CHAPTER NO. II

CONCEPTUAL FRAMEWORK OF THE STUDY

CONCEPTUAL FRAMEWORK OF BANK LENDING

CHAPTER-II

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CHAPTER - II

CONCEPTUAL FRAMEWORK OF THE STUDY & BANK LENDING

CHAPTER-2A : CONCEPTUAL FRAMEWORK OF THE STUDY:

2.1 BANKING BUSINESS: MEANING:-

Banking industry, being the catalyst of economic development, assumes greater importance by virtue of its unique place in the economy. Two basis economic functions are very essential for the nations progress towards development. These are savings and investments. "The Government, through nationalisation of banks has sought to regulate, interalia, savings and investment apart from paving the desirable eliminate for boosting them."[2] After, Govt. take over, the banks have been involved in the majority of the development processes that are initiated and implemented. The banks have a major role to play in 20 point programmes release or bonded labour, rural upliftment, poverty, disaster management and the like.

The role played by banks in rural development, agricultural development, poverty alleviation, inculcating saving habit and enhancing rate of saving, industrial development, trade and exports enterpreneurial developments etc. are noteworthy, particularly in the post nationalisation period. The banks have penetrated into the rural areas & there has been increase in total branch office which is phenomenal. There has been quite an impressive growth in deposits and advances. The national priorities set by the Government has been taken up by the banks in right earnest and a spirit of involvement. The unstinted growth of the banking industry, and its contribution to the economic development and social transformation have been acclaimed by different quarters. The impressive performance was achieved the banking industry in its present hetergeneous system.

2.2 DEFINITIONS OF BANKING:-

The term banker is the technical term and it is used in practice as 'Banking'. The term banking and banker both are synonimous. The term banking or bank is used in day-to-day life. Term banking has its own meaning, which is as -

"B Backing of efforts for nations economic prosperity.

A Advancement of working capital loans for raising crops.

N Nutrient food, As your money helps weaker farmers and landless labourers to purchase milch animals.

K Keeping your ideal money safe & grow at faster rate.

I Industrial devt, especially amongst-weaker sections of society.

N Numerous deposit schemes to suit your pocket & purposes.

G Getting of prompt courteous and efficient services."[3]

According to Michael Moran writes, 'Banking is a risky trade but regulating banks is riskier still.'[4]

According to John A. Brooks, Deputy Managing Director of the Midland Bank and President of the Chartered Institute of Bankers, confirming L.C. Mather's wise saying 'The art of banking is surely to know when to accept the risk. But first the able banker must be able to appreciate and assess that risk.'[5]

ACCORDING TO INDIAN BANKING REGULATION ACT 1949 (Section 5)-

"Banking means the accepting for the purpose of lending or investments, of deposits of money from the public repayable on demand or otherwise and withdrawable by cheque, draft or otherwise."[6]

H.L. HART begins his treatise on Banking Law with the following definition of a bank.

"A bank is a person or company carrying on the business of receiving drafts for customers, subject to the obligation of honouring the cheques, drawn upon them from time to time by the customers to the extent of the amounts. available on their current action."[7]

As per section 2 of the Bills of Exchange Act 1882 of Great Britain, "The term bank includes a body of persons, whether incorporated or not, who carry on the business of banking. Similarly section 3, of the Indian Negotiable

Instrument Act defines Banks as any person or persons corporation or company doing banking business. But such definitions leave guessing about the nature and composition of banking business."[8]

JOHN PAGET :

A prominent authority on practical banking gives a clear-cut meaning of the term. "No one and nobody, corporate or otherwise can be a banker who does not-

i) take deposit accounts,
ii) take current accounts,
iii) issue and pay cheques drawn on himself,
iv) collect cheques for his customers."[9]

IN RE-BOTTOMGATE I & C SOCIETY, SMITH J OBSERVED -

"The Principal part of the business of a banker is receiving money on deposit allowing the same to be drawn again, as and when the depositor desires."[10]

Source :

2. The Banker - A Monthly Economic & Banking Journal, April 1989, P-16.

3. A study of Bank Customers services with Special Reference To Kolhapur Janata Sahakari Bank Ltd., Kolhapur-1988, P-49.

2.3 SCOPE OF INDIAN BANKS :

International business has become highly competitive. The era is of consolidation rather than expansion. The days of easy profits are certainly over and the best managed banks **have to** complete for the shrinking business on highly finer terms. Therefore Indian banks will need to reduce the cost of their operations, increase the volume of business and undertake urgent technological improvement to remain competitive interms of banking business.

As developments in the recent past have demostrated. "Indian banks will have to ensure that to earn profits, the safety of their credit is not jeopardised. In order to ensure this safety and also retain competitive presence, indian banks at different centres and at their head-quarters in India will have to build up a risk monitoring system. Moreover this exercise has to be an on going basis. The risks are indeed of various types and monitoring, the same is not that easy."[11]

Also the cardinal principle of diversification of risk must be adhered to. Because of the problems being faced by one country i.e. Nigeria, the external profit profile of several Indian banks has been spoiled. Not only this the Indian banks operating at Hongkong and London are under tremendous pressure to increase provisions against possible loan losses.

Increasingly, it is felt that the major problems facing the indian banks in today's international environment is the size of the indian banks since they have to compete with the giants not only from the industrial countries but also from the host countries and financially more powerful banks from the newly industrialised countries and china. Therefore, to with stand the competition, it is felt that the operations of the Indian banks at several important centres should be combined on consortium basis to give them a competitive edge.

Therefore it is for consideration whether it is feasible for the banks operating at London, Hongkong, Singapur, Srilanka and New-York to combine into one banking corporation or else the entire operations of the Indian banks abroad should be broadly divided between two banking corporations SBI and other comprising all the remaining indian banks operating abroad. This aspect of the Indian banks operations abroad should merit serious consideration with the banking regulatory authorities in India since not only the competition facing the Indian banks in years a head will increase but the returns will keep thing. As many of the problems before the Indian banks are because of the inadequate capital base, combining them into one or two giant banks will help to overcome this particular constraint.

2.4 TYPES OF BANKS :

The business of the world is an ever increasing activity. It goes on embracing new areas, multiplying agents of production and distribution, achieving minute and complex division of labour. This business activity is split up into two major divisions viz. Production & Commerce. Production itself is subdivided into three groups viz. Primary Industry, Extractive Industry, and Manufacturing Industry. The Commerce is classified as Trade and Aids to Trade. As production grows in its volume and Commerce expands in its area, it becomes necessary to tap and increase sources of finance. We showed rather say that the growth of business depends very much on the availability of finance.

Alongwith this growing business activity the banking business must also grow. The crude and elementary banking system of the early days cannot cope with the increasing needs of the many phases of the business only one type of bank will not do. There should be a net work of various types of banks to facilitate finance in all the areas mentioned above. In the absence of efficient banking system the business acitivity will be checked up. The modern large scale production requires longterm credit facilities and that too at a low rate of interest. While there are occupations which require only short Term Loans.

These requirements of the growing business gave an impetus to establish various types of banks to later to the need of every type of business. A sure indication of the countries industrial growth is its well developed banking system.

"It is quient evident from the foregoing discussion that the growing business needs various types of banks. These banks are classified as under -

1) Central Banks 2) Commercial Banks
3) Industrial Banks 4) Savings Banks
5) Agricultural Banks 6) Co-operative Banks
7) Exchange Banks 8) International Banks
9) Mixed Banks."[12]

Let us now examine briefly the functions of each of these types -

1. CENTRAL BANKS :-

In every country the Central Banks is established to control and maintain the stability in exchange rates, price level etc. This bank is the bank of the Government which does not seek profit and compete with the other private banks. The Central Banks has overall control on the monetary activities of the country.

2. COMMERCIAL BANKS :-

These banks are purely meant to finance the traders who require short-term loans. The financial function of the commercial banks is to finance the business on short-term basis only. Now-a-days, these banks are also financing the industries to purchase raw materials, for a short-term.

