
Building an Institutional Infrastructure

India's economic policy-makers were exercised at the beginning of our period by the problem of mobilizing resources for industrial investment in the private sector. The first five-year plan envisaged a relatively modest outlay of Rs 613 crores for private sector investment in industry. Of this, Rs 233 crores were expected to be spent in the first two years of the plan. However, there were apprehensions already by the end of 1952, that investment by the private sector might fall short of plan estimates. These led to suggestions from departments of government and others for an examination of the possible ways in which resources available for investment by the private sector could be increased. The Governor, B. Rama Rau, to whom many of these suggestions were addressed, was initially reluctant to engage the Bank in such an exercise. But by the middle of 1953, he too came round to the view that this problem was of 'great importance', and that it should be investigated by a 'small expert committee'.

THE COMMITTEE ON FINANCE FOR THE PRIVATE SECTOR

In the beginning, the Bank and the government appeared to disagree on the scope of the study. The Bank had in mind a comprehensive investigation of the financial requirements of the private sector. The Finance Minister, C.D. Deshmukh, on the other hand, preferred the study to be confined to 'bank finance alone for industry, especially the small man in West Bengal and elsewhere'. The Governor's communication to the Finance Minister proposed a small three- or four-member committee comprising A.D. Shroff from Tata Sons, J.V. Joshi from the Reserve Bank, a prominent banker, and perhaps an official of the Planning Commission. But Deshmukh preferred a bigger committee including an economist, the Managing Director of the Industrial Finance Corporation of India, 'a representative of a medium-type bank in

West Bengal', and a businessman with some experience of running small-scale units. In the end, the committee was formed largely by merging the personnel proposed by the Governor and the Finance Minister. A.D. Shroff was appointed its chairman.

Sponsored by the Bank, the Shroff Committee was asked to examine ways in which increased finance, in particular bank finance, could be made available to the private sector of industry.¹ There was some anxiety that the terms of reference of this committee would clash with those of the Taxation Enquiry Commission (chaired by the former Finance Minister, John Matthai) which was engaged at this time in examining the effects of the structure and level of income taxes on capital formation and productive investment. Hence the Shroff Committee was asked to confine its attention to areas and methods which were not already under investigation by the Matthai Commission.

The principal method of inquiry adopted by the Shroff Committee was that of holding discussions with concerned interests in government, industry, the banking and insurance sectors, and agents involved with the capital market. The committee also received over seventy memoranda and notes. As it was represented that banking development was being retarded by the absence of adequate remittance facilities and the steep rise in operating costs arising from wage awards of industrial tribunals, the Shroff Committee appointed two subcommittees to go into these aspects. After taking into account the latter's recommendations, the Shroff Committee submitted its Report in April 1954, i.e. some months before the completion of the Report of the All-India Rural Credit Survey.

The Shroff Committee's Report made a detailed appraisal of the overall climate for private sector investment in India and suggestions for improving it. The committee apprehended that the prevailing climate of opinion in the country 'discourage[d] and discredit[ed]' private enterprise. The private sector was merely tolerated rather than welcomed as an instrument of development, and legislative and other measures in recent years had helped foster an impression that it was incapable of discharging its social responsibilities. The threat of nationalization implicit in the Industrial Policy Resolution of 1948 and the Industries (Development and Regulation) Act, for example, dampened

¹Apart from Joshi, the other members of the committee were S. Anantharamakrishnan, a Madras industrialist and a member of the Bank's Local Board at Madras, C.W. Middleton, Secretary and Treasurer of the Imperial Bank of India, V.R. Sonalkar, Managing Director of the Industrial Finance Corporation, and B.T. Thakur and B.K. Dutt, General Managers respectively of the United Commercial Bank and the United Bank of India. M.S. Nadkarni and K.S. Krishnaswamy of the Bank functioned jointly as secretaries of the committee.

the enthusiasm of both domestic and international investors, and the committee demanded immunity from nationalization for large industry. While generally accepting the principle of a mixed economy and the regulation and control which it entailed over entrepreneurship, the Report demanded an end to hostile discrimination against the private sector with regard to pricing, grant of licences, and operation of controls. Unless the overall climate for private sector investment was improved, multiplying or strengthening agencies supplying finance to industry would not produce any results.

