THE FORMATIVE YEARS: 1935-39

4

The Beginnings

The Reserve Bank of India Act was placed on the Statute-book on March 6, 1934. It was, however, not before another year had passed that the Bank was inaugurated. The Government of India were keen on starting the Bank as early as possible, especially in view of the fact that the Reserve Bank Bill had been rushed through the Legislature in a special session. It would also appear that Sir George Schuster, who had piloted the Bill, was keen to establish the Bank at an early date since he was laying down office. As Finance Member shortly, that is to say, sometime in the spring of 1934. The Government's proposals were that the appointments of the Governor, Deputy Governors- and the Central Board should be made early in 1934 to enable the issue of shares in that summer, which was regarded as likely to be particularly favourable for such an operation. However, the Secretary of State for India favoured a somewhat leisurely time-table, for several reasons. In the first place, apart from the time necessary to make the preliminary arrangements, some of the pre-conditions envisaged for the establishment of the Bank, such as improvement of the budgetary position of the Government and the return of the normal export surplus, required to be fulfilled. The Home authorities also desired that the international monetary situation should clear up, a consideration that had been fully recognised in the Preamble to the Act! Further, the Secretary of State was of the view that ' it would be unfair to hasten the opening of the Reserve Bank until he (the new Finance Member) has had an opportunity of acquainting himself personally with the situation on the spot and-been able to form his own judgment on matters '. A suggestion emanating from the Government of India that the Bank should start without the function of currency regulation was rejected by the Secretary of State. In the end, a compromise emerged in that the Bank started functioning not as early as the Government of India had desired but not so late as the Secretary of State had envisaged.

The provisions of the Act relating to the constitution of the Bank, issue of share capital and establishment of Central and Local Boards became operative from January 1, 1935, under a notification issued by the Government of India on December 20, 1934. The appointment of the first Governor and the nomination of the first Central Board of Directors were also made under the same notification and became effective simultaneously. The first two Deputy Governors were designated in October 1934, but assumed office only from the middle of February 1935. The Central Board of Directors held its first meeting on January 14, 1935, in Calcutta, and considered matters relating to staff, premises, issue of share capital, agreements with the Government and the Imperial Bank of India, regulations regarding scheduled banks and a host of other matters relating to the organisation of the Bank. The Board finalised the organisational preliminaries at its second meeting held in Delhi, on February 23, 1935. The Board also decided to issue the share capital of the Bank at par, after discussing at length proposals for a premium issue mooted by the Government. The issue of shares to the public was made in March and the Bank was formally inaugurated on Monday, April 1, 1935. The launching of the Bank on the first day of the fiscal year was also influenced by considerations of administrative convenience for the change over of Government accounts from the Imperial Bank to the Reserve 'Bank.

On the occasion of the inauguration of the Bank, the Secretary of State for India sent the following message to the Governor:

> As Reserve Bank commences active operations today I take opportunity to convey to you and your colleagues on the Board my most cordial good wishes and to express my confidence that this great under taking will contribute largely to the economic well-being of India and of its people.

Replying on behalf of the Deputy Governors, the Board and himself, the Governor assured the Secretary of State,

> that their utmost endeavour will be to promote the economic wellbeing of India and thereby completely justify the institution of the Reserve Bank of India.

The Bank began operations by taking over from the Government the functions hitherto performed by the Controller of the Currency and from the Imperial Bank of India the management of Government accounts and public debt. The then existing Currency Offices in Calcutta, Bombay, Madras, Rangoon, Karachi, Lahore and Cawnpore became the branches of the Issue Department of the Bank. As the Currency Offices in Lahore and Cawnpore were considered to be adequate for the Northern Area, the Office of the Deputy Controller of the Currency in Delhi had been abolished before the Reserve Bank took over. Hence it was not considered necessary to open an office of the Issue Department in Delhi. Offices of the Banking Department* were established in Bombay, Calcutta, Madras, Delhi and Rangoon, which took over the conduct of Government Treasury business at all those places and the management of public debt in Bombay, Calcutta and Madras, from the Imperial Bank of India. At other places where branches of the Imperial Bank were then doing Treasury business, the Reserve Bank appointed the Imperial Bank as its agent for the conduct of such business. The management of Government Treasuries operating at places where the Imperial Bank had no branches also came under the control of the Reserve Bank.

The Bank's first statement of its affairs, as at the close of Friday, April 5, 1935, is given on page 124. The formal assumption of the functions of a bankers' bank came a little later, on July 4, 1935, when the first official Bank rate was announced, followed by the lodgement with it the next day of the statutory deposits of scheduled banks in accordance with the provisions of Section 42 of the Reserve Bank of India Act; the latter was deliberately timed to take place in the slack season, so as not to cause 'considerable and unnecessary embarrassment' to the scheduled banks. However, some banks had begun maintaining balances with the Reserve Bank even earlier, particularly the Imperial, which did so from the beginning, that is, April 1.

Governor and Deputy Governors

The appointment of the first Governor was regarded as 'a point of vital importance'. It would seem that, as early as December 1933, the Viceroy had sent his personal recommendation in this matter to the Secretary of State. What that recommendation was is not known. Even in February 1934, officials in Delhi connected with the Reserve Bank matters did not know whether the Governor to be was a person who had Indian experience or not. Anyway, on November 29, 1934, the post was offered to and accepted by Sir Osborne Arkell Smith, then one of the two Managing Governors of the Imperial Bank of India, the term of office being three and a half years.

An Australian national, Sir Osborne, then in his late fifties had behind him a life time devoted to banking service; after nearly 20 years in the Bank of New South Wales, the largest Australian trading bank, he joined the Commonwealth Bank of Australia, which he served in

* The Bank also created agencies, i.e., restricted branches of its Banking Department in the branches of the Issue Department at Cawnpore, Lahore and Karachi.

(Rs. crores)

ISSUE DEPARTMENT

LIABILITIES		ASSETS	
Notes held in the Banking Department	19.05	A. Gold Coin and Bullion:	
		(a) Held in India	41.55
		(b) Held outside India	2.87
Notes in circulation	167.00	Sterling Securities	48.63
Total Notes issued	186.05	TOTAL OF A	93.05
		B. Rupee Coin	49.95
		Government of India Rupee Securities	43.05
		Internal Bills of Exchange and other commercial Paper	
Total	186.05	Total	186.05

Ratio of Total of A to Liabilities: 50.013 per cent.

BANKING DEPARTMENT

LIABILITIES		ASSETS	
Capital paid up	5.00	Notes	19.05
Reserve Fund	5.00	Rupee Coin	0.04
Deposits:		Subsidiary Coin.	0.01
(a) Government	18.36	Bills Purchased and Discounted	
(1) Central Government of India		(a) Internal	
(2) Government of Burma		(b) External	
(3) Other Government Accounts		(c) Government Treasury Bills	
		Balances held abroad*	11.95
(b) Banks	7.82	Loans and Advances to Governments	
(c) Others	0.01		
Bills Payable		Other Loans and Advances	
Other Liabilities	0.02	Investments	5.00
		Other Assets	0.16
Total	36.21		36.21

* Includes Cash and Short-term securities

various responsible positions for over a decade, and learned his lessons in central banking. He was its London Manager when he joined the Imperial Bank of India as a Managing Governor in 1926. The circumstances under which he was appointed Governor are described by Sir C. D. Deshmukh, as follows:

> Plans, characteristic of the foresight that the British bring to bear on public affairs in order to preserve what they regard as their own legiimate 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 him self and his sponsors, appointed first Governor of the Reserve Bank in 1935.*

According to Lord Norman's biographer, Sir Henry Clay, Sir Osborne Smith's appointment as a Managing Governor of the Imperial Bank and later as the Governor of the Reserve Bank, had been recommended by Lord Norman. Sir Osborne's reputation as a banker was quite high; his successful stewardship of the Imperial Bank through the difficult years of depression and the salutary reforms he carried out for remodelling its working had received wide recognition. The testimony of the contemporary press indicates that his appointment as Governor of the Reserve Bank was well received in financial and business circles. ' The choice of Sir Osborne Smith is the one aspect of the Reserve Bank in which the entire newspaper world, both at Home and in India, English and vernacular, has been unanimous', was the comment of the Capital†; the Indian Finance‡ echoed the same sentiment when it stated 'Here is just the round peg in the round hole '. There is, however, an element of amusing irony in the first Governor of the Reserve Bank happening to be a man of ' tested banking experience' when one recalls the acrimonious debates on the Reserve Bank Bill in the Legislative Assembly, and the uncompromising stand taken by Government spokesmen to have this provision deleted. Apparently, while a British Governor could have been picked from the higher administrative ranks of the appropriate services of the Government of India (indeed Mr. Taylor himself), there was a desire to have as the first Governor someone outside the Government, in order to demonstrate the principle of independence of the Bank about which very strong sentiments had been professed by Government. However, as it happened, Sir Osborne was not destined to stay for long.

