"SOCIAL CONTROL" OVER COMMERCIAL BANKS

FREE ENTERPRISE
[illegible]5. Dr. D N ROAD, BOMBAY-1

o accept private
necessary evil,
good."

—Eugene Black

"SOCIAL CONTROL" OVER COMMERCIAL BANKS

THERE IS NO ECONOMIC CASE FOR BANK NATIONALISATION

By

CANDIDUS*

With fresh talks on bank nationalisation in the Lok Sabha, the debate on nationalisation has started once again. The difficulty in such a debate is that we are not always guided by objective considerations: the arguments are mostly couched in political and ideological terms rahter than based on any economic reasoning.

A re-assessment of the case for or against nationalisation may therefore be a helpful exercise.

At the outset it is worth emphasizing that nationalisation does not involve any new investment: it only means that private ownership of investment is replaced by public ownership. From the national point of view, therefore, nationalisation does not lead to any additional flow of goods and services. In fact, the public ownership of investment is generally associated with lesser efficiency and more rigidity and red tape. The only doubtful advantage which is claimed on behalf of nationalisation is that it may ensure a better distribution of the scarce resources.

In an underdeveloped economy distributional considerations are not of any basic importance. The major consideration in such an economy is how to create conditions for rapid economic development by a larger out-turn of goods and services. If the size of the national cake is small, no technique of equitable distribution is going to improve the standards of

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living of the people. Poverty can be eliminated only by larger output first and distribution later. Our immediate concern should be to develop the economy faster and to encourage new and diversified investments. By nationalisation of the existing investments in the private sector, Government would not only not be able to improve national production but in fact worsen the situation by disrupting the flow of new private investment. If the threat of nationalisation is constantly held out like the sword of Damocles it will also undermine the confidence of foreign capital on which the success of the Fourth Plan so much depends.

In a mature and developed economy the quetsion of a more equitable distribution through nationalisation may have greater significance. Even so, the brief experiments with nationalisation by the British Labour Government in the 1940's alienated the electorate. The Conservative Party was returned to power in 1950 and some of the nationalised industries had to be denationalised again for restoring the health of the national economy.

In the post-Independence era our Government has carried out several schemes of nationalisation. Civil aviation was nationalised. And the result? The increasing costs and the hardship caused to passengers are a common experience as without competition there is no incentive left for the improvement of the service. With the nationalisation of the life insurance business, the complaints of the policy-holders have kept mounting in the columns of the daily newspapers and the cost of insurance bears no relationship with the expectancy of life. By establishing the State Trading Corporation and the Metals & Minerals Trading Corporation, Government has entered the field of foreign trade, particularly in a big way. But it has not helped to augment the quantum of trade besides replacing the existing trade channels and creating more unemployment in the country. Now there is talk about nationalising banks!

At present almost a third of the Indian banking system, consisting of the State Bank of India and its subsidiaries, is completely under Government ownership and management.

Indian banking is therefore not wholly in the private sector. There is rather a mixed banking in India in which both the public and private sector institutions can play their role in mobilising the community's savings for economic development. At the head of this 'mixed' system of banking is the Reserve Bank of India which is vested with large powers of regulating and controlling the entire banking system, and which is itself owned and managed by the Government.

Why should such a healthy 'mixed' system of banking be overthrown by nationalisation? To suggest that bank nationalisation would release larger resources for Government for defence and development is mere wishful thinking. Nationalisation cannot lead to an increase of the resources of the banks. Any forced and uneconomic diversion of resources from the private to the public sector will only cripple the economy further.

If we look into the deposit-portfolio of all scheduled and non-scheduled banks, the myth of securing large additional resources for Government through nationalisation of banks would become evident. During 1964-65 the total deposit of Indian banks amounted to Rs. 2610.23 crores, out of which Rs. 727.60 crores were already invested in Government securities and therefore available to Government. The balance is available to meet the requirements of the other vital sectors of the economy under the directions and control of the Reserve Bank. According to a recent authoritative study, industrial undertakings in India are at present facing an acute shortage of finance due to a contraction of bank credit. It has been estimated that the contraction of bank credit in 1965-66, compared to 1964-65, was of the order of Rs. 260 crores! Obviously, if Government seeks to divert a larger portion of bank deposits for the public undertakings through nationalisation of banks, it would only mean further starvation of the productive sector of the economy.