The committee also highlighted the existence of irritants in the form of licensing requirements for starting, expanding, or modernizing industry, issuing capital, importing machinery, and securing foreign exchange, and their effect in delaying and retarding private investment. Citing examples, it deplored the amount of time and resources entrepreneurs were required to devote to establishing and maintaining contact with government departments in order to secure various licences, and the scope for corruption in this situation. It also stressed the enormous change that had overcome conditions in the labour market as a result of legislative measures adversely affecting employers' freedom to adopt flexible labour practices, rationalize to step up productivity, or even to discipline their workforce. The Report criticized the low return allowed on capital while giving wage awards, and the implications of this policy for industry's ability to expand or rehabilitate capacities; and complained of the practice of even banks and insurance companies being required to produce original books of accounts for scrutiny before wage tribunals, without any regard to the confidentiality of such information. Observing the need to strike a balance between improving the conditions of labour and providing adequate incentives for private investors, the committee urged immediate steps to 'remove the confusion and uncertainties in regard to labour legislation and Awards and to ensure that a rise in the rewards of labour does not run ahead of the increase in the productivity of labour'. Besides, authorities could not persist in their inquisitorial inquiries against banks without affecting the development of the banking sector. Finally, the committee also noted that the private sector itself was prey to several weaknesses. Entrepreneurs, it felt, could inspire greater confidence in the public by observing a proper code of conduct and eliminating unhealthy practices.

Recounting the steps already taken by the Bank to facilitate the flow of credit to the private sector and promote industrial finance corporations in the states, the committee recommended enabling commercial banks and other financial institutions to make larger investments in industry through suitable adjustments in the Bank's lending and rediscount practices. It felt commercial

banks should not make their medium- and long-term advances to industry conditional upon refinance being available from the Reserve Bank. They could provide indirect financial support to industrial concerns and finance corporations by subscribing to their shares and debentures and providing larger advances against such securities. Commercial banks could also extend assistance to the private sector by forming a consortium under the leadership of the Imperial Bank of India to underwrite and invest in new issues. The other recommendations relating to commercial banks concerned the appointment of an expert committee to examine ways of rationalizing wages and salaries in the banking sector, liberalizing facilities under the bill market scheme and providing medium-term finance too, through 'similar facilities', better remittance arrangements, recognition by the Bank of shares and debentures of the Industrial Finance Corporation and state financial corporations as eligible securities for granting advances, financial assistance to licensed scheduled banks opening branches under an approved expansion programme, and providing security to banks in smaller towns and rural areas. The committee was also in favour of examining the feasibility of introducing a deposit insurance scheme, taking punitive action against persons drawing cheques without sufficient funds in their accounts, and forming an all-India association of banks. It recommended linking indigenous moneylenders with the organized credit market, more liberal facilities from the Industrial Finance Corporation, setting up a special development corporation for financing small-scale industries under the aegis of the Reserve Bank, expeditious payment by the government of its bills to the private sector, improving collection of data relating to joint-stock companies, and establishing specialized institutions such as issue houses and investment or unit trusts.

There survive, in the Bank's files, internal notes and memoranda dealing with sixty-six recommendations of the Shroff Committee. Some of these were of little practical value, while several others were such that few could object to them. Therefore no purpose is served by recounting the Bank's response to every one of the committee's recommendations, and we focus here on a few major issues which the committee's report brought to the attention of the Reserve Bank.

The Shroff Committee reported in favour of greater commercial bank support for the longer-term credit needs of industry. This proposal was not altogether new. The Bank's Central Board had rejected a similar proposal in February 1948; Shroff had himself campaigned for it the following year; while the West Bengal committee on the state's Industrial Finance Corporation and the IMF Mission headed by Edward Bernstein advanced similar suggestions in 1951 and 1953, respectively. In each instance, the Bank took the view that the Indian

banking system responded 'adequately to the requirements of trade and industry consistent with the funds at its disposal', and that it was 'well ahead' of banking systems in other countries in this respect. Besides, given the nature of their liabilities, banks could not be expected to make long-term loans to industry. Apart from the risk arising from the relative illiquidity of such assets, as a Bank note reacting to inquiries from the West Bengal committee argued, it was not appropriate for banks to extend long-term loans since their position would then be that of partners who shared 'only the losses and not the profits'. 'If ... industry makes profits, the banks only get the interest'; should it suffer losses, banks could 'lose their principal as well as ... interest'.

Despite this history, the Bank decided to reject the Shroff Committee's proposal for medium-term bank lending to industry only after some internal debate. By 1954, moreover, the Bank had itself travelled some distance towards making medium-term credit available, for example, by rediscounting bills maturing within twelve months drawn to finance the production and marketing activities of small and cottage industries, making limited advances (not exceeding Rs 3 crores in the aggregate) for periods up to eighteen months to the Industrial Finance Corporation, and advancing loans aggregating to a maximum of Rs 5 crores for periods up to five years for agricultural purposes. Hence one view within the Bank, canvassed by the Department of Research and Statistics, was that a provision similar to the latter could be made for industry as well. However, in order to ensure that the Bank retained the flexibility of its monetary policy and its ability to contract credit adequately, this department argued for restricting aggregate medium-term advances to all sectors to a maximum of five years and to a total figure in the region of 5 per cent of the aggregate liabilities of the Banking Department. Besides, medium-term industrial refinancing should be confined to small plant extensions and renovations, and to a few major banks, with the Bank having pre-emptive rights over the assets of borrowing industrial firms going into liquidation.

