ROLE OF COMMERCIAL BANKS IN FINANCING THE PRIVATE CORPORATE SECTOR IN INDIA: 1970-71 TO 1989-90

Dissertation submitted in partial fulfilment of the requirements for the award of the Degree of Master of Philosophy in Applied Economics of the Jawaharlal Nehru University, New Delhi.

J. DENNIS RAJA KUMAR

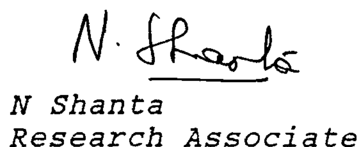
CENTRE FOR DEVELOPMENT STUDIES
TRIVANDRUM
1993

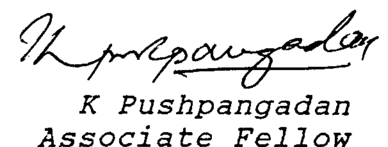
September 2, 1993

I hereby affirm that the research for this dissertation titled ***"Role of Commercial Banks in Financing the Private Corporate Sector in India: 1970/71 to 1989/90"*** *being submitted to the Jawaharlal Nehru University for the award of the Degree of Master of Philosophy, was carried out entirely by me at the Centre for Development Studies, Trivandrum.*

J Dennis Raja Kumar

Certified that this dissertation is the bonafide work of J. Dennis Raja Kumar. This has not been considered for the award of any other degree by any other University.

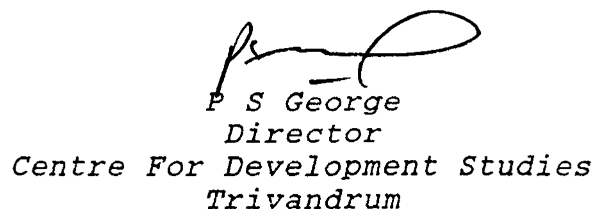




N Shanta
Research Associate

K Pushpangadan
Associate Fellow

Supervisors



P S George
Director
Centre For Development Studies
Trivandrum

ACKNOWLEDGEMENT

I wish to place on records my sincere thanks to the authority of Centre for Development Studies for offering me a place in the M. Phil Programme of the Centre. I thank Dr. G. N. Rao, the course co-ordinator, for all his efforts, and also, the other members of staff from whose lectures I gained a lot.

With a sense of gratitude, I wish to acknowledge the guidance I received from my guides, Dr. N. Shanta and Dr. K. Pushpangadan. My sincere thanks to Dr. N. Shanta for her committed and dedicated guidance throughout the work. But for her constant care and suggestions at every stage of the work, the present version would not have been possible. My experience of working under her has been very enriching, and has helped me learn discipline in research. Dr. Pushpangadan's incisive comments helped shape this work to a great extent. I thank him for his involvement.

I thank Prof. K. K. Subrahmaniam, Dr. K. J. Joseph, Mr. D.Narayana, Mr. Anandaraj, Dr. Sunil Mani, Mr. Pyarelal and Dr. U. S. Misra, for my discussions with them in the initial stages. The frequent enquiries about the state of my work by Prof. K. K. Subrahmaniam was encouraging. I thank him for his concern. I also thank Dr. P. Balakrishnan for my frequent discussions with him, although some of the issues suggested by him could not be looked into. I thank Mr. Jayaprakash Ragaviah too for the useful discussion I had with him.

Bhaskar took the pain of editing the entire draft. I acknowledge with a sense of gratitude, the efforts taken by him. I also thank Mr. Thilak Baker for going through the draft. Rajiv, Murugan, Sudip, Karunagaran, Srijit, Subrahmanian, Saikat, Sudhakar Reddy, Hari Kurup and Suresh helped me a lot while the work was in progress. I thank them all.

I thank the Librarian, Mr. Shankar, Mr. Chidambaram and all other library staff for the help I received from them in the library. I also thank Mr. Murali and all other administrative staff, for their help; and, Mr. Murali and Mrs. Sujana for their assistance in the computer room.

My sincere thanks to Murugan, Rajiv, Karunagaran, Sudip, Bhaskar, Srijit, Albin and Asha for making my stay on the campus a more pleasant and comfortable one. I value my friendship with all of them. Karunagaran was kind enough to tolerate me whenever differences in our opinion arose. I thank him for his brotherly affection which I enjoyed. Bhaskar, Sudip, Srijit and Murugan extended financial help while I was staying without fellowship. More than that, the affection that they showed towards me has been a source of joy for me. I thank Asha for being a good friend while I stayed on campus. My thanks is also due to Rajiv and family for their friendship and hospitality.

I also thank the young couple Misra and Mala, for being very kind to me. The interest that they showed in me and their encouragement has greatly motivated me to work.

I thank Meena, Saritha, Lini, Shaheena, Lalithabai and Nandu for adding charm to my stay on the campus. I also acknowledge the fun I had with Ram Mohan, Sree Kumar, Das, Jayakumar, Subramainam, Babu, Suresh, Saikat, Kurup, Sudhakar, James, Jom, Sanjit, Narayana and Joshy. I thank them for their company.

My brother Rajan has been a source of inspiration and my sister Christy Thomas has always provided me the needed help. I recall at this time how much they have meant to me all along. I also thank Dr. Ruskin for his keen interest in my work and welfare.

J. Dennis Raja Kumar.

CONTENTS

Chapter		Page
I	Introduction	1
II	Supply of Bank Credit	27
III	Bank Credit In Relation to Other Forms of Finance	61
IV	Determinants of Borrowing From Banks	83
V	Summing Up	95
	Bibliography	101

LIST OF TABLES

Nos.	Titles	Page
1.1	Indicators of Financial Development in Indian Economy: 1970/71 to 1989/90	10
1.2	Share of Financial and Non-Financial Sectors In the Total Financial Claims: 1970/71 to 1989/90	14
1.3	Deficit and Surplus Sectors of Indian Economy: 1970/71 to 1989/90.	15
2.1	Main Quantitative Controls: 1970/71 to 1989/90	29
2.2	Sectoral Deployment of Bank Credit: 1971/72 to 1989/90	39
2.3	Distribution of Bank Credit to Industry According to Size: 1971/72 to 1989/90	42
2.4	Growth Rate of Bank Credit: 1971/72 to 1989/90	43
2.5	Distribution of Bank Credit to Industry According to Types of Organisation: 1971/72 to 1989/90	46
2.6	Distribution of Bank Credit to Industry According to Types of Credit: 1971/72 to 1989/90	49
2.7	Investment by Banks in Securities of Joint Stock Companies: 1970/71 to 1989/90	53
2.8	Distribution of Investments According to Types of Securities: 1971/72 to 1989/90	54
2.9	Growth Rate of Investment in Securities by Banks: 1971/72 to 1989/90	55
2.10	Underwriting of Securities By Banks: 1970 to 1985	58
3.1	Relative Shares of Different Sources of Funds Of Public Limited Companies: 1970/71 to 1989/90	65
3.2	Relative Shares of Different Sources of Funds of Private Limited Companies: 1970/71 to 1988/89	67
3.3	Relative Shares of Different Sources of Borrowing Of Public and Private Limited Companies: 1970/71 to 1989/90	70
3.4	Important Bank Borrowing Related Ratios of Public and Private Limited Companies: 1970/71 to 1989/90	74
3.5	Relative shares of Various Sources of Funds Across Different Size Classes: 1971/72 to 1989/90	78
3.6	Size-wise Distribution of Bank Borrowing: 1985/86 to 1989/90	80

CHAPTER I

INTRODUCTION

The Background:

In recent years, the Indian economy has witnessed significant changes in Government policy towards the real sector. These policy changes, aimed at liberalisation of internal and external controls, would enable a greater role for market forces in the economy. Crucial to its success is adequate provision of infrastructural facilities, of which financial intermediation is an important constituent.

As an economy develops, a dichotomy emerges between decision to save and decision to invest, as the distribution of savings among economic units does not always correspond to the distribution of investment expenditure among them (Bhatia and Khatkhate, 1975:133). As a result, some economic units will spend more than what they earn, while some other units will earn in excess of what they spend. The former, a deficit unit, has insufficient funds to cover its investment expenditure, while the latter, a surplus unit, consumes less than its current income.

In the absence of any intermediation between surplus and deficit units, that is, between savers and investors, the savings of the former cannot be channelled to the latter to invest. Under such circumstances, investors are forced to limit their investment to the extent of funds available to them. On the other hand, the savers tend to invest their savings in assets that are of low value

for economic growth like jewellery, land, etc. (Furness, 1972:11). This leads both deficit and surplus units to a balanced budget position where savings equals investment. This arrangement, however, would result in a low level of investment and saving and hence, to a relatively low growth of output (Gurley and Shaw, 1960:196). Hence, it is essential to create a system to channelize funds from savers to investors so as to institutionalize savings and investment.

Deficit units may obtain finance in excess of current income by (i) borrowing, (ii) selling an existing financial asset, (iii) selling a real or tangible asset and (iv) employing existing cash balance (Coghlan 1980:161). In the first three cases, finance will ultimately be provided from current savings of surplus units and by running down of existing stock of cash balance held by some other units, while the last method involves running down the stock of cash balances of deficit units. However, the second and third modes entail a change in the pattern of assets holding by the deficit units. In the first case, deficit units issue claims, that is obligations, against them which equals their deficit, and surplus units would tend to accumulate financial assets that equals their savings (Gurley and Shaw, 1960:199-200; 1968:258).

Deficit units may borrow either directly or indirectly. It is direct when claims are issued directly to the lenders, namely, savers; and indirect when they obtain finance through intermediaries who mobilise the savings of surplus units. Such borrowing is done by issue of primary securities by deficit units to these channels (Gurley, 1967:177-178). Thus, it is clear that

intermediation between savers and investors is crucial to the growth of any economy.

The intermediaries obtain primary securities from deficit units to provide finance and issue secondary securities, namely, claims against them, to surplus units to mobilize their savings. Consequently, they relieve the market of some primary securities and substitute secondary securities whose qualities command a higher price. The margin between yields on primary and secondary securities compensate the intermediaries for their special services (Gurley and Shaw, 1968:258).

Apart from such financial intermediaries, channelizing also requires financial instruments such as securities to effect transactions and financial markets to facilitate such transactions. Thus, a system comprising of all the above is required to channelize savings. Such a system, consisting of financial institutions, financial claims and financial markets constitutes a financial system.

The financial system helps to accelerate economic growth to the extent it facilitates the migration of funds to the best uses, which will yield a higher social return (Goldsmith, 1969:400). Therefore, the development of a financial system is indispensable to stimulate real economic activity by providing finance for investment.

Finance is a crucial infrastructural input for manufacturing activity. Inadequate availability of finance curtails investment

activity, both short-term and long-term. Short-term investment is required to facilitate day-to-day operations whereas long-term investment is essential for expansion of production capacity, diversification, etc.. As investments of this nature are crucial for the growth of firms, it is necessary to raise funds to finance such activity. As pointed out by the Narasimham Committee[1], "With increasing deregulation of industry and the emergence of more competitive conditions the responsibilities devolving on the financial system in mobilizing resources and allocating them efficiently and responding flexibly to emerging situations would be much greater" (GOI, 1991:2-3).

Therefore, in the present changing scenario it seems both relevant and pertinent to study the response of the financial system in India to the challenges of industrialization. In other words, it becomes imperative to understand the role of various financial institutions in financing the real sector. This study is an attempt in that direction. More specifically, this study attempts to examine the role of one such important institution, namely, commercial banks in financing the private corporate sector[2] in India from 1970/71 to 1989/90, that is, the period subsequent to the nationalisation of commercial banks in India.

---

[1]. This committee was appointed by Government of India (GOI) in 1991 under the Chairmanship of Narasimham to examine all aspects relating to the structure, organisation, functions and procedure of the financial system.

[2]. This study is confined to the analysis of private corporate sector defined to include non-governmental non-financial public and private limited companies. Private corporate activity in India is mostly concentrated in manufacturing - in the 80s, about 87 per cent of private corporate activity in India was concentrated in manufacturing (Shanta, 1991:54-55).

As a prelude to this study, the theoretical issues and the development of the financial system in India is examined.

Theoretical Issues: Financial System and Economic Development:

The importance of capital formation for economic growth has been broadly recognised. Although there are several factors governing capital formation, it is not possible to isolate the role of each factor and the extent of its contribution. However, financial factors assume great significance as they influence the availability of funds required to finance capital formation. Thus, there exists a strong relationship between real and financial variables (Porter, 1966:347; Dornbusch and Reynoso, 1989:204).

The corporate sector mobilizes its required financial resources either from internal and external sources. Internal sources, consisting of capital and accumulated savings are preferred as it does not involve any external liabilities. Limitation of internal funds force firms to rely on external funds as investment activities and, consequently output would otherwise be restricted. However, external finance has to be gleaned out of the savings of savers. Firms can borrow from savers directly. If this process becomes difficult, it relies on institutions which mobilize savings directly from savers.

The design of a financial system may stimulate savings and investment in productive use or it may retard savings and divert it to inefficient uses (Gurley and Shaw, 1960:47). Hence, characterisation of a financial system of an economy becomes

important. Conventionally, it has been characterized either as demand-following or supply-leading (Patrick, 1966:174-175). It is said to be demand-following when the creation of financial institutions, their financial assets and liabilities and related financial services is in response to the demand for their services by investors and savers in the economy. When such institutions and services are created in advance of their demand, then system is characterised as supply-leading.

Patrick (1966:175-176) argues that the demand for financial services depends upon the growth rate of real output which results in greater need for intermediation to transfer savings. Such a demand-following financial system can support and sustain the leading sector in the process of growth.

The supply-leading kind of financial intermediation transfers resources from non-growth sector to growth-oriented sector, and offers possible avenues to invest and, consequently, presents an opportunity to induce real growth by financial means. Thus, it is likely to play a significant role in the early stages of economic development. As the process of real growth occurs, the supply-leading impetus gradually diminishes and the demand-following financial response becomes dominant (Patrick, 1966:177).

Patrick (1966:177-178) also argues that the financial system can influence capital stock in three ways; first, by bringing about changes in the ownership and composition of tangible wealth, through intermediation among various types of assets' holders. Second, financial institutions can encourage a more efficient

allocation of new investments, from relatively less to relatively more productive uses. Third, they can induce an increase in the rate of accumulation of capital, by providing a higher incentive to save, invest and work.

In essence, three main issues exist regarding the influence of such a system: impact on the growth of savings, financialization of savings, that is saving in financial assets, and transformation of mobilized funds into real capital (Bhatia and Khatkhate, 1975:133). A financial system satisfying these requirements assumes central place in the developmental process of an economy.

Having discussed the significance of the financial system for an economy's growth, the development of this system in India during the post nationalisation period is examined.

Financial Development in India:

In India, the central role of capital formation in the growth process of the economy had been well recognised since the inception of Five Year Plans[3]. Simultaneously, emphasis was also placed on the financial system. The system in India was more a supply-

---

[3]. At the commencement of planning in 1951, the Indian economy was operating at relatively low levels of saving and investment. The First Five Year Plan noted that in an under-developed country like India with low levels of standard of living and rapidly increasing population, the desirable growth rate in output can be achieved only if the rate of capital formation could be stepped up over the years substantially above the level of 10 per cent of Gross Domestic Product (GDP) observed in 1950/51 (RBI, 1985:4)

leading phenomenon (Rangarajan, 1984:73-74) rather than demand-following[4].

A review of secondary literature (Goldsmith, 1983:220; Morris, 1985:42; RBI, 1985:52; Rangarajan and Jadhav, 1992:146) shows that the Indian economy has witnessed significant development in the sphere of its financial system and compares favourably with those of other developing countries, including some upper income developing countries.

The presence, nature and relative size of financial institutions and financial instruments of various types characterise a country's financial system (Goldsmith, 1969:26). In other words, it is important to know the extent of financing economic activity by the issue of various instruments. The financing of economic activity may be indicated by various ratios (Drake, 1980:25) that measure the financial development of an economy. Some of the standard ratios used are described below:

Finance Ratio (FR) is the ratio of total financial claims issued during a year in the economy to national income. It indicates the relationship between current flow of financial and real variables. In other words, it reflects the relationship between financial development and economic development.

---

[4]. The First Five Year Plan states "central banking in a planned economy can hardly be confined to the regulation of overall supply of credit or to a somewhat negative regulator of the flow of bank credit. It would have to take on a direct and active role, firstly in creating or helping to create the machinery needed for financing developmental activities all over the country and secondly, ensuring that finances available flow in the direction intended" - quoted in Rangarajan and Jadhav, 1992:147.

Financial Inter-relation Ratio (FIR) is the ratio of total volume of financial assets in the economy to net capital formation. It reflects the role of financial system in financing investment. In other words, it establishes the relationship between financial structure and real assets structure of the economy.

Intermediation Ratio (IR) is the ratio of financial assets held by financial institution to the issues of non-financial sectors. It indicates the degree of institutionalization of borrowing and lending and the importance of indirect finance.

New Issues Ratio (NIR) is the ratio of primary issues[5] to net physical capital formation in the economy. This ratio establishes the extent to which the non-financial sectors of the economy reaches out to the other sectors for funds to finance its investment by issuing claims of their own.

An examination of these ratios for the Indian economy[6], shows the following (Table 1.1).

---

[5]. The total financial flows can be classified as arising due to primary or secondary issues. Securities issued by non-financial sectors are termed as primary issues which indicate a direct draft on the resources of the surplus sector to be used by deficit sectors. Secondary issues are created by financial intermediaries which borrow from surplus sectors for lending to deficit sectors (RBI Bulletin, December 1988:1124-1125).

[6]. These indicators with respect to Indian economy have been worked out from "Flow-of-Funds Accounts of the Indian Economy" as published by Reserve Bank of India (RBI). This account describes borrowing and lending operations of individual sectors or `from whom to whom' and `in what manner' basis. These accounts are meant to portray the various channels through which funds flow to finance, and act as a support to the real economic activity. These accounts, thus, reflect the role played by financial intermediaries in general and particular classes of financial institution in channelizing resources from sectors which have surplus funds to deficit sectors (RBI Bulletin, December 1988:1124).

Table 1.1
Indicators of Financial Development in Indian Economy: 1970/71 to 1989/90

Indicators	1970/71 to 1974/75	1975/76 to 1979/80	1980/81 to 1984/85	1985/86 to 1989/90
1. Finance Ratio	0.18	0.29	0.35	0.39
2. Financial Inter-relation Ratio	1.10	1.46	2.32	2.46
3. New Issues Ratio	0.63	0.84	1.37	1.41
4. Intermediation Ratio	0.77	0.74	0.69	0.75

Source: Various issues of RBI Bulletin.

An upward trend in Finance Ratio (FR), Financial Inter-relation Ratio (FIR) and the New Issues Ratio (NIR) signifies financial development in the Indian economy through the seventies and eighties. The upward trend in Finance Ratio (FR) shows that the financial claims which amounted to 18 per cent of National Income in the early seventies has increased to 39 per cent in the late eighties. This clearly brings out the growing role of the financial system in the economy.

