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Central Banking in India
A Retrospect

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A REVIEW of the affairs of a public institution such as the Reserve Bank of India by its Chief Executive is likely to be regarded as an apologia "pro vita sua," and my excuse for undertaking this risky task is twofold. In the first place, I am anxious to fulfil a long-standing promise to the Director of the Gokhale Institute of Politics and Economics to deliver a Memorial Lecture, and I could not select a more appropriate subject than the fortunes and the functioning of an institution with which I have been so intimately connected for the last nine years. In the second place, India has just passed the threshold of a vital political and constitutional development, and in the offing are important changes in the economic and monetary field which involve a vital transformation in the status of the Reserve Bank of India. It seems but proper that at this epochal juncture, there should be a retrospect of the role that the Reserve Bank has played so far in the economic affairs of the country, not only for the purposes of economic history, but also for the search of any guidance that such a review might yield for the conduct in the future of the sector of national affairs which is the concern of the Reserve Bank. For the purposes of such a review, I do not propose to draw more than I can help on the recorded and published material. This material, which is available principally in the Annual Reports of the Bank, the Currency and Finance Reports and the special reports prepared by the Bank from time to time, can be referred to by any student of the subject. My sources would, in the main, be my own personal experience, the information that has been passed on to me by my predecessor, who took me into his confidence to a degree not generally realized, and on the records of the Bank which are not intended, in the ordinary course, for publication. My object will be to focus the spotlight on features of the Bank's genesis, personalities and administration, which are at the moment hidden from the purview of a casual critic of current affairs and may in future elude the researches of the hurrying historian. Central bankers are among the most taciturn members of the banking

fraternity, but in view of the special importance today of setting out the truth, the Central Board of the Reserve Bank have given me permission to tear the veil of secrecy away from the Bank's history and operations to the extent to which I deem it necessary for my purpose.

2. Long before the Hilton-Young Commission recommended in 1926 that India's financial structure should be completed by the creation of a Reserve Bank, the question of a central banking institution for India had been under examination both by Royal Commissions and by the Legislature. The Chamberlain Commission in 1914 included in their Report a comprehensive memorandum by John Maynard Keynes, one of their members, which proposed that the three Presidency Banks should be amalgamated into one central bank to be called the Imperial Bank of India, which would undertake the functions now generally associated with Central Banks. In the latter stages of the first World War, with its increased demand on India's financial resources, the necessity of a central institution became more apparent, and the Imperial Bank Act was passed in 1920 on the general lines of the Keynes' Memorandum. Thus, although the Reserve Bank of South Africa was the first Dominion Central Bank to be established (1920), the seed of a central banking institution for India was also planted at the same time. As it happened, the operation proved abortive. The underlying intention that the Imperial Bank should gradually take over the currency and other central banking functions could not be fulfilled as, in the meantime, central banking theory had developed on the lines that it was unsuitable that a bank which had important commercial functions should also be the central bank of a country. The Hilton-Young Commission took the line that an entirely separate institution should be created, to be called the Reserve Bank of India, and that the Imperial Bank should be more completely commercialised and should merely operate as the agent of the Reserve Bank of India for the routine management of the Government accounts. That it took nine years for this new line of approach to reach its goal was due to more than one reason. Attached to the Report of the Hilton-Young Commission was a Minute of Dissent from an influential Indian member whose views in economic and monetary affairs com-

manded, and have continued to command, very great respect, and who opposed the creation of a separate Reserve Bank as an unnecessary excrescence on the Indian banking system and recommended the gradual evolution of the Imperial Bank on the lines previously contemplated. Among Government circles also, there was powerful support for this view. My predecessor, who was then a Deputy Controller of the Currency, felt inclined to accept this view, but the Controller of the Currency scouted the idea and laid down that the Reserve Bank scheme was the only one that held the field. Much controversy centred round the question of who should be the controlling authority of the new institution. The Hilton-Young Commission, in paragraph 9 of their Report, suggested that the shareholders of the Imperial Bank should be given the first opportunity of subscribing for the capital stock of the new bank, which, of course, meant, in view of the large holdings under the control of the firms which constitute its directorate, that it would have had the full effective control from the start. The Government of India immediately rejected this suggestion as politically impracticable, and their decision was, in my opinion, and as events have proved, very wise. In the Indian Legislature, strong opposition developed to the shareholding conception itself, which was intrinsic in the proposals of the Commission. The Legislature wanted a State Bank, although they did not clearly define what exactly they meant. It was certainly not their intention that the constitution and administration of the Bank should be dominated by the executive of the day. Their thoughts turned rather to securing a constitution for the Bank somewhat comparable to that of the Legislature itself, but attempts to achieve this by various amendments became farcical when the Muslim and other minority communities took the logical standpoint that if the Board of the Bank were to be constituted on essentially the same lines as legislative bodies, those safeguards for the protection of minorities which had been found necessary in the former should be reflected in the latter. "After acrimonious and kaleidoscopic discussions," as the late Sir James Taylor has recorded, the Reserve Bank Bill of 1927, which was being piloted by the late Sir Basil Blackett, was, therefore, eventually dropped. The Report of the Central Banking En-

quiry Committee published in 1931, laid strong emphasis on the early establishment of a Reserve Bank, and in 1933, in the Round Table discussions, the scheme for the creation of a Reserve Bank was again brought forward, but from a new standpoint. The question at issue was that of transferring financial responsibility at the Centre to an Executive responsible to the Legislature, and it was thought by Government sponsors of the scheme that, if a body of shareholders should be created, they would produce a directorate which would operate as an internal safeguard against any rash financial or currency experiments. The successful institution and functioning of a Reserve Bank was, therefore, made a prerequisite to federation, and it was on this basis that the Reserve Bank Bill was resuscitated after the necessary transformation, and passed into law early in 1934. The Reserve Bank of India Act, 1934, varied from the original 1927 model in two important respects. In 1927 England was on the gold standard, and the original Bill contemplated that India should follow suit, with merely a transitory provision enabling it to sell sterling, if it so desired, instead of gold, so as to protect it in the event of there being too heavy a run on that metal. In 1933, however, with the collapse of the World Economic Conference, world exchanges were in a chaotic state, and the obligations of the Reserve Bank to maintain the rupee at a fixed ratio with sterling were, by virtue of the preamble to the Act, read with the amended Sections 39, 40 and 55 (2), intended to last until the international monetary position had become sufficiently clear and stable to make it possible to frame permanent measures. The second important change was as regards the composition of the Board. Here, the full and final acceptance of the shareholding principle made it possible to evolve a much simpler scheme of representation. A provision was also made to ensure that the shares were as widely distributed as possible, and a special delegation of the Central Legislature was to be appointed to supervise the issue of the shares to ensure that this was effectively done.