3. INDUSTRIAL BANKS :-

These banks are established in the countries where the industries are developed to a great extent. These industrial banks Finance the industries for long term process of production. These banks may purchase shares, debentures, and bonds etc. or underwrite the securities of the industries.

4. SAVINGS BANKS:-

These banks are established to accept deposits from the public. Post-office is accepting the savings of the residents. Now some savings banks are accepting the savings and are advancing loans on the savings. But post offices are simply accepting the deposits but not giving loans to the public.

The main objective of this savings bank is to make the people thrifty. These savings banks are the means to pool up the public savings. The amount is used by the Government for the devt. purposes. A moderate rate of interest is paid to the depositors. Now-a-days, the private banks are also accepting the deposits. The depositors are not permitted to withdraw every day. They are permitted to withdraw once or twice a week.

5. <u>AGRICULTURAL BANKS</u> :-

These banks finance the agricultural sector. These banks advance long-term loans, medium term loans and short-term loans also to the agriculturists, according to their needs. These banks help the agriculturists to purchase seeds, manures and the modern agricultural equipments. Even after the harvest these banks help the agriculturist by advancing loans on their produce stored in the Government stores, thus enabling them to wait for the fair price for their agricultural produce.

Agricultural industry is not financed by the commercial banks or industrial banks, because the short-term finance in commercial term ranges from one month to three months. While in agriculture sector the period of short-term is from one month to nine months. The longterm finance in agriculture is upto 20 years while in Industries, the longterm period may be from 10 to 15 years.

Secondly the agriculturists are dependent upon the harvest which itself depends upon the rain and other natural phenomena. If the crop fails the agriculturists will be unable to repay the debt of the bankers.

Thirdly, the agriculturists have no securities to other than the land. The commercial banks do not accept land as security. So to meet this typical problems of finance for agriculture, the agricultural banks have been established. These banks are receiving much help from the central banks.

6. CO-OPERATIVE BANKS :-

Co-operative Banks finance their members for their industries. These banks are spread now in big cities as well as small villages. Co-operative banks are established to promote the individual business and needs.

7. EXCHANGE BANKS :-

These banks are useful in the international trade. With the help of these banks, the currency of one country can be converted into the currency of the other country and these banks try to ease the international trade. These banks are not permitted to finance, internal trade. And from the other private persons who are not transacting internationally, these banks cannot accept deposits too. These banks are meant to finance the international trade only.

8. INTERNATIONAL BANKS :-

After the world war II the economy of many countries suffered greatly. In order to redevelop and reconstruct the economics of these countries the I.B. for Reconstruction and Development of this bank by purchasing the share of this bank.

It will be seen from the above how the banking business developed into several types of bank suitable for various occupations and purposes. In the modern economy of large scale production banking business plays a very vital role of raising capital and financing industrial units without this activity there could be no industrial development at all.

9. MIXED BANKING :-

"A degree of mixed banking was favoured by the Shroff Committee which suggested that the RB could facilitate larger investments by Commercial banks and other financial institutions for private industry by suitable adjustment in its lending and discounting practices and that banks should increase their investment in industrial securities and form a syndicate with finance companies to underwrite industrial securities."[13]

Source :

4.& 5. Indian Banking Today and Tomorrow The Journal of The Banking World Feb.1989, P.1.

6.& 7. Prof. Mugli V.M. : The Law & Practice of Banking, B.S.Hombali Book Centre, Hubali-20, P.-112.

8,9,10. Mitra, R.M. : History of Banking In India-1948, P-79.

11. The Banker, A Monthly Economic & Banking Journal, May 1989, P-27.

12. Prof. Belgali : A Text Book of Banking and Indian Banking Systems, 1969, P-18.

13. Sarkar N.N. : Bank Nationalisation And Corporate financing in India-1988, Discovery Publishing House, Delhi-110031, P-77.

2.5 FUNCTIONS OF BANKS :-

1. Main Functions
2. Miscellaneous Functions

1. MAIN FUNCTIONS :

It is very general terms, the functions of a commercial bank can be classified under the following main heads -

"1. Borrowing money or raising money.

2. Lending of money with or without security.

3. Originate accept, discount or otherwise deal in Bills of lading, Bills of Exchange, Promissory Notes, Funds, Drafts, Railway Receipt and other negotiable or negotiable documents.

4. Issuing 'letters of credit,' useful mostly in Foreign trade. Issuing 'travellers' cheques and circular notes convenient for tourists.

5. Dealing in foreign currency and gold bulion.

6. Purchasing, holding, selling, transferring or issuing, underwriting securities like shares, debentures etc.

7. Providing Collection and remittance facilities in respect of money and securities.

8. Acting as safe custodians of documents and valuable articles.

9. Rendering 'agency services' on behalf of customer's, Government and local authority.

10. Acting as trustees or executors,

11. Negotiating loans or advances.

12. Transacting Guarantee or Indemnity business.

13. Acquring, and holding, managing any property, right or title of such property framing the security for the loans granted by the bank or meant for its own use and convenience.

14. Providing funds, organising or helping organising Associations for benefits of the past and present employees."[14]

2. MISCELLANEOUS FUNCTIONS :

In addition to the main functions given above, modern banks perform miscellaneous services, such as -

1. The issue of various forms of credit,
2. Underwriting of Capital issues,
3. The acceptance of bills of exchange, whereby the banker lends his name to his customers in return for a commission,
4. Preparing incometax, returns for their customers, and
5. Furnishing guarantees on behalf of customers, etc.

Source :

14. Garga K.N. : Banking Trade & Finance, 1977 P-101.

2.6 STRUCTURE OF INDIAN BANK :-

So far we have studied the historicaldevelopment of Indian banking system. We have noted the different types of banks which are operating in the country. This is to be treated as the structure of Indian banking. "In the banking structure, we have the Reserve Bank which is the 'appex' banking institution and is the leader of the whole banking system. The Reserve bank in concerned with the orderly and sound development of Indian banking system. This is followed by the public sector banks in India. The 14 big nationalised banks and the state Bank and its subsidiares are included in the public sector banking. The State Bank is a Semi-Govt. bank while the nationalised banks are Government banks. There are other commercial banks which are operating in the private sector."[15]
In the rural banking structure there are three important agencies namely the money lenders, the indigenous bankers and the co-operative agencies. All these agencies are concerned with agricultural finance and the other financial needs of rural sector.

Lastly, we have the specialised financial agencies which are mainly concerned with the provision of long term finance to industrial units. The agencies mentioned above are divided into two parts namely the organised sector and the unorganised sector. The agencies in the unorganised sector include the money lenders and the indigenous bankers while the rest of the agencies are included in the organised sector of the money market.

[16]The following diagram shows the structure of Indian banking :-

INDIAN BANKING SYSTEM

Organised Sector

R.B.I.

S.B.I.& Its Subsidiares

14 Nationalised Commercial Banks

Commercial Banks

Sche- duled Banks

Non. Sche- duled

Agricult- -ural Banks

Co-op.Banks

State Co-op.

Control Co-op.

Primary Co-op.

L.D.B.

Agricultural financial Corporation

Post Office Savings

Foreign Banks

Specialised Financial Corporations

Un-organised Sector

Indigenous Bankers

i) Banker

ii) Trader

iii) Combine Banking Trading

Money lenders

Agricultural

Professional

As per Reserve Bank of India, Act 1934, Scheduling was done under section 42. As per statistical data December 1985 there are only three Non-Scheduled Banks and most of the scheduled banks are running on commercial basis, the word schedule has become of less importance. Since, Bank Regulation Act 1949, whatever provisions are required are for all the banks i.e. for nationalised as well as all other banks. Therefore functions and working of commercial banks and scheduled commercial banks are practically same and thus clubbed.

However, for the present study it will begin order to have a glance at which a scheduled commercial bank means?

