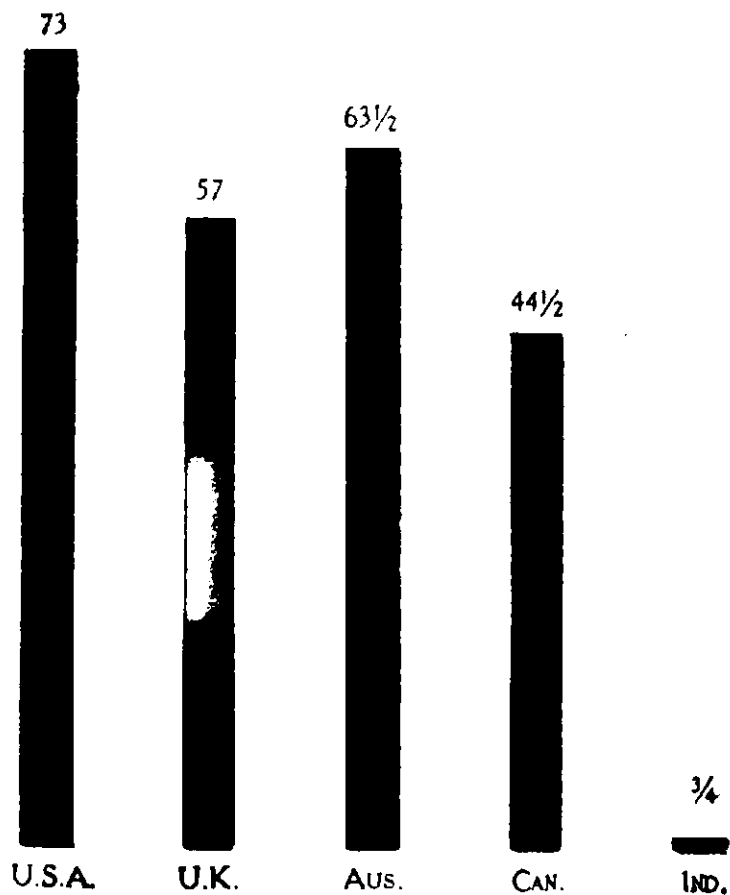
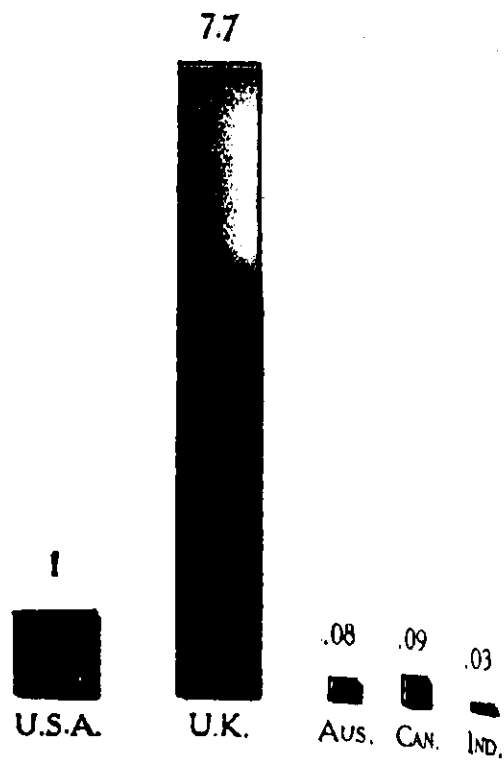


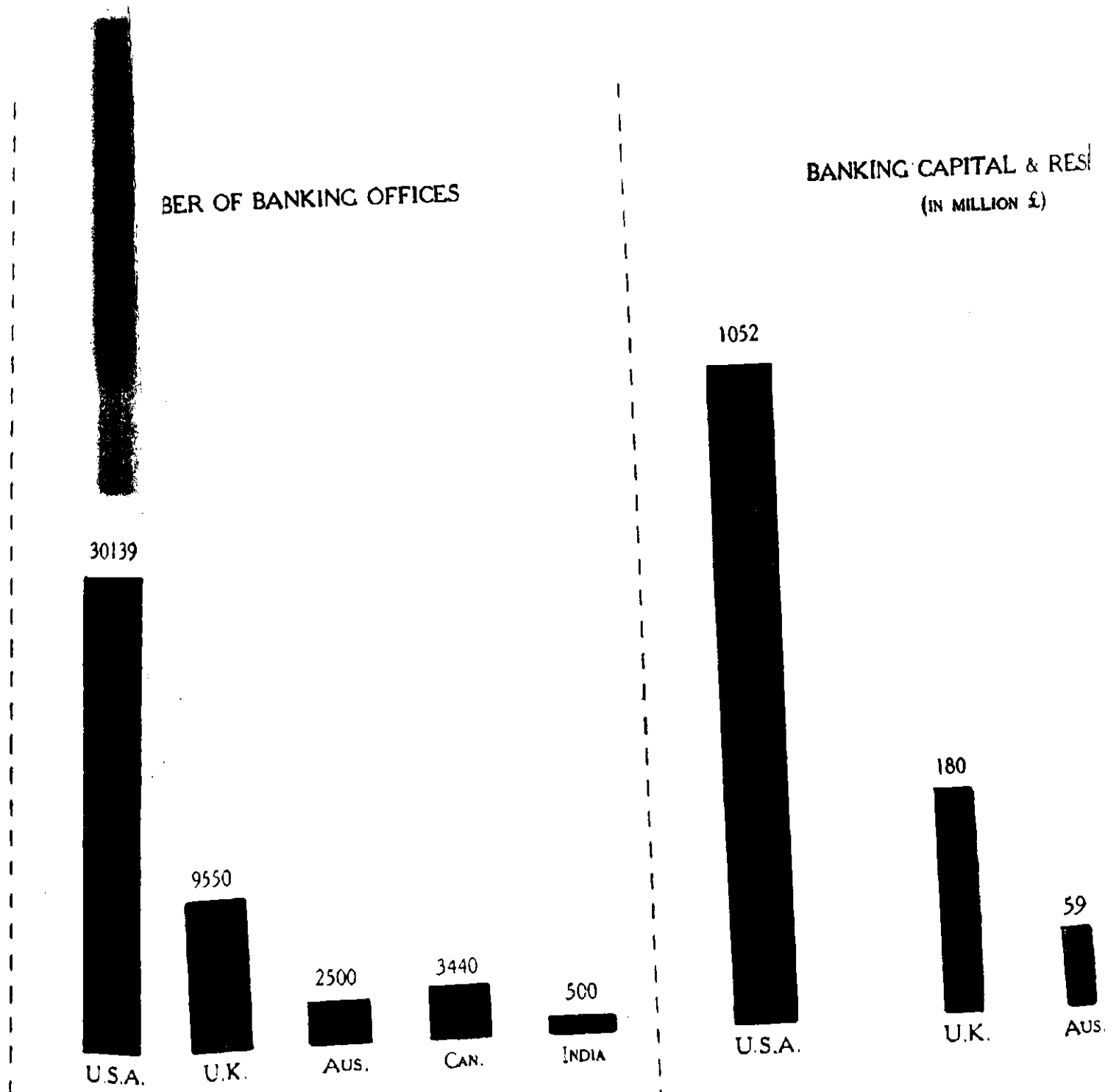
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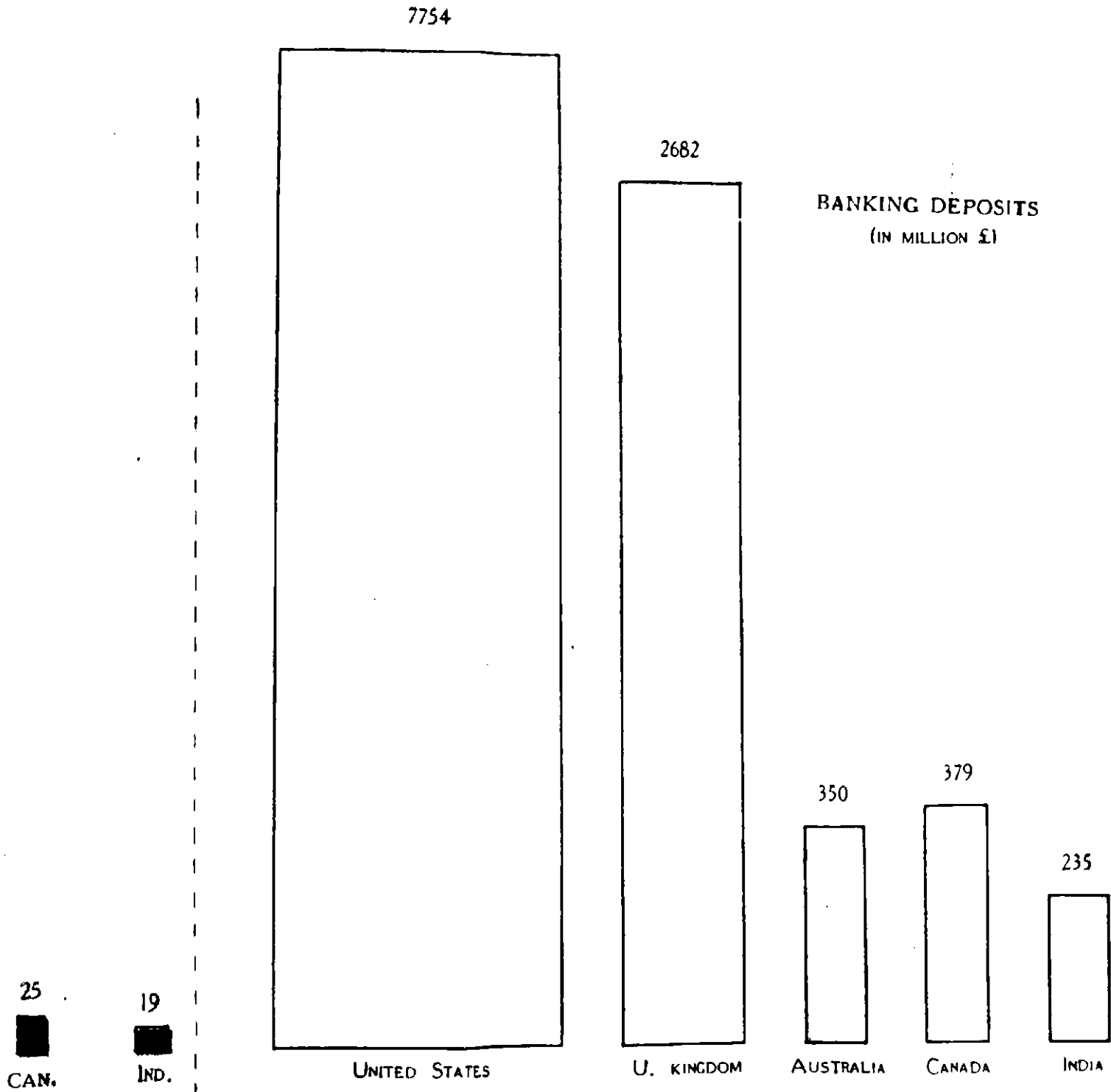
AVERAGE NO. OF BANKING OFFICES
PER 100 SQ. MILES



BACKWARDNESS OF INDIAN BANKING



BANKING DEPOSITS
(IN MILLION £)



ORGANIZATION
OF
INDIAN BANKING

BY

B. T. THAKUR, M.A.

**FELLOW OF THE INSTITUTE OF BANKERS, LONDON;
FELLOW OF THE INSTITUTE OF COMMERCE,
BIRMINGHAM; FELLOW OF THE ROYAL ECONOMIC
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OF COMMERCE, LUCKNOW UNIVERSITY; Etc., Etc.
CHIEF AGENT, U. P. GROUP OF BRANCHES, THE
CENTRAL BANK OF INDIA, LTD.**

WITH A FOREWORD

BY

LALA HARKISHEN LAL

CALCUTTA:

**LAL CHAND & SONS,
76, LOWER CIRCULAR ROAD.**

**Selling Agents in London—Effingham Wilson,
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1927

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THIS BOOK

**Is Dedicated by the Author,
As a token of Gratitude,**

TO

THE CENTRAL BANK OF INDIA, LTD.,

AND ITS

Managing Director,

S. N. POCHKHANAWALA, ESQ.

PREFACE

Of late India has been giving considerable attention to her banking problems. The Commissions and Committees that have been entrusted with investigations in connection with matters economical have all reported upon the necessity of banking development. The Indian Industrial Commission, 1916-1918, reported that there was urgent necessity for the extension of banking facilities and regarded organization of banking as an important preliminary step to the advancement of Indian industries. The External Capital Committee in their report dated the 16th September 1925 said, "India possesses a vast store of dormant capital awaiting development, and in order to make this available for investment banking facilities must be increased and extended..... We would emphasise the importance of a co-ordinated survey being undertaken at the earliest opportunity of the whole field of banking in India". The Royal Commission on Indian Currency and Finance which issued their report in August 1926, have also emphasised the same necessity. They said, "Nothing should be left undone which will tend to facilitate and encourage banking progress in India." Several discussions have taken place in the Central Legislature about the means to promote banking in this country. More than one public man has deplored the insignificance of India's credit institutions and demanded that a systematic scheme should be evolved to accelerate the growth of sound banking. And as students of economics and finance

know that no country can ever hope to attain her economic salvation unless her banking institutions are properly organized, all that the various bodies, referred to above, have said in this connection is nothing but absolute truth. The importance of organizing Indian banking cannot be minimised or belittled. Even the country's currency reform cannot be suitably brought about unless her banking system is constituted on satisfactory lines.

To supply material for consideration and thought in connection with this, one of the greatest and most fundamental problems which faces India, is the object of this book. As far as I am aware there does not exist any book at the present moment which fully and directly deals with the subject. It will be too presumptuous for me to claim any finality or rigidity for the views expounded herein or to regard the scheme outlined as the only possible solution of the problem. I am offering this book primarily with a view to inform the public how backward and deficient is our banking system, secondarily to indicate in what directions steps can possibly be taken to improve the situation and lastly to invite criticism. The task of designing construction of Indian banking is a formidable one and should naturally be undertaken by a competent investigating body which should examine the question thoroughly just as the National Monetary Commission of the United States of America did for that country in 1908. If my writing does anything to increase public interest in the Indian banking problem or assists in determining its solution my efforts will have been sufficiently rewarded.

I take this opportunity to thank all the banks and bankers that helped me in the study of this question during my visit to Europe in 1925. I am conscious

that at the cost of very great inconvenience to themselves they readily admitted me to their institutions and gave me every opportunity and facility to inspect their working and discuss with them various questions pertaining to banking problems. I am specially indebted to the following for valuable information relative to the subject matter of this book.

Lloyds and Midland Banks, London.

Guaranty Trust Company of New York, European branches.

Lloyds & National Provincial Bank, Paris.

Banque DE Paris ET DES Pays Bas, Paris & Brussels.

Netherlands Bank, Amsterdam.

Reichs, Deutsche, Darmstädter und National and Commerz-und Privat Banks, Berlin.

Credito Italiano and Anglo-Italiana Bank, Milan.

I am also anxious to particularly acknowledge my gratefulness to the following gentlemen who gave me much valuable advice and assistance : Dr. Visernig, President, Netherlands Bank, Amsterdam ; Dr. Node, Director, Reichsbank, Berlin ; M. Pierre Guebard of the Bank of France, Paris ; Mr. Spalding of Honkong & Shanghai Banking Corporation, London ; and Mr. Sykes, Secretary, The Institute of Bankers, London.

My special thanks are due to my employers, the Central Bank of India, Ltd., for readily granting my application for long leave to enable me to go abroad and for procuring me the necessary facilities. The visit was, however, on my own private account and I alone am responsible for the publication of and the views contained in this book.

It remains to be acknowledged that I am indebted to several authors who have written books on banking. It would be rather a lengthy matter to name them here. Major portion of the notes which were made use of in

writing this book were originally collected for the sake of personal knowledge without any intention of developing them into a book form ; and as such, I was not too particular to record the source of information in my notes. I have, however, tried my best to state the source wherever possible, and if I happen to omit any author I crave his indulgence and assure him that it is not intentionally done.

The writing of the MS. of the book was completed last year. However, without altering the general design and arrangement, the subsequent events, *e.g.* the Currency and Reserve Bank Bills, the Japanese banking crisis, the closing of the Bengal National Bank, etc., have been duly recorded and taken note of, either in the shape of footnotes or appendices.

Principal M. L. Tanan of the Sydenham College of Commerce and Economics, Bombay, Mr. Dady N. C. Nanavaty of the Central Bank of India and Mr. F. O'Reily, Retired Headmaster, St. Joseph's School, Lucknow, have been kind enough to render me very valuable assistance and advice in compiling this work and I take this opportunity, of expressing my sincere thanks to them.

I am grateful to Lala Harkishen Lal for kindly writing a Foreword for this book.

Owing to the pressure of official duties and the short time in which the book has been written I am afraid I have not been able to give as concentrated an attention to the writing as I should have wished. I am conscious that there is some scope for improvement. However, as the problem is urgent I have thought it advisable not to delay its publication. After all, in cases of this nature it is the matter which counts more than the form in which the matter is presented.

B. T. THAKUR.

CALCUTTA,

19th June, 1927.

FOREWORD

Mr. B. T. Thakur, a high official in the biggest purely Indian Bank and the writer of a comprehensive and suggestive work on "The Organization of Indian Banking", some months ago asked me to write a foreword to his treatise and I readily agreed knowing that Mr. Thakur was a serious student of and an active actor in the banking drama of the country; and one who believes and writes that the importance of organising Indian Banking cannot be minimised or belittled. I realised this situation as far back as early nineties of the last century and attempted to draw attention in a much humbler but more practical way than by attempting a complete survey of the situation and prospects for which perhaps the material was not then quite ready or ample. In those days actual experience gained by working in a Bank was not possible in a capacity from where one could focus attention on the whole panorama of banking. Mr. Thakur being a younger man by quite a generation, has had splendid opportunities of viewing the whole panorama of Banking by holding a very high position in a large Bank from which he could command a place of vantage; and he has freely added to his opportunities by constant observation, by a continuous study and by a special journey to England and the continent of Europe, to compare his conclusions of Indian Banking problems with realities and actualities elsewhere. There the results of long and continuous experience extending over several centuries could be studied and compared more effectively than by a sit-at-

home attempt. Mr. Thakur has unreservedly placed the results of his study, observation and experience at the disposal of the reader of his work styled "Organization of Indian Banking" and one ought to feel really grateful to him; for it is quite conceivable and likely that his attempt at the right time and in the right direction may lead to public discussion of the various aspects of the Banking problems of India and help in their right solution.

Mr. Thakur has divided his work into 15 chapters each being a complete survey of the problems indicated at the head of the chapter. Chapter "Introductory" is naturally the most important as therein he unburdens his full mind and gives expressions to his long cherished notions and feelings. He says that if the people who manage banking concerns are competent, honest, sincere, enthusiastic, respectable and desirable in every other respect, they will inspire confidence. This is very good and fixes a very fair standard of selection for employers, but one might ask, has this high standard been generally neglected in the past or is likely to be buried in the future. My own experience of banking now extending over 34 years leads me to say that this standard is quite easy to maintain in this country and fortunately most Indians can readily answer to these queries in the affirmative.

Mr. Thakur then passes on with enthusiasm to the much discussed question of "Safeguarding interest of depositors against reckless dissipation of their funds by unscrupulous bank directors." If legislation could accomplish this and would assure every depositor that his money will be quite safe under a new legislative dispensation and more so than it is at the present time one would welcome such legislation and wait; but this

has not been yet accomplished even in England or Europe. Without any specific legislation the results of Indian Banking of a quarter of century have been more praiseworthy than anywhere else. Humanity has not yet invented such a perfect legislation and Mr. Thakur himself leaves it to others to devise this legislation, therefore it appears that one should not wait but do the little that one can under the present imperfect human constitutions and human institutions. The law of the survival of the fittest would operate as effectually in this as in other spheres of creation. To create a better humanity by legislation would be quite a new thing and need not be attempted. To regulate by legislation is quite possible ; but the time for that always is when a type has come into existence and has to be perpetuated. Indian Banking must pass through a series of changes before a suitable type is evolved. This type would evolve only when national commerce, national industry, and national agriculture with national fiscal policy are evolved. When is that to be ? On the contrary infanticide of banking is at present apparently looming in the legislative chambers. As a sonless Hindu seeks the help of charms, incantations and prayers for the blessed one to appear to continue the name and the race, so does a Hindu whose country does not present modern industrial growth of Europe ; and which has very little vested interest in its international commerce and trade. But take it from those who have given life-thought to these problems that it is the Hindu himself in his non-official capacity who will win the race for prosperity for his country ; and establish a race of blessed ones to come and to go in the right time.

Mr. Thakur is much more on a solid ground when he addresses his appeal to his own countrymen as shown

from random quotations. "Every country sees that its own banking institutions are developed as quickly as possible if its finances and through it all other activities are not to be dominated by foreign interest." So far excellent, but when he adds that "and how could we bring this about unless there is suitable legislation and support from the country's government" an old man like myself demurs. The older man has better reasons and more experience to guide his opinions than the young Thakur has. Mr. Thakur's survey of banking functions and activities is sound and good as it is based on experience; and his historical survey also appears to me to be quite correct as he therein speaks from the book; but lessons to be learnt and right inferences to be drawn from a survey of the lives of the dead (banks) has not been attempted.

He deals with the "Imperial Bank of India" chapter III, "Backwardness and Defects," chapter IV, and "Two Models" chapter V. In this chapter he gives a reliable account of banking systems of Europe and America and its perusal affords very valuable and suggestive help to the enquirer. Those chapters are followed by chapter VI on "Issues" and chapter VII on "Government Control." Chapter VII is one with which I can't agree for several reasons, the one important being that under the present system of Government in this country there is a very wide gulf between the provisions of an enactment and its administration. It has been noticed, in the case of Land Alienation Act of the Punjab, that the administration has straightway negatived the expressed intentions of the legislature.

Chapter VIII deals with the "Central Bank" and Mr. Thakur ventures on certain opinions but the Draft

Bill now being circulated and considered under the name of "The Reserve Bank" does not, I regret to notice, take full measure of Mr. Thakur's hints by anticipation. The author then proceeds with chapters IX, X, XI and so on, on "Bank Law", "Foreign Banks", "Indian Exchange Banks", "Agricultural Credit", "Industrial Banks", "Other Banks and Bankers" and lastly a chapter dealing with general matters, e.g., propaganda, vernacular accounts, stamp duty, commercial law, mortgages, etc.

For want of time in consequence of an accident I am v ry sorry not to be able to specifically express appreciati n of much widsom and shrewd common sense to be gathered from these pages. I have no hesitation in recommending a careful study of this very creditable effort of Mr. Thakur, and I wish him every success.

LAHORE,

HARKISHEN LAL.

Dated, 16th May 1927.

Since writing the above I have had to study the "Reserve Bank" Bill in a meeting of experts and have been favoured with Mr. Thakur's notes on the same.

One could not devise a deeper measure of monopolising the whole banking of India and more complete usurpation than this Bill does. It amounts to this :—

No Banks but the Imperial Bank of India, no humbug of National Banks, Industrial Banks, Commercial Banks, but the Imperial Bank of India. If the favourite one appears in a fisher's hut or on house boat or in Tambucto, three laes free of interest for five years equivalent to a gift of Rs. 21,000 a year at the

present rate of the Imperial Bank investments. Then the free supply of gold ; not from the Reserve Bank. How sometimes positives are used to mean negatives. I do not propose to dilate on the interliner readings of this measure as I have no doubt Pandit Moti Lal Nehru and his flock in the Assembly and Mr. Thakur outside will be able to meet the situation.

H. L.

16-5-27.

CONTENTS

| | PAGE |
|--------------------------------------|------|
| PREFACE | vii |
| FOREWORD—BY LALA HARKISHEN LAL . . . | xi |

CHAPTER I

INTRODUCTORY

| | |
|--|---|
| Basic conception—East familiar with credit transactions in ancient times—Derivation of “bank”—Money changing—Goldsmiths—Brief history of banking in Europe—Functions and Services—Factors inducing bank deposits—Credit, greatest of banking utilities—Bearing of finance on national interests—Bank of Issue’s utility and importance—Unification of credit and currency—Banks powerful but necessary—Influence on economic activities. | 1 |
|--|---|

CHAPTER II

SURVEY

| | |
|--|----|
| Banking existed in India before British Rule—Indigenous bankers, their business—Early joint-stock banking and its history—Presidency Banks—European hand in bank development—Indian activities in corporate banking—Bank failures—Apathy of Europeans and Government to Indian banking concerns—Exchange Banks—Co-operative Credit Societies—Post Office Savings Banks— <i>Shroffs</i> (native bankers). | 25 |
|--|----|

CHAPTER III

MAJOR BANKS

| | |
|--|----|
| IMPERIAL BANK : Amalgamation of Presidency Banks and Imperial Bank Act—Capital—Management—Business permissible—Restrictions on business—Examination of business figures—Comparison with Central Banks—Tests applied to its working—Complaints against it—Hybrid constitution—Future status and scope; INDIAN JOINT-STOCK BANKS : Registered under Indian Companies Act—Only six banks with deposits over Rs. 1 crore, their names.—Central Bank of India and Pochkhanawala—Competition of Imperial and Joint-stock Banks—Business—Business figures ; EXCHANGE BANKS : Name Foreign Banks more appropriate—Their names—Business—Finance of foreign trade illustrated—Arrangements and facilities in foreign countries—Help foreign merchants and manufactures—How Indian interests suffer at their hands—Predominance in Indian banking. | 45 |
|--|----|

CHAPTER IV

BACKWARDNESS AND DEFECTS

Comparison of banking business of India and United Kingdom, India and Canada, India and Australia, India and United States—Indian banks smaller in size than banks in other countries—Figures of some important banks of the world—Analysis of Indian banking figures according to nationality of capital holders and management—Indian banking not only inadequate but wanting

| | | |
|---|--------|----|
| in systematic organisation—Causes of backwardness : Defects—Components of complete banking system | | 79 |
|---|--------|----|

CHAPTER V

TWO MODELS—EUROPEAN AND AMERICAN

| | | |
|--|--------|------------|
| The Central banking system of Europe and the Federal Reserve system of U. S. A.—EUROPEAN BANKING SYSTEM: Constitution, functions and responsibilities of Central Banks—Whether Central Banks should be owned by State—Bills as reserve for currency—Other classes of banks—Bank rate and its influence—Transactions of bank of issue and commercial banks compared—Peculiarities and tendencies—FEDERAL RESERVE SYSTEM: Principle of federation—Brief history—Early enterprises—State banks, National banks and Trust companies—Crisis of 1907—Aldrich Vreeland Act—National Monetary Commission (1908)—The Federal Reserve Act—Provisions of the Act—Federal Reserve Board, and Federal Reserve banks, their functions and powers—Central banking and Reserve system compared—Peculiarities of American banking organisation—National bank laws—State bank laws—Trust companies laws | | 102 |
|--|--------|------------|

CHAPTER VI

ISSUES

Whether Government administrative organisation to watch and examine banking activities necessary—What form should the Central

| | | | |
|---|-----|-----|-----|
| banking institution take—Whether special banking legislation necessary — <i>Re.</i> formation and constitution of special banks—Whether municipal and local bodies should do banking business; if so, whether under any restrictions — <i>Re.</i> private efforts | ... | ... | 151 |
|---|-----|-----|-----|

CHAPTER VII

GOVERNMENT CONTROL

| | | | | |
|--|-----|-----|-----|-----|
| Banking section in the Finance Department of the Government of India—Comptroller of Banks : his functions and powers—Banking Council : its powers and duties—Bank Examiners : their work, scope of duties, and functions | ... | ... | ... | 161 |
|--|-----|-----|-----|-----|

CHAPTER VIII

CENTRAL BANK—RESERVE BANK FOR INDIA

| | | | | |
|--|-----|-----|-----|-----|
| Whether Imperial Bank of India can be suitably transformed into Central Bank—Compensation to the Imperial Bank for loss of Government banking business—Special charter for incorporating bank of issue—Period of charter—Capital—Shares—Votes and Meetings—Directors—Branches—Management—Local Advisory Committees—Business : Deposits, Investments, Agency, Internal Rupee transfers—Currency functions—Profits—General: Clearing Houses, Safe custody, Audit and Examination, Discount rate, Weekly statement, Balance Sheet, Taxes, Other responsibilities, Liquidation, Staff, Miscellaneous | ... | ... | ... | 171 |
|--|-----|-----|-----|-----|

CHAPTER IX BANK LAW

| | |
|--|------------|
| Scope—Organisation—Incorporation—Classes of banks—Capital—Security Deposit—Certificate to commence business—Directors—Local representation—Business : Deposits, Cash and bank balances, Liquid investments, Bank acceptances, Advances and maxims of Safety, Liquidity and Diversity, Other investments, Agency, Safe Custody, Trust business—Accounts and Audit, Form of monthly statement—Government examination and control—Safety fund—Clearing Houses—General: Examination tax, Penalties, Voting power of banks, Winding up, Date of operation | 213 |
|--|------------|

CHAPTER X FOREIGN BANKS

| | |
|---|---------|
| Necessity of Control over foreign banks—Cunliffe Committees' views on the activities of foreign banks in England—Argument of Imperial brotherhood—Conditions generally imposed—Restrictions suggested : License ; Penalties for not taking license ; should be subjected to appropriate sections of Bank Law, should submit returns and be controlled by appropriate authorities ; Indian advisory committees ; Practice in France ; Caisse de Dépôts et Consignations ; Ordinary and special taxes payable | ... 248 |
|---|---------|

CHAPTER XI INDIAN EXCHANGE BANKS

| |
|--|
| Object—Provision under "Overseas Banks"—One strong bank necessary—It should be |
|--|

| | |
|---|-----|
| a combine of Indian banks for foreign exchange business—Imperial Bank's transformation into the proposed bank—Important points in connection with proposed constitution : Capital, Directorate, Facilities at the bank of issue, Business, Branches, Taxes, Profits, Management, Examination, etc.—Remarks explaining the above ... | 259 |
|---|-----|

CHAPTER XII

AGRICULTURAL CREDIT

Necessity for agricultural credit—Short and long term credit—SHORT-TERM CREDIT : Purpose—Security for credit—Basic idea of credit unions—Originated in Germany—Raiffeisen and Schulze-Delitzsch systems, their peculiarities and objects—How credit machinery works—Constitution of central credit society—State assistance in credit arrangements, basis for such assistance—Principle of co-operation and joint-responsibility introduces sufficient security—Ministry of Agriculture and Fisheries' Report—Maclagan Committee—Drawbacks of Indian system—Ways and Means to reorganise suggested : Propaganda, Provincial Agricultural banks, their constitution and functions, Agricultural Credit Board, Discounts and rediscounts, Charge on farm wealth, etc.—LONG-TERM CREDIT : Importance of German land mortgage banks—Working explained—How repayments facilitated—Experience of land mortgage banks—Bonds as means of obtaining money—Peculiarities explained—Rentenbank as a means to rehabilitate German currency—Long term credit facilities

| | |
|--|-----|
| in the U. S. A : Federal Farm Loan Act, 1916, Federal Farm Loan Board, Method of working explained, American Government help—Credit Foncier de France and subsidy by French Government—Necessity of mortgage banks in India—Would promote land owning farmers—Plan of organizing land mortgage banks in India : Provincial land banks, Directorate, Management, Business, Facilities at the bank of issue, Government assistance, Profits, Taxes, Land Credit Board, etc. | 270 |
|--|-----|

CHAPTER XIII INDUSTRIAL BANKS

| | |
|--|-----|
| Necessity for industrial development—Cottage industries—Industrial Commission's report—Need for organising industrial credit—Result of such efforts in other countries—Activities of company promoter and industrial bank compared—Two Divisions of Industrial Credit : Industrial Credit Unions and Industrial Banks—French and Japanese industrial banks—Working explained—their financial operations—Arrange foreign loans—Difference between the economic effects of foreign capital and foreign loans—Loan operations of the Industrial Bank of Japan—Japan's ambition in the industrial world—State participation in organisation of industrial credit—Outline of credit construction : Provincial organisations, Capital, Directors, Business, Facilities at the bank of issue, Inducements to be offered by Government, Profits, Taxes, Examination, Industrial Credit Board, Management, etc. ... | 310 |
|--|-----|

CHAPTER XIV

OTHER BANKS AND BANKERS

| | |
|--|-----|
| POST OFFICE SAVINGS BANKS ; Improvements suggested : Accounts, Nominees, Deposits by cheques, Limit on annual deposits, Limit on balances, Home Savings safes, Attachment of deposits, Savings facilities for villagers, Letters of Credit—MUNICIPAL AND LOCAL BOARD BANKS ; Object and scope—Municipal Bank of Birmingham—Capital not necessary—Some useful services they can render—Investments—Method of keeping funds—Management—Profits—Small offices to work by turns—CO-OPERATIVE BANKS ; Principle already explained—Capable of extension to a variety of homogeneous groups—PRIVATE BANKS AND BANKERS ; No restrictions needed—Should not participate in trading—Compared to English bill brokers—Conversion of private into corporate banking—“ <i>Commandit</i> ,” <i>i.e.</i> , Limited partnership, principle explained—Opportunities for its development in India. ... | 334 |
|--|-----|

CHAPTER XV

GENERAL

Factors which, though not a part of the organization, will assist and accelerate banking construction: Propaganda—Vernacular accounts and signatures—Stamp duty—Modification of Commercial law relating to Mortgages, Pledge and Hypothecation, Registration of trade names, Investment of trust funds—Bank of issue's special facilities—

| | PAGE |
|--|------|
| Government and cheque currency—Prize drawings—Bankers' association : provincial associations and their federation—Institute of Bankers—Conclusion. | 355 |

APPENDICES

| | |
|---|-----|
| A. Remarks on Reserve Bank Bill | 375 |
| B. Note on Currency | 387 |
| C. Charter of Netherlands Bank | 403 |
| D. Charter of Reichsbank | 416 |

STATISTICAL APPENDICES

| | |
|---|-----|
| I. Table showing total Capital, Reserve, Deposits, and Cash Balances of the old Presidency Banks and their amalgamated institution the Imperial Bank of India | 445 |
| II. Table showing total Capital, Reserve, Deposits and Cash Balances of the Indian Joint-Stock Banks | 446 |
| III. Statement showing failures of Indian Joint Stock Banks | 448 |
| IV. Table showing total Capital, Reserve, Deposits and Cash Balances of the Exchange Banks working in India | 449 |
| V. Statistical Tables relating to Co-operative Societies | 450 |
| VI. (a) Balance Sheet of the Imperial Bank of India as on 31st December, 1925 | 453 |
| (b) Weekly statement of the affairs of the Imperial Bank of India as on 17th September, 1926 | 455 |

| | PAGE. |
|---|-------|
| (c) Fortnightly Statement of the Central Bank of India, Ltd., as on 15th September, 1926 .. | 456 |
| (d) Balance sheet of the Central Bank of India, Ltd., as on 30th June, 1926 | 457 |

CHARTS

| | |
|--|-----|
| CHART illustrating Backwardness of Indian Banking Frontispiece; | |
| CHART showing fluctuations in Rupee-Sterling exchange and changes in Bank rate ... | |
| At the beginning of Appendix B. | |
| INDEX | 459 |

CHAPTER I

INTRODUCTORY

Basic conception—East familiar with credit transactions in ancient times—Derivation of “bank”—Money changing—Goldsmiths—Brief history of banking in Europe—Functions and Services—Factors inducing bank deposits—Credit, greatest of banking utilities—Bearing of finance on national interests—Bank of Issue’s utility and importance—Unification of credit and currency—Banks powerful but necessary—Influence on economic activities.

Banking is an essential economic activity of human society upon the sufficiency and adequacy of which depends its proper economic advancement. In one form or another services corresponding to it have been in existence since very early days. The most elementary economic ideas to save or store and lend, which constitute basis of principal functions of a bank have been in existence since ages. In the early stages of society when institution of money was unknown, people who had no immediate use of their goods or had more than what they required would lend the excess to others who needed them, on the promise or guarantee that such goods, or others, but equivalent in value, would be returned to them at some later date. For example, those who grew cotton would lend certain quantities to spinners and weavers, who would liquidate such loans in yarn and cloth. Originally such transactions were direct, but later when society passed the earlier stage of development, the holder of surplus

goods found it inconvenient or difficult to get at reliable borrowers of his goods, and there came into existence a sort of intermediary who specialised in mobilising the surplus commodities and in lending them to those, who either needed them or could work them up. This intermediary corresponds to our present day Banker. For his services he would get something more in exchange value than what he had lent and likewise as an inducement to people to entrust their surplus stock to him, he would promise them some extra exchange value. Such excess charge and payment correspond to our present day notions of interest. Next, when the system of barter or direct exchange of commodities disappeared on the introduction of money ideas, the excess goods were translated into money, unless the holder thereof as a merchant traded in them, which ultimately brought into existence the deposit of money and its subsequent lending. From this period may be traced the history of banking as it is now understood.

Credit transactions have been carried on in the East—India, China, etc., centuries before Grecians and their conquerors the Romans developed their social organisation. There are references in Manu's books about credit and the rate of interest. Egypt was not unaware of banking operations in her old lofty days. In Assyria they used the instruments of credit even before the advent of official coinage. Later in Athens and Rome the Bankers' calling was publicly recognised. These instances confirm that the business of banking has been in existence in the world long before Europeans realised its advantages and established it on systematic basis.

The word "bank" in the economic sense covers various meanings which all express one object, a contribution of money for a common purpose. Thus Bacon in his essay on usury, while explaining "how the discommodities of it may be best avoided and the commodities retained" refers to a "bank or common stock" as an expression with which his readers would be familiar. Originally connected with the idea of a mound or bank of earth, the term has been gradually applied to several classes of institutions established for the general purpose of dealing with money. Another derivation connects it with "banc" or bench upon which the medieval European money-lenders and money-changers used to lay out their stock and carry on their trade. These derivations, which refer to the introduction or establishment of banking in Europe, do not carry us beyond the middle ages; but they by no means suggest the date of origin of banking in the world which as already remarked is much more antiquated. The credit instruments were known to the Asiatics and the nations in trade relationship with them, centuries before the medieval banker in Europe had developed and perfected his Bill of Exchange.

Money-changing was once regarded principal function of a banker though now-a-days he hardly touches it. It is easy to see why it was so. On the introduction of institution of money different countries adopted different metals and of varying weights, as units of money. This led to the necessity of some sort of organisation whereby money of one country could be changed into that of another. This was but natural. Ways had to be found whereby people in commercial relationship must settle their transac-

tions and pay differences in different monies, which must be changed into the money of their country, where they carried their main business. This brought into existence money-changers who tried to remedy the inconvenience to which merchants were subjected through the uncertain value of different currencies. They were shrewd and soon realised that they could make much better use of their commodities (monies) and also increase their profits. This led to the introduction of credit instruments, deposits, lendings, etc. Thus the later banker was a growth out of the previous money-changer and he naturally long stuck to and regarded his previous occupation of money-changing as his principal business.

In England banking came to be developed through goldsmiths who since the days of James I (1566) accepted deposits for safe custody and gave in lieu receipts or notes for such monies payable on demand. This can be fitly described as the origin of deposit banking in that country. In course of time these receipts or notes began to pass as money from hand to hand. The goldsmiths soon realised the importance and profitable nature of having others' money on deposit and its subsequent lending. The goldsmiths' notes are the origin of the bank notes in England. The system of issuing notes for money deposited continued till 1781 when the London bankers gave cheque books in lieu of notes.

The European banking is indebted to the Jews for the great stimulus which this "despised but industrious race" gave to this form of economic activity. They were excluded by almost all the Christian countries from possessing land which

forced them to have their possessions in liquid form. The constant dread of confiscation sharpened their ingenuity in devising instruments for the rapid and secret transfer of their property which brought into existence in Europe "The Bill of Exchange." Moreover, Christianity forbade the lending of money at interest. This threw the responsibility of finance upon the Jews who grew into a powerful financial race. In course of time their strength and power was very keenly felt by the Christian people who began to change their notions about interest. The European legislators began to permit interest at reasonable rate and determined efforts were made to dislodge the Jews from the supreme position which they had begun to assume in the civic life. Be it said to their credit, the Jews even to-day occupy most important position in the financial world. Some of the biggest banks in the world are owned and/or controlled and/or influenced by these people.

The early bankers did not confine their activities to banking alone. In almost all cases they did other business side by side. It is true that even in the present day some commercial houses have their banking departments but their banking activities are of secondary importance and do not occupy any important place in the banking world. Indian bankers in the past have generally carried on ordinary trade with their banking business with the result that this dual activity has greatly reacted upon banking development of this country. It is only very lately that private Indian bankers have realised the strong necessity of not adding ordinary commercial transactions to their credit business.

As Europe is the pioneer of modern banking it may be interesting to look into its banking history. The banking activities in that Continent developed originally in two directions : " Deposit Banks " and " Exchange Banks " which later mixed with and merged in each other. The Banco di Rialto was the first public bank of the former type founded in Venice in 1584. This bank was called into existence by the natural development of trade to facilitate trade transactions. There are also examples where banks were established by governments not only to facilitate trade of their countries but actually to develop the same. Of the latter type the Bank of Sweden established in 1656 is the earliest instance and it still continues to be the State Bank of Sweden. To this bank is also due the credit of invention of the bank note—perhaps adoption for use in Europe is the better expression, as notes were current in China about A.D. 800. Of the examples of the earliest exchange banks we have Bank of Amsterdam (1609) and Bank of Hamburg (1619). It may be mentioned here that the exchange banks of old differed from banking as now understood. They dealt with foreign exchange and facilitated trade with other countries. Receiving deposits and making loans were not their original functions though they grew up in course of time. They had no capital of their own nor did they require any for the performance of the restricted nature of business which in those days constituted banking. The Bank of Amsterdam was started as a result of the increased international commercial importance of Holland and to avoid the dangers of clipping to which the Dutch currency was subjected. The ordinance which

established the bank required that all bills of 600 *gulden* (£ 50) or upwards should be paid through the bank, or in other words by the transfer of deposits or credits at the bank. These transfers afterwards came to be known as bank money. The charge for making the transfers was the only source of income to the bank. It was required to keep the whole specie for which bank money was outstanding in its vaults. This regulation was, however, not strictly observed. Loans were made on the various dates to the Dutch East India Company and City of Amsterdam. News of these loans impaired the public confidence, and the bank, "after holding the leading place in European commerce for generations," ceased to exist in 1820. The Bank of Hamburg continued to occupy its predominant position in banking till 1873 when its existence was closed by the act of the German Parliament which decreed that Germany should possess a gold standard. This removed those conditions of the local medium of exchange—silver coins of very different intrinsic value whose circulation had provided an ample field for the operations of the bank. The Bank of Hamburg's business was to assist commerce, not by loans, but by the local manufacture, so to speak, of an international coinage. "By supplying a currency of universal acceptance the Bank of Hamburg greatly contributed to the prosperity of that city." *

The Bank of England, the first public bank of that country was founded in 1694. A loan to the British Government was the origin of its establishment which constituted its capital. The management of the British National debt was entrusted to it.

Its scope of usefulness was enlarged from time to time and to-day it is one of the most powerful banks in the world. This is the only bank which enjoyed the privilege of limited liability long before it was publicly legalised in England. For, up to the date of the act of 1862 permitting limited liability, every shareholder in a Joint-stock Bank was liable to the extent of his whole fortune. It may also be mentioned here that in a way even Joint-stock Banking was not permitted till 1833. The Act of 1707 which prohibited more than six persons from issuing promissory notes was intended to prevent any bank being formed with more than six partners, because the issuing of promissory notes for deposits received was then essentially the main feature of banking. This had the effect of preventing any Joint-stock Bank being formed.

In France the first public bank was established in 1716. It was converted in 1718 into Banque Royale and its notes were guaranteed by King Louis XV. The bank, however, failed 3 years later in 1721. Some attempts were made to start fresh banking enterprises but without any material result. Napoleon, however, realised the necessity of having a credit institution and he founded in 1800 the Bank of France which has remained from that time to the present day the most powerful financial institution in that country.

We do not think it necessary for the purpose of this book to pursue any further the historical development of European banking. The few instances that we have given will suffice to show its origin and initial stages of progress.

The present is the age of mechanical development. We find concerns and enterprises on such a large scale as would have been considered impossible in the last century. They have been accelerated into existence by the keen competition which has resulted from the narrowing, if not elimination of distances due to the progress in locomotion, shipping, aerial navigation, telegraph, telephone, radiography, etc. The element of cost is most important and cost can be reduced by large scale production, though after a certain stage the law of diminishing returns sets in. Such big enterprises require much bigger credit facilities than what have been available in the past. This has necessitated organisation of credit institutions so as to meet the modern credit demands. By organisation, systematic work, and co-operation of all concerned, modern banks have developed business, strength and solidarity undreamt of in the past. The fundamental principles of banking are the same whether in the past or now: they are simply getting new shapes and new forms to meet varied needs. Further, it is the organisation, the marshalling of banking activities, which has developed all the latent powers of banking and brought into relief its tremendous strength in the modern economic life. Countries which wish to develop their economic career and do not desire to be swallowed up by foreign competition must first devote their attention to the problem of their credit institutions, satisfactory solution of which is most essential before their other economic activities can progress.

The most important services which modern banks are capable of rendering to society are in

the following directions :—

- (i) Mobilisation of savings and the inculcation of habit of thrift.
- (ii) Organisation of credit on the basis of money deposited with them.
- (iii) Financing of human activities.
- (iv) Exchange and transmission of money.
- (v) Management, control, and issue of Bank Notes—a form of money usually adopted by all the principal civilised countries.
- (vi) Regulation of money market.

The modern banker besides the above functions discharges many useful duties like those of an agent, a trustee and so forth, which, because of his relationship with a vast clientele, he has been called upon to perform in the spirit of rendering greater facilities to his customers. For example he purchases and sells shares and securities on behalf of his customers, he advises them in the matter of investment of their surplus funds, procures insurances of every description, assists in income tax matters, manages affairs of those who may be either in difficulties or require his help, works as executor, administrator, receiver, liquidator, and trustee and so forth. He accepts articles for safe custody and sometimes conducts a special Safe Deposit Vault for such purposes. He procures credit information for his customers. In countries like Germany, France, Holland, Italy, etc., every important bank is a member of the local Stock Exchange and thus not only expeditiously carries out orders of its customers regarding Stock Ex-

change transactions but actually helps to keep the market active and alive. European, specially continental banks are reckoned to be amongst the biggest underwriters of new first class flotations and bring into close touch the real small investors of the country with those wanting capital. They are thus the most powerful instrument in keeping up the economic progress of their respective countries. Some of the continental banks to facilitate investments actually permit delivery and lodgment of bearer securities just as money is withdrawn and deposited by cheques and paying-in-slips. But as the agency functions are not essential to a banker, they will not be dealt with at length here.

If the institution of banks were unknown, people would either hoard their savings or lend directly to those who needed them. In the former case, the savings would remain idle : neither would they bring any return nor be of any use to those who might need them ; also the risk of preserving their monies from theft and the like dangers would fall upon the owners. Further, money in such cases would usually consist of precious metals, which would tend to make greater calls upon their availability with the result that their exchange value would continuously increase—a factor disturbing in itself. If a person thought of lending directly, that would not be possible in every case because he might not know the person who wanted such assistance. Also he might not possess knowledge and ability required for safe lending. Further the lender might not be able to get back his loans when he wanted, whereas in banks, money could be deposited with condition to withdraw it on demand, or at notice

as the depositor pleases. Also a borrower generally finds dealings with a systematic and regular banker more satisfactory. Banks stimulate savings by offering inducement of interest; amounts, however small, are always acceptable on interest to a banker, which ordinarily in themselves may not be of practical use to a borrower. All the above things considered, the banks are doing a distinct service to society in organising accumulation of savings.

There are, however, a few factors, which affect the utility of banks as machines of savings. The first is that the banking system should command requisite confidence of the depositing public. This confidence may be the product of various factors. If the people who manage banking concerns are competent, honest, sincere, enthusiastic, respectable, and desirable in every other respect, they will inspire confidence, provided the general atmosphere and other conditions are satisfactory. Again, confidence may be built up by banking firms and houses gradually after long years of steady, satisfactory work; or in the case of countries newly developing banking institutions on modern lines it may be assured by banking legislation safeguarding interests of depositors against reckless dissipation of their funds by unscrupulous bank directors. It is ridiculous to say that because some countries have been able to build up banking traditions commanding public confidence without any legislation, the countries that are now thinking of systematic growth in this direction, should do likewise. Is it not a fact that the oldest countries have passed through great crisis, which might have been averted

or at least greatly reduced if there had been some sort of control, check, or examination? Again, is it not a fact that the unscrupulous acts of a few have reacted upon the prestige of others and retarded their normal growth? And again, what is wrong in profiting by the experience of others and devising means of smooth and steady development? Pages of history of banking in other countries amply show the need of legislation at least in countries now thinking of systematic development. Let those who doubt read "Romance and Tragedy of Banking in America" and they will be convinced of the force of the above arguments. The present powerful financial and credit structure in America has been greatly accelerated into existence and developed by the existence of banking laws in that country.

Banking is like every other business—those who start early with benefits of past connections and traditions have immense advantages. Even if they move out to new territories they are generally sure of success—these are advantages which the new entrants do not possess, and as such their development is tardy, spasmodic and not without disappointments and failures. Is it not the duty of the State, to find out means by which its institutions are not jeopardised by foreign concerns, merely because the latter come with past history? Every country must see that its own banking institutions are developed as quickly as possible if its finances and through it all other activities are not to be dominated by foreign interests. And how could we bring about this unless there is suitable legislation and support by the country's government?

Banks deal with that precious commodity, money, that unless people were absolutely sure of the safety of their deposits they would not entrust them to banks. And this confidence can be induced, accelerated and fostered by bringing into existence suitable requisite machinery.

The second factor, which successfully induces deposits in banks is, that money should have comparatively stable value. If people are not sure that their money would not depreciate in the course of time during which it lies with banks, they would rather think of converting it into more stable values, like currencies of other countries, precious metals, stones and the like. This is not a work on the monetary reform of India and as such we do not wish to burden its principal pages with any discussion of this subject. But as the currency problem is so intimately connected with banking we shall be giving our views in an appendix.

Other factors affecting this aspect of banking are :—banking habits, depositing facilities, inducement of interest to depositors, withdrawal of money without any extra cost and so on. Banking habits will be developed as a necessary corollary to the foundation of confidence, and require some propaganda. Depositing facilities would multiply as the banking system gains momentum. At present the whole of Europe is studded with banks—even the smallest territorial units are not lacking in banking facilities. Inducement of gain to depositors will be offered by interest. This, however, will have to be limited by the necessity for money and other circumstances, but can be made attractive by prize and lottery drawings, etc. Withdrawal of

money from banks can be made without any cost by abolishing stamp duty on cheques as is the case in America and Germany.

Banks do not accept deposits for the mere fun of keeping money with themselves, but they use them as basis on which they organise credit with which they finance economic activities. The construction of credit is perhaps the greatest of banking utilities. Every unit of money that is not kept in actual circulation or not hoarded but is deposited in banks, serves the purpose of at least 5 units. This may appear as a paradox, but will be apparent on little explanation. Let us assume that banks keep 20 per cent. of their deposits as cash with themselves, and the rest they lend—this is the usual practice. And if the sums advanced are again deposited with the banks, $\frac{4}{5}$ ths of these will again be lent and so on *ad inf.*—This is, of course, on the assumption that the banking system is sufficiently developed, and the amount of money going in actual circulation, by actual withdrawals from the banking organism as a whole, is small. Thus the total cash with banks, satisfies claims of depositors upto at least five times its amount. Claims for money on banks may either be in respect of original savings deposited or in respect of advances made subsequently therefrom. If banking is developed sufficiently, the cash percentage may safely be reduced to 15 in which case every unit deposited serves the purpose of 7 units. This shows how banking credit is of even greater importance, for the development of a country's commercial and industrial activities, than the actual volume of money itself. By the inculcation of banking habits

and introduction of adequate banking facilities legal tender currency of a country can be made to satisfy financial and credit needs many times over and above its volume. A German writer has summed up the credit utility of a bank as under :--

“Through the activity of the bank, the deposit is made to perform several economic tasks at one and the same time. The same sum which the customer has entrusted to the bank may be used by him for business purposes, the manufacturer being able to make contracts, the merchant to order goods, etc., on the strength of his bank balances ; the banker uses the money for his own purpose, granting a loan to a customer. The customer again—say, a manufacturer—uses the loan to pay his workmen, who in turn use it to make purchases ; and all these transactions take place during the intervening few weeks while the deposit remains at the bank. Thus the same sum has performed several economic functions at the same time and in so doing has rendered to the public several times the amount of service that it could have done without the intervention of the bank. Here lies the main advantage of the banks for the money circulation, an advantage which is not sufficiently appreciated.” *

* Director of Statistic's Memorandum on Banking to the Industrial Commission.

[Students of Mathematics can easily verify the above truth by a simple algebraical calculation. Assuming that a sum of money M is deposited and a cash percentage of 20 per cent. is to be maintained, then out of M , $\frac{4M}{5}$ will be advanced and $\frac{M}{5}$ will be retained as cash. $\frac{4M}{5}$ will in turn be deposited in banks by the borrower or borrowers, which will again be treated like the original deposit, *i.e.*, $\frac{4M}{5} \times \frac{4}{5}$ will be kept as cash, and $\frac{4M}{5} \times \frac{4}{5}$ advanced again. The last item will again come as deposits to banks, and be treated in the same way. Ultimately with M units deposited in the beginning the banks will have $M\{1 + \frac{4}{5} + (\frac{4}{5})^2 + (\frac{4}{5})^3 + \dots \infty\}$ deposits built up. The above series can be summed up as a geometrical progression and is equivalent to $5M$.

If M be equal to the volume of legal tender currency, by organisation of banking, it can be made to yield the same amount of financial service as $5M$.]

Savings, which banks accumulate and the credit which they build up are only as a means to the financing of human activities. Agriculture, trade, industry, transport, etc., all require money or orders to money for their existence and growth. Rightly are banks described as giving life blood to human activities. But whether they render this assistance in the right direction or not is another question. They are capable of this power, but sometimes they utilise it, not in the interests of the country where they flourish, but in other interests. If sufficiently powerful and unchecked, they are capable of crippling industry and trade whenever and wherever they wish. It is of utmost importance that financing activities should be direc-

ted in the national interests, and all encouragement should be extended to such of the banks as are fulfilling their mission in this respect.

Credit or financial assistance is of various kinds and can be extended in a variety of ways. It has peculiarities of its own varying with the peculiarities of the activities, which it proposes to assist. This has brought into existence different classes of banks, *e.g.*, Commercial, Industrial, Agricultural, Land Mortgage, etc. Commercial Banks are again sometimes differentiated from Exchange Banks, the latter being confined to the financing of foreign trade. Then we have private bankers or banking houses and discounting houses. Methods by which banking facilities are given take the forms of loans, cash credits, bills, both inland and foreign, guarantees, credits, acceptances, and so forth. Complete description of the above forms is beyond the scope of this book as it more suitably relates to the practical work of a bank and will be appropriate in a treatise dealing with the same. However, such of the points as can be conveniently mentioned to explain the utility and desirability of basing our banking system on a proper division of credit functions will be referred to later in their proper places.

The work of transmitting money on behalf of the customer is a great economic service, which banks have been doing since very early days. The transfer of money from one person to another may be either in the same place or from one place to another. Again it may be from one currency into another. The convenience of such a transfer is, of course, greatly appreciated if it is from one place

to another at a considerable distance. "Where an easy method of transmission of cash does not exist, we become aware that a rate of exchange exists as truly between one place and another in the same country as between two places in different countries." Moreover doing of such services economises the use of legal tender and metallic money.

All the civilised countries have by this time realised the necessity of establishing Bank of Issue, which brings into circulation paper money and concentrates deposit of precious metals for proper use. Such banks further serve as bankers' banks. Currency and credit are so interconnected that it is considered necessary to entrust unified control over them to a body like the Bank of Issue. The availability of precious metals in which legal coins are minted is restricted, which has led to the introduction of bank paper money, portion of which is backed by precious metals and the rest by other easily realisable assets. The total volume of money required to carry on all the activities of a country is much more than the supply of precious metals available to it, and the institution of paper currency has easily solved this difficulty. Without the inception of paper currency the unit of money would be liable to great fluctuations in value, causing economic disturbances and restricting proper growth of economic activities. The Banks of Issue are a powerful factor in expanding and contracting the volume of total currency so as not to cause any great disturbance in the value of money with the expansion and contraction of economic activities. The organised banking system with the Bank of Issue at its back reduces the quantity of precious

metals as backing to the country's monetary system to a very small figure, which to a layman may appear even unthinkable. It is estimated that the amount of gold with the English banks is hardly 5 per cent. of the total banking deposits and Bank of England's Notes in circulation, which means that every gold sovereign or its gold equivalent with the Bank of England, is serving as good a purpose as £20.

Banks with their ultimate support in the Central Bank or Bank of Issue are the guiding factors in the money market. If necessary they bring money from abroad for internal use or *vice-versa*. They may use their power and control over money market rightly or wrongly; they may use it in the interest of one economic activity at the cost of another, or they may abuse it and injure a nation's interests. But there is no doubt that banking like its chief commodity, money, is as powerful as money. Many conflicting demands are made upon bankers for assistance, but upon the proper distribution of their assistance depends the contented equilibrium of society.

Requisite material for the successful prosecution of any business are men, money and goods. This applies to banking also. We have enough honest and God-fearing men in this country whose names will inspire requisite confidence. Owing to the vicissitudes through which Indian banking has passed, some of them are keeping in the background. As soon as suitable legislation, safe guarding general interests and stimulating confidence is sanctioned, there will be no dearth of desirable persons, who will come forward to manage and control banking enterprises. Banking figures of other countries

show that capital forms about 5 per cent. of the total business transacted. And India can be expected to produce requisite capital for banking enterprises, if people can be reasonably secured from bank failures. Commerce Colleges and Departments of Commerce of various Indian Universities are producing good banking students. They can be trusted to be transformed into good banking officials after some training. But the only pity is that they are losing their enthusiasm and wasting their knowledge because there is not sufficient field.

From what has been said above it will appear that the present day banking is not only a very complex and specialised economic activity, but it is extremely powerful in its direct influence on the course of Agriculture, Commerce and Industry, nay on their inception, development and career, and indirectly on human happiness, through the effect, which banking and its inseparable ally, money, have upon prices, wages, and various other factors, which count in the determination of human contentment. Founding of banking system on a proper basis is of paramount importance to a country, which should receive first and foremost attention. Upon its successful functioning depends the growth of country's economic and through it political and social institutions. If banks are working with no other aim but of mere profiteering or if they are controlled by vested interests whose principal object is to further the interests with which they are connected, then it is clear that their existence is against the national interests. The cry of certain sections in some of the Western countries, including England, to nationalise banking is due to this vast

influence which banks exercise over their destiny, to the feeling that such influence is sometimes, if not often, wielded against their country's best interests and to the fear that if unchecked, in course of time, this power may develop to such an extent, as to threaten their individuality.

Some of our readers may be aware of the proverbial though magnified oppression which *Mahajan* or the village *Bania* is capable of inflicting upon his clients—they have simply to substitute the word “bank” for *Mahajan* and they will realise the great influence, which banks are capable of exercising upon society. We do not mean to say that they are actually oppressive, but we are laying emphasis on their capacity and power to stamp their will upon forms of economic activities. True, there are limitations upon their influence in the nature of public support, sympathy of depositors and so on, but they are sometimes of very small value. The influence of banks is extremely large, which a man in the street hardly realises. Banks, at times, can be, if they choose, very arbitrary and despotic. When the Bank of England was being founded in 1694, under the auspices of the ruling prince William III, people were really justified in apprehending the power of the bank “lest it should hereafter join with the prince to make him absolute and so render Parliament useless.” Students of European History must be familiar how the financiers and bankers were powerful and practically controlled the destinies of the various states. The fighting powers were always anxious to be in good books with bankers of international domicile and often their success depended upon the extent of

financial assistance which they could hope to get. Even in the last great war it was the assistance of banks which supplied the requisite money to prosecute it.

But although banks are very powerful they are still without doubt more necessary. And all that the people should aim at is to establish their banking system on proper foundation and prescribe necessary safeguards. One thing is certain that the banking machinery of a country should be in the hands of its own people who are the only persons who can feel into the spirit of the country's necessities and work it according to its needs and requirements. Such an extremely powerful weapon should under no circumstance be allowed to fall in the hands of foreigners who can never resist the temptation of wielding it in the interests of their own nations. If under any circumstances it be absolutely necessary to import foreign talent and/or money to start or give impetus to the whole movement by all means have them. but always keep the goal in front, *viz.*, to guide and control in the national interests and replace them at the earliest possible moment by the indigenous material. If foreign elements are allowed to have undisturbed field to themselves they are sure to develop into a powerful force. This is practically the present case in India, where the major portion of banking activities are in the hands of non-Indians. This has been made greatly possible by the apathy of the Indian Government. No responsible government with national interests at heart could afford to be mere indifferent spectators at the manner in which Indian banking has been allowed to be dominated

by non-Indians. Banking is the key to the solution of all economic problems and should be retained in the hands of India. The task before the people of India of reconstructing their banks although great, is quite clear. Even if India were to get self-government or home-rule, it cannot prevent the great economic loss which the country is suffering at present because its industries are deficient and undeveloped and the major portion of important economic activities are in the hands of foreigners. Preliminary step to the progress and reorganisation of all this, is a sound system of banking. Upon the proper solution of this question depends the real regeneration of this country.

CHAPTER II

THE SURVEY

Banking existed in India before British Rule—Indigenous bankers, their business—Early joint-stock banking and its history—Presidency Banks—European hand in bank development—Indian activities in corporate banking—Bank failures—Apathy of Europeans and Government to Indian banking concerns—Exchange Banks—Co-operative Credit Societies—Post Office Savings Banks—*Shroffs* (native bankers).

Banking in its essential aspects, though not on any large, organised or systematic scale, has been in existence in India long before the advent of the British Rule, remains of which are still greatly visible. The indigenous banker even to-day plays an important part in the financing activities of the country's commerce. The *Multanis*, *Marwaris*, *Chettys*, *Mahajans*, *Nanavatys* and *Village Baniyas* are still the only means of banking assistance to a large portion of the Indian population. They have been accepting deposits and advancing loans like ordinary banks. In fact in the dealings of some, there is a greater personal touch which is often very useful and appreciated. The writer knows of many instances where people refuse to sever their banking connections with these private *shroffs*, in spite of cheaper facilities being available elsewhere; and the only explanation coming forth is that there exists a personal factor which materially smooths their mutual dealings. The institution of bills and hun-

dies has been prevalent in this country long before it was even possibly known in the West. The system of cheque payment although a modern development is nothing but an extension of the practice of "Darshni Hundis" (*i.e.*, Sight drafts), which has been in existence here for ages. Even the safeguard to cheques in the nature of "crossings" was not unknown as there has been a practice of writing on bills, words which imply that they could be only paid through some respectable trader or banker. Business which India used to have internally between various provinces and with the outside world would have been practically an impossibility if banking in some form had not been available. Banking in India would have greatly progressed had it not been for the fact that it was very often carried on jointly with trading. Any sudden variations in trade conditions or vicissitudes of commerce or the resulting losses, no matter whether big or small, always reacted on the banking business of the people affected or concerned, and of others through panics which such events induced. This led to banking failures and stoppage of banking progress.*

* "Whether the banking habit as practised in India in the remote past has for its origin Greece or Palestine need not be discussed, but it may be accepted that a system of banking eminently suited to India's then requirements was in force in that country many centuries before the science of banking became an accomplished fact in England. It is true that the methods of old in force in India were vastly different from the European ideas of banking to-day and partook more of money-lending, money changing, and later of the Hundi business; nevertheless, as applied to the conditions then existing in India, they admirably acted their part, and must be recognised as having rendered immense service to the country as a whole, particularly when we keep in view the enormous agricultural interests of India."—Extract from "From the remote past to an assured future" by Mr. W. F. Preston, Chief Manager of the Chartered Bank of India, Australia & China, and a member of the Hilton Currency Commission, in the semi-annual banking supplement to the "Financial News."

Modern banking with the principle of limited liability underlying its constitution is, however, a later growth. The first Joint-stock banking enterprise known as the Hindustan Bank was established in 1770. It was started by some Agency Houses of Calcutta and its business was more or less intimately connected with those houses. It closed its doors in 1832 when the firm of Alexander & Co. which was the principal party associated with it failed. Like all other similar institutions of the time, it issued notes which although were not recognised as legal tender, circulated freely, their circulation often amounting to Rs. 50 lacs a figure of some importance in those days. The Bengal Bank and General Bank of India came into existence somewhere about 1785. After somewhat interesting career the latter was dissolved by voluntary liquidation in 1791; and a little later the former suspended payment as a result of severe run, occasioned by the reverses with which the English met in their encounters against Tippoo Sultan.

In 1801 the Accountant-General Mr. Henry St. G. Tucker pressed on the attention of the Government of India the necessity of a bank both in the interests of the Government and of the mercantile community, which ultimately led to the establishment of Bank of Bengal in 1806, obtaining its charter little later in 1809. The Capital of this bank was £500,000, one-fifth of which, *viz.*, £100,000 was contributed to by the State, *i.e.*, East India Company. Participation of the Government in the capital of the bank as a shareholder was thought necessary in order to be able to share in the direction of the bank's affairs and to guide it safely. The Government had power to

appoint three directors on the board of its management. The Secretary of the bank was usually a member of the Civil Service.

In 1813 an Act to remove certain restrictions on Europeans settling in India was passed which gave a great stimulus to banking. Several banks were established but many of them did not live long. Although Europeans were solely responsible for these first attempts, failures in many cases were not only due to mismanagement or want of capacity for organised work but also to fraudulent use of banks' money.

The Bank of Bombay was first constituted in 1840 with a Capital of Rs. 52,25,000 of which Rs. 3 lacs were subscribed by the Government. The Bank of Madras was incorporated three years later in 1843 with a Capital of Rs. 30 lacs, of which the East India Company subscribed Rs. 3 lacs. As in the case of Bank of Bengal the Government had intimate connection with these banks, which likewise allowed the Government to nominate some of their Directors and their Secretary and Treasurer was a member of the Indian Civil Service. All these three banks obtained valuable concessions from the Government, chief amongst them being the monopoly of Government banking, and the right to issue notes--this as already mentioned in the preceding chapter was regarded the most important of the functions and privileges of a banking institution. There were, however, certain restrictions upon their powers to issue notes. In the first place limits were prescribed upon the total amount which each bank could issue, *e.g.* limit in the case of Bank of Bengal was Rs. 2 crores. Also the banks had to maintain

a cash reserve of $33\frac{1}{3}$ per cent. of their demand liabilities which included current deposits and outstanding notes. This percentage was later reduced to 25 per cent.

In 1862 the right to issue notes was withdrawn from these banks and the Paper Currency Act of 1862 was brought into operation. The Presidency Banks were, however, compensated for the loss of this privilege by the Government's agreeing to place all their funds at the Presidency towns with these banks.

The Capital of the Bank of Bombay was increased by 1864 to Rs. 2·09 crores. It was, however, unfortunate in its career and suffered severe losses in the wild and excited speculation which followed on the American War and the rise in the price of cotton. It was voluntarily wound up in 1868 and on its ruins rose the new Bank of Bombay, Ltd., which was constituted by Articles of Association under the Indian Companies Act of 1866. Although the depositors got their money back in full the shareholders lost almost the whole of their capital. After this failure the Government thought it advisable to withdraw its portion of capital and along with it relinquished its right to appoint Directors and Secretary and Treasurer.

A Commission was appointed by the Government of India to investigate into the causes of the bank's failure. In 1869 this Commission submitted its report which led to the passing of Presidency Banks Act of 1876. The Banks of Bengal, Madras, and Bombay were all brought under the control of this Act and subjected to the restrictions laid therein. These banks were entrusted with the

banking business of the Government and through this dignity and prestige attracted a good deal of other banking business of this country on very favourable terms. The restrictions imposed by the Act upon the business of the Presidency Banks although not welcome to the bank management were wholesome and in the interests of public and private funds which were deposited with them. In order to free the banks from possible losses which might result from exchange transactions they were not allowed to negotiate foreign bills or borrow outside India. Six months limit was imposed upon the period of their advances. They were not allowed to advance on immovable property which tends to lock up bank funds.

The Presidency Banks had opened branches in many important places in India. They were, however, lacking in points of contact, which was often greatly felt. There had been many occasions on which it was keenly felt that there should have been only one bank of this type for the whole of India. Attempts were made more than once to merge all these banks into one institution but due to selfishness and desire for individuality which the different banks had, those efforts proved futile. War demonstrated the increased necessity of one Central Bank which could adequately guide and control the Indian money market. The pressure of the Government, the force of public opinion and the necessity of union as the better method of increasing business due to altered circumstances, however, finally led to the fusion of the banks into the Imperial Bank of India in January 1921, under the Imperial Bank of India Act of 1920. We shall deal with this institution

fully in a later chapter. Detailed figures of banking business of the three Presidency Banks and of their amalgamated institution, the Imperial Bank, are given in Appendix I. It may be mentioned here that the Imperial Bank at the end of 1925 had about 160 Branches ; and its Capital, Reserve, and Deposits were Rs. 562 lakhs, Rs. 482 lakhs and Rs. 8,330 lakhs respectively.

Reverting to the history of Indian banking we find that the Allahabad Bank was established in 1865. About 10 years later was established the Alliance Bank of Simla, which went into liquidation in 1923. Both of these, however, owe their origin to European enterprise.

All the Indian Joint-stock banking activities before 1880 were started by Europeans. The foreign banking business was in the hands of Exchange Banks, two of which had opened their Offices in India by 1870. More about these banks will be said little later. The first purely Indian Banking enterprise on the principle of limited liability was started in 1881 when the Oudh Commercial Bank was founded. In 1894 the Punjab National Bank was established mainly through the efforts and energies of Lalla Har Kishen Lal who is the pioneer of Indian banking and industry in the province of the Punjab. This bank is doing very useful work and growing stronger day by day. In 1901 Lalla Har Kishen Lal started the People's Bank of India, Ltd., which continued to gain momentum till 1913, when it had developed into greater importance than Lalla Har Kishen Lal's previous similar attempt the Punjab National Bank, Ltd. Its deposits were over $1\frac{1}{4}$ crores of rupees and it

had nearly 100 branches. All of a sudden it was obliged to close its doors. The failure of the People's Bank was not due to any fraud or dishonesty or lack of ability to manage but mainly due to want of knowledge of banking principles on the part of average Indian bank customer, the jealousy and apathy of European banks and Government Officials and the hostile attitude of the then Presidency Banks which even refused to accommodate the bank on the security of Government Paper. Possibly the bank had also stepped beyond the safety line dictated by the then prevailing circumstances. The Liquidators of the bank were finally able to pay more than 100 per cent. dividend to its creditors, but the shareholders did not get anything.*

With the year 1905, the year of the partition of Bengal, began the *Swadeshi* † movement, to patronise local enterprises, which led to the establishment of Indian banks all over the country. In 1910 they totalled 476. The most important of them were the Bank of India and the Indian Specie Bank in 1906 ; the Bengal National Bank§ and

* About 2 years back Lala Harkishen Lal started another banking enterprise under the name "New People's Bank of Northern India." The paid up capital of the bank is about Rs. 20 lacs. It has secured deposits of nearly rupees one crore during this short period. The bank is expected to play an important part in the banking activities of the country.

† National.

§ It is unfortunate that the bank closed its doors on the 28th April 1927. The directors have not issued any official report so far and it is premature to discuss the failure. The immediate cause of the suspension is reported to be precipitated action on the part of the debenture holders, among which, it is understood, is the Imperial Bank. The subscribed capital of the bank is Rs. 15 lacs, half of which is paid up. Its deposits on 31st March 1926 were Rs. 81 lacs.

the Indian Bank of Madras in 1907; the Bombay Merchants Bank and the Credit Bank of India in 1909; the Kathiawar and Ahmedabad Banking Corporation in 1910, and the Central Bank of India in 1911. In the year 1913 came the banking crisis which swallowed many of these concerns and gave a great set back to the Indian banking. It is true that some of these failures were due to dishonest use of banks' funds, mixing of trading with banking, and want of knowledge as to how to do safe banking business, but there were other important contributory causes also. There was want of co-operation and co-ordination between the Indian banks themselves, the attitude of the English and Presidency Banks was unsympathetic and hostile and even the Government was indifferent spectator if not averse to their existence and prosperity. The governments of other countries on such occasions enact special emergency measures and even give monetary assistance to save their credit institutions from, in many cases, unwarranted failures but the State in India did nothing of this sort. This responsibility was first realised, to a small extent only very recently when the Alliance Bank of Simla failed, though this assistance did not save the Bank from failure, possibly, because the affairs of the Bank were past redemption. But the chief reason which induced them to lend this

The bank has been in difficulties for some time past. Its investments are reported to be locked up and liquid resources small. The last balance sheet, 31st March 1926, discloses a cash cover of only 5 per cent. to deposits. This as remarked by the "Statesman" is a mad margin with which to attempt to do business. Reports about resuscitation are being heard in some quarters and it would be very desirable if some scheme of reconstruction succeeds. The failure once more brings the question of organisation of Indian banking into prominence.

assistance was not any anxiety for saving an Indian bank but to help liquidation of an "English managed" institution and its depositors, many of whom were non-Indians. The Bank had great support of Government Officials and through them of the Government. What the Government's attitude in the future will be only time will prove.*

* As soon as the Alliance Bank of Simla closed its doors in April 1923, the Imperial Bank of India announced that it would pay to the creditors of the Alliance Bank up to 50 per cent. of their claims, pending completion of the liquidation work. The Imperial Bank undertook this risk because the Government of India agreed to indemnify the bank in case assets of the Alliance Bank did not equal on realisation to half its liabilities. Government's intervention in matters like this can be justified in the interests of public welfare and public policy, but because the Bank was a non-Indian concern and the benefit of the Government guarantee was mainly to go to non-Indians, the country as a whole protested against the Government's undertaking this liability. The callous apathy of the Government and English banks in the failures of 1913 was quite fresh in the public mind; and the country naturally concluded that the Government intervention and Imperial Bank assistance were simply induced because non-Indians were involved. People were suspicious that if there had been an Indian concern in place of the Alliance Bank no such facilities would have been introduced. India felt so keenly at this act of partiality or favouritism that its Central Legislature successfully carried a resolution recommending to the Governor-General in Council to express his disapproval of the action and policy of the Finance Department of the Government in undertaking a present or contingent liability to the Imperial Bank for losses consequent upon the failures of the Alliance Bank. This was nothing but a vote of censure.

It may also be mentioned here that the Imperial Bank had another motive also in undertaking this work of advance payment. On account of this facility to the creditors it became associated with the liquidation work and it utilised this connection in furthering its business. Practically whole of the clientele and business of the Alliance Bank was transferred to it. Many of the branches of the Alliance Bank, at places where the Imperial had no offices, were taken over by the Imperial Bank, which greatly assisted the bank in completing the work of opening new branches imposed upon it by its charter.

War and post-war boom gave another impetus to the company promotion in India and the Joint-stock Banking experienced similar stimulant. The Tata Industrial Bank was founded in 1918 under very happy circumstances and with very high hopes. It showed signs of very promising career. But on account of the mistake of combining long term credit business with ordinary banking transactions and financing both out of current and annual deposits, instead of having recourse to issue of bonds for the former, in a country like India, where modern banking habits have not been fully established, and also on account of the inexperience of the majority of European employees who controlled, in the main, affairs of the bank, which in due course alienated the sympathy of Indian staff, whose rights were ignored, and of the Indian banking public, the bank at a premature age of 6 years was taken into voluntary liquidation and merged into the Central Bank of India in 1923. The Industrial Bank of Western India, the Karnani Industrial Bank, the Calcutta Industrial, and host of other banks are product of the war boom. And like the sad plight of many of the "after-war" Indian Joint-stock Companies which experienced difficulties and failures within short time of their birth, some of the Indian banks met with the same fate.