3. The student of the economic history of those times will always regret the delay that took place in the establishment of the Reserve Bank. Had it come into existence earlier, India might have been spared action by the Govern-

ment in the field of currency and exchange which proved injurious to India's interests. How the rulers of India tried to maintain a 2s. gold rupee and failed miserably is well known. It is not so well known that Sir Malcolm Hailey, the then Finance Member, was bitterly opposed to the idea and yet had no alternative, short of resigning his office, but to defend it in the Assembly and the country generally. The 2s. gold ratio was a last minute brain wave of members of the permanent staff of the India Office, and once it was accepted was "rammed through with the wooden obstinacy and maladroitness often exhibited by that Office." The failure of this ill-advised venture was a blow to the prestige of the Finance Department of the Government of India, from which it took years to recover; but there were two good and permanent products of the fiasco, the first being the amalgamation of the Presidency Banks into the Imperial Bank, and the other, the expansion of the Currency Department, by the creation of the Deputy Controllers of Currency for Bombay and Northern India. The absence of any popular check on the monetary action of the Government of India likewise led to developments which culminated in the fixing of the exchange at 1s. 6d. Taylor, who regarded Sir Basil Blackett as undoubtedly the ablest Finance Member who was ever sent to India, was convinced that before Blackett arrived in India he had already made up his mind to establish the 1s. 6d. ratio. On his assumption of office Blackett took steps calculated to ensure that that ratio was fixed, although in the light of later events his prognostication that a 1s. 4d. exchange might involve a rise in prices was a grotesque miscalculation and was completely falsified by 1925. Taylor was convinced that the fixing of the ratio at 1s. 6d. was a mistake, not so much on the merits as because of the fact that it ran counter to unmistakably influential public opinion in India and coloured all subsequent criticism of the actions of the Government of India in this field by suspicion and distrust. One good result of Blackett's forceful handling of the matter, however, was the shift of the balance of power in regard to the maintenance of exchange from London to India. Before Blackett, the control of exchange was centralised in London in the hands of the Finance Council of the India Office, in close working touch with the London Offices of the

exchange banks. "The India Office was blind to the impossibility of conducting business in this fashion after the introduction of the Reforms, and unfortunate Finance Members had to stand up in the Assembly and defend policies to which they were themselves opposed and the absurdity of which was often locally manifest."

4. As is well known, the chief Executives of the Bank, viz., the Governor and the two Deputy Governors, are, under Section 8 (1) of the Reserve Bank of India Act, to be appointed by the Central Government after consideration of the recommendations made by the Board in that behalf. Plans, characteristic of the foresight that the British bring to bear on public affairs in order to preserve what they regard as their own legitimate interests, were made to ensure that the first Governor of the Reserve Bank would be a person on whom the Bank of England could rely and of whom they could expect unquestioning co-operation. With this object in view, Sir Osborne Smith was first introduced to the Imperial Bank as the Managing Governor in 1926 in order to familiarise himself with the conditions of commercial banking in India and was, after a period of waiting which must have appeared irksome to himself and his sponsors, appointed first Governor of the Reserve Bank in 1935. His resignation in 1937 put a premature end to his tenure. While it would be obviously inappropriate for me to state the details of his conflicts with Sir James Grigg, the then Finance Member, and my predecessor the late Sir James Taylor, who was one of his deputies, I think I must permit myself to record that the main causes of Sir Osborne Smith's resignation were, apart from his temperamental incompatibility with the other two, the serious difference of opinion which arose between him and the Finance Member over the lowering of the Bank rate, with all its implications, and the management of the Bank's investments.

5. Of the late Sir James Taylor, the second Governor of the Reserve Bank and my immediate predecessor, I am happy to be able to say a very great deal more because of his many sterling qualities and of the length of our contacts and collaboration. Sir James Taylor was among the most remarkable men that it has been my good fortune to know. His intelligence was like a lambent flame which illumined

everything that it touched and purged it of dross, and he had a catholicity of interest, a breadth of outlook and a warm humanity which I have seldom seen equalled. His political views were most liberal and fair-minded. As long ago as 1929 he realised that whether within or outside the British Commonwealth of Nations, the independence of India was inevitable and he held that it would be the greatest work of the English to transform peacefully and purposefully their last and greatest Empire into a Commonwealth of Free Peoples. In his view, all that British vested interests could claim was a reasonable opportunity for liquidation and to secure itself against loss, but not to claim to fetter indefinitely constitutional action in its own interests. It was his firm conviction that the indispensable condition for the achievement and maintenance of self-government for India was a strong, efficient and honest administration through Indian personnel. In spite of the evidence of instances of corruption and nepotism, the causes of which he traced with sympathetic insight, he held that Indians who belong to services with an honourable tradition live up to that tradition in a way which does all honour to them in spite of the mud that is occasionally thrown at them by ignorant outsiders. He also realised with characteristic clarity that one of the strongest and noblest characteristics of the Indian is his "Izzat," which is more than honour and prestige. He was, therefore, an ardent champion of a rapidly progressive Indianisation of the administration with the final goal of complete Indianisation being kept steadily in view. Communalism he regarded as a canker in the body politic, and it was his opinion that communal electorates must go if there was to be any practical political advance at all in India. For the flourishing of communalism in India he largely held the indifference of the Government of the day to be responsible. As a preparation for carrying the burden of self-government, he strongly urged the spread of free and compulsory education and the remodelling of the educational system of the country, so as to put India first and to prevent the teaching of dogmas which inculcated the hatred of fellow-Indians because of their creed. In financial matters he was, even in his Controller of the Currency days, a vigilant watch-dog of India's interests. In the middle of 1931 when the Indian financial situation caused a great deal of

anxiety to the authorities in India owing to political uncertainties, there was a proposal that His Majesty's Government should guarantee credit for India up to £50 million sterling to reinforce currency reserves and to facilitate the early establishment of a Reserve Bank. Taylor was a strong supporter of this idea, and he held that, apart from considerations based on current events, Britain owed it to India to prevent financial collapse as a measure of recompense for a mistaken currency policy which had been followed in India by Great Britain in whom the control of India's finances had been vested since the Mutiny. He held that India's large favourable balance of trade should be settled by Britain, through whom its trade was financed, either in gold or, if in silver, then silver the price of which was internationally guaranteed. Since the proposal to throw the Indian mints open to the unrestricted coinage of gold was rejected in the teeth of Indian public opinion, and largely at the instance of the British Treasury, India had accumulated silver the price of which had crashed, thereby making its currency reserves utterly useless of the real purpose of a reserve. Apart from his intellectual attainments and the liberality of his views, Sir James was well cast to be the Governor of the Reserve Bank of India. As Deputy Controller of the Currency, and then as Controller, he had, between 1921 and 1931, been closely associated with the administration of Indian currency and exchange, and he played a very important role in the formulation of the proposals which were finally enacted in the shape of the Reserve Bank of India Act, 1935.

6. The detailed organisation and administration of the Reserve Bank was from the very first a duty which had been assigned to Sir James Taylor, and his knowledge of the minutiae of administration was unique. His relations with the Board of Directors were generally cordial and he commanded their respect and willing co-operation, except where, in their opinion, the interests of the country called for disagreement. "I must carry my Board with me," he often used to say. That the Directors unanimously recommended a renewal of his term for a further period of five years in 1942 bears testimony to his excellent relations with them and their confidence in him. In those days, that is, before the advent of a national government, the role of the Governor was

most difficult as he had to win and maintain the confidence of a foreign government on the one hand, and a predominantly elected Board of Directors representing the best and the most influential element in the business and public life of the country on the other. It was well understood by the Directors that the Governor was very often consulted by Government in his personal capacity in matters which were outside the sphere of the Reserve Bank, but which, nevertheless, impinged very closely on it. They relied on him to take them into confidence at the proper time, whenever necessary, and, generally speaking, I know of hardly any instance, where this mutual confidence was abused on either side.