"A schedule bank is a bank which is included in the second schedule of the R.B.I. Act, 1934. A bank qualifies to be enlisted in the second schedule, vide section 42(6) of the same Act, when :-

i) its paid up capital and reserves, are of an aggreegate value of not less than Rs. 5 lakhs,

ii) it satisfies the Reserve Bank that its affairs are not being conducted in a manner detrimental to the interests of its depositors, and

iii) it is - i) a company as defined in section 3 of the Companies act 1956, or

ii) State Co-operative Bank or

iii) An institution notified by the Central Government in this behalf, or

iv) A corporation or a company incorporated by or under any law in force in any place outside India"[17]

ADVANTAGES OF SCHEDULED BANK :-

A scheduled bank, under section 17 of the Reserve Bank of India Act, 1934, is entitled to certain advantages such as -

1. The facility of having loans and advances from the Reserve Bank against stocks, funds and securities other than immovable property; gold, and silver, documents of title to goods and bills of exchange, promissory notes etc.

2. The facility of getting rediscounted by the Reserve Bank -

   a) its inland bills of exchange or promissory notes bearing two or more good signatures of which one shall be that of the scheduled bank -

      i) arrising out of bonafide commercial or trade transactions and maturing within go days from the date of rediscounting, or

      ii) issued for the purpose of financing seasonal agricultural operations or the marketing of crops and maturing within 15 months of such re--discounting, or

      iii) issued for the purpose of holding or trading in central or State Government Securities and maturing within go days of such re-discounting, or.

b) Its foreign bills of exchange arising out of any bonafide transaction relating to the export of goods and maturing within 180 days,

3. The facility of purchasing from or selling to the Reserve Bank foreign exchange in amounts of not less than the equivalent of lakhs of rupees,

4. The facility of free remittances or remittances at a nominal cost from the Reserve Bank or its agent, the S.B.I., and

5. The facility of being appointed by the R.B.I. an authorised dealer in foreign exchange.

SOURCE :

15. Sharma B.P. : The Role of Commercial Banks in India's Economy, 1974, P-48.

16. Prof. Kale N.G. : Principles of Bankings & Indian Banks, Qautam Prakashan 1097, Poona-30, P-89.

17. Choudhari B.K. : Practical Banking, Academic Publishers, Calcutta-73, 1978 P-1.

2.7 CHARACTERISTICS OF INDIAN BANKING SYSTEM :-

The most important characteristics of Indian banking may be stated as under -

1. Two sector banking system viz.
   a) Rural Unorganised Sector and
   b) Urban Organised Sector,
2. Credit has been always in inadequacy in Indian banking which is the great defect at the Indian Banking System.
3. There will always be cutthrought competition among banks which leads to the loss and bankruptcy.

2.8 NATIONALISATION OF MAJOR COMMERCIAL BANKS :-

Meaning :-

It may be recalled that the All India Congress recommended, as early as 1948, the nationalisation of banks. Although the insurance was nationalised in 1956, the nationalisation of banks was postponed on some grounds or other. There arose, therefore, a strong demand for the nationalisation of banks with a view to controlling the commanding heights of the country's economy. In pursuance of that demand Government took the step of nationalising the 14 major Indian scheduled banks on July 19, 1969, by promulgating an ordinance.

The Banking companies Acquisition and Transfer of undertaking Bill was introduced on July 25, 1969 to replace the ordinance. The Bill was passed and it received the assent of the president on August 9, 1969.

The validity of that Act was challanged in the Supreme Court, which declared on February 10, 1970, certain provisions as unconstitutional. To remove the constitutional objections, Government promulgated again an ordinance on 12 Feb, 1970. The legal enactment was given retrospective effect so as to validate the original act of nationalisation of 19 July, 1969.

The names of the 14 nationalised Indian scheduled banks together with their respective deposits as at the end of 1968 are given in page No. 29 .

As on July 18, 1969 the date preceding that of nationalisation the above 14 banks had agreegate deposits at about Rs. 2626.2 crores, while State Bank of India and its subsidiaries, which were already brought under State ownership, had total deposits at Rs. 1248.4 crores. Thus, with nationalisation, out of the total deposits at Rs.4683.9 crores of all the commercial banks Functioning in India, deposits agreegating Rs. 3874.6 crores came to be controlled by the public sector banks accounting for 83% of the total number of branches of all commercial banks as on the date of nationalisation. About 36 Indian Scheduled Commercial banks, 12 foreign banks and a few non-scheduled banks remained untouched by nationalisation and were allowed to operate in the private sector.

TABLE NO. 2.1 :

TABLE SHOWING NATIONALISATION OF BANK DEPOSITS IN INDIA

(In crores of rupees)

Sr.No.	Name of the Bank	Deposits
1.	Central Bank of India	433
2.	Bank of India	395
3.	Punjab National Bank	356
4.	Bank of Baroda	314
5.	United Commercial Bank	240
6.	Dena Bank	122
7.	Canara Bank	146
8.	United Bank of India	144
9.	Union Bank of India	115
10.	Syndicate Bank	112
11.	Indian overseas bank	93
12.	Indian Bank	85
13.	Bank of Maharashtra	73
14.	Allahabad Bank	112
	TOTAL	2740

The Prime Minister in her broadcast announcing nationalisation stressed the following points :-

"What is sought to be achieved through the present decision to nationalise the major banks is to accelerate the achievement of over objectives. The purpose of expanding bank credit to priority areas which have hiter-to been some what neglected as also-

i) the removal of control by a few,

ii) provision of adequate credit for agriculture, and small industry and exports,

iii) the giving of a professional bent to bank management,

iv) the encouragement of new classes of entre-preneurs and,

v) the provision of adequate training as well as reasonable terms of service for bank staff, still remain and will call for continuous efforts over a long time.

Nationalisation is necessary for the speedy achievement of these objectives, but the measure by itself will not achieve these objectives."[18]

<u>SOURCE</u> :

18. Basu A.K. : Fundamentals of Banking Theory & practice, Modern Bank Agency Private Ltd., 10 Bankim Chatterjee Street, Calcutta-12, P-76.

The 14 banks so nationalised were originally shareholder's banks and so, compensation had to be paid to the shareholders of the banks. The total amount of compensation so payable was determined at Rs. 87.4 crores, as shown in the following table :-

TABLE NO. 2.2:-

TABLE SHOWING COMPENSATION PAYABLE TO THE SHAREHOLDERS

(Amount in lakhs of rupees)

Sr.No.	Name of the Bank	Amounts
1.	Central Bank of India	1750
2.	Bank of India	1470
3.	Punjab National Bank	1020
4.	Bank of Baroda	840
5.	United Commercial Bank	830
6.	Canara Bank	360
7.	United Bank of India	420
8.	Dena Bank	360
9.	Syndicate Bank	360
10.	Union Bank of India	310
11.	Allahabad Bank	310
12.	Indian Bank	230
13.	Bank of Maharashtra	230
14.	Indian Overseas Bank	250
	TOTAL	8740

The amount of compensation shall be payable to every nationalised bank according to its option either in cash or in saleable or otherwise transferable promisory notes or stock certificates of the central Government Cash payment will be made by cheque on the RBI in 3 equal instalments, each instalment carrying interest at 4% p.a. As regards payment in Government promissory notes, the relative books may be either for 10 years with interest at 4½% p.a.or for 30 years with interest at 5½% p.a. Payment may also be received partly in cash and partly in either of the two types of securities or partly in one type and partly in the other. An interium payment up to 75% of the paid up capital of each bank may also be made it any bank makes such an application, to be set off against the total amount of compensation payable. Any payment, purported to have Act of 1969 shall be deducted by the Central Government from the interium payment, if any, made to a bank.

NATIONALISATION OF SIX MORE SCHEDULED COMMERCIAL BANKS:-

With the nationalisation of six more scheduled private commercial banks, through a Presidential Ordinance on 15-4-1980, the second phase of bank nationalisation in India is complete.