At the end of 1924 there were only 29 principal joint-stock banks (*i.e.*, banks having capital and reserve of Rs. 5 lacs and over). Their total capital and reserve was Rs. 10.70 crores and total deposits Rs. 52.50 crores. On the same date there were 40 other banks having capital and reserve between Rs. 1 lac and less than Rs. 5 lacs. The total

capital and reserve of this second class was Rs. 1·06 crores and their total deposits Rs. 2·66 crores.

The detailed figures of progress of Joint-stock Banks are given in Appendix II.

The statement showing extent of bank failures during the period 1913-24 is given in Appendix III, from which it will appear that over 160 banks registered under the Indian Companies Act, with total subscribed and paid-up capital of approximately $15\frac{1}{2}$ and $6\frac{1}{2}$ crores of rupees respectively, failed during this period. Figures appalling indeed! Over $6\frac{1}{2}$ million pounds of Indian Banking paid-up capital were involved in failures during a short period of twelve years. And excepting a few cases of reconstruction in which failing banks' capital was somewhat saved, whole of this large sum was lost to the unfortunate shareholders. When we look to the fact that the paid-up capital of the existing Joint-stock Banks is only about Rs. $7\frac{1}{2}$ crores, the amount of capital involved in failures is really disastrous. Such losses would discourage even the most optimistic investors. Surely the present system needs thorough overhauling. To pursue the question further, more than 90 per cent. of these failures were in respect of banks having paid-up capital of less than Rs. 5 lacs; and more than 80 per cent. in case of banks whose paid-up capital was less than Rs. 1 lac. Thus failures were chiefly confined to small banks which, in the absence of any suitable emergency arrangements, found it difficult to weather any financial or monetary disturbance. The figures, however, show that the idea of Joint-stock Banking had caught hold of Indian mind but because the guiding, controlling, and co-ordinating forces were wanting the enterprises

had sometimes to meet with reverses and sad fate. If the Government had exploited this enthusiasm to the fullest advantage of Indian credit interests by introducing suitable legislation to guide, control and examine the affairs of Indian banks, the pages of history of modern banking in India would have consisted of much happier reading.

The term "Exchange Banks" has been referred to in an earlier part of this chapter. It comprises joint-stock banks incorporated under Acts of other countries, having their registered Head Offices out of India, but having branches here, doing their principal or partial business in this country. They are called Exchange banks because they principally deal in "Exchanges" or finance payments and financial arrangements in respect of foreign trade. The necessity for some such organisation was keenly felt after the first-half of the last century which induced concerns of this type. As the principal external trade of India was in the beginning with England or *viâ* England and London was fast coming into prominence as the world's centre of money market and clearing house, banks with the object to do exchange business of India were formed in London and registered under the English Companies Act. The lack of general banking facilities thrust upon them ordinary internal banking work and they began to assume very great important rôle in the country's banking system. With their ultimate strength in the support of London banks and of the London money market they progressed very rapidly so much so that to-day they form the most important and powerful group of banks in this country.

Several of the Exchange Banks were founded about 70 years ago. In 1870 there were only 3 Exchange Banks ; in 1880, 4 ; in 1890, 5 ; in 1900, 8 ; in 1910, 11 ; in 1920, 15 ; and in 1924, 18. In 1913 the year preceding that of the great war there were 12 Exchange Banks out of which more than half had their Head Offices in London and the rest were connected with Japan, France, Germany, Russia, and America respectively. The War disturbed the proportion of India's foreign trade with the various countries which induced other banks to establish their branches here. This principally accounts for 50 per cent. increase in the number of Exchange Banks during the period 1913-1924, *e.g.*, in 1918 and 1919 two Japanese, in 1920 Banco National Ultramarino and in 1920 two Netherlandish banks opened their offices in India. In the beginning, of course, the total business of Exchange Banks was very modest but with the passing of time it has gained great momentum. To-day they wield very great influence in the Indian banking activities and are more powerful than the Indian Joint-stock Banks. The Indian deposits of these 18 Exchange Banks at the end of 1924 exceeded Rs. 70½ crores. History and extent of their business figures will be found in Appendix IV.

Besides the above three principal kinds of banks which form the main components of the Indian Banking system there are Co-operative Credit Societies. The co-operative movement dates from 1904 when the first Co-operative Act was passed. In 1912 another Act to bring Co-operative Societies on better basis was passed. The Co-operative Credit Societies are founded with the idea of

facilitating credits for the Indian cultivators. The basic principles of the system are: (i) a number of cultivators residing in a locality join together on the principle of limited or unlimited liability for the obligations of each other, and form a Primary Co-operative Credit Society; (ii) the Primary Co-operative Credit Societies join together and form a District Co-operative Society; and (iii) the District Co-operative Societies combine to form a Central Co-operative Society. The various Credit Societies receive deposits and contract loans which they advance to their members, as and when necessary, in proportion to their worth and requirements. Although the system of Co-operative Credits was first introduced about a quarter of a century back and has made some progress it is still at the beginning of its career and requires vigorous efforts at reorganisation for its advancement. In the beginning the Government gave some stimulant to the system by giving loans but later this assistance began to be restricted and even withdrawn. At the end of the Provincial Co-operative year 1924-25, the number of principal Co-operative Banks having paid-up capital and reserve of Rs. 5 lacs and over was only 8. The number of banks with capital and reserve between 1 lakh and less than Rs. 5 lakhs on the same day was only 90. The total deposits and loans received by the two classes of banks were Rs. 4½ and Rs. 8 crores respectively. If we take into account all the co-operative societies, big or small, banking or non-banking the figures at the end of 1921 were: total number of societies 43,366; total number of individual members 17,56,925; share capital and reserve Rs. 5.53 crores; deposits by members Rs. 1.51

crores, by State Rs. 35 lacs ; loans from private persons, other societies and banks Rs. 17·02 crores ; loans issued to members and other societies Rs. 10·94 crores. When we look to the facts that 224 millions of persons, representing 71 per cent. of Indian population are supported by agriculture, that the rural indebtedness to the money-lenders is about 600 crores of rupees and that the means of the co-operative societies are expected to be utilised both for relief of existing indebtedness as well as for the supply of credit to agricultural production, the above figures show how miserably backward is our Co-operative movement. The Indian cultivator will continue to be in the oppressive hands of the village *Mahajan* unless some immediate solution of the problem is found. India is principally an agricultural country and prosperity of her masses mainly rests upon a sound system of Agricultural and Co-operative Credit Societies.

The detailed figures pertaining to Co-operative Credit Societies will be found in Appendix V.

Survey of present banking activities in India will be incomplete without account of Savings Banks. There are no Savings Banks as such in India. The Imperial Bank of India and most of the Joint-stock Banks have opened Savings Bank departments. Originally there were Government Savings Banks in the Presidency towns. In 1870 District Savings Banks were started in connection with selected treasuries. In 1882 the Post Office Savings Banks were opened which gradually absorbed the business of the previous types of Savings Banks. Now this savings work is principally done by Government Post Offices which have a large organisation for such

purpose. Every Post Office of even ordinary importance has a savings bank counter. This has greatly stimulated small savings specially of ordinary salaried persons. At the end of 1922-23 the total of savings deposits with the Post Office, was over Rs. 23 crores, the annual deposits and withdrawals during that year being Rs. 20·78 crores, and Rs. 19·84 crores, respectively. The number of Post Offices doing savings bank work in that year was 10,730, the number of depositors was over 20 lacs, and average deposit per head was Rs. 113. The total deposits rose to over Rs. 25 crores in 1925.

During the year 1914-15, immediately after the outbreak of War, the Post Office lost much of its savings bank deposits and the movement received not a small set back. The figure dropped from over Rs. 23 crores to just Rs. 15 crores in one year. This was due to the panic among the masses caused by the fear of a possibly adverse result of the Great War which might make the Government bankrupt and involve the savings bank depositors in loss. The fear was unfounded and the movement again took an upward direction.

The figure of Rs. 25 crores of Post Office savings deposits at the end of 1925 when compared with the similar figure of Rs. 23 crores at the end of 1914 may not show sufficient improvement in mass savings at first sight. But during the last few years the Post Office Cash Certificates have been introduced which have attracted over Rs. 20 crores. Thus we can safely say that the savings bank machinery of the Government through the medium of Post Offices is tolerably satisfactory so far as the incul-

cation of habit of thrift in the masses goes. The money thus accumulated however goes to assist the Government finances instead of meeting the commercial needs of the country which are both large and pressing. Efforts should be made to make at least a portion available for the country's direct economic needs through private channels like joint-stock banks, co-operative societies, etc. There is still great room for improvement, *e.g.*, there is no necessity of prescribing any limits as to the total amounts that could be held by a depositor and the amount that could be annually deposited. There can, of course, be reasonable restrictions as to the withdrawals so that the local post office may have reasonable time to obtain funds from the nearest treasury. Again the red tape procedure involving vexatious and undue returns or delay should be minimised. There is still great scope in the savings bank work. At the end of 1923 there were 10,730 Post Office Savings Banks as compared to nearly 5 lacs villages in India on that date which gives one Post Office Savings Bank to 50 villages. In many cases nearest Post Office Savings Banks are situated at a distance 10 to 12 miles from villages, which means villagers must walk over 20 miles before they can deposit or withdraw their savings. This is not a happy prospect calculated to stimulate such savings. People would prefer to keep their small amounts with themselves rather than subject themselves to this ordeal. Means could be devised to facilitate such savings, *e.g.*, by making such transactions feasible through the village postmen, etc. This subject of Savings Banks will be fully discussed later.

It has been said at the beginning of this chapter that *Shroffs* (native bankers) play a very important part in the country's banking system. They advance money on pronotes, hundies and mortgages. They first utilise their own capital and deposits which they get from their clients and when the demand on their funds increases they rediscount the hundies in their port-folio with the major commercial banks and the Imperial Bank of India which extend to them very liberal credit lines for such purposes. A good deal of the "movement of funds" business used to be in their hands. They are very punctual in meeting their banking obligations. As no statistics are available it is not possible to give any accurate figures as to the extent of their business. The writer made sometime back personal enquiries about the assistance which an important section of these private bankers (*Multanis*) give to the merchants and his estimate was that it is somewhere about five crores of rupees. The *Chetys* of Madras are similarly said to be advancing several crores to the agriculturists in Burma, Singapore, etc. Banks are sometimes feeling the competition of this class of bankers which can be easily seen from the fact that the bazar discount rate for hundies is sometimes lower than the Imperial Bank's Hundi rate. According to the Controller of Currency's Report for the year 1924-1925, the bazar Hundi rate in Calcutta was $\frac{1}{2}$ to 2 per cent. lower than the Imperial Bank Hundi Rate during the whole year. The above facts clearly demonstrate the importance of this class of bankers. It would not be much wrong to hazard a guess that the banking business of Indian *Shroffs* and money-lenders is

more than 100 crores of rupees*. The business morality of the indigenous banker has been of a high order. Mr. W. E. Preston, Chief Manager of the Chartered Bank of India, Australia and China, and a member of the last Royal Commission on Indian Currency and Finance, when writing in the last semi-annual banking supplement to the "Financial News" described the activities of the old-fashioned Indian bankers in these words: "While the Commercial man of India of to-day likes to talk lovingly of the old-fashioned Indian bankers—*Shroffs, Mahajans and Chetties*—who still carry on successfully their old vocations, he at the same time is very apt unjustly to criticise what he terms their usurious methods and inhuman habits of bleeding the poor *ryots*, but when the risks are considered which the banker of old took, he may not be held to be quite as bad as he has been pointed. To their lasting credit, however, it must be admitted that they found a clan—the banker caste—whose traditions have for over a period of centuries descended from father to son, a caste one of the most honoured in the land of India, and whose morality, with very few exceptions, was almost beyond reproach, and whose daily transactions, although there was never a written law to regulate or to give protection, rarely showed default."

* It does not include long term advances made by money-lenders against mortgages, etc. The figure represents only short term advances to trade and commerce. The total of both may be about Rs. 700 crores or even more.

CHAPTER III

MAJOR BANKS

IMPERIAL BANK: Amalgamation of Presidency Banks and Imperial Bank Act—Capital—Management—Business permissible—Restrictions on business—Examination of business figures—Comparison with Central Banks—Tests applied to its working—Complaints against it—Hybrid constitution—Future status and scope ; **INDIAN JOINT-STOCK BANKS :** Registered under Indian Companies Act—Only six banks with deposits over Rs. 1 crore, their names—Central Bank of India and Pochkhanawala—Competition of Imperial and Joint-stock Banks—Business—Business figures ; **EXCHANGE BANKS :** Name Foreign Banks more appropriate—Their names—Business—Finance of foreign trade illustrated—Arrangements and facilities in foreign countries—Help foreign merchants and manufactures—How Indian interests suffer at their hands—Predominance in Indian banking.

THE IMPERIAL BANK OF INDIA

As has been said in the preceding chapter the Imperial Bank was founded in 1921 under the Imperial Bank Act of 1920, as the result of the amalgamation of the three Presidency Banks : The Bank of Bengal, The Bank of Bombay, and The Bank of Madras. The Capital of the bank is Rs. 11·25 crores divided into shares of Rs. 500 each. The liability of the shareholders is limited to the amount not fully paid on their shares. The paid-up Capital and Reserve of the bank on 31st December 1925 were Rs. 5·62 crores and Rs. 4·82 crores respectively. The

bank has been paying 16 per cent. dividend * since its commencement. Its shares are consequently at a very great premium. The fully paid-up shares of Rs. 500 each and the contributory shares on which Rs. 125 is paid-up are quoted at Rs. 1,630, and Rs. 418 respectively.† This is, of course, natural because the price of shares rises directly in proportion to the dividend paid thereon and inversely according to the market rate of interest which of late remains within modest limits.

The bank has local head offices at Calcutta, Bombay and Madras. It has also a branch in London but it is not allowed to do any exchange business. This was, of course, conceded to satisfy the vested interests of the foreign banks.

The general superintendence of the affairs and business of the bank is entrusted to a Central Board of Governors. The actual administrative and executive work is carried on by two Managing Governors who are appointed by the Governor-General in Council after consideration of the recommendation of the Central Board. The Managing Governors hold office for such period as the Governor-General in Council may direct.

The business of the territories administered by the three centres, Calcutta, Bombay and Madras is carried by the respective local Boards which are elected by the bank's shareholders. They are of

* The dividends of the three Presidency Banks paid for the year 1920 were 19½, 22 and 18 per cent. respectively for the Bank of Bengal, Bank of Bombay and Bank of Madras.

† These quotations ruled in the Calcutta market on the 21st July 1926. Since the publication of the Hilton Currency Commission's report which recommended establishment of a new Central Bank, the shares have fallen in value. Rates on 3rd September, 1926, were Rs. 1,480 (Rs. 375) respectively.

course to work under the Central Board so far general policy and directions are concerned. The Secretary and Treasurer at each centre is responsible for the executive and administrative work relating to his circle.

The Central Board is at present composed of not more than 16 members, called Governors, as under :—

- (i) 6 : Presidents and Vice-Presidents of the three Local Boards. These are naturally representatives of the shareholders.
- (ii) 1 : The Controller of Currency or such other person as may be nominated by the Governor-General in Council.
- (iii) 4 : Nominees of the Governor-General in Council who will hold office for one year but may be re-nominated. Such nominations will be made from persons who are not officers of the Government.
- (iv) 3 : Secretaries of the Local Boards.
- (v) 2 : Managing Governors.

NOTE :—Governors mentioned at (ii) and (iv) are not entitled to vote.

The Imperial Bank enjoys the monopoly of Government banking business and deposits of Government funds. Besides the above powers of appointing Governors, the Governor-General in Council has power to issue instructions to the bank in respect of any matter which in his opinion vitally affects his financial policy or the safety of Government balances and in the event of the bank's disregarding such instructions he has right to forthwith terminate the agreement regarding Government banking busi-

ness. The Governor-General in Council has also powers to prescribe any special audits or examination of the bank's affairs whenever he may deem the same necessary.

The business which the bank can transact is prescribed in two ways : (i) Business which it can do and (ii) Business which it cannot do. This is mentioned in detail in parts I and II of Schedule I to the Imperial Bank Act, which is reproduced below.

SCHEDULE I

(See Section 8)

PART I

Business which the Bank is authorised to carry on and transact.

The Bank is authorised to carry on and transact the several kinds of business hereinafter specified, namely :—

- (a) the advancing and lending money, and opening cash-credits upon the security of—
 - (i) stocks, funds and securities (other than immovable property) in which a trustee is authorised to invest trust money by any Act of Parliament or by any Act of the Governor-General in Council and any securities of a Local Government or the Government of Ceylon :
 - (ii) such securities issued by State-aided railways as have been notified by the Governor-General in Council under section 36 of the Presidency Banks

Act, 1876, or may be notified by him under this Act in that behalf ;

- (iii) debentures or other securities for money issued under the authority of any Act of a legislature established in British India by, or on behalf of, a district board ;
- (iv) goods which, or the documents of title to which, are deposited with, or assigned to, the Bank as security for such advances, loans or credits ;
- (v) accepted bills of exchange and promissory notes endorsed by the payees and joint and several promissory notes of two or more persons or firms unconnected with each other in general partnership ; and
- (vi) fully paid shares and debentures of companies with limited liability, or immovable property or documents of title relating thereto as collateral security only where the original security is one of those specified in sub-clauses (i) to (iv), and if so authorized by any general or special directions of the Central Board, where the original security is of the kind specified in sub-clause (v) :

Provided that such advances and loans may be made, if the Central Board thinks fit, to the Secretary of State for India in Council, without any specific security ;

- (b) the selling and realisation of the proceeds of sale of any such promissory notes, debentures, stock-receipts, bonds, annuities, stock, shares, securities or goods which, or the documents of title to which, have been deposited with, or assigned to, the Bank as security for such advances, loans or credits or which are held by the Bank or over which the Bank is entitled to any lien or charge in respect of any such loan or advance or credit or any debt or claim of the Bank, and which have not been redeemed in due time in accordance with the terms and conditions (if any) of such deposit or assignment ;
- (c) the advancing and lending money to Courts of Wards upon the security of estates in their charge or under their superintendence and the realisation of such advances or loans and any interest due thereon, provided that no such advance or loan shall be made without the previous sanction of the Local Government concerned, and that the period for which any such advance or loan is made shall not exceed six months ;
- (d) the drawing, accepting, discounting, buying and selling of bills of exchange and other negotiable securities payable in India, or in Ceylon ; and, subject to the general or special directions of the Governor-General in Council, the discounting, buying and selling of bills of exchange, payable outside India, for and

from or to such Banks as the Governor-General in Council may approve in that behalf ;

- (e) the investing of the funds of the Bank upon any of the securities specified in sub-clauses (i) to (iii) of clause (a) and converting the same into money when required, and altering, converting and transposing such investments for or into others of the investments above specified ;
- (f) the making, issuing and circulating of bank-post-bills and letters of credit made payable in India, or in Ceylon, to order or otherwise than to the bearer on demand ;
- (g) the buying and selling of gold and silver whether coined or uncoined ;
- (h) the receiving of deposits and keeping cash accounts on such terms as may be agreed on ;
- (i) the acceptance of the charge of plate, jewels, title-deeds or other valuable goods on such terms as may be agreed on ;
- (j) the selling and realising of all property, whether movable or immovable, which may in any way come into the possession of the Bank in satisfaction or part satisfaction of any of its claims ;
- (k) the transacting of pecuniary agency business on commission ;
- (l) the acting as administrator, executor or trustee for the purpose of winding up estates and the acting as agent on commission in the transaction of the following kinds of business, namely :—

- (i) the buying, selling, transferring and taking charge of any securities or any shares in any public Company ;
- (ii) the receiving of the proceeds whether principal, interest or dividends, of any securities or shares ;
- (iii) the remittance of such proceeds at the risk of the principal by public or private bills of exchange, payable either in India or elsewhere ;
- (m) the drawing of bills of exchange and the granting of letters of credit payable out of India, for the use of principals for the purpose of the remittances mentioned in clause (l) and also for private constituents for *bonâ fide* personal needs ;
- (n) the buying, for the purpose of meeting such bills or letters of credit, of bills of exchange payable out of India, at any usance not exceeding six months ;
- (o) the borrowing of money in India for the purposes of the Bank's business, and the giving of security for money so borrowed by pledging assets or otherwise ;
- (p) the borrowing of money in England for the purposes of Bank's business upon the security of assets of the Bank, but not otherwise ; and
- (q) generally, the doing of all such matters and things as may be incidental or subsidiary to the transacting of the various kinds of business hereinafore specified.

PART II

Business which the Bank is not authorised to carry out or transact.

The Bank shall not transact any kind of banking business other than those specified in Part I and in particular :—

- (1) It shall not make any loan or advance—
 - (a) for a longer period than six months,
or
 - (b) upon the security of stock or shares of the Bank, or
 - (c) save in the case of the estates specified in clause (c) of Part I, upon mortgage or in any other manner upon the security of any immovable property, or the documents of title relating thereto.
- (2) The Bank shall not (except upon a security of the kind specified in sub-clauses (i) to (iv) of clause (a) of Part I, discount bills for any individual or partnership-firm for an amount exceeding in the whole at any one time such sum as may be prescribed, or lend or advance in any way to any individual or partnership-firm an amount exceeding in the whole at any one time such sum as may be so prescribed.
- (3) The Bank shall not discount or buy, or advance and lend, or open cash credits on the security of any negotiable instrument of any individual or partnership-firm, payable in the town or

at the place where it is presented for discount, which does not carry on it the several responsibilities of at least two persons or firms unconnected with each other in general partnership.

- (4) The Bank shall not discount or buy, or advance and lend or open cash-credits on the security of any negotiable security having at the date of the proposed transaction a longer period to run than six months or, if drawn after sight, drawn for a longer period than six months :

Provided that nothing in this part shall be deemed to prevent the Bank from allowing any person who keeps an account with the Bank to overdraw such account, without security, to such extent as may be prescribed.

The bank was required by the Imperial Bank Act to open within five years from the date of the commencement of the Act 100 new branches out of which one-fourth were to be at places directed by the Governor-General in Council. The failure of the Alliance Bank of Simla in 1923 facilitated this task, as its branches were practically taken over by the Imperial Bank. This work was completed year before last, *i.e.*, within the scheduled time.

From the detailed banking figures of the three Presidency Banks and the Imperial Bank of India given in Appendix I, it will appear that on the establishment of the Imperial Bank, the total Capital of the three Presidency Banks was

increased by Rs. 1·87 crores and the reserve by Rs. 37 lacs. The present Reserve figure shows an increase of Rs. 1·05 crores over the total Reserve of the Presidency Banks at the end of 1920. The total of deposits of the Presidency Banks at the end of 1920 was Rs. 87 crores. It is surprising that this figure fell to 72½ crores at the end of the 1st year of the Imperial's career. The drop of Rs. 14½ crores in one year, is distributable between the Public, *i.e.*, Government deposits and Private deposits as Rs. 2 and 12½ crores respectively. The figure further dropped to Rs. 71 crores at the end of 1922. It improved to Rs. 82·7 crores at the end of 1923, to Rs. 84 at the end of 1924 but dropped again to Rs. 83·3 crores at the end of 1925. The difference between private deposit figures at the end of 1920 and 1922, *viz.*, Rs. 21 crores is rather surprising. It is true that India was passing through the aftermath of boom and there was deflation of currency and credit but such heavy fall cannot be attributed to this cause only. The subsequent increase in 1923 was due to bank failures which temporarily gave a set back to the confidence in other banks. Also the whole of the business of the Alliance Bank practically went over to the Imperial because of the special circumstances narrated in the last chapter. The figure at the end of 1924 still shows a fall of Rs. 3 crores as compared to the total of deposits of the three Presidency Banks at the end of 1920. This is hardly encouraging, when we look to the facts that the system of separate treasuries has been abolished, that the bank has opened 100 more branches and that it has gained additional deposits and confidence due to the bank

failures in 1923. It has been often said that the Imperial Bank's new branches have been able to attract Rupees six to seven crores of new deposits ; and a conclusion is drawn from such increase that the bank is demonstrating its usefulness in increasing banking habits. Much of this new money was already in other banks, *e.g.*, Alliance Bank of Simla, and it is wrong to conclude from mere figures that the fresh deposits were not with banks before they came to the Imperial Bank or that the bank has opened up new avenues. Moreover this increase in new deposits, when taken along with the fact that the total deposits are even less than what the Presidency Banks had at the end of 1920 shows that there must be a fall in the bank's deposits at other branches. This fall from the comparison of figures comes to Rs. 10 crores. The only conclusion possible is that the commercial public is finding services of other banks more suitable.

The Bank is bound under its constitution to issue a weekly statement of its affairs. We are reproducing in Appendix VI a copy of one of such statements and its latest available annual balance sheet which will give some idea about the bank's usual business.

The Bank cannot borrow without security or accept deposits outside India. In fact it cannot do any business beyond India, Burmah and Ceylon. The London Branch which it has been permitted to establish can do business only of special kind and is more or less agent for Government and similar business. As already remarked these restrictions were imposed to quiet the foreign banks which have assumed such a predominant influence in Indian banking.

It may be true that as Central Bank it should devote its main attention to the banking activities in this country but there is no reason to limit its activities by statute, especially when it has not fully taken over the roll of the Central Bank and is practically nothing more than a commercial bank at the present moment. Even if it were a full fledged Central Bank it is no use imposing such a restriction because at times it may happen to be in the interests of the Indian money market to borrow or receive deposits abroad, and thus ease the situation—the risk in exchange being suitably covered. The graphical chart of the Indian Bank Rate given at the end of the book shows how at certain times of the year the rate of interest against first class securities has been going as high as 9 per cent. which means that the rate for advances to commerce and trade would be somewhere above 10 or 11 per cent. This reveals a very sad situation specially when we remember that India is as a rule a creditor country in the international market. True, seasonal increased activities make money periodically tight, which the provision of increased currency against trade bills tends to mitigate to some extent, but why should the Imperial be debarred from rendering any further assistance which it can procure in the outside market to improve the monetary conditions in India is beyond comprehension.

The Imperial Bank of India is doing some useful work in financing the commercial activities and in developing banking habits. It is a good model of a conservative commercial bank. Judg-

ing from the dividend which the shareholders have been receiving, it can be said that the bank's working is satisfactory. But these tests are not sufficient in the case of a public corporation enjoying monopoly of the State funds without interest. The primary purpose of such a concern should be not to earn dividends for the capital holders but to see that the money market is properly regulated and that the national considerations are not ignored. Its working should aim at developing national economic activities. With the free funds of the Government averaging about Rs. 20 crores reasonable profits to the shareholders are practically assured. In the absence of a full-fledged Central Bank in India, the responsibilities of such an institution should, as far as practicable, be taken by the Imperial Bank; because, on account of the State assistance and status and privileges resulting from being Government bankers, it is the only bank which approximates to the Central Banking institutions of other countries. One of the aims and objects of amalgamating the three Presidency Banks into one bank was to supply the long-felt want of one strong Central Bank which should work in the public interests and be a support to the Indian money market and Indian banks.

Judging the work of the Imperial Bank from the above standpoints, we are sorry to record, that it does not come up to the expected level. Nor, did many of the public men and economists of the country anticipate any material good from the merger of the Presidency Banks into the Imperial Bank. The old management, the old policies and traditions connected with the Presidency

Banks were simply perpetuated. We have seen how the management of the Presidency Banks was even callous about the cries of Indian banks to get credit against the security of government bonds. The Indian merchants and firms fared no better. It is the general impression, that the foreigners and foreign firms were always favoured in the grant of credit and the greater portion of the banks' total advances was made to non-Indians. It was freely talked that the banks were not even as strict for security in the case of non-Indians as in the case of the people of this country. The management was wholly non-Indian. They had no sympathy for Indian economic regeneration or for the development of Indian credit institutions. The foreigners lack that national ambition, that national outlook, that national patriotism, which is the first requirement of any sound progress. Their connections with the country are practically mercenary and temporary during the periods of office. We do not blame them for their biassed tendencies. As long as man is human he cannot successfully resist the influence of those with whom he is connected by the ties of common habitation or native country, social habits and social intercourse. But the continuance of such a state of affairs was decidedly not in the interests of India.

The complaints against the Imperial Bank of India are on the same lines. The management is mainly non-Indian. The rumour is that the bank is less strict in the matter of advances to non-Indians. Large credit lines are reported to be extended to them which are denied to the people of the country on equivalent security. Even some of

the well-known and reputed Indian banks are not receiving the same facilities as are extended to some of the foreign trading houses or foreign banks. It is even reported, with what truth, we are unable to say in the absence of figures, that on an average the total of the bank's advances to non-Indians exceeds that to the Indians. Some might say that the factor of character preponderates in the case of those non-Indians who are considered to be shown special facilities. True, character is a factor which is to be counted in the determination of risk in advances, but there are many Indians whose standard of character is next to none. The truth is that the English managers do not (or rather cannot, because of different modes of living and different social habits) freely mix with the people of the country and they cannot get first hand information about the credit and character of their possible clients. Their ignorance, however, should not be the ground for absolving them from their responsibilities to this country. Right and true knowledge in such matters is of vital and first rate importance to bank managers.

If the bank has suffered some sad losses from Indian clients its system of management and superintendence is to blame which does not contain a requisite element of proper Indians who would control the affairs in the light of private and personal information which they alone are capable of getting correctly. It may be said that the bank has commenced recruiting Indians for responsible appointments. This is good so far as it goes. But the pity is, it does not go far enough. There are reports that they are not treated as they should

be and that often they are discouraged. The facilities, that are extended to them, are not adequate. Moreover they occupy subordinate posts. Their colleagues who are recruited directly from England enjoy greater privileges and prospects. From our own personal experience of both the materials in India and in England, from which the Imperial Bank officers are recruited, we are emphatically of opinion that the Indian material is much better and more suited to the conditions in India. We understand that the only special qualification which puts the English recruits on a much better footing is two or three years working experience in a bank in England. Those who have knowledge of the vast organisation of English Joint-stock banks can easily see that a new clerk joining any bank in England would probably stick in one department for the first few years of his career ; and to conclude that such service gives him appreciable banking knowledge or entitles him to special terms and special opportunities at the Imperial Bank shows nothing but deliberate ignorance of the true facts. Such recruitment on special terms is not warranted by any grounds of efficiency ; on the other hand it is positively dangerous because raw inexperienced people are given positions of responsibilities. It creates great discontent among the Indian staff who are better educated and more fully equipped. There would be no objection if the bank were to import from abroad really competent and experienced persons to strengthen the management but the recruitment from the clerical staff of English banks on the ground of a few years service in

such institutions is the perpetuation of a system which is highly prejudicial to Indian banking and economic interests. The only explanation for the prolongation of this state of things is the great voice and influence, not unoften strengthened by misrepresentation of the relative efficiency and merits of Indian and English members, which the present non-Indian officers have in the affairs of the bank. They simply wish to continue the monopoly of their vested interests as long as it is possible. In our opinion the sooner the recruitment in England is stopped the better it would be. India possesses much more suitable and efficient material to supply future officers of the Imperial Bank. If it may appear necessary at any time, bankers of repute and great experience may be engaged on contract service to impart tone to the bank's general management. Even if we have to pay them large salaries that would be worth while and to the real advantage of the banking in this country.

From the description we are giving of the working of Central Banking institutions in the subsequent chapters it would appear on comparison that there is much to be done before the Imperial Bank can suitably approximate to that ideal. The present constitution is a hybrid mixture, permitting the bank to do commercial banking up to a certain extent as well as imposing certain restrictions which are only usual in the case of Central Banks. The privileges which it enjoys put it in a position of great advantage as compared to the other commercial banks of the country. The existing Joint-stock Banks no matter howsoever strong, are keenly feeling the competition of the

bank. Nor, has the bank been particular or judicious in selecting the new branches. Many of them had already sufficient banking facilities and the Imperial's going there has simply created unhealthy competition. It is quite simple to see that the supply of free large government funds puts the bank in a position of great advantage in comparison to the other banks with which it has to compete for investments. It would be more in conformity with the right principles of banking if it assumed the rôle either of a true central bank or became a true commercial bank without any restrictions which the present constitution imposes. It does no good to the banking system or to the banking development of the country to continue its present position—on the contrary its privileged existence in the commercial banking impedes the growth of other banks. The determination of the Imperial Bank's future status and scope of activities is connected with the problems with which the book is dealing and we shall revert to this subject in the following chapters.

INDIAN JOINT-STOCK BANKS

Under this heading are included all the banks registered under the Indian Companies Act. The Act hardly contains anything special relating to banks in particular. The law governs all Joint-stock companies practically on identical lines. As will be shown in the following chapter the business of this class of credit institutions is not as it should be. At the end of 1924 there were only six banks which had deposits more than Rs. 1 crore each, *viz.*: The Allahabad Bank 9.25 crores, Bank

of Baroda 4·82 crores, Bank of India 9·50 crores, Bank of Mysore 1·39 crores, Central Bank of India 13·86 crores, and Punjab National Bank 6·26 crores. Out of these six banks of some importance four are managed by Europeans and as such cannot be regarded as indigenous in all respects. The only Indian banks of any consequence are the Central Bank of India, and the Punjab National Bank which between themselves own deposits of nearly 20 crores. Their progress has been very steady and creditable. Although the Central Bank has been faced with situations generally considered serious, created by mischief mongers who had personal malice or jealousy against the bank or its directors, it has always triumphed over them and thus demonstrated completely the fitness of Indians to manage their banking institutions. The Central's business principles seem to be exceptionally sound because some of the heavy rushes which it had to meet at times, and which would have meant real difficulties even for bigger commercial banks, did not ruffle the bank in the least; and the sudden demands of the depositors were met from the bank's ordinary cash balances and ordinary arrangements, just like the usual genuine withdrawals. It is really a matter of very great pride that the Central Bank to-day tops the list of all Joint-stock Banks in every respect, whether we look to Capital, Reserve, Deposits, or any other item of banking business. The outstanding success of the Central Bank is not a little due to its capable Managing Director, Mr. S. N. Pochkhanawala, who has without doubt proved that Indians if given proper opportunities are a match for any

foreign banking talent. It is true that the managing director of the Central Bank of India is a man of rare abilities and people like him are never many in any country ; but his example is sufficient to demonstrate that administrative efficiency in any activity is not a monopoly of any particular community or nation. There are many employees in Indian banks, who if given right chances and opportunities would not be inferior to any average foreign bank manager in India.

Figures in Appendix II show the progress which this class of banks have been able to make since 1870. Their business has trebled during the last ten years. The Indian community is beginning to appreciate their services and transferring gradually its patronage to them. Their progress has been, however, checked from time to time by bank failures and malicious rumours circulated by interested parties. The bank failures of 1923 are the recent and most important. They gave a great set back. The deposits at the end of 1922 were Rs. 65 crores. At the end of 1923 the figure dropped to Rs. 48 crores--a decrease of Rs. 17 crores or nearly 25 per cent. But during the following year, *i.e.*, 1924, the banks recovered Rs. 7 crores of deposits and the figure reached Rs. 55 crores. It is very encouraging to note that they are able to keep up the public confidence in spite of the great crisis of 1923. It is greatly creditable that they have been able to build up this position in spite of the competition of the older and influential Exchange Banks and the Presidency Banks. The competition specially of the latter and the present Imperial Bank has been wholly unequal and definitely weighted against them. The Exchange Banks have very long

starts and enjoy facilities in foreign markets which are factors of great value in the development of their business in India. The present position of the business figures of the Joint-stock Banks definitely proves that they are needed by the country. All that is required to stimulate their growth and accelerate the pace of their development is some amount of fostering care and confidence-inducing measures.

The business which the Joint-stock Banks do is ordinary banking business of receiving deposits, advancing monies, negotiating and collecting bills, etc. They generally receive all kinds of deposits—current, savings and fixed. The rates of interest of different banks vary according to their requirements and status. In the matter of advances they discount local and inland bills, open cash credit accounts and make loans. As regards the security which they insist upon, it greatly varies. In bigger towns where stock exchange securities are available and current, appreciable portion of their advances is made against their hypothecation. In the interior, specially in the agricultural tracts hypothecation of agricultural products in the bank's godowns, *e.g.*, grain, cotton, etc., forms a suitable collateral—the system of public ware-houses is not prevalent in India as in the West and the banks are required to maintain their own godowns or take possession of the customers' godowns when advancing money against goods. Goods and commodities like piece-goods, sundries, etc., are also readily made advances against. The banks supply short term and/or periodical credit to mills and factories, generally against the security of stock-in-trade or some other suitable security. They also advance against mortgages of properties, but this forms a small portion of their individual

total advances. They have learnt well by this time that for successful commercial banking their investments should as far as possible be liquid and easily realisable. They, however, do not rediscount their bills; nor do they do the business of bank acceptances. They as a rule do not do foreign exchange business. Some of the banks have commenced this kind of business but on account of the special advantages enjoyed by the foreign banks in this connection, their progress is small.

The Joint-stock Banks do the agency and safe custody work. They transfer money on behalf of their clients from one place to another. They buy and sell shares and other stock exchange securities for the public and thus popularise the investment habit. But their work and organisation in these matters is not as large or systematic as one finds in banks in Europe. The Central Bank of India, however, as in other banking activities, is progressing rapidly and on right lines in these directions also. It has lately opened a modern safe-deposit vault, erected by the well-known firm of Fichet's of France, in Bombay, which at least equals, if it does not excel, any best built vault found in the advanced countries of Europe and America. Main doors of the vault weigh thirteen tons each. The Indian banks have not as yet begun the "Trust" business. In course of time through the force of circumstance they will be called upon to meet demands of their clients in this direction also.

We have given the names of the six important joint-stock banks in the beginning of this section which had deposits over Rupees one crore each at the end of 1924. Their business figures during the five years 1920-1924 (both inclusive) are given in the following table for general information.

FIGURES ARE GIVEN IN

| Name of Bank. | Year. | CAPITAL AND RESERVE. | | |
|-----------------------------------|-------|----------------------|-------------------|---------|
| | | Paid-up Capital. | Reserve and Rest. | Total. |
| Allahabad Bank, Calcutta. | 1920 | 35,50 | 35,99 | 71,49 |
| | 1921 | 35,50 | 41,50 | 77,00 |
| | 1922 | 35,50 | 41,50 | 77,00 |
| | 1924 | 35,50 | 49,55 | 85,05 |
| Bank of Baroda, Baroda. | 1920 | 24,12 | 15,00 | 39,12 |
| | 1921 | 29,90 | 17,00 | 46,90 |
| | 1922 | 29,99 | 18,00 | 47,99 |
| | 1923 | 30,00 | 20,65 | 50,65 |
| | 1924 | 30,00 | 24,65 | 54,65 |
| Bank of India, Bombay. | 1920 | 1,00,00 | 66,00 | 1,66,00 |
| | 1921 | 1,00,00 | 73,48 | 1,73,48 |
| | 1922 | 1,00,00 | 81,50 | 1,81,50 |
| | 1923 | 1,00,00 | 77,00 | 1,77,00 |
| | 1924 | 1,00,00 | 83,67 | 1,83,67 |
| Bank of Mysore, Bangalore. | 1920 | 19,32 | 6,40 | 25,72 |
| | 1921 | 20,00 | 8,25 | 28,25 |
| | 1922 | 20,00 | 11,00 | 31,00 |
| | 1923 | 20,00 | 13,58 | 33,58 |
| | 1924 | 20,00 | 13,18 | 33,18 |
| Central Bank of India, Bombay. | 1920 | 50,00 | 20,00 | 70,00 |
| | 1921 | 50,00 | 25,00 | 75,00 |
| | 1922 | 50,00 | 30,00 | 80,00 |
| | 1923 | 1,68,13 | 1,00,00 | 2,68,13 |
| | 1924 | 1,68,13 | 1,13,60 | 2,81,73 |
| Punjab National Bank, Lahore. | 1920 | 18,33 | 15,71 | 34,04 |
| | 1921 | 20,46 | 17,20 | 37,66 |
| | 1922 | 26,75 | 18,00 | 44,75 |
| | 1923 | 27,40 | 21,00 | 48,40 |
| | 1924 | 30,66 | 25,15 | 55,81 |

(d)—Includes Savings Bank deposits.

THOUSANDS OF RUPEES.

| DEPOSITS. | | | | | Cash Balance. |
|---------------------|------------------|---------------------|--------|----------|------------------|
| Fixed. | Savings Bank. | Current. | Other. | Total. | |
| 6,85,00 | 21,74 | 2,28,03 | ... | 9,34,77 | 2,40,76 |
| 7,76,78 | 27,02 | 2,49,27 | ... | 10,53,07 | 2,06,54 |
| 7,17,05 | 28,51 | 3,47,98 | 10,50 | 11,04,04 | 2,71,48 |
| 6,67,39 | 32,59 | 2,17,63 | 8,35 | 9,25,96 | 2,19,37 |
| 3,57,80 | 34,20 | 1,15,82(<i>d</i>) | 9,88 | 5,17,70 | 1,24,12 |
| 3,03,58 | ... | 1,69,44(<i>d</i>) | ... | 4,73,02 | 1,01,56 |
| 3,19,14 | ... | 1,57,48(<i>d</i>) | ... | 4,76,62 | 77,01 |
| 3,28,51 | 61,84 | 1,20,75(<i>d</i>) | 9,34 | 5,20,44 | 87,23 |
| 3,18,20 | ... | 1,63,84(<i>d</i>) | ... | 4,82,04 | 85,44 |
| 5,12,53 | ... | 4,54,30 | ... | 9,66,83 | 2,52,51 |
| 4,97,86 | 17,87 | 5,36,19 | 3,23 | 10,55,15 | 1,60,39 |
| 5,38,17 | ... | 4,62,98 | ... | 10,01,15 | 1,85,74 |
| 4,75,42 | 29,81 | 4,62,80 | ... | 9,68,03 | 1,97,71 |
| 5,23,52(<i>d</i>) | ... | 4,27,42 | ... | 9,50,94 | 2,29,64 |
| 49,57 | 63 | 54,12 | 11,00 | 1,15,32 | 25,70 |
| 82,08 | 1,05 | 79,67 | 43 | 1,63,23 | 40,34 |
| 97,78 | 1,37 | 60,74 | ... | 1,59,89 | 39,75 |
| 1,00,77 | 1,60 | 39,27 | ... | 1,41,64 | 18,71 |
| 99,34 | 1,87 | 37,89 | ... | 1,39,10 | 27,65 |
| ... | ... | ... | ... | 11,03,44 | 1,83,44 |
| 7,11,39 | ... | 6,27,91(<i>d</i>) | ... | 13,39,30 | 2,35,71 |
| 7,28,23 | ... | 5,93,85(<i>d</i>) | ... | 13,22,08 | 2,15,95 |
| 8,84,05 | ... | 6,85,46(<i>d</i>) | ... | 15,69,51 | 3,03,69 |
| 7,77,91 | ... | 6,08,25(<i>d</i>) | ... | 13,86,16 | 3,70,34 |
| 2,36,99 | 17,31 | 53,29 | 1,66 | 3,09,25 | 67,86 |
| 3,03,12 | 24,72 | 61,37 | 3,92 | 3,93,13 | 51,53 |
| 3,92,01 | 29,65 | 65,88 | 4,90 | 4,92,44 | 1,04,14 |
| 4,36,13 | 32,60 | 69,26 | 5,41 | 5,43,40 | 59,02 |
| 5,06,94 | 38,18 | 73,44 | 7,51 | 6,26,07 | 81,92 |

EXCHANGE BANKS

It would be more appropriate to describe these banks as foreign banks because they are not registered in India. To designate them by the name of the type of business in which they are mainly engaged is rather misleading. Are not the Joint-stock Banks of the country free to do exchange business? It is a different question that they have not devoted any particular attention to or that they do not possess special facilities for such transactions; but there is nothing to prevent them from engaging in them. Similarly the Exchange Banks are also Joint-stock Banks. They can do the same business as is done by the Indian Joint-stock Banks. The classification of banks working in India should not be overlapping or misleading or violate principles of logic. The best way to classify is to divide the banks between Indian and Foreign and then divide each sub-class according to the nature of business carried on.

The foreign banks which had business offices in India in 1924 totalled nineteen. Their names are : Chartered Bank of India, Australia and China, Lloyds Bank, Eastern Bank, Imperial Bank of Persia, Mercantile Bank of India, National Bank of India, National Bank of South Africa (Indian branch since closed), P. & O. Banking Corporation, Thomas Cook & Sons, Nederlandsche Handel-Maatschappij, Nederlandsch Indische Handelsbank, Banco National Ultramarino, American Express Company, Hongkong and Shanghai Banking Corporation, International Banking Corporation, Comptoir National d'Escompte de Paris, Bank of Taiwan, Sumitomo Bank and Yokohama Specie Bank. From

Appendix IV it would appear that the figure of their Indian deposits is steady round about Rs. 70 crores. In 1913 the total of their Indian deposits was only Rs. 31 crores. It would also appear that their total business both of Indian and non-Indian offices is very large, the Indian business forming a small percentage. As the individual Indian business is not disclosed even in government statistical publications we are unable to give such figures.

The Indian branches of the foreign banks do every type of banking business. Like the Indian Joint-stock Banks they receive deposits in India, make advances in this country, negotiate bills, and do agency business. They, however, devote their main attention to the exchange operations, *i.e.*, to the banking business in connection with the foreign trade of India. These operations include transactions like remittances abroad, drawing of funds from foreign countries, negotiation and collection of foreign Bills, opening of foreign credits, and issue of foreign letters of credits. The foreign trade of India is about Rs. 600 crores per year which principally passes through their hands.

It may be worth while to illustrate how they finance such international business. Suppose wheat or cotton is to be exported. This can happen in two ways. Either a foreign merchant would purchase it or some merchant in India would like to send it abroad to be sold. In the former case the buyer would instruct his bankers to make arrangements with some of the foreign banks working in India to negotiate bills in respect of the shipment, which he would pay on maturity. The bank in India

would discount the bill of the drawer (*i.e.*, pay to the seller equivalent in rupees, at the current rate of exchange, of the amount due to him less any discount, that may be customary or settled between the buyer and seller), and send it to its foreign office. If the bill is a sight bill, *i.e.*, payable on presentation it would be paid by the bank that sent instructions for its negotiation or by the buyer. If the bill is a usance bill it would be simply accepted on first presentation and paid by the drawee at maturity. The bill, however, would not be ordinarily kept by the discounting bank in its portfolio to be collected when due, but rediscounted according to money position with some other bank or some bill broker. Thus the foreign bank could reimburse itself, if necessary with the amount of the bill, less discount, immediately it reaches destination. Similarly if the bill had been directly negotiated from a party in India the same procedure would have been followed and the bank would have got the funds on rediscounting it after arrival at the place where it was due. Thus much of the finance required for dealing in exchange transactions is obtained from borrowed funds. Foreign bills, although not payable in London, are often rediscounted in the London market, as it is more or less the world's clearing house for international payments. The foreign offices would similarly negotiate bills payable in India which when received here are first accepted by the drawees and then paid on due dates. Money originally invested in India in negotiating outward foreign bills is thus ultimately repaid here by the buyers of foreign goods. There is, however, one difference between the financing operations of outward bills and inward bills.

The outward bills are usually rediscounted but the inward bills are held by the banks till they mature. As remarked elsewhere the practice of rediscounting bills on the part of banks does not exist in this country.

Greater portion of India's foreign trade is with England or *via* England and as such, majority of the outward foreign bills are rediscounted in the London market. The rate of discount there is generally lower than that prevailing in India and as such the foreign banks can command cheaper money for financing exchange operations which is not available to the Indian banks. This is the chief reason why the Indian Joint-stock Banks find it difficult to compete with the foreign banks in the exchange business. They not only lack the re-discounting facilities abroad but they also cannot get money so cheaply locally.

Some of the foreign banks working in India have arrangements with other big foreign banks that have no offices here, whereby they enjoy large open credit lines at the bigger banks against the general security of their bills both inward and outward. Such an arrangement gives them command over large funds at very reasonable rate of interest with the result that they are never handicapped for want of money.

Some experience and knowledge of the currencies of the world, of the various discount markets and of the future trade currents is required if the exchange operations are to be successfully carried. But there is nothing extraordinary about these operations as some are led to believe. Given proper chances and opportunities Indians can as successfully put

them through as people of other nationalities. The business no doubt has some risk attached to it due to the unsatisfactory system of our currency whereby the value of rupee is not linked to gold, which is the international basis of money, but liable to fluctuations which sometimes are great.* The risk, however, is greatly eliminated by cautious bankers by the process of covering according to which their sales and purchases very nearly balance. Moreover, the Government of India usually intervenes to maintain the international price of the rupee within certain limits. But the profits which the foreign banks derive from the finance of foreign trade are not small and the risk, even if any, is not much in comparison to such gains.

Main advantage from the finance operations of the foreign banks is derived by the foreign merchants and firms whether working in India or outside. The people of the country are not encouraged to engage in foreign trade because credit facilities are not extended to them as freely as to the foreigners. Without banking assistance commercial operations are practically an impossibility in these days. It may be true that the foreign trade is mainly carried on by the foreigners who have large organisations for this purpose. But these large firms have sprung up in many cases from small beginnings and their present position is chiefly due to the assistance extended to them by banks from time to time. Owing to the immense

* Since writing the above the "Ratio" question has been settled by the Legislature and the rupee has been stabilized at 1s. 6d. gold. If the Indian currency authorities are able to maintain this value future fluctuations in the price of rupee will be between the gold points viz. $1/6 \frac{1}{8}$ and $1/5 \frac{1}{2}$.

profits which the foreign banks are getting from their connections with this country, without restrictions of any kind whatsoever, they should at least pay some attention to the development of foreign trade and commerce on the part of the people of India. The retailers or wholesale dealers, who ultimately market the foreign goods in India, are of course Indians but they are not usually the principal parties to the first hand transactions between the world and this country and their business cannot be called international. When Indians directly deal with the outside world and the volume of such business is large, we can then and only then say that Indians are engaged in foreign trade. Bank facilities and bank assistance are greatly necessary for such development. The foreign banks have not extended any such help nor is there any reasonable probability that they would do so in the future. The vested interests with which they are connected or which influence them are too strong to permit them to encourage Indian enterprise in this direction. The Indian banks in the present stage of their development lack the means to assist them. How should then the problem be solved? We shall attempt a solution in a later part of the book.

Not only do the foreign banks come in the way of Indians engaging in foreign trade but they also encourage the import of foreign manufactures which acts as a deterrent to the advancement of Indian industries. Even the raw products which are exported from India are bought cheaply mainly through the supply of money which the foreign banks give to the foreign merchants in this country. The

poor cultivator very often receives advances of money long before his crops are ripe and they are either sold cheaply to the supplier of money or mortgaged to him. The ultimate results of the financial operations of the foreign banks so far India is concerned are thus not to the advantage of our economic interests.

The foreign banks do not engage Indians in any responsible posts. According to them Indians are only fit to be clerks. During the last so many years that these banks have been working in India there are hardly any instances in which their Indian employees have been promoted to any position of trust or responsibility. Many of their managers have not been slow to speak candidly of the merit of some of their Indian clerks but when the question of promoting them to the Officer's grade comes the obstacle of race or colour becomes insurmountable. During the last great War when the European assistants of foreign banks were called away on military duty the Indian assistants rendered valuable service. Some of the managers out of real appreciation recommended some of the Indian employees to be made into officers. The reply invariably received from the banks' boards was "We do not wish to create a dangerous precedent." Yes, dangerous indeed to the long established monopoly of the foreigners in banking! Another bank manager is said to have written to his London Office, "We cannot long hide from our Indian employees what worthless stuff sometimes we get from Home. It takes lot of time and trouble to 'lick' some of the assistants into shape. Can not we encourage 'versity men to come out for banking service in

the East.....". Whenever the question of chances to Indians in foreign banks has been broached the reply has been that they are either lacking in efficiency and requisite knowledge or that the Indians have to demonstrate their fitness and character for being entrusted with responsibilities. This is, however, simply a make-shift. The above quotations show what is the real position. In point of character Indians are not inferior. Of late some of the large frauds in foreign banks have been committed by their own responsible officers. When Indians are being stigmatised as unfit or lacking in strength of character it is nothing but deliberate misrepresentation of true facts. When one visits foreign countries he always sees that foreign banks there mainly engage local men on their establishments, both junior and senior. One very rarely comes across foreigners managing local offices of foreign banks. In some cases not even a single foreigner is posted and the whole staff is recruited locally. It is only India where this unhappy state of affairs exists and continues to the discouragement of Indian banking.

The foreign banks have assumed great force in the banking of this country. The measures which we are suggesting in a later part although quite legitimate and current in other countries are sure to be resented by this class of banks as they somewhat affect their monopoly or privileged position. And one of the grounds for such opposition, as has been sometimes given, would be the non-availability of sufficient supply of Indian bankers. But in the name of what fairness can they advance this argument when they themselves are to blame

for this state of things? By wilfully excluding Indians from higher posts in banking and continuing to do so India would never be deemed fit by these people to build up her banking system. The country's interests are, however, much more important than their biased opinions.

In fairness to the foreign banks it may be said that they have been the pioneers of corporate banking in this country and helped not a little to develop the banking habits amongst the people. But their services or usefulness in these directions have not been actuated by disinterested or philanthropic motives. Their primary object has been to earn profits and it is only incidentally that India has been awakened by their activities. How befitting it would have been, if they had from their very commencement paid some consideration to India's interests. We would have had then great regard and esteem for them. Their existence side by side with the banks of the country, nay even as an integral part of the banking system of the country would have been welcome. Let us hope that it is not too late even now. And that with the co-operation and sympathy of all persons doing banking business in India which has been giving them large profits, India would soon build up a sound system of banking institutions which would accelerate the country's development.

CHAPTER IV

BACKWARDNESS AND DEFECTS

Comparison of banking business of India and United Kingdom, India and Canada, India and Australia, India and United States—Indian banks smaller in size than banks in other countries—Figures of some important banks of the world—Analysis of Indian banking figures according to nationality of capital holders and management—Indian banking not only inadequate but wanting in systematic organisation—Causes of backwardness: Defects—Components of complete banking system.

We have endeavoured to describe briefly in the preceding two chapters various types of banking institutions existing in India. Our next task is to ascertain how our banking figures compare with those of other countries: whether we are backward in banking activities or not, and whether the growth is adequate. We shall also attempt to find out the disabilities under which the Indian banking system is working, and its defects.

INDIA AND THE UNITED KINGDOM

A comparison of the banking and other statistics of these two countries is specially interesting, as India is ruled by the United Kingdom. The figures which will enter into the Comparative Analysis are given below in Table I.

TABLE I

| i. | ii. | iii. | iv. | v. |
|--|--------------------------------------|---------------|-----------------|--|
| DESCRIPTION. | Year to which the statistics relate. | INDIA. | UNITED KINGDOM. | Percentage which figures in (iii) are of the corresponding figures in (iv) (approx.) |
| Population (in Millions) | 1921 | 319 | 47 | 679 |
| Area (in 1000 Sq : Miles) | | 1766 | 121 | 1460 |
| Total Exports and Imports (in Million £). | 1919 | 350 | 3425 | 10 |
| Banking Capital and Reserves (in Million £). | 1920 | (a) 19(b) | 180 | 10 |
| Banking Deposits (in million £) | 1920 | (c) 235(b) | 2682 | 9 |
| Number of Banks | 1920 | 76(b) | 37 | 206 |
| Number of Banking Offices. | 1920 | 500(b) | 9550 | 5 |
| Average Deposit per head of population in pounds. | | 3/4 | 57 | 1½ |
| Average number of square miles per banking office. | ... | 3532 | 13 | 27170 |

(a) This includes paid-up Capital and Reserves of the then existing Presidency and Joint-stock Banks. Paid-up Capital and Reserves of the Exchange Banks have not been included because they relate to the business of these banks all the world over which is over twelve times their Indian business. To include these figures would be to throw out of proportion deposits when compared to Capital. Moreover their Capital is not subscribed in India and its inclusion in the table is likely to give wrong impression as to the extent to which it has been already tapped and the response which such investment may receive in the future. If, however, it be considered necessary to include a portion of Capital and Reserve of the Exchange Banks it may be permissible to include only $\frac{1}{3}$ th of the corresponding figures in Appendix IV which is the proportion of Indian deposits to their total deposits.

The above table reveals how backward we are in banking activities. The Indian banking Capital and Reserve is only $\frac{1}{10}$ th of that of the United Kingdom. The Indian deposits are only 9 per cent. of the deposits in the United Kingdom. The figures of export and import trade show how closely trade development depends upon the banking development. But our backwardness is not adequately measured only by the above two figures. If we take population into consideration we find India's population is nearly 7 times that of the United Kingdom and if development had taken place simultaneously in both the countries in proportion to the population, our banking figures would be 70 times of what they are now. Again, India has an area nearly 15 times greater than that of the United Kingdom. If banking development in the two countries be compared on the basis of area we are 150 times backward. Both the bases of comparison, *viz.*, area and population are permissible because India is rich in raw products and well populated. Only, organisation of the right type in almost every economic activity is

We have, however, omitted this as the object of the table as well as the comparative analysis is to indicate the development in India.

(b) Figures relating to Co-operative Credit Societies are not included. At the end of 1920 there were only 5 Co-operative banks each having paid-up Capital and Reserve of Rs. 5 lacs and over and 36 Co-operative Banks each having paid-up Capital and Reserve between Rs. 1 lac and Rs. 5 lacs. Total paid-up Capital and Reserve and Deposits of these Co-operative Credit Societies on that date were 106½ and 480 lacs respectively. The exclusion of these figures hardly affects the statistical analysis.

(c) Includes Indian deposits of Presidency, Exchange and Joint-stock Banks. Post Office Savings Bank Deposits are not included.

NOTE:—Indian figures are converted into Sterling at the rate of Rs. 10 to £1.

lacking. Coming to the number of banking offices we find that in spite of its vast area Indian banking offices are only 5 per cent. of those of the United Kingdom. Taking area into calculation we have roughly on an average 1 banking office to every 13 square miles in the United Kingdom against 1 to every 3,532 square miles in India, *i.e.*, we are more than 270 times backward in this respect. And even making due allowance for the density of population, which in the case of the United Kingdom is twice that of India, the backwardness on the basis of area is not less than 130 times. The larger number of banks in India as compared to the similar number in the United Kingdom only shows how small Indian institutions are in comparison to those in the land of her rulers.

It may be noted in passing that the deposits per head of population in India and the United Kingdom are $\frac{3}{4}$ th of a £ and £67 respectively. If we take the Clearing House figures into consideration we find that the amount of cheques cleared through the London Bankers' Clearing House alone in 1920 was £39,019 millions as against the total of £3,144 millions cleared through all the Clearing Houses* in India.

* In India only Calcutta, Bombay, Madras, Rangoon, Karachi, Delhi, Lahore and Cawnpore have Bankers' Clearing Houses. These Clearing Houses clear only "local" cheques, *i.e.*, payable locally and not "out-station" cheques. The latter have to be collected at the paying banker through agents or branches. In other countries not only local cheques and bills are cleared but also those that are payable at other stations.

INDIA AND CANADA

TABLE II

| i. | ii. | iii. | iv. | v. |
|--|----------------------------------|--------|---------|---|
| DESCRIPTION. | Year to which statistics relate. | INDIA. | CANADA. | Percentage which figures in (iii) are of the corresponding figures in (iv) (approx.). |
| Population (in Millions) | 1921 | 319 | 8½ | 3753 |
| Area (in 1,000 Sq. Miles) | ... | 1766 | 3729 | 47 |
| Total Exports and Imports (in Million £). | 1919 | 350 | 485 | 72 |
| Banking Capital and Reserve (in Million £). | 1920 | 19 | 25(a) | 76 |
| Banking Deposits (in Million £). | 1920 | 235 | 379 | 62 |
| Number of Banks ... | 1920 | 76 | 18 | 422 |
| Number of Banking Offices. | 1920 | 500 | 3440 | 15 |
| Average Deposit per head of population in pounds. | ... | 1 | 44½ | ... |
| Average Number of square miles per banking office. | ... | 3532 | 1084 | ... |

NOTE.—Indian figures are subject to the remarks given in the explanatory footnotes to Table I.

(a) The Canadian Banks' liability on account of note circulation was \$232, 486, 734.

Our banking development is even much smaller than that of the Dominion of Canada as the above table indicates. Our banking Capital and Reserve and Deposits are 76 and 62 per cent., respectively of the corresponding Canadian figures, in spite of India's population being 38 times larger than that of Canada. Canada possesses more than double of India's land area, but even then the former has one banking office to every 1,084 square miles against one to 3,532 square miles in the latter. We are more than three times backward in this respect. Canadian Deposit per head of population is £44½ against only 15 shillings in India.

INDIA AND AUSTRALIA

TABLE III

| i. DESCRIPTION. | ii. Year to which the statistics relate. | iii. INDIA. | iv, AUSTRALIA. | v. Percentage which figures in (iii) are of the corresponding figures in (iv) (approx.). |
|---|---|----------------|-------------------|---|
| Population (in Millions). | 1921 | 319 | 5½(a) | 5800 |
| Area (in 1,000 Sq. Miles) | ... | 1766 | 2975 | 59 |
| Total Exports and Imports (in Million £). | 1919 | 350 | 247 | 142 |
| Banking Capital and Reserve (in Million £). | 1920 | 19 | 59 | 32 |
| Banking Deposits (in Million £). | 1920 | 235 | 350(b) | 67 |
| Number of Banks ... | 1920 | 76 | 21 | 362 |
| Number of Banking Offices. | 1920 | 500 | 2500 | 20 |
| Deposit per head of population in pounds. | ... | 3 | 63½ | ... |
| Number of square miles per banking office. | ... | 3532 | 1190 | ... |

(a) This does not include full blood aborigines and the population of the territories.

(b) Estimated.

Coming to the comparison of Indian figures with another important part of the British Empire, viz., Australia we find the same tale repeated. In spite of our population being 58 times greater, our banking Capital and Reserve and Deposits are only 32 and 67 per cent. of the Australians. This appears more gloomy when we see that even our foreign trade is 142 per cent. of that of Australia. Australia has little less than twice of India's land area but in spite of this the former has one banking office to every 1,190 square miles against India's one banking office to 3,532 square miles. Deposit per head of population in Australia is more than 79 times the corresponding figure in India.

INDIA AND UNITED STATES

TABLE IV

| i. | ii. | iii. | iv. | v. |
|---|--------------------------------------|--------|--------------------|---|
| DESCRIPTION. | Year to which the statistics relate. | INDIA. | U. S. A. | Percentage which figures in (iii) are of the corresponding figures in (iv) (approx.). |
| Population (in Millions) | 1921 | 319 | 106 ^(a) | 301 |
| Area (in 1000 Sq. Miles) | ... | 1766 | 3026 | 58 |
| Total Exports and Imports (in Million £). | 1919 | 350 | 2779 | 13 |
| Banking Capital and Reserve (in Million £). | 1920 | 19 | 1052 | 2 |
| Banking Deposits (in Million £.) | 1920 | 235 | 7754 | 3 |
| Number of banks including branches. | 1920 | 500 | 30139 | 2 |
| Deposit per head of population in pounds. | ... | 3/4 | 73 | ... |
| Number of square miles per banking office. | ... | 3532 | 100 | ... |

(a) Exclusive of outlying possessions.

Our banking backwardness although great when compared with similar economic activities of the United Kingdom, Canada and Australia, assumes still much greater proportion when compared with the figures of the United States of America. In spite of our population being three times that of U.S.A. our banking Capital and Reserve and Deposits are only 2 and 3 per cent. of those of the latter. Our banking offices are only 500 as against over

30,000 in U.S.A. There is one bank to 3,532 square miles in India against one to 100 square miles in U.S.A. Deposit per head of population is £73 in the U.S.A. against 15 shillings in this country. There is no wonder that the United States is prosperous with her agriculture, commerce and industry flourishing, because her banking, which is the backbone of economic activity, is greatly developed.

The above few comparative analyses would definitely establish the backwardness and inadequacy of our banking activities. If we compare our figures with the figures of France, Germany, Italy, Japan, and other important countries of the world the same results would be repeated. We have put some of these results in the form of charts on the frontispiece to make them vividly apparent at a glance. Does it not follow then that our rulers have not been as mindful of India's prosperity as they should have been? India is rich in agricultural and mineral products. It possesses large possibilities for industrial and manufacturing activities. And if efforts had been systematically made from the beginning our country would not have shown results inferior to what other countries have achieved through organised exertions during the last 60 or 70 years.*

*Figures given in tables I to IV in this Chapter are only approximate. They are, however, sufficiently reliable as statistical estimate for the purpose in view. Owing to the non-availability of ready figures in certain cases approximations have been worked by interpolation according to mathematical formulæ.

Since writing the above the author has come across statistical figures relating to banks, quoted by Principal M. L. Tannan in his presidential address to the Indian Economic Conference at Calcutta. The statement is given below. These figures are as on 31st December 1924 and as such more recent. They further confirm the correctness of approximations referred to in this chapter.

We have mentioned in an earlier part of this chapter that banks in India are of very small size as compared to the banks in other countries. This can be seen at a glance by dividing the figures of Capital and Deposits by the number of banks. To further establish this point we give on the next page figures of some of the banks in foreign countries and in India. The figures tell their own tale. The deposits of each of the "big five"^(a) of London are more than the Total Indian Deposits. The deposits of the Imperial Bank of India which has the largest deposits in this country are less than $\frac{1}{3}$ rd of the deposits of National Provincial Bank, Ltd., which has the smallest deposits amongst

Statement showing certain banking statistics of a few countries as on 31st December, 1924.

| Serial number. | Name of country. | Number of banking offices. | Number of banking offices per million of population. | Number of banking offices per 2,700 square Miles. | Capital (in Million £.) | Capital (in Million £.) per million of population. | Deposits (in Million £.) | Deposit per head (£). | REMARKS. |
|----------------|---------------------------|----------------------------|--|---|-------------------------|--|--------------------------|-----------------------|---|
| 1 | United Kingdom. | 11,976 | 285 | 362 | 112 | 2.5 | 2510 | 60 | (a) Includes saving and special banks. |
| 2 | United States of America. | 30,000 | 256 | 20 | 664 | 5.6 | 10372 | 87 | (b) Excludes deposits of Exchange Banks. |
| 3 | Japan ... | 7,465 | 92 | 80 | 154 | 1.88 | 1011 | 14 | (c) Excludes capital of Exchange Banks. |
| 4 | Canada... | 4,883 | 448 | 3 | 27 | 3.0 | 458 | 50 | |
| 5 | India ... | 596 | 2 | 1 | 10(c) | .03 | 93.5 | .3 | NOTE— Yen = 24d. 4.86 = £1. Rs. 15 = £1. |

(a) The "big five" banks are : Lloyds Bank, Midland Bank, Barclays Bank, National and Provincial Bank and Westminster Bank.

BANKING FIGURES OF SOME OF THE

| NAME OF BANK. | No. of Branches. | Subscribed Capital £(1,000). | Paid-Up Capital £(1,000). |
|--|--|------------------------------------|---------------------------------|
| <i>British Empire.</i> | | | |
| Bank of England (x) ... | ... | ... | 14,553 |
| Lloyds Bank, Ltd. (a) ... | 1,671 | 71,865 | 14,373 |
| Midland Bank, Ltd. (a) ... | 1,838 | 39,233 | 11,977 |
| National Provincial Bank, Ltd. (a) | 1,128 | 431,617 | 9,479 |
| Bank of Montreal (a) ... | 540 | 6,147 | 6,147 |
| Royal Bank of Canada (a) ... | 656 | 4,192 | 4,192 |
| Canadian Bank of Commerce (a) ... | 581 | 4,110 | 4,110 |
| | | | |
| Bank of Australasia (a) ... | 211 | 4,000 | 4,000 |
| Imperial Bank of India (z) (y) ... | 164 | 11,250 | 5,625 |
| Central Bank of India, Ld. (y) (z) | 18 | 3,362 | 1,681 |
| Bank of India, Ltd. (z) (b) ... | 2 | ... | 1,000 |
| Allahabad Bank, Ltd. (z) (b) ... | 35 | ... | 355 |
| <i>Other Countries.</i> | | | |
| Netherlands Bank (c) (d) ... | 2 | ... | 1,721 |
| The Java Bank (c) (f) ... | ... | ... | 500 |
| Nederlandsche Handelmaatschappij (a) (d). | ... | ... | 10,602 |
| Reichsbank (c) (k) ... | 100(h) | 10,294(j) | 4,015 |
| Guaranty Trust Co. of New York | 10 | 5,144 | 5,144 |
| Darmstädter und National bank (c) (k) | <div style="display: inline-block; vertical-align: middle;"> { <div style="display: inline-block; vertical-align: middle;"> 138(l) 103(m) </div> </div> | ... | 2,941 |
| Credito Italiano (n) (o) ... | 60(h) | ... | 4,000 |

IMPORTANT BANKS OF THE WORLD.

| Reserve £(1,000). | Deposits £(1,000). | REMARKS. |
|----------------------|-----------------------|---|
| 3,616 | 126,031* | (x) From Statement, dated 27th August, 1925. *Includes £22 millions of public deposits. The liability on account of notes issued was £181 millions. |
| 10,000 | 338,371 | |
| 11,977 | 348,359 | |
| 9,479 | 234,291 | (a) From "Banking accounts analysed and compared" issued by Frank Newson Smith & Co., Stock Brokers, London, in 1925. |
| 6,147 | 124,415 | |
| 4,192 | 97,372 | (b) From Statistical table relating to banks in India 1924. |
| 4,110 | 87,631 | (z) Rupees converted into Sterling @ Rs. 10 = £1. |
| | | (y) From Balance Sheet, dated 31st December, 1925. |
| 3,700 | 28,010 | (c) From Balance Sheet, dated 31st March, 1924. |
| 4,825 | 83,300 | |
| 1,000 | 15,933 | (d) Exchange @ f. 11·62 = £1. |
| 837 | 9,509 | (e) The bank had liability for over £87 millions in respect of notes issued. |
| 495 | 9,260 | (f) Exchange @ f. 12 = £1 |
| | | (g) The bank had liability for about £22 millions on account of notes issued. |
| 1,187 | 1,888(e) | (h) Approximate. |
| | | (i) Notes in circulation over 210½ million £. |
| 728 | 6,450(g) | (j) Authorised increase. |
| ... | 40,000(b) | (k) Exchange @ 20·40 marks = £1. |
| 3,530 | 41,219(i) | (l) Main Branches. |
| 4,191 | 130,045 | (m) Sub-branch Offices. |
| 1,960 | 32,801 | (n) From a statement in 1925. |
| 1,300 | 49,720 | (o) Exchange 100 Liras = £1. |

the "big five." The deposits of the Allahabad Bank, the oldest of the Indian Joint-stock Banks, are less than $\frac{1}{28}$ th of the deposits of the same English Joint-stock Bank. The deposits of the Midland Bank, which has the largest business among the "big five" are over four times that of the Imperial Bank and about 40 times that of the Allahabad bank.

Comparisons like the above can be easily made between the figures of Indian Banks and other foreign banks.

The tale of our sluggishness in banking is not finished with the above description. The analysis of the banking figures between the various classes of banks in India reveals a woeful position. We take for this purpose the following table V which gives banking figures as at the end of 1924.

TABLE V

Table Showing Indian Banking Business (1924).

| | IMPERIAL BANK. | JOINT- STOCK BANKS. | EXCHANGE BANKS. | CO-OP- ERATIVE BANKS. | TOTAL. |
|---------------------|-------------------|---------------------------|--------------------|-----------------------------|-------------------|
| | (Rs. in lacs). | (Rs. in lacs). | (Rs. in lacs). | (Rs. in lacs). | (Rs. in lacs). |
| Paid-up Capital ... | 560 | 760 | ... | 170 | 1,490 |
| Reserve and Rest | 480 | 420 | ... | 70 | 970 |
| Deposits ... | 8,420 | 5,520 | 7,060 | 1,250 | 22,250 |
| Cash Balances ... | 1,560 | 1,160 | 1,640 | 60 | 4,420 |

Out of the total deposits of Rs. 222·5 crores, more than $\frac{1}{3}$ rd, viz., Rs. 84·2 crores are in the hands of the Imperial Bank which is managed by foreigners and cannot be called Indian in the true sense. Another $\frac{1}{3}$ rd are secured by foreign banks which

utilise this vast sum principally in the financing of foreign trade. Out of the remaining $\frac{1}{3}$ rd deposits lodged with the Banks of Indian domicile, nearly 25 crores of rupees are deposited with banks under European management whose sympathies with Indian banking aspirations are not as they should be. The purely Indian banks, *i.e.*, owned by Indian shareholders and managed by Indians, possess between themselves about 42 crores of deposits, *i.e.*, approximately $\frac{1}{5}$ th of the total bank deposits in India. Does any country reveal such a deplorable state of affairs? The Central Bank of India which has a Paid-up Capital of Rs. 1.68 crores, Reserve and Rest of Rs. 1.13 crores and deposits Rs. 14 crores (these figures are highest amongst all the Indian Joint-stock Banks), and is a purely Indian managed institution, has clearly demonstrated the capacities of Indians to do banking business on safe lines. It is really creditable for the authorities of the Central Bank, specially for its moving spirit Mr. S. N. Pochkhanawala, that although this bank started less than 15 years ago *i.e.*, long after the existing important Joint-stock Banks had been securely established and had sufficiently progressed, whether managed by Indians or Europeans, it has progressed further than all of them. The Government blue books do not reveal the individual Indian business of Exchange Banks and as such it is difficult to compare the Central's business with any of them. But if averages can be taken Central's position is predominant. Even taking business of the Imperial and Central Banks per branch, the result is in favour of the Central Bank. The Central's foremost position

in the Indian banking field is undoubted. But one Central is not enough. There should be many more Centrals to exert appreciable influence on the conduct of Indian banking in the Indian interests and to win back the banking-field, which if not absolutely lost, has been up till now at least freely given to the foreigners for their fullest exploitation.

The Indian Banking is not only conspicuous by its backwardness but also by the non-existence of any systematic organisation. Further we observe only one type of banking activity which principally deals with short term credit. It is known as "Commercial Banking." The Imperial Bank, the Exchange Banks, and the Joint-stock Banks all transact only short term credit operations and belong to the class of Commercial Banks. The Imperial Bank can not function properly as the Central Bank or bankers' bank and pivot of money market under the present order of things. There do not exist any other types of banks which can adequately assist other economic activities like industry, land and forest developments, etc. The Co-operative Credit movement calculated to help the *ryot* is in its infancy with very doubtful prospects of growth under its present organisation. There are no industrial and land mortgage banks. The municipal and local savings banks are not in existence. The lower ranks of middle class people have no organisation whereby they can get some financial assistance in times of need. The Commercial Banks give them no countenance. They like ordinary cultivators are prey to the money-lender.

The one-sided activity of the Indian banks to assist commerce and trade mainly, is due to the

wholesale copy of the English model without paying any attention to the varying circumstances and needs of India. In fact this complaint of wholesale importation of English economic ideas and practices, without any regard for local conditions or minute study thereof, does not apply to banking alone but refers to our other activities as well. The banking system of England chiefly consists of Joint-stock Banks whose principal business is to assist commerce of the country. The banks there have never thought it to be their province to extend long term credit to industries and agriculture. Possibly this is due to the English habit of direct investment in stocks and shares which has always produced sufficient capital for the conduct of such activities. England is not an agriculturist country and it has not felt any necessity for special organisation for land and agricultural credit. But things here are quite different. India is not simply a principal agricultural country but it has vast mining and manufacturing possibilities also. These sources have been hardly tapped. We need credit institutions that can assist in the divers economic developments and forces of production. We want Agricultural and Land Mortgage Banks that will help the agriculturist class and increase and improve land production, the Industrial Banks that will assist in the foundation and growth of Indian industries, the Commercial Banks that will adequately finance the movement of goods, and the carrying on of internal trade, the Exchange Banks that will assist India's international trade and so on. India is a very vast country having

area bigger than Europe minus Russia, ranking in point of population as the third biggest country in the world. It is not barren or desert land like the desert of Sahara. Practically whole of its area is rich either agriculturally or minerally. It has a beautiful coast line with possibilities of many good commercial harbours. Is it not then really deplorable that in spite of so many natural advantages the country is so backward economically? Even England, with her developed industries and banking, has been now and then feeling want of special banks which will extend help to industries. The Ministry of Agriculture and Fisheries issued last year report on the means of creating and organising agricultural credit, although England is hardly reckoned amongst the agricultural countries of the world. Should not then India also develop all types of credit institutions competent and willing to meet demands from all classes of undertakings? Sound, adequate but diversified system of credit institutions is the only remedy against the economic sluggishness, that has been allowed to exist and continue. It is really an irony of fate that the country which was amongst the first few to realise the importance of credit institutions and possess them—when the modern advanced nations were still undeveloped and even to an extent uncivilised—is now left much behind in the march of progress.

