

Brief Summary of recommendations of  
The Rural Banking Inquiry Committee

# Bombay Co-operative Banks'

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## **BRIEF SUMMARY OF RECOMMENDATIONS OF THE RURAL BANKING ENQUIRY COMMITTEE**

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## REPORT OF THE RURAL BANKING ENQUIRY COMMITTEE

The following paragraphs contain a brief summary of the report of the "Rural Banking Enquiry Committee"\* which was recently published. The Committee were appointed by the Government of India in November 1949 to consider measures for the expansion of banking facilities in rural areas, with a view to mobilising rural savings and stimulating their investment. The Committee were required to consider (a) the measures which can be taken immediately for extending banking facilities to rural areas, (b) the existing arrangements for cash work at government treasuries and sub-treasuries, including those managed by the Imperial Bank of India, and (c) the future arrangements for such work in the Provinces as well as in the States whose financial integration took effect from 1st April 1950, with special reference to the possibility of entrusting the work to a bank or banks.

2. As a preliminary to a consideration of proposals for the extension of banking facilities, the report gives a brief account of the existing facilities offered by the Imperial Bank of India, other commercial banks, co-operative banks and societies, and post-office savings banks. On the basis of facts concerning the growth of these institutions in recent years, it is found that, of late, substantial expansion has taken place in the banking system. "In 1939, the number of Indian scheduled banks was 40, which rose to 84 in 1947, while the number of their offices increased from 1, 179 in 1939 to 3,462 in 1947, the post-partition figure being about 2,877. The offices of smaller (non-scheduled) banks, for which no comparative data are available, appear also to have substantially increased, their present number being about 2,200. In addition, a large number of co-operative banks have come into existence. The provincial and central banks have about 698 offices, while there are in the two provinces of Bombay and Madras alone at least 352 well-organised co-operative urban banks. Savings bank facilities are provided by 9,465 post-offices of which 6,401 are in the rural areas. There are also 1,03,422 co-operative credit and multi-purpose societies providing credit facilities in the villages (1947-48) and 272 primary land mortgage banks and 5 central land mortgage banks providing long-term credit to agriculturists. As against 339 towns out of 2,300 served by banks in 1928, as reported by the Central Banking Enquiry Committee, 1,506 towns out of a total of 2,448 are now being served by banks."

But the present position cannot altogether be considered satisfactory. Not all the expansion in commercial banking has been of the healthy type; in relation to the area and the population of the country, the number of banking offices is still small as compared with the position in

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\* The Committee consisted of Sri Purushotamdas Thakurdas (Chairman); Sri C. H. Bhabha (Vice-Chairman); Sri B. Venkatappiah; Sri Ramgopal; Sri V. R. Sonalkar; Sri J. C. Ryan and Sri N. D. Nangia (Member-Secretary).

more advanced countries ; most commercial banks, particularly, the scheduled banks, are concentrated in the larger cities and towns while the smaller towns, which are more accessible to rural areas, are served largely by non-scheduled banks or co-operative banks, and as many as 869 towns, including 492 places which are either district or taluka headquarters, do not have any banking facilities. The position is more unsatisfactory in Part B States and centrally administered areas. While co-operative institutions are well-developed in Bombay and Madras, their achievement elsewhere is not so satisfactory. The Committee, therefore, consider that there is still much scope for extending the benefits of modern banking to the rural people, but that at present emphasis must be on consolidation and stabilisation, improvement in efficiency, and on orderly growth, particularly in regions where progress has not been adequate in the past.

Referring to the diversity of the institutional structure of the banking system, the Committee believe that this is a natural feature worth preserving. "These institutions," they observe, "have developed their own specialised functions and distinctive spheres of working and are able to offer certain services which others cannot provide with equal facility. It is, therefore, necessary to utilise all of them to the maximum possible extent ; to integrate their working and to improve their efficiency ; the overall requirements of the country demand that every healthy form of banking activity should be encouraged."

3. The most important banking services immediately needed by the rural people are the acceptance of deposits and the making of advances. Remittance facilities are required mainly by the banking and co-operative institutions functioning in rural areas. As regards the agency for extension of banking facilities, it is felt that the Imperial Bank of India and other commercial banks are not likely to find it worthwhile, under present conditions, to go beyond taluka (or tehsil) headquarters towns, mandis or market towns, or other towns of commercial or industrial importance. In view of their close contact with rural co-operative societies and relatively lower costs of operation, co-operative banks can go up to smaller towns and serve rural areas to a greater extent. Small villages could only be reached by co-operative societies and post-office savings banks.