Such views encountered stiff opposition elsewhere. The Department of Banking Operations drew attention to the apparent abundance of medium- and long-term finance and the poor demand for it. It pointed out that industrial financial corporations, for example, had failed to use up their resources which were invested in government securities or kept as deposits with banks. Under these conditions, it was

undesirable to encourage commercial banks in India, which have yet to consolidate their wartime expansion, to finance industry on a larger scale than at present, particularly as (their) ... proportion of advances ... to ... total deposits is already on the high side

Inspections had also shown that the quality of many commercial banks' advances was not 'first class'. Besides, many loans which were put down in the books as demand loans were carried over indefinitely 'without substantial reduction', and were 'in practice ... more or less long-term advances'. 'Any further encouragement to banks to reduce the liquidity of their advances should, therefore, be deprecated', the department remarked, *and concluded* by suggesting that the Bank should allow the new and proposed industrial term-lending institutions to function for some length of time before exploring whether commercial banks could do anything to supplement the availability of longer-term finance for industry. In the meantime, according to another departmental note, banks could extend support to industries by purchasing shares, debentures, and bonds of industrial finance corporations, and through investment trusts 'which may be floated on a larger scale ... by honest and competent industrialists'. Similar views were expressed by the Deputy Governor, Ram Nath, so that the Bank decided to discuss the whole issue in some detail with the bigger banks before taking a final view on it. However, as the later developments surveyed in these pages show, the Bank's attitude towards meeting the longer-term financial requirements of industry grew progressively more liberal over the years.

The Shroff Committee's proposal for unit or investment trusts too evoked a tepid response in the beginning. Such institutions could not be expected to provide risk capital to entrepreneurs. More inexplicably, the Bank felt they could not be of much help to investors lacking knowledge of the investment market. On the other hand, there was little the Bank could do here: there was no suggestion yet that it (or the government) should promote such trusts, and initiative in the matter belonged properly to agents in the private sector. The idea of a special development corporation for small-scale industries did not evoke much support either, since it would merely duplicate the functions of financial corporations coming up in the states. The opposition of the Rural Credit Survey, which submitted its recommendations a few months after the Shroff Committee, helped bury the latter's proposal to allow indigenous moneylenders access to the resources of the commercial banking system. More generally too, the Rural Credit Survey's scheme to expand the reach of the banking system by transferring the Imperial Bank of India and the state-associated banks to public ownership superseded the Shroff Committee's more modest proposals in this respect. Finally, while the Shroff Committee adverted to the advantages of insuring bank deposits, the factors leading to the institution of deposit insurance in 1962 have already been discussed at some length in chapter 12.

The Central Board considered the Shroff Committee's recommendations at a meeting in Bangalore in June 1954. Of the numerous recommendations made by the committee, three were taken up for immediate implementation. In July 1954, the Bank went further than the Shroff Committee's recommendations to extend the bill market scheme to all licensed scheduled banks, and to reduce the minimum amount prescribed for individual advances from Rs 25 lakhs to Rs 10 lakhs and for individual bills from Rs one lakh to Rs 50,000. The minimum amount of individual advances was further lowered to Rs 5 lakhs in February 1957. The Board turned down the Shroff Committee's recommendation for abolishing statutory restrictions on the holdings of shares in the Industrial Finance Corporation and the state financial corporations since it would 'defeat the objects ... which the Government and Parliament had in view in organizing these institutions'. Apart from the possible consequences of control over these institutions passing into the hands of bodies of private shareholders, the Bank apprehended at the time that privately owned financial corporations risked losing access to World Bank (IBRD) loans since the latter required the guarantee of the government. However, in June 1954 the Bank decided to accept the Shroff Committee's recommendation to treat the shares of the Industrial Finance Corporation and state financial corporations on par with government securities for making advances to scheduled banks under the Reserve Bank of India Act. It was not clear how the private sector was likely to benefit from this step, but the Bank felt it was justified by the wider consideration of encouraging commercial banks to invest in the stocks of state financial corporations. From November 1955, the Bank and the State Bank of India, which had come into existence in the meantime, also began implementing the Shroff Committee's suggestion for more liberal remittance arrangements. In actual fact, remittance facilities extended in subsequent years to scheduled and cooperative banks went far beyond the recommendations of the Shroff Committee in this respect.