The upward movement of Finance Inter-relation Ratio (FIR) since 1970/71 indicates the increasing role of financial system in channelizing funds in the economy for investment purposes. Over time, as an economy develops, its financial system experiences a rapid growth in financial assets relative to national income or national real wealth (Gurley and Shaw, 1967:257-258; Goldsmith, 1969: 44) and hence, FIR has a tendency to rise with an economy's growth. The performance of FIR is highly supportive of this hypothesis. In other words, it is indicative of the larger role

played by the financial system in India in mobilising funds for investment purposes.

However, financial claims consists of both primary claims issued by non-financial sectors and secondary issues issued by financial sectors. Hence, the observed rise in Financial Inter-relation Ratio (FIR) is a result of an increase in both the issues. A break-up of these issues into primary and secondary issues reveals the significance of the claims issued by their respective sectors. The New Issues Ratio (NIR), indicating the extent of primary claims issued by non-financial sectors to directly finance their investment, shows a steady increase throughout the period. It shows that the role of non-financial sectors has also increased in line with the development of the financial system so as to mobilize funds directly for its investment.

The Intermediation Ratio (IR), measured as the ratio of secondary issues to primary issues, shows a constant decline till mid-eighties reflecting the increase in primary issues of non-financial sector. However, the relative significance of financial sectors in mobilizing resources has significantly improved in the late 80's, even though NIR has been increasing. This indicates a further revival of the financial sector in relation to the non-financial sector with regard to resource mobilization.

The above discussion clearly points to the increasing importance of the financial system in the economy and of financial flows in relation to economic activity. While these indicators reveal the significance of the financial system with regard to channelising

savings from surplus sectors to deficit sectors of the economy, it is equally important to understand the role and the significance of the different institutions within the financial system.

Financial Institutions in India:

The Indian financial system consists of two major segments: an 'organised sector' and a 'traditional sector'. The organised sector, organised on modern lines, includes commercial, development and co-operative banks, the stock market and various non-banking financial institutions like insurance corporations and mutual funds. The traditional sector, also known as the informal credit market, is the set of indigenous financial institutions such as rural and urban money lenders who mainly finance small enterprises, farms and household consumption (Avadhani, 1978a:15-17; Morris, 1985:1). The role of this sector, however, has been declining and is quite marginal at present. Hence, our study confines itself to the organised sector.

The different institutions within the organised sector can be broadly grouped into banking and other financial institutions with Reserve Bank of India (RBI) as the central bank. The banking system consists of commercial and co-operative banks. Commercial banks include Indian banks in the public and private sector in addition to foreign banks operating in India. Other financial institutions include the special machinery of term-lending institutions, normally termed as development banks. The RBI, being the central bank, has its link with non-financial sectors through banks and other financial institutions which implement the policies initiated

by the Reserve Bank.

The relative importance of different institutions in the financial sector is indicated by their share in total assets of all such institutions (Drake 1980:25). A break-up of the financial assets' structure of the banks and other financial institutions indicates a declining trend in the percentage share of financial assets of banks[7] in the total financial assets of all financial institutions in India[8]. To illustrate, the percentage share of banks was 73.8 per cent in 1980/81 which declined to 70.2 per cent in 1985/86 and further to 66.8 per cent in 1989/90. Thus, going by the magnitude of assets holding, the role of banks continues to be significant in the financial sector, although it is declining.

A more detailed analysis of the share of various banks shows that scheduled commercial banks are the most important banks in the banking system in the country. To be more specific, these banks accounted for 91.7 per cent of the financial assets of banks in the first half of 70s which increased to 95.6 per cent in the second half of 80s. With a share of less than .15 per cent, the role of non-scheduled commercial banks is very negligible. The Co-operative banks had a share of 8.13 per cent in the first half of 70s which

---

[7]. The assets of banks include the following items: (i) Cash in hand and balances with Reserve Bank; (ii) Asset with the Banking System; (iii) Investments; (iv) Bank credit (total loans, cash-credits and overdrafts and bills purchased and discounted) and dues from banks (RBI Annual Report, 1990-91:89).

[8]. Computed from Report on Trend and Progress of Banking in India, 1991-92 (July-June) - issued as a supplement to RBI Bulletin, January 1993.

declined to 4.36 per cent during the late 80s[9].

The role played by each of these institutions as mobilizers of funds is analyzed by studying their respective shares in total claims issued by the financial sector as a whole (see Table 1.2).

Table 1.2
Share of Financial and Non-Financial Sectors
In the Total Financial Claims: 1970/71 to 1989/90

(Percentage Share)

Sectors	1970/71 to 1974/75	1975/76 to 1979/80	1980/81 to 1984/85	1985/86 to 1989/90
A. In Total Claims: (1+2)	100	100	100	100
1. Financial Sector (a+b)	43.1	42.6	40.8	43.0
a. Banking	31.6	30.0	28.9	27.8
b. Other Financial Institutions	11.5	12.6	11.9	15.2
2. Non-Financial Sector (c+d+e+f)	56.9	57.4	59.2	57.0
c. Private Corporate Sector	11.2	8.9	12.9	10.9
d. Government	35.5	32.2	37.5	38.2
e. Households	9.4	10.5	9.0	9.5
f. Rest of the World	0.8	5.8	-0.2	-1.6
B. In Financial Sector Claims: (a+b)	100	100	100	100
a. Banking	73.3	70.3	70.8	65.0
b. Other Financial Institutions	26.7	29.7	29.2	35.0

Source: Same as Table 1.1.

[9]. Calculated from various issues of the Reports on Currency and Finance.

Of the total financial claims issued in the economy, the share of non-financial sector is higher and increasing over the period from 1970/71 to 1984/85. However, in the late eighties, its share has declined. As against this, the share of financial sector has increased in the eighties. Table 1.2 also shows that within the financial sector, the share of banking sector in total claims has been declining, although in terms of magnitude, it still continues to play a dominant role within the financial sector.

However, the gains to the real sector depend on how efficiently the financial sector performs its function of intermediation (Rangarajan and Jadhav, 1992:141). An examination of the surplus and deficit sectors in the economy gives some insights to this (see Table 1.3).

Table 1.3

Deficit and Surplus Sectors of Indian Economy: 1970/71 to 1989/90.

(As percentage of National Income: NNP)

Sectors	1970/71 to 1974/75	1975/76 to 1979/80	1980/81 to 1984/85	1985/86 to 1989/90
a. Banking	0.29	0.57	0.50	0.22
b. Other Financial Institutions	-0.01	0.12	0.71	0.82
c. Private Corporate Sector	-1.37	-1.92	-3.29	-3.02
d. Government	-4.41	-7.18	-10.26	-12.10
e. Households	4.97	7.38	8.41	10.16
f. Rest of the World	0.52	-0.97	1.65	2.89

Notes: The negative sign indicates deficits.

Source: Same as Table 1.1

It is quite evident from Table 1.3 that the Government is the largest deficit sector in the economy. Its deficit as a percentage of national income has risen from 4.4 per cent in early 70s to 12 per cent in late 80s. The other major deficit sector of the economy is the private corporate sector whose deficit as percentage of national income, rose from 1.37 to 3.02 during the same period. The surplus sectors are the `financial', `households' and `rest of the world' sectors. Sukhamoy Chakravarty Committee (RBI, 1985;52-53) studied the sector-wise financial balances and contended that the household sector is the major surplus sector in Indian economy and it is the saving of this sector that is important in financing the deficits of Government and the private corporate sector. Thus, it follows that the savings of household sector is to be mobilized to finance those sectors undertaking investment activities in excess of its savings.

Though the private corporate sector is the second largest deficit sector, the primary claims issued by this sector has accounted for, on an average, 11 per cent of the total claims issued (see Table 1.2). An analysis of the sector-wise pattern of financing the private corporate sector's deficit reveals that the household sector, the largest surplus sector of the economy, has financed, on an average, 25 per cent during the period 1975/76 to 1985/86 which sharply declined to 12 per cent subsequently[10]. It shows that mobilization of savings directly from households by the private

[10]. This has been worked out from the 'Flow-of-Funds account of the Indian Economy'.

corporate sector has not only been small in magnitude but has also declined over the years. This suggests that the link between the households sector and the private corporate sector has not been very strong.

Again, although Government issued claims accounting for more than one-third of total claims issued in the economy (see Table 1.2), its deficit has been widening. Hence, the private corporate sector may not be in a position to secure the required financial resources from Government to fill up its deficit. Thus, it is the financial sector, the other large mobilizer of savings that assumes significance for the private corporate sector.

The importance of private corporate sector in the industrialization of the economy can be gauged from its contribution to the economy's overall capital formation. The share of private corporate sector in the total gross capital formation has been quite impressive in the 80s. The proportion was of the order of 15.5 per cent, 10.8 per cent, 18.7 per cent and 17.1 per cent during the four quinquennium in 70s and 80s respectively[11]. Furthermore, the Eighth Five Year Plan has envisaged an investment rate of 4.33 per cent of Gross National Product for this sector at 1991/92 prices during the plan period (GOI, 1992:53). As this sector may not be in a position to mobilize funds directly from `households' and `government' sectors, the role of intermediation becomes more important. Hence, the role of financial institutions is of cardinal importance for the growth of private corporate sector. In

---

[11]. Computed from National Accounts Statistics, 1990 and 1991.

other words, the private corporate sector depends more on the financial sector for finance than on any other sector of the economy. Given this, the importance of commercial banks in financing the private corporate sector's investment needs to be hardly stated.

Nationalisation of Commercial Banks:

The above discussion brings out the crucial place occupied by commercial banks in the financial system of the country and its role in mobilizing and channelising savings in the economy. An examination of the evolution of commercial banks in India reveals that they had undergone a structural change in 1969 with their nationalisation. The main objectives of their nationalisation, as stated in the preamble to the Banking Company's (Acquisition and Transfer of Undertakings) Act, are "to control the heights of the economy and to meet progressively, and serve better, the needs of development of the economy in conformity with national policy and objectives"[12]. It began with the Government nationalising State Bank of India (SBI) and its seven associate banks along with fourteen major Indian Scheduled Commercial Banks in the Private Sector, having deposits of Rs. 50 crores and above. And again, in April 1980, six more banks with deposit liabilities of not less than Rs. 200 crores each were nationalised. Sukhamoy Chakravarty Committee opines that this move brought a substantial segment of banking business under Government ownership and reinforced its control over the total financial system (RBI, 1985:61).

---

[12]. Quoted from Report on Currency and Finance 1969/70:103.

Nationalisation facilitated Government to exercise greater control over banking business through directed credit programmes, differential interest rates, etc.. The control and regulatory measures adopted by Reserve Bank of India are aimed at controlling the quantum and cost of credit and, at controlling the use and direction of flow of credit. Obviously, these control mechanisms have a bearing on the availability of funds with banks to lend to the private corporate sector.

Banks' provision of finance to the corporate sector can be either direct or indirect. Direct financing involves provision of credit of both short and long term nature whereas indirectly, it provides by underwriting securities such as shares and debentures. Hence, there is a need to examine the composition of flow of finance from banks to corporate sector and its pattern, especially after nationalisation wherein commercial banks became vulnerable to changes in policies initiated by RBI.

The Empirical Studies:

Empirical studies in this direction may be broadly classified into two: those that cover the period prior to nationalisation (Rosen, 1962; Bagchi, 1962; Gupta, 1969; Ambegeokar, 1969; Bhole, 1972) and those covering the post-nationalisation period (Shetty, 1976 and 1978a; Rao, 1988; Sharma, 1991). There are also some studies (Venkatachalam and Sarma, 1978 and Misra, 1989) that cover both periods.

All studies prior to nationalisation have one common finding, that is, the increasing reliance on banks by the private corporate sector. In other words, banks have become an important source of borrowing for this sector, largely to meet short-term needs arising out of inventory holdings. Rosen (1962) observed that the use of bank funds was not influenced by profitability and the rate of expansion, defined as the rate of growth of fixed assets. Bagchi found the magnitude of investment by this sector to be influenced by profit after tax (PAT). However, he argued that external funds, particularly from banks, had accounted for the acceleration of investment whenever PAT was inadequate.

Gupta and Ambegeokar observed that the use of funds from banks by this sector had exceeded its inventory formation. Gupta, hence, argued that a small portion of such finance should have gone to meet fixed investment. Further, he found the growth rate of physical assets to be more directly and closely related to security issues than bank credit. Hence, he argued that the fast growing firms relied heavily on security issues than the use of bank credit. Ambegeokar found that the rate of rise in bank credit exceeded that of inventory, sales and output. Further, he observed that its dependence on banks for working capital had increased, accompanied by a decline in reliance on other financial institutions. Bhole observed an increased tendency to use institutional credit, along with an increase in investment in inventories and fixed assets at a time when the rate of interest was rising. Hence, he concluded that the rate of interest did not exert influence on the investment activity of the private corporate sector.

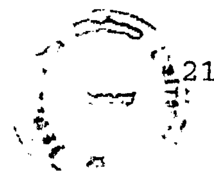
Rosen, Bagchi and Gupta also examined the reliance on banks for finance across different size groups within the private corporate sector. There was a consensus in their conclusions; that both small companies (with paid-up capital of less than Rs. 5 lakh) and larger companies (with paid-up capital Rs. 50 lakhs and above) placed less reliance on banks for finance than those in the medium range. Rosen and Gupta argued that small companies did not have much access to banks, given the nature of the lending policies of banks, whereas larger companies had more access to its own resources, including the internal accretion of funds. Bagchi also observed that bank credit had been predominantly supporting gross capital formation of middle range size groups than the lower and upper size groups which registered the highest rates in gross capital formation.

Rosen and Gupta had also analyzed the supply of finance by banks to meet the long-term needs of this sector. It was observed that it was more by way of underwriting of securities than by provision of long-term credit. Gupta also found that banks were in a leading position in the institutional arrangement of underwriting.

Not many studies have been found on the role of banks in financing private corporate sector since nationalisation. The studies by Shetty and Rao were related to demand for bank credit from manufacturing sector as a whole.

Shetty (1976) assessed the dimensional changes in credit deployment during the first five years of nationalisation in relation to changes in output and prices. The rationale for his analysis was

Diss
X,625:6.44 N90←N70 TH-5283
N3



the fact that, in any accepted model of demand for money, one common variable is the gross national product or some other variant of it in real terms. Consequently, he hypothesised that credit for any sector or industry over a period has to have some relationship with its performance in real terms, particularly, output. He observed a declining trend in the credit extended by banks to industries since nationalisation, though it was higher than other sectors. On finding that the share of manufacturing sector in bank credit to be higher than its share in Net Domestic Product (NDP), he concludes that increase in bank credit has occurred far in excess of increase in output during the years 1968/69 to 1973/74.

In his other paper, Shetty (1978a) observed that the share of medium and large industry in total bank credit had declined due to priority sector lending. Another observation, in line with his earlier finding, was that growth in bank credit had always been disproportionate to growth of their physical output, especially in industries like cotton textiles. His observation, particularly for the years 1975/76 and 1976/77 revealed (a) that increase in average bank credit had been higher than the growth of NDP originating in registered manufacturing sector even at current prices, (b) an appreciable increase in the rate of short-term bank credit to inventories and (c) relatively higher reliance on trade credit. In line with these observations, he suggested policies to scrutinize credit claims vigorously and relate credit to the genuine production requirements so that funds are not tied up with these large borrowers.

Rao (1988) carried out an econometric exercise on the determinants of demand for bank credit of some selected industries for the period between 1970/71 and 1984/85. He observed that output of these industries was the most important factor in determining its demand for bank credit whereas interest rate of banks and relative rate of interest of other sources of borrowing played only a secondary role. Price of output was also found to have affected the demand for credit significantly. The relative interest rate variable was significant with respect to industries like textiles, engineering and total manufacturing, while it was not significant for industries like sugar and other food products and chemicals.

The significance of banks for private corporate sector has been broadly pointed out by Misra (1989) who held that it was declining in the 70s unlike that of 60s. He also observed an upward trend in the provision of term loan by banks to this sector.

The determinants of behaviour of bank borrowing by private corporate sector has been studied by Venkatachalam and Sarma (1978) and Sharma (1991) through an econometric analysis on the financial behaviour of this sector. While the former study covered the period between 1958/59 and 1974/75, the latter covered the period from 1970/71 to 1986/87. Both studies reveal a positive influence of inventory holding on borrowing from banks. Moreover, the advance rate appeared to show a negative impact in the former study, while it proved to be insignificant in the latter study. However, increase in cost of borrowing from alternative sources seems to have raised the demand for bank credit. Further, Venkatachalam and Sarma postulated and found that availability of

internal funds and improvement in liquidity position of firms reduced the demand for bank funds.

To sum up, the private corporate sector has an important part to play in the industrialization of the country. It depends on the financial sector, especially the commercial banks for financing its investment and, therefore, its growth. The step to nationalise banks brought banking business in the economy under the control of Government, thereby reinforcing its control over the financial system (RBI, 1985:61). The control over commercial banks by RBI has a bearing on the availability of funds that banks have to lend to the private corporate sector. Secondary studies show that there have been changes in the role and nature of bank credit. While most of the earlier studies have dealt with specific issues, there are not many studies which examined the role of banks in financing the private corporate sector in an integrated manner. This study tries to fill that gap.

An examination of some of these issues in the post-1980 period in comparison with the early seventies seems both useful and important, especially in the light of the recent policy changes in the financial system both implemented and contemplated[13]. Such changes have implications for the role of commercial bank credit

---

[13]. Many important developments in the financial system having bearings upon the capital and money markets have taken place since 1985/86 (Misra, 1989:4). Further major changes in the policies regarding the financial sector are contemplated on the line of the recommendations of the Narasimham Committee. These policies may be inferred to have implications on the availability of finance, especially the one relating to the different sources from which the private corporate sector could secure funds to finance its investment activities.

which constitute the mainstay of the financial system in India.

Objectives of the Study:

Therefore, this study attempts to examine the role of banks in financing private corporate sector in India for the period 1970/71 to 1989/90. More specifically, the study attempts:

i) to review credit policy in detail and its influence on the supply of credit to industry in general and to private corporate sector in particular;

ii) to study the role of funds from banks to private corporate sector against its overall pattern of financing;

iii) to analyze the reliance placed on banks by different size groups within private corporate sector; and,

iv) finally, to examine the determinants of borrowing from banks by private corporate sector.

Data Sources and Methodology:

The study bases itself mainly on data as published by the Reserve Bank of India (RBI). Data from various publications such as Report on Currency and Finance, Basic Statistical Returns, Statistical Tables Relating to Banks in India and Reserve Bank of India Bulletins have been used. Where published data have not been available, primary data have been collected from RBI. Simple ratios and averages have been used. In addition to this, the Ordinary Least Squares (OLS) method has been used to examine the determinants of borrowing of this sector from banks.

Schemeta of the Study:

This chapter, Chapter 1, gives the background and the rationale for the study. The second chapter gives a brief review of policies affecting the supply of credit by banks to industry and examines the share of private corporate sector in the overall credit provided by banks to industry. The investment made by banks in the securities issued by this sector is also discussed in this chapter. The third chapter examines the role of finance from banks against the overall financing pattern of the private corporate sector. The reliance placed on banks by various size groups within private corporate sector has been analyzed in this chapter. The fourth chapter studies the determinants of borrowing from banks and chapter five summarises the findings of the study.

