

## CHAPTER 7

### MONETARY AND CREDIT DEVELOPMENTS

#### Introduction

7.1 The year 1981-82 has witnessed a moderation in monetary expansion. Aggregate monetary resources ( $M_3$ ) during 1981-82 (up to January 8, 1982) increased by 11.3 per cent compared with 13.4 per cent in the same period last year. Current trends indicate that the overall monetary expansion for the full year 1981-82 is likely to be lower than that in 1980-81. Net bank credit to the Government is likely to show a lower increase than in 1980-81 and the increase in bank credit to the commercial sector is likely to grow at about the same rate as in the previous year. There is also likely to be a substantial decline in net foreign exchange assets of the banking system, which would further contribute to a reduction in the rate of growth of aggregate monetary resources.

#### Monetary Trends in 1980-81

7.2 Monetary expansion in 1980-81 was almost at par with that in 1979-80. Aggregate monetary resources ( $M_3$ ) increased by Rs. 8,317 crores or 17.6 per cent in 1980-81 as against Rs. 7,111 crores or 17.7 per cent in the previous year. Money supply ( $M_1$ ), however, rose by 16.8 per cent compared with 15.7 per cent in 1979-80. Net bank credit to Government showed an increase of Rs. 5,704

crores (28.5 per cent) which was significantly higher than the rise of Rs. 4,084 crores (25.6 per cent) in 1979-80. Bank credit to commercial sector showed a lower increase of Rs. 5,323 crores (17.2 per cent) than Rs. 5,475 crores (21.4 per cent) in 1979-80. The expansionary effect of these two factors on money supply in 1980-81 was to some extent cushioned by a decline of Rs. 613 crores in net foreign exchange assets of the banking sector.

7.3 However, there was some deceleration in the expansion of reserve money in 1980-81 as it increased by 17.3 per cent compared with 17.7 per cent in 1979-80 and 28.7 per cent in 1978-79 (Table 7.1). The growth in reserve money was largely the result of a rise in net RBI credit to Government during these years. An important factor in containing the expansion of reserve money was the much larger decline in the net foreign exchange assets of the banking system. RBI's credit to commercial sector and other banks was also lower than in the previous year.

#### Monetary Trends in 1981-82

7.4 Available comparable data on money supply ( $M_1$ ) increased by Rs. 1,411 crores, till January 8, 1982 as against the higher increase of Rs. 1,752

TABLE 7.1

*Sources of Change in Reserve Money*

	Out- standing as on March 31, 1978	Variations during				
		1978-79	1979-80	1980-81	1980-81 (Mar. 31 to Jan. 9)	1981-82* (Mar. 31 to Jan. 8)
1. Net RBI credit to Government	7644	1772 (23.2)	2989 (31.7)	4038 (32.6)	1641 (13.2)	1986 (12.1)
2. R.B.I. credit to banks	926	191 (20.6)	83 (7.4)	76 (6.3)	(—)81 (—6.7)	159 (12.4)
3. R.B.I. credit to commercial sector	954	296 (31.0)	296 (23.7)	154 (10.0)	78 (5.0)	194 (11.4)
4. Net foreign exchange assets of RBI	4532	899 (19.8)	(—)43 (—0.8)	(—)613 (—11.4)	(—)707 (—13.1)	(—)1776 (—37.2)
5. Government's currency liabilities to the public	593	11 (1.9)	(—)12 (—2.0)	17 (2.9)	15 (2.5)	13 (2.1)
<i>Minus</i>						
6. Net non-monetary liabilities of R.B.I.	3708	27 (0.7)	823 (22.0)	804 (17.6)	(—)191 (—4.2)	393 (7.3)
<b>RESERVE MONEY (1+2+3+4+5—6)</b>	<b>10941</b>	<b>3142 (28.7)</b>	<b>2490 (17.7)</b>	<b>2868 (17.3)</b>	<b>1137 (6.9)</b>	<b>183 (10.9)</b>

\*Provisional/Partially Revised.

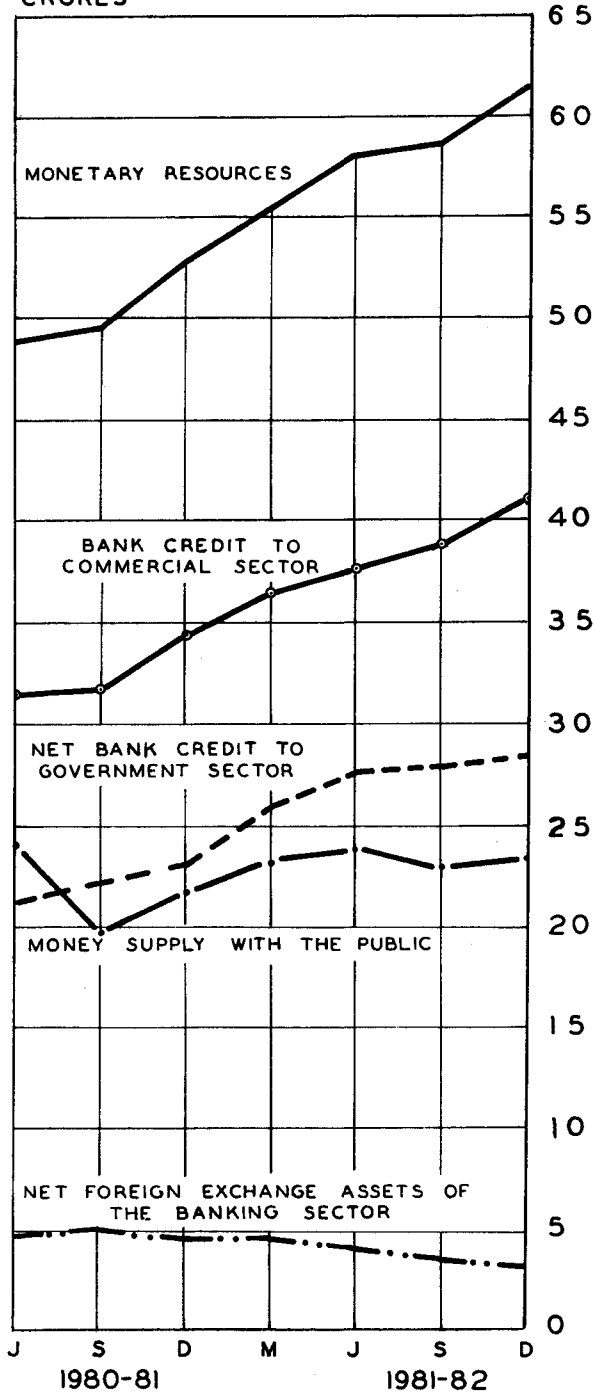
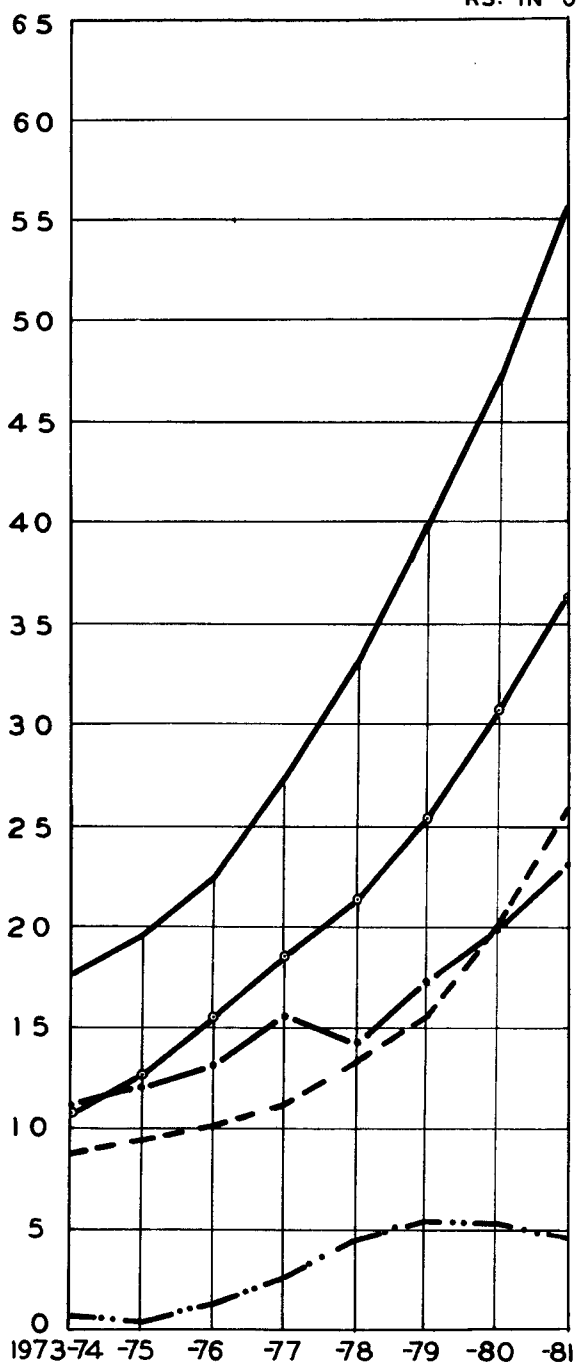
NOTES : (1) Figures in brackets are percentage variations.