4. Since the object of the proposed extension of banking facilities is primarily the mobilisation of rural savings, the question whether any opportunities exist for such mobilisation has been discussed in some detail. It is considered that, in normal times, it would not be unreasonable to assume, at the existing standards of consumption, some net savings in the rural sector of the economy.

Referring to the position in recent years, the Committee observe that available evidence indicates a shift in incomes from the urban to the rural sector, the latter now obtaining a total money income about three times higher than in 1931-32 and enjoying a larger share of the total national income than before. As agricultural prices have risen, in recent years, to a larger extent than the general price level, the money incomes as well as the real purchasing power, and consequently the saving capacity of the rural people are presumed to have increased. Other factors such as a reduction in rural indebtedness, increase in the balances in rural post-office savings banks, and improvement in the financial position of agricultural co-operative societies, are believed to reinforce the above conclusion. Taking the country as a whole, the major part of rural surpluses or savings would be with the bigger land-holders, and non-agriculturists such as village money-lenders, traders, owners of mills, etc., while the savings, if any, with the rest of the population are likely to be scattered in dribbles. Territorially, larger concentrations of savings may be in the more fertile and irrigated tracts or regions growing commercial crops. The Committee are, however, unable to hazard any guess as to the magnitude of current annual savings or the size of accumulated cash savings of the rural people. They believe that "while it would be wrong to assume that large amounts of cash savings are available for collection through the extension of banking facilities to rural areas, it cannot also be categorically held that no possibilities of drawing rural savings into channels of investment useful to the public exist at all."

The Committee emphasize the need to develop banking and to establish a suitable machinery for the mobilisation of rural savings as a permanent part of the mechanism of capital formation, since the internal capital requirements of the country, particularly for the development of projects essential for agricultural purposes, are very large, and the rural people, who would be the principal beneficiaries from such developments, should make their full contribution to it.

5. The Committee are of the view that the problems of mobilising rural savings and of extending credit to the rural people cannot be treated separately; the two have to be tackled largely by the same machinery. The implications of a suitable machinery for rural credit are discussed in the light of the recommendations of other committees which had dealt with these problems, and the following are the main conclusions arrived at :—

(i) Compulsory scaling down and adjustment of rural debts need not be proceeded with under present conditions. Attention should more properly be concentrated on building up the institutional machinery for rural credit.

(ii) For the provision of short and medium term credit, no uniform pattern can be laid down for all regions. Each region should develop

an adequate machinery to suit local circumstances, traditions and ideas ; it should be able to raise adequate finance from the public and not depend upon the State for funds. Emphasis should be laid on building a sound structure of primary co-operative societies, the super-structure being raised, as far as possible, on the basis of the existing institutions ; new institutions such as Agricultural Credit Corporations should be established only to the extent this may be unavoidable.

Commercial banks should play a greater role than at present in agricultural finance, particularly in respect of marketing.

(iii) For long-term credit, separate land-mortgage banks, primary and central, should be established in each State ; the establishment of a Central Agricultural Credit Corporation for the country as a whole is considered inopportune at present.

(iv) In implementing money-lending and other agrarian legislation, Government should take note of the pace at which satisfactory alternative machinery can be established, and the effects of such legislation on credit institutions.

6. Considering the attitude of the State to the question of the expansion of the banking system, the Committee express the view that Government should not assume an entirely passive attitude, but should take such steps as would create the necessary atmosphere for, and assist in, the promotion of orderly development of banking. Proposals for cash subsidies or interest-free deposits to banks to encourage their expansion are rejected both on grounds of principle and of administrative difficulties. The introduction of deposit insurance is not considered opportune at present ; the use of mobile banks on an extensive scale is not considered feasible.

The Committee's proposals for assisting banking institutions consist of (a) the removal of existing impediments to expansion, (b) indirect stimuli, available to all sound banks, and (c) special measures of assistance to co-operative banks and co-operative societies.

Apart from suggestions made to overcome impediments such as illiteracy and conservatism, the Committee have proposed that the provision for road development should be increased so as to improve rural communications and that offices of banks situated in towns having a population of less than 50,000 should be exempted from the Shops and Establishments Acts and from the awards of Industrial Tribunals.