The first Deputy Governors of the Bank were Mr. (later Sir) James Braid Taylor and Sir Sikander Hyat-Khan, appointed for terms of office not exceeding five years. Sir James belonged to the Indian Civil Service; after working in the C. P. and Berar Government for some time, he moved to the Government of India, which he served for over a decade mainly as Deputy Controller and Controller of the Currency. Later, as Additional Secretary in the Finance Department, he was intimately associated with the preparation and the piloting of the 1933 Reserve Bank Bill. The task of planning the organisation and administration of the Reserve Bank was entrusted to Sir James, whose

* Central Banking in India -A Retrospect.

† March 14, 1935. ‡ March 8, 1935.

knowledge of the details of administration was extraordinarily close. The appointment of Sir Sikander Hyat-Khan fulfilled the assurance given in the Legislature by Sir George Schuster, Finance Member, that one of the top executive posts of the Bank would be filled by a qualified Indian. Sir Sikander was a distinguished political figure and an administrator, having been a Member of the Punjab Legislative Council for long and Acting Governor of the Punjab. However, he did not continue in office for long.

One of the terms of appointment of Mr. Taylor was that he should resign from the Indian Civil Service with effect from the date on which he would take up duty as Deputy Governor. It would appear that this condition was proposed by the Secretary of State for India. Apparently, this was done to ensure the independence of the Governor and the Deputy Governors, in conformity with the prevailing philosophy.

In 1953, the Government desired that this requirement be waived in the case of persons appointed to the post of Deputy Governor, but the proposal did not find favour with the Central Board of the Bank and the Government did not pursue the matter.

It was also a condition of appointment that Mr. Taylor's pension as a Government servant would be held in abeyance so long as he was an executive of the Bank. This condition has also remained operative to this date. But here again, several years later, consideration was given to amending the provision to enable the appointee to draw the pension with an equivalent reduction in the salary drawn from the Bank, but it was decided to make no change, except that permission was to be given for commutation of a portion of the pension. The significance of this requirement has been explained thus:

> The principle underlying this stipulation is apparently that officers holding the post of Governors and Deputy Governors should draw their entire salaries from the Bank and should devote their whole attention to the affairs of the Bank, in the conduct of which they should be able to act independently.

Central Board of Directors

Under the Bank's Statute, apart from the four Directors to be nominated under Section 8(1) (b), the first eight Directors representing shareholders on the various registers were also to be nominated by the Governor General in Council from the areas respectively served by these registers [Section 15(3)]. At the end of each successive year after the first nomination of the Directors representing the shareholders, two of them were to retire and be replaced by Directors elected is the manner provided under Section 9. The Joint Select Committee on the Reserve Bank of India Bill had indicated in its report that the power of nomination by the Governor General under Section 8(1)(b) should be exercised with a view to securing representation of territorial or economic interests, and in particular the interests of agriculture and co-operative banking, if these did not secure adequate representation from among the elected Directors. As regards the nomination to the first Board, of Directors representing shareholders, the Committee had made no specific recommendation as it was satisfied with the assurance given on behalf of the Government that such nomination would provide for proper representation of Indians. The Committee had also made it clear that it did not consider anything less than 75 per cent of the voting Directors as constituting a proper representation of Indians.

Although there were no specific stipulations regarding the manner in which the Governor General should exercise his power, the nomination of the first Directors representing the shareholders was done after consultation with the Governors of Provinces and their respective Governments. The choice of persons appears to have been largely influenced by the desirability of affording representation to the various prominent business classes as well as communal interests. While these considerations were kept in view, the choice of individuals was based on their competence and suitability for fulfilling their responsibilities.

The consultation with the Provincial Governors was no mere formality and their views appear to have been given due weight in the final nomination of persons. In one instance, the person suggested by the Government of India was not favoured by the Governor as he did not consider that he 'could be trusted to be impartial as a Director in respect of any issue affecting the interests of himself, his class or his family'. The same Governor found it difficult to approve of another person as he was 'a staunch Congressman and a member of the All India Congress Committee . . . . . who had used the co-operative machine in order to strengthen the hold of the Congress over the population of. . . . . . 'As an alternative, another person was suggested who would be 'an admirable representative of the interests of the co-operative movement '.

The Directors of the first Central Board, other than the Governor, the Deputy Governors and the Government official (Mr. J. W. Kelly, Controller of the Currency), were as under:

Directors nominated under Section 8(1) (b)

Sir Homi Mehta, Kt., Bombay.
Mr. A. A. Bruce, Rangoon.
Lala Shri Ram, Delhi.
Khan Bahadur Adam Hajee Mohammad Sait, Madras.

Directors nominated under Section 15(3)

(1) *Bombay register*
Sir Purshotamdas Thakurdas, Kt., C.I.E., M.B.E.
Mr. F. E. Dinshaw.

(2) *Calcutta register*
Sir Edward Benthall, Kt.
Rai Bahadur Sir Badridas Goenka, Kt., C.I.E.

(3) *Delhi register*
Khan Bahadur Nawab Sir Muzammilullah Khan, K.C.I.E., Aligarh.
Sir Sundar Singh Majithia, K.C.I.E., Amritsar.

(4) *Madras register*
Dewan Bahadur M. Ramachandra Rao, Kt.

(5) *Rangoon register*
U Bah Oh.

On the first Board, the comment of Indian Finance* was as follows:

> The composition of the first Board is one on which the Government do deserve to be congratulated. They have brought together as fine a team as is possible in India. There are at least four or five members of that Board who will exercise such influence and have such a big say that the country may rely upon the functioning of that Board in a way that will prove beneficial to India.

In terms of the Bank's General Regulations, a Committee, to be called the Committee of the Central Board, was constituted to attend to the current business of the Bank. The Committee was vested with full powers to transact all the usual business of the Bank except in such matters as were specifically reserved by the Act to the Governor General in Council, a general meeting of shareholders or the Central Board. The Committee consisted of the Governor, the Deputy Governors, the Directors representing the shareholders of the area in which the meeting was held, the nominated Director resident in such area and the Government Director. The weekly meetings of the Committee were generally held on Wednesdays, this being a convenient day for consideration of the weekly statement of affairs of the Bank of the preceding Friday; this practice continues to this day. The first meeting of the Committee was held on April 10, 1935 in Calcutta. Likewise, a Committee was constituted for each of the Local Boards.

* March 8, 1935.

Sir Osborne A. Smith
Governor, 1935-37

Issue of Share Capital

The Memorandum of Procedure for the issue of shares of the Bank was adopted by the Central Board of the Bank at its meeting on February 23, 1935, in consultation with the Committee of the Legislature appointed under sub-section 5 of Section 4 of the Reserve Bank of India Act and consisting of Hon'ble Mr. Hossain Imam, Mr. Sri Prakasa and Seth Hajee Abdoola Haroon. The announcement of the issue was made on March 8, 1935 and given wide publicity through the medium of English as well as Indian language papers and journals. The shares were issued at par, the cumulative dividend-payable in accordance with the provisions of the Act having been fixed at 3 ½ per cent under a notification dated March 2, 1935, issued by the Governor General in Council. The actual floatation of shares was entrusted to the Imperial Bank of India on a commission of l/8 of 1 per cent of the nominal value of shares receiving allotment; a brokerage of not more than 1/16 of 1 per cent was also allowed. Arrangements were made for receiving applications at 574 centres, comprising offices and branches of the Imperial Bank of India, Treasuries and head post offices.

The Bank's share issue appears to have evoked widespread interest. This was in large measure due to the propaganda carried in the nationalist press urging the people to acquire as large a number of shares as possible so as to avoid control of the Bank- a symbol of India's growing financial autonomy-getting into the hands of 'an exploiting group or caucus'. One Bombay journal wanted every Indian with the money 'to make an effort to secure the minimum of 5 shares that will entitle him to a vote and hold it as a public trust, refusing to part with it to others on any terms '. Appeals of this sort naturally led to widespread expectation that the shares would appreciate in value at no distant date. Indeed, there were rumours that some brokers were dealing in shares of the Reserve Bank at a premium ranging up to Rs. 25 even before the issue of shares had been completed.