(2) Data relate to March 31, after closure of Govt. accounts.

# MONEY SUPPLY WITH THE PUBLIC AND MONETARY RESOURCES

(AS ON LAST FRIDAY)

RS. IN '000 CRORES



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crores in the same period last year. The growth rate of 6.0 per cent in  $M_1$  during the period was significantly lower than 8.8 per cent recorded in the corresponding period of 1980-81. Similarly, aggregate monetary resources ( $M_3$ ) rose by Rs. 6,270 crores till January 8,

1982 as against a rise of Rs. 6,318 crores in the same period of 1980-81. The growth rate of  $M_3$  expansion at 11.3 per cent during the period was also lower than 13.4 per cent recorded in the comparable period last year.

TABLE 7.2

## Sources of change in Money Stock

(Rs. crores).

	Variations during			
	1979-80 (Mar. 31 to Mar. 31)	1980-81 (Mar. 31 to Mar. 31)	1980-81 (Mar. 31 to Jan. 9)	1981-82* (Mar. 31 to Jan. 8)
I. $M_1$ (Money supply with the public)	2709 (15.7)	3359 (16.8)	1752 (8.8)	1411 (6.0)
II. $M_3$ (Aggregate monetary resources)	7111 (17.7)	8317 (17.6)	6318 (13.4)	6270 (11.3)
1. Currency with the public	1422 (13.9)	1772 (15.2)	1314 (11.3)	410 (3.0)
2. Demand deposits with banks	1062 (15.4)	1568 (19.7)	641 (8.1)	1253 (13.2)
3. Time deposits with banks	4403 (19.3)	4957 (18.2)	4565 (16.8)	4859 (15.1)
4. Other deposits with RBI	225	20	(—)203	(—)253
III. Sources of change in $M_3$ (1+2+3+4—5)				
1. Net bank credit to Government. (a+b)	4084 (25.6)	5704 (28.5)	3806 (19.0)	3167 (12.3)
(a) RBI's net credit to Government. (i+ii)	2989	4038	1641	1986
(i) To Central Government.	2650	3551	1899	1779
(ii) To State Governments.	339	487	(—)258	207
(b) Other banks' credit to Government.	1095	1666	2165	1181
2. Bank credit to commercial sector (a + b)	5475 (21.4)	5323 (17.2)	3997 (12.9)	5306 (14.6)
(a) RBI's credit	296	154	78	194
(b) Other banks' credit	5179	5169	3919	5112
3. Net foreign exchange assets of banking sector.	(—)43 (—0.8)	(—)613 (—11.6)	(—)661£ (—12.5)	(—)1730 (—37.0)
4. Government's currency liabilities to the public	(—)12 (—2.0)	17 (2.9)	15 (2.5)	13 (2.1)
5. Banking sector's net non-monetary liabilities other than time deposits (a+b)	2393 (32.8)	2114 (21.8)	839 (8.7)	486 (4.1)
(a) Net non-monetary liabilities of RBI	823	802	(—)191	395
(b) Net non-monetary liabilities of other banks (derived)	1570	1311	1030	92

\*Provisional/Partially Revised.

£The decline in foreign exchange assets would have been much larger but for the accretion of Rs. 544 crores on account of IMF Trust Fund Loan during 1980-81.

NOTES : 1. Figures in brackets are percentage variations.

2. Figures may not add up to totals due to rounding.

3. The demand and time deposits data for March 31, 1979 and March 31, 1980 are worked out on the basis of the proportion in which demand and time deposits were placed for the last Fridays of March 1979 and March 1980 respectively.

7.5 An examination of various components of  $M_2$  reveals diverse trends. Currency with the public rose by Rs. 410 crores or by 3.0 per cent, a much lower pace during the current year up to January 8, 1982 compared with the increase of Rs. 1,314 crores (11.3 per cent) during the same period last year. Demand deposits\* with banks, however, registered a larger increase of Rs. 1,253 crores compared with that of Rs. 641 crores in the corresponding period last year. Time deposits with banks continued to rise, albeit, at a lower rate and the increase amounted to Rs. 4,859 crores compared with the rise of Rs. 4,565 crores in the same period of the previous year. Other deposits with RBI registered a decline of Rs. 253 crores compared with the decrease of Rs. 203 crores in the previous comparable period.