The Shroff Committee's recommendation favouring the creation of a consortium of banks and insurance companies under the leadership of the Imperial Bank of India to underwrite or invest in new issues of shares and debentures of industrial companies was based on a suggestion made originally by the Indian Central Banking Enquiry Committee. Two of the three major Indian banks consulted by Rama Rau supported the recommendation. With consultations necessary with insurance companies as well, the Central Board decided to set up a committee comprising the Managing Directors of three Indian banks and the two principal insurance companies to prepare for its consideration, 'a detailed scheme for the creation of a consortium or syndicate'. This committee, chaired by S.K. Handoo, Managing Director of the Imperial

Bank of India, was set up in July 1954 and submitted its report three months later. The report recounted the problems which a consortium of the type proposed was likely to face. These included the inexperience of banks and other institutions in India in meeting the longer-term financing needs of industry and their lack of expertise in assessing industrial projects and issue prospects, the damage that might be caused to a bank's image should any of the issues it underwrote evoke an inadequate response in the market, the generally speculative nature of the share market, and legal restrictions on the participation of insurance companies. Hence, while the idea of establishing a consortium was 'a step in the right direction', it should be undertaken with caution. The Handoo Committee therefore proposed a consortium in the form of a voluntary association, rather than as a company under the Indian Companies Act, of eight to ten leading banks and insurance companies under the leadership of the Imperial Bank of India. Individual members of this consortium would be free to decide whether or not to underwrite or invest in a particular issue, and no restrictions were intended to be placed on the sale of issues underwritten or purchased by any member of the consortium. To begin with, the proposed consortium would deal in new issues of debentures, and consider the question of dealing in shares after it had been in existence for a year. Finally, the committee recommended certain amendments to the Imperial Bank of India Act and the Insurance Act which it felt were necessary to get the consortium off the ground.

The consortium proposal made little headway thereafter. Although C.D. Deshmukh was initially supportive of the idea, he changed his mind after the Imperial Bank of India was nationalized and moves were initiated to bring the life insurance sector under public ownership. Besides, as he noted in a minute written in December 1955, the 'general economic climate' was turning 'more favourable for investment in the private sector'. Therefore, according to the Finance Minister, a consortium was neither 'necessary nor feasible' and banks could 'go forward if they like[d] without life insurance funds'. The Finance Ministry appears, in addition, to have been of the view that the involvement of life insurance companies in the proposed consortium would disproportionately benefit 'big business' within the insurance sector, since only the larger companies had the resources to undertake underwriting work to the satisfaction of the Controller of Insurance. Within the Bank, opinion was divided, the Department of Research and Statistics seeing little substance in the Finance Ministry's argument against the consortium. Nevertheless, the Bank's general view, at any rate in 1955-56, was that a 'strong presumption' existed within the government and elsewhere 'against a departure ... from ... conservative tradition[s]', and that this militated

against insurance companies joining the proposed consortium. As for the involvement of commercial banks, the Department of Banking Operations successfully poured cold water on the idea by highlighting the mismatch that might arise between the structures of their assets and liabilities and suggesting that banks' role in underwriting work could wait until institutions better suited to carrying it out, such as the ICICI and the industrial finance corporations, began to run short of resources. The emergence of the State Bank of India under a statute which authorized it to invest in the debentures of limited companies also blunted somewhat the sense of urgency behind the consortium idea.

THE REFINANCE CORPORATION FOR INDUSTRY

The Shroff Committee, it will be recalled, had recommended that the Bank should undertake to refinance term loans advanced to industry by commercial banks. Initially, the Bank was not keen to lock up its resources in the form of block capital loans to industry, whether these were advanced through term-lending institutions or by commercial banks. The Bank also sympathized with the reluctance of banks to add medium-term industrial loans to their portfolios. 'Investment of short-term funds in long-term commitments' was not likely, in its view, to foster public confidence in the banking system, and efforts to meet the long-term capital needs of industry were 'more properly ... devoted to aiding the recovery of the capital market'. Disposed to see a modest role for itself in the latter regard, the Bank nevertheless maintained a close interest in the activities and needs of industrial term-lending institutions. As discussed below, the Bank also played midwife in the birth of the Industrial Credit and Investment Corporation of India.

The Reserve Bank's initial reluctance to commit medium-term funds to industry gave way gradually under the force of circumstances. An opportunity to reconsider its earlier stand on medium-term lending by banks, as also to lend coherence and a sense of direction to a policy marked in recent years by improvisation more than deliberation, came the Bank's way following an agreement concluded between the Indian and US governments under P.L.480 (Public Law 480) in August 1956. The agreement, which provided for the supply of surplus American agricultural produce valued at Rs 172 crores to India over a three-year period, envisaged earmarking Rs 111 crores from these proceeds for financing development expenditures in India. Of this, Rs 26 crores were to be lent to private enterprise through established banking channels. Inevitably, the Bank was called upon to play a major role in determining the use of these resources.