The lists remained open for four days from March 22 to March 25, and the issue was oversubscribed to the extent of nearly Rs. 5 crores or 100 per cent, the total number of applications received being 1,34,558. The number of applications for five or more shares in respect of the Bombay, Delhi and Madras registers exceeded the limit of 1/5th of the total number of shares assigned to each of those registers. Accordingly, all applications for less than five shares became ineligible for allotment, while applications for five or more shares which were successful in the drawing of lots received only a minimum allotment of five shares. The position was different in respect of the Calcutta and Rangoon registers, where the number of applications for five or more shares fell short of the limit of 1/5th of the number of shares assigned to those registers. As a result, all such applicants received at least a minimum allotment of five shares; applications for less than five shares also did not involve drawing for allotment. The entire share capital was allotted to the public, with the exception of shares of the nominal value of Rs. 2.2 lakhs which were assigned to the Central Government under Section 4(8) of the Reserve Bank of India Act, to be held for disposal at par to Directors seeking to obtain the minimum share qualification. The number of original shareholders on the various registers was as follows: Bombay 28,000, Calcutta 23,890, Delhi 23,000, Madras 14,000 and Rangoon 3,157.

Organisational Preliminaries: Senior Staff

The initial task in organising the activities of the Bank was to engage suitable personnel and locate premises. Obviously, the most convenient solution to the problem of manning the new institution was to utilise the services of staff of the Currency Offices of Government and the Imperial Bank of India engaged in the performance of functions taken over by the Bank. The junior staff of the Currency Offices were taken over on a permanent footing while those of the Imperial Bank came over initially on a temporary basis and were subsequently absorbed. The transfer of staff in both cases was arranged on the existing conditions of pay and service. By and by, new staff, at the clerical level, were recruited. The employment situation was such that there was a tremendous rush of applications for jobs in the Bank.

For manning the higher positions, the Bank secured the services of Currency Officers from the Government of India and senior officials from the Imperial Bank. Currency Officers whose services were lent by Government were posted to take charge of the branches of the Issue Department of the Bank, while a senior Government official of the rank of a Currency Officer was assigned for the periodical inspection, audit and verification of those offices. Senior officers from the Imperial Bank were appointed as Secretary to the Central Board and the Managers of the five offices of the Banking Department. Mr. S. S. Rachhpal, who was appointed to the post of Secretary to the Central Board in January 1935, went back to his parent institution-the Imperial Bank-in June 1935. The Secretary's work came to be looked after by Mr. K. G. Ambegaokar, I.C.S., who had been earlier appointed as Officer-in-Charge of the Agricultural Credit Department. Messrs R. A. B. Allan, W. T. McCallum, W. J. Lutley, A. J. Elder and J. N. Ahuja became the Managers of Calcutta, Bombay, Delhi, Rangoon and Madras Offices, respectively. The position of the Chief Accountant of the Bank was taken over at the beginning of 1935 by Rai A.C. Mukherji Bahadur, who was then Deputy Controller of the

Currency at Calcutta, and on his resignation for reasons of health, shortly before the formal inauguration of the Bank, Mr. (later Sir) C. R. Trevor, a senior official of the Imperial Bank, was appointed in his place.

The only official to be brought in from abroad was Mr. E. V. M. Stockdale of the Bank of England, who was appointed temporarily as Personal Assistant to the Governor, for introducing in the Bank up to date central bank book-keeping methods. Later, in October 1937, another official of the Bank of England, Mr. P. S. Beale, was brought in as Secretary of the Bank, on account of his experience as a practical banker. This was at a time when the search for a European Deputy Governor was being pursued. It is not unlikely that Sir James Taylor intended this appointment to satisfy to some extent the protagonists of a European Deputy Governor. Mr. Beale returned to the Bank of England soon after the outbreak of war in September 1939.

Office Accommodation

As in the case of the staff, the accommodation of Bank's offices at the various centres was also arranged by leasing the premises of the Government and the Imperial Bank, where the staff taken over from them were wont to function; it is, however, interesting to mention that the India Office had been keen that in respect of accommodation and staff the Bank should be quite independent of commercial banks, to impress on people that the Reserve Bank was a different institution altogether. In Calcutta, the Issue Department of the Bank started functioning in the old Currency Office, while the premises of the Alliance Bank, leased from the liquidators by the Imperial Bank of India, were utilised to house the Banking Department and the Central Office of the Bank. In Bombay, the Issue Department opened in the erstwhile Currency Office building at Esplanade Road and the Banking Department in the Imperial Bank building. More or less similar arrangements were made at other centres also. Soon the Bank embarked on a comprehensive building programme; the Bombay and Rangoon buildings were completed in March 1939, and the Lahore building in January 1940. Construction of the Bombay building was begun in 1937; the work was entrusted to Messrs Shapoorji Pallonji & Co., who worked under the supervision of Messrs Palmer & Turner, Consulting Architects, and Messrs Gregson, Batley & King, Supervising Architects. The building cost Rs. 25.55 lakhs, exclusive of the cost of land. The Rangoon and Lahore buildings cost about Rs.10 lakhs and Rs. 6 lakhs, respectively.

The Bank's Seal

A brief account of the selection of the Bank's common seal should also be of interest. Special care was taken to choose the sketches for the seal as, at a later stage, it was to be used as the emblem of the Bank on currency notes, cheques and publications. The Government's general ideas on the seal were as follows:

(1) the seal should emphasise the Governmental status of the Bank but not too closely;
(2) it should have something Indian in the design ;
(3) it should be simple, artistic and heraldically correct ; and
(4) the design should be such that it could be used without substantial alteration for letter heading, etc.

For this purpose, various seals, medals and coins were examined.The East India Company Double Mohur, with the sketch of the Lion and Palm Tree, was found most suitable; however, it was decided to replace the lion by the tiger, the latter being regarded as the more characteristic animal of India!

To meet the immediate requirements in connection with the stamping of the Bank's share certificates, the work was entrusted to a Madras firm. The Board, at its meeting on February 23, 1935, approved the design of the seal but desired improvement of the animal's appearance. Unfortunately it was not possible to make any major changes at. that stage. But the Deputy Governor, Sir James Taylor, did not rest content with this. He took keen interest in getting fresh sketches prepared by the Government of India Mint and the Security Printing Press, Nasik. As a basis for good design, he arranged for a photograph to be taken of the statue of the tiger on the entrance gate at Belvedere, Calcutta. Something or the other went wrong with the sketches so that Sir James, writing in September 1938, was led to remark:

> . . . . . 's tree is all right but his tiger looks too like some species of dog, and I am afraid that a design of a dog and a tree would arouse derision among the irreverent . . . . . 's tiger is distinctly good but the tree has spoiled it. The stem is too long and the branches too spidery, but I should have thought that by putting a firm line under the feet of his tiger and making his tree stronger and lower we could get quite a good result from his design.

Later, with further efforts, it was possible to have better proofs prepared by the Security Printing Press, Nasik. However, it was eventually decided not to make any change in the existing seal of the Bank, and the new sketches came to be used as an emblem for the Bank's currency notes, letter-heads, cheques and publications issued by the Bank.

Regulations and Agreements

The early months of the Bank were taken up by activities of a preliminary nature, such as the preparation and conclusion of agreements with the Central Government for the management of public debt and

Government accounts and with the Imperial Bank of India for undertaking the work as the agent of the Reserve Bank. Besides, the Bank formulated detailed rules and regulations relating to matters covered under Section 58 of the Reserve Bank of India Act. These related mainly to General Regulations regarding the functioning of Central and Local Boards, Regulations regarding the relations of scheduled banks with the Reserve Bank and returns to be submitted by the former and Staff Regulations pertaining to service conditions of staff to be recruited by the Bank in future.

Elections to Local and Central Boards

The first elections to the Local Boards were held in November 1935 and these Boards were constituted soon after the Central Board of the Bank had nominated the remaining members from the panel of names furnished by the concerned Provincial Governments. In December, it fell to the lot of the elected members of the Local Board of the Western Area (Bombay) to elect two Directors to the Central Board for replacing those nominated by the Governor General in Council to represent that Area. Sir Purshotamdas Thakurdas and Mr. F. E. Dinshaw, who happened to be the erstwhile nominated Directors, were unanimously elected to the Central Board.