7.6 The sources of change in  $M_2$  given in Table 7.2 show that unlike in the previous three years, a substantial step-up in bank credit to commercial sector was a major source for monetary expansion during 1981-82 (up to January 8, 1982). Bank credit to commercial sector during the period increased by Rs. 5,306 crores or 14.6 per cent compared with Rs. 3,997 crores or 12.9 per cent in the corresponding period of the previous year. Two factors have been mainly responsible for the expansion of bank credit to commercial sector. Improvement in production of foodgrains, particularly in Rabi 1980-81, led to higher procurement of foodgrains and larger food credit in 1981-82. Industrial production showed significant increase in 1981-82 over that in the previous year and this in turn, necessitated a larger flow of credit to the commercial sector. In contrast, there was a slow down in net bank credit to Government and its role as a dominant source of monetary expansion in the last three years diminished to some extent in the current year. Net bank credit to Government rose by Rs. 3,167 crores or by 12.3 per cent till January 8, 1982 as against Rs. 3,806 crores or 19.0 per cent in the same period last year. The expansion of money supply resulting from these sources during the current year (up to January 8, 1982) was significantly neutralised by the much larger decline in the net foreign assets of the banking sector by Rs. 1,730 crores or 37.0 per cent as against a decline of Rs. 661 crores or 12.5 per cent in the corresponding period last year.

7.7 The deceleration in monetary expansion in the current year so far was reflected in smaller growth in reserve money. Reserve money increased by 0.9 per cent up to January 8, 1982 which was significantly lower than the growth of 6.9 per cent in the comparable period of 1980-81. The growth of reserve money was lower because of the substantial decline in net foreign exchange assets of RBI by

Rs. 1,776 crores (by 7.2 per cent) up to January 8, 1982 compared with Rs. 707 crores (by 13.1 per cent) during the corresponding period of last year. The increase of Rs. 393 crores in net non-monetary liabilities of RBI this year in contrast to a decline of Rs. 191 crores in the same period last year had also depressed the growth of reserve money. On current indications, the growth in reserve money is likely to further decelerate during 1981-82.

7.8 In view of the anticipated rise in both agricultural and industrial production, bank credit to commercial sector is expected to rise further during the rest of 1981-82. However, net foreign exchange assets of the banking sector which have shown a larger decline so far are likely to decline further, and would cushion the monetary expansion during the year. The rate of increase in net bank credit to Government is also likely to be contained within reasonable limits.

#### **Trends in Scheduled Commercial Banks' Credit**

7.9 In 1980-81, gross bank credit (including participation certificates and bills rediscounted with RBI) showed an expansion of Rs. 3,451 crores, almost similar to the level of Rs. 3,457 crores in 1979-80. This expansion was entirely due to the increase in gross non-food credit which rose by Rs. 3,773 crores as against Rs. 3,618 crores in 1979-80. Food procurement credit, on the other hand, declined sharply by Rs. 322 crores during 1980-81 due to lower food procurement in the wake of the previous year's drought.

7.10 Deposit mobilisation by scheduled commercial banks increased in absolute amounts in 1980-81. Aggregate deposits increased by Rs. 5,874 crores compared with Rs. 4,981 crores in the previous year. The rate of increase at 18.2 per cent was about the same as in 1979-80. The increase was shared by both demand and time deposits which rose by Rs. 1,243 crores and Rs. 4,631 crores respectively. The corresponding increases in 1979-80 were of the order of Rs. 865 crores and Rs. 4,116 crores.

7.11 Scheduled commercial banks' investment in Government and other approved securities increased markedly in 1980-81. This increase was of the order of Rs. 2,435 crores compared with Rs. 1,729 crores in the previous year. Consequently, the investment-deposit ratio of banks rose to 34.0 per cent as at the end of 1980-81 from 32.7 per cent as at the end of 1979-80. The banks' cash reserves in 1980-81 also showed a larger increase of Rs. 1,049 crores than Rs. 831 crores in 1979-80 and the banks decreased their borrowings from the RBI by Rs. 117 crores in contrast to the increase by Rs. 173 crores in 1979-80.

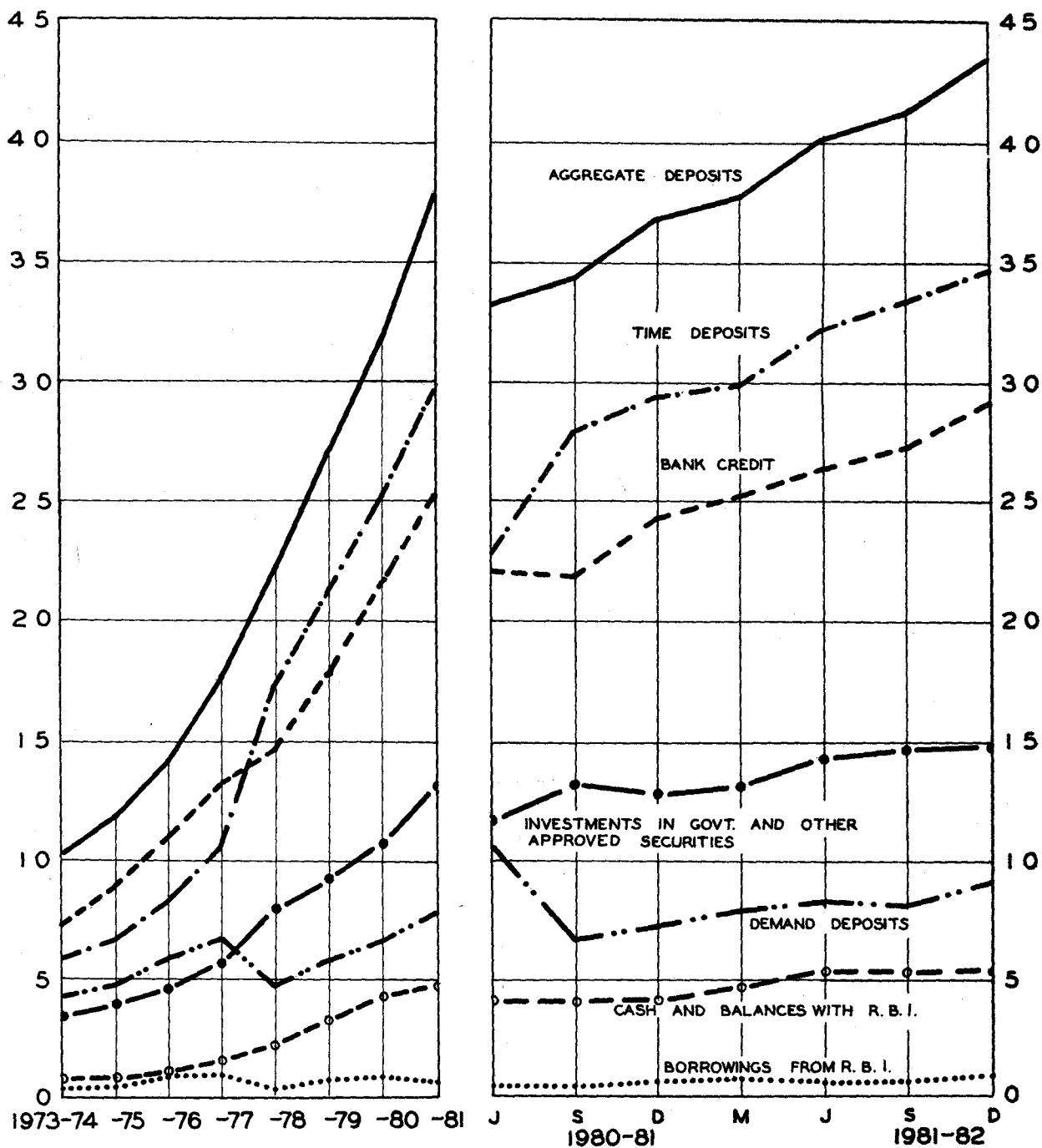
7.12 During 1981-82, gross bank credit by scheduled commercial banks (including participation certificates and bills rediscounted with RBI) till January 8, 1982 expanded by Rs. 4,120 crores (16.2 per cent) which was substantially higher than the increase of Rs. 2,522 crores (11.4 per cent) registered in the corresponding period of 1980-81. This was