In the current Indian situation there is need for more finance for both the public and private sectors. Larger finance will not become available through bank nationalisation. If a large flow of savings is not forthcoming to the banking system to meet the requirements of a developing economy, it is only because the people's capacity to save has been adversely affected by Government's fiscal and monetary policies. The first concern of Government should therefore be to encourage larger savings with the people.

The argument that the nationalisation of banks will place the large profits of the banking system at the disposal of Government is illusory. Out of the total profits of Rs. 32.2 crores earned by the Indian banking system in 1964, Rs. 18.0 crores went to Government by way of taxes and only Rs. 4.2 crores was actually distributed to shareholders the balance going to reserve or to employees as bonus, gratuity etc. According to a study by a leading banking expert in the country, Government would have to pay, after bank nationalisation, a compensation on the paid-up capital and reserves amounting to Rs. 70.46 crores on the basis of the figures for 1964. If this compensation is paid in the form of long-term bonds bearing a rate of interest of 5 p.c., a sum of Rs. 3.5 crores would be taken away from what is now being paid to shareholders as dividends. This would mean that a small sum of Rs. 0.7 crores may be available to Government as a result of bank nationalisation. But if account is taken of the increase of administrative expenses in the State-owned banking system, the availability of even this sum of Rs. 0.7 crores would become doubtful.

The fact remains that the nationalisation of banks would be harmful to the economy. Nor would it be advantageous to Governmen t, as no additional resources would become available to the public sector through bank nationalisation. The Burmese experiment should be a pointer: it will take many years for Burma to recover from the financial disarray created after the bank nationalisation. Experiments in the U.A.R. and some of the East European countries have also been not too satisfactory. We should profit by the experience of other countries. To waste large sums of public money for paying compensation for bank nationalisation, and to weaken in the process our highly developed banking system compared to other underdeveloped countries, would prove ruinous to the prosperity of the national economy.

The philosophy of nationalisation is based more on sentiments rather than economic realities. "To rob Peter and pay Paul" is not what we should be after. If our economy is to develop we have to augment our resources by generating more incomes and savings and help the banking system to contribute fully to economic growth.

— (*Reproduced, with kind permission, from "Amrit Bazar Patrika", Calcutta, of September 15, 1966*)

"SOCIAL CONTROL" ON BANKS

By

A. S. BHASKAR *

It is significant that at the AICC session at Ernakulam, not one spokesman of the party cared to define what the Congress manifesto means by "social control" of banks. The party leaders seem to feel that if they choose to nationalise banks they will not be accused of not having obtained a clear mandate from the electorate. The phrase "social control" is in any case capable of varied interpretations ranging from a tighter control over the working and resources of banks to their outright nationalisation. The uncertainty this will create can hardly be conducive to a healthy growth of banking in the Fourth Plan. It will only make it more difficult for banks to consolidate the gains they have made recently in such diverse fields as deposit mobilisation and branch banking. Banking is not the kind of industry or service that can function best in a climate of uncertainty.

However, it must be some comfort to banks that no leading party spokesman has so far committed the Congress to outright nationalisation. At Ernakulam, many of them did no more than paraphrase the resolution without throwing any new light on the party's thinking. The banks can also draw some comfort from the somewhat cautious interpretation put by the AICC Secretary, Mr. Sadiq Ali, on the phrase "social control". Writing in the **AICC Economic Review** (September

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15) he has pointed out how "agriculture, small-scale industry and new entrants into the industrial field can greatly suffer if either through the concentration of bank resources or some manipulations they do not have access to resources to the extent available." A clearer disclaimer of the intention to nationalise banks has come from the Mysore Chief Minister, Mr. S. Nijalingappa, a member of the Working Committee. After emphasising that the phrase "social control" does not mean the taking over of banks by the Government, he has gone on record that all that it means is that the bank resources should be available for the "country's general good".