London Office

The London Office of the Bank (located at 31-33, Bishopsgate) was formally opened on October 14, 1935 and from April 1, 1936 it took over, from the Imperial Bank of India, the management of the rupee debt of the Government of India enfaced for payment in London and the accounts of the High Commissioner for India. The safe custody and investment of currency reserves held in London, which were being managed by the Bank of England on account of the Secretary of State, also became its responsibility. The Bank of England, however, continued to act as bankers to the Secretary of State on behalf of the Indian Government, and all transfers to the Home Government were to be paid by the Reserve Bank to the account of the Secretary of State with the Bank of England. The original arrangement was to appoint Sir Sikander Hyat-Khan, Deputy Governor, as the first Manager of the London Office for about a year, mainly, it would appear, to enable him to get training in finance and banking in this international centre. This, however, did not materialise and Mr. Ram Nath, who had joined the Bank from the Imperial Bank service, was its first incumbent. The significance attached to the London Office lay not so much in the handling of the routine banking and debt management functions, as in its vantage position for studying world finance and watching India's interests, in the centre of the sterling area with which India had the bulk of her foreign trade. With the co-operation of the 'Old Lady of Thread needle Street', the Bank's Office succeeded in keeping in close touch with events in the London money and capital markets.

Internal Organisational Set-up

The internal organisation of the Bank comprised two broad wings, namely, (i) Central Office units, constituting the direction of the Bank, under the immediate charge of the Governor and Deputy Governors and (ii) operational units, comprising the offices and branches of the Banking and Issue Departments. *

The Central Office of the Bank was divided into the Secretary's and the Chief Accountant's Sections and the Agricultural Credit Department. The Secretary's Section dealt primarily with the work which the Governor and the Central Board were directly concerned with (such as Board and Committee meetings, annual general meetings, correspondence with Central Government on matters of policy), the management of public debt, ways and means requirements of Central and Provincial Governments and all matters affecting the policies of the Bank. It is interesting to find that for over thirty years, that is to say, till July 1967, it was not the practice for the Secretary to attend meetings of the Central Board and its Committee!

The Chief Accountant's Section looked after the maintenance and supervision of the Bank's accounts in its Issue and Banking Departments. It also dealt with a variety of other matters such as Bank's expenditure, remittance of treasure and indent and distribution of notes and coin. Matters relating to staff and premises were also looked after by the Chief Accountant's Section. The set-up and functions of the Agricultural Credit Department, a statutory Department, are discussed in Chapter 7.

While the Central Office of the Bank was initially located in Calcutta, it was the practice for the Governor to spend his time about equally between Calcutta and Bombay, a portion of the Central Office moving with him to Bombay. Commenting on this practice, the Governor observed in August 1937 that:

> the experience of the last two years has shown that the present practice of migrating from one centre to another throws an impossible burden on the administration of the Bank and involves great waste of time and duplication of work.

* The offices of the Banking Department were located in Bombay, Calcutta, Delhi, Madras, Rangoon and London. The Issue Department had branches in Bombay, Calcutta,Madras, Rangoon, Cawnpore, Karachi and Lahore; restricted branches of the Banking Department were also maintained in the three last-mentioned places.

He suggested that the Central Office should be stationed permanently in Bombay and that the touring portion should be confined to the Governor's staff who would be responsible merely for keeping his personal correspondence and the records of the Committee and the Central Board. Accordingly, in December 1937, the Central Office was permanently transferred to Bombay.

As regards the operational units, the offices of the Banking Department, each under a Manager, were entrusted with transactions arising from the Bank's duties as banker to Government as well as to scheduled banks and were organised into five departments, viz., Public Accounts Department, Deposit Accounts Department, Public Debt Office, Securities Department and Share Transfer Department.

The Public Accounts Department received and disbursed monies on behalf of Central and Provincial Governments and maintained accounts of these transactions in the manner prescribed by the Treasury and account codes and the orders of the Accountants General. The Department collected cheques on behalf of Government and encashed interest warrants and repayment orders relating to Government loans. Government Treasury bills were also issued and repaid by this Department.

The Deposit Accounts Department maintained the statutory accounts of scheduled banks and received their statutory returns under Section 42 of the Act. It made remittance of funds by telegraphic transfer for banks between their accounts maintained with the Bank's offices and dealt with sterling purchases and sales, part of the work relating to Treasury bill tenders as well as discounts and advances to scheduled banks. Under the Scheduled Banks' Regulations framed by the Reserve Bank, every scheduled bank was required to intimate to the Bank the name of the Banking Office (of the Reserve Bank) at which the scheduled bank desired to maintain its principal account and to which it desired to submit its statutory returns. The scheduled banks were also allowed to maintain accounts' with the Reserve Bank at its other offices, if the banks concerned had offices at such places. With the establishment of the Reserve Bank and the opening of the statutory accounts by scheduled banks with it, it was arranged that the member banks of regional clearing houses should settle their clearing differences through their accounts with the Reserve Bank. The Bank took over the supervision of clearing houses at most centres where it had offices, although the autonomous functioning of the clearing houses was allowed to continue.

The management of the rupee debt of the Central and Provincial Governments and the maintenance of the relative accounts devolved on the Central Public Debt Office at Calcutta. The regional Public Debt Offices at Bombay, Delhi and Madras were entrusted with certain functions of the Central Public Debt Office, to facilitate decentralisaion of operations. The functions of the Public Debt Offices related to making the necessary arrangements for the floatation of new Government loans, payment of interest on Government securities, enfacement of securities for payment of interest at Treasuries or sub-Treasuries, repayment of maturing loans and various operations connected with renewal, conversion, consolidation and sub-division of different kinds of Government securities. The investigation of disputed claims pertaining to securities and the issue of duplicates of lost, stolen or destroyed scrips also formed part of their responsibilities. The Indian Securities Act, 1920 as amended by the Indian Securities (Amendment) Act, 1937 contained the law relating to Government securities, while the procedure for dealing with the issue, conversion, renewal, payment of interest, etc., of Government loans was laid down in the Government Securities Manual.

The Securities Department dealt with the purchase, safe custody, collection of interest and sale of securities on behalf of local bodies and Government officials in their official capacity. It also undertook the safe custody of securities held by the Bank on behalf of the Issue and Banking Departments as well as those which insurance companies had to deposit with the Government of India under the Indian Insurance Act.

The Share Transfer Department dealt with the maintenance of share registers, issue of share certificates, share transfers, payment of dividends, etc.

The Bank maintained, as indicated earlier, seven branches of its Issue Department, one for each currency circle into which the territory of India and Burma was divided. Each branch of the Issue Department functioned directly under the Currency Officer with general supervision by the local Manager and was divided into the Treasurer's Department and the General Department. The Treasurer's Department comprised the Issue Branch and the Exchange Branch. The Issue Branch was concerned with the receipt, safe custody, examination and issue of fresh bank notes to the Exchange Branch and the currency chests within the circle as also to other circles, receipt and disposal of foreign circle notes and taking over cancelled notes from the Exchange Branch pending verification by the General Department. The Exchange Branch dealt with the exchange of notes and coin of various denominations tendered by banks and the public, the examination of note remittances, the receipt and examination of coin remittances from currency chests and Treasuries and the sorting and listing of defaced notes.

The General Department was sub-divided into a number of branches. The Registration Branch maintained registers of issues of notes exceeding the denomination of Rs.10 and recorded cancellations in these registers. The Cancelled Note Verification Branch took over paid and cancelled notes, subjected them to quality and quantity checks, and issued warrants of destruction. The verified notes were taken over by the Cancelled Note Vault Section which arranged for their safe custody and eventual destruction. The Claims Branch dealt with applications for the payment of the value of lost, stolen, mutilated, altered and other imperfect notes in accordance with the Bank's Note Refund Rules, and also with cases of forged and unclaimed notes. The Resource Branch arranged for the supply of currency at the different centres through the mechanism of the currency chests and for the removal of currency in excess of normal requirements. The Accounts Branch maintained accounts of note circulation and balances of the Issue Department as also the accounts of small coin depots.

Cumency Arrangements

The operations of the Bank in the initial stages were largely confined to its functions as currency authority and banker to Government, The Bank continued the administrative arrangements and operational procedures evolved by its predecessors in the discharge of these functions with the necessary changes required under the new dispensation. The provision of adequate supply of currency for facilitating transactions of the Government and the exchange and remittance requirements of the public required elaborate arrangements, particularly in a vast country like India. Besides the branches of the Issue Department, the Bank also maintained currency chests* at the branches of the Imperial Bank of India carrying on Government Treasury business and at Government Treasuries and sub-Treasuries. The offices of the Issue Department also maintained small coin depots belonging to the Government for supply of subsidiary coin to the public.