CHAPTER II

SUPPLY OF BANK CREDIT

As stated earlier, with nationalisation, the deployment of resources by banks was regulated by policy measures initiated by Reserve Bank of India (RBI) which affect the availability and direction of funds. In a regulated financial system, policies are designed to influence both borrowing and lending. This chapter analyzes the supply of bank credit to industry with specific reference to the private corporate sector. In the first section, a broad overview of policies pertaining to supply of credit to industry is given. Section II analyses the distribution and nature of bank credit to various sectors. The last section examines the indirect form of provision of banks' finance to the private corporate sector.

SECTION I

Credit Policies - A Broad Overview:

As provision of credit is an important function of Commercial Banks, RBI is conferred power by legislation to regulate it by means of policy formulation. Consequently, Commercial Banks have to follow the guidelines and directives issued by RBI from time to time. The control and regulatory measures adopted by RBI for channelizing the flow of credit are both quantitative and qualitative in nature. While the former aim at controlling the quantum and cost of credit, the latter are meant to control its use and direction.

Credit provided by banks influences the stock of money in the economy. The use of instruments of monetary regulation has an important bearing on bank credit in that, these instruments influence its quantum and cost. The instruments which have a bearing on resources available with banks to lend are Cash Reserve Ratio, Statutory Liquidity Ratio and Bank Rate.

Cash Reserve Ratio (CRR) is a ratio of cash reserves to demand and time liabilities, outstanding on the Friday of previous week, to be maintained with RBI by commercial banks (RBI, 1985:246). By the instrument of Statutory Liquidity Ratio (SLR), banks are required to maintain a ratio of liquid assets to demand and time liabilities in the form of cash, gold and unencumbered approved securities at the close of business everyday (RBI, 1985:251). The Bank Rate (BR), one of the instruments of quantitative credit control, represents the standard rate at which Reserve Bank is prepared to buy or rediscount bills of exchange or other commercial papers eligible for purchases under the provision of RBI Act (RBI, 1985:267). It is essentially a rate at which Reserve Bank extends advances to various categories of borrowers.

Therefore, it is clear that credit dispensed with by banks is a residual of these reserve requirements which subsequently influence the quantum of funds available with banks to lend. Whenever banks find inadequate funds to meet the demand, they can borrow from Reserve Bank which carries the bank rate. Hence, higher the rate, higher would be the cost of borrowing. Thus, it is clear that any upward trend in these instruments would affect the availability of resources with banks to lend.

Table 2.1 details the changes in these forms of instruments over the years.

Table 2.1

Main Quantitative Controls: 1970/71 to 1989/90

Years	Cash Reserve Ratio	Statutory Liquidity Ratio	Bank Rate	Credit/ Deposit Ratio	Investment/ Deposit Ratio
1970/71	3.00	28.00	6.00	79.3	23.1
1971/72	3.00	28.00	6.00	74.1	23.2
1972/73	3.00	30.00	6.00	70.8	25.0
1973/74	7.00	32.00	7.00	73.0	23.3
1974/75	4.00	33.00	9.00	74.1	23.9
1975/76	4.00	33.00	9.00	76.8	32.5
1976/77	6.00	33.00	9.00	75.0	31.5
1977/78	6.00	34.00	9.00	67.3	35.6
1978/79	6.00	34.00	9.00	65.9	33.7
1979/80	6.00	34.00	9.00	67.8	33.4
1980/81	6.00	34.00	9.00	66.8	34.7
1981/82	7.75	35.00	10.00	67.9	34.6
1982/83	7.35	35.00	10.00	69.1	35.7
1983/84	9.00	35.00	10.00	68.2	35.1
1984/85	9.00	36.00	10.00	67.8	39.0
1985/86	9.00	37.00	10.00	65.7	35.8
1986/87	9.50	37.50	10.00	61.6	37.6
1987/88	10.00	38.00	10.00	59.8	39.4
1988/89	11.00	38.00	10.00	60.5	39.0
1989/90	11.00	38.50	10.00	60.8	38.6

Note: 10 per cent of incremental demand and time liabilities (DTL) is to be added to Cash Reserve Ratio (CRR) for the periods, 1976/77 to 1979/80 and, 1983/84 to 1985/86.

Sources: Various issues of Report on Currency and Finance.

An upward trend is seen in the use of various monetary instruments, although bank rate has remained stable at 10 per cent in the 80s. As mentioned earlier, such a trend implies that it limits resources available with banks to lend. It is reflected in the downward trend in credit to deposit ratio vis-a-vis an upward trend in investment to deposit ratio. This evidence also suggests that these quantitative instruments have diverted funds towards

investment and away from deployment for credit to the industrial sector[1].

The upward trend in the investment-deposit ratio suggests that commercial banks have increased their investment which would have helped various sectors to augment their financial resources through banks. While credit dispensed with by banks is a direct way of providing assistance, investment is an indirect way of extending assistance. Thus, it appears that commercial banks increased their indirect form of provision of financial assistance more than the direct form due to the increased use of monetary instruments.

Ensuring an increased flow of assistance to the hitherto neglected sectors was one of the prime objectives of nationalisation of banks. To this end, a new policy of priority sector lending was formulated, by which, liberal lending facilities were provided to neglected sectors like agriculture, small scale industries, the self-employed, retail trade, small artisans and others. 33.3 per cent of bank credit had to be allotted to these sectors, which was subsequently raised to 40 per cent by March 1985. Although small scale industries stood to benefit from these measures, it was not so with regard to medium and large industries. Thus, it meant that the availability of resources for industries from banks would be a residual after catering to the credit needs of the priority sectors.

---

[1]. Rao estimated that 1 per cent rise in the SLR between March 1979 and March 1980 had led to a decline in the rate of growth of credit to medium and large industry by 4.8 per cent during the same period (Rao, 1980a: 868).

Apart from such policies, the industrial sector was also affected by other regulatory measures such as `Credit Authorization Scheme' (CAS), introduced by RBI even before nationalisation, in 1965. It was intended to channelize the resources of the banking system to different sectors of the economy according to national plan priorities, and to strengthen the role of RBI in monitoring the flow of credit to big borrowers' accounts. Accordingly, banks were required to take prior authorization from RBI to sanction any credit worth Rs. 1 crore or more to any single party, or any quantum that would take the total limit enjoyed by such party from entire banking system to Rs 1 crore or more on secured and/or unsecured basis (RBI, 1983: 6). As the industrial sector is a large borrower from banks, this scheme did affect the flow of credit from banks to this sector. A brief examination of the working of the scheme throws some light in this regard.

Marathe Committee[2] divides the operation of CAS since its inception in 1965 into four phases (RBI, 1983:6-9). In the first phase, which lasted till 1970, RBI's role was confined to processing banks' applications to exercise a measure of restraint on banks' lending to large borrowers. The absence of a data base, lending norms and information system to follow-up credit handicapped proper assessment of credit needs of borrowers, and to ensure proper end-use of funds. During the second phase, which commenced in June 1970 and lasted till mid-1975, RBI sought to introduce a more

---

[2]. Appointed by RBI in 1982 with reference to examine the objective, scope and context of CAS and to make suggestions with regard to making modifications therein, if any, having regard to the changing economic situation of the country (RBI, 1983: 1-2).

organized approach to the assessment of credit needs of large borrowers; prescribing a set of forms in which essential data were to be obtained by banks from borrowers seeking credit under CAS, and furnishing the same to RBI when authorization was sought.

According to the committee, CAS entered the third and perhaps, the most important phase in the mid-70s with the acceptance of recommendations of the Tandon Committee which became the criteria of CAS scrutiny of application under CAS. The rationale of the recommendations made by Tandon Committee and their suggestions is as follows.

Banks provided working capital finance to industrial units to finance their current assets by way of cash credit. The manner in which banks extended credit under this system had accentuated the problem of potential imbalance in demand for and supply of funds. The level of advance by banks was determined not by how much a banker could lend at a particular point of time, but by the borrowers' decision to borrow at that time. This made credit planning a difficult task for banks. To the extent that outstanding amount in cash credit account never fell below a certain level during a year, there was permanent lock up of bank funds in the borrowers' account. It was, therefore, to rationalize the system of working capital finance by the banks that the Tandon committee was appointed by RBI in 1974 (RBI, 1975:11-14)[3].

---

[3]. The main terms of reference of the Committee was to review the existing system and effect change in such a way that under the new system, borrower would plan his credit needs and banks also would be able to plan having known the credit requirements of borrowers (RBI, 1975:3).

The committee observed that there was no uniformity in approach of any bank in the assessment of working capital requirements, inventories and bills receivables, being the major components. The Committee argued that `if bank credit is to be viewed as a tool of resource allocation in the economy, one cannot get away from the problem of defining reasonable levels of inventories and receivable in each industry and hence the need for norms for these current assets'. In this context, the banker was viewed as a lender to supplement the borrowers' requirements to carry an acceptable level of current assets. The implications were two-fold; one, the level of current assets must be reasonable and based on norms; two, a part of the fund requirements for carrying current assets must be obtained from long-term funds comprising owned funds and term borrowing, including other non-current assets (RBI, 1975:17). Thus, the committee stipulated specific norms for inventory and receivables that could be had in each industry[4].

Further, the Tandon committee went on to suggest some approaches to lending, to determine the quantum of credit. In this regard, it underlined two basic conditions: every industrial borrower should hold only a reasonable level of inventory and receivables conforming to the norms; and second, there must be a surplus of current assets over current liabilities, which meant that, a part

---

[4]. However, no norms have been suggested for highly seasonal industries like sugar, tea, etc. and those industries which work under specific contracts like heavy engineering which experiences a large tie-up of funds in current assets. These norms were applicable to all industries including the small scale industries, with aggregate limit from the banking system in excess of Rs. 10 lakhs and above.

of the current assets should be financed entirely from owned funds or long term borrowing.

Guided by the above objectives, the Tandon Committee formulated some alternatives for working out the maximum permissible level of bank borrowing. In Method I, the borrower would have to contribute a minimum of 25 per cent of working capital gap from long term funds, which would give a minimum current ratio[5] of 1:1. In Method II, the committee envisaged that the borrower would have to provide a minimum of 25 per cent of total current assets from long term funds which would give a current ratio of 1.33:1. And in Method III, the Committee suggested the borrowers' contribution from long term funds would amount to the entire core current assets and a minimum of 25 per cent of balance current assets which would give a current ratio of 1.77:1, thus, strengthening the current ratio further (RBI, 1975:22-29).

Observing several drawbacks in cash credit system, the committee (RBI, 1975:32-35) pointed out that the level of borrowing by industrial units during a course of a year fluctuates from month to month depending on the schedules of purchases of raw materials and despatch of finished goods. It was also noted that the outstanding overdraft in a cash credit account, particularly in non-seasonal industries, did not fall below a certain level, thus indicating a

---

[5]. Current ratio is a ratio of Current Assets to Current Liabilities. Current assets included by the Committee are raw materials, stores and spares, finished goods, receivables including bills discounted with banks and other current assets while current liabilities included creditors for purchases, bank borrowing including bills discounted with banks and others.

stable requirement of funds during a year. Therefore, it suggested a bifurcation of the entire cash credit limit into loan and demand cash credit, which could be reviewed annually. The Committee was of the opinion that the loan would take care of a minimum level of borrowing which the borrower expected to utilize throughout the year, while the cash credit portion would take care of fluctuations in credit requirements due to seasonality of demand.

Reserve Bank of India endorsed their recommendations and eventually incorporated them in their credit control measures on August 21, 1975 (RBI Bulletin, August 1975:676-679). Since then, banks' credit to industry has been largely governed by these measures. Although the recommendations of the Tandon Committee were implemented, the progress had been very slow, especially the one relating to the bifurcation of credit limit into demand and fluctuating cash credit (RBI, 1989a:251). In this context, another Study Group was appointed by RBI in 1979 under the chairmanship of Chore (RBI, 1979:1-2) to review the operations of cash credit system, particularly with reference to the gap between sanctioned credit limits and the extent of their utilization, and to suggest modifications, if necessary (RBI, 1979:1-3).

Of the various suggestions made by Chore committee, what is relevant to this study is the continuation of Tandon Norms. The Chore committee also, like Tandon committee, felt the need to reduce dependence on banks by medium and large borrowers, both in the private and public sectors for their production. Hence, they were of the view that the net surplus plus cash generated by an established unit should be utilized atleast partly to reduce

borrowing for working capital purposes. In other words, it opined that the established units should not divert their cash generation exclusively for expansion purposes which should legitimately be financed by promoters' own fund. Hence, it concluded that owners' contribution for working capital purposes could be enhanced without structurally changing the Tandon committee style of lending. It suggested placing them under Method II of lending, to give a minimum current ratio of 1.33:1 and made compulsory for all borrowers having aggregate working capital limits of Rs.10 lakhs and above.

This recommendation was accepted by RBI and was incorporated in their credit control measures on December 8, 1980[6]. Marathe committee felt that CAS entered the fourth phase in December 1980 with RBI adopting most of the recommendations of Chore committee. Since then, bank finance to industry has been mainly on the line of the recommendations made by Tandon and Chore Committees, although CAS has undergone some changes in its operation. For instance, the upper limit which was Rs.1 crore in 1965 was raised to Rs.2 crore in November 1975 and further to Rs.3 crore in August 1982 (RBI, 1989b:31). In November 1982, it was raised to Rs. 5 crore for export-oriented manufacturing units (RBI, 1989b:38). The CAS was applicable to both private and public sector initially, though the latter was taken out of its purview in May 1969 and brought in

---

[6]. The other accepted recommendations are the one pertinent to the lending system, bifurcation of cash credit into demand loan for core portion and fluctuating cash credit component, separate limit for peak level and normal peak-level period, drawls of funds to be regulated through quarterly statements, discouraging of ad hoc or temporary limits and the encouragement for bills finance (RBI Bulletin, December 1980: 981-985).

again in March 1973, but with an enhanced limit of Rs.3 crore with respect to working capital facilities and Rs. 1 crore with regard to term loan. In 1982, the cut-off limit for working capital funds for the private and public sector borrowers were equalised (RBI, 1989b:31). The limit was further raised to Rs.4 crore (RBI, 1989b:99) in October 1983 and again to Rs 6 crore in April 1986. As for the manufacturer and trader exporters, a uniform limit of Rs. 7 crore was fixed, as against the earlier differential limits of Rs.5 crore and Rs.4 crore respectively. The discretionary power of banks was enlarged to sanction in excess of stipulated limits temporarily, for periods not exceeding 3 months, upto 10 per cent of existing working capital limit, or 25 per cent of credit limit, subject to an overall ceiling of Rs. 2 crore as against the past ceiling of Rs. 75 lakhs (RBI, 1989b:202-203).

However, Reserve Bank withdrew this scheme in October 1989 following its finding that the purpose of CAS was achieved by the enforcement of discipline as referred to earlier. But nevertheless, all proposals involving sanction of aggregate working capital beyond Rs. 5 crore would be subjected to post sanction scrutiny by RBI to ensure that the basic discipline is observed. As for term loans, all proposals which are currently required to be referred to RBI for prior authorization would be subjected to post sanction scrutiny (RBI, 1989b:305-308).

What is more important and, perhaps, has a bearing on the availability of credit is the norms for inventory and receivables and approach to lending. These are the policies by virtue of which, more contribution was expected from owned funds and long

term borrowing and thereby, reduce the dependence placed on banks by large borrowers. To what extent these policies had affected the resources made available by banks to industries has to be empirically verified. However, Narasimham committee is of the opinion that compliance with these norms has not been very satisfactory (GOI, 1991:13-14). In short, the regulatory measures of CAS, guided by the recommendations of the Tandon and Chore committees, changed the policy orientation of banks towards their lending to industry. It is against this backdrop that the pattern and behaviour of banks credit to industry is examined.

SECTION II

Sectoral Deployment of Bank Credit:

In this section, the credit provided by commercial banks to industries has been analyzed. Of the total credit provided to the commercial sector in India, commercial banks accounted, on an average, for 70.6 per cent and 68.5 per cent in the 70s and 80s respectively[7]. This fact clearly brings out the crucial role played by commercial banks in providing credit.

The total credit provided to the various sectors by scheduled commercial banks, the most important segment of commercial banks, as on the last Friday of June 1971/72 was Rs. 5300 crores and this

---

[7]. Computed from 'Sources of Money Stock', Various issues of Report on Currency and Finance.

rose to Rs. 104312 crores in 1989/90. The sector wise distribution of bank credit is shown in Table 2.2.

Table 2.2
Sectoral Deployment of Bank Credit:
1971/72 to 1989/90

(Percentage Share)

Sectors	1971/72 to 1974/75	1975/76 to 1979/80	1980/81 to 1984/85	1985/86 to 1989/90
A. Industry	56.6	47.6	45.5	46.0
B. Agriculture	8.9	12.2	17.2	17.1
C. Internal Trade	17.5	25.8	20.1	16.5
D. Services	5.9	3.6	2.6	3.7
E. Personal Loans	3.4	3.1	3.6	4.7
F. All Others	7.8	7.7	11.1	12.1

Note: 1. Sectors are classified into six on the basis of their economic activity, namely, i) industry, ii) agriculture, iii) services, iv) internal trade, v) personal loans and v) all others. These sectors can also be broadly divided into priority sectors and non-priority sectors.

Source: Various Issues of Report on Currency and Finance

It is evident that though the bulk of bank credit continues to go to the manufacturing sector, its share has declined sharply in the second half of 70s and the 80s. However, there seems to be a revival in the late eighties. The share of agriculture has increased till the mid-80s, remaining constant since then. The share of internal trade which includes both retail and whole sale trade has registered an increase in the 70s, but declined subsequently during the 80s. This seems to explain the rise in the share of manufacturing sector from the mid-eighties. While the share of personal loans increased from 3.4 per cent in the early 70s to 4.7 per cent during the late 80s, the share of all other

sectors jointly increased from 7.8 per cent to 12.1 per cent during the same period.

Prior to nationalisation, industry accounted for more than 60 per cent of total credit[8]. However, the orientation of credit distribution was redefined with nationalisation by introducing priority sector lending, aimed at providing liberal credit facilities to the neglected sectors like agriculture. The movements in the share of industry, and that of agriculture and internal trade in bank credit also show that it is the increased share of agriculture, internal trade and others that has led to the decline of the share of industries in bank credit. Further, the sharp decline since the year 1975/76, as seen in Table 2.2, could also be because of the implementation of Tandon norms in 1975 which intended to reduce the reliance placed by industries on banks. Therefore, a priori, it seems that the introduction of new policies of lending plus the implementation of Tandon norms reduced the share of industrial sector in total bank credit.

