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AN APPRAISAL OF THE STATE BANK OF INDIA

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I. THE PROBLEM

With the inauguration of a planned economy in India in 1951, there has been a great deal of thought about what direction the financial institutions should take to meet the requirements of a developing economy. This change in framework calls for significant changes in the structure, organization, priorities, policies, and operating concepts of financial institutions. Nationalization of commercial banks, a major component of the Indian institutional credit system, has been one of the methods pursued by the Government of India to effect these changes. It was in this context that the Imperial Bank of India was nationalized on July 1, 1955 and renamed the State Bank of India. Subsequently, the State Bank of India took within its fold banks which were associated with the former princely states.

While recommending the creation of the State Bank of India through the nationalization of the Imperial Bank of India and amalgamation of the State-associated Banks, the Committee of Direction of the All India Rural Credit Survey (AIRCS) of 1954 set the following policy goals for the State Bank [34]:

(1) to create a widespread branch banking system over the entire country;

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(2) to stimulate and support the development of cooperative institutions; and

(3) to follow a lending policy which, while not deviating from the canons of sound business, will be in consonance with national policies as expressed through the Central Government and the Reserve Bank of India.

The State Bank of India has completed nearly seventeen years of its operation. This is a sufficient period to evaluate its intervening performance. Although difficulties associated with evaluating the performance of financial institutions are widely appreciated [14, 16, 28, 29, 30, 35, 36, 38], performance appraisal results are essential for any economic enterprise. This appraisal could be used to measure the present efficiency of its performance, indicate the necessity for further improvements, and provide an index of its future potential. The objective of this paper is to evaluate the performance of the State Bank of India:

(1) in mobilizing deposits, and supply of loanable funds;

(2) in extending banking facilities in general and to semi-urban and rural areas in particular;

(3) in supporting the development of cooperative institutions;

(4) in distributing credit in accordance with the following national policy goals (a) assisting small industry; (b) assisting agricultural development; (c) aiding export industries; and (d) aiding small business; and

(5) finally, by its operating efficiency.

These objectives, in a specific way, interpret the policy recommendations of the AIRCS Committee.

In some sense, this appraisal of the State Bank will provide a measure of the success of nationalizing a bank. Thus, comparisons between the performance of the State Bank and the private banking sector will be made whenever data availability permits.[1/]

II. THE STATE BANK, ITS RELATIVE SIZE AND CREDIT OPERATIONS

One way to assess the importance of the State Bank is to compare the number of bank offices, total deposits and total advances against the entire commercial banking system. Table 1 summarizes these comparisons as of June 1971.[2/] As is indicated, the State Bank is the single largest bank in the Indian commercial banking system comprising somewhat less than one third of the offices, deposits and advances of the total system. In addition, it has a slightly larger than average loan-to-deposit ratio which accounts for the fact that although deposits per bank office are smaller than average, loans per bank office is the same as the system.

Although the relative size of the State Bank in 1971 is a measure of its current importance, the trend from 1955 to 1971 will provide an indication of whether its relative importance has changed since nationalization.

[1/] Data for this study were obtained from the following published records:
(1) Records and Statistics, Quarterly Bulletin of the Eastern Economist, New Delhi.
(2) Reserve Bank of India Bulletin (RBIB), a monthly bulletin of the Reserve Bank of India, Bombay.
(3) State Bank of India Monthly Review (SBIMR), a monthly review of the State Bank of India, Bombay.
(4) Report of the Central Board of Directors, annual report published by the State Bank of India.

[2/] Until July 9, 1969, all commercial banks except the State Bank were operated by the private sector. With the nationalization of fourteen major commercial banks on that data, the private banking system became insignificant. However, since the identity of each of the nationalized banks is maintained the performance of the State Bank will be compared with the rest of the banking system even after 1969.

Table 1: Number of Offices, Total Deposits and Total Loans of All Commercial Banks and State Bank of India as of June 1971*
(Amounts in Crores of Rupees**)

	All Commercial Banks	State Bank of India	(2)/(1) x 100
	(1)	(2)	(3)
Number of Offices	11,892	3,538	29.8
Total Deposits	6,190	1,711	27.6
Total Loans	4,776	1,432	30.0
Deposits per Office	.52	.48	--
Loans per Office	.40	.40	--

*Source: See footnote #1.