Under Section 22 of the Reserve Bank of India Act, the Bank was empowered to continue to issue currency notes of the Government of India till its own distinctive notes were ready for issue.Since theCentral Board of the Bank was statutorily responsible for making recommendations to Government in regard to the form and design of

* Currency chests are receptacles in which stocks of new or reissuable notes are stored along with rupee coin. The Treasury or agency of the Bank provided with the currency chest can withdraw funds according to requirements when its payments on any day exceeded its own balances or deposit into it excess funds received. The availability of currency chests obviates the necessity for physical transfer of cash at frequent intervals from one place to another. The mechanism also enables exchange of rupee coin for notes and supply of notes of lower denominations for higher denominations and vice versa, or issue of new notes for old and soiled notes. The currency chests also serve as the basis for the provision of remittance facilities to banks and the public. The number of currency chests maintained was about 1,300 at the end of 1939.

Bank notes, the subject was considered quite early, at its meeting on April 25, 1935. It was resolved to retain the general size, appearance and design of the existing Government currency notes subject to appropriate modifications, namely, the substitution of the words ‘ Reserve Bank of India ’ for ‘Government of India’ and the superscription of the words ‘Guaranteed by the Governor General in Council ’ or alternately ‘Guaranteed by the Government of India ’. The notes were to be signed on behalf of the Bank by the Governor and ‘senior’ Deputy Governor. It was decided to discontinue currency notes of Rs. 50 and Rs. 500 denominations as they had not proved popular. The Central Board also recommended a slight increase in the size of the Rs.10 note and a slight decrease in the size of the Rs.100 note. Subsequently, certain modifications of the proposals made by the Board became necessary; the design of the Rs. 100 note was materially changed on expert advice to give it greater security and a minor alteration was made in the Rs.1,000 note by replacing the agricultural view on its reverse by a Himalayan view. It was also decided to have the signature of only the Governor of the Bank as the Reserve Bank of India (Note Issue) Regulations, 1935, provided for the signature of only one officer of the Bank. The final proofs of the notes embodying these alterations were approved by the Board at its meeting held on December 1, 1936. It was hoped to make the first issues of new notes in the summer of 1937, but the abdication of King Edward VIII delayed this programme by some months, as the King’s head appearing on the notes and in the watermark of the paper had to be changed to that of King George VI. The revised specimens of the notes were approved by the Committee of the Central Board on May 26, 1937; approval of the Government of India, under Section 25 of the Act, was accorded on June 24, 1937.

The Bank made its first issue of currency notes in January 1938 in denominations of Rs. 5 and Rs. 10. Later during the year the Bank issued notes of the denominations of Rs.100, Rs. 1,000 and Rs. 10,000. Although Bank notes in denominations of Rs. 50, and Rs. 500 were not issued, the Government of India notes of these denominations continued to be legal tender.

Banker to Central Government

The Reserve Bank was responsible, under its Statute, for transacting all general banking business of the Government of India, such as, receipt and payment of monies, remittance and exchange, as well as the management of public debt and issue of new loans including Treasury bills. The Government, on their part, were required to entrust these functions to the Bank and to keep all cash balances in the form of interest-free deposits with it. Accordingly, an agreement was entered into between the Reserve Bank and the Secretary of State for India in Council on April 5, 1935, setting out the terms and conditions under which the Bank was to carry out its functions as banker to Government. The agreement laid down that the Bank should discharge its responsibilities and maintain books of accounts in accordance with the orders and directives of the Government. The Bank was not entitled to any remuneration for the conduct of ordinary banking business other than the advantage accruing to it from holding Government cash balances free of interest. For the management of public debt, however, the Bank was entitled to a half-yearly commission at the rate of Rs. 2,000 per crore per annum on the amount of the public debt outstanding at the close of each such period, subject to the exclusion of certain specified items. * The Bank was also entitled to a fixed annual remuneration of Rs. 2,000 in respect of stock certificates falling under the excluded items referred to above.

The agreement enjoined the Bank to maintain currency chests at places prescribed by the Government, with adequate supplies of notes and coin, for carrying out Government transactions and providing reasonable remittance facilities to the public. The Bank was also obliged to meet the exchange requirements of the Government for remittances between India and London at the market rate of the day for telegraphic transfers or at a mutually agreed average rate based on a longer period in the case of large transfers. Since the agreement did not contain any provision regarding remuneration payable to the Bank for the issue of new loans, the terms of such payment were fixed pursuant to arrangements subsequently concluded by the Bank with the Central Government. Under these provisions, which still continue without substantial modifications, the Bank was entitled to a fee at the rate of Rs. 1,000 per crore of all new issues with a minimum of Rs. 5,000 in respect of each loan in addition to renewal fees on applications for conversion (at rates prescribed in the Indian Securities Rules, 1935), brokerage, commission charges and incidental expenses.

Agreement with Imperial Bank

In terms of Section 45 of the Act, the Bank also entered into an agreement with the Imperial Bank of India for the latter's continuing to undertake the work relating to Government transactions as agent of the Bank. The original duration of the agreement, which came into effect on April 1, 1935, was for a period of fifteen years after which it could

* The excluded items covered outstandings of discharged loans after one year from the date of discharge, stock certificates for Rs. 50,000 and above held by the Central and provincial Governments, the amount of public debt outstanding in the London register, and Government of India rupee securities held in the Issue Department of the Bank.

be terminated with five years' notice on either side. It was conditional on the maintenance of a sound financial position by the Imperial Bank, which became the sole agent of the Reserve Bank at all places in British India, where there were branches of the Imperial Bank but no branch of the Banking Department of the Reserve Bank at the time of coming into force of the agreement. The Reserve Bank was to pay a commission on the total of the receipts and disbursements dealt with annually by the Imperial Bank on account of Government at the rate of l/16 per cent for the first Rs. 250 crores and l/32 per cent for the remainder, during the first ten years and thereafter at rates to be determined for every five years on the basis of the actual cost to the Imperial Bank of India, as ascertained by expert accounting investigation, of performing these functions. Besides, the Reserve Bank was to make lump sum payments to the Imperial Bank of Rs. 9 lakhs, Rs. 6 lakhs and Rs. 4 lakhs per year, during the three successive five-year periods of the agreement, on condition that the latter continued to maintain branches not fewer in number than those existing at the commencement of the agreement. The Imperial Bank was also not to open any new branch in substitution of an existing branch without the approval of the Reserve Bank.

The agreement provided for the maintenance of currency chests and small coin depots by the Reserve Bank at branches of the Imperial Bank managing Government accounts and situated in places where there was no office of the Banking or Issue Department of the Bank; such facilities were also to be provided at any local head office or other branch of the Imperial Bank in India if the two institutions so agreed. These facilities could be availed of by the Imperial Bank for exchange of notes for coin and coin for notes as also for making deposits and withdrawals of currency, subject to any general or special directions of the Reserve Bank. Besides, the Imperial Bank enjoyed under the agreement facilities for free transfer of funds between its offices through the medium of the Reserve Bank's offices or currency chests or small coin depots. The Imperial Bank was also obliged to provide to all scheduled banks remittance facilities as prescribed by the Reserve Bank from time to time and also to give the general public all possible facilities for transfer of funds at rates not exceeding those specified by the Bank.

The basis for the payment of commission and brokerage to the Imperial Bank in respect of loans issued by the Central and Provincial Governments was agreed upon in April 1938. The terms of remuneration were: (i)full brokerage on allotments in respect of applications lodged by the Imperial Bank on its own account or on behalf of its customers with the Reserve Bank at Bombay, Calcutta, Delhi,, Madras and Rangoon ; (ii) commission at l/16 per cent on allotments, either by cash or conversion, in respect of applications handled by the offices of the Imperial Bank of India at places other than those mentioned above. In respect of cash applications, the above commission of l/16 per cent was double the commission which the Reserve Bank was entitled to recover from Government. However, this difference of l/32 per cent was set off by the Bank against the general turnover commission payable to the Imperial Bank; and (iii) full brokerage on allotment in respect of applications lodged by other banks and brokers at Imperial Bank offices other than at Bombay, Calcutta, Delhi, Madras and Rangoon; the brokerage was to be passed on by the Imperial Bank to the banks and brokers concerned. Besides, in regard to provincial loans, if the rate of brokerage was higher than the rate of commission (l/16 per cent), the Imperial Bank was entitled to brokerage at the rate of such excess, on the bank's own and its customers' allotments, at places other than those referred to above.