However, a detailed examination of annual figures shows that the share of industry has gone up since the mid-80s from 41.3 per cent in 1984/85 to 48.7 per cent in 1989/90, although it did not regain its position of the 70s. This increasing trend is accompanied by a decline in the share of internal trade and a constant share of agriculture, which in the earlier periods was increasing. Hence, it is inferred that the lending to priority sector, especially

---

[8]. The share of large and medium industries in the total commercial bank credit was around 61 per cent in March 1968 (Mujumdar, 1982:97).

agriculture, which had reduced the flow of credit to industry since nationalisation till the mid-80s. And, the increase in the share of industry since the mid-80s was mainly due to the reduced deployment of credit to internal trade. What is inferred is that the introduction of the policy of priority sectors lending has had an important bearing on the availability of bank credit to industry in that it resulted in reducing the share of industry in the overall credit deployed in the economy.

The industrial sector so far discussed includes also the small scale industry which has been accorded priority in the allocation of overall bank credit. Hence, to examine the impact of priority sector lending on credit flow to medium and large industries, it is relevant to examine in a disaggregated manner, the relative share of medium and large, and small scale industries. Table 2.3 gives the share of medium and large, and small scale industries in credit provided by banks to industries.

Table 2.3
Distribution of Bank Credit to Industry
According to Size: 1971/72 to 1989/90

(Percentage Share)

Particulars	1971/72 to 1974/75	1975/76 to 1979/80	1980/81 to 1984/85	1985/86 to 1989/90
A. In Total Bank Credit:				
a. Medium and Large Industries	44.3	36.2	33.3	33.3
b. Small Scale Industries	12.3	11.4	12.2	12.7
B. In Total Bank Credit To Industries:				
a. Medium and Large Industries	78.3	76.1	73.0	72.4
b. Small Scale Industries	21.7	23.9	27.0	27.6

Source: Same as Table 2.2

Though nearly three-fourth of credit deployed in the industrial sector has been absorbed by the medium and large industries, their continuously declining share implies an increase in the share of small scale sector. This sector has in fact maintained a constant share even in total bank credit, although the share of total industry was declining until the mid-80s. This also suggests that the trend observed for manufacturing sector as a whole is a reflection of the trends in credit to medium and large industries; when the share of medium and large industries decreases, the share of industry as a whole decreases and vice versa (Tables 2.2 and 2.3). All these observations are strongly suggestive of the effective impact of policy measures to curb lending to big borrowers and to promote priority sector lending.

The analysis of the relative share of industry in bank credit however, does not reveal the growth in bank credit to industry over the years. To this end, an attempt has been made to analyze the trends in the growth of bank credit to industry[9] (see Table 2.4).

Table 2.4

Growth Rate of Bank Credit: 1971/72 to 1989/90

Growth Rate of	1971/72 to 1974/75	1975/76 to 1979/80	1980/81 to 1984/85	1985/86 to 1989/90
Total Bank Credit	19.5	18.9	18.6	15.9
Industry	18.9	15.1	15.1	19.8
Medium and Large Industries	18.4	14.2	12.9	22.1
Small Scale Industries	20.9	17.9	21.6	14.6

Source: Same as Table 2.2

The earlier analysis revealed that the proportion of credit provided to industries had declined since early 70s and increased from the mid-80s. However, the positive growth rate seen in Table 2.4 shows that credit to industry has been increasing in absolute terms. Moreover, while the growth rate of credit to industry has been consonant with that of total bank credit in the early 70s, it is much lower during the next two periods, after which it has risen. Given the constant growth rate observed between mid-70s and mid-80s, for both total bank credit and that to industry, it

---

9. The growth rate is simple annual arithmetic growth computed using the methodology of $(t - t_{-1}) / t_{-1} * 100$ where t is the current year and t_{-1} is the previous year.

appears that industries have had an increasingly lesser amount of bank credit deployed in the economy.

Analysis of growth of bank credit of medium and large, and small scale industry shows that the former registered a lower growth than that for entire industry until mid-80s, while small scale industries registered a higher growth during the same period. This suggests that inclusion of small scale industries, which enjoyed priority, with industries on the whole, distorts the picture of amount of credit provided to medium and large industries. However, a reverse trend was seen since the mid-80s. While small scale industries registered a lower growth in bank credit than the earlier periods, medium and large industries registered a higher growth in the post-eighties than the earlier periods. This suggests that the increased share of industry in total credit was largely brought about by faster rate of growth of bank credit to medium and large industries. It further suggests that the higher growth rate of the entire industrial sector since the mid-80s, which is higher than the rate of growth of total bank credit, has been mainly due to increased growth of credit provided to medium and large industries. Hence, it seems that the increased share of industry observed since the mid-80s was due to more credit allocated to medium and large industries whose relative share in the overall bank credit had been declining during the previous periods. Having observed the share of industry in total credit and its growth profile, it is pertinent to examine the distribution of credit by type of organisation.

Bank credit to Industry According to Types of Organisation:

An examination of the share of different types of organisations in total credit to industry would reveal the disparities in credit allocation among these groups. The RBI, in disaggregating credit distribution by types of organisation, identifies four categories, namely, Public sector, Private Sector, Joint Sector and Individuals. Public sector includes the undertakings of Central and/or State Governments and Quasi-Government Bodies. Private sector includes i) Government companies owned and/or managed by either Central or State Governments or both; ii) privately owned companies not falling under (i); and, iii) partnerships, proprietorships and joint family concerns. Analysis has been carried out following RBI's classification. However, the joint sector undertakings and individuals not classified elsewhere is clubbed under one group 'Others'.

It was noted in section I that the quantitative control of credit, namely, Statutory Liquidity Ratio (SLR) and Cash Reserve Ratio (CRR) has been increasing over the years. This implies a rise in reserve requirements on deposits, entailing a reduction in credit-deposits ratio. Narasimham Committee (GOI, 1991:15) argues that the SLR has increasingly been used as an instrument for diverting part of household sector savings mobilised by the banking system to finance public sector investments. Its implications for the private sector are two-fold; first, the increase in reserve requirement implicitly reduces the overall resources available with banks for lending. Second, the proportion of credit to industry in total bank credit itself has declined from early 70s, followed by

a revival since mid-80s. Given this tendency, the share of private corporate sector in total credit to industry has to be examined to discern the importance of private corporate sector. An examination of the distribution of bank credit according to types of organisation (Table 2.5) shows the following.

Table 2.5

Distribution of Bank Credit to Industry According to Types of Organisation: 1971/72 to 1989/90

(Percentage Share)

Organisation	1971/72 to 1974/75	1975/76 to 1979/80	1980/81 to 1984/85	1985/86 to 1989/90
A. Public Sector	10.25	11.16	13.55	9.64
B. Private Sector (a+b+c)	87.30	86.22	84.42	87.60
a. Government Companies	2.89	3.08	2.47	1.74
b. Privately Owned Companies	60.86	58.40	52.74	54.66
c. Partnerships and others	21.91	24.74	29.22	31.20
C. Others	3.26	2.62	2.03	2.76

Source: Various issues of Basic Statistical Returns.

The bulk of credit has gone to the private sector, with the public sector roughly accounting for a mere 10 per cent. A cursory glance at the break-up of private corporate sector in Table 2.5 also points to the falling share of Government companies in the 80s. This observation coupled to the low share of public sector suggests that Public corporations have taken a relatively lesser share of bank credit, particularly since the mid-80s. This may be attributed to the increased use of reserve requirements for public

sector investment, as pointed out by Narasimham Committee, which implicitly means that banks' finance to public sector has been more by way of investment in securities than by direct credit.

Considering the major share of privately owned companies, it is obvious that movement of its share should coincide with that of Private sector as a whole. However, the share of partnerships, proprietorships and joint family concerns show an upward trend. If one views this segment as largely reflecting the small scale sector, then it can be inferred that till about mid-80s, they have been provided credit at the expense of privately owned companies, after which it was done by lessening the share of Public sector including government companies. This suggests that since the mid-80s, the policy orientation to lend more to small scale industries has eroded the share of public sector rather than privately owned companies.

If privately owned companies are viewed to reflect the private corporate sector in the economy, then it can be seen from Table 2.5 that this sector's share of bank credit decreased till mid-80s because of the increase in the share of Public Sector and all other forms of organisations. Thus, one could conclude that the declining share of industry in total bank credit is largely a reflection of a decline in bank credit to private corporate sector.

It has been observed that the policy of priority sector lending has reduced the share of industry in the total bank credit until the mid-80s. Based on the above findings, one could say that the practice of lending to priority sectors during the initial 15 years

of nationalisation was at the expense of the private corporate sector rather than that of public sector.

Further, the share of industry in the overall bank credit has been observed to be increasing since the mid-80s, whereas that of Public sector has declined in that period. It, therefore, suggests that the increased share of industry would have been mostly absorbed by the private corporate sector. It is also seen that increase in the share of industry in the overall bank credit was accompanied by a reduced flow of credit to internal trade. This suggests that the larger share of credit provided to private corporate sector was also at the expense of internal trade.

While the trends in the level of bank credit have been examined, it is equally important to understand the nature of bank credit and its change over time.

Types of Credit:

As stated earlier, the credit provided can be either short-term and long-term. Following the British banking system, Indian commercial banks provide short term credit, governed by physical security and personal guarantee (Rosen, 1962:17). Such short-term credit include cash credit, demand loans and overdrafts. Besides, banks also purchase or discount both export and inland bills, and advance against import bills. There is also Packing credit, which is essentially export promotional finance, specifically meant for production, processing, packing and purchase of goods meant for exports (Panchumukhi et.al., 1991:74). Another type of credit

provided is term loan, which was facilitated by the introduction of refinance facilities by Reserve Bank against approved loans in 1958. The following Table 2.6 presents the distribution of bank credit to industry according to the types of credit.

Table 2.6

Distribution of Bank Credit to Industry According to Types of Credit: 1971/72 to 1989/90

(Percentage Share)

Type of Credit	1971/72 to 1974/75	1975/76 to 1979/80	1980/81 to 1984/85	1985/86 to 1989/90
1. Cash Credit	55.53	54.74	51.33	48.84
2. Overdrafts	7.14	6.19	6.78	7.12
3. Demand Loans	4.18	3.37	3.26	3.00
4. Term Loans	11.65	13.68	16.19	17.46
5. Packing Credit	5.05	5.56	5.08	5.35
6. Purchase/Discount of a. Export Bills	3.85	3.76	3.13	3.04
b. Inland Bills	11.87	11.72	12.1	13.9
7. Others	0.73	0.98	2.12	1.29

Note: 'Others' include advances against import bills and unclassified.

Source: Same as Table 2.5

A structural shift in the type of credit provided to industries can be discerned from Table 2.6. The share of short term credit such as cash credit and demand loans show a constant decline over the years. They jointly accounted for 60 per cent in the first half of 70s which fell to 52 per cent during late 80s. The share of Packing credit, an export promotional credit, has remained constant. Provision of credit via discounting and/or purchasing

bills show a marginal increase, mostly contributed by inland bills rather than export bills, which has declined marginally.

The declining trend observed in case of short term credit may be attributed to the orientation of credit policy towards reducing the dependence of large borrowers on banks for financing working capital as suggested by Tandon Committee. The analysis of the relative share of cash credit too points to the impact of policy measures to discourage cash credit. The increasing use of inland bills is an encouraging sign which again suggests the effectiveness of these measures[10].

More importantly, the share of term loans has increased, suggesting that the role of banks in providing long term capital has increased over the years. Hence, with regard to implementation of norms of Tandon committee, it seems that it has resulted in reducing short term credit and a corresponding increase in term financing.

Perhaps, one may also attribute this to certain other policy measures as well, as provision of term loan was made possible

---

10. The bills system of lending is adjunct to cash credit system. The Chore Committee was of the view that use of bills of exchange enable banks and others with surplus funds to buy bills of various maturity; and, those with inadequate funds to discount such bills in the market to suit their requirements. Such that, it would help eligible bankers to approach Reserve Bank only if they fail to get required amount from the market; thereby imparting flexibility in the money market by evening out the liquidity in the banking system and would also enable the monetary authority to exercise more effective control over the money market, besides promoting the credit planning by banks. These bills, being a self-liquid short term asset, was considered by Chore Committee as the suitable financial instrument of banks as these resources are basically short-term nature (RBI, 1979: 23).

largely due to the introduction of refinance scheme of Industrial Development Bank of India (IDBI). This issue can be examined by studying the total refinance provided by IDBI. The annual reports of IDBI carries institution-wise refinance facilities provided by IDBI. From these reports, it can be found that share of banks in the refinance provided by IDBI amount to, on an average, 38.5 per cent for the entire 70's and 80's. A rise in the banks's share is noticed from 1973/74. However, a break-up between 70's and 80's show that the latter period has registered a higher share than the former period, accounting for 42.7 per cent as compared to 34.2 per cent in the 70's[11]. It is possible that this increased refinancing enabled banks to extend long-term credit to industry. The refinance provided to banks however, could include term loans extended to both the small scale as well as medium and large industries. Due to dearth of data no disaggregated analysis is possible. Nor is any analysis by type of organisation possible.

SECTION III

Participation in Industrial Securities:

Apart from providing credit, commercial banks meet the financial needs of industry by participating in securities issue of the industrial units, which are essentially long-term loans (Rosen, 1962:31). This form of assistance helps industrial units to undertake investment for expansion, modernisation, diversification,

---

11. Computed from various Annual Reports of Industrial Development Bank of India (IDBI).

etc.. The contribution of commercial banks to such types of investment can be gauged by examining their investment in, and underwriting of securities of industrial units.

Investment in Shares and Debentures:

An examination of the investment made by banks in the securities of Joint Stock Companies has been made using the 'Survey of investment of Scheduled Commercial Banks' as published in the RBI Bulletin. Such surveys carry the investment portfolio, both of Indian or Foreign securities, of all Indian scheduled commercial banks (other than regional rural banks) including those of offices in foreign countries. With respect to foreign banks in India, only the investment by their Indian branches is considered. The survey covers the following types of investment: (a) Central and State Government securities, (b) other trustee securities (c) shares, bonds and debentures of Indian joint stock companies, (d) fixed deposits with banks, (e) other domestic securities including initial contribution to the share capital of Unit Trust of India and (f) foreign securities and other foreign investments, both of the Indian scheduled banks; and all branches in India of foreign banks (RBI Bulletin, Nov. 1990:785).

Table 2.7 summarizes the investment made by banks in securities. The proportion of domestic securities exclusive of Indian government securities is also given.

Table 2.7
Investment by Banks in Securities of
Joint Stock Companies: 1970/71 to 1989/90

(Percentage Share)

Nature of Investment	1970/71 to 1974/75	1975/76 to 1979/80	1980/81 to 1984/85	1985/86 to 1989/90
a. To Domestic Investments	7.4	5.5	2.2	5.2
b. To Total Investments	2.1	1.6	0.8	1.9

Note: Domestic investment exclusive of investment in Government securities

Sources: Various issues of Basic Statistical Returns Relating to Banks in India and various issues of RBI Bulletin.

From Table 2.7, it is seen that investment made by banks in securities decreases both with respect to its domestic investment, excluding government securities, and with respect to their total investment till the mid-80s. Since then, an increasing trend is discernible.

Earlier, it was observed that there was an upward trend in the investment-deposit ratio (see Table 2.1), implying that the resources employed by banks in investment has been increasing. It suggests that banks would have helped joint stock companies to augment their finance. When viewed against this, the declining proportion of investment made by banks in the securities of joint stock companies till the mid-80s suggests that the indirect form of financing has declined at a time when the total resources employed by banks by way of investment has been increasing. However, the trend observed for the second half of 80s shows that banks' indirect form of financing has increased simultaneously.

One important consideration guiding investment is the returns from it. Between debentures and shares, while the returns on the former are assured, the return on shares involve risk as they are residual which a firm pays after meeting its other financial obligations such as interest on debentures, provision for taxation and so on. With this in mind, it would be of interest to study the distribution of banks' investment between shares and debentures, given their contrasting nature of return. To understand this, a break-up of investment into shares and debentures has been made and examined (see Table 2.8).

Table 2.8

Distribution of Investments According to Types of Securities: 1971/72 to 1989/90

(Percentage Share)

Nature of Securities	1971/72 to 1974/75	1975/76 to 1979/80	1980/81 to 1984/85	1985/86 to 1989/90
a. Shares	38.2	31.0	31.7	13.9
b. Debentures	61.8	69.0	68.3	86.1
c. Total (a + b)	100	100	100	100

Source: Various issues of RBI Bulletin.

Participation in the ownership of joint stock companies by banks through investment in shares show a constant decline which is especially sharp in the late 80's. Thus, it appears that increasingly `the principle of safety' has guided the banks' portfolio. It also suggests that the declining share of securities in total investment (Table 2.7) has been due to a reduction of

their investment in shares. However, the share of securities in total investment has gone up in the mid-80s. At the same time, a break up of these investments shows that the proportion of shares has gone down in that period. It implies that the increased proportion of investment in securities was made possible by investing more on debentures.

The foregoing discussion highlights the increasing investment by banks in debentures rather than in shares. To study the trend in the growth of investment, their respective growth rates have been computed (see Table 2.9).

Table 2.9

Growth Rate of Investment in Securities by Banks: 1971/72 to 1989/90

Nature of Securities	1971/72 to 1974/75	1975/76 to 1979/80	1980/81 to 1984/85	1985/86 to 1989/90
Total Investment	21.4	22.3	18.8	22.0
Total Investment in Securities	19.3	9.2	9.2	79.5
a. Shares	2.95	12.6	2.1	45.1
b. Debentures	35.7	8.9	13.2	95.6

Source: Same as Table 2.8

Table 2.9 shows that the growth in investment in securities has peaked in the late 80's, with a growth rate of 79.5 per cent which is much higher than that of total investment. It suggests that since the mid-80s, banks' indirect form of providing finance has increased significantly. Although the proportion of investment made in shares went down in the late 80s, the growth in investment

in shares is much more than that for any of the previous periods. The growth in investment in debentures shows a much higher rate than the growth in total investment in securities. This indicates that indirect finance from banks to industries has increased, particularly since the mid-80s, in the form of safe securities such as debentures.

It is important to note that this investment in securities does not include investment in Government securities through which the public sector is financed. In other words, it represents the securities issued by private corporate sector.

To summarize, the analysis show that the proportion of investment in securities has declined from the early 70s till the mid-80s, but increasing since then. The growth in investment in the different forms of securities also show a significant rise since the mid-80s, implying that indirect form of finance, especially investment in debentures, has increased during that period. Analysis of different types of credit also reveal that the share of term loans has increased. This, along with increased investment in debentures shows that since the mid-80s, banks' role in long-term financing of the private corporate sector has increased.

Another aspect of investment in securities is the underwriting of securities. Underwriting is a process whereby the underwriter agrees to sell securities for a commission and takes the responsibility of taking the securities not subscribed by the public. As the primary capital market in India is not well developed to attract savings directly, the role of financial

institutions including banks in the form of underwriting securities becomes critical. The role of commercial banks in underwriting securities can be comprehended by examining the magnitude of securities underwritten and the relative share of banks in underwriting.