**One Crores of Rupees equals $10 million.

Table 2 presents a comparison of bank offices, deposits, loans and loan-to-deposit ratios over that period. We will view each of these trends individually. The trends in total deposits leads to the following conclusions:

(1) Although the State Bank increased its relative size in terms of total deposits from 23.2 percent to 27.3 percent in 1965, this trend did not continue from 1965 to 1971;

(2) Further, of the total increase in deposits, the State Bank accounted for 29.2 percent between 1955-65, 28.8 percent between 1966-71 and 28.4 percent between 1955-71. Thus the State Bank did not significantly alter its relative importance as a deposit mobilizer over the period studied.

Based on its ability as a deposit mobilizer, the change in the structure of the State Bank did not alter its performance. However, it must be realized that the State Bank, as an instrument of national policy, was called upon to open new branches in rural and semi-rural communities where relative deposit

Table 2: Bank Offices, Total Deposit, Total Loans and Loan-To-Deposit Ratios for all Indian Commercial Banks, State Bank of India and Other Commercial Banks, 1955 and 1965-71.*

	1955	1965	1965-55Ψ	1966	1967	1968	1969	1970	1971	1971-66Ψ	1971-55Ψ
Total Bank Offices	2807	5904	3097	6139	6620	7044	8045	9938	11892	5753	9085
State Bank of India	477	1934	1457	2007	2157	2309	2475	2952	3538	1531	3061
Percent of Total	17.0	32.8	47.0	32.7	32.6	32.8	30.8	29.7	29.8	26.6	33.7
Other Commercial Banks**	2330	3970	1640	4132	4463	4735	5570	6986	8345	4222	6024
Percent of Total	83.0	67.2	53.0	67.3	67.4	67.2	69.2	70.3	70.2	73.4	66.3
Total Deposits (Amount in Crores of Rupees)	909	2886	1977	3347	3763	4205	4842	5675	6190	2843	5281
State Bank of India	211	788	577	893	1000	1163	1325	1557	1711	818	1500
Percent of Total	23.2	27.3	29.2	26.7	26.6	27.7	27.4	27.4	27.6	28.8	28.4
Other Commercial Banks**	698	2098	1400	2454	2763	3042	3517	4118	4479	2025	3781
Percent of Total	76.8	72.7	70.8	73.3	73.4	72.3	72.6	72.6	72.4	71.2	71.6
Total Loans (Amount in Crores of Rupees)	498	2101	1603	2413	2725	3058	3585	4428	4776	2363	4278
State Bank of India	116	575	459	643	740	916	1057	1361	1432	789	1316
Percent of Total	23.3	27.4	28.6	26.6	27.2	30.0	29.5	30.7	30.0	33.4	30.8
Other Commercial Banks	382	1524	1144	1770	1985	2142	2528	3067	3344	1574	2962
Percent of Total	76.7	72.6	71.4	73.4	72.8	70.0	70.5	69.3	70.0	66.6	69.2
Loan-to-Deposit Ratio											
All Banks	54.7	72.7	81.0	72.0	72.4	72.7	74.0	78.0	77.1	83.1	81.0
State Bank of India	54.9	72.9	79.5	72.0	74.0	78.7	79.7	87.4	83.6	96.4	87.7
Other Commercial Banks	54.7	72.6	81.7	72.1	71.8	70.4	71.8	74.4	74.6	77.7	78.3

Source: See Footnote #1.

*June and figures on branch offices, and year end figures on deposits and loans; but year end figures on branch offices for the year 1965, and June end figures on deposits and loans for the years 1955 and 1971.

**Other commercial banks include only scheduled banks.

ΨChange between years indicated.

mobilization may not have been substantial but where long range benefits to the rural community might be considerable.[3/]

A. Innovations in Deposit Mobilization

Innovations of financial services is an important dimension of performance [40]. It is the process of institutional innovation which is a critical component of financial market development [8, 9]. A bank, as a multi-product service firm, has to innovate techniques to sell its services to new groups of depositors. Innovations in deposit mobilization are particularly important in India for two reasons. In India the ratio of bank deposits to national income was about 15 percent in 1965 compared to 92 percent in Switzerland, 70 percent in Japan, and 49 percent in U.S.A. Even compared with other developing economies, India's level was particularly low. Thus bank deposits as percentage of national income was 22 in Thailand and 19 in Ceylon and U.A.R. [10]. This is suggestive of the possibilities for the increased monetarization of the Indian economy.[4/] In addition, although higher interest rates can help induce deposit generation, it has been the experience of India that high interest rates alone will not generate a substantial increase in deposits.[5/]

Thus the success of deposit mobilization depends to a large degree on the effort involved in changing basic attitudes. The requirements of a new

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[3/] This will be discussed more fully in section VII.