7. It was unfortunate, although the incident left no lasting bitterness behind, that within a year of his assuming office as Governor of the Reserve Bank, Taylor had to disagree with the majority of the Central Board and support Government in the matter of the alteration of the ratio. During the first two years of the Bank's existence from April 1935 to 1937, the recovery after the world depression of 1931, and the cheap money policy of the United Kingdom, combined to simplify the task of the Reserve Bank. India's export surpluses were sufficient to enable it to build up its sterling balances and to meet its maturing sterling obligations. Thereafter, with the increasing international tension, the tide turned and the elected members of the Board took the attitude that, instead of following the normal measures for coping with such vicissitudes, they should recommend to Government that they considered an immediate alteration in the statutory ratio embodied in the Act. They made an informal representation in July 1938 to which Government replied, and they followed it by a formal resolution at their quarterly meeting at the end of November, in which those who wanted the change pressed matters to a divided vote, all the elected members voting against the Governor and the nominated members. Taylor felt that while it could not be denied that if members of the Board honestly felt that the position was irremediable they were entitled to make these views known to Government, there could be no doubt that Government, both under the Reserve Bank of India Act and the Government of India Act, and, even more, the fundamental constitutional realities of this or any other country,

must reserve the full discretion of coming to a decision on such a matter within their own hands. It appears that, following this line of logic, Government were even prepared to supersede the Central Board, not indeed as a measure of discipline, but to prevent an increasing element of futility creeping into their relations with the Board should this difference of opinion in regard to this vital matter of the ratio persist. As it happened, the Board refrained from pressing the matter any further, possibly on recognising the fact that the ratio agitation did not apparently command more than a formal support from the major political party in the country.

8. At the beginning of the war Taylor foresaw that the demand for silver might revive in India, in particular, if there should be adverse developments. He thought that the best way of stopping this was to make supplies freely available, if necessary, by importing from countries within the sterling area. Up to that time, the India Office had insisted on maintaining a rigid control of all sales through their London brokers and the desirability of transferring control to India was a matter which Taylor had often agitated and urged in the past. He, therefore, once more made efforts to bring control to where it logically belonged, especially in war-time conditions. He pointed out to the authorities in London that the dilatory methods by which Indian Government silver was then being retailed gave the speculator a very good opportunity for squeezing the market, particularly when the settlement date approached and they had reason to anticipate that the London replies might come in too late to affect it; also that the system prevented the use of standard silver, which was acceptable to upcountry buyers and stocks of which could be obtained merely by melting down standard silver rupees returning from circulation. His protests and advice went unheeded and the India Office went on selling silver from London until they got into difficulties over deliveries—when they abruptly agreed to transfer the business to the Reserve Bank of India like a hot potato. The Government of India had supported Taylor and pressed very strongly for the transfer. As Taylor has recorded, "The India Office very nearly landed us in the soup. Luckily they abdicated in the nick of time."

9. That the problem of how to utilise the sterling that

would accumulate to the credit of India as a result of payments made by His Majesty's Government for war supplies and expenditure for which India had not assumed liability emerged soon after the beginning of the war is not surprising. The most obvious solution appeared to lie in the idea that when reserves of exchange had accumulated sufficiently to meet any possible deficits in the balance of payments, the surplus could be used advantageously for the repatriation of India's sterling debt against the sale of rupee counterparts in India. The idea was not entirely new and was first mooted in 1937. The dimensions of the whole problem were, however, so small then that the Government of India were sceptical of being able to redeem even £5 million worth of sterling debt! The Reserve Bank pressed for initiating repatriation almost from the beginning of 1940 and was gratified to find that the idea was well received both in London and in India, except in certain quarters such as the inflationists or those who thought that it only helped the London gilt-edged market. Out of this angle came the suggestion that India's real interests would be served best by turning all surplus external assets into gold. This latter view appealed to some of the Directors of the Board and they explored informally the feasibility of doing so. For the time being, they recognised the force of some of the arguments against such a course, viz., that India had large external liabilities in sterling which obviously called for large sterling reserves; that even repatriation financed by the issue of rupee counterparts would broaden the Indian money market and make its control more effective, in addition to countering incipient inflation.

The prospect of Japan entering the war against them made His Majesty's Government reluctant to go through with repatriation for fear of prices slumping and holders losing as a result of vesting orders based on the market prices. The Government of India, however, felt strongly that, although they did not wish to underestimate the importance of this new factor, the scheme should be carried through as arranged and that the operations should not wait on events. Their views prevailed and repatriation was carried through, with the co-operation of His Majesty's Government in all its stages, the particulars of which are available in the official

records. That transactions resulting in the repatriation of debts amounting to about Rs. 400 crores should have been put through so smoothly and without the slightest breach of secrecy was an achievement of which all concerned may well feel proud. The main operation of repatriation was, on the initiative of the Reserve Bank, followed by arrangements with His Majesty's Government for the redemption of Railway Debenture Stock and also for the funding of the sterling Railway Annuities. In terms of an agreement reached between the two Governments, the British Government agreed to provide the Government of India with annual sums required for the repayment of railway Annuities until their redemption in return for an immediate lump sum payment of a little over £30 million by the Government of India. By the time all the various schemes had been put through, India's sterling liabilities had been reduced to the extent of Rs. 434 crores.

10. Sterling accumulations continued, however, and by the middle of 1942 they became a cause for anxiety to His Majesty's Government on the one hand and to the Reserve Bank Board on the other. The former started exploring the possibility of persuading India to assume a larger liability for war expenditure. On the other hand, Indian opinion, while reluctant to take any action that would discourage supplies to Britain for war purposes on payment, wondered if some of the resulting sterling could not be converted into gold. In July 1940, the Board, therefore, returned to the charge and a senior Director suggested that the Reserve Bank should purchase gold, at least in the Banking Department where its valuation was not subject to any statutory provision. The Governor pointed out that, apart from the technical difficulties, such a course would prevent the accrual to His Majesty's Government of vital dollar resources for the prosecution of the war in view of the cash-and-carry system, and that if the war was won sterling would be as good as gold and that if it was lost even gold would not be left to the country. The advantages of accumulating sterling in order to repatriate India's sterling debt were again mentioned. The Government of India were acquainted with the Board's point of view and by the time the matter came up again before the Board in the beginning of August the Governor had been authorised by the Government of India to convey to the

Board a request from His Majesty's Government and the Governor of the Bank of England to refrain from acquiring gold at that juncture, as it would interfere with acquisition of dollars for the common war purpose. The request was, however, accompanied by an assurance from the Government of India that gold held by the Reserve Bank in the Issue Department was not to be touched by executive action. The Board thereupon resolved to defer consideration of the question of acquiring gold with the Bank's surplus resources, but expressed the hope that the dollar requirements of India would receive special consideration as India's balances abroad had been invested in sterling. Taylor suspected that the suggestion had been put forward in order to forestall any attempt to whisk away existing stocks of the Bank's gold by some Ordinance. As it happened, in this the Directors were shrewder than they knew. For, a few months later, the Secretary of State for India did sound the Government of India about utilising the Reserve Bank's gold in order to assist Great Britain. The Government of India opposed the proposal and His Majesty's Government abstained from pressing it. In opposing it, Government, no doubt, bore in mind the assurance which the Board had a few months before, wrung from them about not touching existing gold holdings by executive action.