To provide indirect types of stimuli for the expansion of sound banks, the Committee propose (a) cheaper and freer remittance facilities from the Reserve Bank of India and its agents, (b) better facilities for the conversion and exchange of notes and coin, (c) facilities for banks to keep their iron safes and chests for safe custody in the strong rooms of treasuries and sub-treasuries, and (d) the establishment of a Warehousing

Development Board with funds contributed by the Central and State Governments and the Reserve Bank of India, for developing warehousing through loans and subsidies to banks or co-operative institutions. It is suggested that banking companies should be permitted to form subsidiaries for the purpose of constructing and running warehouses and that the certificates issued by them should be recognised, as an experimental measure, as valid warehouse receipts by the Reserve Bank of India for the purpose of Section 17 (4) (d) of the Reserve Bank of India Act.

While approving and commending the efforts of various State Governments for assisting, reorganising and developing the co-operative movement, the Committee recommend additional facilities to co-operative institutions in the shape of (a) remittance of funds at concessional rates through post-offices, (b) relaxation, in the case of co-operative societies, of post-office savings bank rules regarding maximum deposits to be held and the number of withdrawals per week, and (c) the approval of co-operative banks and societies as authorized agents for the sale of National Savings Certificates. The Committee suggest that greater use should be made by co-operative banks of the provision for financial assistance at concessional rates from the Reserve Bank, and that there should be a closer liaison between them to facilitate this.

7. As post-office savings banks are considered specially suitable to collect savings from the less well-to-do people in rural areas, the Committee recommend that the number of post-offices doing savings bank work in the rural areas should be increased, that steps should be taken to improve their working, and that, to suggest ways and means of achieving this, an officer, with banking experience, should be entrusted with the task of investigating into the problem.

8. It is emphasized that the implementation of most of the above recommendations would largely depend upon the provision of certain basic facilities by the Reserve Bank of India and its agents, particularly the Imperial Bank of India. An increase in the number of offices of both institutions, recommended elsewhere in the report is, therefore, a vital pre-requisite of the whole scheme envisaged by the Committee.

Referring to the future structure of banking, the Committee observe :  
 "As a result of the steps now proposed and in the normal course of development, we thus envisage a system consisting of (a) the Reserve Bank of India with a branch or office in each major province or State, (b) the Imperial Bank of India and other commercial banks extending their activities upto taluka (or tehsil) headquarters and other semi-urban centres, (c) the Provincial and Central Co-operative Banks, with their branches or affiliated primary co-operative banks and primary co-operative societies located in all towns or large villages or centrally situated villages, (d)

State-owned or State-sponsored Agricultural Credit Corporations or Agricultural Banks or other suitable organisations, (e) a chain of Land-Mortgage Banks for each region.”

9. In dealing with the question of treasury arrangements, the Committee have considered the position in the “provinces” (Part A, Part C and Part D States) separately from that in Part B States. Of a total of 1,304 treasuries and sub-treasuries in the country (excluding Part B States), 140 are being managed by the Reserve Bank and the Imperial Bank, the rest being departmentally managed. It is considered desirable to transfer cash work at as many of these places as possible to a bank, as this may bring the people in taluka towns and in the surrounding villages in contact with banks, and reduce the handling of cash by spreading the cheque habit. It has, therefore, been suggested that the Reserve Bank and the Imperial Bank should jointly investigate the possibility of opening branches or treasury pay-offices at centres where, considering treasury turnover and other general banking business, it would be worthwhile to do so ; the Committee suggest 274 such places for specific examination with a view to taking over treasury work within the next five years. To see that this would not be unremunerative to the Imperial Bank, it is recommended that at least for the first five years the rate of commission for turnover as its new branches and treasury pay-offices should be fixed on a separate basis.

Since there would still remain a large number of “non-bank” treasuries and sub-treasuries, it is recommended that steps should immediately be taken to strengthen them, train their staff, and improve their working.

The Committee consider it impracticable to entrust government cash work to other commercial banks mainly for the following reasons : (a) Government cash work involves the handling of currency chests and small coin depots embodying large public funds. The banks to whom their custody may be entrusted must be necessarily limited. (b) The selection of banks for this work may lead to charges of discrimination and favouritism. (c) The settlement of accounts between Governments, Reserve Bank and the commercial banks concerned may lead to complications and difficulties.

The entrusting of co-operative banks with such work is believed to be impracticable and contrary to the main objectives of such banks.