Data has been collected from the article 'Public Response to the Security issues' in the RBI Bulletins. However, such details are available only upto the year 1985. Hence, the changes in the late eighties could not be examined. It is also important to note that the non-government non-financial public limited companies accounted for the bulk of securities issued[12]. Their share in the total securities issue has been, on an average, 95.4 per cent during the whole of 70s and 98.9 per cent in the early 80s. Hence, the following examination of the underwriting may be considered largely as a reflection of the underwriting of securities of private corporate sector. Table 2.10 gives the details.

---

[12]. Computed from various issues of Reserve Bank of India Bulletin.

Table 2.10
Underwriting of Securities By Banks: 1970 to 1985

(Percentage Share)

Years	Percentage of Underwriting			Underwriting By Banks		
	Shares	Debenture	Total	Shares	Debenture	Total
1970	93.7	92.3	94.9	8.2	10.8	6.6
1971	81.4	100.0	88.6	3.7	8.2	3.9
1972	90.5	72.0	84.6	5.1	1.4	3.8
1973	93.6	71.9	93.3	2.5	12.4	3.1
1974	84.4	100.0	88.6	7.4	5.0	6.6
1975	94.3	100.0	95.2	14.3	0.7	12.5
1976	84.6	100.0	86.4	18.9	23.0	16.7
1977	91.5	100.0	92.4	21.5	18.2	20.5
1978	87.6	100.0	89.2	18.9	13.3	17.5
1979	73.1	100.0	76.5	11.0	0.0	9.2
1980	60.8	16.6	41.5	8.2	0.0	6.3
1981	80.5	85.0	82.6	14.5	20.3	17.3
1982	69.9	129.4	103.3	7.9	30.9	23.9
1983	53.6	82.6	57.6	10.8	40.3	16.9
1984	84.6	95.9	85.9	13.6	36.7	16.8
1985	74.0	82.4	74.9	10.0	24.1	11.7

Source: Same as Table 2.8

It is evident from the Table 2.10 that a major segment of the securities issued were underwritten. The relative share of commercial banks has been increasing. To illustrate, the commercial banks underwrote, on an average, 6.1 per cent during the early 70s, 14 per cent in the late 70s and 17.4 per cent in the early 80s. Underwriting of both shares and debentures by banks has increased over time. The proportion of debentures underwritten by banks is higher than that of shares in the early eighties. This shows that banks were more in favour of debentures than shares.

The details regarding the percentage shares of securities underwritten by other development financial institutions such as IDBI, UTI, ICICI, IFCI, LIC, SIDCs and SFCs vis-a-vis banks is also

examined[13]. Although these institutions account for a substantial portion (more than 50 per cent) of the securities issues in the 70s, their relative share has declined in the 80s to less than 40 per cent. A look at the relative shares of these institutions including commercial banks show that commercial banks have played an important role during the early 70s, next to IDBI, LIC, ICICI and UTI; but was next only to IDBI in the late 70s; and, assumed a leading position in the first half of 80s[14]. This reveals that the role of banks in underwriting securities of the private corporate sector has increased over the years.

Summary of the Chapter

To sum-up the chapter, it may be said that the share of industry in the overall bank credit declined from early 70's and increased from the mid-80s. The share of investment in the securities of Joint Stock Companies in total investment also moved in the same direction. An analysis of distribution of bank credit to industry according to type of organisation showed that private corporate

---

[13]. Their abbreviations are Industrial Development Bank of India (IDBI), Unit Trust of India (UTI), Industrial Credit and Investment Corporation of India (ICICI), Industrial Finance Corporation of India (IFCI), Life Insurance Corporation of India (LIC), State Industrial Development Corporations (SIDCs) and State Financial Corporations (SFCs).

[14]. The relative shares of LIC, ICICI, UTI and IDBI during the early 70s were 11.4, 9.37, 7.5 and 13.8 per cent respectively as against the share of 6.1 per cent of commercial banks. However, the relative share of most of this institution declined during the subsequent periods. Only IDBI had accounted for a share of 21.1 per cent which was higher than that of commercial banks during the second half of 70s. The early 80s experienced a further decline in relative share of all the development banks which all together accounted for about 37.9 per cent against the share of commercial banks which was 17.4 per cent.

sector accounted for the bulk of credit and its share moved in the same direction as that of the share of industry on the whole. That is, it declined during the first 15 years of nationalisation and increased since the mid-80s. While this analysis gives only an understanding of the absolute trends in the pattern and nature of bank credit, it is important to understand what has been its role in financing the private corporate sector vis-a-vis other sources of borrowing. The following chapter focuses on such issues.

CHAPTER III

BANK CREDIT IN RELATION TO OTHER FORMS OF FINANCE

The previous chapter dealt with various policies that affect the supply of bank credit, the trends in bank credit and the various forms in which banks extend financial assistance to the private corporate sector. However, the role of banks in financing private corporate sector can be fully understood only if it is examined in relation to other forms of finance. This chapter, therefore, focuses on the role of bank credit in relation to other forms of finance for the private corporate sector. The chapter begins with a brief theoretical discussion on the financing pattern of corporate sector in Section I. The extent of dependence of private corporate sector on the various sources of finance is examined in Section II. Size-wise analysis of bank borrowing is carried out in Section III.

SECTION I

The significance of bank credit in financing corporate investment may be assessed against the background of the overall pattern of corporate financing (Gupta, 1969: 21). Pattern of financing refers to the various forms of raising funds necessitated by the decision to invest. These forms are the different sources through which required funds are secured by corporate sector to finance their investment. Analysis of their relative shares in total sources of funds would reveal the significance attached to a particular source of fund.

The different sources of funds can be broadly classified as either internal or external. The relative availability of funds from internal and external sources have an important bearing on investment decisions (Hoovar and Klein, 1952: 112) and, therefore, the nature of funds becomes important. Funds from internal sources are those available to firms in the form of their capital and retained earnings like reserves & surplus and provisions.

Funds from external sources are to be mobilized by issuing claims. The means to raise this form of funds are fresh issue of capital, borrowing and resorting to creditors who agree to supply raw materials on credit. All these incur cost, involve the obligation of paying interest and the risk of becoming indebtedness to outsiders. However, this form of fund is indispensable to a firm. Kuh (1971: 26-44) argues that limiting investment only to the extent of available capital and savings, that is internal funds, limits the growth of firms, as it is insufficient to finance investment activity for long-run growth. Therefore, taking recourse to external funds becomes imperative in the context of the potential it offers to the corporate sector to undertake investment in addition to what is available from internal sources.

Studies reveal that the internal funds in the form of retained earnings provides a major share of funds for firms in developed countries (Fazzari, et.al. 1988:146-47). On the contrary, given the scarce capital resources, firms in developing economies are more likely to have recourse to external funds (World Bank, 1991: 36-37).

What order does a firm follow to raise funds from these sources?. Meyers (1984: 581), in his Pecking Order Theory, suggests that firms prefer internal funds first and then, look for external funds if required. It is hence, implicit that external sources are resorted to if internal funds are not adequate. However, when a firm decides to avail of external funds, again an element of Pecking Order is followed. To quote Meyers, "they (firms) start with debt, then possibly hybrid securities such as convertible bonds, then perhaps equity as a last resort' (Meyers, 1984: 581). It suggests that the corporate sector prefers to borrow first without issuing securities of any kind, but agree to pay interest, then borrow by issuing bonds which again results in paying interest and then finally, raise funds by issuing equity, which entails sharing ownership. In situations where firms are reluctant towards raising funds by sharing ownership, investment would be reduced if other forms of external funds are not available to them. Consequently, borrowing becomes a crucial form of external finance to firms, since it does not require sharing of ownership but only requires paying interest.

When a firm decides to borrow, it necessarily relies on the savings of savers. Such saving can be mobilized either directly by issuing claims to the savers or indirectly by relying on institutions which mobilize savings. In this context, the role of banks's finance in relation to other sources of funds has been examined.

SECTION II

Financing Pattern of Private Corporate Sector:

The role of banks' finance in the overall pattern of financing of the private corporate sector is examined by analyzing the relative shares of different sources of funds. Data for analysis have been collected from RBI's Studies on Finances of Non-Government and Non-Financial Public and Private Limited Companies which is periodically published in the RBI Bulletin[1].

Table 3.1 and Table 3.2 bring out the relative shares of different forms of financing pursued by public and private limited companies respectively. In these tables, the sources of funds are classified as internal and external. Internal sources consist of paid-up capital, reserves & surplus and provisions. External funds comprises of fresh issue of capital, borrowing, trade credits and 'Others' which includes capital receipts and non-current liabilities.

---

[1]. The public limited companies covered by the latest RBI's Study of Finances of Public Limited Companies, 1989/90, account for 52.4 per cent of all non-government non-financial public limited companies in terms of paid-up capital as at the end of March 1990 (RBI Bulletin, 1992: 1709). As for the private limited companies, the coverage, for the latest study 1988/89, is to the extent of 6.4 per cent of the total paid-up capital of all non-government non-financial private limited companies (RBI Bulletin, 1992: 965).

Table 3.1

Relative Shares of Different Sources of Funds
Of Public Limited Companies: 1970/71 to 1989/90

(In Percent)

Sources of Funds	1970/71 to 1974/75	1975/76 to 1979/80	1980/81 to 1984/85	1985/86 to 1989/90
Total Funds (A+B)	100	100	100	100
A. Internal Funds: (a+b+c)	57.1	42.9	35.3	31.8
a. Paid-up Capital	4.2	6.0	2.2	2.1
b. Reserves & Surplus	15.2	7.1	9.9	5.4
c. Provisions	37.7	29.8	23.2	24.2
B. External Funds: (d+e+f+g)	42.9	57.1	64.7	68.2
d. Fresh Issues	2.2	2.5	2.6	7.5
e. Borrowing	16.3	27.9	35.7	38.2
f. Trade Credits	24.5	26.5	26.0	22.4
g. Others	neg	neg	neg	neg

Note: a. neg indicates negligible
b. 'Others' includes capital receipts and other non-current liabilities.

Source: Various issues of RBI Bulletin.

A continuous decline in the share of funds generated from internal sources in the total funds, since the early 70s is discernible from Table 3.1. An analysis of the different components of internal sources reveals that the share of capital is low, while that of provisions has been quite high. The reserves & surplus reflect the retained earnings of the corporate sector. It is seen that the funds from this source has fallen quite sharply.

The significance of external sources of funds is evident from its increasing share in total funds (see Table 3.1). While external funds raised through fresh issues of shares are limited and remains at less than 3 per cent of total funds till the mid-80s, it shows a sudden spurt and increases to 7.6 per cent in the post eighties. This may be due to policies initiated by Government to encourage growth of capital market in the country.

It can also be seen from Table 3.1 that the role of borrowing has increased not only among other sources of external funds, but its share is even higher than the whole of internal funds, since the mid-70s. It suggests that public limited companies of the private corporate sector have increased their reliance on borrowing in relation to other sources of finance.

The other major source of external funds, trade credit, accounts for about 25 per cent of total funds and comprises mostly of sundry creditors. Its share in total funds remained constant till the mid-80s and declined since then. However, when its contribution is assessed against that of increasing share of external funds, it is apparent that its role as an external source is diminishing. To illustrate, the percentage share of trade credit in external funds fell from nearly 62 per cent in the early 70s to 33 per cent in the late 80s. However, its share in external funds has declined continuously since the early 70s. The use of capital receipts and other liabilities, representing 'Others' in Table 3.1, has been negligible, the magnitude being less than half a per cent.

Having studied public limited companies, the financial behaviour of private limited companies is examined. Table 3.2 shows the relative share of various sources of funds in total funds of private limited companies during the last two decades.

Table 3.2

Relative Shares of Different Sources of Funds of Private Limited Companies: 1970/71 to 1988/89

(In Percent)

Sources of Funds	1970/71 to 1974/75	1975/76 to 1979/80	1980/81 to 1984/85	1985/86 to 1988/89
Total Funds (A+B)	100	100	100	100
A. Internal Funds: (a+b+c)	42.1	35.2	35.3	31.1
a. Paid-up Capital	2.4	2.4	1.0	0.6
b. Reserves & Surplus	11.4	4.4	8.4	6.8
c. Provisions	28.3	28.4	25.9	23.7
B. External Funds: (d+e+f+g)	57.9	64.8	64.7	68.9
d. Fresh Issues	2.1	2.0	1.3	2.0
e. Borrowing	26.8	23.9	26.9	31.9
f. Trade Credits	28.9	38.8	36.0	34.6
g. Others	neg	neg	neg	neg

Note and Source: Same as Table 3.1

Like the public limited companies, the private limited companies too display a diminishing use of internal funds. Amongst internal funds, the use of capital remains constant in the 70s, but gradually reduces to less than one per cent of total funds during the late 70s. The use of reserves & surplus, reflecting the use of retained earning also dwindles. The use of provision also remains

constant like that of paid-up capital during the 70s, but has declined since then.

The share of external funds increases in the mid-70s, then remains constant till mid-80s, wherefrom it again rises. A break-up of its share shows that the share of fresh issues has fallen till the mid-80s to a mere two per cent. Borrowing has become a prominent external source during the 80s, although it is slightly less than that of trade credit. Trade credit which accounted for about 29 per cent in the early 70s has increased its share during the late 70s to 39 per cent. However, its share has declined during the subsequent periods and was about 35 per cent in the post eighties. Its contribution to total funds, however, has remained quite high vis-a-vis other sources especially since the mid-70s. As observed in case of public limited companies, the contribution of 'Others', inclusive of capital receipts and current liabilities, at less than half per cent, is negligible.

The above analysis of pattern of financing of both public and private limited companies suggests that the use of external funds has increased. Moreover, break-up into shares of different forms of external funds reveals the growing importance of borrowing as an external source with a corresponding decline in the significance of trade credit.

Predominantly, firms borrow either to meet working capital requirements (short-term) or for long-term investment. These funds may be secured or other ways in which borrowing can be undertaken is either by issuing securities like debentures or by attracting

deposits directly from savers, or indirectly through various institutions. The advantage of borrowing directly is that the use of availed funds is at the discretion of the corporate sector, while use of resources availed from institutions require a kind of project scrutiny by the institutions that supply funds (Mohanty, 1986: 60). To get more insight into the nature and pattern of borrowing, an institution-wise analysis is made (see Table 3.3).

Sources of Borrowing:

The RBI's studies on Company Finance gives break-up of lending by a) banks, b) other financial institutions both Indian and Foreign, c) Government and Semi-Government Bodies, d) Indian and Foreign Companies and e)'Others'. From 1980/81, these studies also give details of borrowing made through issue of debentures and through public deposits. The latter is included in the item 'Other'. As the relative share of borrowing from Government and Semi-Government Bodies, and Indian and Foreign companies has been found to be very low, they have been included under the category 'Others' as it appears in Table 3.3. The year 1972/73 has witnessed a negative flow of funds from banks and other financial institutions in case of public limited companies. As the inclusion of the published data of this year would distort the average of the period 1970/71 to 1974/75, the mean values of the years 1971/72 and 1973/74 has been taken.

Table 3.3

Relative Shares of Different Sources of Borrowing Of Public and Private Limited Companies: 1970/71 to 1989/90

(In Percent)

Sources of Borrowing	1970/71 to 1974/75	1975/76 to 1979/80	1980/81 to 1984/85	1985/86 to 1989/90
PUBLIC LTD. COMPANIES: Total Borrowing (a+b+c)	100	100	100	100
a. Banks	71.7	56.7	30.1	35.7
b. Other Financial Institutions	-3.9	13.4	25.9	24.2
c. Others	32.2	29.9	44.0	40.1
PRIVATE LTD. COMPANIES: Total Borrowing (a+b+c)	100	100	100	100
a. Banks	75.6	71.7	62.0	65.6
b. Other Financial Institutions	4.9	11.1	7.2	10.6
c. Others	19.5	17.2	30.8	23.8

Note: 'Others' include borrowing from Government and semi-Government Bodies, Indian and Foreign Companies and Other.

Source: Same Table 3.1.

Table 3.3 shows that borrowing from banks both by public and private limited companies steadily declined till the mid eighties after which it shows an increase. Yet, banks do provide a high proportion of total funds, more so in the case of private limited companies. In case of public limited companies, the relative share of other financial institutions has increased sharply between the mid-70s and mid-80s, accounting for nearly one-fourth of total borrowing during the 80s. However, their role in providing finance to private limited companies does not seem to be very significant.

In category `Others' in the case of public limited companies, the contribution from Government and Semi-Government Bodies has been quite insignificant at less than one per cent of total borrowing except in the late 70s when its share was nearly 9.5 per cent. As for private limited companies, its share was less than two per cent during the 80s. Data on borrowing from Indian and Foreign companies is available only for the last two years. In any case, their contribution was less than three per cent of total borrowing. Given the insignificant contribution from these sources, it appears that the magnitude of `Others' has been mainly influenced by sources like public deposits.

Since the item 'Others' has become a significant source of borrowing, a brief discussion on public deposits, to which the increase in 'Others' could be attributed, is needed to discern its role in providing funds. Secondary literature (Mohanty 1986: 65-77) shows a growing reliance on public deposits during the 70s, despite being brought under stringent credit regulatory measures. The growth rate of public deposits had been of the order of 18 per cent between 1966 and 1981, except during the late 70s, when it was 19.5 per cent. Private sector held more than 95 per cent of these deposits, of which the public limited companies alone accounted for more than 85 per cent. He has argued that this growing reliance on public deposits was mainly due to low cost, convenience in raising funds and decreasing availability of alternative source of funds.

Hence, it is possible that the spurt experienced in public deposits accepted by private corporate sector would have boosted the share of 'Others' in the total borrowing as seen in Table 3.3. The RBI's

Studies on Company Finance gives data on public deposits only from 1980/81 onwards. An analysis of their relative share in 'Others' since then shows that from 15 per cent in the early 80s, it has declined gradually to around 3 per cent in the late 80s. The declining share of `Others' may therefore, be a reflection of the trends in the share of public deposits. As detailed break-up of 'Others' is not available, it handicaps any further enquiry into the nature of sources that contribute to this item.

Table 3.3 also indicates the private corporate sector's demand for finance from banks. The earlier analysis of relative shares of various components of external sources showed that the share of borrowing has been increasing over the years. The contribution of banks to borrowing, nevertheless, shows a declining trend since the early 70s and an upward trend since the mid-80s. Public limited companies, as indicated by Table 3.3, have become less dependent on banks for funds - as the share of borrowing from banks in total borrowing has declined from nearly 71.7 per cent during early 70s to 30.1 per cent during early 80s, which subsequently rises to 35.7 per cent. The private limited companies also show a similar declining share of bank funds to total borrowing, from 75.6 per cent in early 70's to 62 per cent during early 80s and since then it marginally rises to 65.6 per cent.

Although, both public and private limited companies have become less dependent on banks for finance till the mid-80's, a marginal rise in their dependence is seen. While less than one-half of borrowing has come from banks in case of public limited companies, it was nearly two-thirds for private limited companies. This also

indicates that public limited companies are making use of other sources of finance more than private limited companies.

To summarize, private corporate sector has become less reliant on banks for finance, although a reversal is evident since the mid 80s. As the shares of other forms of borrowing have declined during the late 80s, it can be concluded that the spurt experienced in total borrowing since mid-80s was influenced mostly by the larger inflow of funds from banks.