\*Beginning from January 1978, banks started adopting a new classification of their savings deposits into demand and time liability components from different dates. As such, the data on demand and time deposits given in the past three Economic Surveys were not comparable over different years. Now the data are available on the basis of a uniform classification and these are comparable.

# SCHEDULED COMMERCIAL BANKS

[AS ON LAST FRIDAY]

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due to the substantial increase in both food and gross non-food credit. Food credit had shown a rise of Rs. 649 crores compared with Rs. 36 crores in the corresponding previous period, due to a step up in food procurement following the substantial recovery in agricultural production particularly in Rabi 1980-81. Gross non-food credit, likewise, rose by Rs. 3,471 crores compared with Rs. 2,486 crores in the corresponding period last year. The factor contributing to this rise was the continued improvement in industrial production in 1981-82. The rise in administered prices of key inputs and import of additional quantity of sugar and edible oils also led to higher demand for credit in 1981-82. At the same time the flow of credit to the priority sectors was stepped up.

7.13 The rise in aggregate deposits of scheduled commercial banks up to January 8, 1982 at Rs. 5,804 crores was larger than that of Rs. 4,760 crores record-

ed in the same period of 1980-81. This represents a growth rate of 15.2 per cent as against 14.8 per cent last year. The gross credit-deposit ratio at 67.4 per cent on January 8, 1982 was higher than 66.1 per cent as on March 31, 1981.

7.14 Both demand and time deposits showed further growth during 1981-82. Demand deposits showed a rise of Rs. 1,122 crores till January 8, 1982, giving a growth rate of 14.0 per cent compared with the increase of Rs. 455 crores or 6.7 per cent in the corresponding period of the previous year. Time deposits also increased by Rs. 4,682 crores during the period compared with the increase of Rs. 4,305 crores in the same period of 1980-81. The growth rate in time deposits at 15.5 per cent was, however, lower than the 16.9 per cent during the corresponding period last year. The upward adjustment in bank deposit rates announced following the Union Budget for 1981-82 was a positive factor contributing to time

TABLE 7.3  
Scheduled Commercial Banks : Variations in Selected Indicators

	(Rs. crores)			
	Variations during			
	1979-80	1980-81	1980-81 (Mar. 31 to Jan. 9)	1981-82* (Mar. 31 to Jan. 8)
1. Aggregate deposits	4981	5874	4760	5804
(a) Demand deposits	865	1243	455	1122
(b) Time deposits	4116	4631	4305	4682
2. Borrowings from RBI	173	(—)117	(—)212	39
3. Cash in hand and balances with RBI	831	1049	38	46
(a) Cash in hand	116	132	68	101
(b) Balances with RBI	715	918	(—)30	(—)56
4. Net balances with RBI [3(b)—2]	542	1035	182	(—)95
5. Money at call and short notice	(—)114	357	89	(—)288
6. Bank Credit†	3455	3561	2628	4120
7. Bills rediscounted with RBI	2	(—)110	(—)106	..
8. Gross bank credit (6+7)	3457	3451	2522	4120
9. Public food procurement credit	(—)161	(—)322	36	649
10. Non-food gross bank credit (8—9)	3618	3773	2486	3471
Of which :				
To priority sectors ±	1340	1756	N.A.	N.A.
11. Investments in Government and other approved securities	1729	2435	2877	1999
(a) Government securities	1044	1633	2134	1145
(b) Other approved securities	686	802	734	854
12. Balances with other banks in current account	72	4	91	256
13. Gross credit—deposit ratio	67.4	66.1	66.4	67.4
14. Gross credit (excluding food credit)—deposit ratio	60.9	61.4	60.6	61.9
15. Investment—deposit ratio	32.7	34.0	36.2	34.1

\*Provisional/Partially Revised.

†Including Participation Certificates

±Relates to only major banks which account for about 95 per cent of the gross bank credit.

N.A. Not available.

NOTE : The demand and time deposits data for March 31, 1979 and March 31, 1980 are worked out on the basis of the proportion in which demand and time deposits were placed for the last Fridays of March 1979 and March 1980 respectively.

deposit growth during the year. This came about despite still higher interest rates allowed on industrial debentures and company deposits. To the extent more deposits and debentures were raised by the corporate sector, the pressure on the banking system was relieved. The sustained growth in time deposits also showed that the attractiveness of time deposits as providing safe and reasonable return on savings continued, particularly in view of the recent decline in the rate of inflation.

7.15 Banks' borrowings from the RBI increased by Rs. 39 crores till January 8, 1982 as against a decline of Rs. 212 crores during the corresponding period of 1980-81. There was an increase of Rs. 46 crores in the cash reserves of banks during the period which was slightly higher than Rs. 38 crores in the comparable period of the previous year. The cash-deposit ratio, however, declined from 14.3 per cent on March 31, 1981 to 12.5 per cent on January 8, 1982. In the preceding year, the decline in the ratio was from 13.6 per cent to 12.0 per cent. The increase in investments in Government and other approved securities at Rs. 1,999 crores was smaller than that of Rs. 2,877 crores in the same period last year. Consequently, the investment-deposit ratio declined to 34.1 per cent on January 8, 1982 from 36.2 per cent as on January 9, 1981.