It may be difficult to forecast what the party will do. But one point is fairly clear. The party has now moved further left from the position it had officially taken early this year (in February) when the Union Finance Minister firmly denied any intention to nationalise banks. What is not so clear is its assessment of where the present legislation falls short of what is needed. In the interest of clarity the least it can do is to say at what points this legislation has failed and what further powers the Government needs to ensure the desired degree of social control.

There are only two grounds on which the nationalisation of an industry can be economically justified. It must be shown that the industry has mismanaged its affairs to the point where it becomes a threat to the public good. Or its record is such as to prove that it is incapable of modernising itself. On neither ground can nationalisation of banking be justified. It is true that there have been some bank failures. But the record of banks here is on the whole no worse than in several other countries. In any case, the public funds involved have been a minor fraction of the country's total deposits with banks. As for the second ground for nationalisation, Indian banks, like their counterparts in most countries, no doubt tend to be conservative. But they have of late shown sufficient capacity for adjustment to new demands and diversified their services. If anything, private banks have shown a better awareness of the customers' needs than the State-owned sector.

It is unjust to criticise banks for not being responsive to the needs of agriculture and the small borrowers. Commercial banks cannot be expected to lend more freely to agriculture so long as the borrowers' repaying capacity depends to a large extent on the monsoon. The State-owned sector in banking has itself found it difficult to make any great headway in providing more credit to the small farmer. In any case credit can help the farmer only when other inputs such as water, fertiliser, pesticides and technical know-how are available. Where they are in short supply as in this country credit can only be a source of inflation.

The chairman of the Industrial Finance Corporation has rightly said that the Corporation has "no wish to become a cause of unduly large amounts of money without being certain that the extra producing power generated will be absorbed in the very near future by production of the types of goods that the wide public genuinely needs." This is even more true of agriculture where the chances of misuse of credit are larger and the consequent threat of inflation graver than in industry. Finally, as specialised financing bodies exist for aiding agriculture and small-scale units the proper course is to improve their working rather than to force commercial banks to divert their limited resources to fields with which they are unfamiliar. There is no compelling reason to disturb violently the present pattern of credit agencies.

The criticism of banks for lending to the so-called big business is equally misplaced. So long as there is big business and it is credit-worthy it must get the credit it needs. The only result of denial of timely credit to it will be to make industrial output suffer. As for the small borrower, credit is only one aspect of his problems. The economic viability of a small undertaking depends even more on how its raw material and other needs are met. The banks cannot be expected to meet the credit needs of all borrowers, big and small, unless it can be demonstrated that those who think they need credit and do not get it deserve it no less than those who get it and that the over-all growth of savings in the community is sufficient to meet the growing demand.

Whether they are in the public sector or in the private, banks have to recognise the fact that those who need credit are not always worthy of it and that in any case they cannot meet the community's credit needs in full. To force the pace of credit or to compel its diversion along certain channels merely on grounds of social usefulness is bound to lead to grave misuse of resources and also to deliberate credit creation; either or both courses will end up in inflation and loss of efficiency. For banks, such a policy could conceivably mean less profits or even operational losses and inability to pay the depositor an adequate return on his savings; in the latter event, the interest rates on deposits will not reflect the real scarcity of capital in the country and this will, in turn, inhibit both savings and investment. It is all very well to argue for a higher degree of social control of people's savings. But the real problem is to work out a policy for banking which better meets the needs of development.

As for banks' resources, the plain fact is that investment is becoming difficult precisely because their rate of growth has failed to keep pace with the country's needs. This is the hard core of the problem. Neither nationalisation of banks nor tighter control has much relevance to this crucial issue. After all, savings depend on how far real incomes rise and people are induced to keep consumption down. So long as prices continue to rise it is futile to expect savings to grow. and yet, the Congress manifesto makes no more than a passing reference to prices. It does no more than stress the obvious point that increased production is the key to price stability: it has precious little to say on how it proposes to tackle the problem. While it rightly condemns conspicuous consumption it overlooks the fact that the inhibiting effect of this evil on savings is only marginal.