11. Taylor himself was genuinely optimistic about the possibility of eventual repayment to India in goods in liquidation of the sterling balances. He anticipated that, after the end of the war, possibly with American assistance, there would be sufficient productive capacity in England to permit of the using up of India's sterling assets for the development of her industries, for the improvement of her railways and for the undertaking of new irrigation schemes. The Treasury, however, did not feel easy in their minds and continually pressed for a revision of the war expenditure settlement, for which purpose the then Finance Member, Sir Jeremy Raisman, left for London in August 1942. It is easy to imagine to what pressure he must have been subjected, and it will stand to his eternal credit that in the legitimate interests of India he resisted the pressure and came back with a settlement which, everything considered, was not even then regarded as unfair to India. In thus standing firm, he received valuable sup-

port from Taylor, especially in meeting the somewhat cynical argument that since India had already suffered the pangs of parting with the goods she had supplied, she might as well make a gift of them and not insist on payment even on credit. It was Taylor who supplied the argument for resisting this view, viz., that India had already undertaken as much war expenditure as her economic capacity permitted and that if additional resources were to be made available by her they could only be regarded as a loan to be honourably repaid after the war, according to Britain's convenience and India's post-war needs. Hardly had the war finance agreement been signed when a desire to resile seized His Majesty's Government. When the manifest unwisdom of any such course of action was pointed out to them by the Government of India, whose already existing difficulties in the way of securing India's co-operation in the war-effort were serious enough owing to the political situation, they threw out a suggestion that, while it would be impolitic to revise the financial agreement, it should provide a right to revise it after the war, or even before if suitable opportunity occurred, presumably unilaterally. This also was opposed both by Raisman and Taylor, the latter pointing out that were any such attempt to be made it might possibly result in the resignation of not only the Indian Members of the Viceroy's Executive Council but also the Central Board of the Reserve Bank. Taylor himself had been assuring the Board of the Reserve Bank that their sterling would be all right, and any such tampering with an agreement the ink on which had hardly dried would have put him in an impossible position.

12. The Board of the Bank continued to show vigilant concern over the accumulation of sterling balances and the connected problem of inflation in the country. Early in February 1943, they took formal action by drawing the attention of the Government to the seriousness of the situation and passed the following resolution at a meeting held in New Delhi on the 10th of February, 1943:

The Central Board of the Reserve Bank are concerned at the rapidly growing volume of the Bank's external assets exclusively in the form of sterling (apart from the small holding of gold), the bulk of which represents a curtailment in current consumption by the country in the interests of the common war effort, notwithstanding India's backward industrial development and its low standard of living, and with a view to safeguarding the value of these assets and arranging for their utilisa-

tion after the war to India's best advantage, the Board would recommend to Government—

- (i) That they draw up in consultation with business and commercial opinion in the country a considered programme of development and reconstruction for India for the post-war period and frame in connection therewith as approximate an estimate as is possible of her requirements of capital and other goods and the sources from which they can be most speedily and suitably secured, and
- (ii) That they concert with His Majesty's Government equitable safeguards for ensuring that these assets, or their equivalent in foreign currency, will be available to India on a basis which will not involve a loss to India in the value of the accumulated sterling.

At this juncture, the Government of India did not appear to have realised the gravity of the situation regarding inflation as vividly as the Board, and in regard to the specific recommendations of the Board relating to sterling accumulations they took no action, relying on the remote and faint possibility that as a result of the establishment of some international machinery for stabilising post-war currencies and extending multilateral trade, sterling would be safe enough. In fairness to them it must be admitted that for immediate application there was no practical remedy available and that a scheme for some kind of international monetary machinery devised by Keynes had just been brought out for public consideration.

13. On the 17th of February, 1943, Taylor's invaluable career as the Governor of the Reserve Bank was brought to an untimely end by his sudden death as a result of coronary thrombosis. The Government of India were understandably unnerved; the Central Board of the Reserve Bank, while grieved at Taylor's passing away, considered it their duty to ensure that his successor should be an Indian, and that that Indian should be, in the natural course of things, myself, in view of the training I had received under Taylor for about four years, and in view of the fact that I had held the post of Deputy Governor for about sixteen months.

14. I should like to give at this stage an account of how I came to be a Central Banker—a metamorphosis rich and strange for an administrative officer in any country except pre-Independence India. In April 1936, the late Sir Sikandar Hyat Khan, then one of the Deputy Governors of the Reserve Bank, said after a visit to Lahore that it was

possible he would have to go back to the Punjab; as a result of this the problem arose of looking around for a successor. Taylor wrote to Gordon, then Chief Secretary of the Central Provinces and Berar Government to say that they were looking round for an Indian who might in due course be found suitable for promotion to one of the two Deputy Governorships—a man of good general financial knowledge and experience—and from this point of view Government Finance was nearly as useful as banking or commercial experience—but primarily of energy and administrative capacity and presence. He requested Gordon to let him know if he thought that Deshmukh would be likely to suit them and whether, if approached, the Province would be likely to spare him. Since I did not then know Taylor, I can only presume that someone had suggested my name to Taylor. Gordon replied that he considered Deshmukh suitable for the purpose in every way, but he did not think that there was the slightest chance of the Provincial Government allowing him to go "at present," because the Government had just had him trained for dealing with the ways and means and other finance problems that would arise under the new Constitution and needed Deshmukh themselves. The enquiry was renewed in the middle of 1938, but Taylor was told that Deshmukh was not available. In the meanwhile, Mr. (now Sir) Manilal Nanavati had been appointed Deputy Governor. The choice was a happy one and owed its impulse to the wisdom of the senior elective Director on the Central Board. For the time being, this solved the problem of securing an Indian Deputy Governor; but the authorities felt that the interests of the Empire demanded also a European Deputy, to take the place of Taylor who had been appointed Governor, a European Deputy who should primarily be a banker and who would have more or less to be chosen by the Bank of England, so that the Reserve Bank retained the goodwill and confidence of the Bank of England. Taylor did not like the idea of importing someone from England and gently but persistently resisted the idea till it had lost its momentum. It was not, however, dropped, and towards the end of 1938 India Office raised the question of management of the Bank should Taylor fall ill or take leave. The reaction from India was evasive, adducing the difficulty of finding the right type

of European to import. As a short-term solution it was thought best to maintain a liaison officer to keep the Government of India closely in touch with developments by being Government's representative on the Board and also attending committee meetings. Against the contingency of Taylor becoming suddenly and permanently incapacitated, the Government of India thought a senior officer of the Imperial Bank would be most suitable. It would seem that by early 1939 Taylor had suggested Deshmukh for a liaison officer. This suggestion at first found no favour with the then Finance Member, who thought that (1) the Board might not be prepared to recommend him in due course for Deputy Governor as they were predominantly businessmen and he a Mahratta, and (2) even if they did there was the danger that they would later want to make him Governor, and as there was no European Deputy Governor the Bank would be completely Indianised. In spite of these Cassandra-like utterances, Raisman, who succeeded Grigg, and Taylor went on with their efforts to secure Deshmukh's services for the Bank. Taylor at the time thought that to succeed himself, a Governor would have to be imported from England. Early in January 1939 the Bank of England again returned to the charge, pressing that someone with proved and extensive banking experience should occupy one of the leading positions of the Reserve Bank of India. While acquiescing in this, the Government of India hoped that anybody who was being brought out should be sufficiently outstanding to have a good chance of establishing the desired position vis-a-vis the new Indian Deputy Governor for whom plans were to be laid simultaneously. (That is, when ultimately a brand new Governor was imported from England he could supersede both the Indian and the European Deputy Governors and no bones would be broken.) After a great deal of palaver, the Bank of England suggested the name of a comparatively young exchange banker. Meanwhile, Nanavati's health caused anxiety and it was decided to bring Deshmukh as liaison officer forthwith. Deshmukh agreed to come and was appointed liaison officer in July 1939. Taylor's view at the time was that the Indian to be chosen as a Deputy Governor must have sufficient ability and experience to be likely to develop into an efficient Governor at least for acting va-

cancies, and that simultaneously efforts should be made to get a London banker as his colleague; but that Government should bear in mind the probability that when the actual appointment of Governor came to be made, it would probably be necessary to bring somebody out fresh, unless conditions were such that it was thought that the Indian could safely be entrusted with the post. Taylor also thought the officer suggested by the Bank of England too young for the post.