7.16 Generally easy conditions prevailed in the inter-bank call money market during the first four months of 1981-82. The market tended to improve during August-September 1981 and ruled distinctly firm thereafter. The call money rate in Bombay which was quoted far below the ceiling level till July 1981 firmed up to 8-9 per cent in August and ruled at the ceiling of 10 per cent throughout October 1981 to January 1982. In 1980-81 the money market rates had ruled easy during the greater part of the year and were quoted much below the ceiling rate of 10 per cent thus reflecting a comfortable liquidity position of banks.

#### Sectoral Deployment of Credit

7.17 Data on sectoral deployment of bank credit are available for 1979-80, 1980-81 and the first six months of the current financial year, 1981-82 (Table 7.4). The expansion of bank credit in 1979-80 and 1980-81 was entirely on account of the increase in gross non-food credit. In 1979-80, of the total increase in gross non-food credit, priority sectors accounted for 41.9 per cent, followed by industry (medium and large) with 34.3 per cent and the remaining 23.8 per cent was shared by wholesale trade and other sectors of the economy. During 1980-81, the share of the priority sectors in the non-food incremental credit increased to 45.1 per cent, that of industry to 44.0 per cent while the share of trade and other sectors together got reduced to 10.9 per cent. The share of agriculture in total advances to priority sectors which was 45.1 per cent in 1979-80 increased marginally to 45.9 per cent in 1980-81. The share of small scale industries which was comparatively less at 34.2 per cent in 1979-80, declined further to 33.9 per cent in 1980-81. The share of other sectors

in total credit to priority sectors was marginally lower at 20.2 per cent in 1980-81 as against that of 20.7 per cent in 1979-80. The growth in export credit by Rs. 10 crores in 1980-81 was much below the increase of Rs. 140 crores in 1979-80. This could be attributed to the sluggish growth in exports in 1980-81 compared with the earlier years.

7.18 The growth rate of gross bank credit during 1980-81 at 16.7 per cent was somewhat lower than that of 17.0 per cent in the previous year. This was due to the sharp decline in food procurement credit by Rs. 341 crores on top of the decrease of Rs. 110 crores during 1979-80. On the other hand, gross non-food credit in 1980-81 increased by Rs. 3,895 crores or by 20.4 per cent as against the rise of Rs. 3,198 crores or 20.1 per cent recorded in 1979-80. The increase in credit to priority sectors in 1980-81 by 26.1 per cent was higher than that of 24.9 per cent during 1979-80. Similarly the increase in credit for industry (medium and large) at 20.7 per cent was higher than 15.3 per cent in 1979-80. In contrast, credit for wholesale trade and other sectors during 1980-81 showed a lower increase at 4.1 per cent and 15.5 per cent compared with the rise of 22.2 per cent and 22.9 per cent respectively in 1979-80. Within the priority sectors agriculture received higher increase in credit of Rs. 806 crores or 29.1 per cent in 1980-81, as against Rs. 604 crores or 27.9 per cent in 1979-80. The increase for the small scale industries of 22.6 per cent was also higher than 21 per cent during 1979-80.

7.19 For 1981-82, data on credit deployment are available for the first six months of April-September 1981. During this period, gross bank credit showed an increase of Rs. 1,817 crores, which was more than four times the increase of Rs. 450 crores recorded in the same period of 1980-81. Although this increase was shared both by food credit and non-food credit, the latter accounted for the bulk of the increase. Thus, while the increase in food credit was of the order of Rs. 116 crores (in contrast to the decline of Rs. 251 crores in the corresponding period of last year), the increase in non-food credit amounted to Rs. 1,701 crores which was more than double the increase of Rs. 701 crores in the same period in the previous year.

7.20 Advances to priority sectors during April-September 1981-82 also showed an increase of Rs. 1,065 crores compared with that of Rs. 530 crores in the corresponding period of 1980-81. All the categories in the priority sectors shared in this increase. Thus, advances to agriculture registered an increase of Rs. 557 crores as against Rs. 355 crores in the similar period of 1980-81. Similarly, advances to small scale industries shot up by Rs. 288 crores, and to 'other categories' by Rs. 220 crores compared with the increase of Rs. 97 crores and Rs. 78 crores for the respective categories in the comparable period of 1980-81. Advances to wholesale trade registered an increase of Rs. 141 crores in contrast to the decline of Rs. 129 crores recorded in the previous year. Within the wholesale trade sector, advances to the Food Corporation of India (FCI) for fertiliser credit showed

an increase of Rs. 95 crores and advances to the Jute Corporation of India (JCI) and other trade went up by Rs. 3 crores and Rs. 135 crores respectively.

However, advances to the Cotton Corporation of India (CCI) decreased by Rs. 92 crores. Export credit showed an increase of Rs. 86 crores during April—

TABLE 7.4

*Sectoral Deployment of Gross Bank Credit*

(Rs. crores)

	Variations during			
	1979-80	1980-81*	April-September	
			1980-81	1981-82*
I. Gross bank credit (1 + 2)	3088 (17.0)	3554 (16.7)	450 (2.1)	1817 (7.3)
1. Public food procurement credit	(—)110	(—)341	(—)251	116
2. Gross non-food bank credit (a + b + c + d)	3198 (20.1)	3895 (20.4)	701 (3.7)	1701 (7.4)
(a) Priority sectors (i + ii + iii)	1340 (24.9)	1756 (26.1)	530 (7.9)	1065 (12.6)
(i) Agriculture	604 (27.9)	806 (29.1)	355 (12.8)	557 (15.6)
(ii) Small scale industries	458 (21.0)	595 (22.6)	97 (3.7)	288 (8.9)
(iii) Other priority sectors	278 (26.5)	355 (26.7)	78 (5.9)	220 (13.1)
(b) Industry (medium and large)	1096 (15.3)	1715 (20.7)	225 (2.7)	218 (2.2)
(c) Wholesale trade other than food procurement (i + ii + iii + iv)	348 (22.2)	79 (4.1)	(—)129 (—6.7)	141 (7.1)
(i) Cotton Corporation of India	48	31	(—)41	(—)92
(ii) Food Corporation of India	2	32	7	95
(iii) Jute Corporation of India	28	23	15	3
(iv) Other trade	270	(—)7	(—)110	135
(d) Other sectors	414 (22.9)	345 (15.5)	75 (3.4)	290 (11.4)
II. Export Credit (included under item 2)	140 (9.3)	10 (0.6)	(—)38 (—2.3)	86 (5.2)
III. Priority sectors advances as per cent of bank credit (excluding PCs) in the last month of the period	31.9	33.8	33.3	35.5

\*Provisional.