“What are the causes of this backwardness or deficiency?” is a natural question that every reader is likely to ask. The Indian banks are working under grave disabilities and defects which make it, if not absolutely impossible, at least greatly

difficult for any system to be evolved or for regular, systematic and steady growth. Some of these may have been noticed already. We briefly give them below :—

- (i) Want of realisation of the importance and necessity of credit institutions on the part of the people and lack of propaganda for the same.

We have amidst us many movements for social, political, communal and other welfares but none of them has seen or realised the necessity of economic progress, with sound banking at its back, as the first step for any real advancement. No one has seriously considered that banking is the key of economic regeneration and through it of other channels of development. The conception of *Swadeshism* of the Indian National Congress does not go beyond the need for consumption of Indian-made articles. The national importance of economic activities like Insurance, Banking, Shipping, etc., has never been touched upon the political platforms. Even the Indian Chambers of Commerce and the allied bodies have not sufficiently realised the imperative necessity of sound and sufficient credit institutions under the control of the people of the country. The Indian Economic Association has been of late giving some attention to these problems. Banking, however, is such a vital matter that it should not be the subject for deliberations by economists only but recognised as the first article of progress by Commercial, Industrial and Agricultural Associations, and by all the political parties, Congress and Conferences.

Propaganda is specially needed in a country like India where the majority of population is illiterate and modern banking habits are not developed.

- (ii) Want of sympathetic attitude on the part of the Government towards Indian banking and its not realising or reckoning banking development of the country amongst the necessary duties of the State.

The Government's step-motherly treatment of the country's banks is proverbial. It has done all in its power for the development of irrigation, railways, telegraphs, etc., but never seriously tackled the problem of banking in spite of its greatest importance to the body politic. The principle of discriminating protection to Indian industries has been recognised but nothing done for banking reconstruction, without which industries cannot exist or grow. The Government has been, at best, dormant and indifferent spectator of the progressive domination of non-Indian element in Indian Banking. It is spending large sums every year for political propaganda and other publicity works. And should it not spend something to make known advantages of credit institutions and popularise banks and banking habits which alone can bring all the productive forces into satisfactory operation ?

- (iii) Want of requisite machinery whether in the shape of legislative measures as in U.S.A. or some other equally effective arrangement which could control matters like the following :—

- (a) Rigid scrutiny before granting Certificate of Incorporation.

- (b) Nationality of Capital holders and Directors.
 - (c) Minimum amount of Capital which should be subscribed and paid up before commencing business.
 - (d) Relation of minimum Capital to the area or territory and/or population which a bank proposes to serve.
 - (e) Cash reserves in respect of deposits.
 - (f) The correct credit information which each borrower should disclose when applying for credit—borrower being liable to criminal prosecution in the event of deliberately giving false information.
 - (g) Maximum amount that can be advanced to each individual or concern.
 - (h) Frequency with which statement of accounts should be published—nothing inspires greater confidence than the publicity of accounts.
- (iv) Want of examination or inspection on the part of the State in the general interests of the depositing public and shareholders as is done in U.S.A.

This may not be necessary in the case of countries that have their banking well established but countries like India essentially need this to induce requisite confidence in their banks.

- (v) Non-existence on a sufficient scale of the system of discounts and rediscounts.

Commercial paper is a great factor in the money market of other countries, both because of its negotiability and its being reckoned as a back-

ing to currency. Indian money market will not function properly unless discounting and rediscounting of trade bills is adequately organised.

(vi) Want of a properly organised Central Bank with note issuing functions, or of Federal Reserve Banks as in U.S.A., which can work as bankers' bank, exercise toning and co-ordinating influence over the whole system and regulate the money market.

We have shown in a preceding Chapter how the Imperial Bank sadly falls short of the conception of a Central Bank.

(vii) Want of emergency measures upon which banks can rely for support in critical moments.

Like all human undertakings banks cannot be sure of successful career unless they have some reserve arrangements to which they can look up in times of necessity. No such facilities exist in India with the result that the Indian banks have to invest large funds in Government Securities, which constitute their first line of defence, the consequence being that credit is withheld proportionately from commerce and trade.

(viii) Want of co-operation between the banks themselves whether in the matter of mutual assistance or that of establishing general practices on uniform basis.

This is usually voluntary. Associations and institutions of bankers supply this want.

(ix) The non-English knowing customers of banks experience great difficulties in the matter of issuing cheques.

Almost all the banks insist that customers who do not sign in English should sign cheques in presence of their officers either at the time of withdrawal or in advance, which means that merchants have to keep blank signed cheques in their possession long before they are actually needed, which is a source of not small danger. This is the only country in the world where vernaculars are at a disadvantage in the matter of cheque accounts.

(x) The Indian banking system is dominated by non-Indians whose real sympathies and interests can naturally be not with India.

The chief purpose of these people is to earn profits without any regard for the country's prospects or any broad vision for India's economic regeneration. They never admit Indians to any responsible positions, which are a close preserve for non-Indians. They are incapable of that personal touch which is so essential in credit institutions. They hardly come in contact with the masses or needs of the country.

(xi) The deficiency of Indian bankers.

This is but a natural consequence of the vicious system that has been allowed to creep in and continue with the tolerance of the State. Majority of the banks are either owned or controlled by non-Indians who give no opportunity to Indians to hold any responsible post. This deficiency can, however, be easily made up by vigorous measures within 10 or 15 years. The Central Bank of India has been able to bring into existence within so short a period a body of competent people in banking who can easily match with any average non-Indian

banker in this country. And what Central has been able to do should not be impossible of accomplishment by others if they are actuated by same aspirations, patriotism or ambition.

- (xii) Non-existence of diverse types of banks to supply credit to diverse economic activities like agriculture, commerce, foreign trade, industry and so on.

Economic needs of a country like India with vast area and large population can never be adequately looked after by a single type of banks. Moreover, this diversity is specially needed when a country is beginning to grow economically and the productive forces have not been brought into existence or are sluggish. The rapidity with which Germany built up her economic construction, which was proverbial before the Great War, was mainly due to the sound system of her banks, each class principally looking after some major economic development. All the principal countries of Europe, France, Holland, Italy, etc., have practically copied this model. U. S. A. has its banking system divided into different classes. Japan has also organised its banks on the same principle, assigning different types of credit to different types of banks.

The banking system of India to be complete should consist of the following types of banks :—

- (a) Central Bank or an institution corresponding to it which will be centre of the whole banking system and its pillar of support.
- (b) Commercial Banks which will look after the movement of goods and trade and briefly supply short term credit. Prac-

tically all the banks in India belong to this category.

- (c) Exchange Banks that will look after foreign banking and foreign trade. The present Exchange Banks are all of foreign domicile and should be called foreign banks for the sake of distinction. They should not be confounded with this type of banks which should be of Indian domicile and Indian in spirit
- (d) Agricultural and Co-operative Banks which will supply requisite credit to the *ryot*.
- (e) Land Mortgage Banks which will extend long term credit to the land-holding classes as well as help in the establishment of people who will own and cultivate land, *i.e.*, of land holding farmers.
- (f) Industrial Banks which will specialise in industrial flotations and grant long term credit to industrial concerns.
- (g) Savings Banks which will help accumulation of mass savings. We have in India only Post Office Savings Banks but there is scope for Municipal and Local Savings Banks which can employ a portion of their funds as advances to masses in times of necessity and thus be more useful to the society than the Government Savings Banks.

CHAPTER V

TWO MODELS

The Central banking system of Europe and the Federal Reserve system of U.S. A.—EUROPEAN BANKING SYSTEM: Constitution, functions and responsibilities of Central Banks—Whether Central Banks should be owned by State—Bills as reserve for currency—Other classes of banks—Bank rate and its influence—Transactions of bank of issue and commercial banks compared—Peculiarities and tendencies—FEDERAL RESERVE SYSTEM: Principle of federation—Brief history—Early enterprises—State banks, National banks, and Trust companies—Crisis of 1907—Aldrich Vreeland Act—National Monetary Commission (1908)—The Federal Reserve Act—Provisions of the Act—Federal Reserve Board, and Federal Reserve banks, their functions and powers—Central banking and Reserve system compared—Peculiarities of American banking organisation—National bank laws—State bank laws—Trust companies laws.

We have two important models before us in the matter of banking systems.

(i) The Central Banking System of Europe.

(ii) The Federal Reserve System of U.S.A.

It will be worth while to know both these systems, and then determine the basis of our construction.

EUROPEAN BANKING SYSTEM

As the name implies this originated in Europe and is prevalent in all of its important countries. At the head there is a bank of issue also known as Central Bank which is the support of the whole system. Its importance lies not in the volume

of its business which is usually smaller than that of the major commercial banks, but in its currency functions which enable it to regulate the whole money market. A writer has said "the first and chief task of the bank of issue is the regulation of the currency of the country; if the bank of issue had to perform no other function but this, that would be sufficient to justify its existence."

All the European banks of issue, excepting the Bank of England are permitted to reckon bills discounted as a backing to the notes issued, which further impart elasticity to their currency, rising and falling with the commercial requirements. Commercial paper represents commercial activity and increase in one is reflected in the other. The variation in trade activity may be due to seasonal fluctuations or periods of rise and fall. It is quite legitimate to base currency on such activity. Activity means more money is required and decrease in this activity means volume of currency should be proportionately reduced. Unless there is automatic action between the trade intensity and volume of currency, the purchasing power of the monetary unit cannot remain at the same level—assuming other factors to remain constant.

Because of the great importance of the banks of issue they are strictly controlled and rigid restrictions are placed upon the business which they could transact. They are generally not allowed to invest their funds in anything but self-liquidating credits. Their work is national rather than mere concern of profit-making for their shareholders. It is further monopolistic. For these reasons they

are incorporated under special acts of legislature receiving special charters and not under ordinary laws governing corporate banking. The charters are at first fixed for certain periods and then renewed periodically with any changes that may be warranted by circumstances or past history, in the national interests. Legal responsibilities are often placed upon these Central Banks to give special assistance to any particular types of banks and in general to look to the banking development in the public interests. As these banks are owned, managed, directed and controlled by their own nationals, even if there were no legal obligations, they would always have the broad national outlook and foster and guide their credit institutions so as to make them most serviceable to their country's economic needs. Because of the great importance of the banks of issue to the body politic the States exercise some control on their governance. The States also partake in their profits chiefly because their business is of the nature of a monopoly. Sometimes special tax is levied on the amount of notes issued.

Capital of the Central Bank is generally subscribed by private individuals, the voting power being vested in the people of the country only. In some cases, however, part of the Capital is subscribed by the State or the State is solely responsible for the working and obligations of its bank of issue. The Swiss National Bank is an important example of the former where $\frac{2}{5}$ ths of the capital is subscribed by the Cantons, $\frac{1}{5}$ th by the old banks of issues, and $\frac{2}{5}$ ths by the public—only Swiss citizens and corporations domiciled in Switzerland

are permitted to be shareholders. Of the latter, the Commonwealth Bank of Australia is a notable recent example. The bank has no share capital but all its obligations are guaranteed by the Australian Government. There is no board of directors. The profits of the bank are accumulated into two equal reserves: the Bank Reserve Fund and the Redemption Fund. It is satisfactory to note that the sound working of "this State Bank has enabled it to safely survive the criticism levelled against it, as a State Bank, at its formation in 1913. The bank has not only been a steadying influence to the Australian Financial and Banking position, but has given added stability to the banks in the Commonwealth and has certainly strengthened the Commonwealth's position."

In view of the great importance of the subject whether the bank of issue should be owned by the State or be a private corporation it would be worth while to examine this question. All the important banks of issue are privately owned but under strict supervision of the State and majority of bankers think this arrangement to be ideal. They say that Currency functions are very delicate and should be kept clear of political and State domination which may vitiate its working in the political interests. Moreover, State or bureaucratic machinery is full of red-tapism and it cannot be sensitively responsive to monetary vibrations. The working of a State bank would be disturbed and influenced now in one direction, now in another, according as one political party or another is in power. The private bank of issue would only look to the national interests as a whole, the State

supervision curbing any tendency towards profit making at the cost of sound principles. It would be better able to ration credit to different economic pursuits than the State bank which would always favour leanings of the political party in power. Again in the case of private banks of issue penalties or penalty taxes are prescribed which act as deterrent against excessive issue, beyond the limits or without minimum reserves, which are absolutely lacking or meaningless in the case of State banks. What guarantee is there that a State bank would not step beyond the line of safety and endanger stability of its Currency? Moreover the factor of private capital acts as a check on improper grant of credit. Any loss due to negligent advances would affect the shareholders' profits and in serious cases even their capital. The directors elected by the capital holders would always see, that their capital and profits are not jeopardised by the violation of sound principles of central banking. This personal risk is a great safeguard. In the case of a State bank such personal and individual interests do not exist and there is danger of favouritism and irresponsibility influencing its working.

“ A well-managed bank of issue has to fulfil a sharply defined task and it is, therefore, of the utmost necessity that a bank of issue should be entirely free from an influence from any side whatsoever driving it in its management in one direction or another. Party politics should be entirely foreign to its management. A State bank, however, unavoidably comes under the influence of a ruling Government based on the constitution

of political parties. Whereas such political Governments generally succeed one another at relatively short intervals, a State bank will thus unavoidably come under the influence now of one party and then again of another ; and it would seem unavoidable that this will influence perniciously the management of the bank of issue. It will no longer apply the strict rules of economy, but an inclination first in one direction and then in another will mark its business conduct. It can in this way be dragged into foreign political affairs, even as Bismarck with his iron will dragged the "Reichsbank" into hostile action against Russia. This was possible for Bismarck as Imperial Chancellor, because in that capacity he was virtually the Chairman of the Reichsbank and the bank was at that time not sufficiently safeguarded against interference with its business by the Government."

"The dangers attending the establishing of a State bank have during the course of time been so universally admitted that at all the great international economic conferences held during the past six years warnings have been sounded against a State bank and it was recommended that in countries where a State bank was established it should be converted into an independent private bank, naturally, however, under sufficient supervision by the State."

These are extracts from "Reports" issued in 1925 by eminent banker, Dr. G. Visering, President of the Netherlands Bank upon certain aspects of South African Banking and Currency and are entitled to great respect. Specially in a country like India where there are so many

castes and creeds and communal interests very often clash, it would be inadvisable to think of a State bank. The passing of Money Lenders' Bill by the Punjab Legislative Council shows how safe economic principals and even legal obligations are likely to be thrown over-board by the sheer force of numbers of the majority party. It is true that the experiment of a State bank has succeeded in Australia but the conditions there are singular—the Australian Government is largely interested in trade matters. But even then fears are not completely allayed that the State proprietorship would not militate against the best principles of central banking. Moreover the officialism in India is extremely slow and sometimes even irresponsible. Again of late there is a tendency to distribute Government appointments amongst various communities without sufficient regard for the efficiency of service. This principle has been even extended to schools and colleges where admissions are controlled on communal basis. Also recruitment to professional services like those of a doctor, surgeon, and so on, where in many cases human life depends upon the skill and experience of the medical man, are not exempt from the application of this pernicious principle. If the management of a Central Bank were to be carried on these basis there would be no wonder if credit began to be distributed on communal lines instead of according to the necessities and importance of different economic activities. Such a course is sure to lead to currency confusion and defeat the very object of the bank of issue. Thus taking all things into consideration it would be most un-

desirable to entrust the functions of a bank of issue to the official class in this country.

It may also be mentioned that generally there exists only a single bank of issue in each country. There are, however, a few remnants of old banks with powers to issue notes, that exist side by side with the bank of issue in some countries. But the limits upto which they could issue notes are small and their importance in the money market is not much. It has been definitely recognised that plurality of note issue is extremely undesirable as it leads to diverse money rates, diffusion of gold reserves, different degrees of popularity and worth to the notes of different banks, which is specially observable in moments of panic, want of strong centralised force in times of emergency and similar disadvantages and disabilities. The greatest proof and argument of practical value and importance, in favour of a "singular" note issuing institution is the decision recorded in Switzerland in 1905 by a popular referendum, to concentrate note issue in one central institution. Before that date the Cantonal banks in Switzerland had powers to issue notes, which were naturally against withdrawal of this privilege. Even after the result of the popular referendum there was considerable opposition by some portion of the public and Cantonal banks, but as the opposition could not gather 30,000 signatures necessary to admit of reconsideration the proposition became absolute on the 9th January, 1906.

Up till lately Italy had three banks of issue : Banca d' Italia, Banco d' Napoli and Banco d' Sicilia, the first one being the most important. Last year that country adopted a new banking

law, which has, for the first time since the unification of Italy assigned the exclusive privilege of the issue of bank notes to one bank—the Banca d' Italia. The other two banks have lost this right which they held since 1861. They are now nothing more than ordinary credit banks with certain temporary privileges for certain special operations, *e. g.* discount limits, rates of interest, &c., to compensate them for the loss of powers of note-issue which had been granted up to 31st December, 1930. The Italian currency reform is an additional and most recent proof in favour of the “singular” note-issue.

All the banks of issue excepting the Bank of England accept foreign bills in their portfolios and reckon them in their note reserves. “The maintenance of a foreign portfolio is also a means for a bank of issue to protect its own gold supply against sudden drawings. The foreign portfolio can, therefore, serve as a buffer or as a kind of regulator to protect the bullion supply of the country and also to prevent serious changes in the amount of the circulation of money.” The Bank of England's Currency is inelastic in the real sense. It is required to have actual gold against the notes issued beyond a certain figure. And although it can increase the volume of Currency to any limit by having corresponding increase in the amount of gold backing, such increase resembles elongation rather than elasticity. The system is both rigid and costly. Even some English bankers have realised this defect. Lord Swaything in his interview before the United States Monetary Commission of 1908 said, “I am in favour of the Bank of England's utilising

a portion of its banking assets in foreign bills which is profitable as well as strengthens the exchange.....
..... I have been telling Bank of England why not imitate Germany, Italy, and Austria and hold a portfolio of foreign bills. In times of depreciating exchange sale of foreign bills brings greater profit and helps to rehabilitate exchange." But the system has been allowed to continue because of the innate conservatism of Englishmen. Moreover, London is more of an international monetary centre than belonging to one country and the defect is not so apparent but rather eclipsed by her worldwide financial importance. The question has been publicly examined more than once but the investigating bodies have thought it inadvisable to recommend a change chiefly on the ground that it might threaten London's supremacy in the financial world. The Cunliff Committee in its interim report on Currency and Foreign exchanges after the War (1924), remarked: "In view of the comparison with the systems prevailing in foreign countries which have been put forward by various witnesses, we would point that these countries have not in practice maintained the absolutely free gold market, which this country, by reason of its position in international finance, is bound to do. It has, therefore, been open to them to have recourse to devices to steady the rate of discount which, even if successful for this purpose, it would be inexpedient and dangerous for us to attempt." But has not the Bank of England requisitioned special protection in times of special need and the same sanctioned in the public interest? Recourse to expediency in exceptionally critical periods is no

argument against the otherwise everyday soundness of the system. But be it as it may in the case of England, it is quite evident that for a country like India, which is in its infancy economically and would take long before it can aspire to occupy a prominent place in the international finance, the model of Bank of England is extremely unsuited.

Next in point of importance come the commercial banks, industrial banks, and the remaining types. All the banks, however, are independent of each other and of the central bank. There is no official connection between the various parts of the system but all the same there exists a cohesion, a sort of unrecognised but none the less strong connection. All the important banks keep their surplus cash and accounts with the central bank, make large mutual transfers through it, often conduct clearing business at its offices, make provisions for emergency requirements with it and so on. The main source of investments of the banks of issue is to discount trade bills. Other banks also rediscount their bills with this bank whenever they require additional funds and specially in times of crisis. The banks of issue are thus the final source where currency is obtained against discounts and rediscounts. The tests which they establish as to which kind of paper could be accepted for discounting are consequently acknowledged, recognised and insisted upon by other banks also; they would naturally like to have that kind of paper in their portfolios which they could make use of in times of emergency and get rediscounted with the bank of issue. The bank of issue thus to an extent puts commercial practices on a uniform basis.

One of the conditions of creation of currency on the part of the central banks is to maintain a certain proportion of gold. This is, of course, to keep up the international value of their currency. As long as this condition is satisfied the banks of issue can generally go on accepting bills and issuing currency against them. It is, of course, left to them to fix limits up to which they can accept bills from any one individual, firm or bank. And also they are the sole authority to determine the rates at which they would discount bills. Whenever they find volume of currency tending to increase beyond the requisite level or great demands are made upon their gold reserves, due usually to adverse balance of foreign trade, which threaten the stability of their monetary units, they put up the rate of discount. This curbs the undesired trade activity and reduces demand for money. Other banks follow lead and put up their rates accordingly. When rates of interest for advances are put up by banks the rates of interest on deposits are also proportionately increased. This increase in deposit rates induces people to put their surplus money in banks and also restricts their withdrawals. The foreign creditors also postpone the enforcement of their claims and let their money remain to earn higher interest. Further, fresh foreign money is also attracted by the higher rate of interest. Dearness of money lowers prices of local commodities which gives impetus to exports and reduces imports. All these factors act to ease the situation with the result that in course of time tightness for money becomes less and less and the market tends to assume its normal level. Volume

of currency and trade requirements are thus adjusted. As soon as demand for money has slackened and the cash balances with the bank of issue begin to increase, the rate of discount is lowered. This is followed by other banks and the general rate of interest in the market falls proportionately.

Thus the central banks exercise great influence over their respective entire banking systems which always acknowledge their allegiance to their superior strength.

There is some similarity between the transactions of the bank of issue and a commercial bank, *e.g.*, both of them accept current deposits, advance on bills and extend short term credits. But there is fundamental difference between the objects with which they do such business. "The commercial bank finds the centre of gravity of its business on the debit side of its balance sheet, under its assets; it is a trading company established for the purpose of making profits for its shareholders; within reasonable limits of caution it must always be its object continually to extend its operations by increased business and therefore to give more credit in the form of discounting bills, granting advances, with or without security, and looking out investments of money at its disposal or for account of others. It would try to extend its working capital by attracting moneys of third parties in the form of deposits, and with this object in view to pay interest on those deposits."

"The real business of the bank of issue is, on the contrary, to be found on the credit side of the account, under its liabilities. It has always to carry out its business in the direction of the public

interest ; therefore, it should never extend its note circulation for its own interests ; nor should it ever hold out the prospect of interest on the moneys which are entrusted to it. It obtains those moneys from the country because its acknowledgements of debt in the form of notes and demand balances must perform the function of currency and are accepted as such by the public.”

Thus the commercial bank always takes up an active position whereas the bank of issue assumes a passive one, as regards the attraction of funds from the community with the object of extending business. There is really speaking no competition. In spite of this, however, there is complaint in some quarters that the bank of issue should not freely accept business from the public but give cheap facilities to banks alone. This is against the very first principles of a sound bank of issue. One of the chief functions of the bank of issue is to check by its existence, the price of credit from becoming unduly cheap or excessively dear, and to see that credit is properly rationed by banks as a whole. And this it cannot do, if its doors were not open to all the applicants for credit. It “ enters the sphere of banking from totally different motives than to make a profit from it ; it does it because and in so far as it is its public duty.” Its rate of discount is usually higher than that of the commercial banks and it gives no interest on deposits. How can it then be said that a responsible and properly constituted bank of issue competes with other bankers ? It has been in fact fully realised in all the large money centres in Europe and in the United States by all, including the banks themselves, that the

Central Bank has to perform a much higher task, and in addition care for the public interest, and even for the real interests of the commercial banks. "It gives commercial banks great confidence to know that there is next to them a powerful central institution which is always watching the solvency of other banks."

The above is the general description of central banking in Europe. There are, however, variations here and there to suit local requirements. Wherever a country finds its banking system as a whole has some weak spots in its armour it provides special safeguards, and throws additional responsibilities on its central bank to strengthen the weak links; or again in extraordinary times the usual laws are relaxed and special measures of co-operation and assistance are introduced. But these are exception to the every-day working of the general system. And it is safe to say that the European system on the whole has well stood the test of time.

To complete the description of the European banking system a few points remain to be mentioned. They are :—

- (i) In almost every country there is provision usually by a special law, for the formation of the remaining types of banks, *e.g.*, agricultural, land mortgage, savings and so on, which specialise in their special spheres of credit. The central bank is usually charged with the responsibility of giving them adequate assistance and facilities. It is unnecessary to enter into further details concerning them at this stage. We shall have

occasion to refer to them later when dealing with their organisation in this country.

- (ii) The movement towards bank amalgamations during recent years: In almost every country in Europe commercial banking has come to be concentrated in the hands of a few banks. Their business is large, and they between themselves carry on more than 75 per cent. of the banking transactions. In England the "big five" practically constitute the joint-stock banking. In Germany the "D" banks hold the same position. This state of affairs has both advantages and disadvantages. Because of their vast individual business each of the banks can handle any big banking proposition. Also overhead expenses of management tend to lessen. The disadvantage lies in the fact that credit gets concentrated in the hands of a few, who may consequently get more powerful than it is desirable for society to permit or tolerate. The continued bank amalgamations in England between 1917-1919, when scarcely a month passed without the newspapers recording the merging of one large bank into another, caused a certain amount of concern in various directions, doubts being expressed as to its being to the public advantage, which led to the appointment of a Treasury Committee in 1918 to investigate

the matter. The Committee recommended that the approval both of the Treasury and of the Board of Trade should be obtained before any amalgamations were announced and carried into effect. The Government made it absolutely clear that further amalgamations between the "big five" would not be viewed with favour. And although there is no written law still further bank amalgamations are first referred to the Treasury and Board of Trade for permission and their decision is respected and followed.

- (iii) The branch banking has considerably progressed. All the big commercial banks have hundreds of branches. In fact this is a necessary corollary to the decrease in the number of banks. The chief advantage of the branch system is that surplus funds of one locality can be profitably utilised at others where there may be demand for money. Thus inertia of funds is avoided and utmost credit use is made of deposits. The complaints against the branch system are that the places away from the centre or Head Office do not receive adequate consideration in the matters of financial requirement and also the personal touch between the branch clientele and the top management is lacking.

FEDERAL RESERVE SYSTEM OF U.S.A.

The Federal Reserve System is based on the principle of federation which implies a union of

two or more components under a central body for certain permanent common objects. In the most perfect form of federation the composing units agree to delegate to the supreme federal body certain powers or functions inherent in themselves for the better regulation of their common activities. The residue of powers, after what has been allotted to the central body, is enjoyed and utilised by them unimpaired. Thus federated organisations are subjected to two sets of laws, one the laws of the composing organisation itself and the other the laws of the central organisation.

To appreciate sufficiently the importance and usefulness of this new international experiment in banking it would be better if we give some account of the history of banking in the United States and the circumstances which led to the introduction of this legislation. Owing to the limited space at our disposal it would be only possible to give a very brief account of bank reformation in that ever progressive land, but we should strongly recommend anxious students to go through books specially dealing with the subject, particularly "the Tragedy and Romance of banking in America," which fully describes the vicissitudes through which American banking has passed ; and how in spite of colossal bank failures and banking crises not only depriving banks of requisite public confidence, but shaking them to their very foundation, the country has through the legal help, safeguards and intervention of its Government (which has from its very early days regarded it amongst its principal duties to promote foundation and growth of its credit institutions on sound basis), evolved and built up bank-

ing organisation which has successfully stood the test of time.

Banking in America as in every other country came to be developed to satisfy credit needs of growing commercial activities and/or the Government financial requirements. And as in most new countries, it had to pass through many crude experiments. Owing to the undeveloped state of the country there was often great demand for credit and/or currency, much more than could be legitimately satisfied by the amount of available specie, and there was great temptation for the banks to create them without adequate reserves. This was further easy of accomplishment because almost all the first banks had right to issue notes, which as already said elsewhere was regarded integral part of early banking. The creation of excessive credit coupled with inexperience and speculative transactions used to lead to the inevitable result of banking collapse and business prostration. This unhealthy state of affairs obliged the American states to introduce legislation to control bank incorporation and bank working. All the states, of course, did not enact their banking laws at the same time nor were they uniform. Thus came into existence what are up to the present day called state banks. Some of the states authorised issue of notes against the state bonds. Again others insisted that the note issuing banks should keep redemption fund at a certain principal bank in the state from which the respective notes were redeemed and sent home for collection. In New York which was becoming the chief Commercial State of the Union, "Safety Fund System," was inaugurated in 1829 which provided that each

bank should contribute towards a fund to meet the deficit of any contributing bank which might fail with assets insufficient to meet its liabilities. The fund was, however, exhausted by important bank failures, which occurred between 1837 and 1857. In some states (Indiana and Ohio) the right of note issue was exclusively conferred on only one bank, as in the case of central banks in Europe.

The notes of state banks were generally not legal tender even in their respective states. Volume and velocity of circulation of any particular notes depended upon the reputation and confidence which the bank enjoyed in the public. The inconvenience occasioned by the state system of note issue was specially noticed when the notes passed from one state to another, as naturally they could not freely circulate in a foreign state owing to the difficulty of ascertaining the responsibility and respectability of their issuers. It was this defect which Mr. Chase, Secretary of the Federal Government's treasury, wanted to principally take advantage of, when trying to satisfy the government financial necessities in the civil war in 1863, by the creation of the national banking system. He practically created a compulsory market for the government bonds, which it was extremely difficult to issue at favourable rates previously, by offering special privileges to banks organised under Federal Charters, which would issue circulating notes throughout the whole union, only when secured by the deposit of government bonds. Further every national bank was required to invest $\frac{1}{3}$ rd of its capital in bonds. The grant of special privileges to the national banks, however, did not bring the system into prominence as some

of the state banks had by that time assumed a very strong position. The Central Government had thereupon to impose a tax of 10 per cent. upon the notes in circulation of the state banks. This drove them out from the note issuing business and some were converted into national banks, while others continued simple commercial banking under the state laws without the privilege of note issue.

The national banking grew in importance and popularity as time passed. On the one hand there was inducement of getting "double interest" * on notes issued, which brought requisite capital for such enterprises and on the other there was a uniform system of bank law for the whole union, regulating incorporation, capital, reserves, examination and other important matters, and certainty of note redemption by the central treasury, which procured public confidence—both factors giving necessary momentum to the whole system. To-day the national banks form the most important group of banks in the United States, predominantly holding commercial banking assets, the other two types, *viz.*, State Banks and Trust Companies giving special attention to the investment institutions of the nation. At the end of 1920 although there were only 8,000 national banks as against a total of 30,000 of national, state, savings, private banks, loan and trust companies, still the business of the former was nearly 45 per cent. of the total, paid-up capital and deposits being 1,248 and 16,752 million dollars respectively as against the totals of 2,702 and 37,683 million dollars.

* By issuing notes against bonds banks gain interest on bonds as well as on the use of money created against their lodgement.

A class of financial institutions known as Trust Companies has grown along with the state and national banks in America. They are constituted under state laws to accomplish financial objects not specially provided for originally under the national banking system. "The function which gives a trust company its name is to execute trusts for individuals, estates and corporations." In the United States, however, these functions have been extended to include many of those of commercial banks, *e.g.*, receiving deposits payable on demand and subject to check or on notice, advancing against stock exchange securities, buying commercial paper, etc. It is unnecessary for the purpose of this book to describe in detail the trustee and agency business of trust companies, or to show how on account of their corporate and continuous existence and other advantages they are more useful than individuals to discharge such functions. Likewise we pass over the circumstances, *e.g.*, less restrictive nature of trust company laws than either of those which governed the operations of national and state banks, which enabled several trust companies to develop their banking business so extensively and successfully that their preliminary or nominal purposes are largely secondary. The national and state banks have felt the competition of Trust Companies keenly in banking matters and to-day all the three form important component parts of commercial banking in the United States.

Laws governing state and national banks and Trust Companies have been amended from time to time and it is beyond the scope of this book to minutely go through all such changes. We shall

briefly give account of the existing laws little later. To pursue the subject of banking development in America, we find that although the institution of national banks was a step in the right direction and created unification of banking methods it was incapable to withstand stress of panics and crises, because there was no provision for emergency measures or emergency currency. The national banks had power to obtain circulating notes against the deposit of Government bonds but as this amount was limited, it did not give necessary relief when such was needed. Thus we had serious bank crises in the years 1893 and 1907. Some relief measures were introduced after the crisis of 1893 but they did not go far. After the panic of 1907 the so-called Aldrich-Vreeland Act (May 30, 1908) was adopted which made provision for the organisation of "national currency associations," which were to be allowed to issue notes against commercial paper or other securities deposited by constituent banks with the association in question. This plan, however, did not come in operation as the difficulties resulting from the panic had been greatly overcome before the Act was passed. Contemporaneously with the above act National Monetary Commission (1908) was appointed to investigate banking and currency problems. This commission did most wonderful work, travelled through all the important countries and critically examined their currency and banking systems, taking statements, views, and evidence of economists, bank officers and bankers. After a number of years of investigation, the commission issued a report of fifty volumes. It contains detailed description of the various banking systems prevalent

in America and Europe and views of eminent authorities as to how far they supplied their banking needs. It is the most valuable contribution to the banking and currency literature. The reform, which was recommended for adoption, contemplated creation of a central banking organisation with branches. The plan retained the fundamental concept of an emergency currency, but the proposed institution was not equipped with the ordinary powers, duties and responsibilities which had been found necessary in central banking experience elsewhere. The bill incorporating recommendations of the N. M. Commission, ordinarily described as the Aldrich bill, however, did not materialise as the Republican party under whose auspices it had been developed was defeated in November 1912. The Democratic party which came into power undertook the responsibility of bank reformation and it produced a measure which afterwards came to be known as the Federal Reserve Act. The Act was passed on December 23, 1913, *i.e.*, practically within a year of the coming into power of the party and the Federal Reserve system actually came into existence by November 16, 1914. Because the bill was rather hastily constructed and quickly completed, apprehensions were raised in many quarters as to its practicability and value. National banks which were compulsorily required to be members of their territorial Federal Reserve banks were wavering for a long time whether to accept the membership and governance of the law or dissolve themselves and reincorporate under the state laws. Other banks also opposed the measure because they feared that great changes and innovations would result in business from the system.

These fears gradually became less and less and the national banks finally unanimously decided to take stock in the new Federal Reserve banks. The state banks and Trust Companies followed suit and although membership was not compulsory in their case, many of them elected to join the system because of the strength and solidarity which they derived from such strong connection. The subsequent working has fully demonstrated the sterling solidness of the system and the imaginary nature of original anxiety. And although various amendments have been made to the Act from time to time the general purpose of the system continues to be the same. An American author has rightly said, "Next to the Declaration of Independence and the constitution of the United States, the Federal Reserve Act, signed by President Wilson on December 23, 1913, may be the most important measure ever placed before the people of these States."

We have explained at the beginning of this section the principle of federation upon which the Federal Reserve system is based. Coming now to the act itself we find that it purposes to separate the central banking functions of the past from the practical bank operation, the latter being carried on through district reserve banks under the general directions of a board vested with the central banking functions of the past. This is brought about by the creation of a number of central institutions called the Reserve banks, each being allotted certain fixed territory. The whole country has been divided into 12 reserve districts and consequently there are 12 Reserve banks. Each district had in 1914 on an average, population 7.4 millions, over 260,000

square miles and 650 member banks. The capital of a reserve bank is compulsorily contributed by the national banks doing business within its territory in the proportion of 6 per cent. of their capital and surplus, half of which is to be paid up at the time of membership and the remainder remains uncalled liability. The state banks and Trust Companies are permitted to be members on the same terms as the national banks. No Federal Reserve bank can commence business unless its paid-up capital is at least \$4,000,000. An essential and fundamental requirement of the Act is the compulsory transfer of cash reserves of the member banks to their respective Federal Reserve banks (*See National Banks*). Out of the 18 per cent. cash Reserve required in respect of demand deposits and 5 per cent. in case of time deposits in the Central reserve cities, $\frac{6}{18}$ ths is to be kept in the vaults of members banks, $\frac{7}{18}$ ths in the Federal Reserve bank and the balance, *i.e.*, $\frac{5}{18}$ ths in the vaults or Federal Reserve bank at the option of the member banks. Of course, there is no objection to the member banks keeping any deposits with the Reserve bank.

The management of each Federal Reserve bank is through a board of directors consisting of nine persons three of whom are appointed by the Federal Reserve Board (explained later) and six are elected by the member banks voting in three separate groups according to the size of their capital. Out of the latter six directors, three represent the banks, and the remaining three consist of persons who at the time of their election are actually engaged in commerce, agriculture or some other industrial pursuit.

The reserve banks are permitted to open branches so as to be fully serviceable to the whole of their respective territories and not confine their influence in the main to the locality of their habitation.

The capital of a reserve bank is only entitled to 6 per cent. annual cumulative dividend, and one half of its net earnings may be paid into a surplus fund until it amounts to 40 per cent. of its paid-up capital. All net earnings over and above this dividend and surplus are paid to the United States as a franchise tax. The U. S. A. Treasury has been receiving large sums every year from this source.

The board of directors of a reserve bank has to work under the final supervision of Federal Reserve Board which is practically the ultimate banking authority in the U. S. A. This board consists of seven persons ; Secretary of the Treasury and Comptroller of the Currency, as *ex-officio* members and five other members appointed by the President of the U. S. A. by and with the consent of the senate. Not more than one member of the board can come from a single reserve district. At least two of the presidential appointees must have had banking or financial experience, but no member of the board may be an officer, director or stock-holder of any bank. The term of office of the members is ten years but a vacancy occurs every two years by rotation. The board is assisted by a body known as the Federal Advisory Committee of 12 members, each Federal Reserve bank nominating one member. As the name implies the functions of this council are merely advisory with regard to all matters connected with banking, *e.g.*, discount rates, reserve conditions, open market powers, etc., and although

the Board is not bound to accept its advice, it always gives best consideration to its opinions. This Council meets once in every quarter.

The Federal Reserve Board is an unusually powerful supervising and regulating body. It has general powers to supervise and examine the accounts, books and affairs of each Federal Reserve bank and of each member bank and to require such statements and reports as it may deem necessary ; it may suspend or remove, for cause, any director or officer of the Federal Reserve banks ; it may suspend the operation of any Federal Reserve bank and liquidate or reorganise such bank ; it defines the paper which may be rediscounted by Federal Reserve banks ; it has power to review and determine the rates of discount established from time to time by the Federal Reserve banks for the discount of commercial paper offered by the member banks ; it has power to permit, or on the vote of at least five members to require Federal Reserve banks to rediscount the discounted paper of other reserve banks at rates of interest determined by it ; it regulates the issue and retirement of Federal Reserve notes ; it regulates the open market powers of the Federal Reserve banks ; it has powers to suspend every reserve requirement of the act if it deems such a course necessary ; and it has many other powers which give it final and effective control over the whole banking system. In short it carries on those functions which Central Banks perform in the regulation of money market and in the co-ordination of financial activities, possessing examining and inspecting powers and authority to bring about any changes that such examination may reveal.

The Federal Reserve banks are independent of each other. They may, however, with the permission of the Federal Reserve Board rediscount between themselves their discounted paper at rates fixed by the board. Whenever necessary they can be compelled to extend rediscounting facilities to any Federal Reserve banks by the affirmative vote of at least five members of the Federal Reserve Board. Banking items between the various Federal Reserve banks are settled through a clearing house.

The functions, powers and responsibilities of the Federal Reserve banks are briefly as under :—

- (i) To keep accounts of member banks and of the Government. They are required to maintain a reserve of 35 per cent. against such deposits.
- (ii) To extend rediscounting facilities to the member banks at the rate of discount fixed by the Federal Reserve Board and upto the limits that may be decided by the board of directors. This facility is only limited to notes, drafts and bills of exchange arising out of actual commercial transactions, having a maturity of not over 90 days, although a limited amount of live-stock paper may have a maturity not exceeding six months. Loans secured by investment security cannot be rediscounted. The spirit of the Act forbids loans for carrying goods in storage for a higher price and confines them to paper based on goods actually sold. This restriction further curbs speculation on the Stock Exchange by withholding re-

discounting facilities from bills drawn in respect of such transactions.

- (iii) To buy and sell bonds and notes of the United States, any state, district or municipality in the States, issued in anticipation of the forthcoming revenues but having maturity of not more than six months.
- (iv) To do open market business like buying and selling cable transfers, bankers' acceptances, commercial bills under rules prescribed by the Federal Reserve Board, etc. This is a valuable provision as in the first place it avoids uneconomic idleness of funds whenever demand for credit on the part of member banks decreases and in the second place it curbs the tendency on their part to unduly raise the cost of credit or to distribute it improperly.
- (v) To issue currency notes. They can issue two kinds of notes. First like the national banks against certain types of bonds which carry note-issuing privilege—in fact they can be compelled to purchase bonds deposited by the national banks with the Currency Department and against which notes have been issued. If the reserve banks want they can redeposit them and issue notes against them; or with certain limitations they can get them converted into other bonds bearing higher rate of interest but without the privilege of note-issue. The difference between the national and

Federal Reserve bank notes, issued against bonds, is that in the former case the amount issued is limited to the capital of the bank whereas no such limitation is prescribed in the case of Federal Reserve banks. The other type of notes which the banks can issue are the Federal Reserve notes against lodgment of rediscounted paper or other collateral like gold or gold certificates. They are required to maintain a reserve of 40 per cent. against such notes in actual circulation. The rediscounted paper or other collateral is deposited with the Federal Reserve Agent (Chairman of the Board of Directors nominated by the Federal Reserve Board from amongst its three appointees on the Board), who has further power to admit or reject any paper according to his discretion and issue notes against the paper finally passed and accepted. These notes, called the Federal Reserve notes, are obligations of the United States Government and legal tender for all purposes. Out of the reserve of 40 per cent., the banks are to maintain a fund of not less than 5 per cent. with the Treasury for the redemption of notes. The Treasury cannot deposit this gold redemption fund with the Reserve banks like the ordinary funds of the Government. The notes are redeemable in gold at the Treasury department in Washington and at every Federal Reserve bank.

The note-issuing powers give the necessary elasticity to the American Currency as well as provide for emergency measures. By permitting rediscount facilities only in the case of commercial paper of not more than three months, expansion of currency is permitted against real economic needs which automatically contract when the periodical demands are satisfied.

- (vi) To work as supervisory body with examining and inspecting powers over its member banks.
- (vii) To work as clearing house and collecting agent for the member banks. If a member bank has certain items to collect all that it has to do is to send them to its reserve bank where they are cleared along with the items drawn upon it submitted by other banks. Through the medium of the reserve bank the member banks can even clear items payable by banks in other districts—because all the reserve banks clear their items through a Central Clearing House at Washington. This restricts the circulation of actual legal tender currency and enables banks to successfully carry on their operations with smaller cash reserves.
- (viii) To fix discount rate for their respective districts subject to the sanction of the Federal Reserve Board.

From the brief account that we have given of the reserve banks it is apparent that they are similar to the European Central banks and discharge more or less similar functions for their respective terri-

tories. In some ways they are more powerful both as a check and unifying influence, *e.g.*, they possess powers of direct examination and control and through the representatives of the member banks and their nominees on the board of directors they are able to come in closer contact. The Federal Reserve Board acts as a co-ordinating, controlling and centralising authority over what may be called provincial central banks. The whole system aims at decentralising central banking and thus avoids concentration of credit in a single body but with sufficient machinery to mobilise their aggregate resources whenever emergencies may arise. In some respects, however, they apparently differ from the European central banks, *e.g.*, they are not open to public business as a rule. But this restriction does not interfere with a reserve bank's toning influence or its authority as the ultimate determinant of the cost of credit in the market, because it has a large number of member banks, which can avail of its credit facilities and thus reduce the price of credit to the competitive level. Moreover, through the open market business the reserve banks are able to exercise healthy influence. In the case of European countries commercial credit is concentrated in the hands of a few commercial banks and if their central banks were not open to public business the few banks would naturally control the whole market and thus nullify the purpose for which central banks mainly exist. Another special thing to be noted is that the European Central Banks have generally first come into existence and then helped the formation and development of general banking but the American reserve banks were created after the

general banking had been sufficiently developed and so to say super-imposed upon the pre-existing system with a view to consolidate, control and strengthen it.

A peculiar feature of the American banking is that branch banking is not permitted as a general rule. "The usual business of each national banking association shall be transacted at an office or banking house located in the place specified in its organisation certificate." * The Americans think that each place should have its own bank just like a town hall or a local municipality. Some state laws permit opening of branches within their territories whereas others permit within the limits of the town where the Head Office is situated. In States where the state banks have power to open branches, the national banks have been feeling unequal competition with the result that many of them have been driven out of existence or compelled to relinquish their national charters and to re-incorporate under the state laws. This question has been very often discussed in the American banking circles as well as in the American press but the concensus of opinion still continues to be against branch banking which is regarded, "to be against public policy, violating the basic principles of 'our' government and concentrating the credit of the nation and the power of money in the hands of a few." Under certain conditions banks are permitted to open branches in foreign countries for the purpose of transacting exchange business dealing with the finance of imports and exports.

Another important characteristic is the legislative control over the banking system.

* National Bank Laws.

We have already remarked elsewhere that the American banking would not have achieved the progress that it has obtained had it not been for the State intervention by enacting measures calculated to inspire confidence and foster banking as a whole. From the brief account of laws governing national and state banks and Trust Companies given little later and of the constitution of Federal Reserve banks given already, it will be seen that the Government control is exercised in a few important directions, such as : (i) Minimum amount of Capital depending upon the field of operation which must be subscribed before a bank can be incorporated ; (ii) Reserves to be built up ; (iii) Restrictions on directors ; (iv) Cash reserves to be maintained ; (v) Limits on the nature and maximum amount to be advanced to each individual person, corporation or firm ; (vi) Restrictions on investments and/or advances against immoveable properties excepting under certain conditions ; (vii) Power of periodical examination by the Government officers ; (viii) Publicity of accounts, etc.

These legislative and administrative limitations or safeguards can all be justified upon grounds of public policy. The natural tendency of banking like other economic undertakings is towards earning greater profits which not unoften makes the management lose sight of its primary responsibility to the depositors whose monies they hold in trust. Howsoever greatly the management may be honest and conscious of sound banking principles, the law of marginal utility as well as forces of competition not unoften induce them to take risks which although liquidated many a time contain germs of insecurity

or are alien to banking proper. Things go on in this manner daily approaching nearer and nearer to the danger zone when all of a sudden one morning the management decides to close the bank's doors. Apart from the bank failures due to dishonesty and fraud on the part of bank authorities, instances are not wanting in the banking history where concerns started with honest motives have been obliged to stop business. One bank failure leads to another and so on until the whole system gets a rude shock. Even the strongest of them do not come out unscathed. And as the stability of credit institutions is of vital importance to the whole economic structure is it not best to devise measures which will ensure that stability? It may not be necessary to have recourse to legislative and administrative enactments in European countries where banking is concentrated in a few institutions, which have large past experience and traditions to guide them, whose business dimensions are very vast, where the area to be administered is not large and the public is conversant with banking habits. But in new countries with undeveloped economic resources and large areas to serve, the legislative measures are most essential. And again what are these banking laws? They are nothing but banking experience codified. Ordinarily banks working on safe principles would observe them of their own accord. And what is wrong if the observance of such principles based on wide and varied experience is imposed on all banks, by law?

To complete the description of American banking we give below rough outline of the laws governing the three types of commercial banks. America possesses agricultural, land mortgage, and other

types of banks to discharge credit functions peculiar to them but we shall not describe them here but may refer to their constitution in later chapters wherever necessary.

NATIONAL BANK LAWS

CAPITAL AND SHAREHOLDERS' LIABILITY

The amount of Capital which a bank should have before getting incorporation certificate is governed by the following table :

In cities having population of—

| | | | | Minimum Capital Dollars. |
|---------------|--------|--------|-----|-----------------------------|
| not more than | 3,000 | ... | ... | 25,000 |
| „ | „ | 6,000 | ... | 50,000 |
| „ | „ | 50,000 | ... | 100,000 |
| more than | 50,000 | ... | ... | 200,000 |

At least half of the above capital should be paid in before a bank is authorised to commence business. The remainder should be paid up within five months of such date of authorisation in instalments of not less than 10 per cent. of the whole amount of the capital. Payment of each such instalment is to be certified to the Comptroller under oath by the president or cashier of the bank.

“The stock-holders of every national banking association shall be held individually responsible for all contracts, debts and engagements of such association each to the amount of his stock therein, at the face-value thereof in addition to the amount invested in such stock.”

INCORPORATION

The Comptroller instructs the examiner of the district, in which the bank wishes to start business, to enquire into the local need and determine the

possibility of its success. He consults the Federal Reserve bank of the district. And if the reports are favourable he agrees to issue incorporation certificate after all the necessary preliminaries are satisfied.

As soon as a national bank is incorporated it is required to be a member of the district's Federal Reserve bank. The former obligation of owning a certain amount of Government bonds was replaced by the membership obligation on the passing of the Federal Reserve Act.

DIRECTORS

The necessary restrictions and qualifications concerning directors are :

1. Every director during the whole time of service must be a citizen of the United States.

2. At least three-fourths of the directors must have resided in the State, Territory or District in which the bank is located for at least one year immediately preceding their election and should continue to reside therein during the period of office.

3. Every director must own in his name at least 10 or 5 shares of the Capital Stock according as the Capital exceeds or does not exceed \$25,000. As soon as he ceases to hold this much stock he ceases to be a director.

4. Directors hold office for one year and are elected by shareholders in the Annual Meeting which is required to take place on such a day in January as is specified in the Articles of Association.

5. The minimum number of directors should be five. No maximum limit is prescribed.

6. No director (or other officer or employee) of a national bank or Edge Corporation* having resources aggregating more than \$5,000,000 can legally serve at the same time as a director (officer or employee) of any other national bank or Edge Corporation regardless of its location.

7. No person who is a director in a state bank or Trust Company having resources aggregating more than \$5,000,000, or who is a private banker having resources aggregating more than \$5,000,000, can legally serve at the same time as director of any national bank or Edge Corporation, regardless of its location.

8. No person can legally be a director, officer or employee of a national bank or Edge Corporation located in a city of more than 200,000 inhabitants who is at the same time a private banker in the same city or a director, officer, or employee of any other bank (state or national) located in the same city, regardless of the size of such bank.

Items 5, 6 and 7 are considerably modified by the Kern Amendment (1916) the principal provisions of which are :

9. By permission of the Federal Reserve Board, any private banker or any officer or employee of any member bank or class (A) director of the Federal Reserve bank may serve as director, officer or employee of not more than two banks, banking associations or Trust Companies coming within the

* Corporations created under the Edge Act for the purpose of financing American imports and exports. The Edge Act is an amendment to section 25 of the Federal Reserve Act, and governs activities of American banks doing foreign exchange business.

prohibitions of the Clayton Act,* provided such other banks are not in substantial competition with such private banker or member bank.

10. The Federal Reserve Board may give or withhold consent and may define what constitutes substantial competition. If the institutions are in substantial competition the Board must refuse consent.

11. If the Federal Reserve Board gives its consent, it issues to the applicant a formal certificate which continues its permission until revoked. Permits may be revoked at any time.

12. With the approval of the Federal Reserve Board, a director, officer, or employee of a national bank may assume an office under a bank constituted for the purpose of foreign banking provided the national bank holds stock in such a bank.

DISTRIBUTION OF PROFITS

Usually banks issue their stock at a premium so as to start with some reserve. Where this is not the case the Comptroller of Currency may direct that no profits should be distributed as dividend unless a substantial reserve has been built up. Apart from this discretionary power vested in the Comptroller the act lays down: "Each association shall before the declaration of a semi-annual dividend carry one-tenth part of its net profits of the preceding half-year to its surplus fund until the same shall amount to twenty *per centum* of its capital stock." (National Bank Act, June 3, 1864).

* As a result of agitation against trusts and combines, America passed in 1914 the Clayton Anti-trust Act with the object of preventing wealthy people or their nominees from becoming directors of more than one bank and thus acquiring large controlling hand in the credit policy of the country.

CASH RESERVES

For the purpose of Cash Reserves the National banks are divided into three classes: (A) Banks in Central Reserve Cities—New York, Chicago and St. Louis. (B) Banks in Reserve Cities confined to about fifty of the larger cities of the country. (C) Country banks, *i.e.*, the remaining banks.

The cash reserve requirements vary with the class of the banks and are as under:—

- (i) A bank of class (A) is required to hold and maintain a reserve made up of at least 18 per cent. of its demand deposits (*i.e.*, payable on less than 30 days' notice) and 5 per cent. of its time deposits— $\frac{6}{18}$ ths of this must remain in its vaults, $\frac{7}{18}$ ths in its Federal Reserve bank and the balance in its vault or in the reserve bank as it pleases.
- (ii) A bank of class (B) is required to hold and maintain a reserve made up of at least 15 per cent. of its demand deposits and 5 per cent. of its time deposits— $\frac{5}{15}$ ths of this must remain in its vaults, $\frac{6}{15}$ ths in the Federal Reserve bank and the balance either in its vaults or in the reserve bank.
- (iii) A bank of class (C) is required to hold and maintain a reserve made up of at least 12 per cent. of its demand deposits and 5 per cent. of its time deposits— $\frac{4}{14}$ ths of this must remain in its vaults, $\frac{5}{12}$ ths in the Federal Reserve bank and the balance either in its vaults or in the reserve bank.

In estimating reserve requirements the net balance of inter-bank balances is taken into consideration. If at any time the cash reserve falls below the legal requirements the bank concerned is required not to make any new advances or declare any dividends. If the deficiency is not made up within 30 days, the Comptroller may with the concurrence of the Secretary of the Treasury appoint a receiver to wind up the business of the bank. The Federal Reserve Board has power to suspend reserve requirements for a period not exceeding 30 days and from time to time to renew such suspension for periods not exceeding fifteen days, provided that it shall establish a graduated tax upon the amount of the cash reserve deficiency.

LOANS

The following limitations are imposed upon advances made by national banks.

(1) No national bank shall advance a sum greater than 10 per cent. of its unimpaired Capital and surplus or 30 per cent. of its Capital, whichever is less, to any single individual, or a single company, corporation or firm or to any company and its several members. For the purpose of determining this limit the bills of exchange drawn in good faith against existing values or owned by the borrower and discounted shall not be considered as money advanced.

(2) No national bank shall advance against its own shares or be purchaser thereof unless it be necessary to prevent loss upon a debt previously contracted in good faith ; but in such an event it shall be required to sell it within six months from the date of purchase, failing which a receiver may be appointed to close up its business.

(3) It shall not be lawful for a national bank to purchase, hold and convey real estate excepting in the following cases :—

- (a) When the possession of real estate is necessary for its immediate accommodation in the transaction of its business.
- (b) When it is mortgaged or conveyed to it or purchased by it in satisfaction of debts previously contracted in good faith, or in satisfaction of decrees obtained, to avoid loss. Possession of such real estate whether under mortgage or under purchase to secure any debts shall not be held for a period longer than five years.
- (c) A national bank not situated in a Central Reserve City may make loans secured by improved and unencumbered farmland situated within its Federal reserve district, but no such loan shall be made for a period longer than five years nor for an amount exceeding fifty per cent. of the value of the property—provided the total of such advances on its books does not exceed 25 per cent. of its Capital and Surplus or $\frac{1}{3}$ rd of its time deposits, whichever is less.

GOVERNMENT CONTROL

We have already mentioned elsewhere that the national banks are subjected to the supervision and examination of the Federal Reserve banks and the Federal Reserve Board. Apart from this control, the U. S. A. Government through the Treasury Department exercises direct powers of inspection and super-

intendence. A special Bureau of the Treasury Department, in charge of an officer known as the Comptroller of Currency, is entrusted to watch that all laws and regulations relating to currency and banking are properly observed. The duties and responsibilities of this officer are briefly as under :--

(i) To grant certificate of incorporation and certificate to commence business after the receipt of favourable initial reports and when all the necessary preliminaries are complied with ;

(ii) To receive and examine all returns which banks are required to submit according to Law ;

(iii) To see that the banks observe all the laws governing their work and with this view :

(a) to appoint, with the approval of the Secretary of the Treasury, examiners who shall examine every member bank at least twice each calendar year and oftener if considered necessary, the examiners enjoying all powers to carry on thorough examination, to administer oaths and to examine any of the bank officers and agents under oath ;

(b) to require every member bank to submit within five days of receipt of such requisition, not less than five reports during each and every year, which reports shall exhibit in detail and under appropriate heads the resources and liabilities of the association at

the close of business on any past day specified by him ;

(c) to call for special reports from any particular association whenever in his judgment the same shall be necessary ; and

(d) to impose a penalty of one hundred dollars for each day, after the stipulated period of five days, upon any association that may fail to make and transmit reports required under (b) and (c) above.

(iv) To make annual report to Congress giving a summary of the conditions of every national bank together with such special information as may be regarded of importance, whether in connection with national or state banks.

STATE BANK LAWS

Unlike the national banks these regulations are not uniform but vary greatly from state to state. To attempt to refer to the banking laws of all the states would be a task beyond the scope of this book. We note below the broad features :

(i) The capital requirements are so varied that in some states they are not insisted upon whereas in others lower limits are prescribed, *e.g.*, as compared with the national bank requirement of \$50,000 for places of 3,000 to 25,000 population, over three-fourths of the states which prescribe a fixed capital have lower requirements but none of them more. Similarly

some of the states show lack of banking ideals in permitting an authorised capital larger than the paid-in requirements, undue prolongation of the paying in capital and the payment of subscriptions to capital in things other than cash. Most states follow the national bank act in providing for the double liability of shareholders, but there are others whose laws greatly differ in this respect also.

- (ii) As regards surplus requirements, about 20 states follow the national bank act, some have more stringent provisions, some have lower requirements but there are several states which do not insist on surplus accumulation by general law.
- (iii) With reference to the cash reserve requirements the same range of diverse legislation is observed. There are about a dozen states only which follow the national bank act in this respect. Others either insist on much lower limits or do not require any reserve whatever. The difference also is noticeable in the form of reserve, *e.g.*, all states permit balances in other banks to be counted as part of the reserve, the amount of re-deposits so authorised varying from one-half to three-fourths.
- (iv) As regards restrictions on loans, the state laws are in general more liberal than the national bank law. There are only two states which follow the national bank law in this respect, about 25 states

permit 15 to 30 per cent. of Capital and Surplus as the limit to each individual liability to a bank and several others prescribe no limitation whatsoever. In the matter of loans against real estate, state laws are similarly more liberal. The prevailing practice is to limit these loans to 50 per cent. of the Capital and Surplus. A few states permit such advances from 15 to 40 per cent. of the assets and some even up to 20 per cent. of the loans. The laws usually define the character of such security as regards location of property, and the amount of loan in relation to the value of the asset. Holdings are generally limited to a five-year duration following a foreclosure sale.

- (v) Regulations concerning incorporation, directors, deposit of state bonds at the time of incorporation and other relevant matters are often prescribed.
- (vi) Each state has a Superintendent of Banks who is responsible for seeing that the state banks observe the laws concerning them. Like the Comptroller of Currency he appoints examiners to examine periodically affairs of the state banks, issues certificate of incorporation, etc. He is appointed by the Governor of the State by and with the advice and consent of the senate of the State Legislature.
- (vii) Whenever a state bank is permitted to be a member of the Federal Reserve bank

it comes under the control of the Federal Reserve Act and the Federal Reserve Board, and is required to observe all regulations to which the national banks are subjected. Federal Reserve Board, however, may accept examination reports of the state examiners without insisting upon examination by the Treasury examiners. They, however, possess the sole power to withdraw this facility and can subject the member state banks to any sort of examinations.

TRUST COMPANIES LAWS

These laws are the creation of states and greatly resemble the state bank laws. Formalities as regards incorporation, supervision of Superintendent of Banks and similar matters are practically identical. Laws concerning both these institutions are tending to become assimilated. There are, however, certain important differences. They are :

- (i) Usually the Capital requirements in the case of trust companies are larger than in the case of state banks. Similarly stricter regulations govern the provision for paying-in capital before commencing business. The deposit in bonds is required to a much bigger figure in the case of trust companies.
- (ii) The reserve requirements for trust companies are much less than for state banks. This is probably due to the different character of trust company deposits, which are largely inactive and contain

only a small portion which are liable to sudden or large withdrawals.

- (iii) Similarly trust companies are less restricted in the matter of advances.
- (iv) The trust companies are distinctly authorised to accept trusts and to do safe-deposit business in addition to general banking. If a state bank wants to do same sort of business it should deposit the same sort and the same amount of security as the trust company having similar capital.
- (v) The trust companies like the state banks come under the governance of Federal laws as soon as they elect and are permitted to be members of their respective Federal Reserve banks.

CHAPTER VI

ISSUES

Whether Government administrative organisation to watch and examine banking activities is necessary—What form should the central banking institution take—Whether special banking legislation necessary—*Re.* formation and constitution of special banks—Whether municipal and local bodies should do banking business ; if so, whether under any restrictions—*Re.* private efforts.

We have given in previous chapters deficiencies in the present banking organization of India, if at all we can use this expression in connection with this haphazard growth, and also some description of the similar systems in other countries. There are definite issues which present themselves and answers to them will constitute the basis of our scheme of construction. In framing these issues we assume that our new banking system should be self-contained and adequate as fully dwelt upon in the fourth chapter.

The main issues are :—

- (i) Whether there is necessity for special administrative organization on the part of the Government to watch and examine banking activities ; and if so, whether such work should be done by the Central Government or by the Provincial Governments or partly by one and partly by the others ?
- (ii) What form should the central banking institution take ? Should it be similar

to the central banks of Europe or resemble the Federal Reserve banks of U.S.A.; or be a new type altogether but containing features necessary to the discharge of central banking duties? Should this institution be solely state-owned and state-managed like the State Banks or a private corporation sharing its profits with the State and under sufficient control of the Government so as to ensure safety of public interests?

- (iii) Whether there should be special banking legislation to control incorporation and activities of joint stock commercial banks and of the branches of foreign banks in this country?
- (iv) Whether the formation of special types of banks like the agricultural banks, land mortgage banks, industrial banks, exchange banks, etc. should be left to private enterprise, under laws governing joint stock banks and joint stock companies or special measures promising State support and facilities at the central banking institution are necessary?
- (v) Whether Municipalities and other local bodies should be permitted to do banking and if so whether their business should be restricted to any particular type or types?
- (vi) Whether private co-operation on the part of banks, banking propaganda on the part of public bodies and Government and similar measures calcu-

lated to promote growth and inspire confidence, in addition to the legislative enactments that may be considered desirable, are necessary ?

Our answers to the above propositions are as under. They will be elaborated and worked out in the subsequent chapters.

I.—Government Administrative Organization.

Banking History of other countries clearly demonstrates that a vast country like India labouring under economic and banking domination of non-Indians and lacking in corporate activities can hardly be expected to develop her banking system without definite guidance and watchfulness on the part of her government. Government control and examination will impart that healthy tone to the system as well as inspire public confidence which will greatly accelerate formation of banks. The Indian Government's connection with the Imperial Bank has inspired a good deal of confidence in that institution although its working is not subjected to the government examination. Would not such certification on the part of the Government allay public fears against bank failures and lead to increased banking habits and banking activities ? It is further necessary that this work of supervision should be concentrated in the beginning in the hands of one single controlling authority like the Central Government which will further result in the establishment of uniform practices. The establishment of right sort of traditions through the superintendence of one body is of very great importance. In course of time when banking has advanced it may be advisable

to permit provincial incorporations and provincial control. But in the beginning no such arrangement is advisable as it would lead to varying laws and practices. Delegation for administrative economies may be permissible but the real responsibility should rest with the Central Government.

II.—Central Banking Institution.

The Federal Reserve system of the United States represents a model to be attained by large countries in course of time. It is not possible for us to take advantage of this system because it pre-supposes existence of banking activities on a sufficient scale which is not the case here. We think a central bank will be able to control currency and credit conditions much better. There is a great necessity for a single bank of issue to help other banks by giving rediscounting and other facilities. In ordinary times its discount rate would be more unfavourable than that of the commercial banks and as such it would not compete with them. Moreover, it would not allow interest on deposits and thus not interfere with the deposit business of other banks. But it should not be restricted from doing business with any class of people, provided it is within its constitution and otherwise safe; or, if such free permission for doing banking business with public be considered undesirable in the interests of advancement of banking in general, and it be thought necessary to restrict its dealings with banks alone, some enabling provisions, whereby it could enter the general market, when other banks combined to raise price of credit or to distribute it improperly, should be inserted in its charter. The bank should have branches but

they should be restricted to big cities and capitals of different provinces. In course of time when banking has multiplied, decentralization should take place, converting the bank's business in each province into a sort of a reserve bank, all the provincial reserve banks thus formed being federated under one single controlling board. The nature and functions of such reserve banks as well as of the controlling board should be considered when that stage is reached.

The bank should undertake distinct obligations to extend special facilities to the Indian banks and see that they are not over-powered by the foreign banks. It should undertake to supply monetary assistance within fixed limits to special banks like the Indian exchange banks, industrial banks, agricultural and land mortgage banks &c. If necessary, it should be permitted to take up part of capital in such special banks.

As regards the issue whether such a bank should be owned by the State we have given sufficient arguments in a preceding chapter against such institutions and we therefore propose that it should be a private corporation, with predominance of Indian interests in matters like capital, control and management, but the State should have sufficient voice in its affairs to safeguard public interests. Profits of the bank should be shared with the State, dividends to shareholders being restricted within certain limits.

III.—Banking Laws.

There are no specific laws governing corporate banking in this country. The Indian Companies

Act, of 1913 controls them in common with other joint stock companies. Only a few sections of the Act, *e.g.* 133, 136, 145, etc. have any special bearing on joint stock banking. They, however, do not impose observance of any fundamental principles relating to banking transactions but simply require a few formalities to be observed in the matter of preparation of the balance sheet and the form in which statement of affairs is to be published twice a year and exhibited for the information of general public. Moreover, section 277 relating to foreign joint stock companies, including foreign banks, carrying on business in India, is lax and does not subject them to the observance of the same formalities as are imposed upon the Indian companies, *e.g.* clause (3) of the same section requires such a company to lodge balance sheet as required by the law of the country in which it is registered. If that law be less rigid than the Indian law such a company will have advantage over Indian companies. Is it fair that the banks of this country should be required to give certain amount of information which is not insisted upon in the case of foreign banks, if the laws under which they are incorporated do not demand such publication?

Section 138 of the Companies Act gives power to the Local Government to appoint inspectors to investigate affairs of joint stock companies under certain circumstances. The Registrar of Joint Stock Companies has power to call for any additional information over and above what is contained in the returns prescribed by the Act to be submitted to him. But they are so weak

and hedged by such limitations that they are of practically no value—there are hardly any instances in which advantage of such a power has been taken. For all practical purposes we may assume that the Government has no power to examine or inspect affairs of joint stock companies including joint stock banks.

As already demonstrated in the last chapter it is of fundamental importance in the interests of public policy that separate legislation should be enacted to control the banking activities. A bank failure although it may relate to a small insignificant bank is sure to disturb the whole system. Often it brings about failure of others that may be otherwise solvent. The destructive force gains momentum with each failure and ultimately there comes a banking crisis which results in the dislocation of trade and other activities, involves losses and failures of many business concerns and deprives many of their hard-earned savings. Such occurrences are surely against public welfare. State control will enforce working on right principles and curb tendencies for dissipation of public funds.

Institution of a special bank law governing corporate banking is thus necessary in India. We are having so many legislative enactments on various subjects in the interests of general well-being that it is difficult to imagine any real opposition, unless it be from vested interests, against the introduction of this wholesome measure. Bank failures not only retard banking progress, which as already shown is of fundamental importance for economic advancement, but also lead to business prostration and human misery—evils which sap

the very foundation of civic life and which it should be the duty of every civilised government to combat in advance by preventive measures. And what is this banking legislation? It is nothing but experience of other successful institutions put into legal shape for the governance and guidance of those who are entering newly in the field of corporate banking, to minimise their deficiencies in knowledge and experience, and to restrict bank failures by preventive methods and advance control;—and even if in spite of such safeguards, a disturbing situation, due to a combination of unforeseen and adverse circumstances, does arise, where banks are in difficulties, to minimise the disturbance, and by emergency provisions to restore the banking equilibrium within the shortest possible time. If such a law had been in existence in the past not only many of the Indian bank failures would have been avoided but our banks would have been in a much better and stronger position.

If imposition of legal obligations on Indian banks is considered necessary in public interests, it is but natural that foreign banks should be subjected to its governance also. There should be also other modifications in their case, *e.g.* the levy of capital tax, income-tax arrangement, turn-over tax, etc. which countries like France, Spain, Italy, etc. enforce in the interests of their own banks.

IV.—Special types of Banks.

Special sections should be introduced in the proposed Indian Bank Act dealing with the special nature of business of these special banks and the limitations considered desirable. There would thus

be no objection to any private enterprise in these directions. But a good deal of stimulant would be given and very useful purpose served if special institutions of each type are incorporated under special charters, enjoying special facilities at the Central Bank. Indian interests should, of course, dominate in such constitutions. Also because of the special privileges, their profits should be shared with the State, with certain limitations. It should be their concern to expand their activities by bringing into existence banks of their type under the ordinary banking law, making any arrangements with them that circumstances and the special nature of their business may warrant. History of other countries suggests this mode of organization to be the best.

V.—Municipal and Local Board Banks.

Any efforts that can accelerate banking progress should naturally be welcome. In Germany and other countries in Europe, local public bodies are permitted to do savings bank business to assist in the accumulation of mass savings. Their chief investment consists of Government and other trust securities. Public bodies like municipalities and local boards which work under government control, both as regards their administration and banking activities, should be able to win public confidence. Objection to municipal banking chiefly consists of temptation to them or tendency on their part to invest their deposits in their capital works or utilize them as long term advances. Also it is argued that they do not possess any business capacities to carry on such work. England is against municipal banking mainly on these grounds.

But sufficient precautions can be taken to see that they do not lock up their banking funds in long term loans or largely invest them in their works. Also strict limitations on the nature of their advances may be enforced *e.g.* they may not be permitted to invest in commercial bills, etc. Their chief investment may be made in trust securities. Business with such limitations does not require any high degree of business capacities. Of course, certain percentage will have to be allowed to be used by them as capital loans for works of public utility. But such borrowings should form a small portion. Government examination will naturally enforce observance of all laws concerning such banking work. Post Office Savings Bank should continue side by side. Both will work in the same directions, supplementing each other's efforts. Like the Municipal Bank of Birmingham, the municipal banks can fix their business hours in the morning and in the evening to suit the labouring and service classes.

VI.—Private Efforts.

No enterprise of any description, however greatly beneficial, can achieve the expected results unless its aims, objects and utilities are adequately popularised. Propaganda work is very essential. Also bankers should realize that they do not advance their interests, whether individual or mutual, by remaining aloof or maligning each other. Co-operation between them for the purpose of mutual interests, establishing banking practices, prescribing tests for banking staff, advancing common interests and for such other purposes is very desirable.

CHAPTER VII

GOVERNMENT CONTROL

Banking section in the Finance Department of the Government of India—Comptroller of Banks : his functions and powers—Banking Council : its powers and duties—Bank Examiners: their work, scope of duties, and functions.

Under the finance department of the Government of India there should be created a new sub-department which should undertake the responsibility for banking matters and control. It should be in charge of an officer of the same grade as a Secretary of the Government of India who should be independent of the Finance Secretary and directly responsible to the Finance Member. He may be designated as Comptroller of Banks. For obvious reasons this post should not necessarily be filled in from amongst the government civilian officers but the best man available with sufficient experience of banking business should occupy it. When a body of examiners, referred to later, has come into being and gained experience of the duties and responsibilities of the banking section of the finance department, the post of Comptroller may be thrown open to them, but the final choice for such a responsible office should not be restricted to any particular class but left free to the judgment of the Governor-General-in-Council, acting with the advice and consent of the Banking Council (*See below.*) The Banking Council should nominate three persons for this post

and the Governor-General-in-Council should select one out of them. In case, however, it should happen that he does not approve of the nominees of the Banking Council, he should have right to return the nomination paper thrice; but if the same be returned unamended each time, he should either make the choice from the three persons named or submit the question of appointment to the Legislative Assembly whose decision should be final.

Under the Comptroller there should be two Joint Deputy Comptrollers at least one of whom should be an Indian. Appointments to such posts should be in the hands of the Banking Council.

The Comptroller should be assisted in his work by Bank Examiners. There should be two Joint Bank Examiners for each province under whom there should be assistant examiners. The Joint Bank Examiners should be selected by the Banking Council. The number of assistant examining officers would vary from province to province and depend upon the number of banking institutions and the volume of banking business in each province. In the beginning all these posts should be filled from persons having banking experience, but afterwards by advertisement as well as by departmental promotion. If considered advisable an all India Bank Service may be started. Appointments to this service should be by open competitive examination in India, and the probationers should work two years in the bank of issue, two years in any commercial or other banks and one year in the department, before being entrusted with independent inspecting and examin-

ing authority. Arrangements for such practical work should naturally be made by the Comptroller and the banks should be bound by law to admit such apprentices to their banks for practical work, provided it does not involve financial obligation on their part more than they are willing to bear—the balance should, of course, be borne by the State. At least one out of the two Joint Bank Examiners should be an Indian. In course of time the appointments of assistant examiners should be solely made from Indians. Apart from the fundamental question that the activities of the country should be conducted by her people, there is very great advantage of practical value in recruiting such officers from Indians. One of the most important items of bank examination is to value assets, which implies verification of credit information; and only people of this country, on account of their social habits, connections, and opportunities can discharge such responsibilities satisfactorily. The question of grade and emoluments of the bank examiners is a matter of detail but at any rate, a Joint Bank Examiner should not have a lower status or less salary than that of a Collector or Deputy Commissioner.

COMPTROLLER OF BANKS

The functions of the Comptroller of Banks should be briefly as under:—

- (i) To issue certificate of incorporation (*see banking laws.*)
- (ii) To issue certificate to commence business.
- (iii) To see that all laws relating to corporate banking as well as charters issued in

respect of special banks are properly observed.

- (iv) To receive returns, statements of accounts, and balance sheets as may be prescribed, from all banks.
- (v) To receive examination reports from Bank Examiners.
- (vi) To demand any explanations, directly or through the examiners, from the banks concerned, as may be necessary, either in respect of their returns or examination reports.
- (vii) To make or arrange surprise inspection visits to banks.
- (viii) To call for any statements from any bank on any day.
- (ix) To take evidence of any bank official or any other person on oath whenever he may deem it necessary, *i.e.* he should enjoy judicial powers as regards summons, etc. in this respect.
- (x) To impose any penalties that may be prescribed for the non-observance of any banking laws.
- (xi) To prepare annual report on banking business and activities for the public information.
- (xii) To prepare banking statistics.
- (xiii) To send circulars to banks whenever necessary with a view to ascertain their views on problems connected with their work or to draw their attention to any matters of importance.

- (xiv) To convene meetings of Banking Council every quarter or oftener whenever necessary, to place all important information before it and to discuss with it all important matters.
- (xv) To arrange for special facilities and/or assistance in the case of banks that may be in difficulties, either with the bank of issue or with any other bank, wherever possible and desirable, provided such a course is considered in the public interests by the Banking Council.
- (xvi) To arrange for amalgamation of defaulting or weak banks, whenever possible, with the advice and consent of the Banking Council.
- (xvii) To arrange for liquidation of banks as may have continuously failed to observe the banking laws and/or be in financial embarrassment, wherever such an action is approved by $\frac{3}{4}$ ths of the members of the Banking Council.
- (xviii) To grant license for amalgamation of two or more banks as may have applied for the same.
- (xix) To grant license to foreign banks to do banking business.
- (xx) To administer the "Bank *Security Fund."
- (xxi) To administer the "Bank Relief *Fund," under the directions of the Banking Council.