[4/] Although without further analysis it is impossible to determine whether supply or demand conditions are responsible for this, the very low level is suggestive of a potential supply problem.

[5/] This points to a problem between the type of available financial assets, in this case deposits, and the type of assets in which the Indians show a willingness to hold their wealth. See [5].

class of rural depositers who were previously totally unfamiliar with banking requires major modifications in procedures and service. The State Bank has tried to meet this need by introducing new techniques of deposit mobilization such as the Special Credit Transfer System, the Savings Promotion Campaign, the Annuity Deposits Special Facilities Scheme and the Gift Scheme. Although these developments indicate a concern with the issue, success in this area is still not demonstrated.

B. Trends in Loan Behavior

Bank lending policy is a key determinant of the flow of credit to specific sectors of the economy. Thus the trends in the proportion of loans made by the State Bank is one important measure of national credit policy. Several trends are evident in loan behavior (Table 2):

(1) Total loans of all commercial banks increased 959 percent over the period, from Rs 498 Crores in 1955 to Rs 4776 Crores in 1971. At the same time, the amount accounted for by the State Bank increased from 23.3 to 30.0 percent. Thus the State Bank improved its overall loan performance over the period.

(2) This trend is even more clearly recorded in the percent of the increase of loans made over the period. The State Bank advanced 28.6 percent of the increase in loans between 1955-65 and 33 percent between 1966-71.

However, although the overall loan performance is significant, it is through the composition of loans that the impact is felt. For example, between 1968 and 1969, the proportion of loans made to small business, indistries and agriculture rose from 9.3 percent to 16.5 percent. Although this is far from indicative of a substantial commitment to "small" economic units since small units account for more than 16.5 percent of the GNP of India, the trend if it continues would certainly indicate a major shift in lending policy.

C. Trends in Loan-to-deposit Ratios

The loan-to-deposit ratio is the single most important measure of banking performance. The evidence from Table 2 is very encouraging. From 1955 to 1965, the loan-deposit ratio increased in the system from almost 55 to almost 73 percent. During this period there was no significant difference the State Bank and Other Bank category. However, between 1966 and 1971, the ratio for the State Bank continued to increase--to 83 percent by 1971--while the Other Bank category showed no acceptable trend. Thus of the total increases in deposits between 1966-1971, the State Bank utilized 96 percent for loans while the Other Bank group utilized only 79 percent.

Both the marginal and average loan-deposit ratios were exceedingly high over this period. For instance, the loan-to-deposit for all United States commercial banks in January 1972 was only 63.7 percent. And that rate itself was historically high due to the unusual tight credit market conditions in the preceding several years. Thus based on the loan-to-deposit behavior of the Indian commercial banking system, one must conclude that the creation of the State Bank of India made a major change in portfolio composition of all banks in favor of loans and that the State Bank of India carried this process further in the period 1966-71 than did the other commercial banks.

III. BRANCH EXPANSION PROGRAM

One of the policy goals set for the State Bank of India was, to quote the AIRCS Committee Report, to "pursue a large and expenditious program of branch extension to and beyond the district headquarters" [34]. The purpose of this policy was to increase the monetarization of the economy and attempt to institutionalize the saving and investment process.

Involved in economic development is an increasing complexity in economic relations. This complexity makes it more difficult to transfer the command over resources of saving groups to investors who wish to utilize the resources [8]. Thus institutionalization of saving and investment is one of the necessary conditions of economic development. In this context, the branch expansion program can aid in the mobilization of saving out of the incremental incomes generated by economic growth. Without the alternative of financial markets rural savings are used for the accumulation of precious metals and jewelry, hoarded or spent on additional consumption items. Each of these uses prevents resources from being transferred. Thus by providing a financial asset as an alternative to non-transferable uses, some savings mobilization is accomplished [11]. Although savings is usually thought of as a function of income, the lack or undeveloped state of financial institutions can inhibit whatever potential savings exist [3].