NOTES : 1. Figures in brackets are percentage variations.

2. Data relate to major banks which account for 95 per cent of gross bank credit and include bills rediscounted with RBI, IDBI and other approved institutions and Participation Certificates.



September of 1981-82, in contrast to the decrease of Rs. 38 crores in the similar period of 1980-81. The rise in export credit was expected because of the recovery of exports in the current year. These trends in credit deployment are tentative but broadly conform to the sectoral priorities for credit deployment.

7.21 The outstanding bank advances (excluding PCs) at the end of September 1981 were Rs. 26,873 crores while the outstanding advances to priority sector were Rs. 9,551 crores. The priority sectors' share in total outstanding advances at the end of September 1981 thus worked out to 35.5 per cent. This compared favourably with the share of 33.3 per cent as at the end of September 1980.

### Developments in Credit Policy

7.22 The stance of the monetary and credit policy during 1981-82 continued to be that of caution and restraint. It sought to restrain the expansion of money supply while seeking to raise time deposits with a view to mobilising financial savings. Bank credit was to be restrained without inhabiting the increased flow of credit to the priority sectors, food procurement, exports and the genuine needs of industry.

7.23 The measures adopted by the Reserve Bank of India (RBI) to restrain money supply and bank credit in the last few years were discussed in previous Economic Surveys. An important recent development in credit policy pertains to the instructions issued by the RBI to commercial banks in December 1980 regarding modifications to be carried out in respect of cash credit arrangements. The major changes required to be carried out by all commercial banks in respect of borrowers with aggregate working capital limits of Rs. 50 lakhs and over from the banking system were: (a) raising of borrower's contribution to working capital to at least 25 per cent of current assets and in cases where this became infeasible, conversion of the excess over the permissible limits into a working capital term loan with a definite payment schedule, (b) fixing of separate limits for peak and non-peak seasons and (c) conversion of cash credit limits into drawee bill limits wherever possible. The other requirements related to regulation of drawals of funds through quarterly review of all working capital limits of Rs. 10 lakhs and above, submission of half yearly returns by banks to RBI of accounts overdue for review, and charging of 1 per cent penal interest on total outstanding from units which failed to furnish quarterly returns. These measures were designed to promote a more rational management of funds by commercial banks.

7.24 Simultaneously with the presentation of the Union Budget, 1981-82, significant changes were made in interest rates in order to rationalise interest rates structure. The interest rates on bank deposits, last revised on September 13, 1979, were adjusted upwards on March 2, 1981 with a view to promoting savings. The maximum rate was retained at 10 per cent but the period of maturity was reduced from 5 years to 3 years. Interest rates were increased

from 7 per cent to 7.5 per cent on deposits of maturity of one year and above but less than two years, and to 8.5 per cent for deposits of two years and above but less than three years. Smaller scheduled commercial banks and regional rural banks were given the discretion to offer  $\frac{1}{2}$  to  $\frac{3}{4}$  per cent higher interest on deposits of maturities up to three years and on savings deposits. Co-operative banks were given the discretion of paying additional interest in respect of both term and savings deposits, the addition ranging from  $\frac{1}{4}$  per cent in the case of State Co-operative Banks to 1 per cent in the case of primary co-operative societies. Moreover, these banks could also pay additional interest over the maximum rate of 10 per cent applicable to other banks.

7.25 Alongwith the restructuring of interest rates payable on deposits, the lending rates of commercial banks were also rationalised. This was aimed at reducing the existing number of specified rates, introduce better gradation in the interest rates charged to various categories of borrowers in the priority sector and ensure uniformity in maximum lending rate charged by larger and smaller commercial banks. It was also intended to restrain the growth of credit through an increase in average interest rates.

7.26 An important feature of the new lending rates structure was the introduction of four slabs of lending rates for four different categories of agencies dealing with procurement and distribution of commodities. These four slabs were (i) 12.5 per cent—applicable to advances to agencies like FCI for procurement of foodgrains under the full price support scheme; (ii) 15 per cent—applicable to advances to Central and State Government agencies engaged in procurement/distribution of specified essential consumer commodities viz. pulses, edible oils, kerosene, salt and sugar; (iii) 17.5 per cent—applicable to advances to Central and State Government agencies dealing with the procurement and distribution of essential consumer commodities other than those specified in (i) and (ii) above and also engaged in procurement of cash crops like jute as well as in procurement and distribution of fertilisers, pesticides and seeds and (iv) 19.5 per cent—chargeable on advances to Central and State Government agencies engaged in the procurement/distribution of commodities for sale on a commercial basis. Alongside, the lending rates of regional rural banks and co-operative banks were also suitably changed in order to align these rates with the lending rates of commercial banks.

7.27 The minimum lending rates for loans/advances/cash credit/overdrafts against commodities subject to selective credit control were revised upwards. The rate applicable for advances to sugar mills was raised from 16.7 per cent to 17.5 per cent and that on other advances from 19.4 per cent to 19.5 per cent. The interest rates for export credit were also raised. The Special (lower) rate applicable to cotton textile mills in respect of approved stocks was abolished. However, the rates for housing loans were liberalised.

7.28 Along with the changes effected in lending rates of banks on March 2, 1981, the basic lending rate of IDBI was also raised from 11.85 per cent to 14 per cent. The interest rate under the IDBI's refinance scheme, applicable to medium sized units was raised marginally from 13.5 per cent to 14 per cent. The scope of interest rate concession given to projects in specified backward areas was narrowed down by limiting such concessions only to new units and the rate was set at 12.5 per cent. Other term lending institutions followed IDBI's move towards revision of interest rates upwards.

7.29 In view of the persistent inflationary pressures, the RBI issued general guidelines to commercial banks in May 1981 urging them to ensure that non-food credit expansion in the slack season as also in the entire financial year did not exceed the expansion in the corresponding previous periods. Subsequently, several measures aimed at restraining credit expansion were announced. The Cash Reserve Ratio (CRR) was raised in two phases : from 6 per cent to 7 per cent in two stages : 6.5 per cent from the last Friday of July 1981 and 7 per cent from August 21, 1981. The CRR was further increased to 8 per cent in October 1981. This change was to be effected in four stages : 7.25 per cent from November 27, 1981; 7.5 per cent from December 25, 1981; 7.75 per cent from January 29, 1982 and 8 per cent from February 26, 1982. The Statutory Liquidity Ratio (SLR) was also raised from 34 per cent to 34.5 per cent from September 25, 1981 and to 35 per cent from October 30, 1981.