- (xxii) To arrange for clearing houses wherever deemed necessary.
- (xxiii) To be the administrative and executive head of the government banking staff and to make any transfers in the examiners as he may consider necessary.
- (xxiv) To look after banking development and in general to be responsible to the Government and the Indian Legislature for the general satisfactory condition and working of banks.

BANKING COUNCIL

We have referred to the Banking Council above. This should be an advisory body with controlling hand in certain matters, which should guide the Comptroller of Banks. The Council should consist of twelve members. The Finance Member, the Comptroller of Banks and the General Manager of the bank of issue should be *ex-officio* members. The Central Legislature should elect three members. At least two of these three members should be persons unconnected with the Government or the Central or Provincial Legislature. The banks registered under the Bank Law should also elect three members, voting according to the scale referred to therein. At least one out of the three members should be a person unconnected as officer or director with any bank. One member may be elected by banks established under special charters, each having one vote—excluding of course the bank of issue which will be represented by its principal officer. The remaining two members should be nominated by the Governor-General-in-Council to level up any inequalities in representa-

tion of fundamental interests of the country *e.g.* agriculture, industry, commerce, etc. The term of office of members should be three years, but three out of the nine ordinary members should retire every year by rotation. They should, however, be eligible for re-election. This provision would enable to keep up the continuity of work and policy and at the same time give chance to the representation of all interests. The Finance Member should be President and the Comptroller Secretary, of the Council.

Their responsibilities should be more or less in the following directions.

- (i) To advise banks in general and the bank of issue in particular on matters of general interest, like rate of discount, control and distribution of credit, etc.
- (ii) To consider all matters where public may elect to make representation against decision of the Comptroller on subjects within his power and competence.
- (iii) To decide action in respect of defaulting, disobedient (not obeying laws) and tottering banks.
- (iv) To determine when reserve requirements in respect of notes and cash balances may be modified or waived.
- (v) To be supervisory, advisory, regulatory and co-ordinating body for banking as a whole.
- (vi) To sanction any emergency banking measure with the approval of the Governor-General-in-Council for a period of not more than 15 days with power to

renew it with his sanction for seven days at a time, but not for more than a total of 2 months from the beginning, within which period the measure should be passed by the Central Legislature—no such measure should, however, come into operation unless it is passed by three-fourths of the Council's members present in the meeting.

BANK EXAMINERS

The Bank Examiners as the name implies would primarily audit, examine and inspect bank accounts, books and working. By being in continuous touch with the same locality they shall be able to use their local knowledge in assessing accounts at their proper value. Their responsibilities would be briefly of the following nature :—

- (i) To examine applications for incorporation, amalgamation and bank license in the first instance and advise the Comptroller in these respects.
- (ii) To receive in the first instance all returns from banks meant for the Comptroller and submit them with their remarks to the Comptroller.
- (iii) To ascertain by actual audit that banking laws are being observed and to bring any glaring irregularities, whether in the non-observance of laws, violation of fundamental principles of banking or in the system of accounting, to the notice of the management or the bank's board of directors in the first instance,

if considered advisable, and submit such explanations in their report to the Comptroller. Such examination should take place at least once in every year.

- (iv) To take evidence of bank clerks, officers, directors, clients, and others able to materially assist them in their work, on oath and to prosecute them for perjury in case of false evidence.
- (v) To summon books, vouchers, documents, etc. from any one, when and where such requisition may be considered necessary. Where such material cannot be spared for transmission to them, they or their representatives should have right to inspect it.
- (vi) To requisition services of any public servant for consultation in their work *e.g.* in determining legal points, valuation of property, machinery and other assets requiring technical knowledge etc. Remuneration for such services, if necessary, should be determined by the Examiners according to the banking capacity of the institution concerned. As the examination is conducted in the interests of public policy and every public servant is expected to work for such ends, remuneration may not be allowed where circumstances do not warrant.
- (vii) To engage services of any private agency to assist them in points requiring special knowledge, on terms as may be considered

necessary, authorizing payment for such work by the bank or banks concerned.

- (viii) To bring to the notice of the Comptroller any instances which may require special action or deliberation of the Banking Council.
- (ix) To report to the Comptroller general condition and progress of banking institutions, banking business and other connected activities in their territory as well as to advise him on matters of importance.
- (x) To be *ex-officio* members of the bank of issue's Advisory Committee for the province—it would be sufficient if only one out of the two, the senior Joint Examiner, becomes the member.
- (xi) In short to represent the Comptroller in all matters as may be delegated to them.
- (xii) To keep all matters that may come to their knowledge, while in the exercise of public office, secret and confidential, violation of which should be punishable by the Banking Council departmentally, or by a Criminal Court, if the Council so decides.

CHAPTER VIII

CENTRAL BANK

Whether Imperial Bank of India can be suitably transformed into Central Bank—Compensation to the Imperial Bank for loss of Government banking business—Special charter for incorporating bank of issue—Period of charter—Capital—Shares—Votes and Meetings—Directors—Branches—Management—Local Advisory Committees—Business : Deposits, Investments, Agency, Internal Rupee transfers—Currency functions—Profits—General : Clearing Houses, Safe custody, Audit and Examination, Discount rate, Weekly statement, Balance Sheet, Taxes, Other responsibilities, Liquidation, Staff, Miscellaneous.

When considering the constitution of this institution an important problem presents itself *viz* : should the Imperial Bank of India be remodelled to work as the country's central bank or should it be a new formation? The Hilton Commission on Indian Currency and Finance (1926) has decided this point in favour of a new bank. We agree with this view. There are many important considerations which support this opinion. The Imperial Bank and its pre-existing Presidency Banks have never evidenced any broad national out-look for the country's economic well-being nor shown any sympathy for the advancement of national banking. Illustrations have been cited how assistance to banks has been refused even against government securities. The mercantile community knows how vast credit lines are extended to non-Indians whereas even reasonable facilities have been refused to the people of this land. The banks of this

country have been always looked upon with competitive eyes, more as rivals than as complimentary units of the country's banking system. Officers who are product of such tendencies can hardly be expected to be alive to the seriousness of the new responsibilities of a central bank. Its traditions would always hamper the loftiness of the mission of the bank of issue. Moreover, such a large number of branches, as the Imperial has, is an unnecessary appendage to the bank of issue. The principal function of the Central Bank is to regulate the Indian money market. It will be sufficient for this purpose if it operates through its branches in the markets at the most important places, as the latter through the force of economic laws can easily regulate the smaller markets, within their spheres of influence, on the same principles. The central bank fulfills a good deal of its mission by mere existence rather than by actual operations. The certainty that it exists to interfere whenever and wherever the market and credit conditions seem to go against public interests would always keep other operators within limits. Moreover, there would be more efficient control if its energies are not dissipated in a large branch organization.

The Imperial Bank's directorate and management are preponderatingly non-Indian. If it is transformed into the central bank this state of things would naturally continue for sometime. And as non-Indians can hardly feel the economic pulse of the country or identify their interests with the interests of India, which will at times be against their own countries, it is difficult to believe that they will be able to concentrate themselves on the new responsi-

bilities with that singleness of purpose which is the essence of a central bank's working. The central bank's business is to look to national interests alone.

Transformation of the Imperial would naturally require strict examination and valuation of all of its assets. It is likely that the estimate of independent valuers may not coincide with the valuation of the bank management in which case lengthy discussions may take place—the Government is taking responsibility for the redemption of the bank notes and it is but natural that it should satisfy through independent examiners that the assets are actually as stated in the balance sheet. Also there may be certain accounts on its books which it would be against the laws of the bank of issue to carry forward to the books of the new bank. The only way out of the difficulty would be liquidation of such accounts but that may mean not only great financial disaster to the parties concerned but also great disturbance of the market. It would be extremely undesirable to bring about such a situation and make the central bank begin its career with such unfortunate events. Far better it would be, if the central bank be started afresh with no past accounts and with a free hand to mould the shape of its assets strictly according to its constitution.

The Imperial Bank has been hitherto doing a good deal of commercial banking with principal object of making profit for its shareholders. The central bank's primary object is not to earn dividends but to look to national interests. It is extremely difficult to believe that an organization of the former type can smoothly be shaped into the latter. Moreover, even the shareholders will not

agree to the limitation of their dividend to 5 or 6 per cent. which is the limit usually prescribed for central bank's dividends. The Indian Government has hitherto allowed all the profits of a monopolistic concern like the Imperial Bank to its shareholders, whereas it should have legitimately demanded major portion for its revenues ; and when it makes this demand, if the Imperial be reconstructed, these vested interests will raise a great hue and cry. For this reason also it would be better to have altogether a new bank.

The central bank should naturally be modelled on national lines *i.e.* with preponderance of national capital, directorate, and management. It would be difficult if not impossible to successfully remodel the Imperial Bank on these lines. It would involve a good deal of discussion, ill-feeling, and disturbance when attempts are made to impose the new restrictions. In the new institution such safeguards and stipulations as may be necessary, can be provided from the very beginning.

Those of the critics of the new central bank who suggest that the Imperial Bank can be remodelled by super-imposing additional functions like currency powers, etc. on the present constitution of the bank, thereby permitting it to carry on present commercial banking, clearly demonstrate their ignorance of the meaning of central banking. Even taking it for granted that its constitution and working satisfy national points of view, how could its active participation in advancing to people, one and all, make it unbiased controller of credit ? How could it hope to obtain good will and co-operation of other credit institutions, so essential for its success, when with

their free deposits, it competes with them for commercial investments? And lastly as Sir Basil Blackett, the present Finance Member has pointed out, even there is danger, howsoever remote, of the bank's not being able to command as great and as implicit a confidence as a central bank would, if it kept aloof from every day commercial banking. In times of panic when the bank depositors begin to withdraw and the assets are not paid when they mature, would not such a bank be more than occupied with her commercial banking rather than be free to look to the general credit conditions of the country and extend assistance as bankers' bank to other banks of the country? Such a contingency would nullify the very purpose which a central bank is designed to satisfy. And also would not in that case the object of profit-making be primary rather than secondary and the mission of controlling and regulating the money market, the essential and main function of a central bank, be confined to the background? Amalgamation of commercial and central banking may be considered as an unworkable proposition in the present day economic conditions.

The best argument for not interfering with the Imperial Bank in this connection is that four members of the Commission, including a managing governor, who are intimately connected with the bank, have endorsed the proposal of starting a new bank altogether. The cry that has been raised in the press against the formation of a distinct central bank is reported to come from interested quarters. But such sectional considerations should not be allowed to interfere with national purposes.

The Imperial Bank can suitably expand its commercial banking activities. It has past traditions, past prestige and past experience for commercial banking which are advantages great in themselves. It should be able to flourish even much better when the restrictions now imposed on its working are removed. Possibly, in the beginning the withdrawal of about Rs. 30 crores of deposits due to the transference of government, semi-government, and bank balances to the new bank may affect its resources to an appreciable extent, but on the other hand it would be free to allow interest on current accounts as well as raise its rate of interest on savings and fixed deposits and thus attract a portion of funds which hitherto has been lured by higher interest to other banks. But if it is still apprehended that such measures would not sufficiently remedy the disturbance which withdrawals might cause, arrangements could be made for financial assistance at the new bank, within certain limits, for a certain period at a reasonable rate of interest. This arrangement may be incorporated in the charter of the new bank or left to the deliberations of the Banking Council. We do not recommend acceptance of the Currency Commission's proposal to entrust agency work of the bank of issue to the Imperial Bank. This will not only be a deliberate and distinct disadvantage to other banks but even increase the Imperial's power to a much greater extent than at the present time. With the restrictions removed on its business and with a supply of cheap or free funds, it will be in an unrivalled position, dominating over all other banks and interfering with the general banking development. The central bank should thus not be restricted to

entrust agency business to the Imperial but be free to make any arrangements which suit its purpose the best or which are calculated to advance banking progress. Possibly as the result of divestation of government connections, the Imperial Bank may close some of its branches. If branches are closed at places where other banks exist, there will be no harm done to the country by the extinction of such connections, because banking facilities on the part of other banks will continue with greater vigour. At present the unequal competition on the part of the Imperial at such small centres is not only unprofitable to it, but hampers legitimate profits of other banks. With this impediment removed the other banks will have better interest and energy in expanding their work and will rise to any occasion as may be demanded by local trade. But if on the other hand, business at places where there are no other banks, be found unprofitable that will show that either the methods of Imperial's working require remodeling or readjustment or sufficient exertions have not been made to develop business; or in the last source there is no need for banking services of the type of a joint stock bank--possibly a smaller local institution of a class referred to in later chapters is all that is wanted. In the former two cases the instinct of earning will make the Imperial Bank explore the field thoroughly and thus be more serviceable to the community ; and in the latter, no injury will be done by such closure.

There is another way in which Imperial's present organization can be utilized. Possibly it may be a good idea to transform it into the first Indian

Exchange Bank. We shall develop this idea in a subsequent chapter.

The agreement which exists between the Government of India and the Imperial Bank, whereby the latter is appointed the sole banker of the former, is still to run for about four years more. Its cancellation, however, should not prove an insurmountable obstacle. If the new bank is to come into existence the Imperial Bank would not be too particular to plead the continuance of the agreement on the ground of unexpired period. Special assistance of cheap funds as already recommended, or any other suitable compensation for such unexpired period or its transformation into the first Indian Exchange Bank, should be a sufficient advantage to satisfy the Imperial's claim in this respect. We do not approve of the Commission's recommendation that the Capital of the Reserve Bank should in the first instance be offered to the shareholders of the Imperial Bank to compensate them for the loss of Government banking business and for the cancellation of their agreement. Such a course will lead to the indirect concentration of the control of the bank of issue in the Imperial Bank and thus negative the very reasons which have induced the commission to recommend establishment of a separate central bank. With all restrictions removed on its business, with the ownership of the bankers' bank and with the consequent determining voice in that bank's affairs, the Imperial Bank would be a greater menace to the banking of the country than it has been in the past. Compensation to the Imperial Bank for the loss of its contract should not take any shape which would increase its competitive power as compared

to other banks. Of all banks Imperial on account of its prestige and power, least deserves such favouritism. In addition to what has been said above in this connection, or what will be said in the chapter on Indian Exchange Banks, if there is anything further needed to compensate the bank, we would suggest that a portion of the profits of the proposed Reserve Bank be handed to the Imperial during the remaining number of years of the contract. We should not go further. Nor should we recommend an award of a lump sum from the tax-payers' money, about which there is some talk. If the Imperial Bank does not accept compensation of the nature referred to, but insists upon the continuance of its contract, we think it would be better to let the same continue and defer establishment of the Reserve Bank till the contract period is over. In that case, of course, the Imperial Bank will not get anything, nor should any preferential treatment be shown to it.

Having settled this important point about the formation of the central bank the question about the name arises. The Commission have suggested that it should be called "the Reserve Bank of India." The word "Reserve" suggests some sort of similarity with the Federal Reserve System and it would be better if a name without the inclusion of this word be decided upon. Also we should see if a native word for India will not be more appropriate. The name "Bank of Hindustan" or "the Hindustan Central Bank" will answer this purpose better. They also resemble the names of most of the central banks in Europe and may possibly be found acceptable to all.

The bank on account of the speciality of its purpose and functions should naturally be incorporat-

ed by a special charter *i.e.* by a special act of the Indian Legislature. We have broadly discussed in the preceding chapters what the functions of a central bank are. We shall not repeat them here nor give arguments or explanation concerning such functions, but simply refer to the principal provisions which should be incorporated in our central bank's charter. Some remarks may be made to clear the purpose wherever necessary. The provisions are based on what experience in other countries has shown to be the right principles on which the banks of issue should work. Adjustment is, of course, made to suit the peculiarities of Indian requirements. For the benefit of those who may wish to know something about the constitutions of other similar banks we are giving in the Appendix Charters of the Netherlands Bank and the Reichsbank.

PERIOD OF CHARTER

The Charter should be for a period of 30 years in the first instance but renewable thereafter for such periods, with such modifications and under such conditions as the actual experience of working may warrant. During this initial period of 30 years changes in the constitution may take place if approved by the three-fourths of the Banking Council, the three-fourths of the shareholders of the bank, according to their voting strength, and by the three-fourths of the members of the Legislative Assembly or of a body corresponding to it.

The period of thirty years is sufficiently long to enable the bank to assume full responsibilities imposed upon it as well as to show satisfactory working. If the results are not up to the expectation or

if weakness prejudicial to smooth working or national interests is revealed, steps could be taken to improve the constitution as provided for. The limits on voting have been fixed so as to assure that there are very strong grounds, more or less unanimous, on the part of all the parties concerned to make changes.

CAPITAL

Capital of the bank should be Rs. 10 crores out of which Rs. 5 crores should be paid up and the balance should remain as uncalled liability. It should be left to the Bank's Board of Directors with the advice and consent of the Banking Council, to determine when and in what instalments further calls should be made, if necessary. It should also be open to the shareholders to increase the Capital if approved by three-fourths of the Banking Council and the Governor-General-in-Council. Conditions as to the terms of such increase should be mutually settled by the above parties on the same principles.

The Capital* of the bank should be open for subscription in rupees in India and to Indians in the

* The Hilton Currency Commission has recommended that the capital of the Reserve Bank of India should in the first instance be offered to the shareholders of the Imperial Bank. Acceptance of this proposal would virtually mean entrusting the control of the bank of issue to the Imperial Bank. Nothing could be more unthinkable than this. In the reorganized state of affairs, the Imperial would be nothing more than a mere commercial bank and to give directing and determining powers to it would result in its acquiring tremendous competitive advantages over other banks and in giving terrible blow to Indian banking. Such a recommendation nullifies the very canon of Central Banking which requires their management and credit policy to be unfettered and unbiased. Capital of a Central Bank should be widely distributed amongst the people of its country so as to give scope for representation of as large a number of national interests and economic activities as possible.

first instance. If, however, it be considered necessary in the interests of the Empire or of the existing English commercial and banking interests, one fourth of the capital may be permitted to be subscribed by such of the non-Indian subjects of His Majesty as do not belong to a colony or a dominion where disabilities of any kind, whether in this or other respects, are imposed upon Indians. Ordinarily only individuals should be registered as members but if considered desirable there would be no harm if a portion of the Capital is set apart for subscription by the joint stock banks of the country.

Large subscribed Capital will give greater strength to the bank's working and at the same time amount of profits to be distributed to the shareholders will be only limited to the amount of capital actually paid-up. Restrictions on the nationality of subscribers are naturally prescribed in the interests of India so that its working may be actuated by national considerations.

SHARES

Shares should be of Rs. 1,000 face value out of which Rs. 250 should be paid on application, Rs. 250 on allotment and the balance in calls as may be determined under provisions of the last section.

If a portion of the Capital is decided to be offered to non-Indian British subjects two classes of shares should be introduced called "A" and "B", the former being issued in the case of purely Indian subscriptions and the latter in the case of non-Indians—"A" shares will be issued for Rs. 750

lakhs and " B " shares for 250 lakhs. Transfers of " A " shares should be restricted to the people of this country but " B " shares may be transferred without any such limitation so long as the transferee is a British subject. Both the classes of shares should rank equally in all respects. Approval to transfer shares should rest in the hands of the board of directors. Ordinarily there would be no objection to such transfers unless the directors are of opinion that the transferee would not be able to pay further calls if they be demanded. In such a case the transferee should have option to deposit approved securities to guarantee such payment ; but if still the directors refuse registration of the transfer, the transferee should have right to appeal to the Banking Council whose decision should be final.

In case continuance of a particular shareholder is undesirable in the public interests, his name should be liable to removal from the register of members, provided this action is approved by the Banking Council. In such a case he should receive compensation for the shares held at the average rate prevailing in the market in the preceding month or at the rate ruling on the day of removal, whichever is higher. The board of directors should dispose of such shares as best as they think within six months.

VOTES AND MEETINGS

Each share should entitle its possessor to one vote with the stipulation that no one shareholder whether acting for himself or for others or for himself and others collectively should enjoy more than 100 votes. Voting by proxy should be permissible under usual conditions.

This provision is designed to prevent control of the bank falling into the hands of a particular group or section. The Currency Commission have recommended a limit of 10 votes but it is too small to admit of any concentrated and quick action, should circumstances require urgent solution. The Reichsbank has a limit of 300 votes.

Voting in connection with elections and other propositions, which can be previously communicated through post or notification, can be made by shareholders through post, provided the voting papers are filled in the presence of certain designated officers who should authenticate the signatures. As a further check the signatures can be compared with the specimens on record.

In a vast country like India where distances are great and consequently personal attendance may entail great expenditure, a provision like the above will ensure exercise of rights of shareholders, some of whom may otherwise be not able to exercise their influence on important issues.

General Meeting of the shareholders should take place once every year. Special and Extraordinary Meetings may take place under usual conditions. Limits upon the number of signatories competent to summon a special meeting should be prescribed on the general lines governing such purposes.

DIRECTORS

Possession of a minimum number of 50 shares should be a necessary qualification for any share-

holder to be elected as a director. This condition should not operate in the case of special directors referred to below.

The total number of the directors of the bank should be twelve : (i) Five out of this number should be ordinary directors to be elected by the shareholders in the annual meeting but with the limitation that not more than two should be from each presidency and not more than one from each of the provinces ; (ii) Two directors should be elected by the banks of the country voting according to the scale laid down in the Bank Law ; (iii) The Comptroller of Banks or any other Officer representing him and the General Manager of the Bank (referred to below) should be *ex-officio* directors ; (iv) The remaining three directors should be nominated by the Governor-General-in-Council with the advice and consent of the Banking Council. In the case of there being any disagreement between these two bodies the nomination may take place separately, the Banking Council naming one and the Governor-General-in-Council the other two. Directors of the type (i) should not be connected with other corporate banks in any capacity whatsoever. At the most one out of the two directors of class (ii) may be a person connected with corporate banks but the other should under no case be so connected. Directors of the class (iv) should have no limitation upon the business they carry on in their individual capacities.

The qualification as regards possession of shares should not apply to the directors of the class (ii), (iii), and (iv), who should be designated as special directors. There should however be no distinction

as regards powers and privileges between ordinary and special directors.

The above composition of the Board of Directors will safeguard all the interests concerned. Any inequalities whether as regards representation of provincial or economic interests can be levelled by the exercise of nomination powers reserved to the banks, the Banking Council and the Governor-General-in-Council.

At least nine of the directors of the bank should be Indians. To arrive at this figure restrictions will have to be placed on various classes of directors. It would be sufficient if the number of non-Indians be at the most two in case of (i) and the total of such non-Indian directors under (i), (iii) and (iv) should not be more than three—assuming that the directors elected by (ii) would be Indians.

The directors should elect their own Chairman and Deputy Chairman every alternate year.

The term of office of the directors of the type (i) should be five years but one of them should retire by rotation every year. The other directors, excepting *ex-officio* directors, should hold office for two years at a time, it being so arranged that the nomination or election of the classes (ii) and (iv) should take place in the alternate years.

Conditions which usually govern the continuance in office of the directors of corporate concerns, their responsibilities and duties should be prescribed, but as they are matters of ordinary detail we think it unnecessary to enter into them here.

BRANCHES

The bank should have its Head Office at Bombay and Calcutta, every alternate year. One principal branch should be established in the capital town of each of the various presidencies and provinces. If the directors decide and the Banking Council approves branches may be opened at other principal cities where large commercial and banking transactions take place so as to provide facilities for local banks.

The bank should be free to make agency arrangements with any bank or banks as it may deem expedient at places where it has no branches. Government Treasury business and other work for which the central bank is responsible should be permitted to be transacted through such agencies. The bank should be free to decide the terms on which such agency connections are established.

The bank should not open any branches outside India but should be free to open accounts or make agency connections with foreign banks or with branches of Indian banks working abroad. Settlement of details in such matters should be left to the Board of Directors.

Arrangements made for agency work both inside and outside India should be communicated to the Banking Council and should be subject to their veto.

MANAGEMENT

The management of the bank should be carried through an officer called the General Manager, under whom should work Managers. Officers in-charge of important branches like Bombay, Calcutta, Madras,

etc. may be designated Special Managers[§], as naturally they will enjoy special powers, which it would not be necessary to entrust to managers of less important branches. It would be advisable to place such big branches in charge of two Joint Special Managers, at least one of whom should be an Indian. Less important branches can be put in charge of officers who may be called Managers. It is undesirable to designate the principal officer of the bank as Managing Governor or Governor as it conveys a sense of autocratic power.

The Continental and American banks find the word "President" more appropriate but it is likely to be mixed up with the word chairman. The word "General Manager" represents the active connection with management much better.

The General Manager and Special Managers should hold at least 25 and 10 shares of the bank respectively, in their own names.

The General Manager should be appointed by the Board of Directors with the advice and consent of the Banking Council. The appointment should, however, be approved by the Governor-General-in-Council who should have power to veto thrice such appointment at any one time. In case the Banking Council and the Board of Directors do not agree at any time, the selection should rest with the Governor-General-in-Council.

The Special Managers should be appointed by the Board of Directors but approved by the Banking Council. Appointment of ordinary managers should entirely rest with the directors.

§ They can also be fitly designated as President.

Term of office for a General Manager should be five years but he should be eligible for re-appointment. He would be the Board's mouth-piece in all matters connected with the bank and the public, as well as be its chief instrument for carrying on the bank's duties.

The selection for appointments of General Manager, Special Managers and Managers should not be restricted to the bank's ordinary staff but the authorities should be free to select most suitable men for such posts wherever available.

LOCAL ADVISORY COMMITTEES

Management of each branch should be guided in its business by a local advisory committee. Powers of such committees as to the limits, within which they can authorize the local manager to do business without first obtaining sanction of his head office, can be fixed in advance. The functions of this body should ordinarily be, merely advisory and recommendatory. Their views should receive the Board of Directors' best attention when fixing discounting and rediscounting facilities.

The Committee should consist of six members. The Examiner of Banks and the local Manager should be *ex-officio* members. The Board of Directors should appoint two members; the Banking Council should appoint one and the local Government should nominate the remaining sixth member. Besides the above six members, the directors of the bank that may be residing in the local province should have right to join such committees whenever they find it convenient to do so.

The appointment of committees of this nature will ensure full local representation as well as proper control over credits granted. Such a representative body will make discounting of bills of bogus and worthless parties impossible and thus prevent losses of the nature in which the Lucknow branch of the Imperial Bank was involved sometime back. The Bank of France appoints such committees to assist its branches and the arrangement is found of great value by its directors.

BUSINESS

Deposits

The bank should open accounts free of charge subject to any limits that may be prescribed from time to time upon the minimum balances which should be maintained. No interest should be payable on deposits whether current or fixed. The Banking Council may, however, restrict by three-fourths majority the nature of clients other than banks and bankers who can open deposit accounts with the bank.

NOTE.—Nothing under this clause should prevent the bank from taking loans on interest in India and/or outside when such a course is deemed necessary and approved by the Banking Council.

The Government of India and the Provincial Governments should keep all their funds with the bank or with the agencies that may be appointed by it. As far as possible the system of government treasuries should be completely abolished so that all the available cash of the Government may be at the disposal of the country through its central bank and there may not be any disturbance to the market

through the transfer of money from the people to the Government due to payment of land revenue, taxes, etc. The Central Government should, however, be free to transfer its funds partly or wholly to any other banking concern, where such transference is considered in the public interests, with a view to save an institution in difficulties or for similar public purposes, provided such a course is approved by three-fourths of the members of the Banking Council.

A provision of this nature is calculated to enable the Government to intervene and give a helping hand whenever circumstances may warrant such a course. When two of the most important banks of Italy, *viz.*, Banque Italiano Disconto (present Banque Nationale de Credito) and Banque de Rome were in difficulties some years back the Italian Government immediately transferred their funds to them and subsequently helped them to reorganize. This saved big banking crisis and the banks were ultimately able to regain the same position of confidence which they enjoyed in the commercial life of Italy, before their difficulties started.

In case banks choose to lodge security with the Comptroller of Banks, required under the Bank Law (*see next chapter*), in the shape of deposit receipts of the central bank, it should receive such deposits at rates of interest to be determined by the Banking Council from time to time which should, however, be not more than the bank's official rate of discount. Such deposits will be withdrawable under the instructions of the Comp-

troller of Banks when a banking concern is in difficulties or is required to be wound up by the Banking Council.

All the banks of the country whether incorporated under the Bank Law or under special charters should keep their accounts with the Central Bank's branches located in the provinces where they have branches, so as to be able to partake in the clearing house settlement (*see* below).

The Bank should maintain a cash reserve of at least 40 per cent. of its demand liabilities, other than in respect of notes issued—cover for which is referred to hereafter. If at any time this condition is violated the bank should pay penalty on the deficiency at the rate of discount then ruling, considering the amount of deficiency as a day to day advance to the bank. Also no further advances should be made or any profits distributed, unless the deficiency is made good.

The banking law of America requires a cash reserve of 35 per cent. on the part of the Federal Reserve banks. The law of the Reichsbank requires a cover of 40 per cent. in this respect. As the bank of issue is practically bankers' bank, that keep major portion of their cash with it, it is essential that the cash reserve of the central bank should be always strong, because if at any time it happens to be insufficient, the whole banking system would be dislocated.

Investments

The bank should be permitted to invest its funds in the following channels. It should not

make unsecured advances or advances against immovable property.

- (i) To buy and sell gold whether coined or uncoined ;
- (ii) To discount, buy and sell bills of exchange, promissory notes, trade and bankers' acceptances, or other commercial paper, with a currency of not more than three months, and in respect of which at least two obligees of known solvency are responsible, one of whom is a person of Indian nationality or a firm consisting of such people or a corporate company or bank registered in India with at least three-fourths of its capital owned by Indians.

If the last signatory to the instruments referred to above be a Co-operative Credit Society or an agricultural bank, and the finance is required for *bona-fide* agricultural needs, the period of maturity may be exceeded to six months. But the total of such credits granted should not exceed one-fourth of the bank's total discounts.

The condition of Indian signature is necessary to enforce that credit of the bank is primarily meant for the people of the country. Such stipulation is made in charters of other central banks also. Those who have been in touch with the practical banking in India will recollect that the late Tata Industrial Bank was denied rediscounting facilities by the Bank of England on the ground that its charter did not permit such

credit to persons or concerns that did not belong to England.

The operations and facilities referred to in this clause should usually be extended in the case of genuine commercial and agricultural transactions. This restriction may, however, be not insisted upon when a bank wishes to rediscount paper for the purpose of financing securities of Government of India, Provincial Governments, local authorities or bonds of mortgage banks. The maturity of such obligations should not exceed three months.

- (iii) To buy from and sell to banks, bankers, and parties approved by the Board of Directors, transfers by telegrams or letter and sight drafts, payable at any place in India.
- (iv) To make loans for a period not exceeding three months on the security of the following "movable" objects :—
 - (a) Gold and Silver, whether coined or uncoined, or the documents relating to the shipment or storage thereof.
 - (b) Such negotiable paper as is eligible for purchase or discount, with the limitation that advances against "agricultural paper," referred to at (ii) do not exceed 25 per cent. of the total advances.
 - (c) Merchandise whether in the bank's godowns or in approved warehouses in India to the extent of not more than two-thirds of its value.

- (d) Stocks, funds, and securities in which a trustee is authorised to invest trust money.
- (e) Foreign bills, drafts and acceptances as may be eligible for purchase by the bank as referred to in (ii).
- (v) To buy from and sell to banks, bankers and parties approved by the bank's directors, in amounts of not less than the equivalent of Rs. 1 lakh, transfers by telegram, or letter, sight drafts, trade acceptances, banker's acceptances and bills of exchange (including treasury bills), drawn in or on places in such foreign countries as adhere to the gold or gold exchange standard and do not restrict export of gold, of a maturity not exceeding 90 days and it may keep in such foreign countries credit balances with banks or bankers as may be approved by the Banking Council.
- (vi) To buy and sell all securities as are eligible for the cover of the note issue.
- (vii) To invest a sum not exceeding its paid-up capital and reserve, in Government and other securities as may be approved by the Banking Council, maturing within ten years, and deal in such securities within this limit.
- (viii) To buy and sell Government and other securities approved by the Banking Council, which have not more than six months to run, provided the total of such

securities held does not exceed 25 per cent. of its demand liabilities.

- (ix) To make advances to the Government of India under such conditions as regards amounts, period of payment and rate of interest as are approved by the Banking Council—no such advance to remain outstanding for more than 12 months.
- (x) To purchase and subsequently sell, whenever necessary, properties required for its habitation.
- (xi) To buy properties, merchandise, shares, (including its own) and other articles whenever such a course is deemed necessary to safeguard monies originally advanced with good and *bonafide* intentions. All such purchases should, however, be sold off within one year from the date of purchase, excepting immovable properties where the period may be extended to five years. The Banking Council should have discretion to permit extentions of such periods whenever special circumstances may warrant such a step.
- (xii) To subscribe to the capitals of special banks (referred to later), as may be required by the Banking Council.
- (xiii) To extend special credit lines on special terms to credit institutions and banks as may be authorised by the Banking Council.
- (xiv) To give assistance to banks that may be in temporary difficulties, provided such

a step is sanctioned by at least nine members of the Banking Council.

[NOTE.—We think it will be in the interests of banking in general if the Central Bank's dealings as regards discounts, advances, etc., are ordinarily restricted in the first instance to banks. If at any time banks abuse this privilege and put up cost of credit unduly high or starve some legitimate and deserving economic activities from credit or do not behave properly in the matter of rationing credit, the Banking Council should have power to permit the bank to enter general market. Provisions enabling the bank to deal with public have been simply suggested with a view not to create any constitutional or legal disabilities if such an occasion arose. Also the Banking Council should have power to increase limits prescribed on the amount of other investments, temporarily or for stated periods, if such a course be deemed necessary. At times the Central Bank will be faced with large surplus and idle funds, which if uninvested may mean loss of income. The Federal Reserve Act of the United States of America gives similar authority to the Federal Reserve Board whereby it can permit the Federal Reserve banks to do "open market" business, if that be necessary.]

Agency

The bank should be free to do usual agency business which banks often do for their clients *e.g.*, collection of items, buying and selling of securities, etc.

The bank should act as agent for the Government of India and Provincial Governments in the transaction of the following kinds of business :—

- (a) Flotations of Public loans and management of Public debt, including Treasury Bills.

- (b) Remittance and transfer operations.
- (c) Buying and selling of precious metals.
- (d) Buying, selling, transferring, and taking charge of any bills of exchange, securities or any shares in any public company.
- (e) In general to do all monetary or other transactions which may be expedient for the bank to do, in the public interests, on behalf of the Government.

Internal Rupee Transfers

The bank should be bound to transfer telegraphically or by letter (as the remitter may require), any amounts tendered by other banks, from one branch to another, at the following rates:—

| AMOUNT. | CHARGES. |
|--|--|
| Sums up to Rs. 10,000. | 1/4th of a rupee for every Rs. 1,000 or a part thereof <i>plus</i> actual telegram charges. |
| Sums over Rs. 10,000 but less than Rs. 1,00,000. | 1/8th of a rupee for every Rs. 1,000 or a part thereof <i>plus</i> actual telegram charges. |
| Sums over Rs. 1,00,000 | 1/10th of a rupee for every Rs. 1,000 or a part thereof <i>plus</i> actual telegram charges. |

The bank should be free to remit amounts on behalf of the general public but charges for such transfers should be twice of those given above. Also

the minimum sum to be transferred on account of the public should not be less than Rs. 10,000 on each occasion.

One of the principal functions of a bank of issue is to cheapen the cost of transfer of money and the above provision is inserted to meet this requirement. At present the Imperial Bank of India charges for transferring sums over Rs. 10,000, $\frac{1}{16}$ per cent. to the public, and $\frac{1}{32}$ per cent. to banks. This is high. In Germany Reichsbank charges $\frac{1}{2}$ Mark for sums up to Marks 2,500. Every additional Marks 1,000 are transferred at the rate of $\frac{1}{5}$ th of a Mark. But when transfers are made and received by parties having accounts with the bank, and amounts are large, only $\frac{1}{10}$ th of a Mark is charged for every Marks 1,000.

CURRENCY FUNCTIONS

The bank should have the sole right of issuing paper currency or notes in India which should be legal tender for all payments. The Government of India Currency Notes should be gradually withdrawn from circulation, say, within a period of five years from the date of commencing business. In the meantime, all the present currency reserves should be transferred to the bank which should assume responsibility for redemption of the Government Currency Notes. The bank should take up the sole responsibility of maintaining the gold or international value of Indian monetary unit. Although definite reserves for notes are suggested, they should be secured by all the assets of the bank, including the uncalled liability. Over and above this security, the Government of India should guarantee their redemption. In view of full reserves

and liquidity and safety of the bank's business, this guarantee is more or less nominal and the State would in all probability be never called upon to pay anything towards this contingent liability ; still it is better to stipulate for it in the present conditions of India. The notes should be free from stamp duty and note tax.

Following provisions should be prescribed in connection with this business :—

- (i) The amount of notes issued should be fully covered by a reserve consisting of—
 - (a) A minimum of 40 per cent. of gold, silver rupees, and gold securities (approved by the Banking Council), of which at least half should be gold in India.
 - (b) Not more than 30 per cent. of Government of India, and other securities (*e.g.* bonds of mortgage banks, etc.) which may be approved by the Banking Council.
 - (c) The balance should consist of bills of exchange discounted or purchased under its business powers.
- (ii) If at any time the reserves (a) and (b) are not according to the limits prescribed, there should be a penalty tax payable to the Government on the amount by which such reserves are deficient, at a rate which should be made up of—
 - (a) The discount rate, which should not be under 6 per cent. prevalent at the time,

(b) Extra 1 per cent. for every difference of 5 per cent. or part thereof from the stipulated margin *e.g.* if the reserve (a) is 34 per cent. or reserve (b) 36 per cent. and the rate of discount 7 per cent. the penalty tax will be $7 + 2 =$ to 9 per cent. on $6T/100$, where T is the total amount of notes issued.

The discount rate should be put up by $\frac{1}{2}$ per cent. for every variation of 5 per cent. or part thereof from the ratios prescribed for the different kinds of currency reserves.

[If considered necessary exemption for one week from penalty tax for a variation of less than 5 per cent. may be permitted. Also if considered advisable by the Banking Council the composition of the portion of currency reserve represented by metals and government securities may be permitted to continue on the present basis, but such facility should not continue for a period longer than 5 years during which all the government notes are required to be withdrawn].

(iii) The notes should be payable on demand in legal tender or gold, as may be convenient to the bank, at its principal offices like Bombay, Calcutta and Madras; but at other branches the redemption should be at the bank's convenience, unless a fortnight's notice is given in which case the bank should be bound to

pay such notes in gold or other legal tender (*e.g.*, silver rupees).

- (iv) If notes for a sum not less than Rupees 1 lakh are tendered, the tenderer should have option to demand its equivalent in gold or if that be not possible in gold exchange on a country where export of gold is not prohibited.
- (v) The bank should have option to return silver rupees to the Government, whenever their amount tends to be large and receive in return their equivalent in gold.

The Currency Commission have recommended the amalgamation of Currency and Gold Standard Reserves. We think they should remain separate. The bank may administer the Gold Standard Reserve and make transfers therefrom when the number of rupees with it increases, but the final responsibility about its sufficiency should rest with the Government.

- (vi) The bank should make compensation for notes damaged or destroyed under usual rules which may further be approved by the Banking Council. Notes outstanding for more than 20 years may be considered as lost and their equivalent should be paid to the State, which may

thereafter be responsible for their encashment if subsequently presented.

PROFITS

The annual profits of the bank should be distributed as under :

- (i) First 20 per cent. to Reserve until it reaches 50 per cent. of Capital; thereafter such contribution may be reduced to 10 per cent.
- (ii) Over the balance, there should be first charge of cumulative dividend of 5 per cent. to shareholders.
- (iii) Of the remainder, 3 parts should go to the State and 1 part to the shareholders till their dividend has reached 8 per cent.
- (iv) If there is any surplus, the excess should be distributed in the ratio of 7 : 1 (7 parts to the Government and 1 part to the shareholders), till the shareholders' portion allows them 10 per cent. dividend.
- (v) Any balance, after making 10 per cent. dividend possible for the shareholders, should go to the Government.
- (vi) Payments to shareholders in respect of (iii) and (iv) may be either distributed to them or kept in a separate reserve for the purpose of equalisation of dividends, as the Directors may decide.

[NOTE.—Share of profits due to the Government may be utilised wholly or partly as loans with or with-

out interest, to Indian banks or as capital subscriptions to special banks or taken to revenue as the Legislative Assembly may decide at the time of annual budget ; provided, however, if the Banking Council decides by three-fourths majority to utilise such funds for any purposes calculated to safeguard and advance banking interests, at least half of such funds should be so utilised. Government profits of this nature are reserved for the welfare of general and special banking activities in other countries.]

GENERAL

Clearing Houses

The bank should organize clearing houses for the settlement of inter-bank payments at places where it has branches. Every bank registered under the Indian Bank Law should be admitted as a member. Admission of banks not registered under Indian Law but licensed thereunder should be sanctioned by the Banking Council.

Safe Custody

The bank should be free to receive securities and valuables for safe custody.

Audit and Examination

The accounts of the bank should be scrutinised by two independent qualified auditors elected by shareholders at their annual meeting. One of them should retire every year by rotation but be eligible for re-appointment.

The Comptroller and Examiners of Banks should have same rights to examine the affairs of

the bank and to call any returns, as they have over other banks established under ordinary law.

Discount Rate

The bank should notify from time to time the rates of interest and discount at which it is able to transact business permissible to it. The bank should be bound to increase its rate of discount to any figure if the Banking Council by three-fourths majority so desires.

Weekly Statement

The bank should publish once every week on a certain fixed day its statement of accounts as on the preceding working day. The statement should be published in two parts: (i) Issue Department, and (ii) Banking Department. The percentage of various reserves admissible in (i) and the cash reserve in (ii) should be mentioned in the statement. The statements should be in the following form :

Statement.

offor the week ending.....

PARTMENT.

| ASSETS. | Rs. |
|---|-----|
| Rupee coins | |
| Gold specie or bullion in India | |
| Gold specie or bullion outside India ... | |
| Government of India and other admissable securities | |
| Bills of Exchange admissable | |
| Total ... | |

(iii) Ratio of Government of India and other admissable securities to notes outstanding, per cent.

(iv) Ratio of Bills of Exchange admissable as securities, per cent.

BANKING

| LIABILITIES. | Rs |
|------------------------|----|
| Capital subscribed ... | |
| Capital Paid-up ... | |
| Reserve ... | |
| Deposits— | |
| (a) Government ... | |
| (b) Banks ... | |
| (c) Others ... | |
| Bills payable ... | |
| Other Liabilities | |
| Total ... | |

Ratio of cash to demand liabilities.....per cent.

Ratio of gold and gold securities to totals of notes outstanding and demand liabilities. per cent.

Ratio of gold in India to total of notes out-

DEPARTMENT

| ASSETS. | Rs. |
|--|-----|
| Cash... .. | |
| Notes | |
| Silver Rupees | |
| Subsidiary Coin | |
| Bank Balances— | |
| Balance with banks in India | |
| Balance with banks outside India. | |
| Investments | |
| Bills Discounted— | |
| (a) Domestic | |
| (b) Foreign | |
| (c) Government Treasury Bills. | |
| Loans advanced to Government | |
| Other Loans and advances. | |
| Capital holdings under the authority of the Banking Council. | |
| Special loans under the authority of the Banking Council. | |
| Other Assets | |
| Total | |

standing and demand liabilities.....

per cent.

Dated theday of.....192 .

General Manager.

Balance Sheet

The bank should issue balance sheet and profit and loss statement once in every six months. If the mid-year balance sheet discloses satisfactory state of accounts and profits, the directors may provisionally distribute profits on the basis already suggested, subject to the final adjustment at the end of the year.

Taxes

The bank should pay all taxes to which corporate bodies are liable *e.g.* income tax, local rates, etc. excluding the tax and stamp duty on notes issued as already provided for.

Other Responsibilities

It should be one of the primary objects of the bank to look to banking development and render any special facilities as may be decided by the Banking Council, by at least three-fourths majority. The bank should, however, have right to appeal against such orders to the Legislative Assembly whose decision should be final and binding.

This assistance will generally be required by the special types of banks, like the Indian Industrial Banks, the Indian Land Mortgage Banks, the Indian Agricultural Banks, the Indian Exchange Bank, etc. ; and the assistance will be in the form of subscription to their capital, special credit lines, special rates of discount, etc. It is not necessary that such facilities should be sanctioned permanently ; it is sufficient if they are allowed temporarily from time to time whenever expedient. We shall give some idea of such facilities in the relative chapters. Charters of other countries impose definite obligations in these respects upon their banks of issue.

We, however, think it desirable to entrust powers in this behalf to the Banking Council and the Central Legislature who should regulate such facilities as circumstances may warrant.

In times of banking and financial crisis the Central Bank should co-operate with the Banking Council to create emergency measures and give emergency financial help to banks to tide over the situation. The nature and amount of its assistance will naturally depend upon the individual circumstances. If the banks are able to give permissible securities, the Central Bank can easily advance against them. In other cases special sanction of the Banking Council and the Governor-General-in-Council as already provided for may be necessary. In cases where the security is not considered sufficient or liquid, the Central Bank may insist on the Government's guaranteeing the advance. If the panic is widespread and general the Government may be approached to declare moratorium. During the Japanese banking crisis of this year the Japanese Government sanctioned moratorium in the first instance and later authorized the Bank of Japan to advance over 200 million yen to the Japanese banks, under the Government guarantee.

Liquidation

If the bank be liquidated at any time or its charter be not renewed at its expiry, all the assets should be valued by a committee of independent valuers, and the Board of Directors and the Legislative Assembly should each appoint half of its members. An umpire should be appointed by the Banking Council who should be referred to in case of equality of votes on any matters and whose

decision should be final. All the assets should be written down, if necessary, by such amounts as the valuers' report may indicate, first to the debit of reserve and then to the debit of capital. If, however, there is any reserve available the same should be divided in equal parts between the shareholders and the State.

Staff

The Bank should be empowered to establish rules and regulations concerning recruitment and promotion of its staff, their pay, allowances, leave, pension, provident fund, and such other matters, provided future recruitment of clerical staff and of junior officers is restricted to the people of this country who should be made to pass departmental examinations to be specially instituted by the bank, for initial appointment and subsequent promotion to higher posts. The Banking Council should have power to veto any of such rules and regulations.

This clause should not conflict with the appointment of superior staff referred to in an earlier section. The Reichsbank, the bank of issue of Germany, conducts its own examinations to control admission, and promotions in its service, which is working satisfactorily. Such a procedure will remove complaints of partiality on the part of the bank management and procure capable and promising young men who will discharge their duties intelligently and successfully.

Miscellaneous

The bank should conform in other respects to the general laws of the country, provided they are not inconsistent with its purpose.

Note : Since writing the above, the Government has published the Reserve Bank Bill which proposes to establish bank of issue in India. The bill is discussed in Appendix A.

CHAPTER IX

BANK LAW *

Scope—Organisation—Incorporation—Classes of banks—Capital—Security Deposit—Certificate to commence business—Directors—Local representation—Business : Deposits, Cash and bank balances, Liquid investments, Bank acceptances, Advances and maxims of Safety, Liquidity and Diversity, Other investments, Agency, Safe Custody, Trust business—Accounts and Audit, Form of monthly statement—Government examination and control—Safety fund—Clearing Houses—General : Examination tax, Penalties, Voting Power of banks, Winding up, Date of operation.

The purpose of this Chapter is not to give a cut and dried Law in legal phraseology to govern joint-stock banks but to indicate main directions in which such law should be passed, giving explanation wherever necessary. We shall omit ordinary provisions which are necessary for any joint-stock activity and which are found in the Companies Act of almost every country. The Indian Bank Law will thus be the product of amalgamation of such provisions with the new clauses based on the principles enunciated in this chapter.

SCOPE

Every joint-stock company which uses the word "bank," "credit," "discount," "investment" "savings" or some such similar word or their derivative in its name and/or which receives

*The proposed provisions of the Law refer to the commercial banks only. Modifications necessary for other types of banks should be based on suggestions given in subsequent chapters.

deposits primarily with a view to carry on the business of discounting and/or advancing and/or financing, should be governed by the Indian Bank Act, modified wherever necessary, in view of special type of business, by supplementary measures governing constitution and working of such special institutions.

ORGANIZATION

No bank in India should be permitted to be registered as a joint-stock bank unless at least five people of Indian nationality join together to form a bank and make an application to this effect to the Bank Examiner of the locality where the bank's registered office is to be established. The application should contain all the particulars concerning names of such persons, name of the proposed bank, scope of business, capital, shares, field of operations, number and qualifications of directors and other important items. The Bank Examiner should investigate the question and ascertain whether there is any necessity of a new bank of the type applied for. He should submit the application with his remarks to the Comptroller of Banks who should finally dispose it of.

INCORPORATION

If the application referred to above is sanctioned, incorporation papers containing full facts concerning the bank, its capital, shares, first directors, auditors, etc., together with the Memorandum and Articles of Association, all of which should not disagree in the essentials with the particulars disclosed in the organization application, should be lodged with the Comptroller of Banks, through

the Bank Examiner, who should grant incorporation or registration certificate. Registration fee and stamp duty on such registration should be paid as in the case of other companies with similar capital.

NOTE.—It is understood that organization and incorporation applications should not contain anything repugnant to the Indian Bank Law.

CLASSES OF BANKS

Banks should be divided into different classes based upon the field of their operations. There should be: (i) Local banks which can have office or offices in a single city or town; (ii) Provincial banks which can have branches in the province of habitation; (iii) All India banks which can open branches in any part of India; and (iv) Overseas banks which can open branches in any part of the world.

CAPITAL

No joint-stock bank should be registered as a company with limited liability unless its minimum subscribed capital is according to the following scale.

| Class of Banks. | Minimum subscribed Capital. |
|---|-----------------------------|
| <i>Local Banks</i> | |
| Population in cities where the bank is located— | Rs. |
| Not more than 5,000 ... | 50,000 |
| " " .. 10,000 ... | 1,00,000 |
| " " .. 25,000 ... | 1,50,000 |
| " " .. 50,000 ... | 2,00,000 |
| " " .. 1,00,000 ... | 3,00,000 |
| " " .. 2,00,000 ... | 4,00,000 |
| Over 2,00,000 ... | 5,00,000 |
| <i>Provincial Banks</i> ... | 10,00,000 |
| <i>All India Banks</i> .. | 25,00,000 |
| <i>Overseas Banks</i> ... | 50,00,000 |

Restrictions of the above nature are wholesome and shall prevent undue expansion of branches without sufficient capital. Also capital should naturally be in proportion to the services which a bank wishes to render. And as such services would increase with the population to be served it is logical to fix capital requirements in proportion to the population. A bank with small capital and unrestricted number of branches will not command confidence requisite for such big organization nor be able to meet unforeseen circumstance, *e.g.* runs on it, and thus be in a constant danger of collapse. The National Bank Act of the United States of America contains a provision of this nature.

At least three-fourths of capital should be offered for subscription to the people of this country.

One-fourth of capital should be paid at the application time, another one-fourth at the time of allotment and the balance in such calls as the Directors may decide or as may be prescribed in the bye-laws.

The banks should have power to increase their capital at any time subject to the observance of usual formalities. At least fifty per cent. of such new capital offered and taken up should be collected within six months from the date of subscription.

No bank should be permitted to issue its shares at discount. Ordinary brokerage or underwriting commission may be permitted at or under rates notified by the Banking Council from time to time.

One-tenth of the paid up capital should be lodged as " Security Deposit " with the Comptroller of Banks. The security may be in the form of Government paper or special deposit receipts of the Central Bank as referred to in the last chapter. The security should remain under the control of the Comptroller of Banks for the benefit of the bank's creditors. Interest receivable on such security should be paid to the bank concerned.

CERTIFICATE TO COMMENCE BUSINESS

This certificate should be granted by the Comptroller after the following formalities are complied with :

- (i) All necessary returns are lodged;
- (ii) All conditions are complied with;
- (iii) At least half the amount of subscribed capital is collected and a declaration to that effect, signed by a principal officer of the bank is lodged;
- (iv) One-tenth of the paid-up capital is lodged as security.*

DIRECTORS

There should be two classes of directors : Ordinary and Special. Both of them should rank equally in all respects. Ordinary directors should be elected by the shareholders, necessary qualification being holding in their own names a minimum number of shares. Special directors should be elected by the depositors of the bank from amongst themselves, necessary qualifications being : (i) Possession of minimum deposit, in their own names, equivalent to twice the paid-up amount on the

* This is hereafter referred to " Security Deposit."

number of qualification shares ; (ii) They are not borrowers of the bank. The number of special directors should be at least two but not less than one-third of the ordinary directors. Such a number should be divided in two parts in proportion, as nearly as possible to the totals, as at the close of every two years, of deposits payable on less than one week's notice (including demand and savings deposits) and of those payable on longer notice. The division of special directors as thus determined should continue in operation for two years. Each class of the above depositors should elect special directors thus fixed from the depositors possessing minimum deposit qualification, voting in proportion to the amount of their deposits. For the first year after the establishment of a bank the appointment of special directors may either be dispensed with or made by the ordinary directors. In the case of special directors elected by the depositors, it should be within the power of the ordinary directors to reject election of any such director, if he be connected with any other bank as a director or manager or holds any office of remuneration under the same. To insure that undue advantage in voting power is not obtained from any deposit by transferring it from one bank to another, the election of special directors of all banks should take place as on a fixed day annually. Further, items not actually collected, cleared or realised should not be taken in determining the credit balances on which voting power depends. Casual vacancies on the directorate should be filled by the Board of Directors from the shareholders or depositors as the case may be.

The general complaint against the bank directors in India is that they are recruited from the borrowing class who sometimes gamble with the depositors' money. A provision entitling depositors definite representation will produce great confidence, as their appointees will naturally see that their money is not dissipated in worthless or unsatisfactory advances. Some may say that undesirable persons might get on the directorate in this manner, but as the directors have power to refuse opening or continuance of accounts, they can always arrange that such people are not on their deposit ledgers, which means that they cannot be elected as directors.

Arguments may be advanced that there would be some difficulty in arranging such elections. We hasten to assure that the matter can be easily settled. Let the depositors willing to serve as directors and qualified for the same, submit their names to the bank. The bank should scrutinise such applications, reserve minimum balances and notify their names in the press. The depositors should be asked to send their votes by post, if necessary, by the appointed day, balances on which day would determine the voting strength. The correctness of the signatures of depositors on the voting papers could be verified by comparing them with the specimens on

record. Banks are adept in such comparisons. In fact, one of their principal obligations to pay correctly, sums ordered by their customers, depends for its successful discharge, primarily upon correct verification of the signatures. They have taken such a responsibility, although consequences of loss due to a mistake in such verification can be very large. They should have no objection in taking a similar responsibility when the question of election of directors by the depositors is concerned. Within a fortnight of the appointed day the votes could be classified and the result announced. The facility of electing directors through post may similarly be extended in the case of ordinary directors as well.

The term of office of ordinary directors should not be for more than five years but the special directors should hold office for not more than two years. Retirements should, however, take place every year either by rotation or by lots. The retiring directors should be eligible for re-election.

In the case of local and provincial banks at least half of the ordinary directors should have resided for a period of one year immediately preceding their appointment, and continue to so reside during the period of their directorate, in the district or province in which the bank's chief office is located.

In the case of all banks at least three-fourths of the directors should be Indians.

Some restrictions should be prescribed about the inter-locking of directors. Ordinarily a person should not be able to serve as a director on more than two banks, unless permitted by the Banking Council. Even in the case of two big banks having individual business, say of rupees five crores, common directors should not be permitted. Possibly in the beginning restrictions of this nature may hamper growth of banking and it would therefore be better to leave the regulation of such affairs to the Banking Council.

Local knowledge and information is of primary importance in the grant of credit facilities. The directors who control such credits on the part of banks should possess them and hence residential qualifications are necessary. The word "residence" is used in a broader sense implying business or professional habitation. Not unoften banks are involved in huge losses because their directors had no first hand knowledge or information of the transactions which they sanctioned. Moreover, if some directors are not appointed from the locality in which the bank mainly operates, the local interests are likely to be ignored. The chief sound argument against branch banking is that local considerations are in the danger of being overlooked. The National Banking Law* of America imposes similar restrictions. Surplus

* (1) Every director, during the whole time of service must be a citizen of the United States.

funds of a country are chiefly meant for the use of the country's activities and this is only capable of proper compliance if the people of the country mainly control the banking activities.

LOCAL REPRESENTATION

In the case of "All India" and "Overseas" banks it should be obligatory to have at least one director from each of the provinces where the bank has branches; but if this be not possible provincial local advisory committees should be appointed, consisting of local people having local knowledge. Nominations to such committees should be made by the directors. The Banking Council should have power to appoint one of such members whenever they think that local interests are not properly looked after. The functions of such committees should be mainly advisory but the directors may delegate some of their powers, within certain limits, to them, in the interest of expeditious working, if they so desire.

It has been explained in the last section why local representation is necessary. To supply similar deficiency in the case of bigger organisations local committees are suggested. The Americans do not permit branch banking because they say local conditions in the case of branches may be disregarded. In the present state of India we are strongly in favour

(2) At least three-quarters of the directors must have resided in the State, Territory, or District in which the (banking) association is located, for at least one year immediately preceding their election and must be resident therein during the continuance in office.

of powerful organizations with branches all over the country, but at the same time representation of local interests should be insisted upon to insure that they would not be sacrificed to the interests of other localities which may be represented on the directorate. Moreover, such local representation will serve as a very useful check upon the distribution of local credit and its fraudulent use.

BUSINESS

The banks should be permitted to carry on any *bona-fide* banking business as generally understood. Ordinarily scope of such business is defined in the Memorandum of Association but the Comptroller of Banks should have power to refuse to register any such Memorandum if it contains provisions fundamentally contrary to or violating sound principles of banking. Exceptions should naturally be provided for to enable the banks to undertake business not generally included in banking, if such a course be considered essential to safeguard monies already advanced in good faith. The Banking Council should have power to determine from time to time what constitutes banking business. For example, at present we do not think it advisable to permit the Indian Commercial banks to enter into "syndicate operations," although such business is carried on by German banks. But possibly a time may come, after banking has developed, when there would be no harm to permit them to do such business. Also the Banking Council should be at liberty to permit

any banking company to include in its business special functions not ordinarily permitted to banks. It is so difficult to anticipate in advance the peculiar circumstances or needs which some banks may be called upon to satisfy, that it is advisable to make provision for such sanctions. The ordinary business should, however, be of the following nature:

Deposits

Banks should generally be permitted to receive deposits of every kind, up to any amount, and on any interest. We have usually current or demand deposits, savings deposits, and time or fixed deposits. Rates of interest would be different for different types of deposits. Different banks would naturally receive deposits at different rates ; and although it may be advisable that there should not be any unhealthy competition in this respect, leading finally to banks taking more than legitimate risks in advances, still it is difficult to fix limitations on such rates in advance. It is not possible to legislate because money conditions are not constant but greatly vary. There may be local, periodical, or other peculiarities which would require special treatment. Moreover, as some checks are being suggested on the advances to be made and the Examiners would be empowered to inspect them and their nature, the banks would not invest their deposits in risky transactions, yielding unduly high interest, and therefore naturally they would not increase their rates on deposits beyond reasonable limits, because otherwise the net result would be negligent if not loss. If this consideration be not sufficient, the Banking Council which has wide powers, can from time to time

announce maximum limits either absolutely or in relation to the Central Bank's discount rate, beyond which interest should not be allowed. Or, if general limitation is not necessary they can impose limits in any locality or any institution, at any time, which they may deem advisable in the general interests. Of course, when fixing such limits they should pay attention to the power and requirements of small banks and see that they have some margin left over and above the rates allowed by first class banks; otherwise their deposits would be in the danger of being transferred to the bigger banks. Some may say that acceptance of unlimited amount of total deposits should not be permitted because it means in some cases a very low percentage of capital and reserve to deposits. A restriction in this respect is unnecessary because deposits imply confidence of depositors and if a bank possesses that, the amount of capital is not so important, as its purpose is merely secondary. The banking public may be trusted to see that a bank does not expand its business without sufficient backing of capital, and if this condition still continues either there would be stoppage in the further expansion or the bank must be enjoying extraordinarily great public confidence. Further, if any special case arises the Banking Council possess powers wide enough to suggest and even enforce improvements.

Cash and Bank Balances

In the present condition of India, when banking habits are not developed, restrictions as to cash requirements are necessary. Even an advanced country like the United States of America

prescribes rules in this respect. Many of the bank failures are due to the banks not being able to pay deposits when they are due, though otherwise their business may be solvent. On the ability to satisfy demands of depositors depends confidence of the depositing public and the future development of banking. Hence in the public interests it is essential to lay down limits in this respect. The reserve should, of course, be not unduly high to entail unnecessary curtailment of legitimate credit to the market nor too low to subject banks to the danger of collapse. In our opinion the following limits should be prescribed.

| <i>Class of Bank.</i> | <i>Cash Reserve.</i> |
|---|---|
| Local Banks serving population of one lakh or less. | 15 per cent., of demand liabilities and deposits payable within 15 days + 5 per cent., of other deposits. |
| Other Banks ... | 20 per cent., of demand liabilities and deposits payable within 15 days + 5 per cent., of other deposits. |

The location of the cash reserve should be as under :—

- (a) At least one-third of the cash reserve should be kept in the vaults of the bank ;
- (b) another one-third with the Central Bank or its agent, or with the local clearing bank or in its own vaults or

- distributed amongst any or all of them, as may be possible and convenient ;
- (c) the remaining one-third may be kept with any other banks.

In determining credit balances at other banks, payable on demand, as mentioned at (c) balances due to other banks should be first deducted.

Liquid Investments

By this term is meant investments which can generally be liquidated into cash without any difficulty. Trade bills, trade and bank acceptances admissible for rediscounts at the Central Bank, Government bonds and other paper easily saleable in the market and advances against gold and silver are examples of such investments. The Banking Council should notify from time to time what constitutes liquid investments. At least further thirty per cent. of demand liabilities and deposits due within fifteen days and ten per cent. of other deposits should be invested in such liquid assets. Chief reasons for imposing this obligation are that when a bank begins to lose public confidence or if there is any unforeseen rush on it or if there is some other emergency, the banks should be able to rehabilitate public confidence and not collapse at the first attack. The liquid assets may be compared to the second line of defence.

We have advocated already the necessity of establishing rediscounting arrangements between the banks in India, especially on the part of the smaller banks at the major banks. The bank of issue is the final source to supply credit and currency to any one that enjoys suffi-

cient respectability and credit. In fact discounts are the chief instrument which enable creation of additional currency, within certain limits, which assists credit institutions to meet their obligations to their customers in times of panic. There is, however, one important difficulty in a bank's rediscounting bills in its portfolio with any other bank. The difficulty is that the rediscounting bank will endorse over such bills to another bank and this fact will be construed by its clients as a sign of weakness, which would reflect upon its status and thus react upon its business. The Americans have got over this obstacle by permitting such endorsements to be made in pencil and allowing the rediscounting banks to retake or retire such bills a few days before the date of maturity. On the due date the payment is made to the original bank which erases the endorsement before discharging the bill to the acceptor. Thus so far the customer is concerned he does not know whether his banker financed his requirement himself or obtained assistance from some one else. The same difficulty can be got over by having blank endorsements. The bank that gets its bills rediscounted simply puts its signature. The bank that takes such bills does not fill the blanks to make the endorsements in its favour but

retains them as they are. When the bills are taken up they are returned in the same condition. The original bank can then return them, when payment is made, by writing words, "Received payment," over the blank endorsement made at the time of rediscounting. Nothing would appear on the bills to show that they were rediscounted. An arrangement like any of the above can be introduced in the Indian market which will enable it to reap the full advantage of the credit organization which system of discounts and rediscounts makes possible.

The system of bank acceptances is not at present current in the Indian money market. But it is a very useful method of supplying credit and should be introduced by the Indian banks. Under this practice a person who needs financial assistance instead of applying to his banker to advance him money requests him to permit a bill to be drawn upon him (banker), by a person whom he (applicant) owes money, and to accept the same, and that he would supply him with requisite funds before the maturity to enable him (the banker) to retire the acceptance. Of course the banker would satisfy himself that he is not running any serious risk in undertaking such acceptances. As a rule he takes suitable security before lending

his name to such bills. He charges commission about one-eighth to one-fourth per cent. for this type of credit. The system of bank acceptances can be employed both for internal and external finance. The bills being accepted by a banker are regarded as first-class security and readily discounted or advances made against them. The chief advantages are: (i) the Customer has not to pay the interest charges but only a nominal commission; (ii) the banker does not advance any actual money but simply undertakes a deferred obligation to pay it; (iii) at maturity the customer supplies the banker with funds to pay up the bill and the banker has not to make cash arrangements on his part to meet the obligation; (iv) the banker is able to supply more credit than what is possible on the basis of deposits and cash, and thus renders greater services to his customers.

Advances

This term is self-explanatory. Besides discounting bills the banks grant loans, and cash credit or overdraft limits. In the former case money actually passes from the banker to the borrower and begins to earn interest; but in the latter case, simply an arrangement is completed whereby a customer can overdraw his current account up to the limit sanctioned. Thus in the case of cash credit or overdraft accounts the banker undertakes an obligation to supply money on demand up to the

stipulated limit. Arrangements like this increase his demand liabilities, without the certainty of earning interest, unless the money is actually used. But they are distinctly beneficial to the borrower, because he pays no interest as long as he does not utilise the money, and at the same time he is sure to get money when he wants it. Some banks to compensate themselves for the loss of interest on the increased reserves, which they maintain on account of such demands, insist on half or minimum interest clause by which they earn interest at least on a part of the limit sanctioned, even if it may not be utilised to that extent. This is logical on the part of the banks and as a rule the banks should impose it upon the borrowers. But it is undesirable to legislate anything in this respect as there may be individual circumstances requiring special arrangements. The banks should, however, strengthen their cash reserves in respect of undrawn limits on the same basis as if they were deposits payable on demand or demand liabilities. A provision for this is made under the section "Cash and Bank Balances."

Three sound maxims which a banker should observe when making advances are: (i) Safety, (ii) Liquidity, and (iii) Diversity or Distribution of risk. It is difficult to legislate on (i). The bank directorate which contains representatives of depositors should be free to judge whether the security which they are getting is safe and sufficient or not. The Bank Examiners, referred to later, will serve as a check upon the management's estimate of the value of securities. It would, however, be a very desirable thing if the Bank Law would

require banks to demand "loan application" from the borrower where full financial statement of the applicant should be disclosed. Many a time it happens that the directors *bonafidely* make advances to people who are heavily involved. Some borrowers are so smart and active that they hide their true position very cleverly. They take advances from many people and many banks with the result that often all of them meet with losses. It is to prevent honest bankers from such sharks that the law should require every borrower to disclose his financial position, audited by a bank's nominee, if the advancing bank may so require. Penalty should be prescribed for borrowers knowingly making false statements. Beyond such safeguards it is difficult to impose restrictions on the discretion of directors.

Coming now to the second maxim, "Liquidity," we have dwelt on this point in the last section and suggested some measures. Ordinarily a prudent bank would invest much more in liquid channels than what has been suggested; but as the law has to be framed to meet all requirements and circumstances, the minimum provision already suggested is quite safe. Advances on the security of merchandise which form an appreciable portion of commercial banks' advances are also liquid in a sense. The advances which cannot be called liquid are those secured by immovable properties or such other not easily realisable assets. It is advisable to prescribe some checks in this direction. It would be sufficient if provisions are made whereby banks are restrained from investing more than 20 per cent. of their advances or more than their

paid-up capital and reserve, whichever is less, in advances secured by immovable properties, and also from contracting to advance for more than five years. The banks should, however, have power to renew such advances on maturity if their position is safe and if the borrowers are solvent. It is likely that at times banks are obliged to accept security of mortgages to secure advances originally made, and with good intentions, on some other security. If in such circumstances the limit above suggested is increased, the banks should be given one year's time or any further time, as the Banking Council may sanction, in view of special circumstances of any bank, to bring such advances within the prescribed limit. Such banks should, however, not distribute their annual profits unless the business is brought within the limit.

The third maxim "Distribution of Risk" is very important. Many instances are available where banks have failed because they had advanced a good portion of their funds to a single person or group of persons connected with each other, who were unable to meet their liabilities. If the same adverse change occurs in the private or personal fortunes of such borrowers the banks are sure to be hit hard and experience anxious times. Even if such advances are not what are known as "personal" advances, *i.e.*, depending upon the personal respectability and standing of one or more borrowers jointly and severally, but secured by some tangible security, in the declining or panicky market it is very difficult to unload such security and to turn it into cash to meet the demands of panicky depositors. It is thus of very great importance to prescribe some checks in this respect.

In individual cases or in emergent circumstances the Banking Council may permit exceptions but generally the following limitations should be observed.

- (i) Not more than one-tenth of the paid-up capital and reserve should be advanced to a single individual, firm, person, corporation, or to a member, director or partner of a company collectively with other connected persons and the company.
- (ii) Not more than 20 per cent. of total deposits should be advanced upon the same class of security, unless the Banking Council may waive or vary such limitations in the case of any particular types of security or from time to time to suit special circumstances or requirements.

[The most recent example of how banks get into difficulties by violating the principle referred to above is that of the Bank of Taiwan. The bank is reported to have advanced very large sums to Suzuki and Company. The latter got into financial embarrassments which reacted upon the position of the bank, ultimately resulting in the Japanese banking crisis. As already mentioned elsewhere, it was the intervention of the Japanese government which came to the rescue of the banks. Up to the moment of writing, it is not definitely known whether the banks have really come out of the difficulties. For, although the moratorium is removed and the Bank of Japan has made large advances to banks, the depositors are still said to be panicky and nervous. As soon as the banks re-opened their doors the people began to withdraw

their deposits. The instance shows how difficult it is to keep up public confidence, once a bank begins to loose it, and why it is absolutely necessary for banks to conduct their business according to recognised canons of banking.]

Other Investments

Banks are sometimes obliged to invest their funds in bonds, shares, property, etc. If the limitations imposed upon their advances should be followed in the case of such investments also, so as not to disturb the conditions for advances and investments as a whole, the banks would be working on the right side. As a rule the banks should not invest in buildings and properties unless they are required for their habitation. But in that case also they should be bound by law not to invest more than 50 per cent. of their paid-up capital and reserve in such purposes. If they are required to purchase some properties to safeguard advances already made they should be permitted to do so, even if such purchases would make them exceed the above limit. But they should be required to sell off such properties within five years of the dates of such purchase. Sometimes banks are obliged to purchase their own shares to secure advances originally made with good intentions. In such cases purchase of such shares should be permitted but they should be sold off within six months of the date of purchase.

The Banking Council should have power to prescribe any other limitations which they may deem necessary either generally or in the case of any particular bank where the Bank Examiners' report may warrant observance of special conditions.

German and other continental banks engage in what are known as "Syndicate operations." They underwrite industrial and other flotations. They finance an economic enterprise *e.g.* an industrial or mining concern, either by subscribing to its capital or by making advances. If an enterprise is of more than ordinary size a number of banks combine together and finance the project. Different banks have specialised more or less in different branches of industry as well as marked different territories for their operations. If any bank comes across a promising proposition which primarily relates to its industrial or territorial sphere it finances it; but if the proposition is very large it allows other banks to join it in the undertaking. Transactions of this kind are called "Syndicate operations." Banks participate in such operations both on interest and profit sharing basis. It is undesirable to permit Indian banks to engage in such financial operations at this stage, because in the present period of their infancy they could not successfully engage in long term credit business without running a serious risk of collapse. When dealing with industrial banking we shall suggest means of supplying such kind of credit and finance. But if after a number of years when the banks have been firmly established and the people are used to banking habits and familiar with banking methods and functions, the Banking Council may permit banks, either generally or in particular cases to undertake "Syndicate operations" within any limits that may be considered desirable.

Agency

There should be no restrictions on the agency business of banks. There are no financial obligations

involved in such transactions and there is no need of any special legislation on this point. The banks are a great instrument in popularising investments. The present system of double charges by way of commission to banks and brokerage to stock-brokers is rather too much for the investing public. In London there is only brokerage payable which is divided half and half between the banks and the brokers. On the continent banks are members of the Stock Exchange which greatly facilitates execution of clients' orders relating to the buying and selling of Stock Exchange securities. The banks collect cheques, bills, bonds, interest, warrants and similar other items which also increases their serviceableness to the country.

Safe Custody

The banks should be free to accept securities and articles for safe custody from their clients. This business should find greater scope in India as time passes. Some people are in the habit of entrusting their valuables to their friends and relatives, especially during their absence from station, with the result that in some cases their trust is abused and they do not get back what they deposited. Again whenever there is an epidemic or a riot in a village or a town and some inhabitants leave it temporarily, they do not know of any safe and secure place where to deposit their precious things. Not only do they experience great difficulties but often they suffer losses of the nature referred to above. As banks begin to be established and known for their respectability, people would very much appreciate their services in this respect. In big cities separate safe deposit vaults may be possible and necessary

but in the interior banks would remain the only suppliers of such services.

Trust Business

Banks on account of their continued existence and respectability are better able to undertake functions of a trustee than a private individual. Moreover if a number of people entrust such work to them they can engage specialists on their staff to execute commissions requiring special knowledge. Thus the various trusts would be managed more efficiently than what would be the case if each were administered individually. Also the management would be more economical because the overhead, superintending and working charges would be distributed. American banks first undertook this type of business and the people there have found their services in this direction very advantageous. In England, the "Big Five" banks have either opened "Trust" departments or started subsidiary companies, wholly owned and managed by them, to do trust business. In India banks have not devoted any attention so far to this business but it does not deserve to be neglected any further. The Indian Bank Law should permit them to engage in it.

ACCOUNTS AND AUDIT

All the banks should publish an abridged statement of their assets and liabilities at least once a month. Probably nothing leads to greater confidence in a bank than the publicity of its affairs. Further, an obligation of this nature will make the bank authorities conscious of frequent public gaze and as such serve a useful check on its general business. The statement should be exhibited in a prominent place in every office of the bank. The form of the statement should be as under :

X. Y. Z. BANK.

Statement as at the end of.....19 .

| LIABILITIES. | | ASSETS. | |
|-----------------------|-----|------------------|-----|
| | Rs. | | Rs. |
| Subscribed Capital | | Cash ... | |
| Paid-up Capital ... | | Cash in hand | |
| Reserve ... | | Cash with the | |
| Deposits : | | Central and | |
| Current ... | | “ Clearing ” | |
| Savings Bank ... | | Banks ... | |
| Fixed ... | | Cash with other | |
| Other Liabilities ... | | banks ... | |
| | | Investments | |
| | | in liquid | |
| | | securities ... | |
| | | Other invest- | |
| | | ments ... | |
| | | Bills discounted | |
| | | Cash Credits and | |
| | | Overdrafts ... | |
| | | Loans ... | |
| | | Other assets .. | |
| Total ... | | Total ... | |

CERTIFIED that the above statement is in accordance with the bank's books kept in the ordinary course of business, represents true and correct state of affairs and does not violate the Indian Bank Law.

Accountant.

Manager.

At the end of every half year the banks should publish their Balance Sheet and Profit and Loss Statement which should contain more detailed information. It would be sufficient if the banks continue issuing these statements in the form in which the Indian Joint-Stock Banks are publishing their balance sheets at the present moment. The statement should contain a certificate similar to the one appended to the monthly statements. They should be signed by the Accountant, General Manager, at least three directors, one of whom must be a director on behalf of the depositors and the company's auditors.

The banks should appoint in their annual general meeting, auditors who should audit the bank accounts. The half-yearly balance sheets should be scrutinised by the auditors and signed by them.