Having examined the role of finance from banks as against other sources of funds, certain ratios in relation to bank credit are examined. The computed ratios for both public and private limited companies is presented in Table 3.4.

Table 3.4

Important Bank Borrowing Related Ratios of Public and Private Limited Companies: 1970/71 to 1989/90

Ratios	1970/71 to 1974/75	1975/76 to 1979/80	1980/81 to 1984/85	1985/86 to 1989/90
PUBLIC LTD. COMPANIES				
SBB / BB	92.64	90.71	82.11	79.60
Term Loan / BB	7.36	9.29	17.89	20.40
SBB / Inventories	50.65	50.51	43.32	49.36
Term Loan / NFA	3.58	4.84	7.08	6.98
BB / Inventories	54.64	55.69	52.90	61.99
Inventory / Total Asset	34.43	34.15	30.54	24.26
NFA / Total Assets	38.23	36.52	39.85	43.99
PRIVATE LTD. COMPANIES				
SBB / BB	92.06	88.86	87.19	81.43
Term Loan / BB	7.94	11.14	12.81	18.57
SBB / Inventories	62.81	57.97	55.45	60.95
Term Loan / NFA	6.98	10.01	11.40	16.28
BB / Inventories	68.25	65.26	63.62	74.94
Inventory / Total Asset	34.12	35.39	35.07	30.77
NFA / Total Assets	26.49	25.72	24.86	26.41

Note: BB = Bank Borrowing; SBB = Short-term Borrowing from Banks; NFA = Net Fixed Assets

Source: Same as Table 3.1.

In the previous chapter, the term component of credit supplied by banks was found to be increasing. An analysis of its share in total bank borrowing shows that it has increased over the years for both forms of companies. The obverse of this as seen in the SBB/BB ratios which show that short-term credit has declined (see Table 3.4).

Investment in fixed assets reflect long-term investment. The share of net fixed assets (NFA) in total assets is around 40 per cent and around 30 per cent in case of public and private limited companies

respectively. While this ratio increased for the public limited companies in the 80s, it remained more or less constant for the private limited companies. Normally, such investments are financed via long-term borrowing, so that the repayment of borrowed capital can be spread over a longer period. The role of bank credit in financing such investment can be gauged by studying the ratio of term credit to these assets. As is apparent from Table 3.4, the ratio of term loan to NFA shows an increasing trend, implying an increasing participation of banks in the long-term capital formation of the private corporate sector. Although the magnitude is not very significant for public limited companies, it has risen to about 16 per cent for private limited companies in the eighties from a mere 7 per cent in the seventies.

To have a more disaggregated picture of the financing pattern, the pattern of financing followed by different size classes of firms within this sector is examined.

SECTION III

Size-wise Analysis:

Based on paid-up capital, RBI has classified firms into three groups, namely, small companies having paid-up capital of less than Rs. 5 lakhs; medium companies[2] with paid-up capital of Rs. 5 lakhs

---

[2]. Further classification of medium companies are i) Rs. 5 lakhs - Rs. 10 lakhs; ii) Rs. 10 lakhs - Rs. 25 lakhs; iii) Rs. 25 lakhs - Rs. 50 lakhs; and, Rs. 50 lakhs - Rs. 1 crore.

to Rs. 1 crore; and, large companies[3] whose paid-up capital is Rs. 1 crore and above[4].

Other studies (Rosen, 1962; Bagchi, 1962 and Gupta, 1969) show that medium range companies have placed more reliance on banks for funds than small and large companies, before nationalisation. Gupta (1969: 31-32) holds that the influence of size can work from supply as well as from the demand side. On the supply side, the influence of size seems to be particularly important in the case of smaller firms which are generally regarded by lending institutions as poor credit takers. At the other end of the scale are the larger enterprises which enjoy much better access to other sources of finance, including internal accretion of funds and therefore, have less need for bank credit. Gupta also shows empirically that bank credit plays a relatively lesser role in financing both small and large firms as compared to medium-sized enterprises.

The argument for rating small companies as poor credit takers may be attributed to the lending policies of commercial banks, which were mainly governed by physical security and personal guarantee (Rosen, 1962:17). However, over the years, with nationalisation of banks, the approach to regulation of credit to industry by RBI has

---

[3]. RBI classifies the large companies into five, namely, i) Rs. 1 crore - Rs. 2 crores; ii) Rs. 2 crores - Rs. 5 crores; iii) Rs. 5 crores - Rs. 10 crores; iv) Rs. 10 crores - Rs. 25 crores; and, v) Rs. 25 crores and above.

[4]. An analysis of the coverage of each size groups in terms of their paid-up capital shows that large companies account for more than 90 per cent of the paid-up capital of the companies covered in the RBI's Studies on Company Finance.

undergone significant changes. Sukhamoy Chakravarthy Committee, in their review of lending policies of RBI, made an important observation with regard to the credit policy. To quote, "the basis of bank lending should be changed from security based lending to lending based on funds flow" (RBI, 1985: 188). If lending is based more on funds flow, then the changes in policies will be favourable to small companies, since sources of funds for smaller firms is limited. Schmidt (1952:36) argues that small companies have little access to the security market and they are dependent for their initial capital upon owners' personal savings or investment by their relatives, friends or business associates; and upon retained earnings and long-term bank credit for further expansion. The role of banks in providing funds to small companies therefore assumes significance.

Further, with the changes in approach to lending, as observed by the Sukhamoy Chakravarthy Committee, one would expect that the trend prior to nationalisation with regard to the role of banks in financing different size groups would have reversed. It is against this background, that the dependency of different size groups on banks is examined.

Table 3.5 gives the details of various sources of funds across different size groups.

Table 3.5

Relative shares of Various Sources of Funds Across Different Size Classes: 1971/72 to 1989/90

(In Percent)

SIZE GROUPS (IN RS)	1971/72 to 1974/75	1975/76 to 1979/80	1980/81 to 1984/85	1985/86 to 1989/90
A. External Funds to Total Funds:				
Less than 5 lakhs	44.0	--	--	102
5 to 10 lakhs	79.2	90.9	72.3	21.5
10 to 25 lakhs	67.1	102.1	82.6	75.4
25 to 50 lakhs	69.3	116.9	84.2	73.2
50 lakhs to 1 crore	65.0	93.1	78.1	83.8
1 crore to 2 crores	59.3	82.6	79.4	83.8
2 crores to 5 crores	46.0	70.2	70.9	77.7
5 crores to 10 crores	48.6	63.4	66.3	71.5
10 crores to 25 crores	--	--	65.8	71.9
25 crores and above	--	--	53.1	61.3
B. Borrowing to External Funds:				
Less than 5 lakhs	27.9	--	--	122.8
5 to 10 lakhs	39.2	34.5	31.5	2.7
10 to 25 lakhs	12.5	48.4	40.9	52.5
25 to 50 lakhs	33.9	55.6	53.0	61.1
50 lakhs to 1 crore	37.1	48.9	50.3	55.4
1 crore to 2 crores	43.7	49.4	43.4	61.1
2 crores to 5 crores	17.8	34.7	40.6	49.0
5 crores to 10 crores	30.6	52.2	61.4	60.0
10 crores to 25 crores	--	--	61.8	75.4
25 crores and above	--	--	141.6	82.0
C. Bank Borrowing to Total Borrowing				
Less than 5 lakhs	67.3	--	--	61.6
5 to 10 lakhs	94.4	97.6	37.6	92.1
10 to 25 lakhs	89.3	75.4	66.0	59.5
25 to 50 lakhs	111	72.0	49.1	59.2
50 lakhs to 1 crore	-598	70.8	50.2	60.7
1 crore to 2 crores	39.9	47.8	24.4	47.6
2 crores to 5 crores	348	50.8	37.5	42.3
5 crores to 10 crores	22.1	48.3	20.0	31.5
10 crores to 25 crores	--	--	23.7	24.4
25 crores and above	--	--	7.3	30.8

Source: Same as Table 3.1

From the Table 3.5, it is evident that there is high dependency on external funds by all size groups, which has increased over time. While the rise has been consistent throughout the period of analysis for the larger size groups, there has been fluctuations in the case of smaller and medium size groups. The Table 3.5 also shows that the bulk of external funds has come from borrowing for most size groups.

Given the increasing reliance on borrowing, it will be worthwhile to find the share of banks in the total borrowing. It can be seen from Table 3.5 that, although the bulk of borrowing has come from banks, its share in total borrowing declined till the mid 80s in the case of almost all size groups. However, its share has increased since the mid-80s for most size groups. Thus, the importance of banks as a source of borrowing declined till the mid-80s for almost all size groups, even though the share of total borrowing in external funds increased during the same period. It is also seen from the Table 3.5 that as the size of companies increases the magnitude of the share of bank borrowing gets reduced. It suggests that differences exist in the dependency on banks among different size groups within private corporate sector.

The above analysis revealed that as the size of companies increases, the reliance placed on banks gets reduced in relation to total borrowing. Does this imply that the share of these size-groups in the total amount of bank credit disbursed is less? The following analysis addresses this question. The analysis is carried out only for the last five years, and broadly for small, medium and large companies. The methodology followed to adjust the

data needs some mention as data available precludes building up population estimates for each size groups.

Bank borrowing by these size classes are divided by the number of companies covered under these categories and thus, per firm bank borrowing is obtained for each of these groups. The obtained values for these size groups are then summed up to arrive at the total bank borrowing across all size classes. The relative share of each size groups in this total is then worked out. The Table 3.6 gives the relative share of these size groups along with some worked out ratios.

Table 3.6

Size-wise Distribution of Bank Borrowing:
1985/86 to 1989/90

(Percentage Share)

	Small Companies	Medium Companies	Large Companies
a. Bank Borrowing (BB)	0.77	14.80	84.43
Other Ratios:			
BB / Inventories	54.50	76.96	59.65
NFA / TA	22.74	35.50	44.98
Inventories / TA	20.84	30.96	23.60

Notes and Source: Same as Table 3.4

It can be seen from Table 3.6 that the share of small companies in total bank borrowing accounts for 0.77 per cent. The medium range companies have a share of 14.8 per cent, while the rest have gone to larger companies. This shows that though the dependence on banks as a source of finance is low, in absolute terms, the bulk of banks credit goes to the larger size groups.

The ratio of bank borrowing to inventories of larger companies is less than that of medium size companies. It implies that although this group had the largest share in total bank borrowing, its dependency on banks for inventory financing is comparatively lower than other groups.

The higher ratio of bank borrowing to inventory for the medium size companies as compared to large companies appears to be an enigma. It tends to suggest that this size class has not reduced its dependence on banks for financing inventories. Going by the ratio of inventory to total assets, it appears that excess inventory holding by medium size companies has resulted in their higher dependency on banks. And, hence, the higher ratio of bank borrowing to inventories than other two groups. It is this excess holding of inventory that the Tandon committee intended to discourage.

The small companies have a low ratio of inventory to total assets implying that this size group could not maintain or invest enormous amount in inventories like the other two size classes, probably because of limited resources. The bank borrowing to inventory ratio was also lower than that of the other two classes suggesting that banks financed only a small portion of its inventories. The higher dependence on bank borrowing when compared to larger companies suggests that their options for alternative sources of borrowing was even more bleak.

Summary of the Chapter

To sum up, it is seen that the private corporate sector's dependence on external funds and borrowing in particular had increased during the last two decades. While bank borrowing is still a significant source of borrowing in private corporate finance, the role of banks has been declining in importance although there is slight increase in its significance since the mid-80s. The size-wise analysis showed that as size increases, the dependence on banks finance decreases. The relative share of different size groups also revealed that the small companies having paid-up capital of less than Rs. 5 lakhs got a small share of less than one per cent in bank funds while the bulk of it went to the companies with paid up capital of more than Rs. 5 crores.

The growing share of external funds in total funds and more importantly that of borrowing suggests that there was no dearth of demand for external funds to lead to a reduction in the reliance placed on banks. It is also seen that since the mid-80s the overall bank credit to industry has been increasing. Since banks are functioning within the framework of a regulated financial system, it is possible that the changes in the role of banks as an external source of funds and as a source of borrowing could be due to changes in the polices or it could be due to other factors. Thus, it becomes crucial to understand what factors determine the demand for bank funds. The next chapter, therefore, tries to examine the determinants of borrowing from banks.

CHAPTER IV

DETERMINANTS OF BORROWING FROM BANKS

The analysis of bank finance to private corporate sector in the preceding two chapters has emphasised the need to examine the determinants of borrowing of this sector from banks. As a prelude to such an analysis, some of the theoretical issues as well as a few empirical studies on corporate finance are examined to broadly understand the factors that influence firms to go for external funds in general, and banks in particular. It would thus, help to identify the determinants of private corporate sector's demand for finance from banks. Section I reviews the theoretical literature and draws the various hypotheses to be tested in this connection and Section II examines its empirical validity.

Section I

Review of Literature:

Investment precedes the production of output. The behaviour of investment is determined by real as well as financial variables. The real variables include capacity utilization, changes in output, sales and so on, while financial variables consider the availability of funds to finance investment activities (Jorgenson, 1971:1130). Empirical studies on Indian corporate sector also confirm the interplay of real and financial variables in determining the investment expenditure of this sector (Sastry, 1975:62; Krishnamurthy and Sastry, 1975:152-155; Venkatachalam and Sarma, 1978:82; Sharma, 1991:69-72).

Given the context of the present study, our concern will be limited to the role financial variables in influencing the investment decision of a firm. The problem of financing investment leads a firm to explore different sources of mobilizing resources. Each of these sources has its own relevance and influence on the functioning of corporate sector (Balakrishan, 1966:1449).

As stated earlier, though internal sources are the cheapest and beset with least risk, it may not be sufficient to finance the planned investment of a firm. Kuh argues that investment decisions, based on the extent of availability of internal funds limit the growth of the firm. Considering its insufficiency to finance investment activity for long-run growth, it is imperative for a firm to mobilise funds from external sources. External funds therefore, are indispensable when the investment requirement is in excess of what could be financed by internal funds. It follows then, that the use of internal funds should be inversely related to external funds, as the larger availability of funds from internal sources reduces the demand for external funds (Krishnamurthy and Sastry, 1975:85, Venkatachalam and Sarma, 1978:82).

External sources are resorted to when internal funds cannot fully meet the financial requirements arising out of investment, long-term or short-term. While long-term investment takes the form of investment in fixed assets to facilitate expansion, diversification, etc., short-term investment involves investment in current assets, normally termed as working capital, essential for the day-to-day operations. As investment in these assets are crucial for achieving the objectives of firms, a positive relation

can be expected to exist between investment in both fixed assets and current assets, and the demand for funds and hence, external funds (Dhrymes and Kurz, 1967:436; Krishnamurthy and Sastry, 1971:183; Krishnamurthy and Sastry, 1975:152; Sastry, 1975:66; Venkatachalam and Sarma, 1978:82).

There are different external sources to which a firm may resort, to mobilize funds. The issue of fresh capital, borrowing and trade credits constitute the chief means of securing external funds, of which borrowing, more importantly from banks, is the focus of the present study.

In the Indian context, banks, even traditionally, have been one of the important sources of short-term finance (Athawale, 1975:327). Recourse to bank credit is essentially taken to finance inventory holdings, the most important short-term capital requirement (Ambegaokar, 1969:1553), to maintain a minimum level of production. rather than to finance fixed assets which are normally funded by long-term borrowing from other financial institutions. This postulates a positive relationship between demand for finance from banks, and investment in inventories.

Although taking recourse to external sources for funds is inevitable, it involves some elements of cost. The costs usually associated with it are dividends on fresh issue of equities, interest on borrowing and so on. Thus, there exists a significant relationship between demand for external funds and their cost, under circumstances where cost of capital may be below its opportunity cost due to regulations and control (Agarwal,

1987:145). It implies that, given the goal of maximising difference between capitalised value of income and the cost streams associated with any investment, rate of interest would determine the scale of investments (Bhole, 1972: 581). Thus, the cost of funds may be considered to be another determinant of external funds in as much as they exert a negative influence on the demand for external funds (Dhrymes and Kurz, 1967:436). The cost associated with bank credit is the interest rate, and hence it may be postulated that the rate of interest is inversely related to bank borrowing.

This factor may not be really important when interest rates are below their shadow rate on account of regulation and control (Krishnamurthy and Sastry, 1975:78). When quantitative controls exercise more influence than interest rate, availability of funds may become a prime factor rather than its cost. As interest rates in India are administered, one may find that their temporal variability to be negligible and therefore, may not register their influence (Krishnamurthy and Sastry, 1975:78). Some empirical studies (Bhole, 1972:593; Sharma, 1991:100) also argue in a similar vein.

However, the demand for bank credit might continue to increase despite a rise in the rate of interest of banks, if the cost of alternative source of borrowing increases even more than the rate of interest of banks. In other words, demand for bank credit would depend upon the interest rate on advances relative to the cost of alternative source of borrowing (Khusro and Siddhartan, 1972:16). Hence, if the relative cost, that is, the ratio of cost of

alternative sources of borrowing to banks, is positively related to bank borrowing, then the proposition regarding cost of alternative source of borrowing holds good. On the contrary, if such a ratio is negatively related, then, neither the advance rate of banks nor the relative cost of alternative sources matter, but only the availability of funds. Under these circumstances, taking recourse to banks depends on availability of funds rather than the cost factor.

Potential demand for finance need not be fully met by banks if their lending is controlled by various regulatory measures. It was seen earlier that the deployment of resources by banks since their nationalisation, has been regulated by various credit control measures. Among these, `priority sector lending' and the upward increase in reserve requirements by way of Statutory Liquidity Ratio (SLR) and Cash Reserve Ratio (CRR) are the key measures that could have reduced the quantum of resources made available by banks to the private corporate sector during the period under the study, that is from 1970/71 to 1989/90.

It was also seen that industries became vulnerable to newer credit control measures introduced on the line of the suggestions made by Tandon Committee in 1975, primarily relating to fixing inventory norms and method of lending so as to ensure that part of current assets are financed by owned funds and long-term loans (RBI, 1975:27-29). Borkar (1989:10-11) observed that bank credit to industry fell since the implementation of these norms in 1975. Thus, it is possible that the implementation of these norms would have eventually influenced the borrowing of this sector from banks.

Section II

The Model:

In the light of the discussion in Section I, borrowing from banks by the private corporate sector would depend on the following variables, that is,

$$BB = f\ (INV,\ UIF,\ ROI,\ CCM) \qquad \text{----------} \quad (1)$$

where

BB = Bank Borrowing of private corporate sector;

INV = Inventories;

UIF = Internal funds;

ROI = Rate of interest; and,

CCM = Credit control measures.

As has been mentioned, the important determinants are inventories, internal funds, the cost of borrowing and credit control measures. The decision to invest in inventories increases the borrowing from banks as they are short-term in nature and hence, would have a positive relation with borrowing from banks. The availability of internal funds and the cost are postulated to reduce the borrowing from banks. The implementation of Tandon norms along with other credit control measures has been hypothesized to have reduced the borrowing from banks. The specification of the independent variable would be $f_I > 0$; $f_U < 0$; $f_R < 0$ and $f_C < 0$ where f_1 denote the first order derivatives of the dependent variable with respect to the independent ones.