The six banks taken over are :-

1. The Andhra Bank Ltd.,
2. The Corporation Bank Ltd.,
3. The Oriental Bank of Commerce Ltd.,
4. The New Bank of India Ltd.,

5. The Punjab and Sind Bank Ltd.,

6. The Vijaya Bank Ltd.,

The present take over comes eleven years after the first bank nationalisation in July 1969 of 14 scheduled commercial banks with deposits of Rs. 50 Crores or more. All such Indian commercial banks as had not been nationalised would be taken over as and when their deposits crossed the Rs. 200 Crores limit.

The take over ordinance known as the Banking Companies Ordinance 1980 says in the preamble that 6 Former private sector banks have been nationalised "having regard to their size, resources, coverage and organisation in order further to control the economy, to meet progressively and serve better the needs of the development of the economy and to promote the welfare of the people, in conformity with the policy of the State towards securing the principles laid down in clause (B) and (C) of Article 39 of the constitution."

The ordinance covers six banks whose total demand and time liabilities as on March 14, 1980 amounted to over Rs. 2,356 Crores.

The Government has announced the payment of Rs. 18.50 Crores by way of compensation to the six banks. The amounts for different banks are :-

1. The Andhra Bank Ltd., Rs. 6.10 Crores,

2. The Corporation Bank Ltd., Rs. 1.80 Crores,

3. The New Bank of India, Rs. 5.10 Crores,
4. The Oriental Bank of Commerce Ltd., Rs.2.10 Crores,
5. The Vijaya Bank Ltd., Rs. 1.0 Crores and the
6. Punjab and Sind Bank Ltd., Rs. 2.40 Crores,

With the nationalisation of six more private banks, the composition of the 73 scheduled c. banks operating in our country is now somewhat changed & is like this, SBI and its seven subsidiaries, 20 nationalised banks, 33 private sector Indian banks and 12 foreign banks operating in India. The total deposits in the S.C.B. in India now stands at over Rs. 31,000 Crores as against Rs. 5,000 Crores at the time of first nationalisation in July 1969.

As regards composition of branches, the number of bank branches increased from 8262 at the time of July 1969 to 31,557 at the December end 1979 with the result that the average population served by each bank decreased from 65,000 to less than 18,000.

However, before we examine the arguments in favour of the present decision, it would be worth-while to give the bankwise data about the six newly nationalised banks.

TABLE NO. 2.3 :

TABLE SHOWING BANKWISE DATA ABOUT THE SIX

NEWLY NATIONALISED BANKS

(As on 31/12/78 in lakhs of Rs.)

Name of Bank	Paid up Capital	Reserves	Owned Funds	Deposits	Advances	No.of Branches	Priority Sector Adv.
Andhra Bank	100(50)	298 (42)	398 (92)	43806 (3231)	28070 (3545)	666 (167)	8956
Punjab & Sind Bank	58(21)	117 (21)	175 (42)	39041 (641)	26915 (606)	499 (57)	9530
New Bank of India	76(15)	310 (45)	386 (60)	36441 (2395)	22234 (1426)	371 (49)	5947
Vijaya Bank	118(20)	167 (11)	285 (31)	33093 (1871)	17555 (1300)	560 (114)	4579
Corporation Bank	75(18)	102 (38)	177 (76)	20888 (2140)	11838 (1441)	293 (78)	3060
Oriental Bank of Commerce	21(17)	79 (28)	100 (45)	17000 (2703)	10823 (1207)	286 (61)	4243

SOURCE :

Complied from the Economic Times, New Delhi dated 19/4/1980.

NOTE :

Figures in brackets relate to the year 1969.

TABLE NO. 2.4 :

TABLE SHOWING

SELECTED RATIOS FOR SIX NEWLY NATIONALISED BANKS

(As on 31/12/1978)

Name of the Bank	Ratio of owned funds to Deposits	C/D Ratio	Ratio of Priority sector Adv. to total Adv.	Annual Growth Rate 1978 over 1969 of Deposits	of Adv.
Andhra Bank	0.91	64.0	31.9	139.5	76.9
Punjab & S. Bank	0.45	68.9	35.6	665.6	482.4
New Bank of India	1.00	61.0	26.7	157.9	162.1
Vijaya Bank	0.87	53.0	26.2	185.4	138.9
Corporation Bank	0.85	56.6	26.3	97.3	80.2
Oriental Bank of Commerce	0.58	63.6	39.2	58.7	88.6

SOURCE : Complied from Eco.Times, New Delhi, dated 19/4/1980.

Above two tables highlight the performance of six banks in the field of deposits, advances and the branch expansion. Figure as they are quite impressive and show good growth records, but we will get some unusual conclusions if we make a comparative study of the performance of the newly nationalised banks. Mere sizable growth is branch expansion is not enough. We should see the ratio between the number of branches opened by these six banks in unbanked and rural areas, and the no. of branches opened in urban & metropolitan areas. If this ratio is compared to the similar ratio in the case of earlier nationalised banks, the performance of the six banks in the field of branch expansion will pale into insignificance.

The Ratio of paid up capital plus published reserves of six banks to their deposits (popularly known as capital Deposit Ratio or the Capital funds Ratio) given in above table No.2.3 ranges between 1.00 in the case of The New Bank of India Ltd., to as low as 0.45 in the case of the P & S Bank Ltd., These banks thus had been operating with a very low margin of capital funds. The capital funds Ratio is very important from the public confidence angle.

The share of priority sector credit in absolute terms is Rs. 3632 Crores in the total credit of Rs. 1174 Crores provided by the six banks as on 31/12/78. In % terms it comes to 30.9 which is bellow the national target of 33.3%. The worst thing being that in 3 banks, viz, The Corporation Bank, The New Bank of India Ltd., The Vijaya Bank Ltd., the proportion of priority sector lending is hardly ¼th of their total advances. The larger surplus thus left with them always want to big borrowers and for high yielding investments. Private sector advances are made at the rate of 11% p.a. interest while the cost of funds to the banks is around 14 to 15%.

2.9 BANKING TRENDS IN 1988 :

The aggregate deposits and gross bank credit of all Scheduled commercial banks as on the last friday of December last stood at Rs. 141,823 Crores and Rs. 87,746 crores respectively, registering an increase of 19.2% in deposits and 20.9% in credit over the previous years level.

All population groups rural, semi-urban, urban and metropolitan showed a unform growth rate in deposit mobilisation of around 19% over the year.

In the case of bank credit, however, the growth rate in semi-urban population groups was lower at 19.3% than the other groups which registered a growth of about 21%.

Among the banks groups the regional rural banks also foreign banks registered a growth rate of around 30% in deposit mobilisation in the year. This was followed by nationalised banks (19.3%) and SBI and its associates(16.9%). In respect of of bank credit, the picture was slightly different with foreign banks moving to the First position with a Credit growth of 35.4% followed by regional rural banks (26.3%) SBI and its associates (22.5%) and nationalised banks (18.7%).

Commercial banks, operating in Maharashtra attained a record level deposit of Rs. 25,658 Crores. The State also topped in The matter of credit with a figure of Rs. 18,491 crores of outstanding bank credit. The second and third positions in deposit mobilisation went to U.P. (Rs.14,674 Crores) and Delhi Rs. 14,254 Crores respectively. In outstanding credit TamilNadu ranked second with Rs. 8,535 crores followed by Delhi with Rs. 7,738 crores. Therewere four states and Union Territories with deposits more than Rs. 10,000 crores viz. Maharashtra, U.P., Delhi and West Bengal.

A total of 1,851 new offices were opened by the banks in the past one year. Out of these, 890 offices were opened by nationalised banks, followed by regional rural banks (546) offices SBI and its associates (367 offices) and other scheduled commercial banks (48 offices). Banks opened as many as 10,56 at rural centres, followed by 4,48 offices at semi urban centres and 347 offices at urban and Metropolitan centres.

The top 100 centres accounted for 59.3% of total deposits and 63.6% total credit.