GOVERNMENT EXAMINATION AND CONTROL

The banks should be subjected to examination on the part of the Bank Examiners as fully explained in a preceding chapter. The bank management should be bound to carry out any instructions that the Comptroller may send on perusal of examination reports or otherwise, subject to the right of appeal to the Banking Council. The Banking Council should be the final authority on the practical administration of banks whose orders should be obeyed by all the banking companies. If at any time the conduct or business of any bank appears in the opinion of the Banking Council to be grossly objectionable or against the public policy or dangerous to the country's banking and economic interests, the Council should have power to cancel the registration certificate whereupon its business should stop forthwith. The Council

should even appoint its liquidator if that be considered necessary in the general interests.

The Comptroller should have right to enforce submission of any returns, both regularly at stated intervals and on surprise occasions. He should have power to prescribe time, from the date of demand, within which such "surprise" returns should be submitted—the period within which such a "Call" is to be satisfied should, however, be not less than one week.

SAFETY FUND

The banks should contribute 5 per cent. of their net annual profits to a fund called "Safety Fund" which should be administered by the Banking Council. The object of the fund would be to enable grant of assistance to banks in times of panic or distress, whether by loans, with or without interest, or otherwise, or to ameliorate the conditions of bank creditors, if by a bank failure they are affected very terribly. It should be left entirely to the Banking Council to determine whether any assistance from the safety fund to any banks is necessary or not, and on what terms such help should be given. The Safety Fund schemes have been current in other countries also. The chief argument advanced against the proposal is that it makes banks somewhat indifferent and benefits those who are careless or unwise at the cost of those who are prudent. There is some truth in such an allegation but when we are prescribing sound checks on bank working, both in the shape of banking law and government examination, the establishment of the Safety Fund would be in the nature of insurance reserve to help banks as a whole to tide over abnormal circumstances. The premium (in reality this

tax amounts to it), is for mutual benefit. Possibly only small banks may be benefitted by such assistance directly but the indirect effect even on big banks would not be little. Bank failures spread like wild conflagration; and if timely assistance can stop the disastrous fire at the point of start the others would be saved from the scorches, possibly destruction, and thus be greatly benefitted. The small contribution depending upon the net profits is nothing in comparison to the emergency provision that will be created as well as to the amount of confidence which such a fund will infuse in the depositing public. If the fund reaches an appreciable figure and no large demands are made upon it, the Banking Council may absolve banks from this contribution after they have paid fifteen or twenty annual contributions, with power to re-impose it if future circumstances may warrant such a step in the general banking interests.

CLEARING HOUSES

It has been mentioned in the chapter on the Central Bank that that bank should be responsible for the establishment of bankers' clearing houses throughout the country. All banks registered under the Indian Bank Law and others as may be approved by the Banking Council, should be members of the local and provincial clearing houses. The object of such houses is to economise transference and handling of actual cash. The banks will keep their accounts with some bank where mutual transfers will take place. In places where the bank of issue has branches, other banks will keep accounts with it for clearing purposes; but at others, some one of the local banks can be selected by the banks themselves, where accounts could be kept and payments cleared;

or if that be not possible, mutual settlement could be made through the nearest branch of the bank of issue. The important provincial branch of the bank of issue should clear for other banks working in the province and keeping accounts with it, both provincial and inter-provincial items. This would facilitate internal exchange operations of this country without involving undue currency movements. To illustrate clearing settlements of the description given above let us suppose that a bank "B" in Amritsar wants to collect a cheque drawn on a bank "C" in Surat. The bank should send it to the branch of the bank of issue at Lahore, which would be provincial clearing centre, and which would credit the amount to the account of "B" bank in its books. The Lahore branch would send the cheque to its office in Bombay which would debit the amount to the account of "C" bank in its books and send the cheque to the bank at Surat. If the cheque were payable say at a place within the jurisdiction of the Lahore branch of the bank of issue the amount would be credited to the "B" bank and debited to the "C" bank in the books of the Lahore Branch.*

The system of mutual settlements would not only considerably reduce currency movements but it would also avoid great strain upon the bank cash balances and make it possible for banks to carry on their work with smaller cash reserves, which means that banks would be enabled to extend greater credit. If credits are being collected at the same time

* Amritsar and Lahore being both in the Province of the Punjab, clearance would first take place in Lahore. Similarly Bombay and Surat are in the same Presidency and clearance would take place for items relating to that Presidency in Bombay, the seat of Bank of Issue's branch.

when payments are being made, the banks would have to pay or receive only the net balance due on such settlement. If this were not the case the banks would usually first make arrangements for the expected payments and then recoup with the collections.

It is desirable that clearing services should be rendered by the bank of issue gratis, no matter where the items are payable. The only condition which should be insisted upon is that the banks should maintain sufficient balances to permit such debits. If, however, this be not possible a small charge for inter-provincial operations could be prescribed and/or the the system of value-dates could be introduced, whereby actual credit would be available a few days later, depending upon the period of transit.

GENERAL

Examination-Tax

The establishment of a new Government banking machinery consisting of the Comptroller, the Bank Examiners, their staff, etc., will imply large new expenditure. It would be unfair to make the general tax-payer pay for all such expenses. The administration will primarily benefit banks by creating great confidence in them and thereby increasing their business. It is quite reasonable that they should pay special tax for the establishment of a department meant for their benefit. If the banks pay special tax of 3 per cent. of their annual profits a good sum will be collected which will materially assist the general revenues in defraying the new expenditure. Possibly the "examination" tax may not suffice in itself to meet all the expenditure, but as State intervention will in the long run lead to increased

prosperity of banks, which would bring more income tax, there would ultimately be no loss to the general funds. But even if there were some loss to the State, we think it is worth while to bear it in the general interests and in the interests of public welfare.

The income-tax payable by banking companies should be calculated on the residue, after deducting "Safety" and "Examination" taxes from the net profits.

Penalties

There are certain provisions of the act which are always capable of compliance, whereas others may happen to be irregular through no fault of the bank management. In the former case a penalty of rupees one hundred per day should be imposed upon the officer of the bank deliberately and wilfully neglecting the law. If a bank at any time is not able to maintain the cash percentage, already referred to, it should not make any further advances or distribute any profits unless the deficiency is made up. Also it may be liable to a penalty on the deficiency at the current rate of discount, regarding the deficiency as a day to day advance to the bank.

Similarly when an officer whose duty it is to supply the returns to the Comptroller fails to do so within the prescribed period he should pay the same fine.

Voting Power of Banks

For the purpose of electing members to the Banking Council and for such other purposes where representation of banks is necessary, the voting power should be determined by the following scale.

| TOTAL OF PAID-UP CAPITAL AND RESERVE. | NUMBER OF VOTES. |
|---|---------------------|
| Not more than Rupees one lakh ... | 1 |
| More than one lakh but not more than Rupees ten lakhs | 2 |
| " " ten lakhs but not more than Rupees twenty lakhs | 3 |
| " " twenty lakhs but not more than Rupees thirty lakhs | 4 |
| | |
| " " eighty lakhs but not more than Rupees ninety lakhs | 10 |
| " " ninety lakhs but not more than hundred lakhs ... | 11 |
| For every additional ten lakhs or part thereof | 1 |

NOTE.—Business of a bank is generally in proportion to its capital and reserve, and if its voting power is made to depend upon these two factors, the representation would be fair and accurate. If, however, the incidence of banking business is desired to be calculated in each case we might suggest that additional votes depending upon deposits may be allowed, each ten lakhs of rupees of deposits or less entitling one additional vote *e.g.* deposits of 15 lakhs would entitle two additional votes, deposits of 105 lakhs would entitle 11 additional votes and so on.

Winding up

The Banking Council should have power to order winding up of any bank that in their opinion does not work satisfactorily and is not capable of reformation. It would be desirable if the Comptroller of Banks be empowered to veto appointment of any liquidators that may be appointed by the bank directors or shareholders, in case of voluntary or compulsory liquidation, and even to take the liquidation under his supervision. The object of

such control is that bank liquidation would affect the outstanding credit in the market and in the public interests such credits should be collected as prudently as possible. If the Banking Council has some hand in such liquidation affairs they might make smooth arrangements which would not upset the market.

Date of Operation

It may be difficult for the existing banks to obey the Indian Bank Law immediately in all respects on its introduction. A five years' period may be granted to them within which to bring about the requisite changes which are not capable of immediate observance. But once a bank is capable to conform to the law in its entirety it should thence forward observe it always. The new banks that are established after the passage of the act should follow it from the very commencement.

CHAPTER X

FOREIGN BANKS

Necessity of Control over foreign banks—Cunliffe Committees' views on the activities of foreign banks in England—Argument of Imperial brotherhood—Conditions generally imposed—Restrictions suggested : License ; Penalties for not taking license ; should be subjected to appropriate sections of Bank Law ; should submit returns and be controlled by appropriate authorities ; Indian advisory committees ; Practice in France ; Caisse de Dépôts et Consignations ; Ordinary and special taxes payable.

If special law and control are necessary for the banks of the country there is greater reason that some sort of check and superintendence should be imposed upon the establishment and activities of foreign banks *i.e.* banks incorporated in other countries. Whatever chances there may be for the people to know about the real position of the Indian banks, such opportunities would be practically non-existent in the case of banks whose head offices are situated in other lands or whose main activities are controlled from other centres. This is a sufficient reason in itself why State intervention in their case is more necessary. Moreover, if they were left quite free and unfettered that would decidedly be to the great disadvantage of the indigenous banks which have suffered so long from their unequal competition and whose development is so vital to India's interest. When even a country like England which is so power-

ful in banking, let alone other important countries that impose restrictions on foreign banks, does not tolerate the freedom with which such banks can open offices or connections there, it is difficult to understand why India should be so generous at the cost of her own interests. The Cunliffe Committee appointed to look into the question of "Currency and Foreign Exchanges after the War" in their final report said: "Several of our witnesses have called attention to the conditions under which it is open to foreign banks to establish themselves in this country. We suggest that this is a matter which should receive the early attention of His Majesty's Government." This report was signed unanimously by all the members including the present Finance Member of the Government of India, Sir Basil Blackett who was then Controller of Finance, British Treasury. Sir Basil has done so much for the financial welfare of this country. We hope he will realise his duties and responsibilities to India in this direction also and give his serious thought to the question of determination of conditions under which only should the foreign banks be permitted to establish themselves in this country. Their unrestricted existence is a danger to the country's welfare. They occupy such a prominent and controlling position in the Indian banking field that unless limitations are imposed upon them it is futile to think that the indigenous banking system can be developed at the pace and to the extent which India so badly needs.

We are conscious that some would argue that India is a part of the British Empire and no discrimination should be made between banks as long

as they belong to the Empire. We would have been happy to advocate this course if the existing English banks in India had been actuated by the same principles of Imperial brotherhood and not merely carried on their work with a view to exploit this country against her best interests. If other parts of the Empire had extended the hand of fellowship we would have been simply too glad to accept it. But when experience has demonstrated that no such considerations influence their working it is difficult to recommend any preference. Even the Bank of England refuses to extend rediscounting facilities to the Indian banks simply on the ground that they are not registered in England. This was actually proved in the case of the late Tata Industrial Bank. All other self-governing dominions and colonies are free to chalk out their own economic destiny as best as they like and the same principle should govern our economic activities. In the name of what fairness and equity are then we being asked to look to Imperial considerations when firstly they are denied to us and secondly they sap the very foundation of our economic structure? If change occurs in the attitude of other members of the Empire we shall be only too glad to respond to it. But even then the Imperial considerations should not be the sole determining factor. They should be paid attention to only as long as they do not conflict with the national interests. Whenever they clash, the national interests should naturally have first right. In the existing circumstances banks belonging to the other parts of the Empire should not, however, be distinguished from the foreign banks nor any preference shown to them.

Conditions which countries backward in banking usually impose upon the establishment of foreign banks are : (i) That they should conform to the same principles to which the native banks are subjected ; (ii) They should take out a license ; (iii) They should pay capital tax ; (iv) They should pay special taxes on profits and business turnover. Examples of such measures are found in the laws of Italy, France, Spain, Portugal, etc. Is it not really strange that if an Indian bank went and opened branches in any of those countries it would be subjected to their restrictive measures but if any of their banks wanted to establish itself here, it would be at absolute liberty to do so without observing any limitations which its country imposes upon foreign banks ?

We give below important provisions which should be incorporated in the Indian Bank Law to control activities of foreign banks. We do not think that there is anything in these provisions which affects fundamentally business principles of banking which these banks carry on ; but if it be considered that some conditions cannot be immediately introduced without considerably disturbing their existing interests or dislocating commercial and banking activities, the Banking Council should have power to keep in abeyance operation of any of the provisions of the law or to permit exceptions in any individual cases. Further, if any of the existing foreign banks are prepared to reorganise within a period of three years giving reasonable representation to Indians in the matters of capital, management and directorate, of which the Banking Council shall be the sole judge, they may be consi-

dered as banks registered in India for the purpose of the application of the Indian Bank Law. But all new foreign banks which want to open offices in India hereafter should observe the law from their very commencement.

(i) No bank founded on the principles of limited liability but not incorporated under the Indian Bank Law should be permitted to carry on banking business in this country, unless it has applied for and obtained a license from the Comptroller of Banks for doing such business. Application for such license should disclose all particulars concerning such a company as well as its chief office in India and the chief officer who will fully represent the company in this country. If its paid-up capital be less than that prescribed for "Overseas Banks," or if its constitution be repugnant to public policy or violates any of the laws of Indian legislature or if its establishment in India be considered undesirable by the Banking Council on account of any other reasons, which the Council shall not be bound to disclose, no license should be issued. A register should be maintained in which names and particulars of banks issued licensing certificate should be entered.

(ii) If any foreign banking company opens an office in India contrary to as provided for above, the company and its officers

should be liable to the following penalties :—

- (a) The company and its shareholders should be considered as undertaking unlimited liability to the people of this country.
 - (b) Every officer of the company should be considered as personally liable for any amounts due by the company to the people of this country.
 - (c) The company should pay a fine of Rs. 500 a day for the period during which it is working without a license.
- (iii) All foreign banks should pay charges and fees for obtaining license on the same scale as the Indian banks pay for obtaining registration certificate. They should pay "Security Deposit" of 10 per cent. of their paid-up capital or any shorter sum as may be fixed by the Banking Council in each individual case.

This deposit should be primarily held for the benefit of Indian constituents. It should be refunded when a foreign bank closes its office in India and its liabilities to the Indian public are fully satisfied.

- (iv) All foreign banks should observe provisions of the Indian Bank Law governing bank working in India, with any modifications that may be considered necessary in their case by the Banking Council, provided however such a modification does not give them any advantage whatsoever over the country's banks.

- (v) All foreign banks should submit returns and publish monthly statements of accounts (at least of the Indian business) and balance sheets as are required in the case of Indian banks.
- (vi) All foreign banks should be controlled and examined by the Banking Council, through the Comptroller and Examiners of Banks, as is recommended in the case of Indian banks.
- (vii) All foreign banks should appoint Indian advisory committees or local boards to represent Indian interests. One-third of the members of such boards should be elected by the depositors on their Indian books and residing in India as provided for in the case of Indian banks. The remaining two-thirds should be appointed by their respective boards of directors, with the condition that at least one-third of the total members should be statutory natives of India.

The above conditions are based on the fundamental principles that all activities in India should be controlled from the Indian view-points and that foreigners should not have any advantage over the Indian Companies simply because they are foreigners. Laws of all countries are not alike. If any company registered in a country, where laws relating to joint-stock banks or companies are loose or lax or less strict, were to be allowed

to establish itself here without any check, such a company would naturally have a great advantage over the Indian banks.

Laws of France even require that a foreign company must obtain recognition by the Minister of Finance, of a French Representative, who shall be personally responsible for the taxes and duties payable, or if preferred a sum of money can be deposited with the "Caisse de Dépôts et Consignations,"* as guarantee, the amount of which is fixed by the Minister of Finance.

* The "Caisse des Dépôts" is a public State department entitled to receive, hold and remit to parties after justification of their rights, sums or securities which have been held over in virtue of a judgment or administrative decision. It also is entitled to receive deposits made voluntarily—for instance, when a debtor wants to settle his debt and the creditor refuses the offer made to him.

The "Caisse" is also entrusted with the supervision of funds intended for special services, such as the "Caisse National des Retraites" (Old age Pensions), the "Caisses d'Epargne" (Savings Banks), the "Societes de Secours Mutuels" (Benefit Societies), and various State Insurance Funds, etc.

The "Caisse des Depôts" is directed by a General Manager, appointed by the State, assisted by a committee of supervision whose principal task is to see that the funds of the "Caisse" are not diverted from their proper use and are not, for instance, employed to supply the Budget. This committee includes two Senators, two Deputies, two Members of the "Conseil d'Etat" (State Council), the President of the "Cour des Comptes," the Governor of the Bank of France, a delegate of the Paris Chamber of Commerce and the Comptroller of the Currency.

The funds of the "Caisse" are principally supplied by the "Caisses d'Epargne" (Savings Banks), on which it pays a fixed interest, and are mainly employed in "Rente," Treasury Bonds and in loans to Departments, Communes and Public Institutions. The "Caisse" has also a current account with the Treasury.

(viii) All foreign banks should pay all taxes to which the banks of the country are liable, including the "Safety" tax. As regards the income and allied taxes which depend upon the amount of profits, they should be paid either on the total profits or on such proportion of total profits or on such amount fixed in advance from time to time, as the Board of Inland Revenue may prescribe in individual cases.

In the case of foreign companies, specially banks, the verification of income accruing in India is extremely difficult. Main income of banks is derived from interest heads or sources depending upon interest; and the Indian branches of foreign banks can conveniently, without any difficulty whatsoever, reduce such income in respect of operations or investments in India, by showing money received from foreign branches as loans taken at high rates of interest. We do not mean to say that any respectable bank would stoop so low as to have recourse to such devices, but the possibility of abuse is there, which the law has to safeguard against. In France the law is: "If a foreign company, not issuing shares, should exploit an establishment in France and invest all its capital therein, it would be liable to the same taxes and duties as French companies on total income. But if the total capital is not used for the business in France, the amount

payable as income-tax is fixed by the Minister of Finance which forms the basis for the determination of other rates and taxes." A safeguard of this nature is extremely desirable in India.

(ix) Besides the rates and taxes which foreign banks should pay along with the Indian banks as referred to above, they should pay the following special taxes :—

(a) Capital tax of 4 *per mille* (per thousand) on the total paid-up capital.

(b) Loan tax of 10 per cent. on the interest paid on loans and deposits contracted in India.

(c) Exchange tax of one-tenth *per mille* (per thousand) on the turnover in the foreign exchange business.

The object of the imposition of the above taxes is to give a small measure of protection to the indigenous banks from the keen competition of foreign banks which have had a long start in the banking business. The banks would be able to bear them lightly and their business would not be hampered in any way. These measures are current in other countries also. Capital tax is levied in Italy, Spain, etc. Loan and Exchange taxes are levied in France. Proceeds of such impositions should not be taken to revenue but utilised for the development of the country's

banking and kept at the disposal of the Banking Council.

- (x) If at any time the conduct or business of any bank, which has been already granted a license, appears in the opinion of the Banking Council to be grossly objectionable, or against the public policy, or against the interests of the depositors, or dangerous to the country's banking and economic interests, the Council should have power to cancel the license whereupon its active business should stop forthwith in this country. If considered necessary in the general interests, the Council should even appoint a Liquidator to liquidate its business in India.

CHAPTER XI

INDIAN EXCHANGE BANKS

Object—Provision under “Overseas Banks”—One strong bank necessary—It should be a combine of Indian banks for foreign exchange business—Imperial Bank’s transformation into the proposed bank—Important points in connection with proposed constitution : Capital, Directorate, Facilities at the bank of issue, Business, Branches, Taxes, Profits, Management, Examination, etc.—Remarks explaining the above.

This class of banks will transact banking operations in connection with India’s foreign trade. Their activities come under commercial banking which covers both inland and foreign trading business, but as financing of foreign trade involves greater complications and risks due to varying currencies, varying laws, foreign languages and establishment of foreign branches, it is advisable that they should be treated as a separate class in themselves. These banks are not to be confounded with the existing Exchange Banks which as already referred to can be fitly described as foreign banks. The Indian Exchange banks should be of Indian origin and registered in India under Indian Acts.

Provision for the establishment of this type of banks has been made in the “Indian Bank Law” where such banks are described as “Overseas Banks.” Thus any Indian bank satisfying provisions prescribed in respect of such banks can open branches outside India and do exchange business.

In the present conditions of India, however, there should be one strong banking institution which should mainly devote its activities to exchange business and should be in a position to successfully compete with the existing foreign banks which have practically captured the whole of this trade. Examples of such special institutions are current in other countries also. The Indian banks should co-operate with it in every respect, so as to make it a thorough success. It would be advisable if the ordinary banks devote their main attention to the business in the country and allow the contemplated Exchange Bank to do all the foreign business. Concentrated and solid action on the part of one important and powerful institution is much better than the divided activities of a number of smaller concerns. The proposed bank should have Indian branches only in the port and big towns. At other places, in India, it should work through agency arrangements with other banks. It should be free to open branches at any place outside India. In the matter of agency arrangements it should not give the sole monopoly to any one particular institution but should so distribute it amongst the various important banks of the country as to get the happy support of all.

In order to fully interest the ordinary banks in the proposed Exchange Bank a portion of its capital should be reserved for subscription by them. Another portion should be reserved for subscription by the bank of issue, if necessary, and the rest offered to the public. The bank should be more or less a combine of the Indian banks for the purpose of doing foreign exchange business just as

Lloyds and National Provincial, Anglo-Italiana and Barclay's Colonial banks represent foreign banking organisations of some of the English banks.

An institution of the nature referred to above should have special privileges and special support of the bank of issue. For these reasons it is desirable that it should not be incorporated under the ordinary law but established under a special charter.

We have indicated in a previous chapter possibility of transforming the present Imperial Bank into the proposed Exchange Bank. A portion of its ordinary commercial banking business can be taken over by the existing banks and by the new banks that may be formed. At many of the places where the Imperial Bank has branches there already exist important banks and the stoppage or reduction of the Imperial's ordinary banking business there would not be felt in any way. At many of the smaller places the opening of the Imperial Bank's new branches has simply created more than requisite banking facilities. Cessation of such connections would not injure any one. The Imperial can continue to receive private deposits as hitherto. But its activities in India should be restricted to the most important places, which are the chief centres of foreign trade, both inward and outward. At other places it should work through other banks. If necessary it can make arrangements with the banks to which it transfers branch business to keep deposits with it, or give loans to it, within certain limits, at stated rate of interest, for a number of years, so as to continue its present advantage of branch deposits to some extent for the purpose of financing its future activities. It should open branches

outside India first in the most important places which have business dealings with India and then in other foreign towns. Its capital should be naturally reorganised so as to permit representation of other banks. The existing shareholders should get back the difference between the capital reserved for them and the surplus which the valuation of its assets may disclose. Of course, if the shareholders do not agree to the transformation of the bank into the Indian Exchange Bank it is their look out. In that case the Indian banks should combine to start a common Exchange Bank as already referred to. But we think it is advantageous to the shareholders of the Imperial Bank to agree to the transformation. A bank of this nature has immense potentialities.

We suggest below the important points which should be incorporated in the constitution of the Indian Exchange Bank, whether the Imperial Bank is transformed into it or a new organization is formed.

- (i) The Capital* of the Bank should be Rs. 10 crores divided into one lakh shares of Rs. 1,000 each. Half of the Capital should be reserved for public subscription and the other half for the banks of the country. Out of the latter portion one-

* In order that the representative Exchange Bank of the country should command requisite confidence in the outside world, which is so essential for its successful working, we have recommended such a large capital. The bank will need deposits and discounting facilities in foreign countries and they will not be forthcoming to the extent desired and necessary, unless there is sufficiently large capital at its back. If, however, the figure of Rs. 10 crores is considered too high it may be reduced to Rs. 7½ or Rs. 5 crores.

fifth may be subscribed by the bank of issue if necessary. Allotment of shares to banks should be made in proportion to their paid-up capital and reserve. If the shareholders of the Imperial Bank agree to its transformation into the Exchange Bank the portion meant for the public should be allocated to them.* Only half of the above capital should be called in, which should be paid up as soon as the allotment is completed. The other half should remain as the reserve liability to be only collected if the bank is faced with a serious or critical situation. Whether a situation is critical or not it should be referred to a Committee consisting of three persons *viz.*, Chairmen of the Banking Council, the Bank of Issue, and the Indian Exchange Bank, whose decision by majority should be conclusive and final.

- (ii) The Board of Directors of the bank should consist of 12 persons appointed as under :—
- (a) Three to be elected by the ordinary shareholders.
 - (b) Three to be elected by the capital holding banks.

*National interests require that the portion of capital meant for public subscription should be mainly allotted to the people of the country. However, as a compensation to the Imperial Bank's shareholders for the withdrawal of the government banking business, as referred to in a previous chapter, we have suggested this portion to be wholly reserved for them. If the Imperial Bank does not agree to play the new role, at least half of this portion of the capital should be reserved for Indians.

- (c) One to be nominated by the bank of issue.
- (d) One to be nominated by other special banks.
- (e) Two to be nominated by the Banking Council.
- (f) Two to be nominated by the Governor-General-in-Council.

The directors should elect their own chairman.

- (iii) The Bank of Issue should give a cash credit limit of Rs. 5 crores on the security of the Exchange Bank's general assets at a uniform rate of interest of 3 per cent. per annum, but not exceeding the bank rate, for at least ten years. If the Banking Council and the Board of Directors of the Bank of Issue decide each by three-fourths majority to increase the limit or extend this period such increase or extension should be permitted.
- (iv) Besides the cash credit limit referred to at (iii), the Bank of Issue should grant a limit of at least Rs. 15 crores for rediscounting its bills at special rates of discount, not exceeding the bank rate, as the Banking Council may decide from time to time. Bills thus rediscounted should be permissible as backing to the notes issued within the limit prescribed in that behalf.
- (v) Acceptances of the bank should be permissible for discounts at the Bank of

Issue and such discounts should not be calculated as a part of the limit referred to at (iv).

- (vi) The bank should be free to rediscount its bills to other banks whether in India or outside.
- (vii) The bank should do every kind of banking business carried on by exchange banks including taking of deposits and loans both in India and abroad. Its foreign branches should do the agency business of the Bank of Issue which should be required to give preference to it.
- (viii) The bank should open branches in all port towns in India and in such other places in this country as may be decided by its Board of Directors subject to the approval of the Banking Council. It should be authorised to open branches in foreign countries as the directors may decide from time to time.
- (ix) The bank should be liable to all taxes to which other banks of the country are liable including the "Safety" and "Examination" taxes--it should, however, be exempted from the "Security Deposit."
- (x) The profits of the bank should be distributed as and in the order shown below :--
 - (a) Ten per cent. to a reserve fund till it equals the paid-up capital. Further contributions to the fund should be

- determined by the Government and the bank.
- (b) Dividend, not exceeding 10 per cent. on the paid-up amount to the shareholders. The dividend, however, should not be cumulative.
 - (c) Ten per cent. of the remainder to the bank of issue for granting cheap credit facilities.
 - (d) The residue to be divided between the State and the shareholders in the proportion of 3: 1. The State's share of profits should be utilised as provided for in the case of its share of profits from the Bank of Issue. The shareholder's share may be either disbursed as additional dividend or accumulated for the purpose of equalising dividends, as the bank's directors may decide.
- (xi) The management of the bank should be through a General Manager who should be appointed by the directors subject to the approval of the Banking Council. Under him should be Deputy General Managers, Branch Managers, and so on. It is not necessary to put restrictions on the nationality of the managers at this stage, because firstly the Imperial's* European staff has to be provided for and secondly the knowledge of foreign currencies, languages

* This is of course on the assumption that the Imperial's transformation is agreeable to all concerned.

and foreign business is essential, for which sufficient Indians may not be presently available. But within a period of 15 years from the commencement at least half of the Deputy General Managers and all the Branch Managers in India should be Indians. The recognised policy of the bank as regards management should be to accelerate Indianisation consistent with safety and sound working. The bank should have at least one Indian in each of its foreign branches from the very beginning.

- (*xii*) It should be one of the fundamental objects of the bank to promote Indian interests in foreign trade and to afford special facilities to Indians engaged in foreign commerce.
- (*xiii*) The banks should be empowered to promote the formation of other exchange banks both under Indian and foreign laws, either in partnership or in alliance with it or on agency basis, to do business with or in any special countries where such separate arrangements may be necessitated by the laws of those countries, or otherwise considered advisable.
- (*xiv*) The bank should be subjected to the general control and examination of the Banking Council and of the Comptroller and Examiners of Banks like other banks of the country.

- (xv) The charter of the bank should be for 30 years in the first instance. Alterations in the charter during this period, may be sanctioned by the legislature if considered by it necessary, provided the same are sanctioned by three-fourths majority of the shareholders and approved by the Banking Council.

EXPLANATION

A brief explanation as to the object in suggesting the above constitution may be necessary. Large capital has been prescribed because a bank of this nature should command not only great confidence in India but also in the outside world. At the same time to enable a reasonable return to the capital holders, half of the capital has been proposed to be kept as uncalled liability. A bigger limit of dividend than that given in the case of the bank of issue is proposed, because the Exchange Bank's business carries greater risks and the profits should increase proportionately to the risks involved. Special facilities at the bank of issue are suggested because it is difficult for an Indian bank to compete with the existing foreign banks on account of their long connections with the world's important markets and important banks where they command cheap funds. The Indian Exchange Bank will take some time before it can hope to get funds and financial assistance in the outside world and in the meantime assistance on the part of the bank of issue is necessary in the national interests. Examples of such assistance are current in other countries. To compensate the bank of issue for supplying cheap credit facilities a portion of surplus profits has

been proposed to be given to it. We have also anticipated difficulties in establishing branches in some of the foreign countries where restrictions are imposed on foreign banks and provided for the formation of new companies to do banking with such countries. In conformity with the general principle to make the Banking Council as the final authority on banking matters in India controlling and examination powers have been reserved to it.

CHAPTER XII

AGRICULTURAL CREDIT

Necessity for agricultural credit—Short and long term credit—SHORT-TERM CREDIT: Purpose—Security for credit—Basic idea of credit unions—Originated in Germany—Raiffeisen and Schulze-Delitzsch systems, their peculiarities and objects—How credit machinery works—Constitution of central credit society—State assistance in credit arrangements, basis for such assistance—Principle of co-operation and joint-responsibility introduces sufficient security—Ministry of Agriculture and Fisheries' Report—Maclagan Committee—Drawbacks of Indian system—Ways and Means to reorganise suggested: Propaganda, Provincial Agricultural banks, their constitution and functions, Agricultural Credit Board, Discounts and rediscounts, Charge on farm wealth, etc.—LONG-TERM CREDIT: Importance of German land mortgage banks—Working explained—How repayments facilitated—Experience of land mortgage banks—Bonds as means of obtaining money—Peculiarities explained—Rentenbank as a means to rehabilitate German currency—Long-term credit facilities in the U. S. A; Federal Farm Loan Act, 1916, Federal Farm Loan Board, Method of working explained, American Government help—Credit Foncier de France and subsidy by French Government—Necessity of mortgage banks in India—Would promote land owning farmers—Plan of organizing land mortgage banks in India: Provincial land banks, Directorate, Management, Business, Facilities at the bank of issue, Government assistance, Profits, Taxes, Land Credit Board, etc.

Specialisation in banking is as necessary as in other economic pursuits. We have already explained how the ordinary banks are mainly concerned with the financing of the movement or of the commer-

cialisation of goods and cannot be expected to satisfactorily supply credit, when the agricultural products are in the course of formation, or when the cultivators require long-term credit to effect permanent improvements of a capital nature. Separate credit organizations are necessary for the latter type of financial operations. Establishment of such special institutions is particularly necessary in this country because her agricultural population is in the main illiterate and the crude form of credit which these people get from the village banker is very costly and insufficient. The last factor is not only greatly responsible for the rural indebtedness, but considerably reduces the economic return to the cultivator from his crops, firstly because a good bit of the value of his crops goes towards interest and/or principal repayments; and secondly, because he is in the hands of credit suppliers who force him to sell his products not when it is advantageous for him to do so, to get the best price, but when they may happen to need back their money, which may not coincide with the time when best prices could be expected, or when they may wish to further profiteer directly or indirectly by the forced sale of his goods. It has been said elsewhere that the village banker does not give his sole attention to banking but combines money-lending with trading and in the latter capacity he is interested to buy as cheaply as possible the village products. Want of agricultural credit organizations is felt much more keenly in India because the *ryot* is in the main not educated nor familiar with the commercial ways of co-operating, marketing, hedging and other similar operations whereby fair return from the pro-

ducts of the land is generally obtained. India's main industry is agriculture and it is a bare act of social and economic justice to arrange for its credit requirements. Japan, America, Germany, France, Italy, and all other countries engaged in agriculture have established suitable agricultural banks. England, where agricultural activity is insignificant and nothing in comparison to her industrial and manufacturing occupations, has been also of late giving attention to the problem of agricultural credit. A special report of the Ministry of Agriculture and Fisheries was issued last year which deals with this problem and recommends concrete measures to supply credit to the farming community. Much more than, is the urgency of the necessity of organising suitable credit machinery for the Indian *ryot*. The Money Lender's Act (or the Borrower's Protection Act, as it is officially described), which some of the Indian provincial legislatures have passed does not solve the problem of rural indebtedness; it on the other hand hampers the supply of credit, however crude or costly it may be, for the carrying on of the cultivator's business. The proper remedy is to remove the necessity for borrowing from the village *banya* by introducing suitable and satisfactory means of obtaining credit.

The problem of the agricultural credit resolves into two sections: (i) Short-term credit, and (ii) Long-term credit. The former is required for such purposes as buying of seeds and manure, personal and labour expenses, water rates and taxes and other current and incidental expenditure which are needed during the period of cultivation and could be repaid after the relative crops are harvested and sold in

the market. The latter is needed for effecting permanent improvements in land, bringing in of new land under cultivation, buying of fresh land, purchasing of large plant and machinery to increase production and so on. As these two kinds of credit differ very much in duration, there should be two distinct types of institutions to tackle the respective problems represented by them.

SHORT-TERM CREDIT

Some of the principal Indian crops like wheat, oil-seeds, groundnuts take six months from the time of sowing to the time of harvesting while other crops like cotton and rice may take eight to nine months for maturing. Thus the duration for short-term credit should not be for less than six months. In some cases credit may be needed for even nine months and the agencies which are hereafter recommended to handle this type of credit should be empowered to grant such longer credits, wherever necessary, to suit special requirements.

Credit or financial assistance is granted against some tangible security. That security may consist of some goods hypothecated to the creditor or may be represented by the personal responsibility and reliability of the borrower, as embodied in one's general assets, either singly or jointly with others. "Character is also a recognised form of security. Most borrowers possess such security and are entitled to credit upon this basis, but to ascertain the credit to which they are entitled requires a more or less intimate knowledge of their personal habits and of their financial and domestic situation." * The agricultural population, as a whole, possesses suffi-

cient character and even property to warrant any temporary financial help for periodical crops and it is this principle of collective knowledge and responsibility of the community which is fully exploited in the institution of agricultural co-operative credit societies which organise short-term credit for the farmers. "The underlying basic principle is that a man's best asset is his own associate's estimate of him, and the advantage of this estimate is obvious. The primary or basic societies are composed of a small homogeneous membership mutually acquainted. Only those known to be honest and industrious are admitted to membership, and loans are made only to such members as have a legitimate need for the money and for productive purposes only."*

"Wherever the credit unions have been properly established and encouraged they have regenerated and accelerated agriculture, commerce and industry or any other department of human activity to which their principles have been applied. They have stamped out usury and raised millions of human souls from the depths of despair to lives of hopefulness and service. They have supplanted shiftiness by industry, improvidence by sobriety; selfishness by neighbourliness; individual effort by concerted action—in fact they have proved to be one of the most potent moral, educational and social forces in the history of civilisation and in the enrichment of the life of the common people."*

Co-operative credit unionism originated in Germany in 1849. Fredrick William Raiffeisen and Franz Hermann Schulze-Delitzsch were the founders of the

* Moulton.

two systems of co-operative credit which are commonly known as Raiffeisen system and the Schulze-Delitzsch system respectively. In the former case a number of farmers residing in the same neighbourhood or locality combine together and form a union. A few well-to-do people also join the union to help their neighbours by increasing the society's credit. Liability of each member is unlimited though sometimes modifications on the principle of limited liability are introduced. The union obtains funds from deposits and borrowings which are advanced to the members according to their means and requirements. Their work is carried on mostly honorarily excepting by the clerical staff which is paid salary. By common consent the richer members are allowed to do the chief executive and superintending work. Raiffeisen banks boast that neither member nor creditor has ever lost a penny by them, and while this is denied it seems at least near the truth. In the case of Schulze-Delitzsch institutions a number of craftsmen residing in a town and working on their own account, the joiners, shoe-makers and so forth, combine together and form a society. They raise a capital of guarantee by obliging each member to take up one share and one only, which is of large value, say £30 or £50 or even much more. This sum need not be paid at once but its payment can be spread over a convenient period. The object of having a comparatively large value share is to commit every member to a long course of saving. On the strength of this capital and the unlimited liability of the members the union is able to obtain a much larger working capital, through deposits and borrowings. The funds of the bank are advanced as loans to mem-

bers. The management of the bank receives remuneration and the profits are either divided or accumulated as reserve. A number of unions of each type combine to form a central, co-ordinating and supporting institution which assists them in their credit operations. "Both the types agree in being generally founded on unlimited liability, but speaking broadly they are contrasted in that the Schulze-Delitzsch banks work primarily, though by no means solely, among townsmen, are based on share capital, work for profit, which they divide on shares, are conducted by paid directors, and confer their benefits not on the very poorest but rather, as their own friends say, on the middle classes: the Raiffeisen banks are designed for the peasantry, are not based upon share capital, neither divide, nor work for, profit, are conducted by unpaid directors and confer their benefits especially on the poor. The Schulze-Delitzsch type is strong in self-help, but tends to commercialism as it grows; the other needs the help of the well-to-do to back up the self-help of the poor, but it tends to altruism and the union of the classes." *

It may be advisable to explain how the credit machinery of co-operative societies works in practical details. After a union is formed the members elect the executive council which manages the affairs. Usually no borrowing members are elected on this council. The council considers applications for advances from the members and fixes credit lines which can be extended to them. Money is advanced on the note of hand but if the amount required be large, joint responsibility of some other reliable

* Encyclopædia Britannica.

person, whether member or non-member, is insisted upon or some other collateral is required. If demand for money is more than can be met from the union's own funds appeal is made by the union to the higher credit society of which it is a member. The work of this society is controlled by a Board of Directors elected by the member unions. The union's application is decided on its merits, keeping in view requirements of other members of the society. Whatever amount is sanctioned, the union endorses the pronotes and bills of its members to that extent and receives the money. To obtain as great a scope for the supply of credit as possible the higher or district societies generally combine to form a central society which extends credit to them and through them to the unions and their members. The management of the central society is carried on by directors elected by the member societies. The central society makes permanent and emergency arrangements with the major commercial banks and the bank of issue, to advance money to it. Thus a substantial structure is built on the slender security of the individual farmers and steady supply of credit is assured to the cultivating community.

Sometimes the central credit society referred to in the last paragraph is not an organization of the member societies but is either a joint-stock bank, some of whose shares may or may not be owned by the credit societies, or a special State bank which devotes special attention to the financial needs of the peasants. Dresdner Bank of Germany is an example of the former type which is practically a central institution for the Schulze-Delitzsch banks. Preussische Central Genossenschafts Kasse is an

example of the State Agricultural Bank to which the Prussian government endowed over 2½ million pounds of public money. Similarly in France Credit Agricole receives special facilities. When the Bank of France's Charter was to be renewed some years back it was compelled by the French government to lend forty million gold francs to the Credit Agricole without interest and also to give about £120,000 *per annum* out of its profits to assist agriculture. The money thus obtained was lent free by the Credit Agricole to "regional" * banks and by them at about 3 per cent. to local societies. In Austria a great deal of similar help has been given. Assistance on the part of State in the matter of credit arrangements to its cultivators is more or less recognised to be one of the responsibilities of the modern government. The basis for such undertaking are economical, social and political. Economical, because the conservation of agriculture, and as a legitimate corollary, the perpetuation of the food supply, is a vital economic problem and so considered by all nations. It is equally a national and a political problem. Even for the progress of industries it is necessary that the production of raw materials should be kept on satisfactory basis with the help of suitable credit assistance. From the social point of view it is desirable to keep vast portion of population engaged in agriculture always contented and free from the revolting bondage of the usurer which may, at any time, result in their rebellion against society. There are many instances in history of agrarian outbreaks.

* They correspond to district co-operative credit societies in India.

The principle of co-operation and joint-responsibility introduces sufficient security for credits extended to cultivators. Moreover, it is very simple both in conception and in detail of working. There is no danger of any abuse of power in granting credit, because the higher societies serve a sufficient check on the lower societies, and through them on the individual members. It is difficult to think that the members of a primary union will be reckless in the determination of their credit lines because if they do so that would be on their individual and collective unlimited liability which would involve their whole fortune. Moreover, credit limits are restricted by the availability of the union funds and in practical application are subject to the control of higher societies. England, however, is thinking of a different plan. The Ministry of Agriculture and Fisheries issued a report sometime back on the question of agricultural credit in England in which they recommended that the machinery of short-term credits should be concentrated in the hands of banks and that to make the bank system as fully effective as possible, the banks should be empowered to take a charge upon the wealth of the farm either in the form of chattel mortgages or floating charges. They further added that the chattel mortgages in favour of the banks only should be legalised and that a central banker's register should be established in which such mortgages or charges should be registered. These recommendations are good in themselves and sufficient to meet the requirements of a non-agricultural country like England, where the main industry of the people is not agriculture nor the demand for agricultural credit, large,

acute or specialised. They are, however, unsuited and cumbrous for countries where majority of the people are engaged in agriculture. For such countries experience has demonstrated that co-operative credit societies based on proper foundation and with proper encouragement solve the problem more effectively and simply. If, however, further safety is needed in respect of co-operative credits a law could be enacted whereby the farm wealth could not be alienated or the co-operative credit obligations should be considered as a prior charge on it just like rates and taxes ; or, if necessary, the government of a country should extend its guarantee to the co-operative credit machinery and in return for this guarantee legalise a charge on the crops in its favour, which should be prior to all other obligations of the farmers. And because the member farmers will be responsible directly or indirectly for the obligations of credit unions the security of their total farm wealth will be ample for the financial assistance supplied to their community. An enactment of this nature will have a deterrent effect as regards loans from money-lenders to farmers and be much more effective than the "borrower's protection measures" lately sanctioned by some of the Indian Provincial Councils.

In chapter II we have given a brief description of the co-operative credit activities as current in India. The Government of India and the Provincial Governments have been devoting their attention to these problems and committees have been appointed from time to time to tackle them. Lately co-operative conferences have begun to be held in this country which discuss problems peculiar to

them. These are hopeful signs. The Maclagan Committee appointed in 1914 to examine whether the co-operative movement was progressing on right lines, especially in its financial aspects and in its higher stages, made some suitable recommendations. The drawbacks of the Indian system are: (i) There is no suitable propaganda to make known and popularise the movement; (ii) No systematic efforts are made for its growth; (iii) Co-ordinating energy is lacking; (iv) In many cases centralising and supporting institutions to which the societies can first look for support are wanting; (v) There is no strict and vigilant supervision which has led to many frauds and abuses; (vi) The co-operative system has not been assimilated into the country's banking system nor are its efforts supplemented by other banks. It is lacking in points of contact with the rest of the system. When its own funds are utilised it has no arrangements whereby it can fall back upon other important banks for the supply of credit; (vii) It requires active and vigorous support of the Government.

No efforts to put the movement on sound and progressive basis can be minimised. Welfare of the agriculturist is a primary concern. We suggest below ways and means to satisfactorily re-organise the credit machinery for the *ryot*:—

- (i) Vigorous propaganda should be carried on both by private and public agencies to demonstrate advantages of the movement to the cultivating class. The village societies and the village authorities, like the *panchayats*, *patel*, local boards, etc., should give their active support

to the progress of the movement. As a preliminary to their devoting energy to this work they should, of course, be first educated by the district and provincial agencies. The higher societies should further popularise the activity.

- (ii) To give confidence to the movement the basic unions should preferably be constituted on the principle of unlimited liability. Well-to-do farmers and *zamindars* of the locality should be influenced in every possible way to join the unions. In order to facilitate establishment of unions the initial value of shares for forming capital, if necessary, should be kept as low as possible. The management of the unions should be in the hands of comparatively richer members assisted and guided by honorary non-members, wherever deemed necessary. They should get their funds from deposits and by borrowing from higher societies. The work of these societies should not be influenced by any motives for profits but restricted to the minimum necessary to meet the expenses. Their primary object should be to obtain credit for members by joint and co-operative efforts, which members may not be able to get singly. If the annual working discloses any small surplus of revenue the same should be taken to a reserve fund.

- (iii) The primary unions should be federated into a district society. The society should possess capital which should be furnished by the members. If necessary, public should be allowed to subscribe to its capital. Return on such capital by way of dividends should be limited to 6 per cent., surplus being taken to a reserve fund. The member unions should not be permitted to take loans except through the district societies. The district societies should accept deposits from both members and public and obtain loans only from the Provincial Credit Society or Provincial Agricultural Bank. The management of the district society should be in the hands of directors elected by the shareholders with a nominee of the Provincial Agricultural Bank. The society should have power to examine affairs of the member unions.
- (iv) There should be in each of the major* provinces a Provincial Agricultural Bank towards which should converge the whole of the provincial co-operative credit pyramid. Its capital should be at least Rs. 1 crore subscribed, half of which should be paid-up. In the first instance the capital should be offered to the district societies as much

* The major provinces are, Bengal, Madras, Bombay, Bihar & Orissa, United Provinces, Punjab, Central Provinces, Assam and Burma. In the smaller provinces either small central societies or small agricultural banks may be formed or the district credit societies may be attached to the Provincial Banks in the neighbouring major provinces.

as they are able to take up, with an obligation to take up a certain minimum amount, and the balance should be offered to the public including other banks. Any portion that remains unsubscribed within six months of the opening of the subscription list should be taken up by the Provincial Government either by contributing the same in money or by giving its guarantee to that extent. Any fresh district societies that may be formed after the establishment of the bank should be required to buy some minimum amount of shares which may either be issued in addition to the already existing shares or transferred by the Government if the latter so desires. The bank should receive deposits from the members as well as public but the rates of interest which it offers on deposits should be under control of the Banking Council—the object of this restriction is to save other banks from unhealthy competition of these provincial state-aided institutions.

The management of the Provincial Agricultural Banks should be in the hands of a board of twelve directors composed as: (a) Four to be elected by the shareholders voting in proportion to their shareholdings; (b) two to be elected by the district co-operative societies each enjoying one vote; (c) one to be elected by the banks working in the province, each bank enjoying one vote; (e) one to be nominated by the provincial legislature; (d) one

to be nominated by the bank of issue with concurrence of the Banking Council; (f) one to be nominated by the Governor-in-Council; (g) one to be appointed by the All-India Agricultural Bank or the Agricultural Credit Board; (h) Director of Agriculture who should be *ex-officio* director.

The chief object of a bank of this type should be to see that adequate credit arrangements are made to supply the lower societies with necessary credit means. It should be free to borrow from other banks and public. The Provincial Governments may transfer a portion of their funds to these banks as short-term deposits without interest, whenever that may be necessitated by special circumstances. The bank of issue should be obliged to extend reasonable credit lines to every provincial bank. It is not unreasonable to suggest that every such bank should enjoy an open cash credit limit of Rs. 25,00,000 at the bank of issues on the security of its general assets at 3 per cent. rate of interest fixed. Besides this, the bank of issue should extend rediscounting facilities to the extent of at least one crore of rupees. Rate of discount for bills up to this amount should be controlled by the Banking Council but it should, under no case, be more than the official discount rate.

The bank should also do other banking business like drawing, remittance, collection, agency, etc., but for its members only. It should be a member of the country's clearing system.

The Board of Directors of the bank should fix credit lines for the district societies to whom moneys should be advanced on the security of bills and pronotes endorsed by them. The period of such

discounts should ordinarily be not more than six months but it may be extended to a maximum period of one year in particular cases. Renewals thereafter should, however, be permitted, if necessary. The provincial banks should have right and power to examine the affairs of district and primary societies.

Dividends of the bank should be distributed as and in the order shown below :—

- (a) Ten per cent. to Reserve till it equals at least the paid-up capital.
- (b) Seven per cent. to shareholders.
- (c) Ten per cent. of the remainder to the bank of issue for cheap credit facilities.
- (d) The balance to be distributed half-and-half between the shareholders and the Provincial Government. The former may be either distributed as additional dividend or accumulated for the purpose of equalising dividends. The Provincial Government's share should be accumulated at 4 per cent. interest till such times as the bank does not need it any more. The Government's share of profits should not be taken to revenue but utilised for benevolent and educational purposes and for the propagation of the co-operative movement.

All the provincial agricultural banks may either be federated under an All-India Agricultural Bank or be guided and controlled by an Agricultural Credit Board. In the former case separate arrangements on the part of the provincial agri-

cultural banks at the bank of issue would be unnecessary nor such a large capital would be required. In our opinion the Agricultural Credit Board would answer the purpose much better and the provincial organizations should be developed on the principle of self-help.

The Board should consist of the member of the Governor-General's Executive Council in charge of agriculture, as *ex-officio* member and six others, one being appointed by each of the following six bodies : (a) Governor-General in Council ; (b) The Central Legislature ; (c) the Provincial Governments, each having one vote ; (d) the Provincial Agricultural Banks each having one vote ; (e) the Banking Council ; (f) Banks of the country, above the rank of " Local " Banks each enjoying one vote, excepting the bank of issue which should have ten votes.

The Agricultural Credit Board should have controlling, examining and superintending powers over the whole system of agricultural and co-operative banks. It should have power to prescribe limits on rates of interest which should be observed by the agricultural banks both for the purpose of borrowing and lending, subject to the power of alteration reserved to the Banking Council. The Board should be the final authority to regulate the agricultural credit machinery of the country. If the Provincial Agricultural Banks are in need of more funds and their requests in this behalf are legitimate the Board should do all in its power to make arrangement for the same ; and even if necessary, request the Government of India to procure the same on the strength of its credit or guarantee.

- (v) The system of bills, discounts and rediscounts should be introduced and encouraged to facilitate joint-guarantee and responsibility by endorsements as well as to inculcate the habit of meeting monetary obligations on maturity.
- (vi) A suitable legislation should be introduced by the Government by which obligations incurred to the credit societies should be considered as a first charge on the farm wealth of the borrowing farmers just like rates and taxes. Such a security of the credit unions will naturally be considered as pledged to the higher credit societies and through them to the Provincial and Central Governments as well as to others that may have ultimately advanced money on the endorsed notes and bills of the farmers concerned.
- (vii) Power of examination and control has been suggested to be given to the higher societies in respect of the affairs of the lower societies. It would be advisable if the Bank Examiners be empowered to examine the affairs of the credit societies occasionally and make reports to the Banking Council and the Agricultural Credit Board.

LONG-TERM CREDIT

The problem of long-term credit is of equally great importance to the land-holding class. Money for capital improvement or reclamations cannot be repaid but slowly and gradually from annual savings.

Germany is again conspicuous by originating facilities for the supply of this type of credit. She evolved the so-called land-mortgage banks (Landschaften) which advance money on the security of mortgages of property of the borrower. Loans only for productive purposes are made. If a borrower wants money for the purpose of 'consumption' the application is refused. Property against which advance is required is strictly valued from all possible aspects and advance made only up to 50 or 60 per cent. of the value thus determined. Usually property yielding income or capable of yielding income within a short period is only accepted. Advances are made sometimes for periods as long as 50 or 60 years. A borrower is at liberty to pay back his loans earlier if he chooses but the land-mortgage bank cannot compel him. Repayment is generally made by fixed annual instalments spread over the period of loan, which ultimately cover up both principal and interest. It is a simple calculation of mathematics that if the repayment of loan is spread over a long period and is made by annuities or on amortisation principle, the amount of annuity is little more than interest. For example, if the amount of loan is Rs. 1,000, the term of repayment 30 years, working expenses to be paid every year for managing the loan $\frac{1}{2}$ per cent. and the rate of interest 5 per cent. the semi-annual payment is about Rs. 35, or about Rs. 70 a year. This works to an annuity of 7 per cent. or only 2 per cent. over the rate of interest. Similarly if the period of loan is 50 years and the rate of interest 4 per cent., the annual instalment will be only 4.65 per cent. of the amount of the loan, *i.e.*, only $\frac{13}{20}$ of one per cent. over and above the rate of interest.

Sometimes the amount of annuity and rate of interest are fixed and the period of repayment is calculated from this data. Before the war the German landschaften usually fixed the annual annuity at only $\frac{1}{2}$ per cent. over and above the rate of interest. Thus if the rate of interest were 4 per cent., the annuity would be $4\frac{1}{2}$ per cent. and the whole debt would be liquidated within about 55 years. If the amount of loan were Rs. 10,000, the amount of interest alone would be Rs. 400, and an extra payment of Rs. 50 a year enables the whole principle to be repaid. The advantage of repayment by annuities is that the borrower does not feel the burden at all. He at once begins to extinguish the principal of the debt and as each year the principal decreases, the interest, of course, decreases also, and the annuity being fixed, the proportion of it applicable towards the extinction of the mortgage increases. On the next page we give a table showing how a loan gets extinguished by amortisation.

In some special cases period of repayment is increased to 75 years, though such instances are rare. The difference between annuity and interest in that case is further reduced. An honest and hard-working cultivator who wishes to purchase land and repay from annual income will not feel any burden at all. Moreover, the instalment is so small that if he happens to be temporarily without funds to meet the instalment, the local bank or the credit union of which he is a member will help him to pay the amount. The experience of land-mortgage banks is that it is very rarely that a mortgagor does not pay regularly. Hardly one in 150 or 200 mortgagors compels his bank to fore-close and administer

Table showing how a Loan of Rs. 1,00,000 (one Lakh) will be liquidated by amortisation payment of $5\frac{1}{2}$ per cent. every year the Rate of Interest being 5 per cent. per annum.

| Year. | Yearly payment. | Payment towards interest. | Payment towards principal. | Balance of principal. |
|-------|-----------------|---------------------------|----------------------------|-----------------------|
| | Rs. | Rs. | Rs. | Rs. |
| 1 | 5,500 | 5,000-0000 | 500-0000 | 99,500-0000 |
| 2 | 5,500 | 4,975-0000 | 525-0000 | 98,975-0000 |
| 3 | 5,500 | 4,948-7500 | 551-2500 | 98,423-7500 |
| 4 | 5,500 | 4,921-1875 | 578-8125 | 97,844-9375 |
| 5 | 5,500 | 5,892-2469 | 607-7531 | 97,237-1844 |
| 6 | 5,500 | 4,861-8593 | 638-1407 | 96,599-0437 |
| 7 | 5,500 | 4,829-9520 | 670-0480 | 95,928-9957 |
| 8 | 5,500 | 4,796-4496 | 703-5504 | 95,225-4453 |
| 9 | 5,500 | 4,761-2719 | 738-7281 | 94,486-7172 |
| 10 | 5,500 | 4,724-3355 | 775-6645 | 93,711-0527 |
| 11 | 5,500 | 4,685-5523 | 814-4477 | 92,896-6050 |
| 12 | 5,500 | 4,644-8299 | 855-1701 | 92,041-4349 |
| 13 | 5,500 | 4,602-0714 | 897-9286 | 91,143-5063 |
| 14 | 5,500 | 4,557-1750 | 942-8250 | 90,200-6813 |
| 15 | 5,500 | 4,510-0338 | 989-9662 | 89,210-7151 |
| 16 | 5,500 | 4,460-5455 | 1,039-4545 | 88,171-2606 |
| 17 | 5,500 | 4,408-5728 | 1,091-4272 | 87,079-8334 |
| 18 | 5,500 | 4,353-9015 | 1,146-0985 | 85,933-7349 |
| 19 | 5,500 | 4,296-5966 | 1,203-4034 | 84,730-3315 |
| 20 | 5,500 | 4,236-4265 | 1,263-5735 | 83,466-7580 |
| 21 | 5,500 | 4,173-2479 | 1,326-7521 | 82,140-0059 |
| 22 | 5,500 | 4,106-9103 | 1,393-0897 | 80,746-9162 |
| 23 | 5,500 | 4,037-2559 | 1,462-7441 | 79,284-1721 |
| 24 | 5,500 | 3,964-1187 | 1,535-8813 | 77,748-2908 |
| 25 | 5,500 | 3,887-3246 | 1,612-6754 | 76,135-6154 |
| 26 | 5,500 | 3,806-6909 | 1,693-3091 | 74,442-3063 |
| 27 | 5,500 | 3,722-0254 | 1,777-9746 | 72,664-3317 |
| 28 | 5,500 | 3,633-1267 | 1,866-8733 | 70,797-4584 |
| 29 | 5,500 | 3,539-7830 | 1,960-2170 | 68,837-2414 |
| 30 | 5,500 | 3,441-7722 | 2,058-2278 | 66,779-0136 |
| 31 | 5,500 | 3,338-8618 | 2,161-1382 | 64,617-8754 |
| 32 | 5,500 | 3,230-8049 | 2,269-1951 | 62,348-6803 |
| 33 | 5,500 | 3,117-3452 | 2,382-6548 | 59,966-0255 |
| 34 | 5,500 | 2,998-2125 | 2,501-7875 | 57,464-2380 |
| 35 | 5,500 | 2,873-1231 | 2,626-8769 | 54,837-3611 |
| 36 | 5,500 | 2,741-7792 | 2,758-2208 | 52,079-1403 |
| 37 | 5,500 | 2,603-8682 | 2,896-1318 | 49,183-0085 |
| 38 | 5,500 | 2,459-0616 | 3,040-9384 | 46,142-0701 |
| 39 | 5,500 | 3,192-9753 | 2,307-0247 | 42,949-0948 |
| 40 | 5,500 | 2,147-3769 | 3,352-6231 | 39,596-4717 |
| 41 | 5,500 | 1,979-7457 | 3,520-2543 | 36,076-2174 |
| 42 | 5,500 | 1,803-7330 | 3,696-2670 | 32,379-9504 |
| 43 | 5,500 | 1,618-9196 | 3,881-0804 | 28,498-8700 |
| 44 | 5,500 | 1,424-8656 | 4,075-1344 | 24,423-7356 |
| 45 | 5,500 | 1,221-1089 | 4,278-8911 | 20,144-8445 |
| 46 | 5,500 | 1,007-1638 | 4,492-8362 | 15,652-0083 |
| 47 | 5,500 | 782-5220 | 4,717-4780 | 10,934-5303 |
| 48 | 5,500 | 546-6481 | 4,953-3519 | 5,981-1784 |
| 49 | 5,500 | 298-9805 | 5,201-0195 | 780-1589 |
| 50 | 819-1669 | 39-0080 | 780-1589 | ..... |
| | | TOTAL ... | 1,00,000-0000 | |

his estate. The banks, of course, impose strict conditions in the mortgage deed and possess special powers to take estate in their hands for administration but they are very seldom forced to take such steps. But even when they take the mortgaged property under their control their object is not to usurp the property like an ordinary money-lender or usurer but to administer it in the interests of the borrower and to hand it back to him after the loan is repaid.

An interesting part of the working of a land-mortgage bank is the method of its obtaining money for such long periods. It is true that it cannot depend upon ordinary short-term bank deposits to make such loans. It would be dangerous to do so. In fact strict restrictions are levied on the amount of ordinary deposits which it can accept. The total of such deposits is usually not more than 50 per cent. of its paid-up capital and reserve. Moreover, it is required not to mix its ordinary banking business, conducted mainly in the interests of its clients, with the mortgage advances. If there were no restrictions of this nature, because its main advances are locked up for long periods, in times of emergency it would be subjected to very severe strain—often involving failure. Its capital is of course utilised in the first instance in taking some mortgages, but sooner or later the capital amount tends to be exhausted. How then does it get funds to finance further mortgages? It is quite simple. On the security of the mortgages in its favour, obtained in the first instance by using its capital, it issues bonds to the public and gets money with which to finance future mortgages. The second batch of mortgages is similarly assigned for second lot of bonds and the same

procedure repeated. The mortgages are lodged with an official trustee on behalf of the bond-holders. This official further examines the valuation on which mortgage advances have been made. The liability of each mortgage is, of course, only up to the amount remaining unpaid on it. The conditions of period of re-payment of bonds vary with the circumstances. Sometimes they are repaid by drawings, sometimes after fixed periods. The most general form of repayment is to keep them outstanding for some "certain" period, say, ten years, after which they are re-payable either by drawings or by notice. This provision enables the banks to pay off bonds when borrowers do not keep the loan for the full period. The bonds are, of course, generally repaid from the annual instalments. If at any time repayments made by the borrowers cannot be satisfactorily employed in paying back for the bonds, the bank buys its bonds in the market and thus saves interest charges. Sometimes the bonds are bought to popularise them in the market. Owing to the security of the bonds being satisfactory and stable, and the return on them fixed for a comparatively long period they are regarded as first-class paper and always in great demand by the investors. Trust funds are sanctioned to be employed in them. Insurance companies on account of the peculiarity of their finances, which require long-term good interest yielding safe investments, go in eagerly for them. Even ordinary banks deal in them and keep them either as permanent investments or as a means to utilise their temporary idle funds. Owing to there being always a ready market for them they can be resold at any time without any loss, because their

prices are comparatively stable. The bank of issue also makes advances on the security of the bonds within certain limits.

A few peculiarities remain to be explained in connection with the land-mortgage banks. During the first year of a loan, the borrower is required to pay about 3 per cent. to defray necessary expenses in connection with the preparation and registration of the mortgage, the valuation of the properties and other initial expenses. In some cases this charge is also distributed throughout the period of the mortgage. Effect of this course, is to slightly increase the amount of the annuity. The valuation of the property is in the first instance made by the bank's surveyors who are familiar with the locality and the prices reigning there. The appraisers value the property from all the possible points *e.g.* :— (a) What would be the price which the property would fetch if it were sold in the market? (b) What is the annual return from the property? (c) What would be the annual letting value if the property were let? The value as estimated by the surveyors after considering all the relevant points is examined by the relative department of the bank, which puts its own notes on the estimate. The report is then examined by the bank's directors who make any adjustment that may appear proper to them and finally fix the value. When mortgages are lodged as security with the official trustee at the time of issuing bonds the director's estimate is further checked. In some cases this is even voluntarily obtained by the bank before making the advance so that there may be no difficulty when floating bonds. Mortgage advances are not only made against agricultural property

but against residential buildings also. In the latter case only properties situated in good localities and always capable of yielding suitable rents are accepted. The period of loan in their case is also small, usually not more than 30 years. The mortgage banks also entertain proposals for advances from industrial concerns against the mortgage of their factory, building and plant. The period of loan in such cases is, however, not more than 20 years. The banks also make advances to railways and "communes" *i.e.* local and public bodies like municipalities, local boards, etc. Such advances are made on the general security of the revenue of the bodies concerned and bonds issued accordingly. Sometimes to make the bonds attractive in a dull market, lottery or prize conditions are attached to their issue whereby prizes or lotteries are drawn by them. Permission for such issues is, however, first obtained from the Government. Human nature always desires to get something for nothing, from mere chance, and the lottery bonds give ample opportunities to gratify that desire. Taking chances at lottery bonds are much more desirable from social and human points than gambling at the races and games of chances where people stand to lose all their stakes. In the cases of lottery bonds the principal and stipulated interest are always intact and the habit of thrift and saving is promoted.

When floating bonds the practice in the beginning used to be to assign a particular mortgage for a particular bond-issue and even name the issue by the name of the mortgaged estate. The banks now do not issue bonds as soon as a mortgage is made. They collect a number of mortgages and issue bonds as and when necessary assigning them as a collective

security for the issue in particular and other issues in general.

In connection with the land banks of Germany, Preussische Pfandbrief Bank, Preussische Central Boden Credit Actien Gesellschaft, etc. are well-known. The importance and value of land security was further made use of by that country when founding "The Deutsche Rentenbank" for the purpose of rehabilitating German Currency which, as the readers must be aware, had depreciated totally during the years following the Great War. The bank was established in consequence of the Decree of October 15, 1923, with a capital of 3,200 million Rentenmarks (equivalent in value to gold marks), to be furnished half by agriculture and half by industry and commerce, including the banks. The Rentenbank held a general mortgage, expressed in gold marks, on individual agricultural and commercial property, amounting to 4 per cent. of the value of that property. The mortgages carried 6 per cent. interest for the benefit of the bank. The Rentenbank was authorised to issue bank notes expressed in Rentenmarks up to the amount of its capital and initial reserve. Each Rentenmark was equal to a billion paper marks. The security of the Rentenmarks was thus a mortgage on real and to some extent on personal property instead of the usual backing of gold and commercial bills. The plan no doubt stabilised the internal currency. But as currency without the backing of gold, the basis of international currency, is of no use for foreign trade and foreign payments, the Reichsbank was reorganised under the Dawes plan to manage German Currency, supported by recognised backing, and the Rentenbank's

currency functions were taken over by it. The Rentenbank now looks after the credit needs of the agricultural and land interests of the country. The establishment of the Rentenbank and the stability of its notes has, however, successfully demonstrated the intrinsic worth and importance of land security ; and although currency wholly based on such a security may not be a practical proposition because of international financial obligations, which recognise only gold as the medium of settlement, there is no doubt about its popularity as a source of investment, in the shape of land-bonds, or even about its advisability to form a portion of the currency reserve, suitable limit being, of course, prescribed, so that the international value of the currency unit is not disturbed.

The United States of America recognized the necessity of long-term credit facilities for her people and established a suitable machinery for the same by passing the Federal Farm Loan Act in 1916. The Act created Federal Farm Loan Board which has the general supervision of the system. Its powers are to organize land banks, to regulate interest rates and other charges on loans, to audit and examine their affairs and to supervise the issue of farm loan-bonds. The board consists of the Secretary of the Treasury (*ex-officio*) and four other members appointed by the President with the approval of the Senate. Members serve for eight years and receive a salary of \$10,000 per annum, together with necessary travelling expenses. ** The country is divided into twelve federal land-bank " districts " and each district contains a federal farm loan bank. Each bank is managed by a board of nine directors three of whom

* * Moulton.

are appointed by the Federal Farm Loan Board. The Capital stock which each bank was required to possess before beginning operations was fixed at \$750,000 divided into shares of \$5 each, which was open to subscription by any person, firm, corporation, or state, or by the United States. If the capital could not be fully subscribed within thirty days of the commencement of business the remainder was required to be subscribed by the United States. The method of granting credit assistance is through mortgages as explained in earlier paragraphs. There is, however, a slight difference : a number of borrowers join together to form an association, the association gets a mortgage in its favour and it endorses it over to the land-bank. Money for advances is obtained by issuing bonds. The district land-banks can only issue such bonds (called " farm loan bonds "), when specifically authorised by the Federal Farm Loan Board. Each district has a farm loan registrar, appointed by the Federal Farm Loan Board, to whom land-banks desiring to issue bonds may bring the mortgages which they have taken from their borrowers. If the securities are approved by the Federal Farm Loan Board, the land-bank is given farm loan bonds of equal amount in exchange therefor. The total amount of bonds to any bank does not exceed twenty times its capital and surplus. The mortgages are held by the registrar as collateral, being assigned to him in trust by the land-bank. The bonds are exempt from national, state and local taxes. Payments received by the land-banks from the mortgagors are credited to the mortgage accounts under advice to the registrar. All such payments constitute a trust fund with the bank, to be applied by it to pay off its

bonds when they mature, to purchase bonds issued by any district land-bank, to loan on fresh mortgages, and to purchase United States government bonds. When mortgages are redeemed in full, the registrar cancels and delivers them to the proper land-bank for being returned to the mortgagor. It is gratifying to learn that the American Government, in order to popularise the bonds and to create public confidence in them authorised the Secretary of Treasury to purchase such bonds to the extent of two hundred million dollars between the years 1918—1921.

Besides a more or less public organization of the above description there is provision for the formation of ordinary joint-stock land-banks. They enjoy a greater degree of freedom in taking mortgages and in matters like period of advance, purpose of advance, etc. Restrictions as regards interest are, however, imposed upon them also. Also the maximum amount of bonds which they can issue should not be more than fifteen times their capital and surplus. Their bonds should be readily distinguishable in form and colour from those of the federal land-banks. Their zone of operations is limited to the state in which their principal office is located and one other state contiguous to it.

In France, "Credit Foncier de France" looks to the need of long-term credit of the land-holding class. It is a private company but under sufficient State control. It was founded in 1852 and was granted Government subsidy of 10 million (gold) francs. In 1853 and 1856 the Credit Foncier was granted certain privileges and placed under strict supervision by the Government. Like other land-banks it makes loans on the security of mortgages and obtains necessary

funds by the issue of bonds. It can, however, lend only against first mortgage and only up to half the value of the mortgaged property. The French Law has allowed the bank certain advantages, regarding the general regulations applying to mortgages. The governor and two assistant governors are appointed by State decrees. To make the "foncier" bonds attractive, the bank is permitted, with the previous consent of the finance member, to issue lottery or prize bonds.

There is great necessity of land mortgage banks in India. Even England which is principally a manufacturing country is feeling want of an organization which could extend long-term credit to the land-holding class. The report of Ministry of Agriculture and Fisheries, already referred to, recommends formation of land mortgage banks on the model of German land-banks.

Some of the Indian *Zamindars* are heavily in debt and their estates are mortgaged. Even if they were to make all possible exertions to redeem their properties the high rate of interest (24 to 36 per cent.) they are paying would take them a long time to be free from the clutches of money-lenders. Not unoften their estates are bought at low price by their creditors. Further, the irrigation projects, like the Sukkur Barrage, Sutlej Valley Project, etc., which are awaiting completion, will throw large blocks of agricultural land on the market. It is in the national and social interests to enable actual farmers and cultivators to possess reasonable plots and both to own and cultivate them. Even if in certain cases large scale *zamindari* be desirable, it is advisable to entrust that work to the people of the country and devise means

which will facilitate for them to buy land. We often hear reports that owing to the absence of local capital to buy all the land that will be capable of cultivation, after the irrigation projects have been completed, land might be even sold to non-Indians for the purpose of agriculture. It is even said that large foreign syndicates are being formed to buy large tracts of future agricultural land. If these reports be true they are decidedly not in the national interests. All possible efforts should be made to retain future cultivable land in the hands of Indians. The establishment of land mortgage banks will assist such Indian ownership. The interest charges would be moderate and the loan taken for buying land could be easily repaid within 25 to 30 years at the most, from annual income. These banks will give a new, vigorous and prosperous life, so to say, to the agricultural community.

Indians have great attraction for land and regard land security as first class and very valuable. The bonds of land mortgage banks, with the primary stamp of land security embossed on them, would in our opinion be very popular. And if requisite legislative measures are introduced permitting investment of trust funds in such bonds their success would be doubly assured. The issue of bonds is an integral part of the working of mortgage banks and as there appears to be no doubt about their success, the success of the banks themselves may be taken for granted.

Coming to the actual plan of organizing land mortgage banks in India we are of opinion that either there should be separate land-banks in each of the major provinces or separate mortgage departments may be opened in the provincial agricultural banks

referred to in the previous section. In the latter case it would be necessary to strengthen capital of the agricultural banks as well as to keep the mortgage business distinct, so as not to mix up with the short term business. We, however, favour establishment of distinct land-banks. They will be called upon to satisfy large demand for credit of this nature and faced with great business so that a separate organization is necessary. The banks can avail of services of district and primary societies for agency purposes or even take mortgages through them, just as American federal land-banks do.

We offer the following suggestions in connection with the working and constitution of the proposed land-banks:—

(i) In each major province there should be established a Provincial Land Mortgage Bank with a subscribed capital of rupees one crore, at least half of which should be paid up. Owing to the importance and speciality of their business they should be incorporated under special charters of the Provincial Legislatures. Shares should be open to subscription by the public, agricultural credit societies, banks, Provincial and Central Governments, etc. Any portion of capital that is not taken up within three months of the date of issue should be taken up by the provincial government concerned. The shares held by the government may be sold at any time thereafter but not at discount. The whole of the capital should be retained in the hands of Indians.

(ii) The board of directors of the bank should consist of 12 persons appointed as under:—

- (a) Four, to be appointed by the shareholders voting in proportion to their shares.
- (b) One, to be appointed by the Provincial Agricultural Bank.
- (c) One, to be elected by the banks working in the province.
- (d) One, to be nominated by the bank of issue subject to the approval of the Banking Council.
- (e) One, to be nominated by the Land Credit Board (referred to later).
- (f) One, to be nominated by the Provincial Legislative Council.
- (g) Two, to be nominated by the Governor-in-Council, but at least one of them shall be a person unconnected with the government.
- (h) One, Director of Agriculture or any other principal government officer who may be connected with land problems, as *ex-officio* director.

The board should elect its own president.

- (iii) The active management of the bank should be through a General Manager who should be appointed by its directors subject to confirmation of the Land Credit Board. There should be no restrictions upon the nationality of this officer for the first ten years but thereafter he should necessarily be an Indian.
- (iv) The business of every land-bank should be principally to supply long-term credit on mortgages and for this purpose to perform

all kinds of financial operations necessary or incidental to the same and among others the following :—

- (a) To receive deposits payable on demand and on notice with the restriction that the total of deposits payable on a shorter notice than five years should not be more than its paid-up capital and reserve. Such short-term deposits may be principally invested in liquid banking business, which the bank may do whenever necessary for its customers, or which it may be called upon to arrange for, when it takes over mortgaged properties for management. It should also have power to invest such funds in government, trust and other marketable securities, including its own bonds, so as not to lose interest. The Land Credit Board should issue instructions from time to time as to which securities are liquid and marketable in which such funds could be invested.
- (b) To issue savings certificates payable after 5, 10 and 15 years just like the Postal Cash Certificates. Sale-proceeds of these certificates to be regarded as long-term deposits or loans which can be used for making advances on mortgages.
- (c) To borrow money in India or abroad and for this purpose to mortgage any security that may be at its disposal, if necessary.
- (d) To issue with the previous sanction of the Land Credit Board, bonds, in the province of its habitation or in other

provinces or outside India as the Board may authorise on each occasion ; and to assign necessary securities and mortgages which it may possess, for such issues. The bank should have power to attach lottery or prize conditions to its bonds, after obtaining special permission for the same from the Banking Council, through the Land Credit Board.

- (e) The total of long-term deposits, savings certificates, long-term loans and bonds outstanding at any time should not exceed twenty times the paid-up capital and reserve.
- (f) To advance loans against mortgages of properties or supported by other permissible securities, including its own bonds ; but no such loan should be contracted for repayment for a term longer than fifty years.

Also in the case of advances against properties, only first mortgages should be accepted and not more than 50 per cent. of the current value should be advanced. Moreover, advances should be permitted only for productive purposes or for paying already existing debts or releasing existing mortgages. Repayment of such advances may be arranged on the basis of annual instalments or in lump sum as the bank may deem necessary.

- (g) To make loans to Central and Provincial Governments, Municipalities, Local

Boards, Improvement Trusts, Port Trusts, Railways, and other public bodies against their general assets.

- (h) To do other banking operations for its borrowers whenever necessary.
- (i) To open accounts with other banks and to become member of the country's clearing system.
- (j) To take over any properties for administration in the case of defaulting borrowers.
- (k) To buy any property for the purpose of its premises or in respect of advances already made, if that course be necessary to safeguard its interests. Properties bought for purposes other than those of habitation should be sold within a period of ten years from the date of purchase unless the Land Credit Board extends this period in any special cases.
- (l) To do any other business which the Land Credit Board and the Banking Council may authorise from time to time.

(v) The bonds of the bank should be eligible for trust investment and as security for advances by the bank of issue, the latter of course within certain limits. They should be considered as first class paper in every respect and security deposits of other banks should be permitted to be invested in these bonds.

(vi) The bank of issue should render financial assistance to the bank as and when that may be necessary, even by creating additional currency against the security of its bonds, subject, of course, to the limit prescribed in that behalf, provided the Banking Council and the Land Credit Board

recommend the assistance. The bonds thus accepted as security by the bank of issue may be retired as may be settled at the time of advance.