Data, Methodology and Estimation:

It was observed in the earlier chapter that the share of bank borrowing has been declining in relation to total borrowing. To explain this trend, the proportion of borrowing from banks to total borrowing is used as a proxy for the role of banks' finance. The use of internal funds has been compiled by adding up use of capital, provisions and reserves & surplus. Investment in inventories has been taken to include funds used to invest in raw materials, work-in-progress, finished goods and stores and spares.

The rate of interest is collected from 'Structure of Interest Rates in India' in `Report on Currency and Finance'. As data on the flow of funds through issue of debentures is available only from late 70's, and its share in borrowing is less than that of borrowing from other financial institutions, the lending rate of Industrial Development Bank of India (IDBI) is taken as a proxy for the cost of alternative sources of borrowing. Strictly speaking, borrowing from banks is short-term in nature, while that from other financial institutions is long-term in nature and hence, their lending rates are not comparable. As a better proxy, namely,the bazaar bill rate, reflecting the interest rate of short-term borrowing, is not available from late 70's, the lending rate of IDBI is used[1].

---

[1]. Venkatachalam and Sarma (1978) had used bazaar bill rate to reflect the cost of alternative source of borrowing since it was available for the periods of their study. Rao (1988) had used interest on debentures to represent the cost of alternative sources of borrowing.

Moving on to policy variables, one possible way to take into account the influence of these measures, is by introducing time variable 't', in the functional form (1) measured in time periods, from 1970/71 onwards.

Specifying the functional equation (1) as a linear function:

$$ROB = \alpha_0 + \alpha_1 \, INV + \alpha_2 \, UIF + \alpha_3 \, ROI + \alpha_4 \, t \qquad \text{----(2)}$$

where α_0, α_1, α_2, α_3 and α_4 would denote the coefficients of the respective independent variables. The estimate of equation (2) is given below:

a) $ROB = 97.33 + .0071 \, INV - .0032 \, UIF - 2.31 \, ROI - 1.79 \, t$

(5.59)* (1.54) (-.65) (-1.17) (-1.05)

$R^2 = .758$; DW = 1.58; F.stat = 11.74; N = 20.

* indicates level of significance at 1 per cent;
Figures in parentheses are the t-values.

Though the R squared value is quite high, the co-efficient of none of the explanatory variables is significant. Testing for multicollinearity, a high correlation was found between interest rate of banks (ROI) and all other independent variables. Given the problem of using the instrumental variable method for correcting multicollinearity, another definition had been used to reflect cost, namely, the relative cost of borrowing in lieu of interest rate of banks (ROI). Accordingly, the alternative formulation of the equation (2) would be:

$$ROB = \alpha_0 + \alpha_1\ INV + \alpha_2\ UIF + \alpha_3\ BAR + \alpha_4\ t \qquad ----(3)$$

where BAR is the relative cost of alternative source of borrowing to advance rate of banks. The estimated equation is:

b) $ROB = 94.33 + .0049\ INV + .001\ UIF - 17.36\ BAR - 3.83\ t$

$(2.82)^* \quad (1.03) \quad (0.22) \quad (-0.49) \quad (-3.88)^*$

$R^2 = .739$; DW = 1.66; F.stat = 10.67; N = 20.

* indicates level of significance at 1 per cent;
Figures in parentheses are the t-values.

In the above regression results (b), the variable 't' shows a significant negative trend. The equation also shows that only the co-efficient of `t' is significant. One possibility is that `t' may be a dominant variable. This can be tested by estimating the trend equation alone. The trend equation is given below:

c) $ROB = 74.26 - 2.47\ t$

$(14.06)^* \quad (-5.61)^*$

$R^2 = .636$; DW = 1.56; F.stat = 31.44; N = 20.

* indicates level of significance at 1 per cent;
Figures in parentheses are the t-values.

Since the trend alone explains about 64 per cent of the variation, we have a case of dominant variable. Therefore, equation (3) is estimated without the dominant variable.

Since 't', a proxy for all other effects including the policy variable, is dropped from the specification, we have introduced a dummy variable to capture the effects of the implementation of

Tandon Committee recommendations, the most important credit control measures introduced during the period. This has, in principle, put a squeeze on credit for inventory purposes. This impact is measured as slope effect, using the dummy variable method. Since the Tandon recommendations were implemented in 1975, the dummy variable is defined as:

D_1 = 1, 1975/76 to 1989/90; and,
= 0, otherwise.

The inventories effect is captured by defining a new variable:

$$D_1 * INV = DINV$$

Obviously, we would expect a negative coefficient for DINV, if the credit squeeze has affected the behaviour after the implementation of the recommendations of Tandon Committee. Accordingly, equation (3) is rewritten as:

$$ROB = \alpha_0 + \alpha_1 \, INV + \alpha_2 \, DINV + \alpha_3 \, UIF + \alpha_4 \, BAR \qquad \text{----(4)}$$

The estimated equation is:

d. $$ROB = \underset{(.44)}{13.78} + \underset{(2.95)^{*}}{.0321 \, INV} - \underset{(-2.12)^{**}}{.0233 \, DINV} - \underset{(-2.21)^{**}}{.009 \, UIF} + \underset{(1.31)}{46.88 \, BAR}$$

R^2 = .599; DW = 1.23; F.stat = 5.61; N = 20.

* indicates level of significance at 1 per cent; and,
** indicates level of significance at 5 per cent;
Figures in parentheses are the t-values.

Discussion:

The variable `t', denoting time, seems to have exerted a negative influence on the role of banks. The significant negative role played by variable 't', introduced to capture the effect of both qualitative and quantitative credit control measures, shows that these control measures have a significant impact on the role of banks. This suggests that the declining role of banks is significantly explained by the credit control measures. However, as it is found that `t' is a dominant variable, making all other variables insignificant, the equation is again estimated, excluding the time variable `t'.

The Tandon Committee norms have been postulated to have reduced the role of banks. Its influence would be greatly felt in inventories holding, as Tandon Committee defines norms for the level of inventory holding which could be financed by banks. The introduction of a dummy variable to capture this effect reveals that it has had a significant impact on the role of banks. Hence, it can be concluded that true to its objectives, the policies have been effective in reducing the role of banks in financing the private corporate sector.

The review of theoretical issues shows that the use of internal funds would reduce the reliance placed on external funds. Banks being an external source of funds, it was postulated that the use of internal funds would reduce the dependence placed on banks. The empirical results show that this variable has not been significant when variable `t' is included in the equation. As mentioned, `t'

is a dominant variable. Hence, when `t' is omitted, the results confirm the earlier conjecture (equation d). It suggests that the policy measures which reduced the quantum of finance made available to the private corporate sector have led this sector to use of more of internal funds. Thus, as expected by the Committee, the internal funds have been replacing banks' finance.

Moreover, the cost factor appears to have hardly any influence on the role of banks. The relative cost of alternative source of borrowing is also found to be insignificant in influencing the role of banks, although the expected signs emerge.

Summary of the Chapter

The analysis clearly shows that the proportion of bank credit going to the private corporate sector has a downward trend. Moreover, it has been a dominant variable in the estimation. This has made all other financial variables that influence bank credit insignificant in the regression's analysis. However, the exclusion of trend variable indicates that the proportion is particularly influenced by inventory requirement, negatively by internal fund. The cost of borrowing is not significant in any equation. Finally, the implementation of the recommendations of Tandon Committee has a negative influence on the bank credit as is expected.

CHAPTER V

SUMMING-UP

The success of recent policy changes, seeking to give a greater role to market forces in the Indian economy, depends to a large extent on the adequate provision of infrastructural facilities. Central to this, as pointed out by the Narasimham Committee, is efficient financial intermediation, to ensure proper allocation of financial resources. Hence, in the present changing scenario, an understanding of the role of institutions which perform such intermediation becomes imperative. The present study is an endeavour in this direction. It attempts to examine the role of one such important institution, namely, commercial banks, in financing an important deficit sector, the private corporate sector.

The study begins by setting out the role of the financial system and its central place in the growth and developmental process of an economy. It is observed that the Indian economy has witnessed significant development in the sphere of its financial system and that it has played a crucial role in mobilising savings. An examination of sector-wise mobilisation of resources has revealed the significant role of the financial sector and the dominant place of banking system within it.

A sector-wise analysis of financial balances brings out the fact that private corporate sector is a large deficit sector in the economy, second only to the Government. Though household sector is the largest surplus sector in the economy, it is found that its

link with the private corporate Sector is rather weak. Hence, a link is postulated between private corporate sector and banks, the largest mobiliser of savings. This led to an examination of the role of banks in financing private corporate sector, after they were nationalised, consequent to which, the Government attained ownership and reinforced control over the banking system in the economy.

The analysis of the role of commercial banks in financing the private corporate sector is carried out in the context of the changes in the various regulatory measures, especially those relating to deployment of credit to industries, since the bulk of private corporate sector activity is concentrated in the manufacturing sector. This analysis showed that the share of industry, particularly that of medium and large industries, in total bank credit has been declining since nationalisation until the mid-80s and has increased marginally since then. A concomitant rise in the share of priority sectors like agriculture is also observed. The share of small scale industries in the overall bank credit to industry also increased till the mid-80s and remained constant since then. This again can be attributed to the policy of priority sector lending, by virtue of which small scale industries are accorded priority in credit distribution. Hence, it appears that the decline in the share of industry in overall bank credit is mainly due to the reduced share of medium and large industries in bank credit.

A break-up of bank credit to the manufacturing sector by types of organisation revealed that the share of privately owned companies,

reflecting the private corporate sector, has moved in line with that of industry. However, all other forms of organisations have increased their relative shares at a time when the relative share of industry in overall bank credit itself has been declining. Hence, the reduction in share of industry seems to have been brought about by the reduction in the share of Private Corporate sector in overall bank credit to industry. Further, the increase observed since the mid-80s is largely related to the private corporate sector, as its relative share has increased during the phase when the share of total industry has increased, whereas that of other forms of organisation have registered a decline or remain constant. It suggests that the supply of bank credit to private corporate sector, within the industrial sector, has declined during the initial fifteen years of nationalisation, from when on it shows a marginal increase.

In addition, an analysis of investment made by banks in the securities of joint stock companies, a proxy for the private corporate sector, shows that the proportion of investment in this form of securities to total investment has declined from the time of nationalisation until the mid-80s, followed by a rise back to its original position in the early 70s. A break-up of these securities show that investment in debentures has increased while those in shares are declining.

These findings raise certain issues (1) whether there was a dearth of demand for finance? (2) Or, has there been a shift in the pattern of financing? This led to an examination of the pattern of corporate financing. An examination of the pattern of financing

shows that private corporate sector is increasingly relying on external funds in general, and borrowing in particular. A further break-up by various sources of borrowing revealed that the role of banks declined very sharply till the mid-80s, and has since then increased marginally. In other words, there has been a shift in the pattern of financing. A size-wise analysis shows that as the size of companies increases, its reliance on banks for funds declines.

While the analysis of corporate finance revealed certain trends in bank credit, it did not explain the reasons for the underlying trends. To understand the factors behind these trends, an analysis of the determinants of borrowing from banks was carried out. Considering the larger share of public limited companies within private corporate Sector, only the public limited companies were considered for examining the determinants of role of banks' finance.

The exercise clearly points out that the various credit control measures since nationalisation, to be the major factor explaining the observed trend in bank credit. Further, it also shows that the investment in inventory has significantly influenced the demand for bank credit. However, the implementation of Tandon norms is found to reduce the role of banks by influencing the quantum of inventory holdings. The use of internal funds is another factor that contributes to the reduced role of banks. As regards the cost factor, the analysis shows that, neither rate of interest on banks nor the relative rate of interest of alternative sources of borrowing exert any influence on the role of banks. Therefore, it

seems that it could be the availability of funds rather than the cost associated with it, that affects the role of banks in financing the private corporate sector.

The above discussion clearly brings out the significance of the supply of bank credit. In a regulated financial system, this is largely moulded by credit policies. It, therefore, indicates the effectiveness of the credit policies which aimed to reduce the dependence placed on banks by this sector.

It is seen that the supply of credit by banks since nationalisation, has moved in line with an increased use of reserve requirements which reduces the overall resources available with banks to lend. This is evident from the downward trend in credit to deposit ratio vis-a-vis an upward trend in the investment to deposit ratio. Moreover, the supply of bank credit is regulated by the policy of priority sector lending. If the declining role of banks in financing private corporate sector can be attributed to supply rather than demand factors, then the above mentioned two factors have to be necessarily highlighted. These are important observations in the present context of economic liberalisation, particularly in relation to government policies towards this sector.

Narasimham Committee has recommended (GOI, 1991:iv-vi) a reduction of reserve requirements and phasing out of priority sector lending, to a low level of ten per cent. The declining role of banks as an external fund, as seen earlier, is not due to dearth of demand. It implies that private corporate sector can absorb the resources

deployed by banks in the economy. When reserve requirements are reduced, credit to deposit is bound to go up. As a result, more resources will be made available by banks. Moreover, when the priority sector lending is phased out gradually, it is the private corporate sector which would gain by absorbing the additional resources deployed by banks in the economy.

Admittedly, an industry-wise analysis within the private corporate sector would have shed more light on the differences between various industries within this sector. Though it is beyond the scope of this study, this issue deserves serious attention.

BIBLIOGRAPHY

Abdi, AA (1977): Commercial Banks and Economic Development: The Experience of Eastern Africa, Praeger Publishers, New York.

Adve, S (1980): 'Financial Practices in Indian Corporate Sector: Inter-Group and Inter-Size Differences', Economic and Political Weekly, Review of Management, Vol. XV, No. 8, February 23, pp. M.2 - M.10.

Agarwal, RN (1987): Corporate Investment and Financing Behaviour: An Econometric Analysis, Commonwealth Publication, New Delhi.

Ambegaokar, N (1969): 'Working Capital Requirement and Availability of Bank Credit: Indian Processing and Manufacturing Industries', Reserve Bank of India Bulletin, Vol. XXIII, No. 10, October, pp.1535-1553.

Appavadhanulu, U (1971): 'Working Capital and Choice of Technology', The Indian Economic Journal, Vol. XIX, No. 1, July-September, pp. 34-41

Athawale, AG (1975): 'Towards an Integrated Model of Corporate Sectors Behaviour in India', Paper Presented at the Fifteenth Annual Econometric Conference of Indian Econometric Society, Vol. I, Indian Institute of Statistics, Calcutta, pp. 313-347.

Avadhani, VA (1978a): Studies in Indian Financial System, Jaico Publishing House, Bombay.

Avadhani, VA (1978b): 'Credit Input Theory and Monetary Policy', Reserve Bank Staff Occasional Paper, Vol. 3, No.1, June, pp. 17-40.

Bagchi, AK (1962): 'A Study of Investment by Privately Owned Joint Stock Companies in India', Arthaniti, Vol. V, No. 2, July, pp. 153-177.

Balakrishnan, G (1966): 'Significance of Company Financing Trends', Company News and Notes, Vol. IV, No. 18, June 16, pp. 1448-1453.

Bernanke, BS and Lown, CS (1991): 'The Credit Crunch', Brookings Paper on Economic Activity 2, The Brookings Institution, Washington, pp. 205-239.

Bhatia, NJ (1987): 'Trends in Credit-Deposit and Investment + Credit-Deposit Ratios of Scheduled Commercial Banks: 1969-85', Reserve Bank of India Bulletin, Vol. XLI, No. 5, May, pp. 407-421.

Bhatia, RJ and Khatkhate, DR (1975): 'Financial Intermediation, Savings Mobilisation and Entrepreneurial Development: The African Experience', International Monetary Fund Staff Papers, Vol. XXII, No. 1, March, pp. 132-158.

Bhat, NS (1986): 'The Banking System as Financial Infrastructure of the Economy', The Indian Economic Journal, Vol. 34, No. 1, July-September, pp. 34-40.

Bhole, LM (1972): 'Interest Rate and Corporate Investment: An Indian Case Study', The Indian Economic Journal, Vol. XIX, No. 4-5, April-June, pp. 580-593.

Bhole, LM (1985): 'Administered Interest Rates in India', Economic and Political Weekly, Vol. XX, Nos. 25 and 26, June 22-29, pp. 1089-1104.

Borkar, DG (1989): 'Tandon Committee and After', Financial Express, Vol. IX, No. 284, March 4, pp. 10 and 11.

Caligiuri, GF, Fazio, A and Padoa-Schioppa, T (1974): 'Demand and Supply of Bank Credit in Italy', Journal of Money, Credit and Banking, Vol. VI, No. 4, November, pp. 455-499.

Cameron, Rondo (1972): Banking and Economic Development: Some Lessons of History, Oxford University Press, New York.

Carter, H and Partington, I (1984): Applied Economics in Banking and Finance, Oxford University Press, Oxford.

Chandavarkar, A (1992): 'Of Finance and Development: Neglected and Unsettled Questions', World Development, Vol. 20, No. 1, January, pp. 133-142.

Chitale, MP (1980): 'Finance for Industry', Economic and Political Weekly; Vol. XV, No. 17, April 26, pp. 781-793.

Cho, YJ and Khatkhate, DR (1989): 'Financial Liberalisation: Issues and Evidence', Economic and Political Weekly, Vol. XXIV, No. 20, May 20, pp. 1105-1114.

Coghlan, Richard (1980): The Theory of Money and Finance, The Macmillan Press Ltd., London.

Dang, AK (1986): Bank Credit in India, Classical Publishing Company, New Delhi.

Datta, B (1976): 'The Banking Structure: A Reappraisal', Economic and Political Weekly, Vol. XI, No. 22, May 22, pp. 781-786.

Dhrymes, PJ and Kurz, M (1967): 'Investment, Dividend and External Finance Behaviour of Firms', in Robert F (ed). Determinants of Investment Behaviour, National Bureau of Economic Research, New York, pp. 427-467.

Divatia, VV and Shanker, K (1979): 'Capital Formation and its Financing in the Private Corporate Sector: 1961/62 - 1975/76', Journal of Income and Wealth, Vol. 3, No. 2, April, pp. 118-152.

Donaldson, G (1961): Corporate Debt Capacity, Graduate School of Business Administration, Harvard University, Boston.

Dornbusch, R and Reynoso, A (1989): 'Financial Factors in Economic Development', American Economic Review, Vol. 79, No. 2, May, pp. 204-209.

Drake, PJ (1977): 'Securities Market in Less-Developed Countries', Journal of Development Studies, Vol. 13, No.2, January, pp. 73-91.

Drake, PJ (1980): Money, Finance and Development, Martin Robertson, Oxford.

Evans, LT and Quigley, NC (1990): 'Discrimination in Bank Lending Policies: A Test using data from the Bank of Nova Scotia 1900-37', Canadian Journal of Economics, Vol. XXIII, No. 1, February, pp. 210-225.