In situations where effective financial markets are not operating, the ability to mobilize capital is a scarce resource. Unorganized creditors can therefore obtain large economic rents which are reflected in high interest rates. This has the net effect of inhibiting investment and thus reducing the rate of economic growth. Thus in terms of both the saving and investment process the expansion of existing institutional financial markets can have a marked effect on development.

With this background in mind, let us view the evidence of the branch expansion program of the State Bank of India as presented in Table 2. The number of branch offices of all the commercial banks increased approximately four times from 1955 to 1971, from 2,807 in 1955 to 5,904 in 1965, and 11,892 in 1971. Of the total number of branch offices, the proportion of the State

Bank increased from 17 percent in 1955 to 32.8 percent in 1965, and then declined to 29.8 percent by 1971. Of the total increase in offices between 1955-65, 47 percent was accounted for by the State Bank whereas between 1966 and 1971 it was only 26 percent. The decline in the proportion of State Bank offices was particularly evident since 1969, when the Government of India and the Reserve Bank ussued a directive for all banks to undertake a vigorous branch expansion program.

However, the significance of the branch expansion program is not only measured by the magnitude of new offices, but also by the rural-urban location of those offices. Examining this performance reveals the following:

(1) Between 1955-1968, 40.5 percent of the offices opened by the State Bank were located in population centers below 10,000 which is double the percent of other commercial banks.

(2) From 1955-1965, the State Bank opened three offices in semi-urban and rural areas for every two offices in urban areas, whereas other banks opened only one office in four in the same relative areas.

(3) The proportion of offices in cities with population of less than 50,000 increased for the State Bank from 60 to 72 percent from 1955 to 1965 while that of other banks declined from 44 to 39 percent.

(4) From 1955 through 1970, 62 percent of the branches opened by the State Bank were in semi-urban areas with population between 10,000 and 100,000.

It is evident that the State Bank has devoted more resources to providing some form of banking in the semi-urban and rural areas than other commercial banks. However, even with this branch expansion, only 18 percent of the offices of commercial banks were situated in population centers below 10,000 in 1970. According to a recent study, a number of districts which were relatively developed agriculturally (in 1966) were not served by adequate banking facilities [19]. Thus in terms of availability of credit in the rural areas of India, there is still need for further improvements.

IV. ASSISTING COOPERATIVES

One of the rationales for establishing State Bank offices in rural areas is to stimulate the development of other financial institutions, particularly cooperatives. This was the second policy goal set for the State Bank in 1955. Basically cooperatives have been encouraged by providing liberal finance to them. The credit line to cooperative institutions increased by seventeen times from 1955 to 1970, a growth rate exceeding that to any other sector (Table 3). Thus whereas the credit line was Rs 15 Crores in 1955, it was Rs 56 Crores in 1965 and Rs 266 Crores in 1970. The annual growth rate of credit to cooperatives increased from 5.1 in 1958-65 to 34.4 in 1966-70. Thus in this objective, the State Bank certainly succeeded in the goal set for it. However, it is difficult to comprehend why cooperatives warranted such a substantial increase in credit especially in light of the remaining distribution of credit.

Table 3: Trends in the State Bank of India Finance to Cooperative Institutions, 1958-1970. (Year End Figures. Amount in Crores of Rupees).*

Year	Credit Line
1958	15
1965	56
1965-58**	41
1966	94
1967	94
1968	114
1969	168
1970	266
1970-66**	172
1970-58**	251

*Source: See footnote #1.
**Change between years indicated.

V. DISTRIBUTION OF CREDIT

In terms of implementing policy the distribution of credit between various sectors becomes one measure of the loan priorities of the State Bank. Several characterizations of the credit distribution will be investigated in line with the stated credit objectives.

Table 4: Rural-Urban Distribution of Credit of Indian Commercial Banks in 1965.*

Centers	Percentage of deposits	Percentage of loans	Loan deposit ratio
Large cities (population-over 1,000,000)	47.9	62.9	91.3
Other cities (population-100,000 to 1,000,000)	26.6	21.3	55.8
Large towns (population-50,000 to 100,000)	7.2	5.5	53.2
Small centers (population-below 50,000)	18.3	10.3	39.2

*Source: See [20].