7.30 The discretionary refinance and rediscounting rates were revised upward with a view to discouraging banks from seeking refinance from the RBI. The minimum interest rate on refinance was increased from 11 per cent to 14 per cent with effect from June 1, 1981. This would not, however, affect the lending rates of banks. Moreover, it was impressed upon the banks that the facility of refinance would be available only for short periods and in exceptional circumstances and that, too, subject to the satisfactory maintenance by banks of the stipulated reserve requirements. The rediscount rate for bills was similarly raised from 11 per cent to 14 per cent for the first tranche and further tranches would attract even higher rates of interest. The facility of stand by refinance provided for meeting clearing imbalances for two-three days at a time was continued at the existing rate of 11 per cent. However, it was stipulated that effective June 1, 1981, this facility would be provided only against the collateral of Government and Trustee Securities.

7.31 The bank rate was raised from 9 per cent to 10 per cent with effect from the close of business on July 11, 1981. Consequent to this change in Bank Rate, food and export refinance rates were raised from 9 per cent to 10 per cent with effect from July 18, 1981. The refinance rate against shipping loans was raised from 10.5 per cent to 11.5 per cent and that against loans for import of capital goods was

raised from 9 per cent to 10 per cent with effect from the close of business on July 11, 1981. The on-lending rate was raised from 11 per cent to 12 per cent in both the cases.

7.32 In recognition of the need for the flow of finance to the export sector and for food procurement, the commercial banks lending rates for food procurement and export credit were kept unchanged. Banks were asked to expedite extension of credit to exporters and to provide all possible ancillary facilities to them in view of the paramount importance of increasing exports in the context of difficult balance of payments situation.

7.33 Appropriate adjustments were also introduced in the selective credit controls for sensitive commodities. The minimum margins against stocks of wheat, paddy, rice and other foodgrains were raised by 10 percentage points with effect from July 13, 1981, with the exception of advances to roller flour mills against wheat and advances against pulses. However, selective credit control concerning sugar was adjusted subsequently in view of the likely increase in production and stocks. The margin requirement of 25 per cent on advances granted by scheduled commercial banks to sugar mills against security of sugar produced during 1980-81 season was relaxed. The actual quantum of relaxation was to the extent of the deficit in the margin arising from the Government's decision to acquire 4 lakh tonnes of levy free sugar as levy sugar out of current season's production for public distribution during October and November 1981. This relaxation which was effective till January 31, 1982 covered stocks which had not been released for sale by the Government and had not left the factory premises and on which excise duty had not been paid.

7.34 The period of extra credit given by commercial banks to jute mills for purchasing four weeks' consumption for raw jute from the Jute Corporation (in addition to the credit given for carrying stocks for ten weeks consumption as per the norms of the Tandon Committee) was extended further up to the end of January 1982. Besides, banks were permitted to grant additional *ad hoc* accommodation to jute mills for the purchase of raw jute equivalent to two weeks' consumption during the peak marketing period from November 1981 to January 1982.

7.35 The credit flow to the priority sectors, and within them to the weaker sections of the society was further increased. General guidelines were issued to banks to increase their advances to priority sectors in such a way that these advances constituted 40 per cent of aggregate bank advances by 1985. Further, 40 per cent of the priority sector advances should be earmarked for agriculture and allied activities so that this sector accounted for at least 16 per cent of total advances by 1985. Specific measures were also taken to ensure that the weaker sections within the priority sectors received the maximum benefit. Weaker sections were specifically defined within the agriculture and small industry sectors and banks were advised to

ensure that at least 50 per cent of their direct advances went to agriculture, and at least 12.5 per cent of their total finance to small scale industries flowed to the weaker sections by March 1985.

7.36 The Differential Rate of Interest (DRI) Scheme was further extended by including the private sector banks so that its coverage extended to the entire country. Private sector banks were directed to ensure that at least two-thirds of their advances under this scheme were routed through their rural and semi-urban branches. The scheme was also modified to allow banks to route such advances through Regional Rural Banks (RRBs) on refinance basis. Target groups which are beneficiaries of the 20-Point Programme were also identified within the priority sectors. The scope of advances to priority sectors was widened to cover housing loans for scheduled castes/tribes and economically weaker sections and also cover consumption loans under the 20-Point Programme. Banks were asked to give special attention in providing assistance to the beneficiaries of the 20-Point Programme within the district credit plans. Lending procedures of banks were simplified further to ensure the disposal of small loan applications within three to four weeks of applications. Security and margin requirements were also relaxed for this purpose. For example, banks were to take only Demand Promissory Notes for crop loans of up to Rs. 1,000. For artisans, craftsmen and village and cottage industries, the banks were not to insist on securities other than hypothecation of assets. Moreover, the Integrated Rural Development Programme (IRDP) was extended to all blocks with a view to providing greater financial assistance to the weaker sections of the society.

7.37 As discussed earlier, advances to priority sectors increased and the rising trends of advances to priority sectors was maintained in 1981-82. The DRI Scheme was also showing encouraging progress. According to preliminary estimates, the total outstanding advances by public sector banks under this scheme amounted to Rs. 189.96 crores involving 24.7 lakh borrowers at the end of December 1980. The figures at the end of December 1976 were Rs. 47.24 crores and 10.0 lakh borrowers and at the end of December 1979 the corresponding figures were Rs. 140.96 crores and 20.8 lakh borrowers. Advances made by private sector banks (excluding six newly nationalised banks) under the scheme amounted to Rs. 90 lakhs covering 10,460 borrowal accounts at the end of June 1980. Similarly, the flow of bank credit to IRD Programme showed an increase. During 1979-80, the credit mobilised through commercial banks for the programme was Rs. 85 crores compared with Rs. 63 crores from co-operatives. In 1980-81, the credit from commercial banks increased to Rs. 124 crores and that from co-operatives to Rs. 74 crores.