Banker to Provincial Governments

Before the inauguration of provincial autonomy on April 1, 1937, the Government of India held all the cash balances in the Public Account for British India and were responsible for the ways and means requirements of Provincial Governments. Under this system of centralised accounts, there was no need for the Reserve Bank to act as banker to Provincial Governments separately. Accordingly, the obligation placed on Local (Provincial) Governments under the Reserve Bank of India Act to entrust the Bank with all their banking transactions and to maintain their cash balances with it was conditional on their having custody and management of provincial revenues as envisaged under the new constitution. Provincial Governments were also required under the Act to entrust the Bank with the management of their public debt and the issue of new loans. In the pre-autonomy period, however, Provincial Governments generally had recourse to borrowings from the Central Government, which set up in 1925 a Provincial Loans Fund for the purpose. Even so, in the period prior to the establishment of the Bank, some of them (Bombay, the U.P. and the Punjab) had raised loans in the open market under the provisions of Section 30(1a) of the Reforms Act of 1919. Soon after commencing operations, the Bank entered into agreements with these Governments for the limited purpose of management of their public debt and issue of any new loans.

Provincial autonomy entailed the separation of provincial balances and the assumption of responsibility by Provincial Governments for their ways and means requirements. The major alterations in accounts and important questions of principle associated with these changes were settled at a meeting of the representatives of the Government of

India and the Reserve Bank with the Finance Ministers of the various Provinces, held in Simla in August 1936. In order to afford Provinces the necessary experience in framing their ways and means requirements, it was decided that the Central Government should remain responsible for these requirements during the financial year 1937-38. Hence, it was only from April 1, 1938 that Provincial Governments assumed full responsibility for their ways and means requirements.

`With the separation of provincial balances and decentralisation of accounts, it became necessary for Provincial Governments to enter into direct relationship with the Reserve Bank as their banker and to maintain their cash balances with the Bank. To meet their short-term requirements, they were required to obtain ways and means advances from the Bank or to issue their own Treasury bills. Besides, as the Provincial Loans Fund was wound up, they were also obliged under the new set-up to meet their long-term financial requirements by raising market loans and to entrust the issue and management of their public debt to the Bank. The terms and conditions governing the performance of these various functions to be undertaken by the Bank were set out in separate agreements entered into with each of the Provincial Governments.

The agreements entered into by the Bank with the various Provincial Governments were more or less similar to its earlier agreement with the Central Government and covered both general banking business and public debt management. The Bank was not to receive any remuneration for the conduct of their ordinary banking business, but the Provincial Governments had to maintain with the Bank interest-free cash balances at an agreed minimum level. The Bank was entitled to charge the Governments for extra-territorial remittances at rates not exceeding those applicable to scheduled banks, subject to a minimum of four annas for each single remittance. The Provincial Governments could also avail of ways and means advances from the Bank; the out-standings under such advances were not at any time to exceed the amount of minimum balances provided in the agreements and had to be paid off at intervals not exceeding three months from the date of initial advance. The investment of Government owned or managed funds was to be entrusted to the Bank as sole agent on a commission of 1/16 per cent on sales in addition to brokerage and other charges. The terms of remuneration payable to the Bank for the management of public debt and the issue of new loans were the same as those provided for in the agreement with the Central Government except for the minimum fee payable in respect of each provincial loan which was to be Rs.1,000. The agreements also contained identical provisions covering currency chest arrangements and exchange obligations of the Bank.

Central Banking Functions in Burma

The Reserve Bank continued to function as the central banking authority for Burma even after its political separation from British India on April 1, 1937. The Indo-Burma monetary settlement embodied in the Order in Council known as the India and Burma (Burma Monetary Arrangements) Order, 1937, provided for the Bank continuing to manage the currency of Burma and to perform the functions of banker to the Government of Burma. To facilitate the division of currency profits between India and Burma, the Reserve Bank was required to issue as soon as possible after separation distinctive notes for Burma. The profits payable to Burma were to be based on the proportion of the Reserve Bank notes in circulation in Burma to total note circulation in the two countries. The Bank was also required to provide remittances between India and Burma at such fixed rate of exchange, and subject only to such rates of commission, as might be approved by the Governments of India and Burma; however, as long as the Bank was bound, under the Order, to issue on demand India rupee coin in exchange for legal tender notes, the rate of exchange was to be par.

The Bank entered into a separate agreement with the Burma Government in April 1937 for the discharge of its functions as banker to Government on the lines of the earlier agreement with the Government of India. The Bank started issuing new Burma notes of distinctive design from May 1938.

The Burma Monetary Arrangements Order, which could be terminated by either Government on a two-year notice given after March 31, 1938, also detailed the manner in which certain assets and liabilities of the Government of India and the Reserve Bank were to be transferred to the Government of Burma in the event of full currency separation. On such separation, the Bank’s liability for Burma notes was to cease completely, and any guarantee thereof of the Government of India had to be deemed to be that of the Government of Burma. Simultaneously, from the Bank’s Issue Department, assets, i.e., gold, sterling securities, India rupee coin and rupee securities, equal to the total liability in respect of Burma notes outstanding on the date of the currency separation, were to be transferred to the Government of Burma in the proportions in which they were held in the Issue Department on that date. The Government of Burma were also to be given credit-as a capital payment in reduction of the Burma debt to India-for an appropriate portion of the Bank’s surplus assets (including a share of the Reserve Fund).

Public Debt Function

The responsibilities of the Reserve Bank as banker to Government, apart from the performance of the ordinary banking transactions, related to the issue and management of Government loans, sale of Treasury bills, provision of ways and means advances and purchase of sterling for meeting exchange requirements. In these matters, the Bank's role was not merely one of carrying out the Government's instructions but also of advising the Government on all matters connected therewith, for instance, the quantum, the terms of issue and the timing of floatation of Government loans.

During the period 1935-39 the Government of India floated one sterling loan in London and four new rupee loans, mainly to provide for the repayment of maturing obligations. The first loan operation to be handled by the Reserve Bank was the issue of the 3 per cent sterling Loan, 1949-52, for repaying nearly £ 12 million of the 6 per cent sterling Bonds, 1935-37. The terms and timing of the issue were settled by the Governor, who was in London, in consultation with the Bank of England and the India Office. The details of the loans floated during the period were as under:

Date	Maturity	Type	Interest	Issue Price	Amount offered	Amount allotted
			Sterling Loan			
July1935	1949-52	Cash	3%	£98	£10 million	£10 million
			Rupee Loans			
Aug.1935	1951-54	Cash cum Conversion	3%	Rs.961/2	Rs.15 crores	Rs.15-13 crores
May 1936	1948-52	Cash	2¾%	Rs.100	Rs.12 crores	Rs.12-01 crores
May 1938	1963-65	Cash cum Conversion	3%	Rs. 98	Rs.15 crores	Rs.26-31 crores
July 1939	1963-65	Cash cum Conversion	3%	Rs. 98	Rs.15 crores plus	Rs.15-72 crores

The loan operations met with success in nearly all cases. The sterling loan evoked very good response; subscriptions amounted to more than £ 72 million and only 14 per cent of the applications over £ 500 could be allotted.

Total subscriptions to the first rupee loan amounted to Rs. 29.6 crores and the loan was closed within about twenty minutes of its opening on the first day, that is, August 5, 1935. Cash subscriptions totalled Rs. 16.5 crores ; subscriptions in the form of the 5 per cent Bonds, 1935 and the 6 ½ per cent Treasury Bonds, 1935, amounted to Rs. 8.4 crores and Rs. 4.6 crores, respectively. It was planned that the Reserve Bank and the Imperial Bank should subscribe about Rs. 3.5 crores and Rs. 6 crores, respectively, but it is not known as to what they actually tendered. Conversions were accepted in full and the allotment in respect of cash subscriptions amounted to Rs. 2 .1 crores only. Reporting to the Government on the loan, the Controller of the Currency remarked that 'this was the first loan which the

Reserve Bank had to handle, but the manner of the handling left little to be desired '.