This, however, was not the end of the European-from-Home idea. It was revived by the India Office when Deshmukh was appointed Deputy Governor towards the end of 1941, but was again discouraged by Taylor, as not being in the best interests of the selected European officer himself, apart from being unfair to the European officers already in the permanent service of the Bank. He also doubted if a second Deputy was really necessary as long as there was an Indian Deputy. The India Office were glad to know that Deshmukh had fulfilled expectations and agreed to his appointment as Deputy Governor in succession to Nanavati. By this time, indeed, they appear to have modified their original conception of the need of a European Deputy in a liberal sense, viz., that he was needed not with any idea of barring Deshmukh's way to Governorship, but to give the necessary professional support to Deshmukh were he to be appointed Governor. They did not, however, press their point of view.

15. It was necessary to give this somewhat lengthy background in order to facilitate the proper understanding of the struggle that took place over my appointment as Governor. With the resignation of the Congress Ministers in the Provinces and the absence of the Congress Party from the Legislatures, the Central Board of the Reserve Bank remained the only elected or representative custodians and trustees of India's economic and monetary interests and the determination with which they successfully recommended the appointment of an Indian to the post of Governor, undoubtedly a key post in the Indian monetary field, when World War II was being fought with desperate concentration of men, money and resources, has never received adequate recognition.

They owe their success to the rare sense of fair play and statesmanship that the Secretary of State appears to have displayed. The Government of India were more royalists than

the King himself and at first opposed unqualifiedly any suggestion to appoint Deshmukh as Governor, although he had been introduced to the Bank with their concurrence. It is possible that responsible as they were for running the war, with no popular support, they shrank from taking a risk. They sponsored the appointment, instead, of the then Managing Director of the Imperial Bank of India, and, when they found this likely to be unacceptable to the Board, sought to make terms with them by pledging themselves in advance to appoint Deshmukh as Governor after three years, during which period the banker they had selected was to be the Governor. They also attempted to induce Deshmukh to stand down in the public interest, which, in all humility, Deshmukh declined to do as it would have amounted to spiking the guns of the Central Board. The Board rejected the compromise resolution and recommended Deshmukh.

The Government of India were, as stated above, overruled by the Secretary of State and Deshmukh was appointed Governor in the middle of August 1943. So once again went a-gley the schemes of mice and M. N. although it was one of the inscrutable turns of Destiny that the Indianisation of the Governorship of the Reserve Bank should have been advanced by a few years by the premature death of Taylor, himself a champion of Indianisation. I have little doubt that he himself deliberately worked towards making me fit to carry the responsibility in succession to himself. He taught me all he knew of Central Banking and the currency and exchange and bullion problems of the country, withheld no confidences and pressed on purposefully with my training. I well remember a day in 1942 when he walked into my room after he had almost submerged me with work and said: "I often feel a great compunction, Deshmukh, in flinging all this work at you, especially as I could polish it off in half the time you take, with my fifteen years of experience in this field. But one day you will have to do it yourself and you will learn much quicker by doing it yourself now than by watching me do it."

16. It was Sir Jeremy Raisman who was the first in the Finance Department of the Government of India to bow with grace to the inevitable and, from the outset, he seems to have determined to ensure that nothing interfered with the close confidence and mutual co-operation that must exist be-

tween the Finance Member and the Governor of the Reserve Bank. The Finance Secretary and the Economic Adviser, no doubt, realising the loss they had sustained by the sudden removal by death of the prop in the person of Taylor that they were wont to rely on, were a little less forthcoming and more censorious. For the first few weeks, Finance Department went to the length of suggesting in almost every important case that, in addition to furnishing my own views, I also ascertained the opinion of the Managing Director of the Imperial Bank. They abandoned this practice, however, when they found that in no case was the second opinion different from mine. It is notoriously dangerous to change horses in mid-stream, and the anxiety of the Finance Department to ensure that the new mount would not sink with them in the stream was understandable. I have reason to believe that, in course of time, their diffidence disappeared and their confidence strengthened, and if only in proof of the then Finance Secretary's bona fides I should like to refer to a recent private letter of his in which he has expressed concern over the impending termination of my tenure as Governor of the Reserve Bank.

17. The understanding and friendship between Sir Jeremy Raisman and myself matured as a result of our both being members—he as the Leader—of the Indian Delegation that went to Bretton Woods in connection with the formulation of proposals for the International Monetary Fund and the International Bank for Reconstruction and Development, in July 1944. He handled India's case with sympathy and loyalty, and only wavered for one brief instant. That was in connection with the fixing of the quota for India. He announced to the rest of the Delegation one morning that there was a danger of India's quota being fixed too low so as to imperil the chance of representation on the governing bodies of the Fund and the Bank even by an elected Executive Director of her own. I said that, in that case, the Indian Delegation must withdraw, and was wholeheartedly supported by Chetty and Shroff. He lost his poise for a moment and thought that this was another manifestation of the unfortunate Indian tendency to non-co-operate. Half an hour afterwards, he came to me and said that he had thought over the matter and was convinced that withdrawal was the only

honourable course to take should there be no improvement in the proposed quota for India. As a result of his resolute attitude, supported, I am happy to record, by the United Kingdom Delegation, India ultimately succeeded in securing her present quota which, as events have transpired, secured her a place among the big five.

18. At this stage, I should like to make a few stray observations in regard to the International Monetary Fund and the International Bank for Reconstruction and Development. While I met John Maynard Keynes for the first time at Bretton Woods, I had no great opportunity of getting to know him well, as Sir Jeremy Raisman was the Leader of the Indian Delegation. That opportunity came my way in March 1946 when I led the Indian Delegation at Savannah where the Fund and the Bank were inaugurated. I was accompanied then by the Reserve Bank's Economic Adviser, J. V. Joshi, whom Keynes regarded as one of his most brilliant students at Cambridge. Savannah furnished, therefore, many opportunities of developing acquaintance, and in the matter of interpreting India's rights to representation on the Board of Directors Keynes rendered valuable guidance and assistance. I was told that in his reports to his own Government on proceedings at Savannah Keynes went out of his way to commend the work of the Indian Delegation. An echo of the compliment was sounded in a tribute which Sir Archibald Rowlands, as Finance Member of the Government of India, paid to the work of the Indian Delegation at Savannah in the Indian Legislature later in the year. I mention these matters because I believe it was confidence in the worth of the Indian Delegation's work and appreciation of its Report that finally induced the Indian Legislature to give its consent to India becoming a member of the World Bank and Fund. They had considerable hesitation in regard to the Bank, in particular, as there is always the risk which every member-country carries of having to bear its share of the loss that might result from any unwise loan by the Bank. I am happy to be able to say that evidence of the handling of its affairs by the Bank that is available to date is such as to induce confidence that such a risk is very remote. I should also like to take this opportunity of recording my satisfaction which, I feel sure, is shared by Government, of the ex-

cellent work done in these two bodies by India's representatives, that is to say, Mr. J. V. Joshi as Executive Director on the Fund, and Mr. N. Sundaresan as Executive Director on the Bank, with Dr. B. K. Madan as an Alternate to both. The current year may perhaps see India availing herself of the facilities which the Fund and the Bank offer to its members, and I feel confident that this assistance will be arranged in a manner satisfactory to both parties, largely as the result of our excellent representation.

