \[ Ec = \frac{\Delta c}{C} / \frac{\Delta b}{B} \]

Where,

Ed represents deposit elasticity coefficient
Ec represents credit elasticity coefficient
\( \Delta d \) represents change in deposits
\( \Delta c \) represents change in credit
b represents change in branches
D represents deposit
C represents credit

ADDITION TO LITERATURE

The present investigation on progress and performance of banking would help in drawing inferences on scientific lines which in turn would aid the management in taking decision to overcome constraints and patronage thrust for rapid economic development. The analyses studied in this study and suggestions to findings would add to literature on subject, Indian Banking Sector.