Table 4 presents the distribution of credit between rural and urban centers in 1965. Small centers contributed over 18 percent of the total deposits, but only received a little over 10 percent of total loans. On the other hand, large cities contributed about 40 percent of the total deposits, but received about 63 percent of the total loans. Cities with population over 100,000 received about 84 percent of the total loans, whereas the entire remaining portion of India received only 16 percent of the total loans.

The loan-deposit ratio was 39 percent in small centers, whereas in large cities it was over 91 percent. In certain metropolitan cities, the loan-deposit ratio actually exceeded 100 percent. For example, in Madras, it was 141 percent, in Ahmedabad it was 118 percent, and in Calcutta it was 107 percent.

Although there was a great disparity in the rural-urban distribution of credit a similar disparity appears in the sectoral distribution of credit. It is to this question that we now turn. Table 5 presents a breakdown of credit to the following sectors: industry, commerce, finance consumption, agriculture and others. We can make the following observation on this. Over a period of seventeen years, the percentage of commercial bank credit to industry nearly doubled, from 34 to 67.5 percent. There was a substantial decline to all other sectors except for agriculture which was relatively constant around 2 percent (except for 1961). However, this is surprisingly low considering the relative importance of agriculture in the economy.

Table 5: Sectoral Distribution of Commercial Bank Credit, 1951-1968.*

Sector	March 1951	March 1956	April 1961	March 1966	March 1968**
Industry	34.0	37.1	50.8	62.7	67.5
Commerce	36.0	36.5	28.6	21.4	19.2
Finance	12.7	9.3	5.1	3.3	2.7
Consumption	6.8	6.6	6.7	4.6	3.7
Agriculture	2.1	2.0	3.1	2.4	2.2
Other	8.4	8.4	5.6	5.6	4.7
Total	100.0	100.0	100.0	100.0	100.0

*Source: Reserve Bank of India Bulletin, Vol. XXV, Number 5, May 1970.
**Provisional

Thus, there was a massive diversion of rural resources to urban areas. Further, the disparity in the distribution of credit between agriculature and industry was widening.[6/] It is this disparity which led the government to create the National Credit Council in order to redirect the allocation of bank credit. The following are important dimensions of the new credit policy:

(1) Allocation of credit in accordance with the plan priorities. Apart from fixing the aggregate of bank credit at the desited level, such selective approach can ensure its proper distribution according to the requirements of plan targets [13, 21, 25, 33]. In this context, small scale industries, agriculture and export have been designated as priority sectors for which the National Credit Council lays down credit targets.

(2) Shift of banking from 'big' customer to the 'small' customer is another dimension of new credit policy. It is a socio-economic objective of the government to reduce the income disparity by assisting the lower economic groups in bettering their conditions. In this regard it was felt that the banking system should play a key role by providing the finance for increased productivity of these groups.

It follows from the new credit policy discussed above that there is need for significant changes in the lending concepts, policies and practices of banks. For example, security, although significant as a measure of repayment ability, should not be the only criterion for advancing loans. The need for credit itself should be considered. Thus, a shift of emphasis is taking place from security to productivity. To insure that there is no

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[6/] This disparity in distribution of credit by commercial banking system between agriculture and industry was not only due to the attitude of the banking system towards agriculture; it was equally due to the official policy of the Government of India and the Reserve Bank in not encouraging the branching of commercial banks into the area of agricultural credit with the apprehension that this would discourage the growth of the cooperative agricultural credit system.

increase in risk to the banking system from this change in emphasis, a government-backed institution was set up for each of the major loan priority categories, the Credit Guarantee Scheme for small industry finance, the Agricultural Refinance Corporation for the agricultural sector, the Export Credit Guarantee scheme for export finance, and the Credit Guarantee Scheme for financing transport operators, traders in fertilizer and other goods, and professional and self-employed persons. Let us evaluate how well the State Bank has performed in implementing this new credit policy in regard to financing each of these sectors.