It was in connection with the consideration of proposals out of which the World Bank and Fund came into being that the Bank had the advantage of the expert advice of the distinguished Director of the Gokhale Institute, whom the Bank is proud to count as a Local Board member. His advice was also sought and helpfully given on the question of the appropriate par value of the rupee in terms of gold for communication to the International Monetary Fund. On the invitation of the Government the Board examined the matter at a meeting held in New Delhi in November 1946 to which Prof. D. R. Gadgil was specially invited. It is common knowledge that the Board advised that no change be made in the par value already communicated to the Fund, viz., 4.14514 grains of fine gold per rupee, which was based on the existing rupee-sterling rate of 1s. 6d. and the sterling-dollar rate of \$4.03.

19. Returning to the problem of sterling accumulations, the Board of the Bank continued to watch the position anxiously and, at a meeting held in Calcutta on the 11th of December, 1944, they tendered advice to Government in the form of the following resolution:

The Board is of the opinion that the expansion of currency that has been continuously taking place in India as a result of the method which has had to be adopted for the financing of allied war expenditure has approached a level beyond which it may prove disastrous to the larger interests of the country, by reason of the inflationary trends it creates. In the opinion of the Board it is imperative to check these trends forthwith. To this end the Board recommends to the Government of India that in order to enable the Reserve Bank to limit their further note liability to the barest minimum possible as well as to arrest effectively further accumulation of sterling they take the following steps:

(a) make renewed efforts to stop the export of essential manufactured articles and raw materials of which there is shortage in this country; and

(b) to request His Majesty's Government to find, as far as possible, the rupees for their disbursements in India by

- (i) the sale of gold and silver in India, and
- (ii) the facilitating of the supply of capital goods to India at fair prices.

This was followed by a further resolution passed at a meeting held at Lahore on the 25th of February, 1946, which runs as follows:

The Board of the Reserve Bank is alarmed at the continued accumulation of sterling even after the termination of the war and requests the Governor to apprise the Government of India of the considered views of this Board—

That all disbursements in future made by His Majesty's Government in rupees must be paid for either in free foreign currencies or in capital goods or in such consumer goods as are acceptable to India or in bullion.

20. While, during the course of the war, there was not much that could effectively be attempted in regard to the accumulations of sterling, there was at least one direction in which the problem could have been eased. In the beginning of 1943, Taylor had pointed out that the funding of the pensionary liabilities of the Government of India, expressed in terms of sterling, was likely to furnish a means of utilising a substantial sum. The matter was mentioned in a Board meeting but failed to receive enthusiastic support, possibly as a result of a lack of a clear understanding of its implication. The suggestion was taken up by Government and pursued to the stage of working out a provisional basis for funding the pensionary liabilities, and I took every opportunity of urging Government to carry the scheme to completion. The matter was mentioned in a Budget session by Sir Jeremy Raisman, but had again a somewhat cold reception. In the meanwhile, much valuable time had been lost and, by the time it was brought to a head, His Majesty's Government, who had at first been inclined to put the scheme through, had modified their views and begun to consider that the proposals raised fundamental problems affecting not only India's obligations, but also the sterling obligations of the United Kingdom arising from the war to other countries as well as India.

21. In my opinion, the Government of India were rather late in getting off the mark in handling the inflationary situation in India. There was a time, even towards the end of 1942, when any assertion that continuous currency expansion against sterling led to inflationary conditions in India aroused ire in the Imperial Secretariat at New Delhi. The

Government of India commenced taking effective steps only towards the beginning of the financial year 1943, and I have no doubt that they were goaded into action by the almost unanimous criticism of their miscalculation contained in the pronouncements of influential Indian economists.

22. The Reserve Bank can justly claim that the management of the money market on behalf of the Government of India was of material assistance to them in fighting inflation. Apart from being the agents of the Government of India in the management of their public debt, the Reserve Bank and, in particular, its Chief Executive, are the advisers of Government in the planning of loans and in the maintenance of the health of the money market, and the discharge of this responsibility is perhaps the most onerous part of the duties of the Governor. It was realized by the Reserve Bank that if the cheap money policy is to be pursued successfully, the steps to be taken in that direction should be small and just perceptible enough to inspire confidence in the private and institutional investor. This policy was followed steadily, after the abandonment by Taylor on the then Deputy Governor's advice—Sir Manilal Nanavati—of some idea of increasing the Bank Rate at the beginning of the war in imitation of the action taken by the Bank of England. By the beginning of 1946, the yield on non-terminable loans had been reduced from a little short of 3.75% to round 3.25%, and the yield on long-dated Government securities had been brought down from 3.15% to a little under 3%, and there was a general feeling of confidence in the money market. During this period there was only one instance in which the advice of the Reserve Bank was rejected by the Finance Department, and not with very good results. That was in connection with the issue of the interest-free Prize Bonds 1949, in January 1944. When Government consulted the Bank regarding the issue of this loan, the Bank expressed itself as opposed to the issue of any form of lottery loan, as it was felt that on ethical grounds certain principles should not be abandoned by the State, no matter how severe was the crisis calling for such abandonment. That is to say, that in no circumstances should the State appeal to the baser passions of the populace. The Bank considered that this aspect was of particular importance in a country like India

where, owing to lack of education and poverty, the least provocation was sufficient to encourage gambling. Apart from this, it was pointed out that if the State countenanced even a mild form of gambling, it would be weakening its hands for dealing severely with the various forms of speculation which it was endeavouring to check. These arguments failed to impress the Government, and Prize Bonds were issued and were on sale up to the 4th of December, 1945, when it was decided to discontinue them as it was found that the response was meagre, the total sales of the Bonds having amounted to only Rs. 5.30 crores.

23. The question of the Bank Rate was among the earliest matters considered by the Board of the Reserve Bank and, on the 27th of November, 1935, the Committee of the Central Board, after considering a statement made by the Controller of the Currency on behalf of Government, resolved to reduce the Bank Rate from $3\frac{1}{2}\%$ to 3% . In 1936, the then Governor, possibly at the instance of some of the Directors, thought of making a further reduction to $2\frac{1}{2}\%$, but preliminary discussions with Government revealed that they strongly opposed any such move, in view of the glut of money which then seemed to be in evidence in the money market. The proposal was, therefore, dropped. Incidentally, this was possibly the beginning of a rift between the Finance Member, Sir James Grigg, and the Governor, Sir Osborne Smith, which was later to widen as a result of other differences and culminate in the latter's resignation. During the course of the war, the Bank Rate remained high and dry, and there was no occasion for considering any modification of it. In the beginning of 1946, however, Government seem to have felt that a more determined effort should be made to cheapen money, particularly with a view to facilitating on advantageous terms to Government the redemption of $3\frac{1}{2}\%$ Paper. With this end in view, they suggested to the Reserve Bank that a reduction in the Rate be effected. On a very careful consideration of the relative factors, the Committee of the Central Board of the Reserve Bank resolved, however, not to make any alteration, and the Government very wisely refrained from pressing the suggestion.