While interms of number of offices, the top 100 centres had only around 19% of the total.

SOURCE : Eco. Times, New Delhi, dated 19/4/80.

Singhvi, Dr.L.M.: Bank Nationalisation and the Supreme Court Judgement, National Publication - Delhi 1971.

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Sharma, Harish C : Nationalisation of Banks In India, Retrospect and prospect, Sahitya Bhavan Agra 1970.

TABLE NO. 2.5 :

TABLE SHOWING PROGRESS IN BRANCH EXPANSION OF NATIONALISED BANKS

Names of the Banks	1969	1970	1975	1980	1981	1982	1983	1984	1985
Bank Of India	325	416	934	1385	1542	1605	1684	1764	1899
Bank Of Baroda	430	538	852	1492	1611	1675	1762	1810	1902
Central Bank of India	673	925	1296	1974	2057	2125	2226	2337	2468
Punjab National Bank	619	710	1202	1680	1812	1890	1982	2092	2262
Canara Bank	368	504	906	1284	1355	1393	1443	1525	1840
Syndicate Bank	355	461	778	1117	1206	1224	1300	1360	1434
Indian overseas Bank	226	253	494	808	886	924	980	1033	1084
UCO Bank	375	442	824	1267	1375	1470	1516	1576	1712
Union Bank Of India	273	374	773	1171	1308	1338	1409	1504	1619
United Bank of India	200	265	502	845	875	897	918	951	1063
Indian Bank	244	280	578	825	874	902	964	1041	1100
Allahabad Bank	169	214	498	958	999	1041	1087	1223	1297
Bank of Maharashtra	164	211	454	714	792	891	924	953	1979
Dena Bank	259	352	604	830	870	888	929	972	1000
Andhra Bank	-	-	-	627	675	728	749	789	825
Punjab & Sind Bank	-	-	-	536	558	576	605	621	637
New Bank of India	-	-	-	423	455	481	486	505	542
Vijaya Bank	-	-	-	578	602	607	635	646	679
Oriental Bank of Commerce	-	-	-	327	363	386	406	425	454
Corporation Bank	-	-	-	323	340	383	370	380	400
Total for 20 Nationalised Banks.	4680	5945	10695	19164	20555	21389	22375	23507	25196

TABLE NO. 2.6 :

TABLE IN DEPOSIT GROWTH OF NATIONALISED BANKS

Names of the Banks	1969	1970	1975	1980	1981	1982	1983	1984	1985
Bank of India	435.88	513.01	1132.10	2858.57	3537.36	4071.78	4934.78	6021.83	7578.64
Bank of Baroda	354.91	421.06	995.69	3016.23	3711.40	4251.47	5193.51	5611.92	6186.67
Central Bank of India	500.75	563.35	1180.53	2787.17	3267.62	3861.64	4491.98	5200.18	6096.26
Punjab National Bank	391.09	459.73	959.55	2765.03	3376.80	3938.15	4572.12	5122.19	6312.76
Canara Bank	185.24	239.92	706.91	2099.06	2545.81	3036.93	3448.81	4324.52	5628.22
Syndicate Bank	144.72	167.75	536.60	1692.35	2178.35	2436.70	2939.40	3625.57	4175.63
Indian Overseas Bank	89.68	108.23	328.75	1506.39	1949.99	2383.65	2729.38	3229.17	3408.03
UCO Bank	257.53	295.81	623.17	1905.41	2289.49	2476.21	2700.99	3055.96	3367.81
Union Bank of India	133.10	175.74	534.97	1436.98	1722.81	2019.70	2334.82	2819.77	3274.52
United Bank of India	168.34	203.65	560.65	1326.15	1559.19	1719.88	1974.51	2445.79	2707.28
Indian Bank	90.01	101.78	362.85	1092.44	1287.19	1496.55	1786.90	2381.40	3164.36
Allahabad Bank	124.91	140.70	296.63	867.48	1042.82	1210.21	1437.46	1704.64	2083.93
Bank of Maharashtra	87.19	103.68	262.17	832.02	937.14	1073.80	1315.23	1566.32	1805.24
Dena Bank	135.61	154.99	347.93	838.70	972.78	1084.05	1256.42	1460.13	1654.07
Andhra Bank	-	-	-	666.09	765.21	905.55	1089.72	1368.03	1713.87
Punjab & Sind Bank	-	-	-	625.83	727.82	836.10	942.49	1133.62	1350.48
New Bank of India	-	-	-	503.28	585.21	697.71	751.10	874.08	1137.12
Vijaya Bank	-	-	-	437.21	506.03	604.46	689.17	873.97	1048.22
Oriental Bank of Commerce	-	-	-	315.26	396.32	487.35	610.33	752.03	1019.61
Corporation Bank	-	-	-	307.95	356.98	406.05	517.50	658.62	790.74
Total for 20 Nationalised Banks.	3098.96	3649.40	8828.47	27979.60	33752.32	38998.00	45716.62	54229.64	64503.46

TABLE NO. 2.7 :

TABLE SHOWING TRENDS IN GROWTH IN ADVANCES OF N.B.

Names of the Banks	1980	1981	1982	1983	1984	1985
Bank of India	1784.76	2162.48	2531.37	3227.29	3779.20	4384.85
Bank of Baroda	1670.68	2055.46	2419.41	2733.93	3198.23	3575.48
Central Bank of India	1595.61	1985.35	2295.80	2670.74	3124.52	3465.19
Punjab National Bank	1535.16	1913.76	2342.69	2775.93	2962.18	3359.31
Canara Bank	1172.29	1448.61	1726.08	2140.26	2813.84	3560.23
Syndicate Bank	1070.06	1467.13	1686.57	1963.59	2423.76	2719.38
Indian Overseas Bank	975.21	1338.18	1628.74	1818.55	2251.65	2218.27
UCO Bank	1125.41	1445.21	1558.83	1605.43	1815.96	1907.11
Union Bank of India	797.37	1000.81	1171.65	1407.72	1744.55	1846.51
United Bank of India	742.18	835.45	953.82	1055.71	1315.82	1538.10
Indian Bank	681.95	853.67	957.64	1156.04	1514.98	1876.29
Allahabad Bank	494.24	601.89	650.19	735.28	902.85	1050.95
Bank of Maharashtra	481.17	561.27	621.71	751.36	912.66	987.46
Dena Bank	491.64	572.43	617.94	722.22	892.57	967.93
Andhra Bank	356.12	449.34	526.48	669.02	802.04	927.06
Punjab & Sind Bank	388.56	486.00	522.85	587.00	443.62	696.71
New Bank of India	256.62	330.37	375.00	406.19	689.85	620.09
Vijaya Bank	244.74	269.39	336.89	408.37	499.66	625.29
Oriental Bank of Commerce	168.96	223.64	265.24	337.84	396.98	526.91
Corporation Bank	161.08	191.00	216.84	304.09	406.88	457.24
Total for 20 Nationalised Banks.	16193.81	20191.36	23405.74	27476.56	32891.20	37310.36

TABLE NO. 2.8 :

TABLE SHOWING NUMBER OF EMPLOYEES IN THE N.B.