A. Financing small scale industries.

Small scale industrial sector plays a significant role in the Indian economy. According to the Annual Survey of Industries (1963), small units accounted for 91.5 percent of the total number, 34.8 percent of the employment and 28.9 percent of the gross output of the registered factory sector [22]. Development of small industry sector needs to be encouraged for the following reasons:

(1) In the context of capital scarcity including the foreign exchange component and enterpreneurial resources, it would be a prudent strategy of economic growth to encourage small industrial units.

(2) With the onset of the 'Green Revolution', scope for the development of small industries seems to have been enchanced since there is a new impetus to demand for manufactured farm inputs as well as consumer goods [25].

(3) Since small industries produce mainly the basic necessity of life such as food products, grain milling, and ginning and processing of fibers, development of these industries would add to the welfare of the common man.

Table 6: State Bank of India Credit to Priority Sectors in its Total Advances, 1956-70*
(Year end figures. Amount in crores of Rupees)

Year	Total Advances	Small scale industries: Number of units finances	Small scale industries: Credit limits	Agriculture: Number of accounts	Agriculture: Credit limits	Export sector: Number of accounts	Export sector: Credit limits	"Small business"**: Number of accounts	"Small business"**: Credit limits
1956	N.A	25	0.11	--***	--	--	--	--	--
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1965	575	10,307	60 (10.4)	--	--	--	--	--	--
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1968	916	19,941	137 (15.0)	N.A	85 (9.3)	N.A.	N.A	--	--
1969	1,057	31,493	245 (23.2)	120,548	241 (22.8)	846	112 (10.6)	18,166	19 (1.8)
1970	1,361	51,296	330 (24.2)	283,503	311 (22.9)	1,337	167 (12.3)	43,206	34 (2.5)

*Source: See footnote #1. The numbers in parenthesis are percentages to total advances.

**Includes retail trade, professionals and self-employed persons, and other small businesses.

***None or innegligible amount.

Thus, development of small industries may be supported both on economic and equity grounds. Many times a lack of acceptable security seems to prevent small industries from gaining access to commercial bank credit. This needs to be kept in view while evaluating the role of State Bank in financing small industries.

The percent of loans to small industries increased from 10.4 in 1965 to 24.2 in 1970 (Table 6). The number of units assisted increased to 10,307 in 1965 from 25 in 1956, and there was nearly a five-fold increase from 1965-1970.

Further, of total loans made to small industries by all the scheduled commercial banks, the State Bank increased its share from 29.7 percent in 1965 to 41.5 percent in 1971 and of the increase in total loans between 1965-1971, the percentage of the State Bank was 43.6 implying a higher rate of growth in credit advanced. Thus, the State Bank improved its performance with respect to small industries both on absolute and relative amounts. Let us explore the lending "strategies" underlying this change in policy.

The Bank will provide loans to small scale industrialists based on productive capacity even if they do not maintain the usual debt--equity ratio or have normally acceptable security, provided the productive capacity of the borrower is acceptable. With the aim of nurturing entrepreneurial talent, the Bank has embarked on a new scheme which seeks to assist technically competent persons without adequate resources of their own, to set up new industries in the priority fields [37].

In addition to providing financial help, the Bank assists small industrial units complementary ways such as getting licences for importing raw materials and guiding them to other specialized institutions such as State Financial

Corporations, National Small Industrial Corporation, and Small Industries Corporation in various states.

2. Financing Agriculture

As stated already, the National Credit Council has declared agriculture as one of the priority sectors under the new credit policy. Until recently the role of commercial banks in agricultural finance was confined to the indirect role of assisting cooperatives [24]. With the onset of the 'Green Revolution' multiagency approach to farm finance has become imminent. As a result, the State Bank along with other scheduled commercial banks, has started providing direct credit to agriculturalists in addition to providing financial support to cooperatives.

"Direct loans made to farmers to help in transforming the pattern of their farming into one of higher technological content would highly be a new experience of banks (in India)" [23]. However, the State Bank seems to have made a good start in this regard. There are two interesting observations to draw from Table 6 concerning State Bank financing agriculture: (1) Of the total loans made by the State Bank, the percentage to agriculture increased from 9.3 in 1968 to 22.9 in 1970. (2) The number of agricultural accounts increased more than a two-fold within a year.