24. This episode brings to the forefront the divergence

of views which existed at that time between the then Finance Member, Sir Archibald Rowlands, and the authorities of the Reserve Bank of India. The former appeared to subscribe to the view that, as a result of the end of the war, a depression was round the corner, and his Budget for 1946-47 bears the imprint of this view. The Reserve Bank Board on the other hand, were of the opinion that inflationary conditions were likely to persist for some time longer, and they were, therefore, naturally anxious to abstain from any action calculated to give an impetus to the speculation that is always attendant on inflation. As events have proved, the Board were right, and Sir Archibald Rowlands wrong in his diagnosis of the situation and, therefore, the prognosis. The redemption of 3½ % Paper on the terms on which it was redeemed was a measure which the Reserve Bank had opposed as likely to aggravate inflation. A conference followed between the Finance Member and myself in the beginning of 1946 and, in order to give the views of the Finance Member a fair chance, I suggested that before any announcement regarding redemption was made, the Government should test the situation by the floating of a dated loan for a longish term at 2¾ %. This was the genesis of the 2¾ % Loan 1960, which made a sorry debut in January 1946. I thought that this sealed the fate of the redemption and went off to Savannah to attend the International Monetary Conference. Much was my surprise when, on returning towards the end of March 1946, I discovered that the money market had been unusually buoyant as a result of premature tax concessions by the Finance Member. All loans had moved up by several points, and not only had the original amount of 2¾ % Loan 1960 been taken up, but even a re-issue had become necessary. With these signals of success, the Finance Member was not to be denied and the redemption of 3½ % Paper had, according to our bargain, to be announced, much to the eventual disturbance of money market conditions. It is only now that the money market may be said to have recovered from the unwholesome buoyancy of that period, at a cost, I am afraid, to many an investor in Government securities.

25. While the war continued it was not practicable to suggest any alteration in the arrangement under which the dollar resources of the country were passed on to the com-

mon reserve, subject to the satisfaction of the country's requirements of dollars for essential purposes. In administering the import control at our end the Commerce and Finance Departments of the Government of India were unduly squeamish, although there was no rigid regulation from India Office, and the Indian public developed a feeling of animosity towards the Empire Dollar Pool. As it began to be apparent that India's net contribution to the Pool was appreciable, the Reserve Bank felt that steps should be taken to accelerate the utilisation of our surplus, and in the beginning of 1946 proposals were submitted by the Bank to the Government of India for terminating the pooling arrangements so far as dollars were concerned, any surplus which India could not for the moment utilise being lent to His Majesty's Government on a short-term basis. This proposal was, however, kept in cold storage by the Government of India, with the result that we have had to obtain as a release from sterling balances what in reality is still our own accumulated credit surplus. That a certain amount of self-restraint is called for on our part in order to ensure the safety of the basket in which we have put all our eggs is undeniable. But we also need sustenance and have far smaller scope for tightening the belt. At one stage during 1945 I was asked by a representative of the Finance Department what I thought of a proposal to give India one dollar for every two pounds sterling acquired, in order to help keep sterling from depreciating. I said that reminded me of the Irish legend in which it is written that the snakes committed suicide to save themselves from slaughter! The proposal was not pursued.

26. Gold and silver run like twin threads through India's economic destiny, and operations in these metals have occupied quite a substantial part of the time and attention of the Executive of the Reserve Bank. The transfer of the official selling of silver from India Office to the Reserve Bank has already been mentioned. While sales of silver in the early years of the war were necessary and justifiable, the Reserve Bank had always doubted the wisdom of, and demurred to the selling of American lease-lend silver for anti-inflationary purposes. Government at first took a contrary view, but, as the ploughing-the-sands character of the operation became apparent, the sales were stopped—and no

great harm had been done. The sales of gold on behalf of His Majesty's Government had their origin in their readiness to help in countering inflationary pressures in India and were discontinued only when the importance of conserving available gold and dollar resources against a mounting sterling liability appeared urgent to the British authorities. Sales of gold on behalf of the U. S. A. were undertaken later and were continued longer than sales on His Majesty's Government's Account. India acquired in all about 7½ million ounces in this manner at an average cost of about Rs. 70 per tola, which, with gold at round Rs. 110 a tola today, does not appear to be such a bad bargain after all.

27. Perhaps in no other sphere of its activity has there been such an enlargement of the Bank's functions and responsibilities as in exchange control. It would be wearisome to recapitulate here the various stages of expansion which the work of this department has undergone. It is worthwhile mentioning here, however, that thanks to the type of organization evolved, there has been effective co-operation and mutual understanding of problems between the British and Indian Controls. An important domestic result of this has been the possibility of placing facilities at the disposal of Indian banks anxious to develop their exchange business. In the beginning licences to deal in foreign exchange were issued only to scheduled banks who had been dealing in foreign exchange in the past; but with the development or emergence of Indian banks, licensing was extended so as to include all banks of good standing with adequate resources, competent technical staff and a prospect of attracting exchange business. As many as thirty Indian banks are now so licensed, out of which seventeen are authorised to deal in all currencies and thirteen in sterling area currencies only. In pursuing this policy the Bank had to counter a certain amount of opposition from the vested interests which came to the surface in one case. Wires were pulled through the customary channels and the Finance Department, which had until then been content to leave things wholly to the discretion of the Reserve Bank, thought it fit to enquire why a licence had been issued to a new Indian bank. The reply was that it fulfilled all the conditions, with a private word by me in the ear of the Finance Member that India was the only country in which

Government could bring itself to question why a trading privilege had been granted to a national. That word proved to be the last word on the subject.

28. The Bank was called upon to assist Government in their administration of the Defence of India Rule 94(a) regarding control of capital issues in so far as it related to banking and insurance companies and investment trusts. The chief object of the rule which was promulgated in May 1943 was to prevent the growth of mushroom companies which stood little chance of survival in the post-war period and other undesirable practices such as over-capitalisation of concerns on the basis of abnormal war-time profits to the detriment of the investing public. Another important consideration was the diversion of available capital from unsound and speculative enterprises to investments in Defence Loans so as to mobilise the financial resources of the country for the prosecution of the war on the one hand, and to combat inflation on the other. In conveying its confidential opinion to Government the Reserve Bank took into account, among other things, the financial standing of the proposed Directors and the prospects of successful working in the case of new companies and the financial position, management and the methods of operation in the case of existing companies. Although the Defence of India Rules have now lapsed, the control of capital issues is still being continued with certain relaxations under the Capital Issues (Continuance of Control) Act 1947. The number of applications dealt with by the Bank since the institution of control in 1943 is as follows:

Banking Companies	1,050
Insurance Companies	290
Investment Trusts	60

The Bank continues to give advice on applications for capital issues by banking companies, but with regard to insurance companies, the Bank has requested Government to relieve it of this responsibility in view of the change in the Government's policy of dealing with applications on other than strictly technical considerations, and a consideration of factors which are outside the scope of the Bank. The applications of insurance companies are now dealt with direct by Government.