It may be good politics for the Congress to give Indian banking a bad name and nationalise it. But it is bad economics. Credit is a sensitive plant which can easily wither in a climate of uncertainty and aggressive State control. A more sensible course will be to order a thorough inquiry into the working of banks. Mr. T. A. Pai, the erstwhile chairman of the Food Corporation and himself a banker and a member of the AICC, has pleaded for a probe of this kind. It is up to New Delhi to set up a broad-based committee to examine the whole policy in regard to rural, commercial and industrial credit, to outline a course of banking reform and to suggest the lines on which the issues involved in a closer alignment of monetary and fiscal policies can be tackled effectively. It is only a comprehensive review of this kind that can provide the basis for a meaningful banking policy.

— (Reproduced from "Times of India" of October 7, 1966, with kind permission of the editor)

RESERVE BANK EMPLOYEES OPPOSE NATIONALISATION OF BANKS

On the 3rd July 1964, an extra-ordinary General Meeting of the Reserve Bank of India Employees' Association, Bombay, passed the following resolution with an overwhelming majority:—

"This extra-ordinary General Meeting of the Reserve Bank of India Employees' Association Bombay, held on 3rd July, 1964, having considered the question of Nationalisation of Banks, resolves that this Association is opposed to the Nationalisation of Banks, since experience shows that Nationalisation would not be conducive to the interests and welfare of the employees. As such this meeting decides to dissociate itself and the Association from the campaign for Nationalisation of Banks and to take all such steps necessary in furtherance of this decision. This meeting also resolves to send copies of the Resolution to the various organisations of bank employees all over the country."

WHAT THE PUBLIC SAYS

Reproduced are but a few of the numerous letters which have appeared in the Press protesting against the idea of nationalisation of banks. Public opinion in the country after seeing the public sector enterprises liks L.I.C., State Trading Corporation, etc. in operation has turned against State enterprises, and is apprehensive of any further expansion of the Public Sector.

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'Social Control' of Banking Industry is a Retrograde Measure

The Congress draft election manifesto contains a disturbing reference to "social control" over banks. Our experience clearly shows that no good can come out of hasty nationalisation; on the contrary, much irreparable harm will be done to the economy. True, there may be some instances of malpractices in private banks, but the Government and the Reserve Bank of India are already armed with enough powers to check and rectify these. If the Congress wants to extend rural credit facilities, this can also be done without nationalisation of the banks. Putting down malpractices, if any, in a State-owned bank will be much more difficult than in a private bank.

At a Government bank, be it in Bombay, Calcutta, Madras or elsewhere, one is never allowed to forget for a moment that one is dealing with a Government organisation, that one is an unwelcome intruder come deliberately to disturb the repose of the bank staff. Everything takes a long time whether it be depositing of money, cashing of cheques, buying a draft or retiring some shipping documents. The employees may be Government servants, but in practice they consider themselves as the masters and expect the ordinary citizens to treat them as such.

In private banks, as far as I know, when one deposits cash, one is given the receipt immediately; the passbook may be written up then or later. But at a Government bank, this is not so. They take one's cash and throw the deposit slip into a tray somewhere. After vainly waiting for the counterfoil (if one is new to the bank's methods), if one asks, for it, the clerk concerned may condescend to reply if he feels like it and tell you to call for it later. The money has been paid in but the depositor has nothing with him to prove it. Of course, the money may be safe enough; but the procedure is certainly not one to instil confidence in a new depositor. There is no valid reason for this peculiar procedure, unless it be that the bank, which has a monopoly of the huge Government business cannot be bothered with small depositors.

While it is a tedious process to retire shipping documents from a Government bank, it is even more so to realise the proceeds of outward bills through them. A bill may be paid promptly on presentation at the other end, but the drawer here may have to wait for a week or more to get the amount. The manager of the collecting branch of the bank unhurriedly remits the proceeds, not to the drawer, but to his local head office, and the latter takes its own sweet time to credit them to the drawer. Any telephone or personal enquiries are looked upon by the head office as a nuisance and seldom elicit any information. When the bill is drawn through a private bank, on the other hand, the proceeds arrive in two or three days once the drawee pays the bill anywhere in India.