The medium-term cash loan of 1936, the terms of which reflected the easy conditions in the money market (the rate of 2¾ per cent being the lowest recorded for a Government loan in India) was designed for institutional investors and it was heavily oversubscribed, the applications amounting to Rs. 30 crores. About half the loan allotment of Rs. 12 crores was made to the Imperial Bank and the Reserve Bank. The Finance Member as well as the Governor of the Bank of England congratulated the Governor on the success of the loan. The next loan, a cash-cum-conversion issue, came two years later, in May 1938. This was the 3 per cent Loan 1963-65 and was also heavily oversubscribed. Cash subscriptions amounted to Rs. 12 .2 crores ; conversions in respect of the 5½ per cent Loan, 1938-40 and the 5 per cent Loan 1939-44 totalled Rs. 20 crores. Total allotment was for Rs. 26.3 crores (of which the cash portion was Rs. 6.3 crores); the Reserve Bank and the Imperial Bank were allotted to the extent of Rs. 5.7 crores and Rs. 3.7 crores, respectively. The second issue of the 1963-65 Loan made in July 1939 was not, however, a success, mainly on account of the troubled international situation. The amount offered was Rs. 15 crores in cash or conversion of the 5 per cent Loan 1939-44, while subscriptions in the form of the 5 per cent Loan 1940-43 were to be without limit. Subscriptions in the form of cash and the 5 per cent Loan 1939-44 amounted to Rs. 1.3 crores and Rs. 8.2 crores, respectively, or a total of Rs. 9.6 crores; subscriptions in the form of the 1940-43 Loan amounted to Rs. 6.1 crores. Thus, the total amount subscribed and allotted was Rs. 15.7 crores. The Reserve Bank alone tendered Rs. 10 crores by way of conversion, while the Imperial Bank accounted for Rs. 1 crore of the cash subscription.

In those days, as now, subscriptions to Government loans came mainly from institutional investors; apart from the princes, subscriptions from individuals generally were of a small magnitude. Thus, in respect of the 3 per cent Loan 1963-65 issued in 1938, out of the total subscription of Rs. 22.6 crores in regard to applications of Rs. 1 lakh and above, the contribution of individuals amounted to Rs. 36.3 lakhs only. Statistics of subscriptions in the various slabs, namely, up to Rs. 10,000, Rs. 10,000 to Rs.1,00,000 etc., also support this conclusion.

The floatation of new loans was undertaken after careful consultation and preparation of the ground. In the interests of secrecy, the matter was also handled at the highest level. During the initial phase of the Reserve Bank's regime, detailed consultations on these matters had to take place among five parties, namely, the Reserve Bank, the Imperial Bank, the Controller of the Currency, the Finance Department of the Government of India and the Secretary of State for India, who was no doubt consulting the Bank of England. In the beginning, the consultations were prolonged and there used to be lengthy discussions on paper relating to the various items of the loan programme, 'for the satisfaction of the Secretary of State'. But, progressively an endeavour was made to curtail these, since, in the words of Sir James Taylor, 'such discussions were always rather platitudinous and their most usual and undesirable result was premature leakage '. As a result of these discussions and in the light of the situation .in the gilt-edged market, reflecting domestic as well as international conditions, appropriate changes were made in the amount as well as the price of issue. Thus, in respect of the first rupee loan, the original idea was to issue it for an amount of Rs. 18 crores, but finally it was reduced to Rs. 15 crores, partly on account of the disturbance to the market arising from Italy's attack on Abyssinia. Moreover, the Finance Member was keen on a relatively high issue price. Similarly, in the case of the 1963-65 Loan issued in 1938, the original suggestion was to raise a loan of Rs. 20-25 crores but the offer was reduced to Rs. 15 crores, on account of the disturbed political situation in Europe. In the prewar years, the terms of issue of rupee loans in India had to take note of the prevailing conditions in the London gilt-edged market, which was naturally sensitive to international political and financial developments.

When the Bank took over the management of the public debt, it made appropriate modifications to simplify the procedure for floatation of Government loans. Thus, the arrangement for receiving loan applications at Treasuries and sub-Treasuries was discontinued and applications were to be received only at the offices of the Reserve Bank and branches of the Imperial Bank of India. Since the 2 ¾ per cent Loan 1948-52 issued in 1936 was intended mainly for institutional investors like banks, applications were received only at the offices of the Reserve Bank. The second change related to the discontinuance of the practice of issuing scrip over the counter in exchange for cash on application. Apart from the fact that this was not always found practicable in the larger centres, it also tended to result in premature leakage of information about the loan and also wastage of forms. According to the revised procedure, subscribers were required to put in regular applications for which they were initially to be given a receipt which was to be exchanged for the new scrip in due course. The receipt of applications through the post offices was also discontinued, except in regard to conversion of loans deposited with the postal department by investors. Other matters, such as, how long to keep a loan open and the scale of brokerage and commission payable to the Reserve Bank, the Imperial Bank, scheduled banks and recognised brokers, were also settled by the Bank in consultation with the Imperial Bank and Government.

As already mentioned, the Reserve Bank also became responsible for the management of market borrowings by the autonomous Provinces under the agreements entered into with them. The first borrowing programme of Provincial Governments was announced on August 24, 1937; loans aggregating Rs. 460 lakhs were issued by five Provincial Governments, namely, Madras, Rs. 150 lakhs; the United Provinces, Rs. 100 lakhs; the Punjab, Rs. 100 lakhs; the North West Frontier Province, Rs. 60 lakhs and the Central Provinces and Berar, Rs. 50 lakhs. The loans were offered on uniform terms and consisted of 3 per cent Stock 1952 at an issue price of Rs. 99. The Punjab loan was a cash-cum-conversion issue, while the other four were purely cash loans. In fixing the terms of the issue, the idea was that the yield on provincial loans should be approximately ¼ per cent above that of Central Government issues of comparable maturity. The original intention was to float twelve to fifteen year -loans, but in view of, the improvement in market conditions, a maturity of fifteen years was fixed. With a view to ensuring the success of all loans, subscribers were asked to state whether, in the event of the loan specified by them being oversubscribed, they wished their applications to be transferred to other loans. The issues were on the whole successful, particularly as there was no loan floatation by the Central Government during the year; the lists opened on August 31 and were closed within two hours.The Madras, U.P. and Punjab loans were oversubscribed, while the other two were fully subscribed after the transfer of options from other loans.

During the early years of provincial autonomy, the Bank had a specially useful and effective role to play as adviser to Provincial Governments on public debt matters owing to their comparative inexperience in this behalf. It was necessary to restrain the general tendency among these Governments to pitch their loan requirements somewhat high without due regard to their borrowing capacity, in their eagerness to undertake various productive schemes. While the Central Government on their part sought to ensure a detailed screening of provincial loan proposals which came up to them for approval under the Government of India Act, 1935, the procedure of an annual conference of representatives of Provincial Governments enabled the Bank to assess their loan requirement in the light of their budgetary position, the requirements of the Central Government and the conditions in the gilt-edged market.

The diversity in the budgetary position of various Provincial Governments also posed a problem for the Bank in fixing the terms of individual loan issues. Whereas in the case of the Central Government loans, the issue price and other terms were fixed by the Government on the advice offered by the Reserve Bank in the light of prevailing market conditions, the Bank felt that the same procedure would not prove adequate in the case of provincial loan issues, as an important consideration in their case was the possible variation in the market assessment of the credit of different Provinces. It was considered necessary to devise a system whereby the market itself could be the judge of the terms on which it was prepared to lend to the Provincial Governments, so as to preclude the possibility of an open failure of loans. During his visit to London in the spring of 1937, Sir James. Taylor studied loan procedures in the U.K. and in other Empire countries, particularly those with Federal Constitution.

Accordingly, in June 1937, the Bank drew up a scheme for underwriting loan issues and forwarded it to Provincial Governments for their views. On the basis of their replies and after discussion with the market, the scheme was modified in certain respects and put into operation beginning with the loan floatations for 1938. There were again some modifications in 1939. The main features of the underwriting scheme were: (i) enrolling of scheduled banks and stock brokers of standing as underwriters on the Bank's list, subject to their complying with standing instructions drawn up by the Bank; (ii) advising underwriters regarding proposed loan floatation and calling for tenders ; (iii) fixing the issue price on the basis of the lowest tender necessary to complete underwriting; and (iv) distributing the unsubscribed portion of the loan among the underwriters in proportion to their allotment, subject to some adjustments.

Provincial Governments desiring to float loans made a formal approach to the Bank, which, in consultation with the Government concerned, fixed the terms of the loan and called for tenders from underwriters. On receipt of tenders, the Bank took instructions from the Provincial Government whether to float the loan or drop it or issue for a reduced amount. In 1939, when the scheme was revised, the option to the Provincial Governments of reducing the loan amount was withdrawn formally, but it was open to any Provincial Government to reintroduce a provision for reducing the amount of a loan through the letter to underwriters. The underwriting arrangement devised by the Bank did not impose any obligation on a Provincial Government to have their loans always underwritten and they could make a direct issue, if the underwriters' terms were not satisfactory. The Bank was also willing to provide assistance in bridging the gap in cases where a loan could be underwritten at a fair and reasonable price except for a very small shortfall in the amount. During 1938, the Madras and the Punjab Governments issued loans for a total of Rs. 2.50 crores, while in 1939 these two and the C.P. and Berar Governments floated loans for Rs. 4.70 crores. The amounts of acceptable tenders exceeded the amount offered in all the issues except for one where the

Bank had to underwrite a small amount. The issue price fixed ranged between Rs. 98 and Rs. 99. All the loans, except one, were oversubscribed; in regard to the one loan which failed to evoke adequate public response, the underwriters were called upon to take a substantial amount.