The bank of issue should extend discounting and short-term credit facilities, against appropriate security, on the same lines as it may prescribe for other banks.

(*vi*) The Provincial Government should offer special inducements to make the bank a success. The inducements may take any or all of the following shapes :—

- (*a*) To guarantee a dividend of 5 per cent. to the shareholders for the first five years.
- (*b*) To guarantee bonds of the bank as and when that may be necessary to popularise them.
- (*c*) To lend its credit to the bank for raising loans in the foreign markets.
- (*d*) To make loans both short and long-term, when such assistance may be necessary and possible ; and to buy whenever convenient, the bank's bonds to strengthen public confidence in them.

(*viii*) The profits of the bank should be distributed as and in the order shown below :—

- (*a*) For payment of guaranteed dividend of 5 per cent.
- (*b*) For payment of any amounts due to the Government for paying the guaranteed dividend, together with 5 per cent. simple interest due thereon.
- (*c*) From the balance, 10 per cent. of the annual profit *i.e.* of the profit before deducting payments in respect of (*a*) and (*b*),

should be taken to the Reserve till it equals paid-up capital.

- (d) The balance to be divided in the proportion of 3:1, to the Government and the shareholders. The Government's share of profits should not be taken to revenue but utilised for educational and beneficent purposes.

(ix) The bank should be liable to pay all taxes to which other banks and companies of the province are liable, excepting the "Safety" tax. It should also be exempted from the "Security Deposit." It would be advisable if the bonds of the bank are exempted from income-tax; or, if necessary, the bank may pay consolidated sum for that purpose to the Board of Inland Revenue.

(x) All the provincial land-banks should be co-ordinated under a board to be called the Land Credit Board. It should exercise controlling and examining powers with regard to the affairs of the banks. It should prescribe rates at which advances should be taken, made and bonds issued. It should also prescribe necessary initial charges to be charged by the mortgage banks, when advancing on mortgages. If necessary, the board should assist the banks in negotiating loans or in issuing bonds. The mortgages set apart for the bonds issued should be lodged with the board or its nominee. It should have power to re-value the mortgaged properties and charge any fees for this work that may be necessary. In emergent cases the board should procure special facilities at the bank of issue and monetary assistance or financial guarantee for loans raised from the Govern-

ment of India. It should issue instructions from time to time for the guidance of the banks. The board should consist of seven members. One of them should be the member of the Council of the Governor-General in charge of Lands and Irrigation and the remaining six should be appointed, one each, by each of the following six bodies :—

- (a) Provincial Governments, each Government having one vote.
- (b) Provincial land-banks, each bank having one vote.
- (c) Banks of the country above the rank of "local" banks, each having one vote, excepting the bank of issue which should have ten votes.
- (d) Banking Council.
- (e) Central Legislature.
- (f) Governor-General in Council.

The term of office of each of the above six members should be three years at a time, but retirement should take place of two members every year by rotation.

(xi) The Banking Council should, of course, continue to be the final authority on banking matters in this country and orders and decisions of the Land Credit Board should be liable to be overruled by that body. The Land Credit Board should work in close co-operation with the Banking Council.

(xii) The Provincial Land Banks may open branches in the province of their habitation though that would not be necessary. If, however, necessity is felt for branch organization, arrangements could be made with other banks or Credit Societies to represent the land-banks.

CHAPTER XIII

INDUSTRIAL BANKS

Necessity for industrial development—Cottage industries—Industrial Commission's report—Need for organising industrial credit—Result of such efforts in other countries—Activities of company promoter and industrial bank compared—Two Divisions of Industrial Credit: Industrial Credit Unions and Industrial Banks—French and Japanese industrial banks—Working explained—Their financial operations—Arrange foreign loans—Difference between the economic effects of foreign capital and foreign loans—Loan operations of the Industrial Bank of Japan—Japan's ambition in the industrial world—State participation in organisation of industrial credit—Outline of credit construction: Provincial organisations, Capital, Directors, Business, Facilities at the bank of issue, Inducements to be offered by Government, Profits, Taxes, Examination, Industrial Credit Board, Management, etc.

If India wishes to attain full economic development which her natural resources make possible, establishment and progress of industries is of paramount importance. By exporting raw products and importing finished goods we are paying unnecessarily for freight both ways and for foreign middleman's profits. We are further paying to foreigners for labour and other charges which go to make up manufacturing cost. They would be paid to the people of the country and thus saved to her, if she herself worked up the goods from natural to manufactured condition. Besides the abundance of all kinds of raw materials India's population is large, many of whom are not fully employed. For the well being of social order it is necessary

that every able-bodied man should have enough work to do which should procure him suitable living. It is true that the Indian labour is not at present fully suited to the carrying on of large scale industries. It is also equally true that the supply of skilled men with organizing brains, who can work industries in the country is very small. But the absence of these factors does not mean that India should always remain simply a producer of raw materials. Labour should be gradually improved, and better class of people with good grounding of education should turn their energies to industrial education and industrial pursuits. No doubt other countries do not freely admit foreigners in their manufacturing concerns to enable them to learn the work and technique but if the Government and other public bodies that purchase large quantities of foreign goods were to insist that such facilities should be provided, before placing their orders, something would be attained in that respect. Moreover, there is no objection to importing skilled men in the country to conduct industries in the initial stages, provided they are also required to train our young men who should ultimately take over the charge. Even if India has to pay much more than the market price for the services of such competent and willing trainers that would not be objectionable. Such additional expenditure could be fitly described as educational and training outlay which would be more than repaid when Indians replace foreigners on lower salaries. If all the important industries which are managed by foreigners had this aim in view in the beginning, many of our young men would

have been trained and the working costs would have also decreased. Japan which only half a century back had no industrial life worth mentioning has by systematic efforts in all directions built up at remarkably rapid pace industries of almost every description. If organized energy and true foresight are directed to the promotion of Indian industries the task is not difficult of accomplishment. It is only when half or haphazard measures are taken or vested interests are allowed to interfere, that endless amount of difficulties can be created or advanced.

Indian industries should be advanced both of the smaller type as well as on large scale. Much of the cultivating community is not fully engaged in agricultural labour for the whole year round. There are many periods of slackness when they have great leisure. Such free time should be utilised in working small or cottage industries to supplement their slender income from farming. Similarly in towns the small artisans, who on account of peculiar or local circumstances cannot migrate to the big industrial districts or who have enough scope in local work, can start home industries. Examples of successful cottage industries are available in Switzerland, Germany, Italy, Japan, and other countries. Reuter's telegram of 19th September, 1926, from Berlin announced "An exhibition of products of German handicraft industry is leaving Bremen by steamer to-morrow on a visit to North and South America, Africa, Australia, South Sea Islands, India, China and Japan, with the object of obtaining new customers. The venture is supported by prominent firms,

including Krupps." If German handicrafts can produce goods so cheaply as to be successfully exported abroad it is not difficult to anticipate that Indian cottage industries can work up articles at a fairly reasonable and marketable price. Such small industries need not always produce "complete" goods ready for immediate use. Often they can successfully produce parts which can be suitably assembled to represent whole articles. It would be an immense advantage if the workers in small handicrafts supplemented their manual labour with mechanical devices and mechanical energy. The hydro-electric schemes awaiting development in the various Indian provinces will supply cheap electric current to be used as convenient mechanical energy.

The problem of Indian industries has been examined from time to time. The Industrial Commission's Report is an important document on the subject. The Tariff Commission examined the question with a view to determine if any protection was needed to the industries of the country. The Indian Government has accepted the Commission's recommendation for discriminating protection and established a Tariff Board which examines representations from Indian industries for any preferential consideration. The Board is doing very useful work. The Tata Iron & Steel Company is receiving large bounties as a result of the acceptance of the policy of discriminating protection. And at the present moment the representation of the Indian Cotton industry is being examined by a special Tariff Board. All these measures are welcome and a move in the right direction.

But one of the most important factors* which is the life-blood of industrial growth has not been tackled as yet. We mean the question of systematic supply of industrial credit. Unless such an institution is satisfactorily organised it is idle to hope for any material advancement. The Industrial Commission's Report dealt with this subject and recommended the formation of industrial banks to supply this deficiency. We have already referred to the Tata Industrial Bank which was constituted by private effort to meet this requirement and how and why it prematurely failed. Its failure has discouraged establishment of other similar banks. But these failures do not show that they are not wanted. They prove that in the present state of banking in India they require something more than a mere private effort, that they need special organisation and constitution to meet activities peculiar to them and that the ordinary joint-stock banks designed for commercial banking are not fit to handle industrial finance at the present moment. What other countries like Germany, Japan, etc., have been able to achieve in the industrial domain through the guiding, fostering and financing hands of industrial banks† should be possible in this country also. Germany was mainly an agricultural country before 1870, or even 1888, which chiefly marks the beginning of a period of vigorous industrial de-

* To deal with the whole subject of industrial development in India and to determine ways and means for the same is beyond the scope of this book. We have referred to the subject to show the necessity and possibility of such development and how credit is an essential factor for the same.

† The word industrial bank is often loosely used to denote a bank which among other functions engages in industrial finance also.

velopment and her subsequent transformation from an agricultural to an industrial nation is not a little due to the active part which her Grossbanken (big banks which participate in syndicate operations) have played in such development. In England too, in spite of the advanced stage of her industries which are more or less fully grown and the liberal help which her big banks give to her industries, a section of people maintain that there should be special industrial banks to help the industrial growth.

Industries need great capital for their development and it is the province of the industrial banks to help in the mobilisation of capital. Ordinary commercial banks deal only in short-term or floating capital. It would be dangerous to mix up this business with long-term credit or fixed capital. Availability and organisation of industrial capital can be greatly promoted by industrial banks. The company promoter who, up till now, has been the chief instrument of procuring such money is often looked upon with distrust by the investing public. Investors do not get any satisfactory assurance from him that the business would be well looked after when the capital has been subscribed. His primary interest is to make the issue a success and not the business for which money is wanted. A respectable industrial bank on the other hand would first carefully examine and investigate a proposition before interesting itself in its flotation and thereafter see that it is well-managed. It endeavours to obtain at all times a comprehensive and accurate insight into the general conditions of the branches of industry chiefly dependent on

it for support in order to be able to discriminate between necessary requirements and false hankerings after expansion and aggrandisement. And as it is staffed with competent men conversant with industrial and financial matters and further possesses a somewhat controlling hand over the companies to which it extends financial aid, it should be able to intervene or at least restrain and check, in cases where the form and extent of the credit received cause the fear of unsound development. Moreover, an organised undertaking like a bank can even expect government assistance and raise foreign loans for the purpose of producing special facilities and finance which would ordinarily be not possible in the case of a private underwriter. A prominent English banker has said: "Company promoters do not exist in Germany, and in England they have, as a body, done great harm by their action as intermediaries in converting private concerns into public companies. The company promoter exists to induce the public to take shares in a private concern which he is turning into a limited liability company, and, as a rule, his personal interest is to inflate the issued capital of the new concern to his personal profit, without regard to its future welfare. This is a serious public evil and demands a remedy. Shall we prohibit the company promoter, and in any substituted system provide that flotations of new companies shall be made only by responsible bodies who have an interest in the continued prosperity of the companies, they put on the market?" And what is true in this respect in case of England is equally true in any other country.

We have referred to the syndicate operations of the German banks in a previous chapter and that it is not possible to thrust this responsibility on the ordinary banks of the country. The Industrial banks of the country should specialise in syndicate and industrial operations. In the present conditions it is most desirable and economical to concentrate such activities in the hands of a few powerful institutions. In addition to the dangers of combining short-term with long-term credit referred to above, which is a potential and real source of danger as long as banking habits are not fully formed, the industrial banks by engaging special staff of industrial financiers will be better able to judge and control propositions submitted to them for their considerations. Staff of ordinary commercial banks does not generally possess such requisite technical knowledge. The commercial banks would of course continue to provide working capital against the security of movable goods of factories, whether raw or manufactured or in the course of manufacture but the financial part of the business which deals with the establishment of the factory or the industry must be left in the hands of an industrial banker.

INDUSTRIAL CREDIT UNIONS

Industrial banking like the division of industry into small scale and large scale referred to already, should be divided into two parts: (A) Those which would specialise in assisting small and cottage industries, and (B) those which would specialise in assisting bigger industries and factories. Institutions of the type (A) would be better formed on the co-operative principles fully explained in the last

chapter. They should be called Industrial Credit Unions. A number of artisans and manufacturing workers residing in a locality should combine to form a credit association. Influential neighbours should be invited to join. It would be advisable to form them on the Schulze-Delitzsch principles. These associations should procure necessary credit by taking deposits and raising loans. For the steady supply of credit they can make arrangements with local and other banks or even with the industrial banks. The members of these credit unions, small artisans and workers, would not generally require any long-term credit. Their every-day plant and instruments would not be costly or require much outlay. They can purchase them from their own means ; or if they borrow for such purposes they can soon repay them. If in particular cases they need for occasional use comparatively expensive plant, to increase production or value of their products, they can co-operate and purchase a common machine to be used by turns. The class of workers we have in mind will, of course, not much rely upon high class machinery which on account of its vastness and complexity requires different mode of operation. The small hand operators will mainly want short-term loans to enable them to buy raw materials, turn them into finished goods and then repay their debts from the sale-proceeds of such articles. This assistance will, of course, increase their sustaining or holding power and they would not be simply at the mercy of the buyer of their goods. By paying ready cash for raw materials they would buy them cheaper. Also loans taken from credit unions would be at

reasonable rates of interest. Thus the cost of manufactured article would be less than if the workers had not the advantage of co-operative credit. They can further improve their economic position by co-operative purchases and co-operative marketing of their goods. If suitable industrial education, supplemented by actual demonstration pertaining to their business is imparted to them, or if any new devices calculated to economise labour are made known to them, the advantages of credit and co-operative unionism can be further increased. It is, of course, necessary that the industrial credit unions should be well supervised and strictly examined from time to time. Apart from the superintendence and control of the Banking Council, which is suggested to be the final administrative authority on banking activities in India, it would be desirable if the unions are placed under the co-ordinating and controlling influence of the industrial banks.

INDUSTRIAL BANKS

The other type of Industrial banking *viz.*, represented by (B) above, should be a much bigger affair and able to meet the financial demands of large-scale-industry. An early example of such a special institution is "Societe Generale de Credit Mobiler" established in France in 1852. Its chief function was to promote industrial and financial enterprises. Within a short period of fifteen years after its coming into existence it succeeded in establishing numerous railway, gas, shipping and other companies. Japan has built her industrial bank on the model of the Credit Mobiler and the part which it is playing in her industrial development

is commendable. The way in which industrial banks carry on their business is somewhat as follows.

The bank staff examines any industrial propositions which are submitted to it or which it may come across during its industrial survey. The proposition may be either to establish a new industry or to suitably alter or expand an already existing one. If the bank is satisfied that there are reasonable chances of working such a company successfully, a number of people take up the responsibility of floating it. The bank is a principal party in such a flotation and besides subscribing a sufficient sum, it often underwrites a good portion of its capital. The bank, of course, gets underwriting commission. Any portion of shares which is not taken up by the public is taken up by the bank which subsequently sells them off as the company gets public confidence. If the bank does not need any money it may hold on the shares, in spite of the investor's interest in them, till such time as it may happen to need funds. Any appreciation in the shares of the company naturally goes to the bank. The bank under the arrangement made at the time of flotation continues to have a controlling hand in the management and its nominees work on the directorate. These nominees are either the bank's managers, directors or in any other way connected with it and are competent to handle and guide the business of the company. The public on account of these circumstances, respectability of the bank and its financial support to the company in times of emergency, is more inclined to subscribe to issues in which banks take part than if it were promoted

independently of any such connection. The industrial banks are generally members of the Stock Exchange. This connection further helps them to interest the public in the issues with which they are connected as well as to keep up a market in those shares.

The above is only one way of financing industries. If the circumstances are such that the bank does not feel inclined to subscribe or interest itself in the underwriting operations or if the assistance is required by an already established company which thinks it unnecessary to issue further shares, the mode of financing adopted is to advance long-term loans on the mortgage of the company's assets, securing at the same time a hand in the management. Such loans are financed by the bank by issuing bonds in the market supported by such mortgages and the bank's general assets. Operations of this nature resemble more or less the transactions of land-mortgage banks referred to in the last chapter. The difference between the two banks are: (i) Industrial banks take part in the management of the actual business whereas such a power is not considered necessary in the case of mortgages taken by land-mortgage banks. (ii) The period of mortgages taken by Industrial banks generally does not exceed 20 years but the mortgage period may even go up to 75 years in the case of land-mortgage banks. Owing to constant depreciation in the plant and machinery and buildings of an industrial company a smaller period is, of course, necessary for the safety of the bank's money.

In addition to the above ways of financial operations, industrial banks sometimes take up and/or

underwrite debenture issues of companies, selling the debentures as and whenever convenient. They also extend liquid credit to companies against their stock-in-trade and trade bills. Facilities of this type pertain more to the sphere of commercial banking than to that of industrial banking, but sometimes a company in which an industrial bank is heavily interested finds it more agreeable and convenient to look to that bank for this assistance also. The Industrial banks also engage in commercial banking to some extent usually so far as it relates to the companies in which they are interested. They may accept deposits from the public but such funds should only be invested in easily realisable assets and not mixed up with capital operations. Long term deposits say payable after five years or more or proceeds of savings certificates payable after similar periods may be utilised for the purpose of supplying long term industrial finance but any money payable at shorter notice should be only invested in floating assets.

One of the chief important functions of an Industrial bank is to arrange for foreign loans either directly to companies or on its own guarantee. Capital is an important factor for industrial progress. Available local or national capital, in the shape of money, necessary to purchase foreign materials, like machinery, etc., and to pay for foreign labour, which may be necessary in the commencement, may be insufficient. An Industrial bank can suitably raise credit in the foreign market to be repaid from the profits of industries. To allow import of foreign capital by foreigners for the purpose of starting industries with sole control in their hands, is not at

all in the national interests. All the profits would be exported or drained from the country. A good portion of wages would be received by foreigners who would further continue to retain the management in their hands, and one of the chief advantages of having national industries, *viz.* to remunerate Indian labour and brains from the working costs of the industries and thus raising their economic standard would greatly disappear. Moreover, the companies would be worked in the foreign interests. Any advantage of protective system* which a country may introduce in the national interests would be equally available to the foreigners at the cost of the country's consumers. Return on foreign capital for its use should be limited to the lowest figure possible. This figure is represented by interest. Thus it is advisable to import foreign funds only by means of loans which should be gradually paid off from the surplus income.

Banks are great instruments for successfully negotiating such loans. The Industrial Bank of Japan during the nine years, 1902 to 1911, arranged for twelve loans, aggregating £26½ millions. Ten of these loans for £17 millions and Yens 88

* It may be mentioned in this connection that Swedish match manufacturers have started match factories in India so as to avoid increased import duty on matches, that was sanctioned some years back. Japanese cotton manufacturers are also reported to have decided that if the special Tariff Board, which is investigating the question in Indian cotton industry, recommends enhancement of duty on imports of cotton piecegoods and such a recommendation is accepted by the Government, they should seriously consider the question of opening cotton mills in India. It is thus evident that tariff duties in themselves are not sufficient protection for the advancement of Indian industries, unless side by side restrictive measures on the import and activities of foreign capital are also introduced; otherwise such measures instead of helping the growth of industries may simply result in the reduction of revenue.

millions (combined total, converting Yen at its par value*, equals £26 millions), were issued in London. The remaining two, out of which one was a sterling loan amounting to a small sum of a quarter million pounds, were only issued in Tokio. The loans issued in Japan were also open to foreign subscription. Out of the total of twelve loans, eight were raised on behalf of industrial companies, like railways, paper mills, collieries, etc.; three were raised on behalf of local bodies and the remaining one was issued on behalf of the Japanese Government. Thus practically all the loan requirements for Japanese industries which the industrial bank was called upon to negotiate were obtained in a foreign market. And if a Japanese bank can successfully tap the London market cannot similar banks organized in India, with the support of British connection, hope to achieve at least the same success in the same and other foreign markets?

Organization of national and foreign finance, which includes having recourse to foreign loans, has so much advanced in Japan that that country is now seriously thinking of even owning industries in foreign countries. Surely this would not be possible if her credit institutions were not competent to provide, whether directly or indirectly, financial aid for such purposes. The papers had hardly finished announcing the news of the success of the Japanese loan in London last year, when another piece of news came, that a Japanese syndicate had purchased a number of cotton mills in Bombay belonging to an important group at a price of over

* Par of Exchange between England and Japan is 2s. 0·58d. = 1 Yen or ·1024£ = 1 Yen.

two million pounds. The news of purchase was unconfirmed, but the report at least shows the Japanese ambition to own foreign industries. Is it not a matter of woeful surprise that a foreign country, with the help of London Market, should be able to aspire for a footing in the industries of India and the Indians themselves, in spite of their intimate (and insuperable ?) connections with the British Empire and of the influence which such connections should give them in the London Market, should not only be backward in industries but even sell their existing industries to foreigners ? Possibly there may be no direct connection between the loan and the rumoured purchase but the facts at least prove that foreign loans assist Japan's local finances and to that extent release national capital to be employed in foreign countries. Want of organization of our credit institutions is solely and wholly responsible for the deplorable state of our affairs.

Owing to the national importance of industrial banks, States usually take active part in their formation and management. They, often, subscribe a portion of their capital, nominate their chief managers and some directors on their boards. To induce investment in their capital they sometimes go to the extent of guaranteeing dividend on their shares at a certain rate either for some initial number of years or permanently. They also lend state credit to the banks whenever that may happen to be necessary in the public interests. In the case of the Industrial Bank of Japan 5 per cent. dividend for five years was guaranteed to the shareholders by the Japanese Government.

In the scheme of banking organization in India there should be at least one important industrial bank in each of the major provinces. As administration of industries is delegated to provinces, banking activities relating to them should naturally be distributed by provinces. All the banks should, however, be co-ordinated under one central board to strengthen, guide and systematise their organizations. To minimise expenditure on technical services, whose reports and advice would, of course, be necessary for examining propositions placed before them, common industrial staff, expert in special subjects or of a high order, may be maintained by or under this central board for the benefit of all the provincial industrial banks. These banks should further enjoy special privileges at the hands of the government and of the bank of issue. Owing to the peculiarity of their business and the national importance of their activities they should be incorporated under special provincial charters. The following brief outline is suggested to form the basis of their constitution :—

(i) The capital of each of the provincial industrial banks should be at least rupees two crores half of which should be paid up before the commencement of business. The other half may remain as reserve liability or be called up as and when necessary. The capital may be increased from time to time as may be necessary. Shares should be offered for subscription to the public, banks, companies etc. with this restriction that not more than one-fourth of the capital should be allotted to non-Indians. Any portion of the capital that is not taken up within six months of the date of issue should be taken up by the provincial government. If

demand for the bank's shares be great, portions may be prescribed for allotment to public, banks, industrial companies, and so on, allotment in each section taking place on suitable basis.

(ii) The board of directors of the bank should consist of 12 persons appointed as under :—

- (a) Three to be elected by the shareholders voting in proportion to their shares ;
- (b) One to be elected by the industrial companies of the province, each enjoying one vote ;
- (c) One to be elected by the banks working in the province ;
- (d) One to be elected by the Industrial credit-unions of the province ;
- (e) One to be nominated by the bank of issue subject to the approval of the Banking Council ;
- (f) One to be nominated by the Provincial Legislative Council ;
- (g) Two to be nominated by the Governor-in-Council but not more than one should be a government official ;
- (h) One to be nominated by the Industrial Credit Board ;
- (i) The Director of Industries who should be *ex-officio* director.

The directors should elect their own Chairman.

(iii) The business of the bank should be to promote industrial growth and for this purpose to perform all kinds of financial operations necessary or incidental to the same and among others the following :—

- (a) To receive deposits payable on demand and on notice with the restriction that the

total of deposits payable on a shorter notice than 5 years should not be more than its paid-up capital and reserve. A convenient mode of receiving long-term deposits would be to issue "Savings Certificates" just on the model of the Postal Cash Certificates.

- (b) To borrow money both in India and outside, either directly or by issuing bonds, and for this purpose to assign or mortgage any security that may be under its disposal. The total of bonds outstanding at any time should, however, be not more than twenty times of its paid up capital and reserve.
- (c) To advance loans to or open cash credits in favour of industrial companies, but no such advance should be for a period longer than 20 years.
- (d) To subscribe to the shares and debentures of industrial companies and underwrite the same whenever advisable.
- (e) To guarantee loans to or of other companies as may appear to it advisable.
- (f) To do commercial banking operations for companies to whom financial assistance has been supplied or for whom loans have been arranged.
- (g) To do business referred to at (c), (e) and (f) for any local body, government or other institution subject to the approval of the Industrial Credit Board.*

* When the bank has free surplus funds it should be at liberty to invest them in suitable papers so as not to lose in interest.

- (h) To own, manage, superintend, direct, and work industrial concerns whenever necessary.
- (i) To consolidate, co-ordinate, guide, superintend, examine and control the industrial co-operative credit unions and render them reasonable financial assistance.
- (j) To be a member of the Stock Exchange and to deal in Stock Exchange paper.
- (k) To do any other business which the Industrial Credit Board (referred to later) and the Banking Council may permit it from time to time.
- (l) To keep accounts with any other banks and to become member of the country's clearing system.

(iv) The bonds of the bank should be eligible for trust investment and as security for advances of the bank of issue, the latter, of course, within suitable limits. They should be regarded as first class security.

(v) The bank of issue should render financial assistance to the bank as and whenever that may be necessary even by creating additional currency against the security of its bonds, subject, of course, to the limit prescribed in this behalf not being exceeded, and provided the Banking Council and Industrial Credit Board recommend that action. The bonds thus accepted as a part of the Currency Reserve may be retired as per terms that may be settled at the time of advance.

The bank of issue should discount the bank's bills as may have been acquired by it when financing short term credit operations.

(vi) The government of the province in which the bank is situated should offer special inducements to make the bank a success. The Government has lost a good deal of the tax-payer's money in establishing railways and it is not too much to hope that some subsidy should be extended to industrial banks, the fountain of industrial activity, specially when the risks, if any, are much less than what there were in the case of railways. The inducements may take any or all of the following shapes :--

- (a) To guarantee a dividend of 5 per cent. to the shareholders for a number of years, say 10 or more;
- (b) To guarantee bonds of the bank as and when that may be necessary to popularise them;
- (c) To lend its credit to the bank for raising money in the foreign market;
- (d) To make loans both short and long term when such an assistance may be necessary and possible; and to buy its bonds off and on, to strengthen public confidence in them;
- (e) To keep its industrial and technical officers at the disposal of the bank, without any or at nominal charges (which will depend upon circumstances), for assisting the bank in the examination or superintendence of propositions it may be interested in.

(vii) The profits of the bank should be distributed as and in the order shown below :—

- (a) For payment of guaranteed dividend of 5%;

- (b) For payment of any amounts due to the government for paying the guaranteed dividend, together with 5 per cent. simple interest.
- (c) From the balance, a sum not exceeding 10% of the annual profit, *i.e.* of the profit before deducting (a) and (b), should be taken to the Reserve till it equals paid-up capital ;
- (d) The residue to be divided in the proportion of 3 : 1 to the government and the shareholders. The government's share of profits should not be taken to revenue but utilised for promoting technical education, and industrial facilities, for making loans to the industrial bank and the industrial credit unions and for other beneficent purposes.

(viii) The bank should be liable to pay all taxes to which other banks and companies of the province are liable, excepting the 'safety' tax.—It should also be exempted from the "Security Deposit."

(ix) The bank should be under the control and examination of the Banking Council and the Comptroller and Examiners of banks.

(x) All the provincial industrial banks should be co-ordinated under a board to be called the Industrial Credit Board. The board should exercise supervisory, controlling, and examining powers with regard to the affairs of the banks. It should assist in the negotiation of loans, issue of bonds, etc. of the banks, whenever necessary and possible, both in India and abroad. In emergent cases the board

should procure special facilities at the bank of issue, and monetary assistance or financial guarantee for loans raised from the Government of India. It should maintain a competent and efficient industrial staff to advise it and the provincial industrial banks in important matters, like industrial investigations, surveys, estimates and so on—necessary expenses for the maintenance of this staff and the board being paid by the banks either in equal parts or in proportion to their business. It should issue instructions from time to time for the guidance of the banks. It should be in close co-operation with the Banking Council—the decisions of the latter should however be binding upon it. The board should consist of seven members, besides the member of the Governor General's Council in charge of Industries, who should be an *ex-officio* member. The seven members should be appointed as under :—

- (a) Two to be elected jointly by the provincial industrial banks and provincial governments, each bank and each government exercising one vote. Not more than one of these two members should be a government official ;*
- (b) One to be elected by the industrial associations of the country each having one vote ;
- (c) One to be elected by the banks of the country above the rank of " local " banks, each bank having one vote excepting the bank of issue which should have 10 votes ;
- (d) One to be appointed by the Banking Council;

* If the method of joint election is not agreeable, each of the two bodies, Provincial Governments and Provincial Industrial Banks may elect one member.

(e) One to be elected by the Central Legislature ;

(f) One to be nominated by the Governor
General-in-Council.

(xi) The active management of the bank should be through a General Manager who should be appointed by its directors subject to confirmation of the Industrial Credit Board. Under him there should be necessary officers. There should not be any restrictions on the nationality of the personnel of the managerial staff but within twenty years from the establishment of the bank at least half of the officers under the General Manager should be Indians and after 30 years from the commencement the General Manager should also be an Indian.

(xii) The bank should be free to open branches in the province of its habitation, though it would be hardly necessary. In special cases it can be represented by ordinary banks, at places other than its place of business, with whom agency arrangements can be made.

CHAPTER XIV

OTHER BANKS AND BANKERS

POST OFFICE SAVINGS BANKS ; Improvements suggested : Accounts, Nominees, Deposits by cheques, Limit on annual deposits, Limit on balances, Home Savings safes, Attachment of deposits, Savings facilities for villagers, Letters of Credits—MUNICIPAL AND LOCAL BOARD BANKS ; Object and scope—Municipal Bank of Birmingham—Capital not necessary—Some useful services they can render—Investments—Method of keeping funds—Management—Profits—Small offices to work by turns—CO-OPERATIVE BANKS ; Principle already explained—Capable of extension to a variety of homogeneous groups—PRIVATE BANKS AND BANKERS ; No restrictions needed—Should not participate in trading—Compared to English bill brokers—Conversion of private into corporate banking—“*Commandit*,” *i.e.*, Limited-partnership principle, explained—Opportunities for its development in India.

We have attempted so far to deal with the most important components which should make up the Indian banking system. There are, however, a few further types which are none the less necessary to complete the system. We shall now briefly refer to them.

POST OFFICE SAVINGS BANKS

This subject has been referred to in Chapter II. We have said there that there is room for improvement in this institution. The inauguration of banking reform and the introduction of requisite measures as suggested in this book may possibly decrease the present importance of Post Office Savings Bank as an instrument of accumulating savings. People

may get better facilities elsewhere. Municipal and Local Board banks referred to in the following section may likely appear more attractive, specially because such banks can give occasional advances to their depositors—of course within certain limits and under certain conditions. But these are not reasons why the Post Office should not improve its savings bank machinery to increase its usefulness to the public. Even in countries where banking has considerably developed savings bank departments of their post offices continue to function and the same should be the case in this country. There will always remain a portion of population that will not entrust its savings to any one excepting a government organization. To prevent such people from hoarding their savings, to assist such people in accumulating their savings and lastly to mobilize surplus capital of such people and make it available for the country's* credit requirements, the savings bank counters of the Post Office are necessary. And anything that can increase the attractiveness of the Indian Post Office Savings Bank or make it more serviceable to the people should be welcome. We suggest the following improvements in this connection.

* Possibly it may appear a paradox to say that the Post Office Savings Bank deposits assist country's credit needs. In as much as such deposits assist the Government finances and thus decrease the Government's demand on the money market, to that extent they can be said to help the country's credit requirements, by relieving Government pressure on the same. Moreover, if at any time the savings bank machinery of the post office attracts more funds than are actually wanted by the Government, the Government can lend the surplus as short-term deposits to commercial banks either directly or through the medium of the bank of issue, or use it in buying up its bonds in the market, which will supply the market with money and thus satisfy credit demands.

(i) **Accounts.**—At present accounts cannot be opened in the name of two or more persons, jointly. This is an unnecessary hinderance. Even the British Post Office allows opening of such accounts in its Savings Bank departments. Accounts “payable to either or survivor” should also be permitted. A provision like this will enable withdrawal of deposit after the death of an operator, by the surviving operator *e.g.* a husband and wife can open an account of this description. During their lifetime both of them can operate upon the account and after the death of either of them, the survivor can carry on.

(ii) **Nominees.**—Depositors should be permitted to designate their nominees who could receive their deposits after their death. The British Post Office Savings Bank permits this facility. An arrangement of this nature will facilitate transference or payment of deposit after the death of depositor and even save the Post Office from much botheration of investigating the rightful claimant.

(iii) **Deposits by Cheques.**—A savings bank depositor, keeping an account with an Indian Post Office, cannot deposit cheques for the credit of his account. The Government should encourage the use of cheque currency and this disability should be removed. The British Post Office permits deposits by cheques. Such deposits are, however, not available for withdrawal for ten days. This limitation is necessary to enable the Post Office to know fate of cheques and can be introduced in this country also, when permitting deposits by cheques.

(iv) **Limit on Annual Deposits.**—A depositor cannot deposit more than Rs. 750 a year in his savings bank account. This is an unnecessary impediment. Suppose a poor man by chance gets a few thousands in any year. It means he can only put Rs. 750 to his account and for the rest he must either make other arrangements or hoard it. When the British Post Office can accept amounts upto £500 in a year, the limit of Rs. 750 is ridiculously low. It should be at least raised to Rs. 5,000.

(v) **Limit on Balances.**—No depositor can have more than Rs. 5,000 to his credit at any time. If an account is opened on behalf of a minor, the limit is reduced to Rs. 1,000 only. These limits are a hinderance. The British Post Office does not prescribe any such limits. The only argument for imposing such limits is that people may not embarrass a local post office at the time of withdrawal. To safeguard this a certain notice may be insisted upon when withdrawals, say over Rs. 5,000, are being made. Removal of the limit of this nature will not throw large amount of money on the post office, all of a sudden, say for the purpose of earning interest when money is plentiful, because a limit on the amount that can be deposited in a year is prescribed. Moreover, as suggested elsewhere, if the Post Office is faced with large deposits which the Government cannot make use of, it can lend them to banks on interest. After the introduction of suitable controlling and inspecting agency the Government should not hesitate to trust banks of the country.

(vi) **Home-Savings Safes.**—The British Post Office issues these small safes on payment of three shillings to induce people to collect small savings

at home. We are referring to this mode of inculcating habit of thrift in the masses elsewhere ; but if the Indian Post Office Savings Bank were to introduce this arrangement, it may considerably assist its mission.

(vii) **Attachment of Deposits.**—Deposits in Indian Post Office Savings Bank can be attached by the order of a competent court in satisfaction of suits against the depositors. The British Post Office, however, clearly lays down in its rules that : “ A deposit book is not a proper security for money lent, and no claim by any person holding a deposit book in respect of a loan can be recognised. Deposits in the Post Office Savings Bank are not liable to ‘ Attachment ’ or to its Scottish equivalent ‘ Arrestment. ’ ” Although we would not go to the extent of suggesting wholesale copy of the British rule in this respect, as it may mean creating a wilful method of defrauding one’s creditors, still we should wish that some minimum portion of an account, say Rs. 5,000, may be prescribed, which could not be attached. An arrangement of this nature will enable people to make emergency financial arrangement for their families.

(viii) **Savings Facilities for Villagers.**—We have suggested in chapter II how villagers must sometimes walk large distances before they can deposit in or withdraw from the nearest Post Office Savings Bank and that some arrangement in this respect should be possible through the village postman who visits the village for delivering post. Such an arrangement is quite feasible. Let the postman be given a book of receipts printed in duplicate, one of which he should hand over to the village deposi-

tor whenever he is entrusted with money and the pass book to be deposited in the post office. When he returns to the post office the authorities can examine the duplicate impression in the book and check the deposits and pass books received by him. On his next visit the pass books should be returned and the original receipts collected which should be pasted in the book and verified at the post office. Similarly when withdrawing money, the same procedure of receipts, with duplicate impressions in the book, could be introduced, the receipt given by the postman, when getting withdrawal form and pass book, being collected, at the time of handing money and the pass book. It may be said that it would be risky for the postman to carry such money. As the amounts would ordinarily be small there would not be any further risk than to what he is subjected now when carrying money-order amounts. If necessary, limits on such deposits or withdrawals, say Rs. 20 at a time, may be prescribed. It may also be urged that owing to the illiteracy of the villagers the postman may be induced to commit frauds. We do not think that any undue further temptations would be created for the postman by this arrangement, than what already exist when illiterate persons open accounts with Post Office Savings Banks. However, if a precaution be necessary such operations, through the postman, may take place in the presence of the village headman or the village police constable. The day and time of visits of the postman being more or less fixed, there should be no difficulty in arranging for co-operation of a respectable villager to attest such transactions.

NOTE—Post Office can also help to develop banking habits in other ways as well as be a means of economising actual cash circulation. If it were to issue letters of credit payable at any post office in India a good deal of convenience and easy mode of carrying money would be introduced. Post Office would not run any more risk in respect of forged letters of credit than it does at the present moment when issuing postal orders. Specimen signature of beneficiaries on letters of credit would be a sufficient means of identification. If, however, further safeguard be necessary, or if special convenience for illiterate people be desired, the issuing office can paste the beneficiary's photograph, duly attested by it, on the letter of credit.

MUNICIPAL AND LOCAL BOARD BANKS

If bodies like Local Boards and Municipalities are permitted to do a modified form of banking business, without taking any risks which ordinary banks take, there could possibly be no objection to that. On the other hand this new activity would be greatly appreciated. In Germany these banks are ordinary feature of local bodies and do useful work. England, however, does not appear to be sanguine about such banks.* Her objections are that such bodies do not possess adequate experience for the conduct of banking business and further that there is danger of bank deposits being locked up in capital works and as non-liquid advances. The Municipal banks are not expected to do commercial or any high class or complicated banking and as such there is not much need of previous experience. Their work is mainly to accumulate savings of poor classes and to invest them as a man of ordinary common sense and prudence would invest. It is remarkable to note that in spite of England's doubts about this kind of banking the Municipal Corporation of Birmingham has started a municipal bank which

* The British Government has lately appointed a committee to examine and report on the question of municipal banking in England.

is doing very active and prosperous work. The bank started work in 1919. Its deposits on 31st March, 1921 *i.e.* at the end of nineteen months of working, were about one million pounds. On 31st March, 1925, the deposits were over three million pounds, *i.e.* the deposit figure increased three times during the short interval of four years. The bank has over thirty two branches and sub-branches. These figures show that the bank's services are being well appreciated. The response which it has received from the public conclusively refutes any arguments against municipal banking. The bank mainly keeps savings bank accounts and invests its funds in gilt-edged securities. It makes advances for house purchasing and renders some other services to the community. In order to give the readers some idea of its activities we are publishing its 1925 balance sheet on the next page.

No capital is required in the case of municipal banks. The municipal general revenues and properties are a sufficient guarantee for the depositing public. The banks should mainly receive savings bank deposits, at a rate not exceeding that which is allowed by the government post offices, which should be mainly invested in trust securities. This would give a margin of profit more than sufficient to meet the running expenses. The Banking Council should, however, have power to allow any municipal banks to put up their interest by half a per cent. over and above the postal rate. At places where there are no banks, local bodies may be permitted to open floating accounts without allowing any interest on them. In fact at such places the municipal banks can even

BIRMINGHAM BALANCE SHEET

| LIABILITIES. | £ | s. d. | £ | s. d. |
|--|--------|-------|-----------|-------|
| Amount standing to Credit of Depositors (including interest) ... | ..... |  | 5,611,532 | 8 11 |
| Sundry Creditors for Rent, Printing, Heating, Repairs, Outlay, etc. ... | ..... |  | 8,580 | 5 |
| Reserve Fund— | | | | |
| As at 31st March, 1924 | 8,808 | 7 4 | | |
| <i>Add.</i> —Superannuation Contribution as per Income and Expenditure Account for the year ended 31st March, 1925 ... | 476 | 18 5 | | |
| Total Reserve, including Liability for Superannuation ... | 59,285 | 5 9 | | |
| <i>Add.</i> —Excess of Income over Expenditure for the year ended 31st March, 1925 ... | 10,462 | 14 6 | | |
| | | | 69,748 | 0 3 |
| GRAND TOTAL ... | ..... |  | 5,689,860 | 11 7 |

We have audited the Accounts as set out above, and we certify the affairs of the Bank.

(Sd.) J. P. HILTON,
General Manager of the Bank.
110, Edmund Street, Birmingham.

MUNICIPAL BANK.

31st MARCH, 1925.

| ASSETS. | | £ | s. | d. | £ | s. | d. |
|--|--------|-----------|----|--------|-----------|----|----|
| Cash in Hand at Head Office and Joint-stock Bank | | 471,103 | 11 | 3 | | | |
| Cash with Corporation ... | | 4,454,624 | 19 | 6 | 4,925,728 | 10 | 9 |
| NOTE.—The Corporation holds upwards of £3,500,000 British Government Securities. | | | | | | | |
| House Purchase Department— | | | | | | | |
| Amount repayable by depositors ... | | 658,466 | 4 | 7 | | | |
| Land Settlement (Facilities) Act, 1919:— | | | | | | | |
| Amount repayable by small holders as at 31st March, 1924 | | | | | | | |
| 826 | 18 | 1 | | | | | |
| Less.—Repayments during the year | | 395 | 17 | 2 | | | |
| | | 431 | 0 | 11 | | | |
| Amount expended on the Purchase and Adaptation of Premises for Permanent Branch Banks and those in course of erection— | | | | | 658,897 | 5 | 6 |
| As at 31st March, 1924 | 51,568 | 9 | 2 | | | | |
| Additions during the year | 10,859 | 7 | 7 | | | | |
| | 62,427 | 16 | 9 | | | | |
| Less.—Depreciation | 1,443 | 11 | 5 | | | | |
| | | | | 60,984 | 5 | 4 | |
| Furniture and Equipment at Head Office and Branches— | | | | | | | |
| As at 31st March, 1924. | 7,201 | 13 | 3 | | | | |
| Additions during the year | 2,563 | 5 | 2 | | | | |
| | 9,764 | 18 | 5 | | | | |
| Less.—Depreciation | 2,560 | 8 | 11 | | | | |
| | | | | 7,204 | 9 | 6 | |
| Sundry Debtors, including Claim for Repayment of Income Tax | | | | | 68,188 | 14 | 10 |
| GRAND TOTAL ... | | | | | 37,046 | 0 | 6 |
| | | | | | 5,689,860 | 11 | 7 |

that, in our opinion they represent a true and correct statement of

(Sd.) J. R. JOHNSON, F. S. A. A.,
Treasurer of the Bank.
(Sd.) AGAR BATES NEAL & Co.,
Chartered Accountants

handle government treasury business. Necessary limitations as regards notice of withdrawals, amount to be withdrawn etc., as are usually prescribed in the case of savings banks should, of course, be imposed in the case of similar deposits of these banks. The most important reason for suggesting the introduction of this class of banks is that on account of local influence and prestige the local bodies would greatly assist in speeding up the development of banking habits. They would supplement the work of post office savings banks so far mobilisation of mass savings is concerned. To suit the convenience of the labouring and poor classes business hours of the branches of municipal banks situated in such localities may be so fixed as not to clash with the periods of their work or attendance ; or again they can open offices on different days in different localities.

Usefulness of municipal banks would be considerably enhanced if their services could be enlarged to meet some other demands of the community as well. For example, if municipal banks take up the duty of paying house-tax, water-tax and charges, lighting charges etc., which are usually due to the municipalities from the deposit accounts of their depositors, a good deal of convenience would accrue to the local people. The work will be quite simple for the banks. They will have simply to make transfer entries. Also if the banks invest a portion of their funds in meeting occasional need for loans of their depositors a greatly needed want would be supplied. The poor although possessing sufficient tangible security are often obliged by circumstances to fall into the clutches of devouring money-lenders who literally fleece them. If they opened " pawn-brokers " department where the needy

could get occasional assistance against the pledge of their wares the municipalities would not run any danger of losing money. If necessary the banks could appoint a guarantee broker who on a nominal commission would assess the value of the pledge and determine the amount to be advanced and in case of the borrower's failing to repay the advance, would meet any short-fall that may result after the security has been exhausted. This function of guaranteeing "pawn-brokers" loans could be very conveniently combined with the duties of the cashier or treasurer. Moreover, the banking committee of the municipality on account of local knowledge would be able to assess the need of the borrower and test the estimates of the treasurer. Some of the municipal banks in Europe greatly assist their local population in such advances.

House accommodation for the local population and town improvement are important problems which local bodies have often to tackle. Any measures which can induce ordinary middle class people to own or build their houses or induce congested population to move out and inhabit new plots, should always be welcome from all points of view. The municipal banks can greatly encourage efforts in these directions by agreeing to advance some amount on the security of the mortgage of the property to be bought or built. Of course the borrower would be required to find a portion, say half, himself and the rest could be advanced to him. The loan could be repaid gradually, say by monthly instalments. It would be easy for municipal appraisers to determine the value of the mortgaged property because they often handle such matters. An approximate indication

about the worth of a house is the house-tax which is being paid to the municipality, because that tax depends upon the annual rent and rent is one of the basis of valuation. Moreover, banking committee of the municipality can further scrutinise the valuation from local knowledge and recent similar sales. The bank would not stand to lose anything. Experience of other municipal banks which render this kind of assistance to their depositors shows that monthly instalments are punctually paid.

Advances of the nature referred to above should be made on very conservative basis and within certain proportion to the total funds. A good bit of the bank's funds should be invested in first class negotiable securities so that in case of emergency the bank should be able to meet the demands of its depositors and not make them lose faith in it.

Another way of utilising the bank's money would be for the purpose of municipal finance. At certain times of the year the incoming revenue may not be sufficient to meet the current expenditure. And temporary ways and means advance from the bank, or the utilisation of its funds, would enable the municipality to pass over the difficulty. The advance could be repaid from the subsequent surplus revenue. Again a part of the bank's funds may be utilised for capital purposes. Great caution is, however, necessary when such advances are taken because there is always a danger of overdoing them. It would be very desirable if some limitations could be imposed upon the proportion of various advances to be made by a municipal bank. The bank should maintain a cash percentage of 15 to 20 per cent. of deposits; and a further 40 per cent. should be invested in nego-

liable and readily saleable securities. These items will keep the bank's position liquid and enable it to meet even panicky demands of its depositors. The remainder of its funds may be utilised for making advances of the nature referred to already. Deviation from the investment percentage *viz.* 40, may be allowed in special cases by the Banking Council, in order to enable the municipality to meet its capital programme, provided the bank's general position is otherwise safe and not likely to cause any anxiety.

There would be no harm if the municipal banks offer safe custody facilities. We have referred elsewhere how people badly need such an arrangement specially in small places.

As regards the method of keeping funds of the municipal banks there are two practices :—

- (i) which keep the funds separate in every respect; and
- (ii) which merge the bank funds into the municipal funds.

Whatever method is adopted it practically amounts to the same thing, as virtually the municipality is responsible for the affairs of its bank and shall meet any losses that its working may disclose. In the case of (ii), however, the municipality should hold liquid investment and maintain cash position at least to the extent suggested above.

The management of the bank should naturally be in the hands of the municipality. The members could elect a committee to be in active touch with and superintend the bank. The banks' officials and staff would be under this committee. The "Local

Fund" auditors should audit the bank accounts just like all the other accounts of the municipality. Besides the municipal control and routine audit of auditors, there should be occasional independent supervision and examination of the bank's affairs by the Bank Examiners. Municipality or the bank should pay for such examinations and visits. The Banking Council as in other banking activities should be the final administrative authority for municipal banks as well.

Profits resulting from the working of the bank should not be taken to ordinary municipal revenue. A portion should be set apart every year to form a Reserve Fund and the balance should be utilised for beneficial purposes like education, sanitation, medical aid, local improvement and so on.

The bank should be free to open offices and sub-offices within the municipal boundaries. In a large place like Bombay or Calcutta some twenty local offices can be conveniently opened. Possibly all these offices may not be busy whole day. Hence to economise working costs such branches may be kept open only on certain days of the week or only at certain hours of the day—same staff sufficing, by turns, for the work of a number of offices. This is how the Birmingham Municipal Bank is working a number of its smaller offices.

The outline of municipal banking constitution which we have given above is based upon practical experience obtained by similar banks in other countries and appears to be quite suitable for adoption in India as well.

CO-OPERATIVE BANKS

We have explained in preceding chapters the principles of co-operative banking in connection

with agricultural credit and credit for artisans. The principle, is however, capable of being applied to any set of individuals having some common bond or community of interest, *e.g.* labourers of the same mill, clerks of the same office, employees of the same railway, people of the same profession, occupation, caste or locality and so on. The services which such institutions render are: (i) They provide a convenient machinery for promoting savings of their members; (ii) They make their members industrious by facilitating advances for productive purposes; (iii) They eliminate usury by offering credit at reasonable cost; (iv) They train people in business methods and self-government and endow them with sense of social responsibility; and (v) They enable the members to borrow for their requirements on their collective or total credit, whereas individually they might not succeed in raising any money. Almost all the co-operative banks are based on two common principles; equality in privileges and democracy in votes. As the subject of co-operation has been already dealt with in detail it will serve no useful purpose to repeat here their mode of formation, and we must pass on to another section.

PRIVATE BANKS AND BANKERS

This section does not require any special treatment. Private banks and bankers should continue their activities as best as they like and no sort of hinderance or check or regulations should be imposed upon their business. The sanctity of private business so long as its liability is unlimited and it does not violate public morals should be left untouched. Moreover, in practice it would be difficult to segregate them from other private business concerns because

very often such banks and bankers combine other business with banking. They should be left to be judged by their customers who naturally are not blind to their own interests. If such banks do not give sufficient publicity to their affairs or appear to be violating safe principles of banking their customers can be expected to bring pressure upon them. In their own interests this class of people will tend to reform themselves if they wish to continue their business satisfactorily. Some of the private English banks have begun recently to publish statements of their accounts to keep up confidence of their clients. Similar bodies will do so in India also, specially when banking facilities on the part of public companies are introduced in accordance with the suggestions given in this book.

It may, however, be mentioned here that private bankers would greatly enhance their business and confidence in themselves if they confined their attention to banking and allied activities and did not participate in active trading, involving trade risks. They could, of course, continue their commission agency business but anything smelling of trading on their own account with the depositors' money would in the long run be injurious to their prosperity. They can do bill-brokers' and discounting business which affords great opportunities. They can thus be a connecting link between ordinary small borrowers and big banks. Such houses play an important part in English banking and to some extent in this country also. These activities are capable of expansion to the mutual advantage of themselves, corporate banks and borrowers.

“Local” and “Provincial” banks referred to in an earlier chapter offer great field for private bankers. They can suitably convert their present business into either of these classes, according to their present business and means, on the principles of limited liability and reap all the advantages resulting from such organisation. They can continue to have principal hand in the active management, as well as maintain personal contact with their localities and at the same time reap principal profits. The remodelled companies on account of the public examination and superintendence, would inspire greater confidence and thus lead to increase in their business.

Besides the above way in which private bankers can reorganise their business with great advantage, there is another important direction also *viz.* combination of private bankers with corporate banks which affords great field both for useful work and profits. In Germany banks are sometimes constituted on what are known as “*Commandit*” principles. In addition to the responsibility or guarantee of the bank’s capital, its liabilities are further secured to an unlimited extent by the personal fortunes of some of its principal controlling officers who rank as private partners with it. Such personally liable officers have chief voice in the management, though of course they pay great regard to the advice of the directors or representatives elected by the shareholders. They contribute a portion of the capital as well. They are as a rule men of some substance and inspire confidence in the bank’s customers. They are usually bankers with adequate experience and know how to work banks on sound lines.

Because they are personally liable they do not take any undue risks or do speculative banking. They do not get any salary but receive 20 per cent. of surplus profits after paying a certain minimum initial dividend (usually 4 per cent.) to the stock-holders. Certain percentage of profits is also taken to reserve until it reaches one-third of the capital. In case of the bank's liquidation if the surplus or reserve is intact, partly or wholly, one-fifth of the same is paid to such director partners. Any one of these partners can retire and sell his interest to others, provided the affairs of the bank do not disclose any necessity of falling back upon his personal fortune and the substitute is acceptable. Such retirement is usually made on account of advanced age. In many cases such transfers are made in favour of a son or next-of-kin of the retiring partner and the partnership share continues to remain in the same family. Some of the biggest banks of Germany are registered on the "*Commandit*" basis. The "*Darmstädter und National Bank*," which is one of the "D"* banks of Germany, is working on these principles.

The partnership co-operation of the Indian private bankers with the joint-stock banks on the principles referred to in the preceding paragraph affords ample opportunities of mutual benefit with very great advantage. Such combinations can take place in all types of joint-stock banks referred to in the chapter on "Bank Law." "Local" banks,

* It is simply a coincidence that the names of the biggest banks of Germany begin with "D" and they are colloquially and collectively known as "D" banks. They correspond to the "Big Five" banks of England. Their names are Disconto Gesellschaft, Deutsche, Dresdner and Darmstädter.

however, afford a very prosperous field. The local private banker on account of his local knowledge and local associations can strengthen his private business by converting it into a limited liability corporation and at the same time continue to be a partner with it. A special share of surplus profits would be paid to him on account of his taking unlimited liability and looking to the management, and as such, he would continue to reap special benefit, on the strength of his private fortune and banking abilities, which he was getting when he had private business. The result of converting his private business would thus not affect him so far his personal income is concerned. On the other hand there are chances that such income would be increased. By his associating extra capital, albeit on the limited liability principles, he not only gets more funds but enhances the respectability of and confidence in his business and as such the business progresses, resulting in all round increased profits. Moreover, he can retain such partnership in the family after his retirement as is a chief feature of Indian joint-family system. Unfortunately history of small joint-stock banks in this country has been full of unhappy episodes; and although the Government control which has been suggested already is expected to restore them to public confidence, we think it would build up that confidence more speedily, if in addition to the State supervision, the public are assured that losses, if any, would be made good from the personal liability of the principal officers of the bank, who work on partnership basis. The banks will of course continue to be regarded as public corporate banks for the purpose of registration

formalities, restriction on business, administrative control of the Banking Council, the Comptroller and Examiners of Banks, the payment of security deposit and taxes and other similar details. The only difference would be that their clientele would get additional guarantee for losses and the profits would be distributed in a pre-arranged manner.

CHAPTER XV

GENERAL

Factors which, though not a part of the organisation, will assist and accelerate banking construction : Propaganda—Vernacular accounts and signatures—Stamp duty—Modification of Commercial law relating to Mortgages, Pledge and Hypothecation, Registration of trade names, Investment of trust funds—Bank of issue's special facilities—Government and cheque currency—Prize drawings—Bankers' association : provincial associations and their federation—Institute of Bankers—Conclusion.

We have given our views in the preceding chapters as to how banking in India should be organized to adequately serve the economic needs of the country. There are, however, several other factors which although not a part of the organization will greatly assist the formation and accelerate the growth of Indian banking. We shall now briefly describe these supplementary measures.

PROPAGANDA

However well thought-out, useful and important a scheme may be, its success is greatly strengthened by a vigorous propaganda in its favour. All associations in the country whether under official or non-official control should from time to time preach the importance of a sound banking system to the country and that the Indian banks should be encouraged and patronised. The Indian National Congress and political and social conferences should impress upon their audience the great necessity of public co-operation in the promotion of banking in India. It

is really surprising that the wide awake political body like the Indian National Congress which is championing the cause of Indians in every respect has not made any effort so far to popularise Indian banking. Trade Associations and Chambers should regard it as one of their principal aims to help Indian banking and to ask their members to keep accounts with Indian banks—what right has an Indian trader or manufacturer to ask for public and government support for the promotion of his *Swadeshi* enterprise if he, in turn, does not possess the same feelings for the *Swadeshi* banks? The government officers, in their durbars and other public functions, whenever opportune, should describe the great banking need of the country and why the people should have accounts with Indian banks. The Government should not favour or sympathise with any one particular bank, like the Imperial Bank of India but treat all the banks alike. Discrimination in favour of any one single bank or a set of banks would dwarf the progress of general banking. Similarly the bank of issue should not extend special patronage to any particular institution. This is one of the greatest reasons why its agency business should not be reserved for the Imperial Bank of India as suggested by the Currency Commission. Growth of one bank, albeit howsoever important or big, is not banking development. Patronage as regards agency work should be so distributed amongst the banks of the country as not to throw any suspicion of inferiority or insecurity on any bank. All banks whether big or small are required by the country to do their part in her development, each in its own way. The press of the country should also do its duty in this respect, whenever con-

venient, and impress upon the newspaper readers why for the country's advancement, indigenous banking development is necessary.

If habits of thrift are inculcated in the people from their young age they would have lasting effect. The "Home Safes" * introduced by banks are a great instrument of propaganda and familiarise people to banks. The Central Bank of India, Limited is the only bank so far that has introduced them in this country, and deserves public appreciation for this enterprise. It has sufficiently demonstrated the utility of these small iron receptacles as a means of economy and of promoting banking habits. The system deserves wider popularity. Specially students should be encouraged to form a "home-savings" habit; and for this, if necessary, small departments may be attached to schools and colleges to facilitate such accounts.

We are conscious, that some would argue that it is dangerous to carry on propaganda in matters of banking, because that involves safety of money. From the scheme of organization outlined in the preceding chapters the whole system has been suggested to be brought under public supervision and scrutiny and legal measures safeguarding depositors' interests are recommended. With the introduction of those safeguards banking would be safe. Whatever scruples there may be at the present

* These are small iron receptacles, of the size about 4" x 3" x 2" issued by banks to their savings banks constituents. The "Safes" are locked, the key remaining with the bank. They have small apertures through which coins and notes can be thrown inside but not withdrawn unless the lock is opened. At convenient intervals they are taken to the bank which opens them and credits the "savings" to the accounts of the depositors.

moment in carrying on the public propaganda would disappear when Indian banking has been put on systematic basis.

VERNACULAR ACCOUNTS

All the existing banks at present carry on their work in English and follow the English system of accounting. Many of them are reluctant to open accounts of those who cannot sign their names in English ; or even if they do so, they insist that either such depositors should sign the cheques in advance in the presence of their officers, and then fill in blanks as regards date, name and amount, as necessity may arise, or that they should indemnify the bank against fraudulent signatures. Both of these arrangements imply considerable risks to the depositors. Again great difficulties are experienced in the matter of negotiating instruments bearing vernacular endorsements as banks, specially the Imperial Bank of India, raise great difficulties in these matters. Sometimes in the case of female signatures on cheques, counter-signature of a magisterial officer is insisted upon. It is really strange that the vernaculars should be at such a great discount. Knowledge of English language may be of great advantage but it is not essential to the people of the country or to its commercial and banking activities. Many of the most respectable Indian houses carry on their business through the medium of Indian vernaculars, and to deny or restrict to them banking facilities is not in the national interests. In justice to the languages of the country as well as to speedy up banking development restrictions should be removed upon the language in which

accounts could be kept by banks or in which depositors could negotiate or sign cheques and bills. Restrictions, whenever necessary, may be imposed upon the form of accounting in the case of public companies but not upon the language in which such accounts are maintained. The Bank Examiners, if they are natives of this country, can easily pick up Indian languages for the purpose of audit even if they happen to belong to a province different from the province of their office.

STAMP DUTY

The present scale of stamp duty on cheques and negotiable instruments is prohibitive and not a little impedes the growth of handling and use of cheques and bills. More than one responsible person has recommended modification of this scale. On a motion in the Central legislature the Government of India commenced last year to ascertain public opinion in favour of reduction of stamp on cheques. The Hilton-Young Currency Commission in their report in paragraph 216, under "means to promote banking development," say: "Of the other measures which are understood to be under consideration, one which appears to us likely to be particularly fruitful is the abolition of the present stamp duty on cheques. This charge is undoubtedly an obstacle in the way of the development of banking in the country. It probably tends to restrain many people from opening current accounts and so making payment by cheque instead of cash. A similar duty was at one time in force in the United States of America. It was found to be unsatisfactory restraint upon the use of cheques and upon economy in the use of currency and was abandoned....."

Abolition of stamp on cheques would accelerate the use of cheque-currency.* But equally important is the reduction, if absolute abolition be not practicable from the point of State finances, of duty on bills. Popularisation of bills as a means of credit with the natural consequence of discounts and rediscounts is greatly required for the advancement of banking. The present scale of duty considerably impedes the "bill-habit." We personally favour total abandonment of stamp duty on bills. The Government should recoup loss of revenue resulting from this course in some other suitable manner. In the course of time, banking development and banking prosperity would add to the sources of Government revenue in some other ways which might compensate even to a greater extent than the portion lost under this arrangement. And if subsequent events do not warrant its continuance, the duty can be re-imposed.

COMMERCIAL LAW

The Indian law regarding commercial and banking transactions requires to be modified, if not generally, at least in the case of *bona-fide* banking transactions. Apart from the vexations which banks experience at the hands of Indian courts, specially in the up-country places, either due to want of experience of commercial cases on the part of the trying judges or due to the slowness and indifference of judiciary, the law regarding securities in the banks' possession should be simplified so as not to involve

*It is gratifying to record that the Finance Member announced in the course of his Budget speech on the 28th February 1927, that from 1st July 1927, stamp duty on cheques and demand bills would be abolished.

cumbersome procedure. Improvement in this direction will greatly add to the usefulness of credit institutions. We suggest the following few amendments.

Mortgages.—At present equitable mortgage is permitted only in certain places and banks cannot make use of it as a substantial security at all places. The law should be modified so as to legalise equitable mortgage in favour of banks registered under the Indian Bank Law or incorporated under special acts of the central and provincial legislatures. Whatever objections there may have originally existed against allowing equitable mortgage uniformly throughout India, they do not exist to the same degree now; and even if they do, corporate banks on account of being subjected to public supervision and examination will hardly abuse the facility. Many a time it happens that a party requires financial assistance urgently which cannot await completion of legal formalities in connection with mortgages and registrations. If there were facility of creating security by mere deposit of title deeds, as is the case in Presidency Towns, in England and other countries, many a deserving concern would get timely aid. Sometimes it happens that a constituent wants accommodation very temporarily and the only security he can offer is property. If he were to execute legal mortgage the cost would be great and out of proportion to the price he should pay for obtaining credit. If this anomaly were removed credit transactions through banks would be greatly facilitated.

Some improvement is also necessary in the case of legal mortgages. At present it is only

“English” mortgage that gives power to the mortgagee to sell the mortgaged property, if the mortgagor does not abide by the terms of the mortgage deed, without the intervention of a court. In all other cases the mortgagee has no such power and he must appeal to a court for fore-closure. Those who have experience of these matters know how annoying, troublesome, and dilatory are the court proceedings in this connection. If the banks had power to enforce clauses about fore-closure and sale of mortgaged property, in case of non-observance of terms about payment, etc., bank borrowers would be more punctual which would induce banks not to shun this security for *bona fide* short term loans. This power is essential in the case of mortgage and industrial banks, otherwise the borrowers, not being afraid of their properties being seized for satisfaction of debt, are liable to be lax, which would dislocate financial operations of banks. If the interests of debtors are a concern of the State, the interests of creditors should be equally looked after. Punctuality of payment makes the wheels of financial machinery move smoothly; and the providing of reasonable powers to induce it at least in the hands of *bona fide* and respectable institutions like banks, should not be shirked.

In the case of land-mortgage and industrial banks further special mortgage facilities, besides the power to foreclose, are necessary so as to enable them to seize, work and manage mortgaged property if at any time they think such a course advisable in their interests.

Pledge and Hypothecation.—It should be possible for banks, without the slightest legal danger, to

advance against factory stocks, stocks in trade, etc., in possession of the borrowers. At present some doubt is felt in accepting this security. If necessary, bank hypothecation register can be maintained in each district where pledge of goods to a bank should be registered. Facility of this nature would greatly facilitate supply of short term credit to *bona fide* traders and manufacturers.

Registration of Trade Names.—In England all trade names are required to be registered and the names of partners should be printed on the letter papers of firms. If either of these things is not done, it is a violation of law involving penalties. In India also the same law should be introduced. It would help banks to know with what people they are really dealing. Unless a person is trading beyond his means or wishes to benefit by keeping people ignorant about his trade relationship there should be no objection to the introduction of this sound measure.

Investment of Trust Funds.—The Indian law governing investment of trust funds should be modified so as to allow investment of these funds in bonds of industrial and mortgage banks referred to in the preceding chapters. Investments are absolutely safe. A change of this nature would increase public confidence in such investments and make them popular. This would be an additional reason for insurance companies and banks to deal in such securities.

Bank Law.—Chapter IX dealing with this matter, mainly refers to commercial banking. There should, however, be no objection to any joint-stock

bank being formed to do special type of banking business, like agricultural, land mortgage, industrial, etc. We have suggested incorporation under special charters of some special banks but that is no reason why private efforts should not be permitted in these directions also, if there is sufficient demand for their services. The banking law should, however, be modified on the basis of suggestions given in the relative chapters and the constitutions of such joint-stock banks should contain those modifications. The appropriate credit board should have preliminary superintendence over such banks.

BANK OF ISSUE'S SPECIAL FACILITIES

We have suggested arrangement of special facilities in favour of special banks at the bank of issue. The total of such arrangement may amount to a large figure ; and it is a natural question which some of our readers may put, whence this money is to come ? Is it to be provided by withdrawing or curtailing existing credit facilities to commerce and trade ? Our reply to the last question is, no. The organization of banking will increase bank deposits and thus increase volume of credit which banks will be able to allow. An appreciable portion of the suggested credit through the land mortgage banks will be utilised for repayment of loans already taken from money-lenders which will naturally throw an equal amount on the market either in the shape of investments or as bank deposits. Moreover, through the organisation of credit, deposits will permit grant of greater volume of facilities than it is possible in the present unorganized state of banking. Lastly, the inclusion of discounts and other securities as a part of the currency reserve

would enable increase in the volume of currency which would be sufficient to meet all demands, that can be foreseen at the present moment. Gold will lose much of its attraction, so far hoarding is concerned, and will be available for currency purposes. Gold will also be received to settle balance of international payment which is usually in India's favour. And on account of the feature of elasticity which has been suggested to characterise the currency reserves of the bank of issue, the quantity of gold that will be taken to the reserve will enable creation of currency to two and a half times its amount, the rest of course being backed by other suitable securities, (*i.e.* in reality by instruments of credit). We do not anticipate any difficulties on the part of the bank of issue to supply the facilities which we have suggested in the earlier chapters. As an ultimate source the bank of issue can fall back upon foreign markets for any assistance it may need, though as far as we can see there would be no necessity for such assistance. India may need foreign loans for capital purposes but they can be arranged independently of the liability of the bank of issue *e.g.* by special banks or through other channels. Other markets will not hesitate to accommodate the bank of issue if they are sure that it is properly organized and the country's banking system is based on sure and strong foundation.

It is far from our intention to suggest or imply that the bank of issue should be a medium of inflating currency. Currency and credit should be only increased to meet increased economic activities and only in proportion to the increase as actually takes place. That would keep currency and economic

activity at the same level without disturbing the value of monetary unit. Every one agrees that India has vast potentialities for economic growth and it is but meet to make arrangements for expansion in our currency to meet demands that it may be, hereafter, called upon to satisfy.

GOVERNMENT AND CHEQUE CURRENCY

The public knows at present how the Government stands in the way of the increased use of payments by cheques. If government dues are to be paid they must be paid in cash. If rates and taxes are to be paid they must be paid in cash. If telephone bills are to be paid to the Government telephone department the payment is not accepted by cheque: the department insists that payment should be made in actual cash to the local post office on its behalf. These hinderances do not encourage banking accounts. If banking and cheque currency are to be developed they must be allowed full field to play their part. The Government should authorise that all payments to be received on its behalf could be made in cheques—exchange or commission being charged if cheques are not payable locally at the place where payment is due. It is, of course, understood that receipts granted in respect of cheque payments should contain a provision that in case of non-realisation of the cheque, the receipt would have no value. Cash payment should be only insisted in cases where something is being handed in exchange there and then *e.g.* when buying railway tickets, and paying for the like.

The Government should permit all public departments like municipalities, local boards, uni-

versities, etc., to keep banking accounts in any properly constituted banks they like. They should not restrict them to any particular bank. In other countries, including England, all such bodies are free to choose their bankers. After the active control and superintendence which has been suggested to be given to the Banking Council it is no use discriminating between country's banks for this purpose, which would simply create discouraging suspicion. The local bodies should be trusted to possess sufficient sense of responsibility to look after the safety of their funds. Whenever absolutely necessary the Government can mildly give hints about caution which would be quite sufficient. The present method of the Government's distrusting and black-balling all excepting one bank is most discouraging to Indian banking. Some of the government officers have even gone to the extent of forbidding grant-in-aid schools,* major portion of whose funds are private, from keeping accounts with joint-stock banks, howsoever a respectable position they may have in the country's banking. Against this rigidity compare the attitude of the British Government which permits its officers to keep even government funds at their disposal in any joint-stock bank, according to their discretion. Is this calculated to promote banking ?

PRIZE DRAWINGS

Thousands and thousands of people are gambling at the race-course and games of chance with a view to gain something from nothing or over and above their stakes—or to live a life of excitement

* These are educational institutions organized through private effort. They mainly depend upon their own funds and receive small annual grant from the Government.

as some of their votaries are wont to describe. Whatever the real motive may be it is easy to see that betting or gambling is a great degenerating factor in human morals not unoften involving great misery and unhappiness. There are many instances in which people have been totally ruined; in others, the unfortunate victims have ended their penury by suicide. The contagion is rapidly spreading to the poorer classes. One often comes across the pitiful sight of families faced with starvation, having nothing to eat nor any money to buy eatables with, as the result of the earning members' having lost all their slender weekly wages on the race-course or in a gambling den. The losers take a solemn vow not to frequent such places nor "try their luck again." But as soon as the next pay day comes the magic of chance lures them---they first try to resist the temptation, the resistance becomes feebler and feebler till at last they are overpowered by the hypnotic temptation and the same tale of woe and distress is repeated. There are legislations trying to restrict or penalise such gambles but all the same the "wheel" goes round and round. Possibly there is something inherent in human nature which is fascinated by "chance"; or, is it because life itself is a "chance" that people cannot resist to gratify their impulses to try further chances?

Be as it may, it is quite clear that there is a strong desire in humanity to gain something from nothing. If this wish can be gratified without involving any serious consequences, if the attention of the people can be turned to some other ways which can satisfy this craving without the serious

risks at present attending games of chance, a great social and economic problem will have been solved. And if means could be found to associate habits of thrift with the trials at chance, the solution should be doubly welcome. The risk of losing all the stakes is replaced by certainty of accumulating savings, with the chance of an additional prize or fortune if the luck favours. This principle has been at present confined in its application although to a small extent, to prize or lottery bonds as explained in Chapter XII. But it is capable of expansion to the deposit accounts also. Let the banks so adjust their interest rates and shareholders' profits as to give them a margin of, say, half* a per cent. on their total deposits. This sum could be set apart for distribution as prizes by drawings to the depositors who should be allotted numbers on a certain basis. It may be necessary to allot separate prize amounts to different classes of depositors, current, savings and fixed--each depositor getting a number of tickets in proportion to certain "units of deposits" that may be prescribed. Separate drawings can take place for each class of deposits. A depositor does not lose anything of his deposit or interest due thereon but still stands the chance of winning a substantial prize if luck favours him. If he does not win a prize he has not lost the stake, nor is he faced with destitution as is the danger in other games of chance. With the hope of winning a prize some day, or with a view to increase his chances by entitling himself to more tickets, which will depend

* This is only a tentative suggestion. The figure may vary with different banks.

upon his deposit figure, he will have great incentive to save more and more. To show that the amount of prizes would not be small we may give a few figures. If the total deposits of a bank are Rs. 5 crores, Rs. 2½ lakhs would be available as total prizes. If the total deposits are Rs. 10 crores, Rs. 5 lakhs could be distributed as prizes. The total bank deposits in India are over Rs. 200 crores which could enable distribution of over a crore of rupees as prizes. Figures like these are very tempting. We feel confident that institution of this measure will promote banking habit rapidly. Under ordinary circumstances possibility or apprehension of loss to depositors through the unwise act of bank directors might restrict bank deposits; but as the banking activities are suggested to be under active State control and the representatives of depositors would work on the directorate, such chances of loss are greatly mitigated. And the desire to save together with a chance of winning a handsome prize would always impel people to entrust their savings, however small, to banks.

Laws of India should make issue of prize-bonds and distribution of prizes to depositors as explained above, possible. Human craving will be satisfied and at the same time investments and savings will be made more attractive. The Banking Council should exercise requisite control in this respect also and see that the banks do not unduly increase their prize funds. As in the case of interest, the Council should have power to prescribe the upper limit of rate at which the Prize Fund of a bank should be calculated. It should have right to appoint some one to superintend drawings, etc., if necessary.

BANKERS' ASSOCIATION

The banks of the country should form an association just like the British Bankers' Association* to consider matters of mutual interest. When all other activities find it profitable to join into a common body to consolidate and safeguard their business there is no reason why banks should not associate in the same manner. We have Chambers of Commerce, Mill Owners' Association, Insurance Association and so on. If the banks join together they can always take concerted action for their common good as well as suggest to each other how to improve their importance, business

* There are in London at least five organizations that may be classed as professional organizations of the banking business. These are : (i) The British Bankers' Association—an association of banks and not of individuals, whose primary object is to provide facilities for the discussion of matters of interest to bankers, (ii) The Committee of London Clearing Bankers—a committee of banks that are members of the Clearing House, whose business is to consider matters relating to the Clearing House and, generally speaking, all questions affecting London joint stock-banks. (iii) The British Overseas Banks' Association—All British Banks engaged in overseas banking, having an office in London are eligible for membership. The Association's objects are to "further the interests of the banks comprising the association, it being understood that the special and particular local interests of said banks in their respective fields of operations are excluded from the scope of the association unless at the request of the banks concerned and with permission of the General Committee." (iv) The Institute of Bankers—This body looks after education in banking subjects, conducts examinations, facilitates consideration and discussion of banking matters, takes measures to promote interests of banking, &c. (v) The Bank Officers' Guild—This is a trade union of bank clerks. "Among other objects it seeks to co-operate with directors in all educational facilities that will encourage the higher education of bankmen and produce general technical efficiency, and above all, to establish Whitley Council of bank employees and bank directors for the discussion of aims, ideals and grievances, affecting the staff and the profession. The Guild has a membership of about 30,000, but is not formally recognised by the management of banks"—MINTY.

and prosperity. In times of difficulty they can club together and devise means how to overcome them. If any abnormal situation arises in trade, industry, agriculture, labour, etc., they can determine a common line of attitude or action so as to properly control the situation. The Association can make representations to the Banking Council, the Government and other public bodies whenever deemed necessary for the common good. Joint and combined representation has always more value and force than individual representation. It is true that the Banking Council acts as a co-ordinating agency but private co-operation has its own meaning and significance.

It would be advisable if there is a bankers' association in each province and all the provincial associations should be federated under an All-India association. All the banks working in a province should be eligible for membership under certain rules and regulations. The provincial associations should elect their Federal Board which should convene meetings of federated associations say, once a year or whenever necessary.

INSTITUTE OF BANKERS

Like the Institute of Bankers, London, there should be a similar institute in India. The Indian institute should have central office at one place, say, Bombay, and provincial branches in each of the Indian provinces. If necessary, district offices could be opened later in important districts where banking activities prevail in a sufficient degree. The objects of the institute should be, to promote banking knowledge and education both from the

theoretical and practical stand-points, to afford opportunities for the discussion of matters of interest to bankers, to take any measures which may be desirable to further the interests of banking, etc. Universities and Commercial Colleges do impart some amount of useful banking education but as they do not possess points of contact with practical banking, the education is lacking in ideas of practical application. Persons engaged in banking should be eligible for membership. The institute should arrange for banking lectures and examinations and should issue diplomas. It should conduct a banking journal as well. In view of the increasing great importance of foreign languages it is desirable that the institute should make special arrangements for their study, either independently or in collaboration with other educational institutions. If Indians want to do foreign banking and foreign trade successfully, knowledge of foreign languages is of paramount importance.