Names of the Banks	1980	1981	1982	1983	1984	1985
Bank of India	32295	35485	39306	41850	45556	48411
Bank of Baroda	30216	31577	36037	37292	40666	42029
Central Bank of India	35299	37741	39370	41689	43553	45152
Punjab National Bank	30225	33873	37469	41184	44406	48200
Canara Bank	29042	32237	35789	39772	42818	46640
Syndicate Bank	25496	26750	28385	29900	32924	35382
Indian Overseas Bank	16977	19024	21852	23142	25694	25852
UCO Bank	23437	25280	28742	30900	33392	33902
Union Bank of India	23038	24053	25261	26270	27949	29124
United Bank of India	16469	17244	18444	19240	20581	20929
Indian Bank	14964	16108	17035	17751	19381	20769
Allahabad Bank	12363	13097	14612	15198	16899	17954
Bank of Maharashtra	11250	12608	13896	14825	16180	16388
Dena Bank	13066	13857	14221	14755	15360	15792
Andhra Bank	7585	8801	10342	11061	12141	13611
Punjab & Sind Bank	9822	9961	10256	10827	11348	11741
New Bank of India	7598	8370	9498	10569	11158	11565
Vijaya Bank	9253	9628	10720	11426	11965	12210
Oriental Bank of Commerce	4254	4923	5714	6468	7396	8208
Corporation Bank	3831	4460	5080	6010	7278	8135
Total for 20 Nationalised Banks	356453	385078	422029	450129	486645	511993

TABLE NO. 2.9 :

TABLE SHOWING TRENDS IN NET PROFITS OF THE NATIONALISED BANKS

(Rs. In Crores)

Names of the Banks	1980	1981	1982	1983	1984	1985
Bank of India	4.12	5.05	5.06	5.11	5.30	8.53
Bank of Baroda	5.91	6.25	8.05	8.60	7.01	9.68
Central Bank of India	3.60	3.73	3.88	3.99	3.07	6.75
Punjab National Bank	4.00	4.51	7.99	8.53	9.01	12.00
Canara Bank	4.26	4.47	4.57	4.96	5.51	11.00
Syndicate Bank	1.50	3.55	4.13	4.94	5.08	5.99
Indian Overseas Bank	4.46	2.49	-	4.73	4.82	5.00
UCO Bank	2.28	2.41	-	2.36	2.36	0.50
Union Bank of India	2.32	2.36	-	2.90	3.11	5.06
United Bank of India	1.23	1.37	-	1.36	1.18	0.22
Indian Bank	1.60	1.28	1.35	1.40	1.41	3.52
Allahabad Bank	1.50	1.61	1.35	1.70	1.80	2.72
Bank of Maharashtra	1.13	1.24	1.65	1.93	1.20	2.27
Dena Bank	0.83	0.75	2.10	1.20	0.81	1.75
Andhra Bank	1.12	1.96	1.01	2.48	2.64	3.48
Punjab & Sind Bank	0.42	0.45	2.30	0.62	0.65	0.68
New Bank of India	0.83	0.88	0.51	0.72	0.26	0.76
Vijaya Bank	0.36	0.25	0.61	0.05	0.06	0.31
Oriental Bank of Commerce	0.53	0.55	0.19	0.72	0.80	1.49
Corporation Bank	0.77	0.99	0.64	0.93	1.10	1.37
Total for 20 Nationalised Banks	42.79	48.15	57.27	59.23	57.18	83.62

CHAPTER 2-B : CONCEPTUAL FRAMEWORK OF BANK LENDING

2.10 INTRODUCTION: (A)

"Lending activity plays an important part in the gross earnings and net profits of commercial banks, and promote the economic development of the country."[20] The basic fanction credit, whether provided by SCB's or by other sources is to enable individuals and business enterprises to purchase goods and or services ahead of their ability or desire to pay. Demand for credit by business firms arises because of the time consuming nature of the productive and distributive processes.

Consumers demand credit to acquire goods in advances for which they pay in future. The time gap between production, distribution and consumption gives scope for the wide use of credit, and with the devt. of the economy and its complexities, a number of financial institutions have come to birth-general & specialised. Credit demands are accommodated by savings, but the demand for credit for productive purposes outstrips savings, and hence the need for additional funds from financial institutions. Commercial banks fill the credit demands that are not accommodated by the savings process and other financial instititions. As a result, the commercial banking system is a residual supplier of credit.

B) MEANING OF BANK LENDING :-

Lending provides the bank a major source of revenue.

A branch has to advance or lend money subject to the guidelines issued by its Head Office and within the framework of the norms laid down by R.B.I. Despite paying considerable attention in selecting applicants for lending, there is evidence of a general rise in the size of bad debts of the banks.

C) EVOLUTION OF LENDING :-

Significant developments have taken place since the midfifties in regard to the range of financial assistance provided by commercial banks to industry. Commercial banks have been officially encouraged to branch off into newer forms of industrial financing of which two are particularly important.

Medium term lending, underwriting new issues of industrial securities. The introduction of medium term lending by commercial banks in India is in fact a part of an almost universal post war tendency on the part of the banking systems. The presure of the financial needs of industry since the world war II has led in many countries to a fairly insistent demand infavour of some relaxation of the orthodox rules of commercial banking.

There is a course of no general deposition to plunge banks into the more adventurous forms of financing on any significant scale, but there is a wide measure of agreement on the desirability and feasibility of taking up.

medium term financing of industry by commercial banks.

It may therefore be said that the model towards which commercial banking system in a growing number of countries seem to be moving is neither the orthodox British model which restricts itself, atleast in theory, more or less to self liquidating shortterm credits nor the 19th century German model with its deep involvement in the Fortunes of industry, but the current American model which openly recognises medium term loan within well-defined limits as a legitinate field of operation for commercial banks. The long standing controversery, sourrounding the participation of commercial banks in long term industrial financing seems to be setting down in favour of a middle course.

A reconsideration of the possibility of commercial banks in India taking up medium term financing of industry because necessary very soon in the context of enlarged programe of industrial development in the 2nd five year plan. This appears to have been the most important consideration behind the commercial decision taken about 1956 to bring the commercial banks into the Field of medium term lending.

Another reason for which the commercial banks were allowed to enter this new field of lending was the Governments eagerness to help the small and medium sized business. SFC in their operations and lacked local contacts. It was thought that these small business units could be helped more effectively if only the larger banks were presuaded to come forward for supplying finance to them.

A scheme of formal term loans was formulated by the Government of India in 1958. Under this scheme the lending banks were to be provided refinancing facilities against approved term loans. An institution known as the Refinance corporation was set up on June 1958 for this purpose. The Refinance Corporation of India has subsequently been merged with the I.D.B.I. with effect from September 1,1964. Subsequent to this merger, the I.D.B.I. decided to provide refinance to the extent of 80% of the amount outstanding in the refinance account, the balance of 20% being left for the banks to supply from their own resources. The scheme, initially confined to only 15 major scheduled banks which controlled about 80% of total deposits of all scheduled banks in India in 1958, now covers 58 scheduled banks, 6 state co-operative banks.

"Refinance to commercial banks is provided only to those commercial banks which satisfies the following eligibility requirements -

a) The loan should be for a period ranging from 3 to 10 years.
b) The maximum amount of the loan to any party should not exceeds Rs.1 crores through the I.D.B.I. may

consider applications for longer amounts of merits. The minimum is Rs. 5 lakhs but the minimum limit may be reduced to Rs. 1 Lakhs in the case of small scale industries provided the loan is covered under the credit Guarantee.

c) Lastly, the loans should be given for the purpose of increased production in industries which are listed for development in the five year plans or which serve the purposes of the plans. The I.D.B.I. will normally refinance only loans granted for acquisition of fixed assets."[21]

It may be mentioned above that the initial response of the banks to the refinancing scheme was rather dis-appointing, in the scheme began to increase. During 1963 the number of banks applying for refinance was 23 out of 64 eligible banks against only 3 in 1959. Over the three years 1963-64 to 1965-66, term loans disbursed by commercial banks under the refinancing scheme was about ¼th of the total term loans from all term financing institutions. The progress in this direction will depend on the banks ability to bear the additional risks and to tackle the organisational problems involved in term lending. Banks ability to shoulder additional risks usually related to the size of their equity funds. On the considerations of prudence, the total amount of term loans granted by any bank should not exceed a small multiple of this equity funds, whatever the source of funds for term lending may be, because the credit risk has to be done entirely by the lending bank. The I.D.B.I. has laid down the ceiling for refinance for individual banks at three times the paid up capital plus reserves in the case of Indian banks and at 10% of the Indian deposits in the case of foreign banks. The desirability of raising the ratio of equity funds to deposits becomes important in this connection.