The prospect of utilizing P.L.480 resources for industrial development was, of course, an attractive one. But the Bank's decision to assist medium-term lending by commercial banks to industry despite the well-advertised dangers of such a practice stemmed also from its changing recognition of the role that 'multi-purpose' banking institutions were capable of playing in India. The State Bank of India was already being equipped to function as an 'instrument of national policy' even though this involved modifying conventional banking principles. There was, in the Bank's still evolving view, no reason why other commercial banks too should not be encouraged to follow the State Bank for some distance of its way, so long as modifications to these principles were undertaken with suitable caution and an understanding of the risks involved. As an article by B.K. Madan in the June 1957 *Bulletin* of the Bank noted, a multi-purpose banking structure could contribute usefully to development if adequate safeguards existed to prevent banks' liquidity from being impaired. Citing recent developments in banking practices in Europe and elsewhere, Madan advocated a measured policy stance based on examining how far these developments could be adapted to the Indian context through 'cautious modification, rather than thoughtless abandonment' of 'conservative ... banking practices'.

Cautious as the Bank was in giving expression to such views, they nevertheless marked an important departure from the position it had adopted in the immediate aftermath of the Shroff Committee. Several events had occurred during this interval to give shape to the Bank's new line of thinking. The conditions in the Indian capital market ruled out term-lending institutions such as the Industrial Finance Corporation and state financial corporations raising large sums of money through public issues for some more time without assistance from the Bank, commercial banks, and insurance companies. The decision, taken in the early fifties, to advance interim loans to the Industrial Finance Corporation against its own bonds and debentures inevitably ended up deepening the Bank's interest in that institution's ability to raise longer-term resources. It was a short step from here to taking a wider interest in the longer-term resource needs of term-lending institutions; particularly since, as discussed in the next chapter, state financial corporations too soon appealed to the Bank to help them raise resources from the market. Gradually a stage came when the Bank began to encourage commercial banks (and insurance companies) to invest in the long-term paper offered by these term-lending institutions. Although these assets were guaranteed by the Government of India and the respective state governments, it was becoming apparent that traditional banking practices were coming under some strain in the face of necessity. When the American proposals for using a part of the P.L.480

resources for industrial development came up, therefore, the Bank had already resiled considerably from its earlier opposition to involving the banking system in medium- or long-term lending to industry.

The Bank considered various means of routing the American loan. The Americans themselves preferred the Bank to hold these funds and oversee their distribution through selected scheduled banks. In their view, advances under the scheme should not be made 'on the basis of cold calculations' of assets 'by a faraway central agency', but by local branches of banks having 'personal knowledge about the integrity and reliability of the borrowers'. Loans made in this way, American officials felt, would also be more visible and transparent to the American tax-paying public and their representatives in Congress. The Bank was not enthusiastic about these proposals. It pointed out to the American aid delegation that few commercial banks allowed their local offices to advance large loans. Besides, 'most ... banks were linked ... with ... business houses', and the additional resources placed in their hands were unlikely to be 'distributed fairly or widely' if banks were 'left entirely to themselves'. Industrial finance corporations, on the other hand, would be able to achieve a wider dispersal of P.L.480 funds, particularly if they could be used to support lending to small industries. Making a case for including small-scale industries in the proposal, the Deputy Governor, B. Venkatappiah, also counselled that whatever the scheme adopted to channel P.L.480 funds, it should help foster, rather than undermine, existing initiatives and programmes of term-lending institutions and promote the accepted 'pattern of banking development' in India. The Bank also held to the view that the organization chosen or created to distribute P.L.480 resources should have the freedom to handle funds from other sources as well and be able to survive independently even after the American funds were exhausted.

Not long after these proposals were first mooted towards the end of 1956, another Deputy Governor, K.G. Ambegaokar, held a conference with bankers to discuss them. The bankers did not believe there was any danger of the additional resources being monopolized by a few interests, particularly since the amounts involved were relatively small and no bank was likely to get more than Rs 3 crores under the scheme. After this meeting, Ambegaokar too was inclined to follow the bankers in taking a 'less alarmist' view of their ability for 'mischief' in the distribution of the P.L.480 funds. But the view prevailed that the latter should be channelized through a central agency rather than directly to the banks or through the Reserve Bank. The Bank felt none of the existing agencies, namely the Industrial Finance Corporation, the National Industrial Development Corporation, the Industrial Credit and Investment Corporation of India, the National Small Industries Development Corporation,

and the state financial corporations, were suited to undertaking the additional responsibility. These institutions were set up for specific purposes and were bound by their constitutions. Besides, the functioning of the Industrial Finance Corporation had come under close scrutiny and attack in Parliament and elsewhere, and prospective borrowers hesitated to approach it for fear of adverse publicity. Many of these corporations, including the private sector Industrial Credit and Investment Corporation, also had surplus funds at this time in the form of deposits with banks or as investments in government securities and little purpose would be served by adding further to their resources.