Such instances of indifference and inefficiency can be multiplied. Free and fair competition among banks with adequate Government supervision will be much more beneficial to the country than the creation of further Government monopolies which will do irreparable harm by slowing down the tempo of commerce, industry and investment and by frightening away depositors when savings are so vital to the economy.—

Madras, September 22. S. N. IYER

("Mail", Madras)

* * *

L. I. C. Is An Example of An Inefficient State Monopoly

Your editorial entitled "March of L.I.C." (published in your issue of 5th September) is timely and thought-provoking. You have rightly drawn attention to "the lack of proper attention to the interests and the proper servicing" of policy-holders. In this context, it would be pertinent to voice the grievances of policy-holders. Letters to the Corporation do not receive even acknowledgements, leave alone clear and prompt replies. A policy-holder has to wait indefinitely for payment on his policies and is kept all along in the dark about the fate of the same. I know of instances where premia remitted to the Corporation were not receipted at all and, after an interval of four or five months, the parties were issued reminders for payment of the same and even lapse notices. Representations to the local L.I.C. office are of no avail and we are asked to write direct to the Divisional Office, where, of course, the correspondence is dealt with at the sweet will and pleasure of the staff concerned. Unless something is done to tone up the administration a fair deal for the policy-holders will remain only a dream.

One cannot but wonder whether there is any justification for the agitation against automation, especially in the light of the repeated assurances given by the Government to the employees. And also whether nationalisation, which is only another name for Government monopoly, of insurance is so successful as to call for further nationalisation, for example, of banks? The way things are shaping, the march of L.I.C. does not appear to be one of triumph from success to success but a slow movement towards red tape and stagnation.

Tirunelveli. S. G. Subramanian.

("Hindu", Madras. September 10, 1966)

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Public Sector Leads To Corruption And Inefficiency

It is a precious and timely service to the country to publish such short but illuminating articles like the one headed "The Meaning of Socialism" (Sept. 24) by "Alter Ego".

I hold no brief for the private enterprise, but to call a spade a spade, I must say that the way our public sector is being expanded is not socialism but totalitarianism. Trades and industries that have passed from the private on to the publice sector have invariably become a curse to the people. The monopolies have only passed into incompetent and corrupt hands that are eating into the national economy like the termites.

In the monopolised life insurance business troubles of policy-holders are multiplying. The State Transport is another example of the curse of our public sector. On the other hand, where private buses are operating, the number of buses is more than sufficient to meet the needs of travellers. There is no overcrowding. Much needed convenience of carrying luggage is always provided, and fares are also cheaper.

While a private enterprise, Calcutta Electric Supply Corporation Ltd. charges for lights and domestic appliances at the rate of about 18 paise and 12 paise per unit respectively, the West Bengal State Electricity Board charges 36 paise (double) and 18 paise per unit respectively, and yet the supply and service are far from satisfactory. The current goes off very frequently every day causing serious losses and inconveniences to domestic and industrial consumers. New connections are delayed for many months on flimsy excuses; meters are in short supply and so on.

While the public sector presents such an ugly picture, I may cite one—only one example of the competence and capability of the private enterprise.

This is the taxi business; in pre-war days, taxi fares were Re. 1 for the first mile and 12 annas for the next. But now when both the capital investment and the running costs have multiplied many times, taxi fares are on the contrary reduced to 60 paise for the first and 50 paise for the next. Is it not a miracle of the private enterprise and free competition?

Shame to the so-called public sector and the so-called Socialism and the corrupt officialdom that runs it all.

Ganganagar, 24-Parganas. N. Goyal

("Hindusthan Standard", Calcutta, October 4, 1966)

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Allow Banks to Compete with Each Other

It is with great alarm that I read the report of the A-ICC meeting that some of the members demanded that scheduled banks be nationalised.

The system that we will be faced with in case of nationalisation is demonstrated by the service that the people are getting from the Life Insurance Corporation. And what a contrast between the services that we are getting from the Corporation and those that we used to get from the better-managed companies!

Customers, both big and small, of banks are accustomed to getting a variety of services from them, as also an amount of courtesy which is tragically absent in Government offices.

The best course would certainly be to leave banks to compete with one another under the strict surveillance of the Reserve Bank and of the Legislature.