So far as organisational problems are concerned, these are no doubt serious limitations in the shortrun. But it should not be difficult for the bankers over a period to develop the skill and organisation necessary for administering term loans business efficiently.

2.11 DEFINITIONS OF LENDING :-

According to The International Webster New Encyclopedic Dictionary of The English language & Library of useful knowledge :-

The lending means -

"To grant to another for temporary use; to furnish on condition of the thing or its its equivalent in kind being returned; to afford, grant, or furnish in general, as assistance."[22]

According to Concise Oxford Dictionary of Current English by H.W. Fowler and F.G. Fowler :-

The lending means -

"To grant (to person) use of (thing) on understanding that it or its equivalent shall be returned, allow use of (money) at interest, lending library, bestow, contribute, (something of temporary service or effect, as enchantment, aid, dignity)."[23]

2.12 PURPOSE OF BANK LENDING :-

Money once obtained by the borrower is soon amalgamated into the overall business of circulating funds or used for expenses but if the creditors have been pressing and the bank funds are used to take off the pressure all that will have been achieved will be that the bank will have to step into the shoes of the creditors and will likewise have to press for payment. If the real purpose of the lending is to finance stocks or day to day requirements, then, presumably, there is sufficient generation of funds and retained profits may be enough to repay the loan and likely to restore the working capital.

The banker has to verify the position with regard to the liquidity position of the borrower. The causes for slow turnover and collections are to be probed thoroughly. Whether the bank credit is being utilised to lending the special buying opportunity which may promise quick returns. Whether increase in turnover is linked with the availment of limit sanctioned. If the resources of the enterprise are too small as compared to increased turnover, it could be a clear indication of overtrading. Depending upon the turnover of the enterprise a corresponding swing in the account of the borrower be noted very carefully. This will definitely indicate the position of sale proceeds. While granting loan for the purchase of fixed assets it should be carefully noted that margin contributed towards loan account is not by way of depletion of working capital.

Bank lending is very important to the economy, for it makes possible for financing of the agricultural, industrial and commercial activities of the country.

Bank loans are called agents of indirect production. They also make possible production for inventory. In addition to the financing of agricultural, commercial & industrial activities, banks, through their consumer loans, contribute to consumption activities creating constant demand for consumer goods like houses, furniture, appliances, etc.

SOURCE :

20. The Banker July 1988, A monthly Economic & Banking Journal.

21. Mukharjee P.K. : Modern Banking Theory, The world press pvt. , 1972, Calcutta P.P.141, 145.

22. The International Webster New Encyclopedic Dictionary of the English language & library of useful knowledge Page No. 546.

23. Fowler H.W. & Fowler F.G. : The Concise Oxford Dictionary of current English. 7th Edition 1982, Bombay Oxford University press Delhi, Calcutta, Madrass P-575.

2.13 PRINCIPLES OF SOUND LENDING :-

There are a few general principles of good lending followed by bankers while considering proposals for advances. These are discussed below :-

1. Safety
2. Liquidity
3. Purpose
4. Profitability
5. Security
6. Spread
7. National Interest.

1) SAFETY :-

The first guiding principle of sound lending is safety. The very existence of a bank depend upon the safety of its advances. Safety should never be sacrificed for profitability. The failure of a single advance will affect a good portion of banks profits. Scrupulous care should, therefore, be exercised to ensure that the funds lent out are not subject to the risk of being lost. Advances should be expected to come back in the normal course i.e. the banker may not have to resort to legal action or to sell the securities to liquidate the advances. In short, if a banker expects the advances to comeback in the normal course, the borrower should be chosen carefully. He should be a person of good character and capacity. It is also desirable that the borrower has employed his own funds in the business and does not expect the lending banker to finance his business to the full extent. This will indicate the proprietor's stake or interest in the business. Thus the banker has to ensure that his funds go to the right type of borrower and are utilised in such a way that they remain safe and that repayment comes in the normal course.

2) LIQUIDITY :-

Bulk of banks deposits are repayable on demand or at short notice and so a banker would also like to employ his funds in such a manner that the funds are not locked up. A sizable portion of bank advances are, therefore, granted to meet the working capital requirements of the borrowers. An advance account which is well operated by withdrawals and deposits indicated liquidity of the advance.

In cases where a banker grants advances on medium term basis, say, for 3 to 7 years, to enable the borrower to meet his fixed capital requirements, i.e. for purchasing or renovating fixed assets, the banker insists upon a regular repayment programme so that the advances are progressively liquidated. The banker thus ensures a certain degree of liquidity in the advance account.

3) PURPOSE:-

Closely connected with the principles of safety and liquidity is the purpose. For which an advance is required by a borrower. If the funds borrowed are employed for unproductive or speculative purposes, the repayment in the normal course will become uncertain. Banks, therefore, discourage advances for speculative activities. Purpose has assumed a greater significance in the present day concept of banking for example, bankers have started financing small borrowers who have little or no funds of their own but have character and posses the requisite technical know-how and ability to run a particular project. If the banker is satisfied with the integrity and capacity of the borrower to employ the funds properly and complete the project successfully, he may not in certain cases insist on a security from the borrower. Purpose goes a long way in ensuring repayment of an advance.

4) PROFITABILITY :-

There is little point in a banker granting facilities which do not being directly or indirectly some return. Banking is essentially a business which aims at earning a good profit. The working funds of a bank are collected mainly by means of deposits from the public and interest has to be paid on these deposits. Again, offices have to be maintained to run the business of banking. This involves considerable amount of expenditure by way of salaries to staff, rent, electricity charges, taxes, etc. The difference between the interest received on advances and the interest paid on deposits constitutes a major portion of the bankers income from which most of the transaction unless a fair return from it is assured. It is sometimes possible that a particular transation may not appear profitable by itself, but there are may be some other business available, such a deposits from the borrowers other concerns or his foreign exchange business which may be highly remuneratives. In this way the transaction, on the whole, may be profitable to the bank. The rates of interest at any time are influenced by the bank Rate, Governments and Reserve Bank's policies and inter bank competition.

5) SECURITY :-

The security offered for an advance is a cushion to fall back upon in case of need. But it is incorrect to presume that an advance should be granted purely on the basis of the security offered. A banker would not normally like to recover the advance from the sale of the security. Realising the security might involve considerable delay and expense, and the entire advance may not be liquidated. A banker would, therefore, prefer an advance to come back from the normal sources. The importance of an adequate and acceptable security can, however, be hardly overemphasised. It will be observed that except for strong and convincing reasons, a banker will not agree to waive the security. Apart from the fact that taking security serves as a safety value for an unexpected emergency, it also renders very difficult, if not impossible, for the borrower to raise an advance from another source against the very security.

6) SPREAD :-

A prodent banker will avoid lending a major portion of his funds in meeting the needs of any one industry. Similarly, advances should not be concentrated in the same group of borrowers or against the same type of security. There should be spread of advances amongst different securities, industries as well as areas. If a banker has advanced too large a portion of his funds against one type of security, he will run a big risk if that class of security steeply depreciates in value. By having a wide network of branches, a banker will be able to get a variety of commercial commodities as securities against advances slump does not normally affect all industries at the sametime. Thus by a diversification of his advances, a banker will be able to spread his risk and considerably improve the safety of his outstandings.

7) NATIONAL INTEREST :-

The development of banking has reached a stage where the banker is required to identify his business with national policies. Banking industry has a significant role to play in the economic development of a country. The savings of the people which are mobilised by banks must be distributed to those sectors which require development in the countrys planning programme. Our country is presently eager to develop agriculture, small industries and exports. There is also a great need to promote retail trade and render financial assistance to an enterprising person who may not have sufficient means. In this way, the country can solve the problem of unemployment and also accelerate the growth of trade, industry and commerce. With this end in view, commercial banks have formulated schemes to finance agriculture, small scale industries, exports and small borrowers.