Therefore, in the Bank's view, the balance of advantage lay with 'having an altogether new agency' to advance funds made available under the aid agreement with the United States government. It was originally proposed to set up a refinancing corporation, as a public limited company under the Companies Act. After further reflection, the Bank decided to set up the new entity as a private company (since this arrangement provided greater flexibility) jointly with the Life Insurance Corporation, the State Bank of India, and fourteen other major scheduled banks selected on the basis of their deposits.² Explaining the Bank's justification for this shortlist of participating banks, the Governor, H.V.R. Iengar, pointed out that these banks were being asked to undertake a 'novel' activity which was 'contrary to traditional conceptions of banking in our country'.

If there was any risk of loss—and in prudence we must always provide for such a risk—I was anxious that it should fall on the bigger banks who would find the incidence of the loss to be of small proportions rather than the smaller banks on whom the burden might be serious.

While the selected Indian banks readily agreed to participate in the proposed corporation, the four foreign banks were torn between their reluctance to foster the new company and a desire to maintain 'friendly relations' with the Bank and the Government of India. They also wanted to avoid appearing to be 'dragging their feet'. With the Americans finally coming round to the

² The fourteen banks were the Central Bank of India, Punjab National Bank, Bank of India, Bank of Baroda, National Bank of India, United Commercial Bank, Lloyds Bank, Allahabad Bank, Chartered Bank, Indian Bank, United Bank of India, Mercantile Bank, Devkaran Nanjee Banking Company, and State Bank of Hyderabad. The fifteen banks together accounted for nearly 80 per cent of the total advances of all licensed scheduled banks and 91 per cent of their industrial advances.

Bank's proposals for a new refinancing agency to channel P.L.480 resources, the foreign banks also fell in line. Their inclusion caused 'some rumbling of discontent' in Indian banking circles, but the Bank maintained that these institutions were not included in the scheme as exchange banks but on the strength of their deposits in India, and that it was bound by the government's policy of not discriminating between foreign concerns established in India and locally-owned enterprises.

According to the final proposals, the Refinance Corporation for Industry was to be set up as a private limited company with an authorized share capital of Rs 25 crores. The issued share capital of Rs 12.5 crores was to be distributed principally between the Bank (Rs 5 crores), and the State Bank of India and the Life Insurance Corporation (Rs 2.5 crores each). The remaining capital, of Rs 2.5 crores, was to be allotted to the fourteen other participating banks, their individual contributions ranging from Rs 10 lakhs to Rs 25 lakhs. The corporation's Board of Directors was to consist of seven members, with the Governor of the Reserve Bank as its Chairman, and one of the Deputy Governors, the Chairmen of the State Bank of India and Life Insurance Corporation, and three representatives of member banks as directors. Each of the participating banks was to be allocated a quota from the corporation's total funds of Rs 38.5 crores, comprising the issued capital of Rs 12.5 crores and a long-term loan of Rs 26 crores from the American counterpart funds of the Government of India. The State Bank's quota was fixed at Rs 5 crores, while the quotas of the other banks varied between Rs one crore and Rs 3 crores. Loans given by member banks to medium-sized industrial concerns for amounts not exceeding Rs 50 lakhs and for periods ranging from three to seven years were eligible for refinance within the quota specified for each bank. These loans were to be made for the purpose of increasing production, primarily to industries included in five-year plans. In order to ensure that medium-sized firms benefited from the lending facility, a ceiling of Rs 2.5 crores was stipulated for the paid-up capital and reserves of borrowing concerns. Lending banks were to assume the full credit risk on loans submitted to the corporation which was not expected ordinarily to concern itself with details such as the creditworthiness of borrowers or the adequacy of their collateral. Member banks were to be allowed a maximum spread of 1.5 per cent between their borrowing and lending rates.

The Committee of the Bank's Central Board approved these proposals in May 1957. The new corporation necessitated a few amendments to the Reserve Bank of India Act to enable the Bank to subscribe to its share capital and grant short-term advances of up to ninety days to institutions specified by the government. These amendments too, were shortly approved by the Committee

of the Central Board. Amendments were also considered necessary to the State Bank of India Act to enable the State Bank to extend term loans for periods exceeding six months. The two bills were taken up for consideration towards the end of May 1957, and passed by Parliament the same month. With this, the decks were cleared for the Bank to participate in the new institution.

The founding of the corporation had however to await the resolution of some uncertainties pertaining to the audit of P.L.480 funds, and it was not until June 1958 that the Refinance Corporation for Industry was registered as a private limited company. The corporation began operations in an office within the Bank's premises in Bombay, with T.K. Ramasubramaniam, Chief Officer, Industrial Finance Department, as its first General Manager. The corporation became a public limited company in March 1961 following an amendment to the Companies Act which automatically converted into public companies all private companies in which a quarter or more of the paid-up capital was held by corporate bodies.