7.38 In order to strengthen the institutional arrangements for the supply of credit to agricultural and rural sectors, the Government enacted legislation to

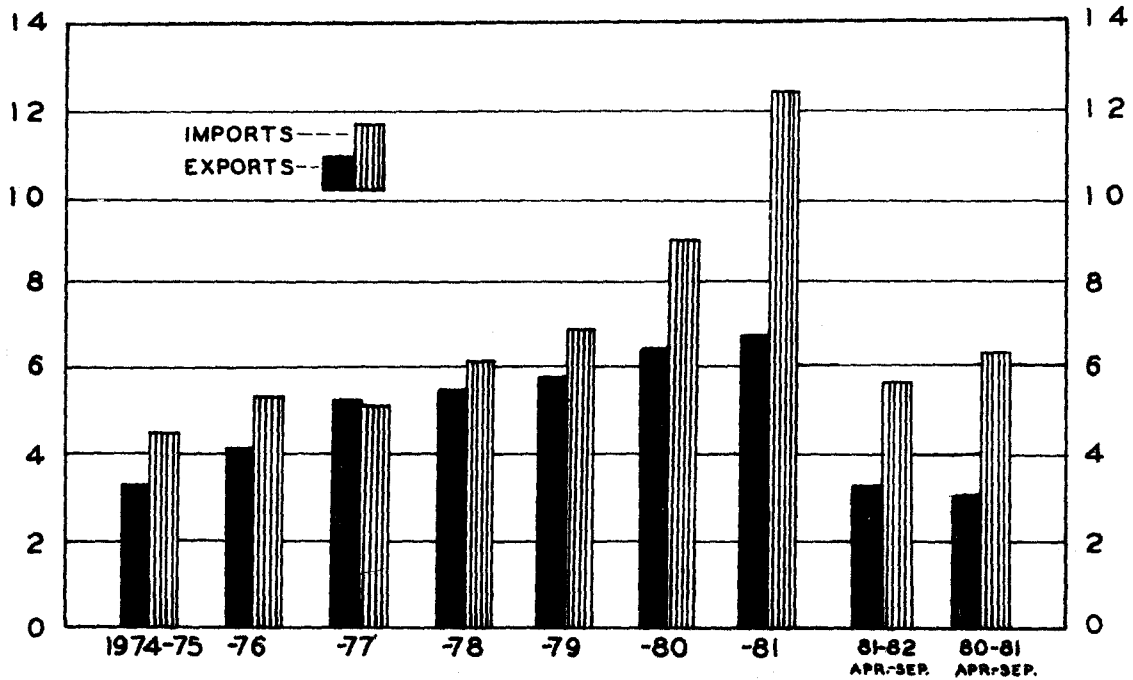
set up a new apex bank viz. the National Bank for Agriculture and Rural Development (NABARD). The NABARD will be responsible for short term, medium term and long term financing of agricultural and allied activities and for overseeing the entire rural credit system including the statutory inspection of co-operative banks and Regional Rural Banks (RRBs). The authorised share capital of the NABARD is Rs. 500 crores and the paid up capital Rs. 100 crores which will be contributed equally by the RBI and the Government of India. The National Agricultural Credit (Long Term Operations) Fund with the RBI is now proposed to be transferred to the NABARD to form part of its National Rural Credit (Long Term Operations) Fund which could be used for providing term loans. The NABARD is also permitted to raise resources from the Government and the market. It can also draw on the assistance from RBI for short term credit and working capital loans.

7.39 Recognising the importance of exports in the country's development programmes, the Government has set up an Export-Import (EXIM) bank which started functioning from 1st January, 1982. The EXIM bank would provide financial assistance to exporters and importers and function as the principal financial institution for co-ordinating the working of other institutions engaged in financing exports and imports. It would also provide refinance facilities to commercial banks and financial institutions against their export-import financing activities. Broadly, the functions of the EXIM bank include (a) financing of exports from and imports into not only India but also third countries, (b) financing of joint ventures of foreign countries, (c) financing of export and import of machinery and equipment on lease basis and (d) providing loans to Indian parties to enable them to contribute to the share capital of joint ventures in a foreign country. The EXIM bank would take over the functions of the international finance department of the IDBI. It would have an authorised capital of Rs. 200 crores which may be subsequently raised to Rs. 500 crores. The paid up capital is Rs. 50 crores which is proposed to be raised to Rs. 200 crores by 1987-88. The bank is also empowered to raise resources through market borrowings at home and abroad. It is contemplated that gradually the EXIM bank would have branches in major cities of India and abroad.

7.40 In sum, it would appear that the monetary trends are broadly consistent with the aims of policy. The expansion of money supply with the public ( $M_1$ ) will be lower during the year and expansion in aggregate monetary resources ( $M_2$ ) is likely to be contained despite continued buoyancy in time deposits. The flow of credit to priority sectors will be higher and the higher expansion of overall bank credit is explained by larger food procurement, imports and the continued improvement in industrial activity and investment climate. However, although inflationary pressures in the economy have abated during the year, the credit policy has to continue emphasising the need for greater discipline in credit creation.

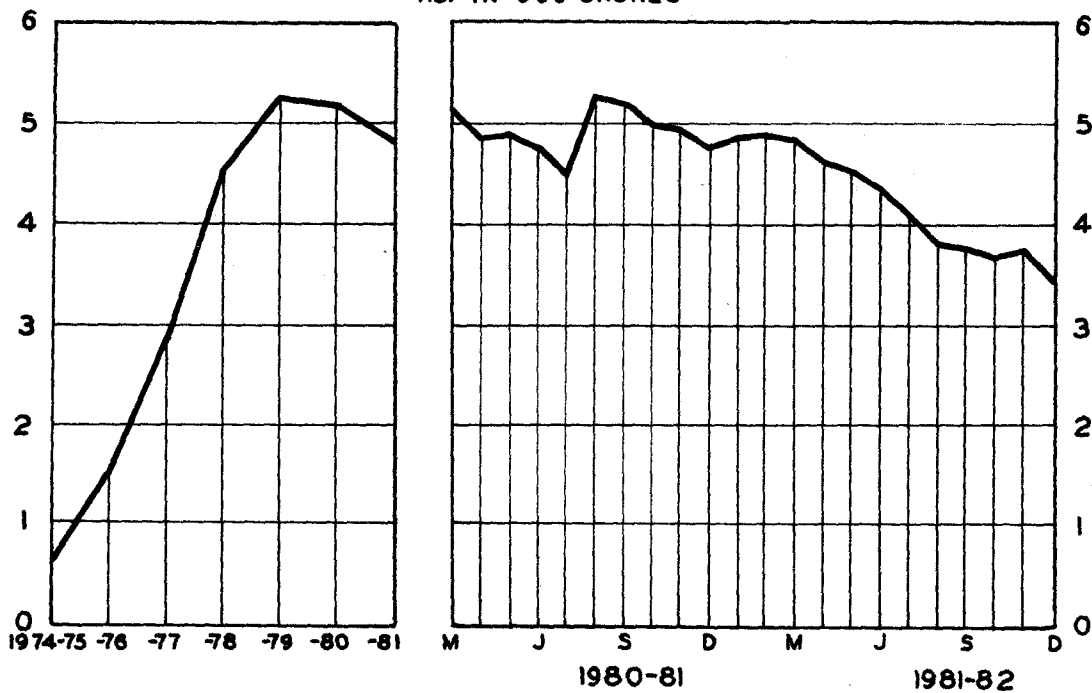
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