It is too early to be conclusive on the success of the State Bank's agricultural program. However, there are some important dimensions in evolution. Credit is provided by the State Bank for the manufacture, distribution and purchase of farm inputs. Credit to private distributors of fertilizers, and credit to purchase of agricultural implements on installment basis are the two major components of this input credit program. Credit is also

Table 7: Trends in the State Bank of India Loans to Small Scale Industries as a Percentage of Loans by All Commercial Banks, 1965-1971.* [March end figures (outstandings). Amount in Crores of Rupees.]

Year	Total loans by all the scheduled commercial banks [(2) + (4)] (1)	State Bank of India: Total loans (2)	State Bank of India: Percentage to (1) (3)	All other scheduled commercial banks: Total loans (4)	All other scheduled commercial banks: Percentage to (1) (5)
1965	74	22	29.7	52	70.3
1966	91	34	37.4	57	62.6
1967	179	45	25.1	134	74.9
1968 (June)	190	57	30.0	133	70.0
1969 (June)	286	93	32.5	193	67.5
1970	394	155	39.3	239	60.7
1971	494	205	41.5	289	58.5
1971-65**	420	183	43.6	237	56.4

*Source: See Footnote #1.

**Change between years indicated.

provided for some specific regional agricultural development schemes such as Vara nasi-Etah Scheme involving intensive ground water and land development, and the Terai Region Scheme involving the development of hybrid seed farms.

The "Village Adoption Scheme" is another facet of regional approach to farm finance [42]. In the adopted villages, intensive efforts are made to reach all the economically viable farmers, irrespective of the size of their farm holdings. Until March 1970, 421 villages were "adopted" by the State Bank.

In view of credit problems facing small farmers [1, 18] as well as the policy of the government to support this section of farm community the State Bank has started financing their needs. One of the distinctive features of the credit program to small farmers is 'group borrowings' i.e., while loans are granted to individual farmers, these loans are secured by the guarantee of all the farmers in the group.

The State Bank's Farm Graduate Scheme is designed to extend finance to farm graduates who have worthwhile farm development projects but unable to undertake them due to lack of resources. The motivation for this credit program is to assist the emergence of new class of agricultural entrepreneurs in rural areas.

3. Financing Export Sector

The State Bank of India credit to export sector is another specific credit program under new credit policy. As shown in Table 7, the percentage of credit to export sector in total loans increased from 10.6 in 1969 to 12.3 in 1970.

4. Financing Small Business

Once economic development gathers momentum, economic activities of small institutions such as those of printing presses, catering establishments, retail trade, transport services, and of professional personnel like doctors, architects would become in demand. Further, financially weaker sectors will have to be drawn to the development stream by spreading entrepreneurship. Development of small business through specific credit program could facilitate the attainment of this end. This explains why credit to small business programs is gaining momentum during recent years. As revealed in Table 6, the percentage of credit to small business' increased from 1.8 in 1969 to 2.5 in 1970, and the number of accounts under this head more than doubled within a year implying the increased access of small business figures to bank credit.

It is clear from the discussion preceeded that even though credit to priority sectors is rather a recent program, the performance of the State Bank in this front is encouraging. Of the total credit advanced by the State Bank, the percentage to priority sectors increased from 58.4 in 1969 to 61.9 in 1970.

VI. OPERATING RESULTS

We have evaluated the performance of the State Bank in mobilizing deposits, supplying loanable funds, extending branch offices, supporting cooperative institutions, and distributing credit in consonance with the national policy goals. It would be interesting to examine the impact of the State Bank's commitment to new goals on profitability of its business, since this would throw light on the possible conflict between new goals and profitability.

It is evident from Table 8 that the net profit earned by the State Bank as a percentage to its total earnings nearly halved within a period of seven years. In fact, this was a feature of the Indian commercial banking system. For example, the ratio of profits before tax to total earnings nearly halved from 23 percent in 1961 to 12 percent in 1968 [12]. Thus, continuously declining profit margin in the case of the State Bank is possibly suggestive of the conflict between new goals and relatively high percentage of profitability. The State Bank of India may well be advised to operate with low profit margin, if the alternative is to abandon the new goals. However, a search for specific causal forces giving rise to declining profit margin would suggest courses of action to be considered for reversing this trend if possible.

Three important causal forces seem to have accounted for the declining profit margin.