Calcutta-29. Taradas Dutt

("Hindusthan Standard", Calcutta, October 4, 1966)

SOCIALIST U. NU ON STATE ENTERPRISES

"Because of our intense enthusiasm to achieve these results in the quickest possible time, we have committed several blunders. I have just confessed to our greatest blunder. This is no other than our diversion to economic and social welfare activities as soon as law and order situation improved slightly, instead of concentrating all our energies on the complete restoration of law and order in the country.

"After this blunder, we committed another blunder. It was no other than the launching of our plants without first preparing the ground systematically. This hasty action has resulted in the following:

"(1) Before the foundations for industrial buildings were laid, machineries arrived and they lay scattered in the sun and rain without any use being made of them.

"(2) The completion of industrial buildings long after the scheduled time.

"(3) Even after the completion of these industrial buildings and installations, specific plans were not formulated for the production and supply of raw materials.

"(4) Due to lack of adequate managerial personnel, undue losses were incurred by many industries.

"(5) Inefficiency due to inadequacy of managerial schemes.

"(6) Wastage due to mismanagement.

"(7) Due to lack of qualified accountants in several enterprises, the accounts were more or less in a mess..........

"In order to step up production in the economic field, the operation of all industrial and mining enterprises, except certain key projects, should not be entrusted solely to those who are only interested in getting salaries. They should be entrusted also to those who have profit motives..........

"From practical experience, I no longer like to see Government's finger in all sorts of economic pies. If it is allowed to go on unchecked, then due to lack of proper supervision and efficient management, the State enterprises will sooner or later only line the pockets of thieves and pilferers."

— *From the speech of the then Premier U. Nu of Burma on the 4-Year Plan published by the Director of Information, Union of Burma.*

SOVIET ECONOMIST ON NATIONALISATION

"When nationalisation is being effected, it is important to take into account its economc and political feasibility in the concrete conditions existing in each country and even in each branch of the economy."

— *From "By-passing Capitalism" by V. Tyagunenko, Soviet economist*

AFRICAN SOCIALISM IS CAUTIOUS ABOUT NATIONALISATION

"Nationalisation is a useful tool that has already been used in Kenya and will be used again when circumstances require. The pertinent questions are at what cost, for what purpose, and when. The Constitution and the KANU Manifesto make it clear that African Socialism in Kenya does not imply a commitment to indiscriminate natonalisation. These documents do commit the Government to prompt payment of full compensation whenever nationalisation is used. Kenya's policy with respect to nationalisation should be more clearly defined with these stipulations.

"It should be recognised that if the nation's limited domestic capital is used to buy existing land, livestock, buildings, machinery and equipment, the nation has no more productive assets than before—only their ownership has changed. What may be lost are the new resources that could have been purchased instead—the new schools, hospitals, roads, water supplies, irrigation schemes, rolling stock, land surveys, housing, lodges, airports and harbour development—and the employment opportunities and added output that these new developments would create. Further, the money paid for nationalised resources and the people who managed them before nationalisation would most likely leave the country increasing our foreign exchange and skilled manpower problems. There is also the firm likelihood that nationalisation would discourage additional private investment, thus reducing further the rate of growth of the economy. It is also the case that the use of domestic capital to nationalise would reduce our ability to match foreign aid funds leading to an even greater-reduction in developmeunt expenditure."

— "*Republic of Kenya — African Socialism and its Application to Planning in Kenya — 1965.*"

The views expressed in this booklet are not necessarily the views of the Forum of Free Enterprise.

"Free Enterprise was born with man and shall survive as long as man survives."

—A. D. Shroff

Have you joined the Forum?

The Forum of Free Enterprise is a non-political organisation, started in 1956, to educate public opinion in India on free enterprise and its close relationship with the democratic way of life. The Forum seeks to stimulate public thinking on vital economic problems of the day through booklets and leaflets, meetings, essay competitions, and other means as befit a democratic society.

Membership is open to all who agree with the Manifesto of the Forum. **Bona fide** students can get our booklets and leaflets by becoming Student Associates. Write for further particulars (state whether Membership or Student Associateship) to the Secretary, Forum of Free Enterprise, 235, Dr. Dadabhai Naoroji Road, Post Box No. 48-A, Bombay-1.

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