CONCLUSION

The present is the most opportune time to take up the task of reconstructing Indian banking. The Currency Commission's report has again brought the problem in the fore-front. The question of Reserve Bank for India, strongly recommended by the Commission and reported to be greatly favoured by the Government of India and many public bodies, is only a part of the bigger question of banking reformation. In our own opinion the matter should be taken all together and not piece-meal. The foundation of Reserve Bank on right lines may induce to some extent increased banking activity but it will not be sufficient to completely solve

the problem. Moreover, its constitution and working should be determined not in absolute isolation but with relation to the whole banking system. The whole subject should be collectively taken. Let us hope that the Government of the country fully responds to the demand for thorough investigation in this connection, which is getting more and more insistent and acute every day, and appoints a competent body to examine the Indian banking problem. The Commission or Committee, whichever may be formed for the purpose, should not hurry over the matter. The examination should be minute. If necessary, the examiners may undertake a tour round the world with a view to study on the spot other banking systems and then determine the scheme of organization for this country. The United States of America permanently solved her banking and currency difficulties by appointing a commission which was asked to travel over the world and personally examine different systems and then submit proposals to solve local problems. As already said elsewhere, the report of the Commission is a marvellous contribution to the banking and currency literature of the world. If the proposed Indian Banking Enquiry Committee contains proper Indian representation and undertakes the work on the same lines we are sure their labours would produce an equally momentous document and considerably assist in the permanent solution of our banking and currency requirements.

APPENDIX A

Remarks on Bill No. 2 of 1927 *re* Reserve Bank of India.

[The bill was published on the 17th January, 1927, in the *Gazette of India Extraordinary* of the same date.]

The above bill was published when the book was in print. The subject of Central Banking and Reserve Banks has been fully dealt with in chapters V and VIII. Appendices C and D contain charters of two of the most important central banks in Europe. It is hoped their reading will enable the reader to assess the bill at its proper worth and determine the changes which should be introduced before it can satisfy Indian requirements. However, to focus the attention we are indicating below the main points of the bill which require principal consideration.

It would be better if the constitution of the Reserve Bank is deferred till the question of banking organisation and reform is solved. The Reserve Bank will be only a component, albeit a very important component, of the banking system and it is necessary for satisfactory and permanent solution that the problem should be considered as a whole, at one time, and not part by part. If subsequent investigations about the banking construction show that the constitution of the Reserve Bank as now determined, requires changes in certain directions it would be difficult, if not impossible, to bring them about. The question of compensation to the shareholders and many similar obstacles will arise. When the Imperial Bank of India was founded in 1921 it was considered as a proper advance in banking development, but a few years of experience have shown that it does not satisfy all requirements and that there should be another central institution. And this means compensation to the Imperial Bank shareholders for which people will have to pay. Who knows that after some

PRELIMINARY OBJECTION.

years of working or when the problem of banking organisation is tackled it will not be necessary to alter the constitution of the proposed Reserve Bank, so that it may better fulfil its mission? And then the same question of compensation to its shareholders would again arise. Moreover, as will be shown later, compensation out of all proportion is designed to be given to the Imperial Bank, which will be all saved to the government, if the Imperial's agreement is allowed to run for the full period. The Reserve Bank is proposed to be brought into existence in 1929 and the Imperial Bank's agreement expires early in 1931. Is it not better to defer the measure for a small period of two years and save all the immense advantages which are being conferred on the Imperial Bank? And further, we can profitably utilise the interval for investigating the whole banking problem, giving proper weight to each factor and considering each component in relation to the others. By rushing through a measure of this magnitude and importance and ignoring other important issues we are surely paving a way for some defects in the future.

Subject to the above preliminary objection, the following are some of the main points which should be carefully looked into.

As the bill stands the charter can be renewed, on the expiry of the initial period of 25 years, by the Governor-General-in-Council. This right should be reserved to the central legislature. The legislature should have a voice in bringing about changes in the constitution which experience of the working of the Reserve Bank may warrant. Further the legislature should have power to discuss working of the bank. Provision should also be made for any amendments in the charter, that may be considered necessary hereafter, provided the same are accepted by the majority of shareholders and the legislators.

The bill provides that three-tenths of the capital should be offered in the first instance to the Imperial Bank and that the rest would be offered to the public. It is not defined as to who constitute the public, whether foreigners and non-Indians come

**LEGISLATIVE
CONTROL ON
THE BANK'S
CONSTITUTION.**

**CAPITAL &
DIRECTORS.**

under this term, nor is it provided as to who will make allotment and on what principles. It has been shown in chapter VIII why the Imperial Bank should not be shown any preference in the matter of capital. It has been also explained there why the capital should be reserved for Indians. The charters of the Netherlands Bank, Appendix C, and other Central Banks contain the provision that only nationals should be the voting shareholders. Looking, however, to the importance of English interests in India a portion of capital may be allotted to them but the amount should naturally be small so as not to give them the controlling hand. A representation made by some of the Indian Joint-stock banks to the Government contained a suggestion that the capital should be offered to the "scheduled banks." There are twenty six banks mentioned in the first schedule of the Bill (which are designated as the scheduled banks). Out of these nineteen are foreign banks, six Indian Joint-stock banks and the remaining one is the Imperial Bank. To distribute capital of the bank amongst these banks would mean handing of control of the bank to the foreign banks, which form overwhelming permanent majority. This, as already explained in the book, will be suicidal to Indian banking and economic interests. This suggestion about distribution of the capital appears to be based on the principles of the Federal Reserve Act. But foreign banks working in America are not allowed to participate in the capital of Reserve Banks and therefore the suggestion has no support from that direction. Moreover, the list of "scheduled banks" can be increased or decreased. And how would the banks that are "scheduled" hereafter get a portion of the capital of the bank? It would be unfair to debar them from participating in the capital simply because they did not come under the schedule at the time of incorporation of the Reserve Bank. It would not be right to submit the non-scheduled banks and the future banking concerns in India to the control of the "scheduled banks."

An equitable way of distributing capital, and at the same time safeguarding national interests would be to divide the capital in eight parts: one part to the Imperial Bank, one part to the foreign banks, two parts to the Indian Joint-stock

banks, including Central Co-operative Banks, and four parts to the Indian public. Basis of allotment in the case of banks should be paid-up capital and reserve. Provision should be made for increase in capital of the Reserve Bank for allotment to new Joint-stock banks, Indian owned and Indian managed, that may come into existence hereafter. Allotment of shares to the public might be based on provincial basis.

As regards directors there is no objection to the six directors referred to in (a), (c) and (d) of clause 9(1) of the bill. As regards the nine directors referred to at (b), four should be elected by the banks referred to above, one for each one-eighth part of capital and the remaining five should be elected by the ordinary shareholders. Out of the last five directors one should be elected to represent business interests in Bombay, one to represent business interests in Calcutta and the remaining three should represent business interests of the rest of British India. All the directors should be Indians excepting the one representing the Foreign Banks, the nominee of the Governor-General-in-Council (*vide d*) and the Governor of the Bank, who may be of any nationality.

A considerable portion of responsible Indian opinion appears to favour creation of a state bank in India, without share capital. We have dealt with this problem in the book and shown there how dangerous it is to entrust credit and currency control to such an institution. The advocates of the Indian state bank are of opinion that such dangers can be avoided by associating representatives of independent bodies, like chambers of commerce &c., with the nominees of the Government, in the governance of the bank. Such an association, to effectively overcome the dangers inherent in a state bank, should naturally contain greater portion of independent representation *i.e.* the nominees of the Government should be in minority. But this raises a fundamental question, how far should the Government be expected to relinquish its authority over the bank in favour of outsiders, when it is wholly and solely responsible for its working. If a Central Bank with preponderance of national capital and national directorate can be brought about, that would be by

**STATE
BANK.**

far the better proposition. But if our legislators do not succeed in establishing such a bank and there is danger of the Central Bank being dominated by foreigners, the alternative of a state bank may be accepted and sufficient safeguards prescribed.

The bills which should be admissible for discounts at the bank should bear at least one Indian signature. Similar limitation should apply to the credit policy of the bank in general.

**BUSINESS
AND RESPON-
SIBILITIES.**

The business of the bank should be primarily to facilitate Indian economic activities. This restriction is imposed on every central bank in every country. As the readers will have seen even the Bank of England does not extend rediscounting facilities to the Indian banks. If national considerations do not regulate the credit policy of the bank it is feared that the same state of affairs wherein non-Indians get a preponderating portion of financial facilities, as has been the complaint in the case of Presidency and Imperial banks, may be repeated.

Business of the bank should be ordinarily restricted to the banks working in India. However, there should be emergency provision to permit it to do business with the public, if the other banks combine to raise up the price of credit to the public or do not ration it properly or do not give sufficient business to the Reserve Bank to profitably utilise its funds.

Responsibilities of a special nature, calculated to promote banking, as referred to in the book, should be imposed. Like the Bank of France the Reserve Bank should lend cheap funds to the Indian Agricultural Banks. It should allow facilities of cheap discounts to the Indian Exchange Bank when it comes into being. It should help in making popular, bonds of land mortgage and industrial banks as referred to in the book. In times of panic it should try and restore confidence in banking institutions by extending all reasonable facilities. If any banks whose business is otherwise sound are faced with temporary embarrassments the Reserve Bank should give them every possible assistance

But if some banks are past redemption it should help in their liquidation or re-organisation as may be considered advisable, so as to reduce the inconvenience to the banking public to the minimum possible. Provision for these responsibilities and emergency measures should be now made in the charter and not left to the future. When the bank's charter has once received the legislative sanction it will be difficult to impose any new obligations. The shareholders will then refuse to undertake such responsibilities on the ground that their acceptance would lower their profits and be not in their interests. The only way to overcome such an opposition would be to offer some compensation or privileges. And how long should India pay unnecessary compensations for lack of foresight on the part of people responsible for such enactments ?

Provision should be made for the indianisation of the management, if not immediately, at least gradually. The Deputy Governor should be Indian from the beginning. All Provincial Managers at the end of the first fifteen years should be Indians. Competent foreigners may be engaged on contract service, in the initial stages, but future recruitment should be made in India and from Indians. Entrance and future promotion should not be by favouritism but by competitive and departmental examinations.

As explained in the book the bank should open at least one branch in every province. It is not necessary to open a branch in London. The Imperial Bank's branch there can easily represent the Reserve Bank, and do all its foreign business.

The Reserve Bank should establish a Banker's Clearing House in each of the Provinces. Its provincial branch should be the seat of provincial Clearing House, for provincial and inter-provincial clearings.

The bill requires certain banks mentioned in Schedule I to maintain a cash balance with the Reserve Bank amounting to $7\frac{1}{2}\%$ of their demand deposits and $2\frac{1}{2}\%$ of their time deposits.

As explained later scheduling of banks is injurious to the development of banking. It would be better if all the banks of the country keep certain cash reserves with the bank but the percentages should be reduced to 5 and 2 respectively. No further reserves should be required for the purpose of clearings. In seeing whether the reserve requirements are observed or not, balances of all the branches of a bank at all the branches of the Reserve Bank should be taken into calculation. Also inter-bank balances and deposits, and deposits against which advances are made, should be exempt from reserve requirements, if not wholly, at least to the extent of such " re-deposits " or loans ; *i.e.* only net balance of deposits, after deducting deposits with other banks and loans made against deposits, should be liable to cash reserve requirements.

If the Reserve Bank does not establish clearing facilities, it will be unjust to compel other banks to keep with it, without interest, a portion of their cash, more or less as locked-up reserves. Such a course will appreciably affect the credit assistance which they extend to commerce and also reduce their profits. Cost of every deposit in the books of banks will increase in proportion to the percentage required to be lodged with the Reserve Bank. This tax can be only justified if there is compensating gain due to economy in the handling of cash which Clearing House System makes possible. Unlike other countries payments by banks here are principally made in cash, which requires them to keep large amount of cash as till money ; then, they have to keep reserves for clearing purposes ; and if on the top of these two reserves they are required to maintain an idle reserve with the Reserve Bank that would be deliberately and unduly retrenching their power of extending credit. Further, if the Reserve Bank does not open branches in all the provinces, there will be instances where banks will not get equitable facilities, whether clearing or credit, at the Reserve Bank. For instance, the Punjab National Bank, Ltd. does its principal business in the Northern India and its main deposits are received in that territory. If it is compelled to deposit a reserve at flat percentage of its total deposits with the Reserve Bank in Bombay and Calcutta, the reserve

will be out of proportion to its clearing requirements in these two cities—and further why should cover for deposits taken in one part of India be compelled to be kept at such distant places? Nor, will the bank be able to take advantage of the credit facilities of the Reserve Bank at these places, to the full extent, even if it cared. And again what justification there is for transferring money from the Northern India for utilisation in the port towns?

There is no provision for rupee transfers. The Reserve Bank should take responsibility for telegraphic transfers between its branches at certain fixed rates. The rates are suggested in the book. If the bank opens offices in Calcutta, Bombay and Madras as at present contemplated, it is not understood how the exchange work will be cheaply carried on. At present the Imperial Bank with the help of the system of currency chests and their inter-transfers, is able to give cheap facilities in the matter of movement of funds. Will that work continue to be carried on by the Imperial Bank? It is imperative that the Imperial Bank should have no such monopoly. The responsibility should be undertaken by the Reserve Bank and for its satisfactory discharge it is necessary that the Reserve Bank should have more branches than at present contemplated.

We have explained in the book why it is extremely undesirable that one single bank should get special favour in the matter of agency arrangements. If the Imperial Bank is given the monopoly of this work that would greatly handicap Indian Joint-stock banks. Ordinary Joint-stock banks have done considerable amount of spade work for advancing banking in the country, in spite of the unequal competition of the spoon-fed Imperial Bank. They deserve greater credit and greater encouragement.

The bill does not clearly mention, nor does it give an estimate, of the amount of compensation that will be paid to the Imperial Bank. Probably this is purposely done to hide from the public gaze the huge sum that the Imperial Bank will get under the provisions of the agreement

RUPEE TRANSFERS.

AGENCY WORK.

COMPENSATION TO THE IMPERIAL BANK.

referred to in clause 42 of the bill. From calculations made it appears that under the proposed arrangement, when only three branches will be opened, the amount of total receipts and disbursements which the Imperial Bank will handle will be nearly Rs. 450 crores. Commission at $\frac{1}{10}$ per cent. on the first Rs. 250 crores and $\frac{1}{32}$ per cent. on the remaining Rs. 200 crores would be nearly Rs. 20 lacs. Interest on the free loan of Rs. 3 crores during the first five years even at a low rate of $3\frac{1}{3}$ per cent. would be Rs. 10 lacs.

Thus the Imperial Bank will get Rs. 30 lacs a year. Even taking into consideration that the Reserve Bank would open more branches in the future, which will decrease the amount of receipts and disbursements, and that the amount of free loan would gradually decrease, the average compensation to the Imperial Bank would not be less than Rs. 25 lacs a year for 25 years which means a total of Rs. $6\frac{1}{4}$ crores. Is it fair that the general revenues——because ultimately the surplus profits, after paying dividend to the shareholders at certain percentage, are payable to the government——should be defrauded of this huge sum? If the Imperial Bank does not agree to the forms of compensation suggested in the book it would be better to allow it to complete its agreement and establish the Reserve Bank in 1931. The only concession which the Imperial Bank foregoes by agreeing to the withdrawal of the government banking business is the loss of an average current account balance of at the most Rs. 10 crores for two years, 1929 and 1930. Computing this loss in terms of interest at 2 per cent. it comes to Rs. 20 lacs a year for two years. What business principle is it to pay Rs. 25 lacs a year for 25 years, besides other advantages, when the total loss is not more than Rs. 40 lacs?

It is not mentioned in the bill whether the money received by the Imperial Bank on behalf of the Reserve Bank would be immediately passed on to the Reserve Bank, or the Imperial Bank would keep it with itself on account of the Reserve Bank; and whether in the former case any exchange or transmission charge would be claimed by the Imperial Bank and in the latter any interest would be paid to the Reserve Bank on its

balances lying with the Imperial. These points should be clarified.

Besides the above compensation the Imperial Bank will get Rs. 3 lakhs of free loan in respect of each new branch it may open. This means Rs. 15,000 a year gratis, at the average rate of the Imperial Bank's investment. With such a subsidy it will be impossible for other banks to tap new avenues or for new banks to come into existence. Banks have already met with painful experience that whenever they have prepared any territory for banking operations and educated the people in banking habits, the Imperial Bank has not been slow to invade such fields and take advantage of their preparatory work, thus interfering with their reaping the fruit of their toil and initial efforts. This danger of encroachment will considerably increase if the Imperial gets such a substantial subsidy for each new office that it opens. With the help of such free money the Imperial can afford to reduce the price of credit to such a low level so as to make advancing by other banks unremunerative and thus drive them out. Banks are not afraid of wholesome and equal competition. But when competition is financed and subsidised nothing can withstand it. The concessions in their nakedness mean nothing but that the Imperial Bank alone should constitute the country's banking system.

Too much importance is given to the new branches opened by the Imperial Bank and the losses which have fallen upon the bank from such connections. We have fully discussed this question in the book. From analysis and deductions it appears that the net loss from all the new branches, if any, is not much. The amount of compensation suggested to be given is about one-fifth of the total expenditure of the bank per year. Surely the amount of net loss, if at all any, in respect of the new branches, which are mostly small and manned by junior officers, and many of whom are either self supporting or giving good profits, is not so much. Further, as suggested in the book the questions whether the Imperial's branches are really working at a loss, and if so, why, should be carefully examined. Branch profit and loss as apparently

indicated by the branch books is not always the true indication, whether it is working at loss or profit——there may be many factors attributable to it which indirectly help other branches and thus increase profit of the institution as a whole. When other banks do not find branch banking unprofitable on the whole, there is no reason why Imperial Bank should so find it. There is no justification for such an agreement unless it be that the Government wishes to make a free gift to the Imperial Bank. As already explained in the book, of all banks, the Imperial Bank is the least deserving of such a subsidy.

If the points explained in this Note are observed, there would be no necessity to maintain a schedule of banks which will be required to keep cash reserves at the bank or be entitled to credit lines.

SCHEDULED BANKS. When branches are opened in all the provinces it would be possible for all banks to observe the reserve requirements. As regards credit facilities the same should be left to the discretion and judgment of the bank directors. Differentiation between banks as "scheduled" and "non-scheduled" would tantamount to classifying banks as superior and inferior and it is not in the interest of banking development to legally introduce any such distinction.

There are some further points which require attention. They can, however, be easily studied by referring them to the principles already expounded in the book. In the end, let us hope that the constitution of the bank when it finally emerges from the Legislative Assembly and the Council of State really bestows upon the country that liberalism in finance which the Finance Member promised when introducing the measure—real liberalism and not the sham form of independence which gives by one hand and takes, possibly more, by the other. If Sir Basil Blackett succeeds in giving India a central bank whose sole object would be to control credit and currency in the Indian national interests he will have earned great gratitude of the country.

NOTE.—This opportunity may be taken to say a few words about the modifications intended to be introduced in the

Imperial Bank Act of 1920, *vide* Bill No. 3 of 1927. There does not appear to be any necessity to continue the Act. It would be far better to remove it from the Statute Book and allow the bank to be reincorporated under the Indian Companies Act. Of course, if the Imperial Bank agrees to be the Indian Exchange Bank as suggested in the book a suitable fresh charter may be framed. But there does not appear to be any necessity to continue preference to the Imperial Bank by continuing its incorporation under special act of the legislature or to involve the legislators into the botheration of amending the act for the sake of one private company, when common machinery of the Indian Companies Act already exists for the purpose.

RUPEE=STER

RUPEE-STERLING EXCHANGE.

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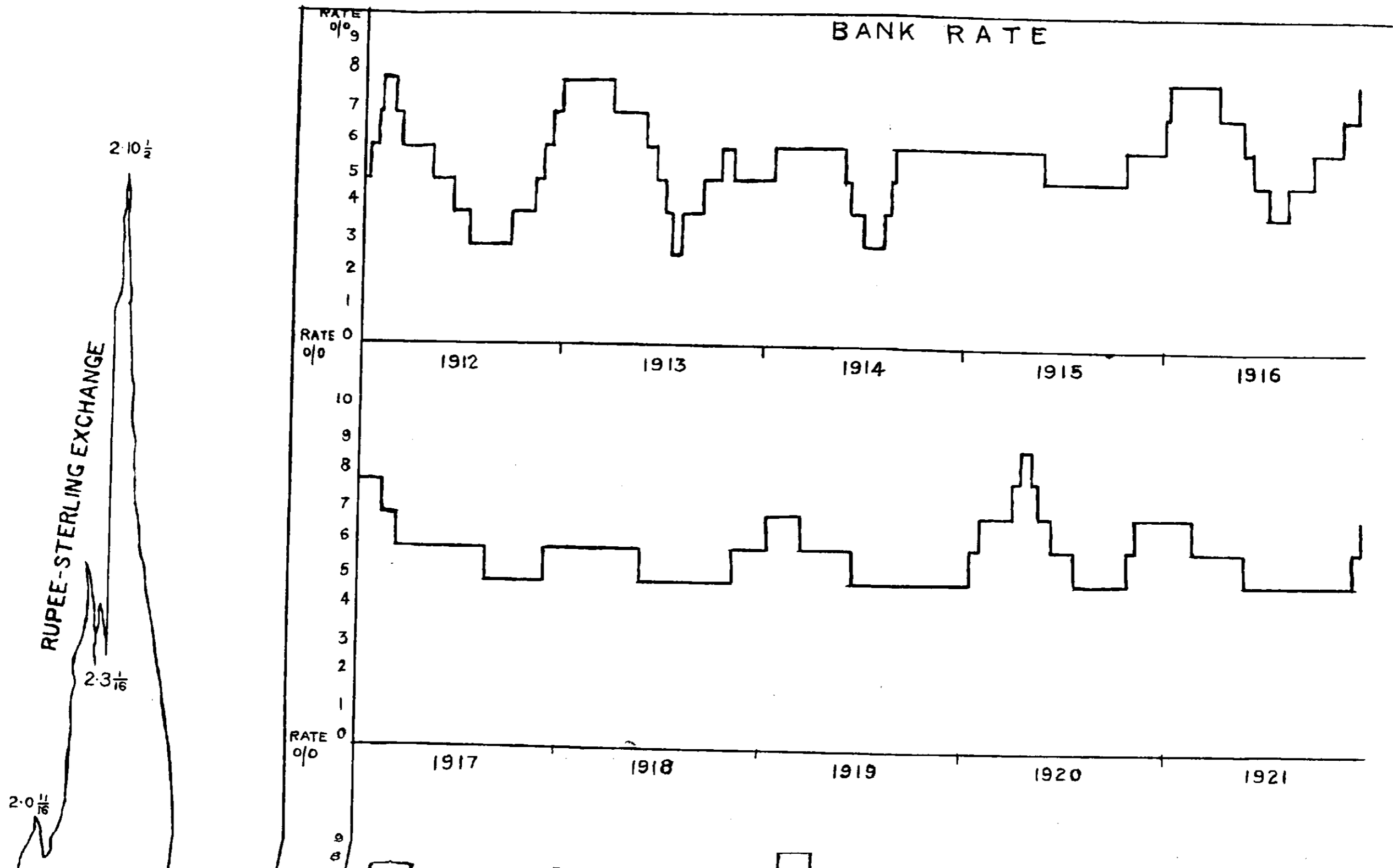
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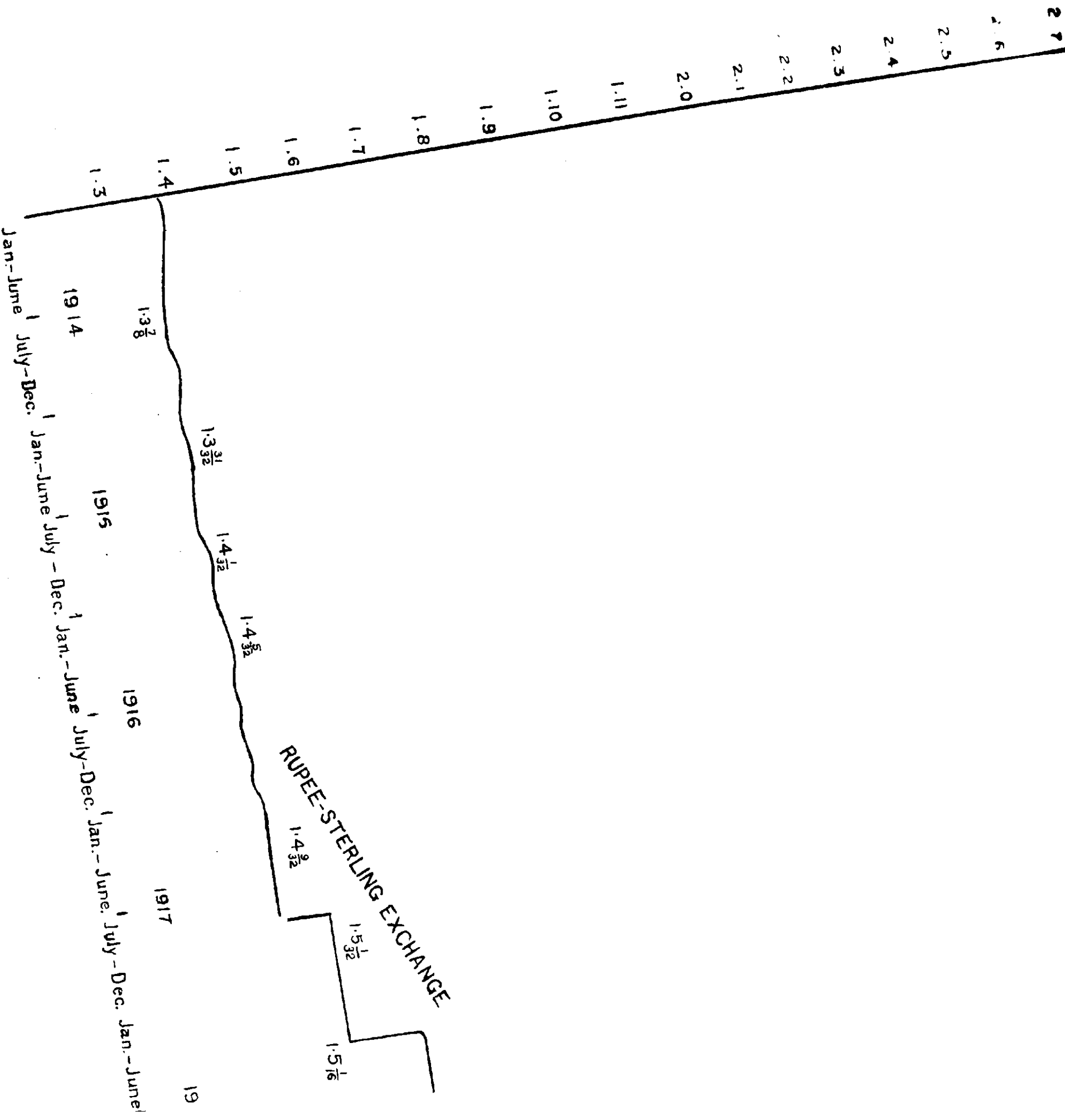
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EXCHANGE & BANK RATE 1914-1925)





APPENDIX B

NOTE ON CURRENCY

The word was originally applied to the currency, or passing from hand to hand, of money ; but it has now come to be applied to the money itself. It covers all forms of money, *e.g.*, gold, silver and copper coins, bank-notes, bills of exchange, cheques, etc. Ordinarily, however, it refers to "legal" money only and when we talk of the currency system of a country we mean its monetary system as established by law. It is only in this limited sense that the subject is discussed here.

It is not the intention of this note to enter into a minute discourse on the theory and history of money. Many valuable books are written on the subject. Our object is to briefly refer to the functions of money, the monetary system of India and whether the Indian Currency satisfies the canons of stable money.

Many attempts have been made to give a good cut-and-dried definition of money. One such definition is that "money includes those instruments of exchange which pass freely from hand to hand, without reference to the personal credit of the parties concerned." But this is not comprehensive as it omits conceptions of value and storage. Knapp deals with money "as a creature of law." Ordinary man in the street knows what money is and therefore without attempting to discuss the various definitions given in books on Economics we proceed to the functions and basis of money.

The main functions of money are—

- (i) *It is an instrument of payment or medium of exchange.*—When any one wants to buy anything he has not to pay directly in commodities, as in the old days, but in money. He parts

with money when purchasing and gets money when selling. The former barter-transaction is replaced by two operations : (a) He sells his goods and with the money that he thus gets, (b) he buys his requirements.

- (ii) *It is a standard or measure of value.*—Amount that has to be paid for any commodity is briefly called its value. The value is expressed in terms of the monetary unit. In order that the unit of money should be able to measure value it should itself possess or represent value. Further, like other units, *e.g.*, of length, heat, etc., the unit of value should be constant.
- (iii) *It is a store of value, or a medium of savings.*—In order that the exchange operations of selling and buying need not necessarily take place at the same time it is essential that money taken in exchange of goods should be capable of storage and available for use at some later date, and that its value during the period of storage should not undergo change.
- (iv) *It is an instrument of deferred payments.*—Whenever a contract is made covering a period of time, the payments relating thereto, are generally spread over ; and the medium of payment, specified in the contract, should be such that it does not change in value during the period payments are postponed.

A unit of money should perform all the above functions. Because it has value it must be represented by some commodity. The commodity should be such that its value does not undergo change in terms of other commodities, whose value it will have to measure, nor by lapse of time. Our other units, *e.g.*, of measurement, weight, etc., always remain constant and therefore our unit of money should also possess that virtue of constancy. Further, the material of money should possess features of portability, indestructibility,

homogeneity, divisibility and cognizability—ordinary books on Economics will show why these characteristics are necessary.

The monetary history of the world records various experiments that have been made in selecting commodities that would possess all the peculiarities referred to above, but unfortunately nothing has been hit upon so far which will satisfy all the conditions fully. There is no absolute measure of value as there is, for example, of length. A foot is a constant measure of length but the commodity which represents money can never be an unvarying measure of the relations existing between it and other commodities, which are always changing relatively to each other. The value of article chosen as standard of value may itself change by causes affecting it (*c.f.* how the discovery of new silver mines in the nineteenth century considerably lowered its value), and the value of other articles (which are compared to the standard), can be changed by causes affecting them and the material of money. The value of the monetary unit can remain constant in terms of all other commodities only if its material alters exactly and in a compensating direction with all other commodities. It is impossible to conceive of such a substance.

In the absence of there being any commodity which completely satisfies the tests imposed on perfect money, the problem has been to find the next best thing. From very early days gold and silver have been selected as satisfying, as approximately as possible, the requisite conditions. To facilitate the currency of money governments have taken upon themselves the task of introducing in circulation minted coins, which bear certificate upon their face about the quantity and fineness of the composing metal.

Metallic money of a country is usually of two kinds: standard and subsidiary or token. The former is used for large payments and the latter for small transactions. Limits are usually prescribed on the amounts which can be paid in token currency. The value of units of principal money, both as coin and bullion, is usually the same; in fact people can take any quantity of the metal to the mint and get it coined

on payment of a small charge. But in the case of token coins, their value as money is much more than their bullion value and for this reason their creation is the monopoly of the State.

When both gold and silver are basis of money and there are no restrictions on their coinage it will be easily seen that there will be two sets of prices, gold and silver prices of commodities, and that any change in their relative value will affect the two sets of prices. History of money shows that disturbances of this nature finally led to the adoption of the monometallic principle in currency.

If there are two countries in trade relationship they will find mutual dealings smooth and easy if the bases of their currencies are same ; otherwise variation in the relative value of their bases would affect relative prices of their commodities, *e.g.*, if the monetary system of a country (A) is based on gold and the monetary system of another country, (B) is based on silver and the value of silver in terms of gold drops, assuming other factors to remain constant, the prices ruling in (A), which are based on gold currency, will rise relatively to silver, *i.e.*, in terms of the money of (B) ; and the prices in (B) which are based on silver currency, will drop relatively to gold, *i.e.*, in terms of the money of (A). Thus people of (B) will find it more costly to import goods from (A) but the people of (A) will find it cheaper to import goods from (B). The converse would be the case if price of silver rose in terms of gold. Of course, ultimately the relative prices of the two countries would be readjusted but the immediate disturbance would be there. Frequent trade fluctuations due to varying basis of currency units ultimately resulted in the adoption of gold as the basis of currency. And to-day the yellow metal is recognised by all the civilised countries of the world as the most suitable material to serve as the basis. Any country that has its currency based on any other metal will be subjected to trade disturbances due to variations in relative prices consequent upon fluctuations in the value of its monetary unit in terms of the gold standard currencies.

In course of time there came into existence paper money. This money represents promise of the issuing authority to

deliver stated amount of metallic money on demand. It is necessary that the authority taking responsibility for the issue of paper currency should keep sufficient reserves so as to be able to meet all demand for conversion of notes into specie otherwise the notes will drop in value and the public will lose confidence in its solvency. And if the issuing authority has intentionally tampered with the reserves, it will be accused of bad faith and dishonesty to the public. If the promise to redeem is upheld, the paper money retains same value as the metallic money but when the authority fails to abide by the obligation, paper money is depreciated in terms of the metallic money, the extent of depreciation depending upon individual circumstances. The depreciation in the case of French paper money is nearly $87\frac{1}{2}$ per cent., (*e.g.*, Francs 200 = £1, against par exchange of Francs 25·2215 = £1). The depreciation in the case of German paper currency was tremendous and ultimately a billion paper marks were equivalent to a gold mark. When paper money is not redeemed in metal and if the laws of the country impose an obligation to accept both paper and metallic moneys at the same value, Gresham's Law comes into operation and good (*i.e.*, metallic) money is driven out by bad (*i.e.*, paper) money, the latter being only visible in circulation. Further, as paper money has no intrinsic value persons not under the legal power of the issuing authority cannot be compelled to accept it in payment of their dues. It is of course another thing that on account of the unimpeachable respectability of and confidence in the issuing authority, its paper currency may command acceptance in territories not under its legal or political influence, but it is not legal tender for such people. It is therefore of paramount importance that the currency authority should keep sufficient reserves against paper currency so as not to endanger its value, whether internally or externally. It is not necessary that for every unit of paper money there should be corresponding increase in the metallic reserve. Experience has demonstrated that if the metallic portion is about 40 per cent. of the notes issued, value of notes can be easily maintained. Other 60 per cent. of the reserve consists of "obligations to pay" of the Government/and or of the mercantile

community ; *i.e.*, is based on credit. If large payments are to be made to settle the balance due in respect of foreign trade, which will naturally be made in metallic money and thus affect the ratio of metallic money and metallic reserves to the total currency, the machinery of the Bank rate, as explained in the book, is put in operation which ultimately restores the equilibrium. It is a sound principle that the portion of currency against "credits" should be reduced proportionately to the depletion of specie reserves, and the corresponding credits called back, *i.e.*, there should be contraction in credit and currency. Unless there is a national calamity ordinary payments in respect of international balance of account would not be so much as to endanger the reserves ; and even if there is abnormal situation due to imports being more than exports, the raising of Bank rate, with the consequent effect on relative prices would soon rectify the situation.

Legal tender currency of a country is that portion of its currency which by law can be tendered in payment. There is also another kind of money, *viz.* cheques, bills, etc. (it would be better to call it as orders to money), which although not legal tender is accepted in settlement of dues. Acceptance of such money is of course provisional and subject to the "orders" being honoured in due course. It thus rests on credit also. In the modern economic society such "credit money" plays an important part. The basis of the whole volume of currency, both legal and non-legal tender, is of course, the same metal, *viz.*, gold. And because credit and currency are so intermingled final control over them is entrusted to a single authority, usually the bank of issue.

It is an economic law that the value of a commodity varies inversely to its supply or quantity, unless there is compensating variation in its demand. The same principle applies to money. Other factors remaining constant, value of monetary unit, in terms of commodities increases if the volume of currency decreases, demand remaining constant *i. e.* prices fall ; but if the demand also decreases proportionately, there may be no change in its value. Similarly the converse will be the

case if the volume increases. With the help of the paper portion of currency, a portion of whose reserve consists of short term commercial assets (*see Chapter on Central Bank*), which should rise and fall according as there is increase or decrease in the commercial activity, the ultimate volume can be regulated so as always to correspond to the intensity of demand for money and thus the value of monetary unit can be kept steady. Individual values of commodities may undergo changes but in that case the changes will not be attributable to the change in the value of money but to circumstances affecting the commodities themselves.

If the currency of a country has no stable value in terms of gold it is evident that people will begin to accumulate their savings in gold or gold coins ; or keep their savings in other countries where currency and gold are interchangeable at fixed ratio. Of course for their business purposes people will keep as much money as they need in circulation, but their all reserves and surpluses will consist of stable values. Such circumstances do not conduce to the increase in the bank deposits of the country. When the German currency was depreciating the Germans tried to convert their money in sterling and dollars and kept their accounts with the English and American banks. The stability of value of currency in relation to gold is thus of great importance for the increase in bank deposits and bank accounts.

Having briefly discussed the theory of money our next task is to describe the Indian Currency system. Before 1893 India had silver currency—rupees and notes. People had great liking for gold but never was any serious attempt made to introduce gold currency. All transactions were in terms of silver rupees. Minting of silver was open to the public. The bullion and face-value of the rupee was the same.

On the adoption of gold standard by important countries of the world, value of silver depreciated considerably which greatly disturbed exchange value of rupee in terms of the gold standard currencies. And as India had trade relationship with those countries and its financial connection with England was more or less intimate, the fluctuations in exchange led to disturbances in India's foreign trade and foreign finances.

To avoid such embarrassing fluctuations Herschell Committee was appointed in 1893 to consider the question of the rupee. It recommended closing of mints to free coinage of silver. Henceforward the Government only was to coin silver rupees and to control the volume of silver rupees and notes in circulation. Value of rupee appreciated and it was worth more than its bullion contents. By 1898 the exchange touched 1s. 4d. Rupee no longer represented merely value of certain quantity of silver (one tola or 180 grains, $\frac{1}{12}$ th fine) ; but it had assumed a distinct value of its own and was equivalent to 7.53344 grains of gold. Although the Government of India did not undertake any obligation to give gold against rupees, yet it accepted the converse arrangement of giving Rs. 15 for every sovereign.

The position was again examined in 1898 by the Fowler Committee. It recommended : (i) Indian mints should continue closed to the free coinage of silver but the coinage of gold should be open to the public ; (ii) Sovereigns should be made legal tender and current coin ; (iii) Rs. 15 should be equal to a sovereign ; (iv) Profits on the coinage of silver should be taken to a special reserve. Thus the Committee definitely recommended establishment of gold standard and introduction of gold currency in circulation. The recommendations were accepted both by the Secretary of State and the Government of India. However, in course of time proposal to introduce gold into circulation did not materialise and "the currency system developed on lines different from those foreseen in 1898. Apart from small change, the internal currency consisted almost entirely of tokens, one printed on silver, the rupee, and the other on paper, the currency note." The value of tokens was artificially maintained at 1s. 4d. gold (gold and sterling were equivalent in those days), and the following devices helped to keep up the value :

- (i) The Government was bound to give Rs. 15 for every sovereign. Whenever there was need for more currency people could import sovereigns and get them exchanged in rupees.
- (ii) The Secretary of State sold bills on India, without limit of amount, at the rate of one rupee for

1s. $4\frac{1}{8}d.$ Foreigners who wanted to remit rupees to India used to buy such bills on tendering equivalent sterling. Of course, whenever there was not much demand for rupees the rate was lowered and in practice no such bills were sold at a rate lower than 1s. $3\frac{3}{8}\frac{1}{2}d.$

(iii) Whenever due to adverse balance of trade India was required to export money and because rupee could be only accepted at its bullion value by the outside world, which was less than its face-value, the Government of India sold drafts on the Secretary of State at a rate slightly less than 1s. $3\frac{3}{8}\frac{1}{2}d.$ There was no obligation on the part of the government to do so though in practice they tried to have recourse to this whenever gold value of rupee tended to be divorced from it.

Obligation (i) was of course recognised by law, and obligation (ii) was a necessary corollary to (i). Obligation (iii) was not imposed by law though observed in practice.

Whenever there was demand for silver rupees the government would import silver, turn it into rupee coins and the profit from coinage was kept in a reserve known as the Gold Standard Reserve. If notes were needed, the currency reserve was strengthened to that extent. The location of these reserves was not fixed at any one place. The reserves could be kept at any place in India and/or England. And it was this facility of unfixed location which enabled operations of the nature (ii) and (iii) referred to in the last paragraph. Whenever there was demand for rupee currency and the Secretary of State sold bills on India, all that was to be done was to create or manufacture, so to say, currency notes in India, with which to honour the bills, strengthening the currency reserve by the addition of the proceeds of the bills. Such addition was of course made in the portion of reserve located in England. Similarly when the Government of India sold drafts on London, the payment in London was made from the reserves located there, the equivalent amount of notes, received as price for the sale of drafts, being can-

celled in India. If at any time the amount in the currency reserve in England did not happen to be sufficient to honour the drawings of the Government of India, sufficient amount was transferred to it from the Gold Standard Reserve held in England, the corresponding adjustment in the reserves being made in India.

We have said the rupee was for practical purposes equivalent to 1s. 4d. gold. The question may be asked why the government charged 1s. 4 $\frac{1}{8}$ d. when selling rupee transfers and gave only 1s. 3 $\frac{7}{8}$ d. when selling sterling drafts. The variation of $\frac{1}{8}$ from the par represents the cost of transmission which people would incur if they actually transferred gold sovereigns or gold bullion. The upper and lower limits on the sterling or gold value of the rupee are known as gold points. Ordinarily the value of rupee fluctuated between these two points the actual rate depending upon the actual trade position of India with the outside world. When the rate tended towards the upper limit it meant that India was creditor country and money must come in; but when the rate approached the lower limit it signified that India was debtor in the international market and money must go out.

The currency system working on the above principles is said to be based on the Gold Exchange Standard.

The maintenance of the value of rupee within the limits given above depended on two factors: (i) Value of silver contained in the rupee should not be worth more than its value as coin, *i.e.*, not more than 1s. 4d. gold. When silver became dearer than this the Gresham's Law would come in operation and silver rupees would disappear or be sold as bullion; (ii) Demand for export of money from India should not be more than the amount of currency and gold standard reserves in England; or if the reserves were less than the demand, the government should be able to raise enough foreign loans to meet such demand. If neither of these were possible the government's drawings on England could not be met and the value of rupee would naturally depreciate.

The currency system of India was one sided: although the government gave Rs. 15 for every sovereign it did not undertake any obligation to give sovereigns for rupees. And though in practice it did try to do so still the defective law was there—the law which could defraud holders of Indian Currency by refusing to give them the same amount of gold which had been taken from them when issuing rupees.

The problem of Indian Currency was referred to the Chamberlin Commission in 1913 to inquire among other things whether the then existing practice in currency was conducive to the interests of India. The Commission recommended that the Gold Exchange Standard had worked satisfactorily, that the Gold Standard based on gold circulation was neither required nor necessary, that the government should continue to aim at giving the people the form of currency which they demanded, whether rupees, notes or gold, and that thorough and adequate reserves of gold and sterling should be maintained to support the exchange value of rupee. Owing to the outbreak of the War no action was taken on the Commission's report.

“The War of 1914-18 put the currency system of India to a severe test. The price of silver rose to unprecedented heights and the material of the silver token became worth more than its face-value. The government found it difficult to continue their obligation of issuing rupees at the long-established rate. There was great demand for Indian exports, and there were exceptional disbursements to be made on behalf of the British Government. Internal Currency had to be in some way provided, and it could no longer be provided in the old forms. Confronted with these difficulties, the authorities allowed the rupee, so long anchored at 1s. 4d., to break loose from its moorings and follow the course of silver prices. The rate of exchange accordingly rose rapidly until it reached 2s. 4d. (sterling) in December, 1919.” *

The Babington Smith Committee was appointed in May, 1919, when the rate was 1s. 8d., to examine again the question of Indian Currency. The Committee recommended

* Currency Commission's Report, 1926.

that the value of rupee should be fixed at 2s. gold, and to keep up the value, the Government of India should be free to sell transfers on London at that rate. The government accepted the recommendations and sovereign was made equivalent to Rs. 10, *i.e.*, rupee became equal to 11·30016 grains of fine gold.

At this time, February, 1920, large demand arose for transfers on London and the government in terms of the recommendations of the Babington Smith Committee sold transfers on London at the new exchange rate. And because the gold value of sterling was widely fluctuating, the rupee sterling exchange followed the same, which thus varied from 2s. 3 $\frac{2}{3}$ $\frac{1}{2}$ d. to 2s. 10 $\frac{2}{3}$ $\frac{1}{2}$ d. The attempt to maintain rupee at 2s. gold failed whereupon in June, 1920, steps were taken to keep it at 2s. sterling. The latter attempt also failed and was abandoned on the 28th September, 1920. These attempts, of course, involved the country in great losses. Reserves which had been built at 1s. 4d. were squandered at over 2s., *i.e.*, the amount of sterling which had been originally received for two rupees was roughly handed back in exchange of only one rupee. The exchange continued to fall heavily and in early part of 1921 it was quoted at 1s. 3d. sterling or 1s. gold. By January, 1923, the tide of exchange turned upwards and it recovered to 1s. 4d. sterling. The upward tendency continued till in October, 1924, the rate was 1s. 6d. sterling or 1s. 4d. gold. The government freely purchased sterling at this rate and the upward movement was arrested. Sterling regained its parity with gold in the middle of 1925 which improved the value of rupee to 1s. 6d. gold, at which level it remains to-day.

We may mention here that a portion of Indian public opinion was vehemently opposed to the government's exchange policy during the period of the War and afterwards. As soon as price of silver began to rise so as to appreciate rupee more than its face-value, some of the Indian economists suggested that fineness of silver in the rupee should be reduced. There was no objection to it because the rupee was only a token coin. It had been always regarded as representing a certain quantity of gold and not as a piece of silver of

certain weight and fineness. The Indian member on the Babington Smith Committee, Sir D. Dalal, strongly advocated this course. He was of opinion that the rise in the price of silver was only temporary and would not be permanently maintained; and further, that appreciating rupee to such an extent would upset financial arrangements and might ultimately lead to great monetary disturbances, owing to the inability of the government to keep up the ratio. Subsequent events have proved that his diagnosis was correct.

The wide range of value to which the rupee has been subjected is given in the exchange chart. To what uncertainties have its holders been subjected! Evidently the Indian Currency has not conformed to one of the most important canons of stability, in terms of gold—the international basis of money; nor does the law impose definite obligation upon the currency authority to give a definite amount of gold in exchange for the rupee. And unless these conditions are provided for our money will always remain unstable in terms of the currencies of the civilised world and our foreign obligations, foreign financial relations and foreign trade will be liable to frequent fluctuations which would react upon home economics as well. Such unstable currency discourages import of foreign capital; it discourages banking habits and gives impetus to hoarding and fondness for gold.

To revert to the question of the Indian Currency history, the subject was again referred to the Hilton Young Commission whose report was published last August. The Commission has made three main recommendations—

- (i) That there should be gold bullion standard in India. The peculiarities of this standard are—
 - (a) Basis of currency will be gold, the rupee being equivalent to a certain fixed quantity of gold;
 - (b) The currency authority will be under legal obligation to give rupees against gold at a fixed ratio;
 - (c) The currency authority will be bound by law to give in exchange for rupees at a fixed

- ratio, gold or its equivalent in currencies of other countries, which are based on gold and which do not prohibit its export ;
- (d) The rupee will be a token coin and may be printed on silver or paper, its intrinsic value being less than its monetary value ;
- (e) Gold currency will not be in circulation nor legalised ;
- (f) Value of the rupee in terms of gold will vary between the gold points ;
- (g) Minimum limits on the quantity of gold, against which rupees are required or which is required against rupees, are prescribed.
- (ii) The value of rupee should be 1s. 6d. gold, *i.e.*, it should be equivalent to 8.47512 grains of gold.
- (iii) The control of credit and currency should be vested in one institution, the Reserve Bank of India.

The gold bullion standard appears to be sound in principle and can be upheld on many grounds. Gold as cover for currency should be centralised and not used in a manner which would make it scarce at the very time when its conservation is most needed. Actual circulation is not necessary for maintaining the gold value of money provided obligations to give rupees for gold and gold for rupees are irrevocably recognised. Moreover, if every country of the world were to insist on actual gold circulation there would not be enough gold available to satisfy the total demand. All the important countries of the world should so organise their currencies that the utmost economy in the use of gold is possible, consistent of course, with stability, and a situation where gold becomes scarce by hoarding, etc., is not normally possible.

The question of ratio is important but the expert opinion is divided. Some say that complete adjustment in prices, wages, etc., has not taken place, that the present ratio of 1s. 6d. is only a temporary phase and that it is maintained by artificial and objectionable means. Others are of opinion

that the ratio has come to exist and it should be stabilised at this figure, otherwise great disturbances would be caused. It is difficult to say whether adjustment of every possible kind, to the higher ratio has actually taken place. There is no doubt that the 18*d.* ratio will give a set back to Indian exports and manufactures and give an impetus to imports and use of foreign articles. Even England experienced the same depression in 1925 when due to the restoration of the gold standard there was sudden appreciation in the value of pound sterling. Also adjustment in wages, specially of government officers, taxes, revenues, etc., is not possible for a long time. All contractual obligations will be affected by the higher ratio—creditors being benefited to the disadvantage of the debtors. It would have been a thousand times better if the government had tried to stabilise exchange at 1*s.* 4*d.* in 1924 when Sir Purshotamdas Thakurdas appealed to the legislature and the executive government to do so. The ratio 1/4 existed more or less without a break from 1898 to 1916 and all persons interested in the rupee had assumed it as equal to $\frac{1}{15}$ of a sovereign. In fairness to all it would be better to restore it to the same value. The argument that 18*d.* rupee would reduce sterling expenses of India and ease the budget, no doubt true, should not be allowed to influence the economic consideration of the question. Further, the saving thus made by the government is a form of indirect taxation on the people, who get less for their products, because when rupee appreciates in value, prices must fall. Many are of opinion that it would be impossible to keep up the rupee at 18*d.* One or two bad monsoons would turn scales against India in the international balance of trade, which would necessitate great demands for gold and that might severely strain the currency reserves. Trade currents this year show how exports are suffering. Bombay mills are finding it cheaper to import foreign cotton which can be only accounted for by the higher ratio.*

* Since writing the above the Legislature has passed the Government's Bill fixing the rupee's value at 18*d.* gold. The Bill was based on the commission's recommendations. The new Currency Act is known as No. 4 of 1927 and came into force on 1st April 1927.

The Currency Commission have also recommended that gold savings certificates should be introduced. This will be a move in the right direction. People can deposit rupees or gold at interest with the option of getting the amount at maturity in gold. The present uneconomic habit of hoarding, which does not increase the quantity of gold during the period it is stored, will be replaced by economic savings where increased quantity would be returned at maturity.

To complete the account of Indian Currency a few words remain to be said about the total amount of money in circulation and the nature and proportion of the reserves. The total amount of silver rupees in circulation is about Rs. 350 crores, against which there is £40 million in the Gold Standard Reserve. The composition of the reserve on the 30th June 1926, was made up as (i) Cash at short notice, £3,706 ; (ii) British Treasury Bills, £4,896,761 ; and (iii) Other British and Dominion Government Securities £35,099,533. The amount of currency notes outstanding is about Rs. 186 crores, and the reserve against it consists of : (i) Silver coins, 77 crores ; (ii) Silver bullion, 7·7 crores ; (iii) Gold coin and gold bullion, 23·3 crores ; (iv) Rupee securities, 57 crores ; and (v) Sterling securities, 21 crores. The Indian Currency Act provides that the gold and silver metallic reserve should not be less than 50 per cent. of the total note circulation with the proviso that the amount of the fiduciary portion should not be more than Rs. 100 crores. Trade bills endorsed by the Imperial Bank of India can be accepted as a part of the fiduciary reserve to the maximum extent of Rs. 12 crores. Limitations are also prescribed on the maturity of securities and the amount of Indian securities that could be held in the reserves. Interest realised on the investment portion of the reserves was originally taken to the strengthening of the reserves but during the last three years it has been taken to revenue by sanction of the Legislature.

APPENDIX C

CHARTER OF NETHERLANDS BANK

[BANK OF ISSUE OF HOLLAND]

Regulations according to which De Nederlandsche Bank by virtue of the acts of December 22, 1863, (Staatsblad No. 148)*, August 7, 1888, (Staatsblad No. 122), December 31, 1903, (Staatsblad No. 335), August 3, 1914, (Staatsblad No. 345), and of July 25, 1918, (Staatsblad No. 475), is entitled to act as a Bank of Issue. †

ARTICLE 1.

(1) No Bank of Issue may be established, and no foreign Bank of Issue may have its bank-notes brought into circulation in this country, otherwise than by virtue of a special Act and on the basis and terms laid down in such Act.

(2) By the term Bank of Issue is to be understood every institution established for the purpose of issuing or bringing bank-notes into circulation.

ARTICLE 2.

(1) The period for which De Nederlandsche Bank is authorised to act as Bank of Issue by virtue of Article 2 of the Act of December 22, 1863, (Staatsblad No. 148), and Article 1 of the Act of August 7, 1888, (Staatsblad No. 122), and Article 1 of the Act of December 31, 1903, (Staatsblad No. 335), in connection with Our Decree of February 14, 1917, (Staatsblad No. 216), is to be extended for fifteen years dating from the 31st of March 1919, therefore to the 31st of March 1934 inclusive, subject to the stipulations laid down

* "Staatsblad" is the name of the official gazette in which all Acts are published.

† Royal Decree of September 28, 1918, (Staatsblad No. 553.)

in those Acts and in the Act of August 3, 1914 (Staatsblad No. 345) in as much as they are not amended by this present Act.

(2) The said period shall be considered to have been extended for the space of one year after the expiration of this and every other period for which it is extended unless we or the Bank, by giving notice, indicate reluctance to have the period extended. This notice may not, however, terminate the right to act as a Bank of Issue before the expiration of five years, dating from the first day of April after the notice has been given.

ARTICLE 3.

De Nederlandsche Bank is a Naamlooze Vennootschap (Limited Company).

ARTICLE 4.

The Deed of Incorporation of De Nederlandsche Bank as a Limited Company shall be based on the stipulations of this Act.

ARTICLE 5.

(1) The seat of De Nederlandsche Bank shall remain established at Amsterdam.

(2) On or before the 1st of January 1865 the Bank shall establish a Branch Office at Rotterdam and Agencies and Correspondentships at other places.

(3) Not less than one Agency shall be established in each province.

(4) The number of Correspondentships shall be determined according to requirements.

(5) The organisation and the scope of the Branch Office and of the Agencies shall be submitted to Our sanction.

ARTICLE 6.

(1) The authorised capital of De Nederlandsche Bank shall be Twenty Million Guilders, fully paid-up.

(2) The amount of the capital may be increased by law with the approval of the Bank.

ARTICLE 7.

Only Netherlanders may be voting shareholders.

ARTICLE 8.

(1) The Bank shall form a Reserve Fund to the sum of one quarter of its authorised capital.

(2) The Reserve Fund is intended, subject to the provisions of Clause 2 of Article 31, to make good any losses which may be incurred on the capital.

ARTICLE 9.

(1) With the approval of Our Minister of Finance, the Bank is authorised to form special Reserves.

(2) Every year, when fixing the Balance-Sheet, it will be determined, with the approval of Our Minister of Finance, whether the reserves referred to in the preceding clause shall be maintained, or partially or entirely added to the profits of the year covered by the Balance-Sheet.

ARTICLE 10.

The Bank is authorised to form a Pension Fund for its staff. The means of forming this fund, the payments into the fund and further rules relating to such fund shall be laid down by instructions which are to be submitted to Our approval.

ARTICLE 11.

(1) The scope of the Bank includes :

1°. The issue of bank-notes and the sale of assignments on its offices and of assignments and cheques on its correspondents ;

2°. discounting (a) bills of exchange, assignments and promissory notes bearing the signatures of two or more persons or firms who are severally liable for the whole amount, with a currency which is not longer than is required by the customs of trade ; (b) debenture bonds redeemable within

six months, accompanied by the full guarantee of the discounter for the whole amount ;

3°. the purchase and sale of telegraphic payments, cheques, bills of exchange and other commercial paper payable abroad ;

4°. advancing loans on securities, goods, warrants, coin and bullion and paper of value referred to sub 2° and 3° ; advancing loans also includes the advancing in account current against surety of securities which may be accepted against loans ;

5°. trading in precious metals, causing same to be coined, and the assaying and refining of ores and metals ;

6°. the keeping of accounts current for its clients, including the effecting of orders to transfer (giro), effecting clearances with or between other parties and the collection of moneys on behalf of its clients ;

7°. the taking into custody of securities, goods, warrants, deeds, valuables and other objects of value upon terms to be published by the Bank.

(2) The Bank may, with Our approval and after the Raad van State (Council of State) has been heard, perform in the public interest other transactions than those mentioned above sub 1°. to 7°. inclusive. Our Decrees containing the approval above described shall be published in the Staatsblad and the Staatscourant.

ARTICLE 12.

(1) The Bank shall not grant to any person whomsoever any credit or advance without security ; the terms credit or advance without security do not include moneys or goods entrusted by the Bank in its own interest to mandatories who are not in its regular service, or to the Postal Cheque and Transfer Service.

(2) At a sale under an execution of goods, securities or other pledges placed in the hands of the Bank by way of guarantee for obligations towards it, the Bank is authorised to purchase such goods, securities or such other pledges, either partly or entirely, for subsequent realisation.

ARTICLE 13.

(1) The Bank is authorised to invest the Reserve Fund and one-fifth part of its share capital.

(2) These investments shall be effected according to rules laid down by the combined meeting of the Management and Commissaries of the Bank.

ARTICLE 14.

(1) De Nederlandsche Bank shall continue to be entrusted with the custody, without charge, of the Treasury Funds at Amsterdam.

(2) The Bank shall also undertake free of charge the duties and functions of Government Cashier and Paymaster at Amsterdam, also at Rotterdam and at all places where the Bank possesses or will eventually establish Agencies.

(3) For these services the Bank is responsible to the Minister of Finance and accountable to the Algemeene Rekenkamer (Accountant-General).

(4) Should the Minister of Finance consider this necessary, the Bank shall moreover undertake free of charge the duties of cashier and paymaster to the Post Office Savings Bank or to any other institutions founded by law or by Us, and also the custody of all securities belonging to the Government and those institutions and of securities taken in pledge by them.

ARTICLE 15.

(1) De Nederlandsche Bank shall without charge afford its assistance and co-operation for the withdrawal of the Government Notes.

(2) The manner in which the Bank shall execute the duties imposed upon it by this and by the preceding article will be determined by Us after obtaining the advice of the Management of the Bank.

ARTICLE 16.

(1) As an exception to the stipulations of Clause 1 of Article 12 the Bank is bound, whenever the Minister of

Finance shall deem it necessary to replenish temporarily the State Treasury, to advance moneys to the State in account current, against sufficient security of Treasury Notes, the issue or pledging of which is permitted by law.

(2) These advances shall be given without interest by the Bank but they may not at any time exceed a total of fifteen million guilders.

(3) The obligation to make such advances shall cease :

1°. if the State should, after the October 1st, 1904, resolve to issue Government Notes ;

2°. as soon and as long as the metallic surplus of the Bank has dropped below ten million guilders. The said obligation shall cease whenever the metallic surplus, by reason of such advances, falls below the abovementioned amount.

ARTICLE 17.

(1) The shape and size of the bank-notes to be issued shall be announced to the public by the management of the Bank.

(2) The Bank shall not issue bank-notes for a smaller amount than f 10--(ten guilders).

ARTICLE 18.

(1) The notes of the Bank are payable on demand at the Head Office, the Branch Office and at the Agencies, excepting on the days mentioned in Article 154 of the Commercial Code.

(2) The payment at the Agencies may, however, be postponed until specie could have been received from the Head Office.

(3) The notes of the Bank are free of stamp duty.

ARTICLE 19.

(1) In case of war or danger of war the obligation of De Nederlandsche Bank to pay its notes may, by Order in Council, be suspended.

(2) An Order in Council as referred to in the first clause of this Article shall fix the period of such suspension. This period may be extended by Us as frequently as this may, in Our opinion, be necessary.

(3) The Order in Council referred to in the first clause of this Article will be withdrawn as soon as, in Our opinion, the war or danger of war, by reason of which it was proclaimed, has ceased.

ARTICLE 20.

In deviation from the stipulations of Article 3 of the Act of April 26, 1852 (Staatsblad No. 92) amended by the Act of June 23, 1893 (Staatsblad No. 111) the proclamation of an Order in Council as referred to in the first clause of Article 19 shall be considered to be known throughout the whole Kingdom immediately after such proclamation has been simultaneously inserted in the Staatscourant (State Gazette) and Staatsblad.

ARTICLE 21.

(1) The holder of a bank-note is exclusively authorised to claim from the Bank the payment of the sum of money stated upon it.

(2) No compensation need be given by the Bank on account of the loss or destruction of bank-notes.

(3) On suspicion of fraud, or at the request in writing of parties concerned, the Bank is at liberty to exact a receipt against payment of, and the signing of the bank-notes by the person presenting them for payment.

(4) The stipulations of Article 227—229 of the Commercial Code are not applicable to bank-notes.

ARTICLE 22.

(1) The Management of the Bank may, after having obtained Our permission to do so, call up holders of notes issued by it to present them for payment.

(2) We shall, when granting such permission, fix the period during which such presentation must be done.

(3) The notice to do so will be inserted at least once in the Netherlands Staatscourant (State Gazette).

(4) On expiration of the period referred to in Clause 2 of this Article, the notes mentioned in the notice will be exclusively paid by the Head Office of the Bank after examination has shown that the application for payment must be complied with.

(5) Ten years after the expiration of the period already referred to, the amount of the notes called up but which have not been presented for payment shall be added to the profit of the current year. Any notes presented for payment subsequently shall, after examination as mentioned in the preceding clause, be paid and debited to the Profit and Loss Account.

(6) Should the Bank, before the expiration of the period of ten years referred to in the preceding clause, have lost the right to act as a bank of issue, the amount referred to in the preceding clause shall be divided between the Bank and the State in the same proportion as would have been done if such amount had been added to the profit of the last financial year for which the Bank was authorised to act as a bank of issue. Any notes presented for payment after such division shall, after examination as mentioned in Clause 4, be paid by the State.

(7) After the expiry of thirty years after the termination of the period mentioned in the second clause of this Article, the right to demand payment of the notes called up will lapse.

ARTICLE 23.

The proportion of the total amount of bank-notes, bank-assignments and balances of accounts current which must be covered by coin or bullion shall be laid down in a Royal Decree to be passed at the recommendation of the Management of the Bank. This Decree will be published in the Staatsblad and, if necessary, will be changed from time to time.

ARTICLE 24.

(1) The Management of the Bank shall consist of a President, a Secretary, and not less than two Directors.

(2) The number of Directors will be fixed by the combined meeting of the Management and Commissaries.

ARTICLE 25.

(1) The President and the Secretary shall be appointed by Us, for a term of seven years at each appointment. In a combined meeting of the Management and of the Commissaries a nomination list containing two names for each appointment shall be prepared and submitted to Us for such consideration as may seem desirable to Us.

(2) The Directors shall be appointed by the voting shareholders for a term of five years at each appointment, from a nomination list of three persons prepared by the Management and the Commissaries in a combined meeting.

(3) All the members of the Management are eligible for immediate re-election on their resignation.

(4) At the proposal of a combined meeting of the Management and Commissaries both the President and the Secretary may be suspended or dismissed from their office by Us. If suspension is proposed, a proposal will at the same time be made with regard to the temporary filling of the vacancy.

(5) Upon a similar proposal the other members of the Management may also be dismissed by the voting shareholders.

ARTICLE 26.

The combined meeting of the Management and the Commissaries may appoint Deputy Directors for such term and under such regulations and conditions as may be laid down by the meeting at their appointment.

ARTICLE 27.

(1) Side by side with the Management there will be an Advisory Committee consisting of five persons.

(2) The voting shareholders shall elect the members of this committee from a nomination of two persons for each vacancy. The Board of Commissaries shall prepare this nomination. The members of the Committee shall each sit in this committee for five years in succession. After this period they are not eligible for immediate re-election.

(3) The members of this committee shall, for the first time, sit for a period of one, two, three, four and five years respectively. They are not eligible for immediate re-election. The year in which these members are to resign in order of rotation shall be determined by drawing lots.

(4) On a vacancy occurring in the interval, the Board of Commissaries shall temporarily appoint a new member to fill the vacancy. The member thus appointed shall sit until the next ordinary general meeting of shareholders, who may confirm the appointment or not.

(5) On a vacancy occurring in the interval the newly appointed member shall, as regards his term of office, take the place of the member in whose stead he has been appointed.

(6) The members of the Committee may also be members of the Board of Commissaries.

(7) The Committee shall meet with the Management at fixed periods and shall be consulted by the Management concerning important matters, all of which shall be done according to instructions laid down by the combined meeting of the Management and the Commissaries. These instructions shall be submitted to Our approval.

(8) Should the Management differ in opinion from the Committee concerning the important matters referred to in the preceding clause, they shall immediately communicate such difference to the Board of Commissaries.

ARTICLE 28.

There shall be not less than fifteen Commissaries. They shall be elected by the voting shareholders.

ARTICLE 29.

(1) Supervision of the transactions of the Bank on behalf of the Government will be exercised by a Royal Commissioner to be appointed and dismissed by Us.

(2) The Royal Commissioner shall have the right to attend all meetings of Shareholders and of Commissaries and to return an advisory vote at such meetings.

(3) The Management of the Bank is bound to furnish the Royal Commissioner at his request with all the information he may deem necessary to the proper exercise of his supervision.

(4) Any further instructions for the Royal Commissioner shall be laid down by Us by decree.

(5) His remuneration shall be paid by the State.

ARTICLE 30.

The Management of De Nederlandsche Bank shall publish once a week, by insertion in the Netherlands Staatscourant (State Gazette) a concise bank return in a form to be sanctioned by Us.

ARTICLE 31.

(1) The profits of the Bank shall be exclusively to its benefit to the amount of three and a half per cent. of its authorised capital.

(2) Should in any year the profits be less than three and a half per cent. of the said capital, the deficit shall be furnished from the Reserve Fund, provided that this fund does not fall below fifteen per cent. of the authorised capital.

(3) Should the profits exceed $3\frac{1}{2}$ cent. of the authorised capital, ten per cent. of the surplus will first be laid aside to the Reserve Fund until it has reached the amount stipulated in Article 8. Three per cent. of the remainder shall be paid as bonus to the Management, Advisory Committee, and Commissaries. If the Management consists of more than four members, the payment just referred to will be $3\frac{1}{2}$ per cent. of the remainder. Of what then

remains the Bank will receive one-fourth and the State three-fourths until the profit share of the Bank, besides the prescribed addition to the Reserve Fund, and the bonuses paid, amounts to seven per cent. of the authorised capital. Of the profit then remaining the Bank shall receive one-eighth and the State seven-eighths.

(4) As basis for the distribution of the profits will be taken the annual Balance-Sheet of the Bank as determined by its Commissaries, if it is in accordance with the stipulations of the law and with those of the Statutes of the Bank.

(5) Differences of opinion as to whether the Balance-Sheet is in accordance with those stipulations shall be finally determined by three arbitrators. One of these arbitrators shall be elected by the Minister of Finance, one by the Management of the Bank, and the third is to be appointed by the Tribunal at Amsterdam. No shareholder of the Bank may be elected or appointed to such function.

(6) The share of the State in the profits of the Bank will cease to be paid if :

1°. any other body besides De Nederlandsche Bank should be permitted to issue bank-notes and bring them into circulation ;

2°. the State should resolve to issue Government Notes after the 1st of October 1904.

ARTICLE 32.

The interest on the investments mentioned in Article 13 shall be included in the profits of the Bank. Any rise or fall in the value of the possessions obtained by that investment shall be credited or charged to the Reserve Fund.

Regulations relating to the period of transition.

ARTICLE 33.

If, at the expiration of the term for which Article 2 of this Act entitles De Nederlandsche Bank to act as a Bank of Issue, the obligatory Reserve Fund should prove to be more

than it was on the 31st of March 1889 as shown by the Balance-Sheet for the financial year 1888-89, and this term should not be extended, one-half of such excess shall revert to the State and the other half shall be for the Bank.

ARTICLE 34.

(1) If, at the expiration of the term referred to in the preceding article the right to act as a bank of issue is not further granted to the Bank, the real property and office furniture of the Bank will be valued. This valuation shall be performed by three experts, one of whom is to be appointed by Our Minister of Finance, one by the Management of the Bank, and one by the Tribunal at Amsterdam.

(2) A balance to the good or a deficit, resulting from the valuation described in the preceding clause, as compared with the balance value, will be credited or charged to the profit and loss account of the last financial year during which the Bank may act as a bank of issue.

Concluding Regulations.

ARTICLE 35.

The Statutes of De Nederlandsche Bank shall, subject to Our approval, be amended to conform with the stipulations of this Act.

ARTICLE 36.

The whole, of the foregoing regulations may be referred to as the "Bank Act 1919," mentioning the year and number of the Staatsblad in which Our Decree was published.

ARTICLE 37.

This Act shall come into force on the 1st of April 1919.

Belongs to the Royal Decree of September 28, 1918, (Staatsblad No. 553).

Known to me,
The Minister of Finance
DE VRIES.

APPENDIX D

CHARTER OF REICHSBANK

[BANK OF ISSUE OF GERMANY]

[NOTE BY THE AUTHOR.—The law which governed the Reichsbank before 1924 was much different from the present act. Formerly Capital of the bank could be only owned by the Germans who further had the full control over its affairs. To understand the question why foreign control has been imposed or tolerated it would be necessary to study terms of the peace—the Treaty of Versailles, the political and financial handicaps which it involved, the debacle in German Currency, etc. The new act is based on the Dawes scheme, recommended by a committee of experts, under the chairmanship of Charles G. Dawes, appointed by the Reparation Commission. The study of the law will, however, show that in spite of such great domination of foreign influence over the German finances, it leaves great scope for the national control over the credit and currency policy of the country.]

BANK LAW.

The Reichstag has adopted the following law, which, with the assent of the Reichsrat, is hereby promulgated.

The following provisions shall henceforth apply to the legal condition of the Reichsbank which was incorporated by the Bank Law of 14th March 1875.

I.—Privilege of the Reichsbank as to Note Issue.

§ 1

The Reichsbank is a Bank independent of the control of the Reich Government and having the character of a corporate body whose task it is to regulate the circulation of money in the whole area of the Reich, to facilitate the clearance of payments and to provide for the utilisation of avoidable capital.

The seat of the Reichsbank is at Berlin. It is entitled to maintain everywhere within the area of the Reich Branch Establishments (Reichsbank Head Establishments, Reichsbank Establishments and Reichsbank Supplemental Establishments). The Managing Board of the Reichsbank (Reichs-

bankdirektorium) has to determine these matters as well as the organisation of the Branch Establishments.

§ 2

The Reichsbank has for a period of fifty years the exclusive right to issue bank-notes in Germany.

The existing rights as to the issue of bank-notes of the "Bayerische Notenbank," the "Württembergische Notenbank," the "Sächsische Bank" and the "Badische Bank" remain unaffected. The maximum amount, up to which the private Note Banks are authorised to issue bank-notes, may not in the aggregate exceed the amount of 194 million Reichsmarks.

The limit up to which any individual Private Note Bank may issue bank-notes shall be determined by a special law which shall also regulate the legal position of these banks in other respects.

The "Rentenbank" may not increase the (aggregate) amount of the "Rentenbank Certificates" issued by it.

The right of the "Gold Discount Bank" to issue notes is rescinded. The notes in circulation on the coming into force of this Law have to be called in and withdrawn. The Managing Board of the "Gold Discount Bank" shall frame the detailed rules relating to this matter.

§ 3

The bank-notes shall be expressed in Reichsmarks. Bank-notes for amounts of less than ten Reichsmarks may only be issued with the assent of the Reich Government for the purpose of satisfying a transitory trade requirement.

The bank-notes of the Reichsbank are, in addition to the Reich gold coins, the only legal tender for an unlimited amount in Germany.

The Reichsbank is bound to call in the whole of its notes hitherto in circulation and to exchange them against Reichsmark notes. A billion marks of the late issue shall be replaced by one Reichsmark. The notes which have been called in shall be destroyed. The detailed provisions as to the calling-in, and as to the periods for the delivery and cancellation of the old notes, shall be fixed by the Managing Board of the Reichsbank.

§ 4

Foreign bank-notes or other non-interest bearing certificates of indebtedness issued to bearer by foreign corporate bodies, partnerships or private individuals may not be used for payment within the area of the Reich, if they are worded as payable in Reich currency either exclusively or concurrently with other determinations of value.

II.— Capital of the Reichsbank.

§ 5

The Reichsbank has the right to increase its foundation capital to 400 million Reichsmarks. The Managing Board of the Reichsbank has to take the measures required for the increase of capital and more particularly to determine the amount of the foundation capital within the said limit, provided always the foundation capital so to be determined shall not be less than 300 million Reichsmarks.

The payments of the new shares, not being shares to be given in exchange for the existing shares of the Reichsbank or for the shares of the "Gold Discount Bank," shall be made exclusively in gold or foreign bills at their current gold values.

New share certificates shall be issued for the whole of the foundation capital. The owners of the old share certificates shall, in exchange, for the same, receive new share certificates in the proportion to be fixed by the Managing Board of the Reichsbank, but so that the maximum aggregate nominal amount to be attributed to the old shares shall in no case exceed one hundred million marks nominal value.

Each Reichsbank share certificate is of the nominal value of 100 Reichsmarks. The certificates are issued in the shareholders' names.

The particulars as to the form of the share certificates shall be determined by the "Satzung."

The shareholders are not personally responsible for the liabilities of the Reichsbank.

III.—Organisation of the Reichsbank.

A.—ADMINISTRATION.

§ 6

The Bank shall be administered by the Managing Board of the Reichsbank (Reichsbankdirektorium) which consists of a President as Chairman and the required number of members. In particular the Managing Board shall direct the policy of the Bank, as to currency, the discounting of bills and the granting of credits.

The President and the members must be German nationals.

The resolutions of the Managing Board shall be passed by simple majority; in the case of an equality of votes the President shall have the casting vote.

The President shall be elected by the General Board. Such election requires a majority of at least nine votes, out of which at least six votes must be given by German nationals. The President shall receive a deed of appointment, which has to be signed by the members of the General Board taking part in the election as well as by the Reich President. The President elected as aforesaid shall be deemed lawfully appointed by the delivery of the said deed.

If the Reich President refuses to sign the deed of appointment of the elected person, another election shall take place. If the Reich President also refuses to sign the appointment of such other person, a third election shall take place. The said third election shall be final and the appointment shall be deemed lawful, notwithstanding the absence of the signature of the Reich President on the deed of appointment.

The members of the Managing Board, having been approved of by the General Board, shall be appointed by the President. The approval of the General Board requires the same majority as the election of the President. The appointment shall be for a term of twelve years, subject always to the condition that on attainment of the age of 65 years, a member shall cease to hold office.

As regards the term of the first appointed members of the Managing Board, the following special provision shall apply. With the exception of the President, they shall be divided into three groups, of which the two first must be equal in number and the third group must either be equal in number with each of the two first groups, or, if this is arithmetically impossible, it may consist of a smaller number, but the number must be as near as possible to the number of each of the other groups. The first group shall contain the youngest members, the third group the oldest members and the second group shall embrace the remaining members. The members of the first group shall be elected for twelve years, the members of the second group for eight years and the members of the third group for four years. The age-limit of 65 years shall also apply to members elected at the first election.