(1) At the end of 1969, 85 percent of the State Bank's new branches in rural areas and 80 percent of the branches in semi-urban areas were incurring loss [39]. To meet this problem, a program of action that may be considered is to locate rural branches in centers which have witnessed or have the potential for increased productive activities. The 'Lead Bank Scheme' introduced recently seems to have this strategy in view.

(2) Rising costs of resources also accounted for diminishing profitability of the State Bank operations. As evidenced in Table 8 the percentage of total expenditures to total earnings increased from 98.5 in 1964 to 95.2 in 1970. There is some evidence to suggest that increasing labor cost unaccompanied by increased productivity had contributed much for this behavior of trends in total expenditure. For example, while the cost per employee

Table 8: Trends in the State Bank of India Net Profit as a Percentage of its Total Earnings, 1964-1969.* (Year end figures. Amount in Crores of Rupees).

Year	Total earnings	Total expenditures	Net profit
1964	30.95	28.00 (90.5)	2.95 (9.5)
1965	43.99	40.69 (92.5)	3.30 (7.5)
1966	54.67	50.88 (93.1)	3.79 (6.9)
1967	65.99	61.56 (93.3)	4.43 (6.7)
1968	79.76	74.70 (93.7)	5.06 (6.3)
1969	91.40	85.90 (94.0)	5.50 (6.0)
1970	112.67	107.27 (95.2)	5.40 (4.8)

*Source: See footnote #1.

The numbers in parentheses are percentages to total earnings.

increased by 60 percent, profit per employee decreased by 32 percent.[7/]

(3) A considerable increase in the number of small transactions with the implementation of new credit policy is bound to account for declining profit margin. As shown in Table 6 between 1969 and 1970, increase in the amount of credit limits sanctioned was about 1-1/4 times in the case of

[7/] See for details State Bank of India Chairman speech at the annual meeting of shareholders, State Bank of India Monthly Review, Vol. IX, No. 3, March 1970.

agricultural finance, whereas the number of accounts to the processed was more than 2 times. In the case of finance to "small business", the amount of credit limits sanctioned was slightly less than 2 times, whereas the number of accounts to be processed was considerably more than 2 times.

One of the most challenging tasks for the State Bank at present is to minimize the declining profit margin without giving up the implementation of new credit policy. Given the inevitability of implementing the new credit policy, the Bank has to explore the ways and means of increasing the productivity of its operations. The concept of productivity in all its comprehensive meaning does not seem to have influenced the management of the Bank [31].[8/] The rising proportion of the Bank's expenditure to its total income seems to be an account of total absence of any idea of the magnitude of costs underlying various banking operations and various banking services. Creation of the Management Division within the Bank to explore the possibilities of improving the productivity of Bank's operations is nothing more than a beginning in this direction.

VII. SUMMARY AND CONCLUSIONS

In this paper, we have evaluated the performance of the State Bank of India in relation to other commercial banks over the period 1955-1970 in regard to how well they have met the objectives set forth by the AIRCS committee of 1954. The conclusions of the paper are mixed. In terms of deposit mobilization, it does not appear that the State Bank obtained a substantially

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[8/] Also, see "Meeting The Challenge of Growth Through Improved Productivity in Banking," State Bank of India Monthly Review, Vol. V, No. 11, November 1966.

larger portion of total deposits over the period. In addition, credit was extended to industry at the expense of all other sectors but agriculture which received a constant but small portion of the total credit advanced. Although this latter fact does not in itself imply poor performance, it certainly must be asked whether it is intelligent development policy to provide the agricultural sector--the single most important sector of the Indian economy--with such a small share of credit. In addition, although the priority sectors have received an increased share of credit in the most recent year of the study, they are still getting far less than their economic importance implies.

On the positive side, the State Bank significantly outperformed the other commercial banks in regard to the loan-to-deposit ratio especially in the period 1966-1971. In fact, although it is a difficult proposition to test, it appears as though the existence of the State Bank and its changing objectives was a prime motivating force for the entire Indian Banking System to raise its loan-deposit ratio. This ratio was exceeding high by western standards and undoubtedly was an important contributor of Indian economic development.

Lastly, the change in objectives of the State Bank from a purely profit orientation to an instrument of national policy led directly to a substantial reduction in the profit rate. Although this is not surprising, great effort should be made to limit the bureaucratization of the State Bank with its inherent inefficiency.

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