The R.B.I. issues directives to commercial banks to maintain ceilings on credit limits or higher margins against certain essential commodities which are in short supply. The directives are issued with a view to preventing the hoarding of stocks by unscrupulous borrowers and maintaining the price level. These directives must be strictly followed.

2.14 TECHNIQUES OF LENDING :-

In considering the techniques to be adopted by the commercial banks for their rural credit operations, it is mainly to the financing of the cultivator for production and investment that thought has to be given. Other activities such as marketing, processing and supply have always been financed by the banks when undertaken by private trade and the procedures to be adopted & safeguards to be observed for them are, therefore, Fairly well established. It is clear that the rules and regulations for advancing loans to cultivators for various purposes will have to be evolved by each bank in the light of its own experience and traditions and also with reference to individual areas and categories of purposes. We shall only make a few general observations. The basic principle of sound production credit are well known and have only to be adopted to the conditions under which agriculture is financed by these banks. The size of the loan has to be determined with reference to the outlay on the purposes proposed, after allowance is made for the extent to which the outlay may be met from the borrower's own resources.

The loan should be advanced in such a manner that the chances of misapplication are minimised. The implies, on the one hand, disbursement of the loan in kind or other arrangements to ensure that part of it is used for purchasing inputs as intended and, on the other, observance of seasonality in lending and recovery. Supervision should be such as to make sure of the proper utilisation of the loan and its recovery on the sale of the crop. All the types of credit required by the cultivator for agricultural purposes should be provided, preferably by the same institution, so that the borrower does not have to turn to non-institutional sources for part of his needs. Lastly, the loans must be suitably secured, the type of security insisted upon being tailored to meet the borrower's circumstances and convenience. Supervised credit would also imply that the banks interest will not be confined to the provision of credit but will extend to efforts to ensure that the borrower receives appropriate guidance from the extension agency and the required supplies of inputs or machinery, and disposes of his produce on satisfactory terms. These briefly, are the wholesome principles of productive lending which, we hope, the commercial banks will keep in view in formulating their specific operational regulations. As this is a new field, a considerable measure of innovation and enterprise will required initially till procedures and policies, tailored to the needs of different types of credit and clientele, can be finalised on the basis of experience.

2.15 ORGANISATION OF BANK LENDING :-

Principal responsibility of formulating loan policy for a bank and its implementation lies with the board of directors. Since the members of the board being pre-occupied with other important activities do not attend to day-to-day lending functions of the banks, they constitute a seperate lending body known as 'Credit department' to carry into effect the loan policies which they formulate.

"Broadly speaking, credit department of a bank performs the following functions :-

1. To receive loan applications.
2. To collect credit information about the applicant from numerous sources and to conduct interview with the applicants to solicit additional information and to verify the accuracy of the information given by them in the application.
3. To investigate the credit worthiness of applicants by making use of numerous tools of credit analysis.
4. Once the loan has been granted, to supervise loans by visiting the borrowers, keeping constant vigil on the

borrowers deposit balances, obtaining financial and other reports and checking with other creditors and calling attention of the borrower's to unsatisfactory performance.

5. To maintain records of credit information and revise them constantly so that the bank officers may come to know the status of their accounts.

6. To furnish credit information to other banks and creditors who seek it."[24]

In a bank with a large number of its branches the lending organisation varies considerably. Branch managers are given loan sanctioning authority upto a certain limit which is usually kept at a lower level. Loan request beyond this limit is referred to the regional manager if it falls within his loan limit otherwise the same would be referred to the Head Office. In large branches there may be good deal of specialisation of lending work as in the case of big unit bank and small branches would have the same organisational set up as with a small unit bank. for expeditious disposal of credit requests it is desirable to delegate more and more powers to branch and regional managers. Borrowers particularly those requesting for a small amount of loans can not be expected to wait for a long time for credit decision. Furthermore, personal touch with the borrowers is maintained which is very necessary for development of banking business.

ORGANISATION CHART OF A BANK LENDING WORK

BOARD OF DIRECTORS

LOAN COMMITTEE

CHAIRMAN

Loan Officer (Bill Discount)	Loan Officer (overdraft & Cash credit)	Loan Officer Reale-state	Loan Officer Consumption loan	Credit Manager	Loan Officer (Agricultural loans.)

Receipt of loan Application Section (Officer in charge)	Credit information section (officer in charge)	Credit Investigation section (Officer in charge)	Credit supervision (Officer in charge)	Despatch Section (Officer in charge)	Record section (Officer in charge)

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SOURCE :

24. Dr. Srivastava R.M. : Management of Banks, Pragati Prakashan, P.B. No. 62, Meerut- 25001, 1982, P-246.

2.16 SOURCES OF FUNDS FOR LENDING :-

A study of the balance sheet reveals that the main sources of funds available for lending and/or investment are:-

1. Paid up capital
2. Reserves
3. Deposits and other accounts.
4. Borrowings from the Reserve Bank.
5. Participation certificates.
6. Undistributed or unallocated protions of the current years profits.
7. Refinance loans from the Industrial Devt. Bank, Agricultural Refinance and Development Corporation etc.
8. Other financial institutions.

Under the present RBI directives, banks are required to maintain 10% of their total demand and time liabilities in cash resources with the Reserve Bank of India effective from November 16, 1984 and 37% in cash, investments and treasury bills with effect from July 6, 1985. Most of the investments of commercial banks are in union Government and State Govt. securities and other approved securities. A small portion is also held in the debentures and preference shares of companies. Banks, moreover, keep a small amount with other banks.

Thus the amount available for lending is restricted to 53% of demand and time liabilities & other resources, minus other assets comprising stationery, furniture and fixtures, premises etc.

Bank credit may be classified in a variety of ways, according to security, maturity, method of repayment, origion and purpose. Generally speaking, the bank advances in the country are classified as follows :-
Cash credit, Overdrafts, Demand Loans, Term loans etc.

2.17 RURAL LENDING :

RESERVE BANK OF INDIA GUIDELINES TO BANKS :

"The Reserved Bank issued comprehensive guidelines for speedy implementation of the new scheme of assigning specific areas of each bank branch for improring the quality and productivity of rural lending.

The guidelines over allocation of service areas, survey of villages, preparation of credit plans and co-ordination and monitoring on the part of branch managers. They must intensify their interface with their prospective customers at the field so that adequate and timely credit is made available for meaningful activities and effective recycling of bank fund ensured.

According to the guidelines, the allocation of specific areas will have to be made to all the rural and semi-urban banks. The service areas of each branch will typically comprise 15 to 25 villages. Proximity to the branch and contiguity of villages will be the main criteria for allotment of villages.

Villages in the same grampanchayat should, as far possible, be allotted to the same branch. The banks have been asked to keep in mind the existing allocation of villages to different bank branches for the implementation of the Integrated Rural Development Programme also while designating the specific areas for different branches.

The banks have been asked to complete before the end of June the allocation of villages in a time bound manner.

After the allocation of villages, the branch managers should undertake a survey of villages alloted to them and prepare a village profile.

The survey will cover important aspects like types of economic activities undertaken and potentialities for expansion of these areas or for families to take up different activities and the coverage of rural families by credit institutions operating in the area.

The third stage is the preparation of annual credit plans for each of the villagers in the service area by the branch manager in a phased manner. The annual credit plans should reflect the potentialities and the needs of the service area on the basis of the intimate knowledge gained by the branch managers through the survey and availiability of other information."[25]

The regional rural bank branches need prepare credit plans only for the target groups in their services areas. Similar credit plans for the non-target group will be prepared by the designated commercial bank branch.

While availiability of resources should be the basis for drawing up the lending programme, the branch manager should take into account accertion to deposits and improvement in recovery.

The banks have been told that since-co-ordination among them, and with block officials is essential, a block level bankers committee should be constituted. The lead district officer from NBARD would also attend some of the meetings of the block level bankers committee.

SOURCE :

25. The Banker June 1988, A Monthly Economic & Banking Journal.

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