The corporation's early performance fell below expectations. In the first two years, i.e. until May 1960, it managed to draw only Rs 5 crores from P.L. 480 funds, having sanctioned twenty-one loan applications for a sum of Rs 4.26 crores to five member banks. The Bank's review of its operations revealed that they were hampered by inflexibility. Hence it canvassed several proposals intended to enhance the operational flexibility of the Refinance Corporation. These included extending refinancing facilities to a larger number of banks without requiring them to become shareholders of the corporation, removing bank-wise refinance quotas, allowing the corporation discretion to determine which industries were eligible for refinance, dispensing with the limit on the maximum paid-up capital and reserves of borrowing concerns, raising the loan ceiling from Rs 50 lakhs to Rs one crore, and allowing banks freedom to set lending rates. These suggestions were discussed at meetings between representatives of the American Technical Cooperation Mission, the Government of India, and the Bank in January 1960. Though the Americans accepted most of these proposals, they did not favour raising either the ceiling on loans to individual borrowers or that on the latter's paid-up capital and reserves. The mission also suggested that the corporation should reduce the rate of interest on its loans from 5 per cent to a minimum of half a per cent above the Bank rate, refinance loans made to small-scale industries—a reform the Reserve Bank had favoured even in 1957—and extend its facilities to state financial corporations and apex cooperative banks.

Following these discussions, the corporation liberalized its refinance facilities in October 1960. Despite opinion within the Bank being sceptical

about the uses of the proposed reform, refinance facilities offered by the corporation were now extended to forty-three more banks and fifteen state financial corporations without requiring any of them to become its shareholders. The extension of refinancing facilities to state cooperative banks had engaged the Bank's attention since 1957 when R.G. Saraiya, Chairman of the Bombay State Cooperative Bank first raised the subject. Saraiya's view, that state cooperative banks should be included in the scheme since they lent substantial amounts to meet the longer-term needs of food-processing industries such as sugar, also had the support of the Bombay government. The Bank was not disposed to modify the scheme at the time, particularly as resources available under the Indo-American aid agreement were limited and state cooperative banks were already being financed or refinanced by the government or by other state-sponsored financial institutions. Besides, the Bank was uncertain whether cooperatives formed a distinct sector or were part of the private sector, some government documents such as those of the second plan, for instance, appearing to support the former interpretation. Clarification from the government that cooperatives indeed formed part of the private sector came almost at the same time as recognition dawned on the Bank that the 'outgo of funds' from the Refinance Corporation was 'extremely slow', and in March 1959 officials at the Bank toyed with the idea of allotting a quota of Rs 2 crores to all state cooperative banks and state financial corporations without making any of them members of the corporation. But citing the 'special position and needs of the cooperative movement', the Board of the Refinance Corporation opposed proposals to include apex banks in its refinancing scheme. The corporation appears subsequently to have been encouraged by the changed context to modify its views, since the state cooperative banks of Maharashtra, Madras, and Andhra Pradesh were admitted to its refinance facilities in October 1960. More state cooperative banks were added to the list later.

As part of the effort to promote the activities of the Refinance Corporation, it was also decided to widen the list of eligible industries and refinance loans to small-scale industries covered by the Credit Guarantee Scheme.³ The maximum period of loans eligible for refinancing was increased to ten years, and the assets ceiling of Rs 2.5 crores allowed to be relaxed in deserving cases. Bank-wise quotas were also removed and the rate of interest was left to be determined by the lending institution.

These initiatives were complemented by efforts to diversify the range of the corporation's refinancing activities. From 1961, it arranged to provide

³ For details of the Credit Guarantee Scheme, see chapter 14.

foreign currency loans through the ICICI, the Commonwealth Development Finance Company, and the International Finance Corporation to industrial concerns obtaining rupee finance from its constituents. Refinance facilities were further liberalized in 1961–62 by extending them to cover long-term loans made jointly by two or more banks or term-lending institutions, the medium-term part of such loans being defined as comprising instalments payable within seven to ten years, and to private sector coal-mining units receiving assistance from the World Bank. Following suitable modifications to the agreements on the basis of which it was founded, the Refinance Corporation introduced a scheme in January 1963 to refinance medium-term export credits extended by banks for periods from six months to five years at a concessional rate of 4.5 per cent on the condition that the financing bank did not charge more than 6 per cent from the borrowing firm. The interest charged on other exports and industrial loans remained at 5 and 5.5 per cent respectively. To assist small exporters shipping orders in several consignments, the corporation also agreed to refinance individual export credits of less than Rs one lakh each, provided the 'relative export contract' was for at least that amount.

The liberalization and diversification measures of 1960–61 appear to have succeeded in achieving the intended object of stepping up the pace of the corporation's activities. Applications it received for refinancing increased steeply from twenty-five (for Rs 4.6 crores) in 1960 to sixty-nine (Rs 11.27 crores) in 1961, eighty-eight (Rs 13.77 crores) in 1962, and 221 (Rs 29.96 crores) in 1963. Applications sanctioned also climbed from fourteen (Rs 1.75 crores) to fifty-nine (Rs 10.71 crores), seventy-three (Rs 10.63 crores), and 171 (Rs 24.09 crores) during the same years.