29. The difficulty of the task of the Reserve Bank of

India in dealing with the banking system of the country does not lie in the multiplicity of the banking units alone. It is aggravated by its diversity and range. The Imperial Bank, the Exchange Banks, the bigger Indian banks and the smaller scheduled banks, not to mention the hundreds of non-scheduled banks, pose their own problems of relationship and there can be no common standard of treatment in practice, although in theory the same law governs all. With the Imperial Bank the relations of the Reserve Bank have always been special for historical reasons, as well as those arising out of the agency agreement. While the bigger Indian banks have always responded readily to advice and guidance and have at all times been eager to co-operate, some of the newer or smaller ones have pursued policies that did not accord with the best traditions of commercial banking and a few have, regrettably, actively abetted tax evasion. In such a milieu the avowed censoriousness of the Reserve Bank has been misunderstood as arising out of a lack of sympathy, whereas its impulse lies in reality in the anxiety of the Reserve Bank to improve the tone, management and solidarity of Indian banks. There is, perhaps, a growing perception of the truth in Indian banking circles, and the emergence and development of the Indian Banks Association, Bombay, which was unofficially encouraged by the Reserve Bank, ought to reinforce this tendency. The Exchange Banks were inclined to show signs of the hauteur of a highly privileged class in the early years of the Reserve Bank, but unlike Canute, they have recognised the force of the onrushing tide of nationalism and have for many years, and particularly during my tenure of office, been friendly and co-operative. This attitude was appreciably strengthened in the early years of the war by the sympathetic assistance which the Reserve Bank was able to render in the matter of the calling of their European staff for military service.

30. As there has been a certain amount of criticism regarding the Reserve Bank's role as a Central Bank when the Travancore National and Quilon Bank suspended payment in 1938, it may be pertinent to make a reference to the action taken by the Bank in regard to that bank. Although from the time of the amalgamation of the two banks (Travancore National Bank Ltd., and the Quilon Bank Ltd.)

the Reserve Bank was uneasy, it gave them a larger line of credit to cover the actual period of change over as we felt that an amalgamation, if soundly conducted, might be of material assistance in improving the position. Thereafter, the Reserve Bank made it quite clear that no further assistance could be sought from it until they had given full information as to the actual position of the amalgamated institution. They refused to give the Bank the necessary facilities to enable it to make a full inspection of their books. Under the circumstances, the Bank did not consider that it would be justified in giving what would have amounted to an unconditional assistance. In the light of the repayment made to the depositors by the liquidators it has been argued in some quarters that the intrinsic position of the bank was sound and that the failure could have been avoided had the Reserve Bank given timely assistance to the bank. The Board could be expected to take into account only the existing conditions and the information available to them. Although the depositors were paid 12 to 14 annas in a rupee, it may be mentioned that this was possible only by calling in from the shareholders their liability in respect of the unpaid amount of the shares; and another fortuitous circumstance was that, as a result of war, the liquidators were able to realise much larger prices for the estates and lands on which advances had been made by the bank.

31. Section 54 of the Reserve Bank of India Act, under which the Agricultural Credit Department was created in April 1935, was an almost last minute inspiration. During the last thirteen years the organization and scope of activities of the Department have expanded and proliferated to an extent not realized by either the Governments in India or the public concerned with its operations. The foundations of the Department were laid under the experienced and solicitous eye of Sir Manilal Nanavati, Deputy Governor from 1936-41, who brought to bear on the task all his rich administrative experience and his constructive talents. As in administration so in matters of co-operation; almost everyone somehow feels that he has nothing much to learn. Moreover, the technical experts in co-operation available to Governments in India, whose experience lies particularly in the executive field, are apt to be impatient of the advice or guidance of a cen-

tral advisory organization. To these reasons must be ascribed the failure of many Provincial Governments to take advantage of the rich store of expert knowledge of co-operation acquired by the Agricultural Credit Department of the Reserve Bank of India, a knowledge which it is only too anxious to share with anyone interested. Even from the relative departments of the Central Government, appreciation has often been tardy or grudging. It has been left to special committees with whom the Department has been closely associated, such as the Committees on Co-operation and Agricultural Credit set up in recent years for the post-war planning of the co-operative movement, to acknowledge the extent of the assistance rendered by the Department. The original Department has now been split up into three, the other two being the Department of Banking Operations and the Department of Research and Statistics. The Agricultural Credit Department, as now constituted, is in close touch with the Division of Rural Economics, which is now a part of the Department of Research and Statistics. This latter department has two divisions, one for Monetary Research and the other for Statistical Research. It was first started as a small statistical section consisting of one Superintendent and three Assistants, and its principal function was the compilation of the Annual Report on Currency and Finance, which the Bank took over from the Government of India in 1937. It was on Sir Manilal Nanavati's initiative that in 1941 a Director of Research was appointed, but it was not till 1945, with the assistance of the Economic Adviser to the Reserve Bank, a post created in 1944, that the Department developed into its present size, consisting of 16 officers, 11 superintendents and 53 clerical staff. A system has been instituted under which senior officers of the Department are deputed to America, Canada and the United Kingdom, to acquaint themselves with the latest methods and technique adopted in foreign countries in the compilation of international accounts. The Reserve Bank has also kept itself in close touch with developments in foreign countries by deputing officers to international conferences. For instance, the Director of Statistics and the Director of Monetary Research attended the Balance of Payments Conference held at Washington in September 1947, while the former also attended the World Statistical Con-

ference held about the same time. The Director of Rural Economics attended the 6th International Conference of Agricultural Economists, and the 10th Conference of the Institute of Pacific Relations, held in England in 1947. As already mentioned, the Economic Adviser of the Bank, Mr. J. V. Joshi, is Executive Director for India on the International Monetary Fund, and Dr. B. K. Madan, the Director of Monetary Research of the Bank, is an Alternate Director on both the Fund and the Bank. It is not possible within the compass of this lecture to review the functions and activities of the new Department of Banking Operations. Its Chief Officer has also had the advantage of a sojourn in the U. S. A. and the U. K. for the study of their banking institutions, and the Department now handles an immense amount of work connected with the Banking Legislation, the inspection of banks and the maintenance of day-to-day relations with the banking system of the country. The Bank has thus a fully equipped machinery for dealing with all problems of the regulation of commercial and agricultural credit, and research in the field of economics and statistics and the collection of relevant facts and considerations for the formulation of the Bank's policies in these matters.

32. This completes the retrospect. A word about the prospect, and I shall have done.

Government have recently announced their intention to nationalise the Reserve Bank. Although the Board of the Bank sincerely believe that this decision is premature and not logically necessary in view of the stage of economic development reached by the country, they will, in the event of the decision proving to be irrevocable, co-operate with Government in evolving a scheme of nationalisation that is calculated to ensure with a reasonable prospect of success the same degree of advice and assistance to Government that the present type of constitution offers. After all, it is not the theoretical constitution of the Institution that matters, but the spirit in which the partnership between the Ministry of Finance and the Bank is worked. The success of the partnership will, in the ultimate analysis, depend on the manner in which Government desires to be served and provides opportunities accordingly. No country can have better public institutions than it deserves.

Will Be Shortly Out

Publication No. 17:

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By D. R. GADGIL

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