Fazzari, SM, et. al (1988): 'Financing Constraints and Corporate Investment', Brookings Paper on Economic Activity 1, The Brookings Institution, Washington, pp. 141-206.

Feldman, DH and Gang, IN (1990): 'Financial Development and the Price of Services', Economic Development and Cultural Change, Vol. 38, No. 2, January, pp. 341-352.

Furness, EL (1972): An Introduction to Financial Economics, William Heinemann Ltd., London.

Galbis, V (1977): 'Financial Intermediation and Economic Growth in Less-Developed Countries: A Theoretical Approach', Journal of Development Studies, Vol. 13, No.2, January, pp. 58-72.

George, PV (1972): 'Inventory Behaviour and Efficacy of Credit Control', Anvesak, Vol. II, No. 2, December, pp. 168-175.

Goldsmith, RW (1955): 'Financial Structure and Economic Growth in Advanced Countries: An Experiment in Comparative Financial Morphology' in National Bureau of Economic Research (eds) Capital Formation and Economic Growth, National Bureau of Economic Research, New York, pp. 113-160.

Goldsmith, RW (1969): Financial Structure and Development, Yale University Press, New Haven.

Goldsmith, RW (1983): The Financial Development of India 1860-1977, Oxford University Press, Delhi

Gordon, MJ (1960): 'Security and A Financial Theory of Investment', Quarterly Journal of Economics, Vol. LXXIV, No. 3, August, pp. 472-492.

Government of India (1986): Directory of Joint Stock Companies in India 1985, Volume I, Ministry of Industry, New Delhi.

Government of India (1982): Report of the Study Group on Financing of the Private Corporate Sector in the Sixth Five Year Plan (Rangarajan Committee), Planning Commission, Government of India, New Delhi.

Government of India (1991): Report of the Committee on the Financial System (Narasimham Committee), Reserve Bank of India, Bombay.

Government of India (1992): Eighth Five Year Plan, Planning Commission, New Delhi.

Government of India, National Account Statistics, Various Issues, Central Statistical Organisation, New Delhi.

Goyal, OP (1979): Financial Institutions and Economic Growth in India, Light and Life Publishers, New Delhi.

Gupta, GS (1972): 'A Prototype Model of Bank Credit', The Indian Economic Journal, Vol. XIX, No. 4-5, April-June, pp. 515-529.

Gupta, GS (1974): 'Forecasting Bank Credit at Corporate Level', The Indian Economic Journal, Vol. 22, No. 2, October-December, pp. 143-155.

Gupta, LC (1969): Changing Structure of Industrial Finance in India: The Impact of Institutional Finance, Clarendon Press, Oxford.

Gupta, SB (1979): Monetary Planning for India, Oxford University Press, Delhi.

Gurley, JG (1967): 'The Market for Loanable Funds, Creation of Liquid Assets, and Monetary Control', in Deena Carson (eds) Money and Finance: Readings in Theory, Policy and Institutions, John Wiley & Sons, Inc, New York, pp. 177-183.

Gurley, JG and Shaw, ES (1955): 'Financial Aspects of Economic Development', American Economic Review, Vol. XLV, No. 4, September, pp. 515-538.

Gurley, JG and Shaw, ES (1960): Money in a Theory of Finance, The Brooking Institution, New York.

Gurley, JG and Shaw, ES (1967): 'Financial Structure and Economic Development', Economic Development and Cultural Change, Vol. 15, No. 3, April, pp. 257-268.

Gurley, JG and Shaw, ES (1968): 'Financial Intermediaries and Savings - Investment Process', The Journal of Finance, Vol. XI, No.2, May, 1956, pp.257-266.

Harris, DG (1974): 'Credit Rationing at Commercial Banks: Some Empirical Evidences', Journal of Money, Credit and Banking, Vol. VI, No. 2, May, pp. 227-239.

Hawkins, RG (1972): 'Indicative Planning and the Efficiency of French Capital Markets', in Arnold W. Sametz (eds). Financial Development and Economic Growth, New York University Press, New York, pp. 43-63.

Hoovar, EM and Klein BH (1952): 'Factors Influencing the Demand for Funds by Business Enterprises and the Problem of Projecting Business Capital Requirements', in Conference on Research in Business Finance, National Bureau of Economic Research, New York, pp. 89-120.

Industrial Development Bank of India: Annual Report, Various Issues, Industrial Development Bank of India, Bombay.

Joshi, MS (1965): Financial Intermediation in India, University of Bombay, Bombay.

Johnson, OEG (1974): 'Credit Controls as Instruments of Development Policy in the Light of Economic Theory', Journal of Money, Credit and Banking, Vol. VI, No. 1, February, pp. 87-99.

Jorgenson, DW (1971): 'Econometric Study of Investment Behaviour: A Survey', Journal of Economic Literature, Vol. IX, No. 4, December, pp. 1111-1147.

Kalecki, M (1955): 'The Problem of Financing Economic Development', The Indian Economic Review, Vol. 2, No. 3, February, pp. 1-22.

Khan, MS and Sundararajan, V (1991): Financial Sector Reforms and Monetary Policy, Working Paper No. 91/127, International Monetary Fund, December.

Khan, MY (1980): Indian Financial System, Vikas Publishing House Pvt. Ltd, New Delhi.

Khatkhate, DR (1972): 'Analytic Basis of the Working of Monetary Policy in Less Developed Countries', International Monetary Fund Staff Papers, Vol. XIX, No. 3, November, pp. 533-558.

Khusro, AM and Siddharthan, NS (1972): 'An Econometric Model of Banking in India', in Technical Studies Prepared for the Banking Commission, Vol. I, Reserve Bank of India, Bombay, pp. 1-77.

Krishnamurthy, K and Sastry, DU (1971): 'Some Aspects of Corporate Behaviour in India: A Cross-Section Analysis of Investment, Dividends and External Finance for the Chemical Industry 1962-67', Indian Economic Review, Vol. VI (New Series), No. 2, October, pp. 152-184.

Krishnamurthy K and Sastry, DU (1975): Investment and Financing in the Corporate Sectors in India, Tata Mc Graw-Hill Publishing Company Limited, New Delhi.

Krishnaswamy KS, Krishnamurthy K and Sharma PD (1987): Improving Domestic Mobilisation Through Financial Development: India, Asian Development Bank, Manila.

Kuh, E (1971): Capital Stock Growth: A Micro-Econometric Approach, North-Holland Publishing Company, Amsterdam.

Kuchal, SC (1973): Corporation Finance, Chaitanya Publishing House, Allahabad.

Kuznets, S (1965): Economic Growth and Structure, Oxford and IBH Publishing Company, New Delhi.

Lakdawala, DT and Mody RJ (1972): 'Mobilisation of Savings and Financial Assets', Anvesak, Vol. II, No. 2, December, pp. 111-122.

Lee, CH (1992): 'The Government, Financial System, and Large Private Enterprises in the Economic Development of South Korea', World Development, Vol. 20, No. 2, February, pp. 187-197.

Leff, NH (1976): 'Capital Markets in the Less Developed Countries: The Group Principle', in Ronald I McKinnon (eds) Money and Finance in Economic Growth and Development, Marcel Dekker Inc., New York, pp. 97-122.

Madan, BK (1957): 'Banks and Medium-Term Credit to Industry', Reserve Bank of India Bulletin, Vol. XI, No. 6, June, pp. 521-527.

McKinnon, RI (1973): Money and Capital in Economic Development, The Brookings Institution, Washington.

Menon (1977): 'Liquidity of the Indian Corporate Sector', Reserve Bank Staff Occasional Papers, Vol.2, No. 1, June, pp. 149-172.

Meyers, SC (1977): 'Determinants of Corporate Borrowing', Journal of Financial Economics, Vol. 5, pp. 147-175.

Meyers, SC (1984): 'The Capital Structure Puzzle', Journal of Finance, Vol. XXXIX, No. 3, July, pp. 575-592.

Misra BM (1989): Financing of Private Corporate Sector in India: 1961/62 to 1985/86, Unpublished M.Phil Thesis, Jawarhalal Nehru University, Centre for Development Studies, Trivandrum.

Modigliani, F and Miller, MH (1958): 'The Cost of Capital, Corporation Finance and the Theory of Investment', American Economic Review, Vol. XLVIII, No. 3, June, pp. 261-297.

Mohanty, SS (1986): 'An Empirical Evaluation of Public Deposits as a Source of Finance in the Corporate Sector', The Indian Economic Journal, Vol. 34, No. 1, July-September, pp. 59-78.

Morisset, J (1993): 'Does Financial Liberalisation Really Improve Private Investment in Developing Countries?', Journal of Development Economics, Vol. 40, No. 1, February, pp. 133-150.

Morris, F (1985): 'Indian Financial System: An Overview of its Principal Structural Features', World Bank Staff Working Papers Number 739, The World Bank, Washington.

Mujumdar, NA (1982): 'Structural Transformation in the Deployment of Credit: Some Implications', Reserve Bank of India Occasional Papers, Vol. 3, No. 2, December, pp.97-113.

Narasimham, M (1972): 'Monetary and Credit Policies in the Development Context', Prajnam, Vol. XI, No. 7, July-September, pp. 239-247.

Narayana, D (1992): 'Directed Credit Programmes: A Critique of Narasimham Committee Report', Economic and Political Weekly., Vol. XXVII, No. 6, February 8, pp. 255-258.

Neogi, C (1991): 'Forces Behind Structural Changes: A Quantitative Analysis of Indian Corporate Sector', Artha Vijnana, Vol. 33, No. 4, December, pp. 279-304.

Panchamukhi, VR and et. al (1991): Export Financing in India, Interest Publication, New Delhi.

Panda, J and Sahu PK (1985): Corporate Sector and Institutional Finance in India, BR Publishing Corporation, Delhi.

Patrick, HT (1966): 'Financial Development and Economic Growth in Underdeveloped Countries', Economic Development and Cultural Change, Vol. XIV, No. 2, January, pp. 174-189.

Porter, RC (1966): 'The Promotion of the Banking Habit and Economic Development', Journal of Development Studies, Vol. 2, No. 4, July, pp. 346-366.

Raj, KN (1948): Monetary Policy of Reserve Bank of India, National Information and Publishers Bureau, Bombay.

Raj, KN (1984): 'Some Observations on Economic Growth of India over the Period 1952/53 to 1982/83', Economic and Political Weekly, Vol. XIX, No. 41, October 13, pp. 1801-1804.

Rangarajan, C (1982): Innovation in Banking: An Indian Experience Impact on Deposits and Credit, Oxford and IBH Publishing Company, New Delhi.

Rangarajan, C (1984): 'Financial Infrastructure and Economic Development', Reserve Bank of India Bulletin, Vol. XXXVIII, No. 2, February, pp. 71-79.

Rangarajan, C (1993): 'The Macro Economic Scenario and Credit Policy', Reserve Bank of India Bulletin, Vol. XLVII, No. 2, February, pp. 149-153.

Rangarajan, C and Jadhav, N (1992): 'Issues in Financial Sector Reform', in Bimal Jalam (eds) The Indian Economy: Problems and Prospects, Penquin Books Indian (Pvt) Ltd, New Delhi, pp. 141-162.

Rangarajan, C and Patil K (1979): 'On Constructing a New Series on Corporate Fixed Investment', Journal of Income and Wealth, Vol. 3, No. 2, April, pp. 153-162.

Rao, DC (1980a): 'The Statutory Liquidity Ratio - Its Role and Some Policy Issues', Reserve Bank of India Bulletin, Vol. XXXIV, No. 11, November, pp. 860-870.

Rao, DC (1980b): 'The Structure of Corporate Finance and Some Related Policy Issues', Reserve Bank of India Occasional Paper, Vol. 1, No. 2, December, pp. 121-154.

Rao, KSR (1988): Demand for Commercial Bank Credit 1970/71 to 1984/85: A Study of Selected Indian Industries, Unpublished M.Phil Thesis, Jawarhalal Nehru University, Centre for Development Studies, Trivandrum.

Rao, RTVS and Mishra, GD (1976): 'Investment Financing in the Corporate Sector', The Indian Economic Journal, Vol. 23, No. 4, April-June, pp. 311-318.

Rao, SKGK (1977): 'Shift in the Pattern of Financing Capital Formation in the Private Corporate Sector', Reserve Bank Staff Occasional Papers, Vol.2, No. 1, June, pp. 136-148.

Rao, VG and Vivekananda, M (1980): 'The Determinants of Corporate Savings Behaviour', Margin, Vol. 12, No. 3, April, 38-50.

Reserve Bank of India (1970): RBI Functions and Workings, Reserve Bank of India, Bombay.

Reserve Bank of India (1971): Report of the Study Group on Term Loan Participation Arrangements (Ramanujam Committee), Supplement to RBI Bulletin, April 1991, Reserve Bank of India, Bombay.

Reserve Bank of India (1975): Report of the Study Group to Frame Guidelines and Follow-up of Bank Credit (Tandon Committee), Reserve Bank of India, Bombay.

Reserve Bank of India (1979): Report of the Committee to Review the System of Cash Credit (Chore Committee), Reserve Bank of India, Bombay.

Reserve Bank of India (1983): Report of the Committee to Review the Working of Credit Authorization Scheme (Marathe Committee), Reserve Bank of India, Bombay.

Reserve Bank of India (1985): Report of the Committee to Review the Working of the Monetary System (Sukhamoy Chakravarty Committee), Reserve Bank of India, Bombay.

Reserve Bank of India (1989a): Circular on Credit Policy Vol. I, Reserve Bank of India, Bombay.

Reserve Bank of India (1989b): Circular on Credit Policy Vol. II, Reserve Bank of India, Bombay.

Reserve Bank of India: Banking Statistics: Basic Statistical Returns, Various Issues, Reserve Bank of India, Bombay.

Reserve Bank of India: Report on Currency and Finance, Various Issues, Reserve Bank of India, Bombay.

Reserve Bank of India: Report on Trend and Progress of Banking in India, Various Issues, Reserve Bank of India, Bombay.

Reserve Bank of India: Reserve Bank of India Bulletin, Various Issues, Reserve Bank of India, Bombay.

Reserve Bank of India: Statistical Tables Relating to Banks in India, Various Issues, Reserve Bank of India, Bombay.

Rosen, G (1962): Some Aspects of Industrial Finance in India, The Center for International Studies, MIT, The Free Press of Glencoe: New York.

Roy Choudhury, UD (1992): 'Finances of Private Corporate Sector: 1955/56 to 1986/87', Journal of Indian School of Political Economy, Vol. IV, No. 4, October-December, pp. 599-653.

Saha, A (1993): 'Lending to Industry: Emerging Options', Prajnam, Vol. XXI, No. 4, January-March, pp. 417-438.

Sarkar, NN (1988): Bank Nationalisation and Corporate Financing in India, Discovery Publishing House, Delhi.

Sastry, DU (1975): 'Investment Behaviour in the Indian Capital Goods Industry', The Indian Economic Journal, Vol. 23, No. 1, July-September, pp. 56-77.

Schmidt, CH (1952): 'Analyzing the Effects of Business Size on Sources and Uses of Funds', in Conference on Research in Business Finance, National Bureau of Economic Research, New York, pp. 35-64.

Shah, BG (1980): 'Role of Banks in Financing Working Capital Requirements', Prajnam, Vol. IX, No. 2, April-June, pp. 119-142.

Shanta, N (1990): Size, Profitability and Growth of Firms in Indian Manufacturing Industry, 1960 - 1980, Unpublished Ph. D Thesis, University of Kerala, Centre for Development Studies, Trivandrum.

Shanta, N (1991): Trends in Private Corporate Savings, Occasional Paper Series, Centre For Development Studies, Trivandrum.

Sharma, KC (1991): 'Investment and Financial Behaviour of Public Limited Companies', Reserve Bank Staff Occasional Papers, Vol. 12, No. 2, June, pp. 59-109.

Shaw, ES (1973): Financial Deepening in Economic Development, Oxford University Press, New York.

Shetty, SL (1976): 'Deployment of Commercial Bank and Other Institutional Credit: A note on Structural Changes', Economic and Political Weekly, Vol. XI, No. 19, May 8, pp. 696-705.

Shetty, SL (1978a): 'Performance of Commercial Banks since Nationalization of Major Banks: Promises and Reality', Economic and Political Weekly, Vol. XII, No. 31, 32 & 34, Special Number, August, pp. 1407-1451.

Shetty, SL (1978b): 'Structural Retrogression in the Indian Economy since the Mid-Sixties', Economic and Political Weekly, Vol. XIII, Nos. 6 & 7, February, pp. 185-244.

Shetty, SL (1991): 'Need for Fresh Approach to Credit and Monetary Policy Formulation in India: A Few Suggestions', Reserve Bank Staff Occasional Paper, Vol. 12, Nos. 3-4, September-December, pp. 227-249.

Shetty, SL and Menon, KA (1980): 'Savings and Investment without Growth', Economic and Political Weekly, Vol. XV, No. 21, May 24, pp. 927-936.

Singh, A, Shetty, SL and Venkatachalm, TR (1982): Monetary Policy in India: Issues and Evidence, Supplement to RBI Occasional Papers, Vol. 3, No. 1, June.

Singh, B (1972): 'A Cross Section Study of Business Demand for Money- An Indian Experience', The Indian Economic Journal, Vol. XIX, No. 4-5, April-June, pp.528-535.

Singh, M (1984): 'Indian Banking System in the Seventh Five Year Plan', Reserve Bank of India Bulletin, Vol. XXXVIII, No. 9, September, pp. 377-390.

Spellman, LJ (1976): 'Economic Growth and Financial Intermediation', in Ronald I McKinnon (eds) Money and Finance in Economic Growth and Development, Marcel Dekker Inc., New York, pp. 11-22.

Sundar, N (1980): 'Working Capital Management and Finance', Economic and Political Weekly, Review of Management, Vol. XV, No. 8, February 23, pp. M.25 - M.31.

Tarapore, SS (1993): 'Issues in Commercial Banking System', Reserve Bank of India Bulletin, Vol. XLVII, No. 1, January, pp. 69-73.

Uppal, JS (1984): Public Financial Institutions in India, MacMillan India Limited, Delhi.

Uppal, JS (1986): 'Public Financial Institutions and Economic Concentration in India', Journal of Development Economics, Vol. 20. No. 1, January-February, pp. 135-144.

Venkatachalam, TR and Sarma, YSR (1978): 'An Econometric Analysis of Financial Behaviour of the Private Corporate Sector in India', Reserve Bank Staff Occasional Paper, Vol. 3, No. 2, December, pp. 69-87.

Verma, JC (1985): Corporate Finance: Legal Aspects of Borrowing, Vision Book, New Delhi.

Vickers, D (1987): Money Capital in the Theory of Firm: A Preliminary Analysis, Cambridge University Press, Cambridge, New York.

Virmani, A (1982): The Nature of Credit Markets in Developing Countries: A Frame for Policy Analysis, World Bank Staff Working Paper, No. 524, The World Bank, Washington.

World Bank (1989): World Development Report 1989, Oxford University Press, New York.

World Bank (1991): Financing Corporate Growth in the Developing World, Discussion Paper Number 12, International Finance Corporation, Washington, July.