The term of office of the President is four years. The President and the members are eligible for re-election.

In the case of a new election or of an addition to the membership of the Managing Board, the candidate must be approved by the Managing Board.

On important grounds the President or a member of the Managing Board can be dismissed at any time without prejudice to their contractual rights. The dismissal on important grounds can be given to the President by the General Board with the same majority as provided for in paragraph 4 above, and to a member of the Managing Board likewise by the General Board with the same majority, but not without the President's consent.

§ 7

The Bank is represented by the Managing Board in all judicial and extra-judicial proceedings. The authority of the Board in legal transactions is to be verified by an official certificate on the part of the Certificating Official of the Managing Board appointed in accordance with § 8.

Any declarations to be made by the Managing Board are binding on the Reichsbank if made by two members of the

Managing Board. The declarations of members may be replaced by the declarations of substitutes. Declarations to be made by the Directorates of the Reichsbank Head Establishments and the Reichsbank Establishments are binding on the Reichsbank if made within the ordinary course of business of the Branch Establishment concerned in the matter by both members of the Directorate or by their substitutes.

The provisions of section 232 (1), clauses 2 and 3 of the German Commercial Code shall be applied *mutatis mutandis*.

In the case of actions against Reichsbank Head Establishments and Reichsbank Establishments, having relation to the conduct of their business, the Court of the place in which the Branch Establishment has its office, has jurisdiction.

§ 8

The President of the Reichsbank Managing Board shall, as regards the "Reichsbank Head Establishments," appoint Bank Commissioners and, as regards "Reichsbank Establishments," appoint Bank legal officers whose respective spheres of action shall be determined by him.

The President of the Reichsbank Managing Board has power to appoint for the Reichsbank as well as for the Branch Establishments Certifying Officers, who must have the qualifications required for appointment to a German Judgeship, for being appointed as judges; they have official seals. In the case of Branch Establishments the Bank Commissioners and Legal Officers shall as a rule be appointed as Certifying Officers.

The documents drawn up by the Certifying Officers in matters concerning the Reichsbank shall have the same effect as if they had been drawn up by a Court of Law or by a notary. The Certifying Officers have the right in matters concerning the Reichsbank to legalise signatures and to issue certificates proving the authority of the Reichsbank Managing Board and of officials of the Directorates of the Branch Establishments having the statutory power of agency for the Reichsbank as regards legal transactions.

§ 9

The President shall appoint the officials in accordance with the proposals of the Managing Board and determine the distribution of their work and duties in respect of the business of the Bank.

The legal positions of the officials of the Bank shall be determined by special "regulations relating to officials" to be issued by the Managing Board.

The "regulations relating to officials" shall preserve for the officials of the Reichsbank the rights of Reich Government Officials and impose upon them the duties of Reich Government Officials. Deviations from the Law concerning Reich Government Officials are admissible only so far as they are required for the maintenance of a well-arranged and efficient conduct of the business of the Bank.

Breaches of duties imposed by the "regulations relating to officials" shall be dealt with in accordance with a disciplinary procedure in accordance with the rules governing the penal procedure against Reich Government Officials. In these proceedings the President of the Reichsbank exercises the functions of the Supreme Reich Authority.

The Bank may appoint employees and workmen by contract; the rights and duties of such employees and workmen are determined by the general legal rules and by tariff contracts in force at the date of this Law coming into force. On notice to terminate the tariff contract being given, special house tariff contracts are to be entered into by the Reichsbank.

§ 10

As regards the President and the members of the Managing Board the rules relating to shares, intermediate salaries, pensions and the allowances to dependents on death to be issued by the General Board.

As regards the officials of the Bank the Reichsbank Managing Board issues the rules relating to salaries, intermediate salaries, pensions and the allowances to dependents

on death ; these rules are to be based on the principles of Reich Law.

A more favourable determination of the salaries of the officials of the Bank in comparison with the salaries of Reich Officials is only admissible in so far as such more favourable determination is necessary for the maintenance of a well-arranged and efficient conduct of the business of the Bank.

The regulations relating to the salaries of the Bank officials as well as any amendments and additions to the same shall be communicated by the Reichsbank Managing Board to the Reich Government before they become operative. In the case of any difference of opinion as regards the admissibility (see above under paragraph 3) of the regulations of salaries between the Reichsbank Managing Board and the Government, the latter may within four weeks after having received such communication, invoke the judgment of a Court of Arbitration.

The Court of Arbitration shall consist of three members. Each party shall appoint one member ; the third member, who shall be a permanent member and shall preside over the Court of Arbitration, shall be chosen by the President of the Reichsgericht out of such suitable persons as are known to be experienced in matters of the kind in question.

The application for arbitration is to be made to the Chairman of the Court of Arbitration. The award of the Court of Arbitration shall be binding on the Reich Government and on the Reichsbank Managing Board. Pending such award the former rules shall remain in force.

The provisions contained in the above paragraphs 3 to 6 shall not affect the power of the Reichsbank in any individual case of special services, according to the requirements of the Reichsbank, to make special grants, as long as such special grants shall not in the aggregate exceed 10 per cent. of the total amount applied to the remuneration of officials.

The persons mentioned in the above paragraphs 1 and 2 shall have no claims against the Reich arising out of their contracts of service.

B.—REPRESENTATION OF SHAREHOLDERS.

§ 11

The General Meeting represents the shareholders. Every shareholder not being under any legal incapacity, who is entered in the registers of the Reichsbank as owner, is entitled to participate in the General Meeting in the manner determined by the "Satzung."

The number of votes to which everyone appearing at the General Meeting is entitled is determined by the nominal amount of the shares represented by him. Every share is entitled to one vote, no person shall be entitled to more than three hundred votes.

Decisions are taken by simple majority. In the case of an equality of votes the nominal amount of shares is decisive.

§ 12

In every year a report as to administration shall be presented to the General Meeting. The General Meeting shall decide as to the Balance Sheet and as to the distribution of profits in accordance with this Law.

It shall also determine any changes in the "Satzung" proposed by the Reichsbank Managing Board and approved of by the General Board.

§ 13

There shall be formed with the Reichsbank a permanent Committee of the Shareholders (Central Committee) whose consultative opinion the Managing Board may obtain, if they think fit. The members of this Committee shall be elected by the General Meeting of the shareholders on the proposal of the Managing Board from among German shareholders representing the banks, agriculture, commerce, industry, handicrafts and labour.

The "Satzung" shall prescribe the rights and duties of such a Central Committee.

There shall be elected Deputies of the Central Committee for the purpose of consultation of the Reichsbank Managing

Board in special matters, who may be invited to the meetings of the Managing Board upon the consideration of such matters. The "Satzung" shall prescribe the rights and duties of such Deputies.

In the same manner there shall be formed Local Committees of the greater independent Branch Establishments of the Reichsbank, from among whom Local Deputies shall be elected. The "Satzung" shall prescribe the rights and duties of such Local Committees and Deputies.

C.—GENERAL COUNCIL.

§ 14

A General Board of the Reichsbank shall be constituted, consisting of 14 members, seven of whom must be German nationals, while the other members must consist of one British national, one French national, one Italian national, one Belgian national, one American (United States) national, one Dutch national and one Swiss national. The General Board shall have power by an unanimous vote to increase the number of its German members.

§ 15

The President of the Reichsbank Managing Board shall be one of the German members and at the same time the Chairman of the General Board.

The term of office of a member of the General Board shall be for three years except in the case of the President and the Commissioner. During the first period of the existence of the General Board three German members and three foreign members shall serve for the term of one year, two German members and two foreign members for the period of two years, and two German members and two foreign members for the period of three years. It shall be decided by ballot at the first meeting of the General Board which members— with the exception of the President and the Commissioner— shall accordingly serve during the shortened term of one or two years. If any person is appointed as President, who did not previously belong to the General Board, such German

member shall vacate his membership as has been a member for the longest period. In case of doubt the decision shall be taken by lot.

§ 16

The German members, with the exception of the President, are elected by such of the shareholders of the Reichsbank as are German nationals ; in so far as the "Satzung" establishes a right of co-optation, confirmation on the part of the said shareholders shall take the place of election.

The special mode of election is determined by the "Satzung."

The Organisation Committee shall, with the assent of the President, issue the regulations required in respect of the election of the first German members.

The first foreign members shall be appointed by the Organisation Committee.

Whenever subsequently a foreign member vacates his office a person of the same nationality as such member shall be elected in his place by the foreign members being members at the date of the election. Unanimity save for one vote shall be required in respect of such election.

Before a foreign member is elected, the General Board shall request the Central Note Issuing Bank of the country whose national is to be elected to express its opinion.

§ 17

The following classes of persons shall not be elected as members of the General Board :—

- (a) officials in the immediate service of the German Reich or of any German State ;
- (b) persons who receive any payment from the German Reich Government or from the Government of any German State.

The provisions of the first paragraph of this section shall apply *mutatis mutandis* to the officials of any foreign

State and to persons receiving payment from any such State or its Government.

§ 18

The resolutions of the General Board require a majority of at least ten votes, but a simple majority shall be sufficient if it includes the votes of the President and the Commissioner. A member unable to be present at a meeting shall be at liberty to authorise another member, by registered letter or telegram, to vote on his behalf.

At each of its meetings, and at least once every month, the General Board shall examine the reports submitted to it by the President and the Commissioner. It shall decide on the proposals made to it by the President and the Commissioner, provided that those decisions do not encroach upon the rights of administration reserved to the Managing Board.

§ 19

The General Board shall appoint one of its foreign members or another foreigner who is a national of one of the countries represented on the General Board pursuant to § 14, as Commissioner for the issue of notes. The resolution appointing him requires at least nine votes including at least six foreign votes. The election of a person who is not a member has the effect of causing the vacation of the membership of the member who is a national of the same State as the person elected. The person elected as Commissioner by virtue of such election shall become a member of the General Board. His term of office shall be for four years.

§ 20

All persons taking part in the business of the Bank as managers, officials or employees, as well as the members of the General Board of the Central Committee and of the Local Committees are under an obligation to observe secrecy as to all matters and arrangements of the Bank coming to their knowledge and especially as to all individual transactions of the Bank and as to the extent of the credits granted, even

after the cessation of their employment or of their membership of the General Board, the Central Committee or a Local Committee.

The meetings of the Reichsbank Managing Board, the General Board, the Central Committee and of the shareholders in General Meetings shall take place in Berlin.

In order to maintain permanent contact as to currency matters and financial policy, the Reichsbank Managing Board shall be under an obligation to report at regular intervals to the Government of the Reich, or at any time on special request of the Government in regard to these matters.

IV.—The Bank's Sphere of Business.

§ 21

The Bank shall be authorised to undertake the following classes of transactions :

- (1) To buy and sell gold and silver in bars or in coins as well as "Devisen."
- (2) To discount, buy and sell bills of exchange with a currency of not more than three months and in respect of which three obligees of known solvency are responsible, and also cheques in respect of which three obligees of known solvency are responsible. The requirement of a third signature may be dispensed with in cases in which the safety of the bill of exchange or cheque is secured by a collateral security or in some other manner. But in no case must the amount of the bills of this last category exceed 33 per cent. of the total amount of bills discounted by the Bank at any given time. The bills to be discounted shall be exclusively good commercial bills.
- (3) To grant loans at interest for a period of not more than three months on the security of moveable objects (Lombardverkehr), *i.e.*—
 - (a) On the security of gold and silver whether coined or in bars ;

- (b) On the security of fully paid original shares or original preference shares or preferential obligations of German Railway Companies whose Railways are working ; or on the security of the Mortgage Bonds of Provincial or Communal Land Credit Institutes or of other Land Credit Institutes under State supervision ; or of German Mortgage Banking Companies (the amount lent not to exceed three-quarters of the market value of such Mortgage Bonds), (the following securities being deemed available in the same way as the said Mortgage Bonds, *viz.*, the bonds to bearer of German Public Land Credit Institutes as well as such bonds to bearer of the other hereinbefore mentioned Institutes and Banks which are issued against loans granted to a German Communal Corporation or in consideration of the undertaking of a guarantee by any such Corporation) ;
- (c) On the security of bonds to bearer (maturing within a year) of the Reich, of any German State or any German Communal Corporation or on the security of interest bearing bonds to bearer of which the interest is guaranteed by the Reich or by any German State ; but loans against securities enumerated in this clause shall be made only to Banks of known solvency, the amount lent not to exceed three-quarters of the market value of such securities ;
- (d) On the security of interest bearing bonds to bearer of foreign States and also on the security of foreign railway preference debentures guaranteed by a foreign State to the extent of not more than 50 per cent. of the market value ;
- (e) On the security of bills of exchange in respect of which the obligees are of recognised solvency, subject to a deduction of at least 5 per cent. of their market value ;

- (f) On the security of merchandise stored in Germany to the extent of not more than two-thirds of its value.

The Bank shall have the power, if specially authorised thereto by the General Board, to accept bonds of the Reich maturing at a distant date as security for loans repayable within three months if two obligees are liable for the loans apart from the security resulting from the pledging of the bonds (one of the obligees to be a bank carrying on business in Germany), but subject to the condition that loans, in respect of which bonds of the Reich maturing at a distant date are pledged, may never exceed the amount of the paid-up capital of the Reichsbank and its reserve funds.

- (4) To buy and sell bonds of the kind hereinbefore mentioned under (3c); but for its own account only in so far as this shall be necessary for the maintenance of the ordinary business relations with customers of the Bank.
- (5) To collect sums of money for account of private persons, institutions and public authorities and, after having received cover for the same, to make payment or transfers through the Branch Establishments or correspondents.
- (6) To buy Stock Exchange investments of any kind or gold or silver for account of others after having in advance received cover in respect thereof and to sell the same after previous delivery to the Bank.
- (7) To receive sums of money free of interest either on deposit account or on current account.
- (8) To assume the custody and administration of articles of value.

If a person liable as a debtor in respect of a loan granted to him against security of moveable articles is in a state of delay, the Reichsbank is authorised, without having previously obtained judicial authorisation or assistance, to cause the pledged article to be sold publicly by one of its officials or by an authorised auctioneer, or in any case in which the pledged

article has a Stock Exchange value or market value, to cause the pledged article to be sold even without publicity by one of its officials or by an authorised broker or in default of any such, by an official having authority to act as auctioneer, at the current price, and to recoup itself out of the proceeds in respect of principal, interest and costs. This right is vested in the Bank even as between itself and other creditors of the debtor as well as between itself and the debtor's estate in bankruptcy.

§ 22

The Reichsbank is under obligation to take bar gold at the fixed rate of 1392 Reichsmarks for one pound fine in exchange against its notes.

The Bank is authorised to cause such bar gold to be examined and assayed by any technical experts to be appointed by the Bank in that behalf, at the vendor's expense.

§ 23

The Reichsbank Managing Board is bound from time to time to determine and publish the percentage rates at which it discounts bills or grants loans at interest.

§ 24

Subject to the stipulation contained in § 21 (3*b*), the Bank is forbidden to accept bills, to grant loans on the security of land or mines, oil-fields or shares except by way of additional security, and it is also forbidden to buy or sell land, shares or goods except in the case of purchases for the purpose of carrying on the business of the Bank or of the realisation of existing assets.

§ 25

The Reichsbank is under obligation to accept or make payments for the Reich at the request of the Government Authorities by any of its establishments appropriate for that purpose and also to effect transfers without the transmission of cash between the various financial establishments of the Reich.

Without prejudice to the rule contained in the fourth paragraph of this section the Bank is authorised to give credit to the Reich for purposes of administration ; but in each case for a term not exceeding three months and only up to the maximum amount of one hundred million Reichsmarks. At the end of any business year of the Bank the Reich must not be indebted to the Bank in any way.

The Reich will entrust the Reichsbank with all banking business concerning the general administration of the Reich. The Reichsbank as a matter of principle is bound to transact such banking business; if the Reichsbank declines a particular transaction the Reich is authorised to have such transaction carried out by another agency. The freedom of the Reich as regards the channels to be utilised for the issuing of loans or Treasury orders shall be preserved ; but it is understood that such loans shall be placed mainly through the organisation of the Reichsbank. In any event the Reich shall communicate to the Reichsbank in good time its intentions in regard to all such matters.

The Reichsbank is also authorised to grant credits to the German Reich Post and the German Reich Railway to a reasonable extent for the purposes of their ordinary business up to the aggregate amount of two hundred million gold marks for both. In any such case the rule contained in paragraph 3 is to be applied *mutatis mutandis* at the request of the Reichsbank. The direct financial relations between the Reich Post Office and the Ministry of Finance shall not be affected by the rules contained in this paragraph.

The fulfilment of the tasks mentioned in paragraph 1 as well as the payment of interest and the repayment of loans of the Reich is to be carried out for the general administration of the Reich free of all costs and charges. As regards the other kind of Banking business of the Reich the Reichsbank shall at the utmost charge the same rates as those generally chargeable to the other customers of the Bank. The Bank is however authorised to agree to a reduction of its charges by contract with the Reich.

Except as aforesaid the Bank shall not grant any credits directly or indirectly either to the Reich or to the States or Communes (Unions of Communes) or to foreign Governments.

§ 26

A separate account will be kept at the Reichsbank for the Reparation payments to be made to the Bank. The relations between the authorised representatives of the Reparation Commission in its capacity of a creditor of the amount standing to its credit of the one part and the Bank of the other part, are merely those existing between a Bank and its customers.

The amount standing to the credit of the Reparation Commission shall not without the Bank's consent exceed the amount of 2 milliard Reichsmarks.

V.—Issue of Notes, Cover, Commissioner for the Issue of Notes.

§ 27

The preparation and completion, the issue, the withdrawal and cancellation of bank-notes shall be effected by the Note Department of the Bank under control of the Commissioner.

The Commissioner shall be empowered and it shall be his essential duty to insist upon the carrying out of such of the provisions contained in the Law and in the "Satzung" as refer to the exercise of the right of issue of notes and the preservation of the cover in gold for the notes in circulation. With that object the Commissioner shall have the right to have furnished to him all statistics and documents which he may deem useful for the accomplishment of his task. He may also, either personally or through his assistants, undertake all investigations in the Bank relevant to the performance of his duty. He may be present at the meetings of the Managing Board.

The daily statistics as to the cover of notes and as to the notes in circulation must be continually submitted to the commissioner for his examination and approval.

The participation of the Commissioner in the preparation and completion of the notes shall be evidenced by a special "Completion Control Stamp" which shall be placed on the

notes under the Commissioner's directions. Every note put into circulation by the Bank must be marked with this stamp.

The Commissioner and his assistants shall be bound to observe complete secrecy in respect of all affairs and arrangements of the Bank which have come to their knowledge.

§ 28

The Bank shall be compelled to keep at all times in respect of its notes in circulation—

- (a) A cover of at least 40 per cent. in gold or "Devisen" (Gold Cover). This cover must at least as to three-quarters consist of gold.

The expression "Gold" within the meaning of this direction connotes bar gold as well as German or foreign gold coins (the pound fine being calculated at 1392 Reichsmarks) in so far as such gold is in the possession of any office of the Bank or deposited with any foreign Central Note-issuing Bank in a manner to be at all times at the free disposal of the Reichsbank.

"Devisen" are bank-notes, or bills of exchange having not more than 14 days to run, cheques and claims due from day to day payable in foreign currency by a bank of known solvency in foreign financial centres. They are to be taken at their gold value for the time being.

- (b) For the remaining amount discounted bills of exchange or cheques satisfying the requirements specified in § 21.

§ 29

In exceptional circumstances the cover referred to in § 28 under (a) may be reduced below 40 per cent. on the proposal of the Managing Board by a resolution of the General Board; such a resolution of the General Board requires unanimity except as to one vote.

In the case of such a reduction of the cover extending over more than one " Bank return week " the Bank has to pay to the Reich in respect of the amount by which the prescribed cover of 40 per cent. falls short a percentual note tax computed in accordance with the following directions :—

In the case of a cover between 37 and 40 per cent. :
3 per cent. per annum,

In the case of a cover between 35 and 37 per cent. :
5 per cent. per annum,

In the case of a cover between $33\frac{1}{3}$ and 35 per cent. :
8 per cent. per annum,

In the case of a cover of less than $33\frac{1}{3}$ per cent. :
8 per cent. per annum with the addition of one per cent. per annum in respect of each one per cent. by which the percentage of the reserve falls short of $33\frac{1}{3}$ per cent.

The rate of discount must in any case in which the cover during a Bank return week or during a longer period remains uninterruptedly below 40 per cent. amount to at least 5 per cent.

Whenever a note tax is payable the rate of discount shall be raised by at least one-third of the percentage of the tax which is payable, and this increase shall be in addition to the increase of the said rates of discount required for the purpose of satisfying the requirements of the third paragraph of this section.

§ 30

For the purposes of the assessment of the tax the Reichsbank Managing Board must not later than the tenth of each month deliver to the Reich Finance Minister the data required for the assessment of the tax for the last preceding month. The tax must be paid not later than the end of the month.

§ 31

The Bank is under obligation to pay its notes to the bearer thereof—

(a) at its principal office in Berlin immediately on presentation ;

- (b) at any branch establishment in so far as its available cash and its cash requirements admit of such payment.

Payment at the Bank's option may be made—

- (1) in German gold coins of the weight and fineness authorised by law for the time being at their par value ;
- (2) in gold bars in pieces of not less than 1000 Reichsmarks and not more than 35000 Reichsmarks, at their value in pure gold in German gold coins of the weight and fineness authorised by law for the time being ;
- (3) in cheques or orders to pay in foreign currency equivalent in value to the market value of the currency concerned in the matter as expressed in gold. The "Satzung" enumerates the foreign banks on which the cheques or orders to pay may be drawn. The Reichsbank may in such a case charge a commission. The said commission may, however, not exceed the amount representing the share apportionable to the amount paid in the cost of transmission of larger sums of gold to the place of business of the foreign bank concerned in the matter, together with interest.

§ 32

The Bank must make compensation for damaged notes in so far as the bearer either presents a part of the note that is larger than one-half of the note or produces evidence showing that the remaining part of the note of which he presents only the half or a smaller part has been destroyed.

The Bank is under no obligation to give compensation for notes which have been destroyed or lost.

§ 33

Bank notes which are returned in a damaged or soiled state to the office of the Bank or to one of its branch estab-

ishments or to an office appointed by the Bank for the payment of bank notes may not be re-issued.

§ 34

The calling in and withdrawal of notes shall be effected by the Managing Board, which shall issue special rules relating to these matters and to the cancellation of the notes which have been called in. These rules must be published in the Reich Gazette.

§ 35

In addition to the cover of its note issue provided for in § 28 the Bank shall at all times hold a special cover of at least 40 per cent. of the liabilities falling due from day to day; this cover must consist of deposits at call (money due from day to day) in Germany or abroad, cheques on other banks, bills of exchange having not more than 30 days to run or claims recoverable at call arising from debts covered by pledges.

The requirements as to special cover provided for above shall not apply to the account opened by virtue of § 26.

§ 36

The Bank shall publish statements as to its assets and liabilities in accordance with the following rules:

The weekly statement must contain—

(1) On the side of the liabilities—

The foundation capital,
The reserve funds,
The amount of the notes in circulation,
The other debts maturing from day to day,
The debts dischargeable after notice,
The other liabilities.

(2) On the side of the assets—

The stock of gold (bar gold as well as German and foreign gold coins, the pound fine being calculated at 1392 Reichsmarks);
The stock of "Devisen" suitable as cover,

Other bills of exchange and cheques,
German token coins,
Notes of other Banks,
Debts covered by pledges (Lombardforderun-
gen), stocks and shares,
Other assets.

In addition to this there must be a statement showing any liabilities in respect of re-discounted bills of exchange payable in Germany.

In addition to this the Bank must within six months after the end of each business year publish at its own expense in the Reich Gazette a detailed balance sheet of its assets and liabilities as well as the yearly statement of the Profit and Loss Account. The "Satzung" shall contain the detailed rules relating to the preparation of the balance sheet.

VI.—Distribution of Profits.

§ 37

Twenty per cent. of the yearly net profit shall be carried to reserve fund as long as the amount of such reserve fund is less than 12 per cent. of the amount of the notes of the Bank in circulation computed on the basis of the average of the preceding six months.

Shareholders are entitled to a yearly dividend of 8 per cent. If in any year the dividend is less than that percentage, the deficiency is to be the first charge on the net profit of the following years after deduction of the amounts which according to law must be added to the reserve fund, unless such deficiency can be made up out of an existing Dividend Reserve.

The balance of the net profit remaining after payment of the said dividend has to be distributed as follows: 50 per cent. of the first 50 million Reichmarks falls to the Reich and 50 per cent. to the shareholders, 75 per cent. of the next 50 million Reichmarks falls to the Reich and 25 per cent. to the shareholders, of the remainder, if any, 90 per cent. falls to the Reich and 10 per cent. to the shareholders. The amounts so allotted to the shareholders may be paid out as an additional

dividend or may be used for a special reserve for future dividends created for the purpose of equalisation of dividends.

Any money derived from premia on shares issued by the Bank shall be placed to reserve.

VII.—Liquidation.

§ 38

After the lapse of the Reichsbank's right to issue bank-notes in Germany, the Reich shall be entitled, subject to one year's notice, to dissolve the Reichsbank and to take over the premises belonging to it.

The price at which parcels of land belonging to the Reichsbank on the 1st January, 1925, shall be taken over shall correspond to the market value of such parcels of land on the 1st January, 1925. This price must be determined during the year 1925 by agreement between the Finance Minister of the Reich and the Reichsbank. If the said parties cannot agree, the price shall be fixed by Court of Arbitration. The said Court of Arbitration shall consist of two representatives of the Reichsbank and two of the Reichs Minister of Finance and of an Umpire to be appointed by the said representatives. If the said representatives cannot agree as to the person of the Umpire the said Umpire shall be appointed by the President of the "Reichsgericht."

The price at which parcels of land acquired by the Reichsbank after 1st January, 1925, shall be taken over shall be the purchase price paid by the Reichsbank and in default of any such purchase price, the market value of such parcels of land at the date of their having been acquired. As regards the determining of the market value the rules contained in the second paragraph of this section shall be applied *mutatis mutandis*.

Before going into liquidation the Reichsbank shall give notice to the Government in good time.

VIII.—Penal Provisions.

§ 39

Any person, who shall unlawfully issue bank-notes or any other certificates of indebtedness payable to bearer, shall be

subject to a fine amounting to ten times the amount of the notes or certificates issued by him but not amounting in any case to less than 5000 Reichsmarks.

§ 40

Any person who, in disregard of the prohibition contained in § 4, makes use for purposes of payment of foreign bank-notes or other non-interest bearing certificates of indebtedness issued to bearer by foreign corporate bodies, partnerships or private persons expressed as payable in Reich currency either exclusively or concurrently with other determinations of values, shall be subject to a fine of a minimum amount of 50 Reichsmarks.

If the person concerned makes a regular trade of such an unauthorised use, a sentence of imprisonment for a term not exceeding one year shall be added to the fine. An attempt to commit the said offence is punishable.

§ 41

The members of the Managing Board shall be subject to the following penalties :—

- (1) If in the publication described by the rules contained in § 36 they shall knowingly misrepresent or veil the position of affairs of the Bank, they shall be punishable with imprisonment for not more than three months ;
- (2) If the Bank issues notes for a larger amount than the authorised amount, they shall be punishable with a fine equal to ten times the amount of the excess of the issue up to at least 5000 Reichsmarks.

§ 42

Any official or employee of the Bank who, in reply to an enquiry addressed to them by the President, by the Reichsbank Managing Board, by the General Board or by the Commissioner within their respective powers, shall knowingly make false statements, shall be punishable with a fine not exceeding 500 Reichsmarks, or with detention except in so

far as they are punishable with a severer sentence under any other laws affecting the matter.

§ 43

In so far as any fines have to be imposed by virtue of this law the fine to be fixed in Gold marks as long as, according to the rules of the German Penal Code, any fine has to be fixed in Gold marks. In this respect the Gold mark is to be deemed equal to a Reichsmark.

IX.--Concluding and Transitory Provisions.

§ 44

The "Satzung" of the Reichsbank shall determine the following matters :—

- (1) The form of the shares in the Reichsbank and the dividend certificates and "talons," relating to the same ;
- (2) The form to be observed as to the transfer or pledging of share certificates;
- (3) The rules as to the public notice to be given in the case of the loss or destruction of share certificates and as to the annulment thereof and as to the procedure in the case of lost dividend certificate and "talons;"
- (4) The principles according to which the yearly balance sheet of the Reichsbank is to be made up ;
- (5) The dates and methods for the collection of dividends ;
- (6) The form to be used for the convocation of the General Meeting as well as the conditions and the methods to be applied as to the exercise of the voting rights of the shareholders ;
- (7) The mode of election of the Central Committee and its Deputies, of the Local Committees, and of the Local Deputies at the Reichsbank Branch Establishments ;
- (8) The form in which the notices to be issued by the Company are to be given as well as the public journals in which they are to be inserted ;

- (9) The names of the foreign banks on which cheques and orders for payment may be issued under §31(b) (3) ;
- (10) Regulations as to the election of the German members of the General Council.

The Organisation Committee shall issue the first "Satzung." Such "Satzung" as well as later amendments shall be published by the Managing Board in the Official Gazette.

§ 45

The Reichsbank and its branches within the whole area of the Reich shall be free of all corporation taxes, income-taxes and trade taxes.

In so far as any privileges in respect of the tax on transfers of capital (Kapitalverkehrssteuer) have been established in favour of the Reichsbank or of any business transactions with the Reichsbank, such privileges shall continue. The payment of notes (§ 31) shall not be subject to the tax on Stock Exchange transactions (Börseumsatzsteuer).

In so far as share certificates of the Reichsbank are owned by foreigners not being domiciled within the German Reich, the dividends and other profits to which the shareholders, as such, are entitled shall not be subject to a tax on income (which expression shall include the tax on the profits derived from capital).

§ 46

In so far as a privileged status has hitherto been accorded to the Reichsbank or to its organs the Reich Government will guarantee its continuance. In particular the following provisions shall apply :

The privileges accorded from time to time to the public authorities of the Reich in matters relating to residences and letting agreements by virtue of any statutory enactments, shall apply to the Reichsbank, subject to the modification that the Reich Government shall be substituted for the Supreme Government Authority having to determine these matters under the said enactments. In so far as the Reich Government has to determine questions as to residences

and letting agreements of Public Authorities, such matters shall also, as regards the Reichsbank be determined by the Reich Government. Ejection decrees ordered by the Housing Authorities relating to business premises of the Reichsbank or official residences of Reichsbank officials, or hired official residences of Reichsbank officials shall not be enforced unless they shall have been previously sanctioned by the Reich Government.

The Reich Government shall determine to what extent the Reichsbank Managing Board shall have authority, in the interest of the conduct of its business, to request any public authority to give information and, more particularly, to forward public records and registers of Criminal Courts.

The Reichsbank shall not belong to any Industrial Chamber or to any Chamber of Commerce.

No person acting as manager, official, or employee of the Reichsbank shall be appointed as Assessor of any Chamber of Commerce.

As regards the care of persons having suffered serious injuries, the appointment of authorised candidates for employment, the regulation of the working hours, trade inspection and other matters within the domain of social welfare, the rules applying to the Reich Public Authorities shall apply to the Reichsbank *mutatis mutandis*.

The provisions of § 359 of the German Criminal Code and of §§ 54, 76 and 96 of the Criminal Procedure Code and of §§ 376 and 408 of the Civil Procedure Code as well as the law concerning the liability of the Reich for its officials of the 22nd May 1910 (Reichsgesetzbl, p. 798), shall apply to the Reichsbank, its managers and officials *mutatis mutandis*.

§ 47

The provisions of the Commercial Code relating to entries in the Commercial Register and as to the legal effects of such entries shall not apply to the Reichsbank.

§ 48

The provisions of the Bourse Law as to the compulsory issue of prospectus shall not apply in respect of shares in the Reichsbank.

§ 49

As long as the notes hitherto issued by the Reichsbank have not been withdrawn, the Reichsbank shall observe the same rules as to cover as have been enacted in respect of the new issue of notes, a billion marks of the late issue being deemed equal to one Reichsmark.

§ 50

The pecuniary claims of all persons who, prior to the coming into force of this Law, had the status of Reichsbank officials shall be preserved.

§ 51

The first election of the President shall take place within six months of the coming into force of this Law.

§ 52

The date for the coming into force of this Law shall be determined by the Reich Government. The coming into force of the rules of § 31 requires in addition concurrent resolutions of the Reichsbank Managing Board and of the General Board. Such resolutions are to be published in the Reichsgesetzblatt. Up to that date the rules contained in § 2 of the Law of the 4th August, 1914 (Reichsgesetzbl. page 347) concerning Reichskassenscheine and bank-notes, shall remain in force, in so far as it relates to Reichsbank notes.

§ 53

Subject to the provisions contained in § 52 above the Bank Law of the 14th March 1875, and the Laws amending the same shall cease to be in force except the Law of the 19th March 1924 (Reichsgesetzblatt II, page 73). At the same time the provisions of the Rentenbank Ordinance of the 15th October 1923 (Reichsgesetzblatt I, page 963), and of the Law relating to the German Gold Discount Bank of the 19th March 1924 (Reichsgesetzblatt II, page 71), shall cease to be in force in so far as they are in contradiction with this Law.

BERLIN, August 30th 1924.

APPENDIX I

Table showing total Capital, Reserve, Deposits, and Cash Balances of the old Presidency Banks and their amalgamated Institution the Imperial Bank of India.

| Year. | Paid-up Capital. | Reserve and Rest. | Total. | DEPOSITS. | | Total. | Cash Balances. |
|-------|------------------|-------------------|-------------|-------------|-------------|-------------|----------------|
| | | | | Public. | Private. | | |
| 1870 | Rs. (1,000) | Rs. (1,000) | Rs. (1,000) | Rs. (1,000) | Rs. (1,000) | Rs. (1,000) | Rs. (1,000) |
| 1880 | 3,36,25 | 25,57 | 3,61,82 | 5,43,05 | 63,961 | 118,266 | 9,96,87 |
| 1890 | 3,50,00 | 55,27 | 4,05,27 | 2,91,15 | 84,928 | 11,40,43 | 7,41,45 |
| 1900 | 3,60,00 | 97,54 | 4,47,54 | 3,59,25 | 14,76,35 | 18,35,60 | 12,96,75 |
| 1905 | 3,60,00 | 1,99,61 | 5,59,61 | 2,80,53 | 12,88,27 | 15,68,80 | 5,04,49 |
| 1910 | 3,60,00 | 2,63,37 | 6,23,37 | 3,11,91 | 22,26,37 | 25,38,28 | 8,23,01 |
| 1913 | 3,75,00 | 3,31,03 | 6,91,03 | 4,23,63 | 32,34,38 | 36,58,01 | 11,35,12 |
| 1914 | 3,75,00 | 3,73,07 | 7,48,07 | 5,88,66 | 36,43,50 | 42,37,16 | 15,37,75 |
| 1915 | 3,75,00 | 3,89,17 | 7,64,17 | 5,61,52 | 40,04,08 | 45,65,60 | 20,83,92 |
| 1916 | 3,75,00 | 3,72,50 | 7,47,50 | 4,88,67 | 38,61,19 | 43,49,86 | 14,65,24 |
| 1917 | 3,75,00 | 3,60,99 | 7,35,99 | 5,20,58 | 44,70,87 | 49,91,45 | 17,27,25 |
| 1918 | 3,75,00 | 3,67,52 | 7,42,52 | 7,71,28 | 67,71,74 | 75,43,02 | 33,77,31 |
| 1919 | 3,75,00 | 3,44,58 | 7,19,58 | 8,64,28 | 50,97,75 | 59,62,03 | 17,07,62 |
| 1920 | 3,75,00 | 3,57,81 | 7,32,81 | 7,72,24 | 68,21,37 | 75,93,61 | 23,62,93 |
| 1921 | 5,62,24 | 3,77,79 | 7,52,79 | 9,02,63 | 78,01,90 | 87,04,53 | 26,03,34 |
| 1922 | 5,62,50 | 4,14,54 | 9,76,78 | 6,80,01 | 65,77,99 | 72,58,00 | 18,60,23 |
| 1923 | 5,62,50 | 4,33,07 | 9,95,57 | 14,15,73 | 57,00,57 | 71,16,30 | 15,07,47 |
| 1924 | 5,62,50 | 4,55,21 | 10,17,71 | 8,56,94 | 74,19,51 | 82,76,45 | 15,01,34 |
| | 5,62,50 | 4,80,08 | 10,42,58 | 7,50,26 | 76,71,22 | 84,21,48 | 15,60,20 |

APPENDIX II

Table showing total Capital, Reserve, Deposits and Cash Balances of the Indian Joint Stock Banks.

CLASS A.—Banks with capital & reserve of Rs. 5 lakhs and over.

| Year. | Number of reporting Banks. | Paid-up Capital | Reserve and Rest. | Total. | Deposits. | Cash Balances. |
|-------|----------------------------|-----------------|-------------------|----------------|----------------|----------------|
| | | Rs. (1,000) | Rs. (1,000) | Rs. (1,000) | Rs. (1,000) | Rs. (1,000) |
| 1870 | 2 | 983 | 182 | 1,165 | 1,395 | 507 |
| 1880 | 3 | 1,800 | 311 | 2,111 | 6,337 | 1,663 |
| 1890 | 5 | 3,350 | 1,759 | 5,109 | 27,078 | 5,679 |
| 1900 | 9 | 8,212 | 4,560 | 12,772 | 80,752 | 11,904 |
| 1905 | 9 | 8,457 | 7,782 | 16,239 | 1,19,892 | 17,350 |
| 1910 | 16 | 27,566 | 10,055 | 37,621 | 2,56,585 | 28,025 |
| 1913 | 18 | 23,133 | 13,294 | 36,427 | 2,25,919 | 40,017 |
| 1914 | 17 | 25,140 | 14,188 | 39,328 | 1,71,058 | 35,318 |
| 1915 | 20 | 28,139 | 15,665 | 43,804 | 1,78,727 | 39,941 |
| 1916 | 20 | 28,736 | 17,366 | 46,102 | 2,47,105 | 60,349 |
| 1917 | 18 | 30,370 | 16,299 | 46,669 | 3,11,701 | 76,484 |
| 1918 | 19 | 43,645 | 16,559 | 60,204 | 4,05,948 | 94,858 |
| 1919 | 18 | 53,907 | 22,427 | 76,334 | 5,89,947 | 1,21,663 |
| 1920 | 25 | 83,702 | 25,546 | 1,09,248 | 7,11,464 | 1,63,070 |
| 1921 | 27 | 93,880 | 30,081 | 1,23,961 | 7,68,963 | 1,56,590 |
| 1922 | 27 | 80,224 | 26,165 | 1,06,389 | 1,16,386 | 1,20,388 |
| 1923 | 26 | 68,905 | 28,439 | 97,344 | 4,44,282 | 73,701 |
| 1924 | 29 | 69,055 | 38,039 | 1,07,094 | 5,25,052 | 1,12,970 |

APPENDIX II—(contd.)

CLASS B.—Banks with capital and reserve between Rs. 1 lakh and less than Rs. 5 lakhs.

NOTE—Amounts are in thousands of rupees.

| Year. | Number of re- porting Banks. | Paid-up Capital. | Reserve and Rest. | Total. | Deposits. | Cash Balances |
|-------|------------------------------------|---------------------|-------------------------|---------|-----------|------------------|
| | | Rs. | Rs. | Rs. | Rs. | Rs. |
| 1913 | 23 | 39,14 | 11,35 | 50,49 | 1,51,15 | 24,95 |
| 1914 | 25 | 42,22 | 13,02 | 55,24 | 1,26,54 | 27,99 |
| 1915 | 25 | 45,38 | 9,73 | 55,11 | 91,37 | 20,01 |
| 1916 | 28 | 51,77 | 11,50 | 63,27 | 1,01,23 | 16,76 |
| 1917 | 25 | 44,16 | 10,24 | 54,40 | 99,20 | 20,42 |
| 1918 | 28 | 48,65 | 14,43 | 63,08 | 1,55,35 | 36,90 |
| 1919 | 29 | 53,11 | 21,86 | 74,97 | 2,28,49 | 53,71 |
| 1920 | 33 | 61,42 | 19,95 | 81,37 | 2,33,46 | 41,91 |
| 1921 | 38 | 77,05 | 23,23 | 1,00,28 | 3,26,02 | 43,52 |
| 1922 | 41 | 83,00 | 27,65 | 1,10,65 | 3,37,89 | 56,02 |
| 1923 | 43 | 81,14 | 30,20 | 1,11,34 | 3,26,50 | 61,47 |
| 1924 | 40 | 72,64 | 34,22 | 1,06,86 | 2,66,53 | 34,36 |

APPENDIX III

*Statement showing failures of Indian Joint Stock Banks from
1913 to 1924.*

| Year. | Number of Banks that failed. | TOTAL CAPITAL OF BANKS THAT FAILED IN Rs. (1,000). | | |
|-----------|------------------------------------|---|-------------|----------|
| | | Authorised. | Subscribed. | Paid-up. |
| | | Rs. | Rs. | Rs. |
| 1913 ... | 12 | 2,74,00 | 1,64,56 | 35,14 |
| 1914 ... | 42 | 7,90,70 | 2,45,48 | 1,09,02 |
| 1915 ... | 11 | 56,50 | 7,79 | 4,50 |
| 1916 ... | 13 | 2,30,90 | 20,90 | 4,23 |
| 1917 ... | 9 | 76,50 | 35,76 | 25,26 |
| 1918 ... | 7 | 2,09,50 | 4,86 | 1,46 |
| 1919 ... | 4 | 52,50 | 6,47 | 4,03 |
| 1920 ... | 3 | 10,40 | 7,68 | 7,25 |
| 1921 ... | 7 | 70,40 | 5,81 | 1,25 |
| 1922 ... | 15 | 10,15,55 | 27,26 | 3,30 |
| 1923 ... | 20 | 21,86,90 | 9,92,36 | 4,65,47 |
| 1924 ... | 18 | 6,30,31 | 26,46 | 11,34 |
| Total ... | 161 | 55,23,16 | 15,45,39 | 6,72,25 |

NOTE.—Out of 161 failures, 146 were in respect of banks that had paid-up capital of less than Rs. 5 lakhs each, and 126 in respect of banks that had paid-up capital of less Rs. 1 lakh each.

APPENDIX IV

Table showing total Capital, Reserve, Deposits and Cash Balances of the Exchange Banks working in India.

| Year. | Number of Banks. | CAPITAL AND RESERVE. | | | DEPOSITS. | | | CASH BALANCES. | |
|-------|------------------|----------------------|-------------------|-----------|---------------|-----------|---------------|----------------|--|
| | | Paid-up Capital. | Reserve and Rest. | Total. | Out of India. | In India. | Out of India. | In India. | |
| | | £ (1,000) | £ (1,000) | £ (1,000) | £ (1,000) | £ (1,000) | £ (1,000) | £ (1,000) | |
| 1870 | 3 | 20,04 | 180 | 21,84 | 26,88 | 52,31 | 26,11 | 61,13 | |
| 1880 | 4 | 25,32 | 541 | 30,73 | 73,05 | 3,39,88 | 20,46 | 1,80,09 | |
| 1890 | 5 | 63,84 | 16,99 | 80,83 | 3,07,34 | 7,53,60 | 58,10 | 3,50,43 | |
| 1900 | 8 | 1,18,03 | 39,71 | 1,57,74 | 5,42,63 | 10,50,35 | 1,19,45 | 2,39,58 | |
| 1905 | 10 | 1,52,04 | 72,19 | 2,24,23 | 9,45,36 | 17,04,45 | 2,15,04 | 3,78,13 | |
| 1910 | 11 | 2,17,34 | 1,26,10 | 3,43,44 | 13,41,66 | 24,79,17 | 1,78,10 | 4,38,51 | |
| 1913 | 12 | 2,36,40 | 1,41,85 | 3,78,25 | 18,11,38 | 31,03,54 | 2,56,88 | 5,88,24 | |
| 1914 | 11 | 2,28,15 | 1,41,57 | 3,69,72 | 16,49,70 | 30,14,76 | 4,06,04 | 8,39,37 | |
| 1915 | 11 | 2,26,81 | 1,41,12 | 3,67,93 | 17,99,48 | 33,54,56 | 4,51,11 | 7,60,13 | |
| 1916 | 10 | 2,28,36 | 1,50,95 | 3,79,31 | 20,82,32 | 38,03,88 | 4,13,67 | 10,14,01 | |
| 1917 | 9 | 1,83,84. | 1,42,98 | 3,26,82 | 22,80,01 | 53,37,53 | 5,47,65 | 33,74,37 | |
| 1918 | 10 | 2,22,69 | 1,71,80 | 3,94,49 | 30,59,37 | 61,85,60 | 5,79,81 | 15,17,55 | |
| 1919 | 11 | 3,19,31 | 2,11,39 | 5,30,70 | 43,30,01 | 74,35,90 | 6,35,71 | 29,98,32 | |
| 1920 | 15 | 5,41,93 | 3,60,19 | 9,02,17 | 51,36,71 | 44,80,71 | 8,41,97 | 25,17,53 | |
| 1921 | 17 | 6,63,69 | 4,52,63 | 11,16,32 | 52,64,73 | 75,19,61 | 8,23,18 | 23,56,74 | |
| 1922 | 18 | 6,65,41 | 4,56,80 | 11,22,21 | 52,73,48 | 73,38,44 | 8,16,54 | 16,17,63 | |
| 1923 | 18 | 8,30,38 | 5,69,65 | 14,01,03 | 89,49,46 | 68,44,28 | 11,79,15 | 14,47,86 | |
| 1924 | 18 | 7,25,38 | 5,79,26 | 13,04,64 | 84,46,82 | 70,63,48 | 11,46,48 | 16,36,69 | |

APPENDIX V—(contd.)

Table II.—CO-OPERATIVE BANKS.

(In thousands of Rupees.)

Class A.—Banks with capital and reserve of Rs. 5 lakhs and over.

| Year. | No. of Banks. | Paid-up Capital. | Reserve. | Total. | Deposit and Loans received. | Loans outstanding. | Cash Balance. |
|---------|---------------|------------------|-------------|-------------|-----------------------------|--------------------|---------------|
| | | Rs. (1,000) | Rs. (1,000) | Rs. (1,000) | Rs. (1,000) | Rs. (1,000) | Rs. (1,000) |
| 1915-16 | 2 | 7,81 | 55 | 8,36 | 19,46 | 26,71 | 122 |
| 1916-17 | 2 | 10,33 | 78 | 11,11 | 25,03 | 33,78 | 151 |
| 1917-18 | 3 | 16,58 | 1,74 | 18,32 | 52,79 | 58,91 | 61 |
| 1918-19 | 4 | 19,99 | 4,68 | 24,67 | 1,35,44 | 1,11,09 | 736 |
| 1919-20 | 2 | 10,34 | 4,08 | 14,42 | 96,34 | 86,93 | 410 |
| 1920-21 | 5 | 28,15 | 8,41 | 36,56 | 2,29,38 | 2,31,59 | 383 |
| 1921-22 | 5 | 29,80 | 9,96 | 39,76 | 2,82,68 | 2,59,30 | 22,89 |
| 1922-23 | 5 | 30,68 | 12,92 | 43,60 | 3,41,05 | 2,57,48 | 47,71 |
| 1923-24 | 8 | 44,36 | 17,99 | 62,35 | 4,13,99 | 3,32,89 | 37,13 |
| 1924-25 | 8 | 47,53 | 21,73 | 69,26 | 4,51,41 | 3,53,81 | 19,08 |

APPENDIX V—(contd.)

Table II.—CO-OPERATIVE BANKS.

(In thousands of Rupees.)

Class B.—Banks with capital and reserve between Rs. 1 lakh and less than Rs. 5 lakhs.

| Year. | No. of Banks. | Paid-up Capital. | Reserve. | Total. | Deposit and | Loans | Cash |
|---------|---------------|------------------|-------------|-------------|-----------------|-------------|-------------|
| | | | | | Loans received. | outstanding |  | Balance. |
| | | Rs. (1,000) | Rs. (1,000) | Rs. (1,000) | Rs. (1,000) | Rs. (1,000) | Rs. (1,000) |
| 1915-16 | 18 | 17,29 | 5,17 | 22,46 | 1,14,71 | 1,11,95 | 7,24 |
| 1916-17 | 21 | 21,02 | 6,73 | 27,75 | 1,49,45 | 1,45,47 | 6,86 |
| 1917-18 | 24 | 22,27 | 8,22 | 30,49 | 1,52,34 | 1,53,78 | 3,94 |
| 1918-19 | 29 | 31,78 | 8,82 | 40,60 | 1,57,37 | 1,73,73 | 7,12 |
| 1919-20 | 29 | 48,96 | 15,12 | 64,08 | 2,63,79 | 2,83,92 | 7,17 |
| 1920-21 | 36 | 55,73 | 14,22 | 69,95 | 2,48,90 | 2,77,38 | 12,87 |
| 1921-22 | 46 | 77,29 | 16,75 | 94,04 | 3,63,00 | 3,78,38 | 16,24 |
| 1922-23 | 63 | 1,01,63 | 29,42 | 1,31,05 | 5,02,02 | 5,18,84 | 15,08 |
| 1923-24 | 71 | 1,16,00 | 55,48 | 1,71,48 | 5,84,32 | 6,40,76 | 24,39 |
| 1924-25 | 90 | 1,18,05 | 48,76 | 1,66,81 | 7,94,47 | 7,61,80 | 39,51 |

APPENDIX VI (A).
STATEMENT OF THE AFFAIRS OF THE IMPERIAL BANK OF INDIA.
BALANCE SHEET as at 31st DECEMBER 1925.

| LIABILITIES. | Rs. | A. P. | ASSETS. | Rs. | A. P. |
|--------------------------------------|---------------------|-------------|---|---------------------|-------------|
| Subscribed Capital | 11,25,00,000 | 0 0 | Government Securities | 15,79,54,836 | 2 11 |
| Capital paid-up | 5,62,50,000 | 0 0 | Other authorised Securities under the Act | 1,21,89,154 | 1 6 |
| Reserve | 4,82,50,000 | 0 0 | Loans | 14,70,09,105 | 1 3 |
| Public Deposits | 5,46,44,291 | 14 2 | Cash Credits | 35,77,51,718 | 0 4 |
| Other Deposits | 77,83,32,840 | 3 5 | Inland Bills discounted and purchased | 4,88,62,293 | 0 0 |
| Loans against Securities per contra | ..... | ..... | Foreign Bills discounted and purchased | 1,08,52,274 | 13 8 |
| Loans from the Government of India | ..... | ..... | Bullion | ..... | ..... |
| under Section 20 of the Paper | ..... | ..... | Dead Stock | 2,73,98,557 | 1 5 |
| Currency Act, against Inland Bills | ..... | ..... | Liability of Constituents for Contingent Liabilities per contra | ..... | ..... |
| discounted and purchased per contra. | ..... | ..... | Sundries | 45,75,909 | 11 8 |
| Contingent Liabilities | ..... | ..... | Balances with other Banks | 5,84,259 | 15 6 |
| Sundries | 43,83,380 | 1 3 | Cash | 76,71,78,108 | 0 3 |
| TOTAL | 94,18,60,512 | 2 10 | TOTAL | 94,18,60,512 | 2 10 |

The above Balance Sheet includes—

| | | | |
|---|-----------|----|----|
| Deposits in London | £. | s. | d. |
| Advances in London | 1,016,273 | 0 | 4 |
| Cash and Balance at other Banks in London | 1,098,540 | 17 | 9 |
| | 47,201 | 12 | 4 |

APPENDIX VI (A) — (contd.)

PROFIT AND LOSS ACCOUNT for the half-year ended 31st DECEMBER, 1925.

| | INCOME. | | | EXPEN ITURE. | | | Rs. A. P. | | | Rs. A. P. | | |
|---|-------------|----|----|--------------|----|----|-----------|----|----|-------------|----|----|
| | Rs. | A. | P. | Rs. | A. | P. | Rs. | A. | P. | Rs. | A. | P. |
| Amount brought forward | 21,97,874 | 8 | 2 | | | | | | | | | |
| Amount received in Interest, Discount, Exchange, Commission, etc. | 1,26,26,018 | 3 | 10 | | | | | | | 1,48,23,892 | 12 | 0 |
| | 60,16,657 | 10 | 7 | | | | | | | | | |
| Establishment | 95,706 | 8 | 7 | | | | | | | | | |
| Governors' and Local Board Members' Fees | 22,500 | 0 | 0 | | | | | | | | | |
| Auditors' Fees | 5,29,665 | 2 | 10 | | | | | | | | | |
| Rent, Taxes, Insurance, Lighting, etc. | 1,37,333 | 7 | 10 | | | | | | | | | |
| Pay of Guards | 9,73,030 | 0 | 6 | | | | | | | | | |
| Depreciation and Repairs to Bank Property | 49,318 | 1 | 4 | | | | | | | | | |
| Law Charges | 1,92,700 | 0 | 6 | | | | | | | | | |
| Postages and Telegrams | 3,38,479 | 7 | 11 | | | | | | | | | |
| Stationery | 4,45,593 | 3 | 1 | | | | | | | | | |
| Miscellaneous Expenses | ..... |  |  |  |  |  |  |  |  | 88,00,973 | 11 | 2 |
| | | | | | | | | | | 60,22,919 | 0 | 10 |
| Amount set aside for payment of a Dividend at the rate of 16 per cent. per annum (free of Income-Tax) | 45,00,000 | 0 | 0 | | | | | | | | | |
| Amount transferred to Reserve Fund | 5,00,000 | 0 | 0 | | | | | | | | | |
| Balance carried forward | 10,22,919 | 0 | 10 | | | | | | | 60,22,919 | 0 | 10 |

APPENDIX VI (B).

Statement of the Affairs of the Imperial Bank of India on the 17th September, 1926.

| LIABILITIES. | | Rs. | A. P. | ASSETS. | | Rs. | A. P. |
|---|-----|-----------------------|------------|---|-------|-----------------------|------------|
| Subscribed Capital | ... | 11,25,00,000 | 0 0 | Government Securities | ... | 20,32,32,000 | 0 0 |
| Capital paid up | ... | 5,62,50,000 | 0 0 | Other authorised securities under the Act | ... | 1,22,32,000 | 0 0 |
| Reserve | ... | 4,92,50,000 | 0 0 | Loans | ... | 11,76,15,000 | 0 0 |
| Public Deposits | ... | 19,49,81,000 | 0 0 | Cash Credits | ... | 21,10,21,000 | 0 0 |
| Other Deposits | ... | 80,19,37,000 | 0 0 | Inland bills discounted and purchased | ... | 4,58,67,000 | 0 0 |
| Loans against securities per contra | ... | ..... |  | Foreign bills discounted and purchased | ... | 21,12,000 | 0 0 |
| Loans from the Government of India under Section 20 of the Paper Currency Act, against Inland bills discounted and purchased per contra | ... | ..... |  | Dead Stock | ... | 2,77,07,000 | 0 0 |
| Contingent liabilities | ... | ..... |  | Bullion | ..... | ..... |  |
| Sundries | ... | 83,67,000 | 0 0 | Liability of constituents for contingent liabilities per contra | ... | 46,46,000 | 0 0 |
|  | ... | ..... |  | Sundries | ... | 4,34,000 | 0 0 |
|  | ... | ..... |  | Balances with other Banks | ... | ..... |  |
|  | ... | ..... |  | Cash | ... | 62,48,66,000 | 0 0 |
|  | ... | ..... |  |  | ... | 48,59,19,000 | 0 0 |
| Total | ... | 1,11,07,85,000 | 0 0 | Total | ... | 1,11,07,85,000 | 0 0 |

The above Balance Sheet includes—

| | | |
|--|-----|-----------|
| Deposits in London | ... | £ 889,300 |
| Advances in London | ... | 948,700 |
| Cash and Balances at other Banks in London | ... | 18,300 |

Percentage 48.33. Bank Rate 4 per cent.

N. H. Y. WARREN,
N. M. MURRAY.

Managing Governors.

APPENDIX VI (C).

THE CENTRAL BANK OF INDIA, LIMITED.

Following is the statement of Liabilities and Assets of The Central Bank of India, Ltd. for the Fortnight ended 15th September 1925.

| LIABILITIES. | Rs. | ASSETS. | Rs. |
|---|--------------|--|--------------|
| Capital Subscribed <u>Rs. 3,36,00,000.</u> | | Cash (credits and overdrafts on Government and other authorised securities ... | 4,20,36,000 |
| " Paid up ... | 1,68,00,000 | Loans on Government and other authorised securities ... | 3,48,82,000 |
| Reserve Fund ... | 1,00,00,000 | Bills Discounted ... | 1,36,16,000 |
| Deposits, debts due to Banks and Agents, Bills payable, etc. ... | 14,69,30,000 | Bank Premises ... | 54,36,000 |
| Sundries including Branch adjustments ... | 2,36,73,000 | Sundries including Branch adjustments ... | 2,02,51,000 |
| | | Cash in hand, at Banks, and Investments in War Bonds, Government Paper, Shares, Debentures, Properties, etc. ... | 8,11,82,000 |
| | 19,74,03,000 | | 19,74,03,000 |

A. S. BALSEKER.

Chief Accountant.

INDEX

- Acceptances, bank, 229.
Accounts, vernacular, 358.
Act.
 Aldrich-Vreeland, 124.
 Co-operative, 38.
 Federal Farm Loan, 297.
 Federal Reserve, 125, 126.
 Imperial Bank of India,
 31.
Indian Companies, 29, 155
 —156.
 Paper Currency, 29, 401.
 Presidency Banks, 29.
Advances, maxims for, 231.
Restrictions on, 143.
Agency Houses, 27.
Agency work, 382.
Agricultural bank, Provin-
 cial, 283, 284.
Agricultural banks, 93, (*See*
 Chap. XII).
Agricultural Credit, 270.
Agricultural Credit Board,
 285, 286.
Aldrich bill, 125.
Aldrich-Vreeland Act, 124.
Alexander & Co., 27.
Allahabad Bank, 31, 63, 90.
Alliance Bank of Simla, 31,
 33, 34.
All India Banks, 215.
Act--*contd.*
Amalgamation of banks,
 117.
Amalgamation of Central
 and Tata banks, 35.
America, Romance and
 Tragedy of Banking in,
 13.
American banking, 118—
 150.
Peculiarities of, 135.
American and Central
 banking, 133.
American Express Company
 70.
American War, 29.
Amortisation payment
 table, 291.
Anglo-Italiana Bank, 261.
Asiatics, Credit instruments
 Known to, 3.
Assyria, 2.
Athens, 2.
Bacon's Essay on usury, 3.
Backwardness and Defects
 of Indian Banking, Chap.
 IV.
Backwardness of Indian
 Banking, Causes of, 94.
Chart of, Frontispiece

Balance Sheet of,
 Birmingham Municipal
 Bank, 342—343.
 Central Bank of India, 457.
 Imperial Bank of India,
 453.
 Banca Italiana, 109.
 Banco d'
 Napoli, 109.
 Rialto, 6.
 Sicilia 109.
 Banco National Ultrama-
 rino, 70.
Bania, 22 25.
 Bank Acceptances 229.
 Bank Amalgamation, move-
 ment towards, 117.
 Bank,
 Credit utility of, 16.
 Derivation of, 3.
 Examiners, 145, 162, 168,
 189.
 Failures, 36.
 Law, 192, 213, 363.
 Money, 7.
 Rate, machinery of, 113.
 Relief Fund, 165.
 Bank of
 Amsterdam, 6.
 Baroda, 64.
 Bengal, 27.
 Bombay, 28, 29.
 England, 7, 103, 110, 111,
 112, 250.
 France, 8, 278.
 Hamburg, 6, 7.

Bank of—*contd.*
 India, 32, 64.
 Issue, 19, 103, 106, (Also
see Central Bank).
 Issue's special facilities
 364.
 Madras, 28.
 Mysore, 64.
 Sweden, 6
 Taiwan, 70, 234
 Bankers,
 Association, 371.
 Early, 5
 Indian, 5.
 Institute of, 371, 372.
 London, 4.
 Medieval, 3.
 Banking,
 American—system, 118—
 150.
 (Also *see* Federal Farm
 Loan Act).
 Backwardness and Defects
 of Indian—system,
 Chap. IV.
 Branch, 118.
 Council, 161, 166, 180,
 181, 192, 197 221, 223.
 Crisis, 33, 124.
 European—system, 6, 102
 —118.
 Figures (*see* Tables).
 Functions, 9.
 History of, 2, 6, 119.
 In England, 4, 93.
 In India, 25, 31, 92.

Banking—*concl'd.*

In U. S. A., 199.
System to be complete,
should consist of, 100.

Banks and Bankers,
Private, 349.

Banque,
de Rome, 191.
Italiano Disconto, 191.
National de Credito, 191.
Royale, 8.

Barclay's Colonial Bank, 259.

Bengal Bank, 27.

Bengal National Bank, 32.

"Big Five" banks, 87, 90.

Bill of Exchange, 3.

Bills, institution of, 25.

Bills, as reserve to currency,
103, 110, 200, 392.

Bismarck, 107.

Blackett, Sir Basil, 175, 249.

Bombay Merchants Bank,
33.

Branch banking, 118.

British National Debt, 7.

Business of,

Exchange Banks, 71.
Indigenous Banks, 25, 66.
Imperial Bank, 48—54.
Joint-stock Banks, 66.

Business figures of Banks,
(*see* Tables and statistical
appendices).

Caisse de Dépôts et Con-
signations 255.

Business of.—*cont'd.*

Calcutta Industrial Bank,
35.

Cantonal Banks, 109.

Capital of Banks, 137, 215.
(Also *see* Tables and statis-
tical appendices).

Central Bank, 20, 104, 108,
171, (Also *see* Bank of
Issue).

Influence of—over banking
system, 112, 114.

Proposed, 171.

Central banking system of
Europe, 102.

Central Bank of India, 33
35, 64, 91, 357.

Central Board of Imperial
Bank of India, 47.

Chase 121.

Chartered Bank of India,
Australia and China, 70.

Cheque currency and
Government, 366.

Chettys, 25, 43, 44.

China, Notes current in, 6.

Clearing Houses, 82, 133,
203, 242, 380.

Commandit, 352.

Commercial Banks, 92, 112.

Commercial and Central
Banks, 114—116.

Commercial Law, 360.

Commission,

Chamberlin, 397.

Currency (Hilton Young)
46, 171, 181, 202, 399.

- Commission—*contd.*
 Industrial, 313—314.
 National Monetary, 110,
 124.
 Re. Bank of Bombay, 29.
 Tariff, 313.
- Committee,
 Babington Smith, 397.
 Cunliffe, 111, 247.
 Fowler, 394.
 Herschell, 394.
 Maclagan, 281.
- Commonwealth Bank of
 Australia, 105.
- Company promoter and in-
 dustrial banks, 316.
- Comparative analysis of
 banking figures, 80—87,
 88—89.
- Complaints against Imperial
 Bank of India, 59.
- Comptoir National d'Es-
 compte de Paris, 70.
- Comptroller of Banks, 145,
 161, 162, 163, 191.
- Controller of Currency's
 Report, 43.
- Co-operative Act, 38.
- Co-operative Banks, 348.
- Co-operative Credit Socie-
 ties, 38.
- Machinery of, explained, 39,
 276.
- Cottage industries, 312.
- Credit Agricole, 278.
- Credit Bank of India, 33.
- Committee—*contd.*
 Credit, construction of, 15.
 Credit Foncier de France,
 299.
- Credit,
 Machinery for *ryot*, or-
 ganisation of, 281.
 Organisation of institu-
 tions, 9.
 Transactions in the East,
 2.
 Utility of a Bank, 16.
 Various kinds of, 18.
- Crossing, 26.
- Cunliffe Committee, 111, 247
- Currency Commission (Hil-
 ton Young), 46, 171, 181,
 202, 99.
- Currency functions of Cen-
 tral Bank, 199.
- Currency Note on, 387.
- "D" Banks, 352.
- Darshini hundies, 26.
- Darmstädter and National
 Bank, 352.
- Dawes Plan, 416.
- Deposit banking in England,
 4.
- Deposit Banks, 6.
- Deposits (*see* Tables).
- Directors,
 Interlocking of, 139—140,
 221.
 Ordinary and Special, 217.
- Discounts, 97.
- Discount Houses, 350.

- Directors** --*con'd.*
Discount rate (*see* Bank rate and Hundi rate).
Dresdner Bank, 277.
Dutch East India Company, 7.
East, Credit transactions in, 2.
East India Company, 27.
Eastern Bank, 70.
Economy in circulation, 19.
Education, banking, 372.
Egypt, 2.
Elasticity of currency, 110, 133.
Emergency measures, 98.
England, banking system of 4, 93.
Equitable mortgage, 361.
European banking system, 6, 102—118.
Examination tax, 244.
Examiners of Banks, 145, 162, 168, 189 (*Also see* Bank Examiners).
Exchange Banks, 6, 31, 37, 38, 70—78, 93.
Indian, 259.
Exchange (Rupee-Sterling) fluctuations, 397—399, (*see* Chart).
Federal Farm Loan Act, 297.
Federal Farm Loan Board, 297.
Federal Reserve,
 Act, 125, 126.
 Banks, 126—128, 130—133.
 Board, 129.
 System, 118—138.
Federation, principle of, 118.
Finance of international trade, 71.
Financial News, 44.
Foreign banks, 70, 75, 76, 77, 78, 248 (*Also see* Exchange Banks).
Conditions imposed upon, 251.
Figures of business of some, 88—89.
Result of financial operations, of 74.
Foreign capital and loans, difference in economic effect of, 322.
Foreign trade of India, (*see* tables on pages 80—87).
Functions of banks, 9.
General Bank of India, 27.
Germany, 274, 289, 312, 314, 351, 352.
Gold,
 Backing to Currency, 390.
 Exchange Standard, 396.
 Reserve, 109, 395.
 Standard, 393, 395.
 Standard Reserve, 402.
Goldsmiths, .

Gold—*contd.*

Governor-General-in-Council
46, 161, 162, 181, 186,
264, 287, 309.

Government Control 161.
and Examination 240.

Government want of sym-
pathy of, 33, 96.

Government, vote of cen-
sure upon, 34.

Grecians, 2.

Gresham's Law, 391.

Grossbanken, 315.

Harkishen Lal, 31, 32.

Herschell Committee, 394.

Hindustan Bank, 27.

History of banking, 2, 6, 31,
119.

Home Savings Safes, 337,
357.

Hongkong and Shanghai
Banking Corporation, 70.

Hundies, 25.

Hundi rate, 43.

Imperial Bank, 43.

Imperial Bank of India, 31;
34, 43, 45—63, 87, 172,
176, 199 &c.

Act, 31.

Balance Sheet of, 453.

Business of, 48—54.

Comparison with Central
banks, 57, 62.

Compensation to, 178,
382.

Complaints against, 59.

Imperial Bank of India,—
(*contd.*).

Figures of business of, 45,
445.

Remodelling of constitution
of, 174, 386.

Transformation of—into
Exchange Bank, 178, 261.

Weekly statement of, 56,
455.

India, banking in, 25, 31,
92 etc.

Indian, Australian, Cana-
dian, United Kingdom,
United States, banking
and other figures, 80—87.

Indian Bank of Madras, 33.

Indian bankers, 5.

Indian banking, defects and
drawbacks of, 94.

Indian banking, history of,
31.

Indian Companies Act 29,
155—156.

Indian Currency, (*see Note
on Currency*).

Indian Economic Con-
ference, 87.

Indian Exchange Banks,
259.

Indian Joint-stock banks,
63—69.

Business of, 66.

Indian Specie Bank, 32.

Industrial Bank of Japan,
325.

Industrial Bank of Western
India, 35.

- Industrial Banks 93, 310, 319.
 Business of 320.
 Provincial 326.
 Scheme of organisation of 326.
- Industrial
 Commission's Report 313 314.
 Credit Board, 329, 331, 333.
 Credit Unions, 317.
- Issue, Bank of, (*see* Central banks and banks of issue).
- Issues re :
 Banking Laws, 155.
 Central banking institution, 154.
 Government Administrative organisation, 153.
 Municipal and Local Board banks, 159.
 Private efforts, 160.
 Special type of banks, 158.
- James, I, 4.
- Japan, Industrial Bank of, 325.
- Japanese,
 Banking crisis, 234.
 Industrial Bank's loan operations, 323.
- Jews, 4.
- Joint-stock bank (S), 63—69.
 First—in India, 27.
- Japanese—*contd.*
 Business of, 66.
 Figures of business of (*see* Tables).
 Joint-stock banking in India 27, (*see* Chaps. II, III, and IV).
 Karnani Industrial Bank, 35.
 Kathiawar and Ahmedabad Banking Corporation, 33.
 Knap's Theory of Value, 387.
 Krupps, 313.
 Lala Harkishen Lal, 31, 32.
 Land banks, 302.
 Land Credit Board, 303, 304.
 Land Mortgage Banks, 93, (*see* Long Term Credit, Chap. XII).
 Land Mortgage Bank, Provincial, 302.
 Landschaften, 289.
 Lloyds and National Provincial Bank, 259.
 Lloyds Bank, 70.
 Local Advisory Committees, 189.
 Local Banks, 215, 351.
 Local Board Banks, 340.
 Local representation, 222.
 London bankers, 4.
 Long term credit, 272, 288.
 Lottery bonds, 295.
 Louis XV, King of France,
 Maclagan Committee, 281.
 Mahajans, 22, 25, 44.

Japanese—contd.

- Managing Governors of Imperial Bank, 46.
 Manu's books, reference about credit in, 2.
Marwaris, 25.
 Medieval Bankers in Europe, 3.
 Mercantile Bank of India, 70.
 Midland Bank, 90.
 Ministry of Agriculture and Fisheries report, 94, 279, 300.
 Money,
 Changers, 3.
 Changing once principal.
 Function of bankers, 3.
 Lenders, 3.
 Lenders Act, 272.
 Lenders Bill, 108.
 Paper, 19 (*see* Paper Money).
 Transmission of, 18.
 Monometallic principle, 390.
 Mortgage Banks (*see* Land Mortgage Banks).
 Mortgages, 361.
 Movement of funds, 42.
 Municipal and Local Board Banks, 340.
 Municipal Bank of Birmingham, 160, 340.
 Balance Sheet of, 342—343.
Multanees, 25, 43.

Money—con'd.

- Napoleon Bonaparte, 8.
 National Bank of India, 70.
 National Bank of South Africa, 70.
 National bank laws, 138—146, 221.
 National Banks, 122.
 National bank system, 122.
 National Monetary Commission, 110, 124.
 National Provincial Bank, 87.
 Nederlandsche Indische Handelsbank, 70.
 Nederlandsche Handel Maatschappij, 70.
 Netherlands Bank, 180.
 Charter of, 403.
 New Peoples' Bank of Northern India 32.
 Note issue, 199.
 Note on Currency, 387.
 Oudh Commercial Bank, 31.
 Overseas Banks, 215, 259.
 P. & O. Banking Corporation, 70.
 Paper Currency, 19
 Act, 29.
 Paper Money, 390 (*Also see* Paper Currency, Currency)
 Partition of Bengal, 32.
 Pawn brokers, 345.
 Penalties, 245.
 People's Bank, 31.
 Pledge modification in the law regarding, 362.

- Money—*contd.*
 Plurality of note-issue, 109.
 Pochkhanawala, S. N., 64,
 91.
- Post Office,
 Cash Certificates, 41, 304.
 Savings Banks. 40, 42,
 334.
 to make them more ser-
 viceable, 335.
- Presidency Banks, 29, 30,
 31, 32, 46, 54.
 Act, 29.
- Preston, W. F., 26, 44.
- Preussische
 Central Boden Actien
 Gessellschaft, 296.
 Central Genossenschafts
 Kasse, 277.
- Pfanbrief Bank, 297.
- Prize drawings, 367.
- Propaganda, 355.
- Provincial Banks, 215, 351.
- Punjab National Bank, 31,
 64, 381.
- Raiffeisen system (of Co-
 operative Credit), 275.
- Raiffeisen William Fred-
 rick, 274.
- Rediscounting arrange-
 ments, 130, 227.
- Reichsbank, 107, 180, 184,
 199
- Charter of, 416.
- Rentenbank, 296.
- Rentenmarks, 296.
- Report of—
 Babington Smith Com-
 mittee, 397.
- Chamberlin Commission,
 397.
- Controller of Currency, 43.
- Cunliffe Committee, 111, 247.
- Currency (Hilton Young)
 Commission, 46, 171, 181,
 399, 202.
- Fowler Committee, 394.
- Herschell Committee, 394.
- Industrial Commission, 313
 —314.
- Maclagen Committee, 281.
- Ministry of Agriculture and
 Fisheries, 94, 279, 300.
- National Monetary Commis-
 sion, 110, 124.
- Tariff Commission, 313.
- "Reports," 07.
- Reserve Bank of India, 178,
 212.
- Remarks on—Bill, 375.
- Reserve,
 Cash, 130, 141, 226, 380.
 Currency, 131, 103, 200.
 From profits, 128, 141.
- Romans, 2.
- Rome, 2.
- Safety Fund system, 120,
 241.
- Savings Banks, (*see* Post
 Office Savings Banks), 40.
 Certificates, 328.

- Schultze-Delitzsch Franz
 Herman, 274.
 System, 275, 277.
 Security Fund, 165.
 Short term credit, 272, 273.
Shroffs, 43, 44.
 Singular note-issue, 109, 110.
 Societe Generale de Credit
 Mobiler, 319.
 Special Directors, 217.
 Stamp duty 359.
 State Bank Laws, 146—149.
 State Bank of Sweden, 6.
 State Bank (s), 105, 122,
 378.
 Dangers attending establish-
 ment of, 107.
 Statement,
 Fortnightly of the Central
 Bank of India, 456.
 Monthly, 239.
 Weekly, 206—209.
 Weekly of the Imperial
 Bank of India, 456.
 Statistical Appendices, 445
 —457.
 Stock Exchange, 10, 329.
 Sukkur Barrage, 300.
 Sumitomo Bank, 70.
 Sutlej Valley Project, 300.
 Suzuki and Co. 234.
 Swaything, Lord, 109.
 Swedish match manufac-
 turers, 323.
 Swiss National Bank, 104.
 Switzerland, Referendum in,
 109.
- Statement—*contd.*
 Syndicate operations, 223,
 236, 317.
 Taiwan Bank, 70, 234.
 Tables,
 Amortisation Table. 291.
 Banking figures of some
 of the important banks
 of the world, 88—89.
 Banking statistics of a
 few countries of the
 world, 87.
 Capital, reserve, deposits
 and cash balances of
 Exchange Banks, 449,
 of Indian Joint-stock
 Banks, 446, 447, of old
 Presidency Banks and
 the Imperial Bank of
 India, 445.
 Failures of Indian Joint-
 stock Banks, 448.
 Figures of business of
 important Indian Joint-
 stock Banks, 68—69.
 Indian and Australian
 banking and trade
 figures, 84.
 Indian and Canadian
 banking and trade
 figures, 83.
 Indian and United King-
 dom banking and trade
 figures, 80.
 Indian and United States
 banking and trade
 figures, 85.

Tables—*cont'd.*

- Indian banking business,
90.
Statistical tables re. Co-
operative Societies, 450
—452.
Tanan, M. L. 87.
Tariff Board, 313.
Tariff Commission, 313.
Tax on note-issue, 200.
Tata Industrial Bank, 35,
250.
Tata Iron and Steel Com-
pany, 313.
Thomas Cook and Sons, 70.
Tipoo Sultan, 27.
Trade names, Registration
of, 363.
Transfers, Rupee, 198, 382.

Tables—*cont'd.*

- Transmission of money, 18.
Trust business, 238.
Trust companies, 122, 123.
Laws, 149—150.
Trust funds, investment of
363.
Tucker, H. St. G., 27.
Vernacular Accounts, 358.
Versailles, Treaty of, 416.
Visering, G., 107.
Voting power of Banks, 245.
War boom, 35.
Warehouses, 66.
Weekly statement, 206, 209,
455.
William, III, 22.
Yokohama Specie Bank, 70.

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