Another aspect of the Bank's role in the sphere of public debt related to Treasury bill issues. The Reserve Bank conducted sales of these bills *, whenever considered necessary, on behalf of the Central and Provincial Governments, by calling tenders. The first sale of Central Government Treasury bills was made in April 1935; the first sale of Provincial Treasury bills was effected in April 1938 by the C. P. and Berar Government. The Central Government bills were all three months bills. In the case of Provincial Governments, bills were generally of three months maturity; however, bills of longer maturities were also sold by some Governments during 1938 and 1939.†

Treasury bills from the holdings of the Bank's Issue Department were made available on tap to the Provincial Governments, semi-Government institutions and foreign holders like the Board of Commissioners of Currency, Ceylon, at a price 1/64 a rupee higher than the bulk tender rate (that is. carrying a fractionally lower yield) of the preceding auction, The bills were sold from the Reserve Bank's holdings, to be replaced, if necessary by special bills created by Government. The idea was that such funds should not compete with the usual money market funds for the auction, but at the same time the rate of these tap bills should not be different from that established at the auction. There were also practical difficulties in the Government of India's varying their Treasury bill offerings to suit the surplus position of the Provinces. Hence the sale of tap bills, but this was regarded as a temporary arrangement. On October 30, 1937, the Bank informed the Provincial Governments, after obtaining the concurrence of the Central Finance Department, that from January 1, 1938, the Provinces must obtain their requirements of Central Government Treasury bills through tenders, in competition with other investors and that the Bank would not be in a position to suggest to them the rates at which they should tender, since 'it would obviously not be fair either to the market or to the other Provinces if it assumed this responsibility'. The Provincial Governments in general preferred the continuance of the then existing arrangement, though they did not state this in strong terms. The Madras Government, however, sent a strong representation. After consulting the Finance Department, the Bank decided in November 1937 to continue the system of tap sales.

* The system of sale of Treasury bills by tender, by the Government of India, has been in vogue from October -1917.

† The longer maturities were for periods of four, six, eight and nine months.

The Bank also sold bills between auctions to non-Government investors at a price 1/64 a rupee above the bulk rate of the last auction; these were referred to as ‘intermediate’ bills. But, unlike the tap sales to the Government and semi-Government institutions, the sales were entirely at the discretion of the Bank. These sales enabled the unsuccessful tenderers at the auction to buy the bills at a discount rate fractionally below the auction rates; also, funds that accrued after the auction could be invested. The intermediate bills system provided an elastic method of relieving the market of surplus funds. The device of intermediate bills also enabled the Government to obtain, within limits, larger funds, without forcing the discount rate upwards. It should be mentioned that the main response to Treasury bills came from institutional investors, especially commercial banks. The Imperial Bank of India was the largest supporter, followed by the exchange banks and a few leading Indian joint-stock banks. The Reserve Bank also held Treasury bills in the Issue Department; in the Banking Department it rediscounted bills for the account of banks and Provincial Governments. On special occasions, such as in connection with the repatriation of sterling debt, Government also sold ad hoc bills to the Bank.

Ways and Means Advances

The Bank was authorised under Section 17(5) of the Act to make to Central and Provincial Governments ways and means advances which were repayable in each case not later than three months from the date of making the advance. There were no statutory provisions as regards either the rate of interest to be charged or the maximum amount of the advance. These matters were regulated by the respective agreements or arrangements between the Bank and the Central and Provincial Governments. This position has remained unchanged. According to the agreements with the Provincial Governments, the Bank undertook to make ways and means advances at rates not exceeding the Bank rate provided the total of such advances outstanding at any one time did not exceed the minimum balance of deposits agreed to between the Bank and the Government concerned. These advances were granted without any collateral. The minimum balance of the Provincial Governments varied from Rs. 5 lakhs in the case of Orissa, N.W.F.P. and Sind to Rs. 40 lakhs in the case of Madras; the aggregate of the minimum balances was Rs. 1.95 crores. The minimum balance prescribed for the Central Government was Rs. 4.25 crores (in terms of an exchange of letters rather than a formal agreement) and for the Government of Burma Rs. 85 lakhs, including Rs.10 lakhs on account of that Government’s requirements in London. The aggregate of the minimum balances was about the same as what the Government of India had agreed to maintain with the Imperial Bank. In the case of the Central Government there was no limit with regard to the amount of ways and means advances granted by the Bank, but in practice these advances were neither large nor continuous. In fact, it was a clear understanding between the Bank and the Government that ways and means advances should be a temporary arrangement, mainly to enable Government to spread their Treasury bill maturities as conveniently as possible, the idea being that Government's short-term requirements would be met principally through sale of Treasury bills. Estimates of Government's ways and means position used to be sent to the Bank in advance to enable it to plan Treasury bill issues and ways and means advances. All along, the rate of interest on the ways and means advances has been 1 per cent below the Bank rate (except for a short period between October 1939 and April 1940, when the rate was ½ per cent below Bank rate). The records do not contain any discussion of the grant of these advances below Bank rate. In September 1935, when the Controller of the Currency approached the Bank for ways and means advances, he presumed that the lending rate would be 3 per cent (the Bank rate then was 3½ per cent) ; in a telegram, Deputy Governor Taylor replied that 'in this case ' he would make the advances at 2 per cent. Apparently, this rate continued, this being per cent below Bank rate consequent on the reduction of Bank rate to 3 per cent in November 1935. This arrangement along with other procedural matters was standardised effective April 1, 1938. It would appear that the intention was to base the rate on ways and means advances on the prevailing discount rate on Central Government Treasury bills. In September 1935, when the advance was first asked for, the Treasury bill rate for several months past had been in the neighbourhood of 1.75 per cent. The Bank, as already mentioned, agreed to lend ways and means at 2 per cent. That the intention was that the rate should be close to the Central Treasury bill rate is also evidenced by the fact that when the ways and means rate was raised to ½ per cent below Bank rate in September 1939, the reason given was the rise in the Treasury bill rate and likewise when the old rate was restored in April 1940, the reason was the decline in the rate.

Sterling Transactions

The responsibility for sterling purchases and remittances to the Secretary of State was also transferred to the Reserve Bank. Prior to its establishment, the purchases of sterling by competitive tender used to be conducted by the Central Government through the Imperial Bank. Purchases were made from the scheduled banks from time to time, ordinarily in amounts of not less than the equivalent of Rs. 1 lakh, by calling for tenders once a week and also by accepting intermediate offers which were made by banks during intervening days. The purchases were made at all offices of the Banking Department of the Bank and also at the branch of the Issue Department at Karachi. The tenders were to be for multiples of £1,000 subject to a minimum of £ 7,500 and the rate of exchange was to be expressed in pence or in pence and a fraction of a penny per rupee, such fraction being expressed in multiples of 1/32 of a penny. The allotment was made on the basis of the best rates offered and the payment of the rupee equivalent was made to the scheduled bank on presentation of a receipt for having issued telegraphic instructions to its agents in London to pay the sterling to the credit of the Reserve Bank. When a scheduled bank was prepared to sell intermediate sterling to the Reserve Bank, it made an offer and the rate at which the Bank was prepared to buy was communicated to it. The offers of intermediate sterling were accepted for amounts of not less than £ 25,000 at Bombay and Calcutta and £ 10,000 at Delhi, Madras, Rangoon and Karachi and in multiples of £ 1,000.

The Bank also sold sterling to scheduled banks in amounts of not less than the equivalent of Rs.1 lakh. Whenever there was likely to be a demand for sterling from the banks, the Central Office of the Bank informed the various offices of the rate at which they were to effect sales of sterling. Sales were to be for ready telegraphic transfers only and in amounts forming multiples of £ 1, 000 subject to a minimum of £ 7,500. On a scheduled bank tendering the equivalent amount in rupees, the Bank issued a memorandum in token of having received a specified sum of rupees being the equivalent of the amount of sterling payable to the bank on demand at the Bank of England. The scheduled bank then telegraphically arranged with its agent in London to receive the sterling.