10. The Committee have, therefore, come to the conclusion that the existing arrangement whereby Government cash work is done by the Imperial Bank of India as the sole agent of the Reserve Bank should be continued. They visualise the future role of the Imperial Bank as that



of an auxiliary of the Reserve Bank, and regard it, to all intents and purposes, as a "State-sponsored" institution. Considerable importance, therefore, is attached to the recommendations concerning the expansion of the branches of the Imperial Bank, and to the control and regulation of that institution in the national interest. While it is believed that altered political conditions and rapid Indianization would remove the basis for some of the criticism now levelled against the Imperial Bank, it is considered necessary that the Reserve Bank should ensure the proper discharge of its functions in respect of the facilities to be offered to commercial banks as the Reserve Bank's agent.

To ensure that the monopoly enjoyed by the Imperial Bank is exercised in the national interest, it is recommended that provision should be made in the Imperial Bank Act for (i) the appointment of the Managing Director and Deputy Managing Director being made subject to the approval of the Central Government who will also have the right to demand the removal from office of any such person who does not continue to enjoy their confidence, (ii) the Government Director on the Board being empowered to ask for the postponement of decisions on questions having a bearing on the policy of Government and for the review of similar decisions if already taken. It is also recommended that the representation of Government on the Central Board of the Bank should be made more effective. An alternative plan suggested by the Committee is that the constitution of the Bank should be altered, so that the overall policy and the general super-intendence of the Bank is placed in charge of a Chairman whose appointment would be subject to the approval of the Central Government, and a Board of Directors, two of whom will be nominated by Government, while the day-to-day working of the bank would be entrusted to a General Manager, who will be an employee of the Bank and will not have a seat on the Board.

It is also suggested that the power which the Bank's executive possesses at present to execute proxies on behalf of shareholders under general powers of attorney should be removed, and that the provisions of clauses (iii) and (iv) of Section 12 of the Banking Companies Act, which prescribe that shareholders should have only such voting rights as would be strictly proportionate to their paid-up capital in the company and that such rights should be limited, for any individual to a maximum of 5 per cent of the total, should be made applicable to the Bank.

11. The question of arrangements for cash work at Government treasuries and sub-treasuries in Part B States is more complicated due to the existence of a number of banks in these States with varying degrees of State control or interest, some of them being entrusted with Government cash work. While federal financial integration would imply the application of a uniform system and set of principles for the whole

country, this might lead to difficulties both for the Banks and the States resulting in a contraction of banking facilities, owing to a sudden withdrawal of Government balances, or to the emergence of competition from an institution like the Imperial Bank. The Imperial Bank may not be in a position to establish offices in these States immediately. Although most of the banks now working in the States would not qualify for appointment as the Reserve Bank's agents, it is not considered desirable to prejudice their case by giving a monopoly of Government business to the Imperial Bank. These considerations have led the Committee to the conclusion that "it would not be advisable to take a final and irrevocable decision on this question at the present stage, but that arrangements should be made to carry on cash work for a period of five years largely with the machinery that is now being used ; also, where consistently with the scheme of financial integration and the new set-up this is possible, the existing agreements with the various banks should be allowed to run their course." Meanwhile, steps should be taken to appoint the Reserve Bank as their banker, and transfer their balances to it, subject to transitional arrangements, and entrust it with the management of their public debt. Arrangements are also to be made to set up treasuries where necessary and to establish currency chests on the lines of the rest of the country. Recommendations have been made for each individual State in the light of these principles. At the end of five years from 1st April 1950, the whole question of the management of government cash work in Part B States should be re-examined by another committee.

12. The Committee do not favour the establishment of a new State-sponsored bank, whether by the amalgamation of existing State-owned or State-controlled banks in Part B States or otherwise. Nor do they accept the proposal for such a large extension in the branches of the Reserve Bank as to take up cash work at all treasuries and sub-treasuries, since this would raise difficult problems of personnel, organisation and cost. But they emphasize that the existing number of offices of the Reserve Bank is too small and inadequate for the requirements of the country, and recommend that steps should be taken to establish an office of the Bank at the headquarters of each major State, special attention being paid to the requirements of Part B States where the Reserve Bank of India has no branches at present. A reason for not recommending the establishment of a new State-sponsored bank is that the Committee consider the Imperial Bank as a State-sponsored bank and believe that "the multiplication of institutions which will perform similar functions and compete with one another with the aid of the State will not be a desirable development."

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