With the setting up of the Industrial Development Bank of India (IDBI) in July 1964, the Refinance Corporation had little reason to exist as a separate entity. The IDBI Act provided for taking over the business of the Refinance Corporation, and with the concurrence of the American authorities, the latter undertaking was transferred to the new institution in September the same year. The IDBI paid the Refinance Corporation Rs 2.5 crores (this equalled its paid-up capital) as compensation for distribution to shareholders in proportion to their contributions to its paid-up capital. The Refinance Corporation for Industry was dissolved on 26 July 1965.

Since its inception in June 1958, up to the end of August 1964, the corporation received in all 577 applications for Rs 88.15 crores under its refinance schemes. Of these, the corporation rejected twenty-four applications for Rs 4.49 crores. Refinance disbursed totalled Rs 42.25 crores, or nearly two-thirds of the amount sanctioned. The total refinance outstanding at the

end of this period amounted to Rs 36.72 crores. Apart from the initial allocation of Rs 26 crores out of P.L.480 *counterpart funds*, the corporation also received Rs 10 crores from the Government of India on an ad hoc basis pending an agreement with the US government for another line of P.L.480 credit. Although state financial corporations and state cooperative banks too received accommodation from the corporation after 1960, the overwhelming proportion (about four-fifths) of the refinance it made available went to commercial banks. Besides testifying to their success, the sharp increase in the 'outgo of funds' from the corporation after the liberalization and diversification measures of 1960-61 signified the *accelerated tempo* of private investment activity in industry and helped illustrate the latent demand within the country for an expanded industrial financing agency. The Industrial Development Bank of India was designed to meet this demand.

THE INDUSTRIAL DEVELOPMENT BANK OF INDIA

The idea of an industrial development bank is almost as old as the history of planned development in India. Two competing proposals were advanced in the early fifties. The first came in August 1953 from T.T. Krishnamachari, then Minister for Commerce and Industry in the Government of India, while the other proposal was advanced a few weeks later chiefly at the initiative of the American administration and the President of the World Bank, Eugene R. Black.

Krishnamachari's proposal was a relatively unusual one. He advocated extending the government's efforts to promote industrial development beyond establishing a 'few odd enterprises' and helping private enterprise 'in conventional ways ... to somehow do whatever else is needed'. Financial assistance to private enterprise might suffice in situations where entrepreneurs had already finalized their projects and were only attempting to raise the necessary resources. But where entrepreneurs were shy, Krishnamachari stressed, the State would have to take the initiative to set up industries, jointly if necessary, with private investors. But the 'ordinary machinery' of the government being unsuited to entrepreneurial tasks of this nature, TTK proposed an industrial development corporation comprising government nominees, scientists and engineers, and industrialists of 'proven reputation'. This corporation would have a wide brief: plan and initiate projects, coordinate investments, provide technical and managerial expertise, and help raise resources for undertaking these investments. Commending his proposal as the only way out of the 'present paradox of shortage of internal resources while we are adding to our idle assets abroad', Krishnamachari insisted that the

assets created by this corporation should, in due course, be sold to the private sector. Maintaining that it was necessary to look beyond 'traditional investors' who were both 'shy and dry', he argued in a follow-up note that his plan would attract the support of those who lacked 'faith in paper prospectus' and were unaccustomed to investing in shares, but who may be 'prepared to put their money in a going concern'. Apart from helping to widen the pool of private savings available for industrial investment, regular sales by the corporation of its assets would also help mop up the 'inflationary forces' generated by public investment and keep deficit financing in check. Since a statutory corporation would take time to establish, Krishnamachari proposed that the industrial development corporation should first be set up as a company under the Companies Act and converted in course of time to a statutory corporation.

Though it felt the proposal should properly be examined by the Shroff Committee, the Bank, when consulted by the Finance Ministry, was quite supportive of the idea of the government assuming an 'entrepreneurial role' through the proposed corporation and 'endeavouring to make good the deficiencies of private enterprise' But it felt the corporation's role would be a 'modest one until the resources available to it can be increased through an expansion of private savings'. It could not depend on banks to finance its activities since the Indian banking system already had as high a ratio of advances to deposits as was consistent with 'any assurance of safety'. Nor could the Bank provide long-term finance to the corporation through the banking system without hampering the flexibility of its monetary policy and assisting 'inflationary creation of credit'. Turning the proposal on its head, the Bank stressed that the corporation would be useful in 'promoting development where the obstacle ... is not so much the lack of material resources as the psychological inertia of the private sector'.

Even as the Government of India was engaged in considering this proposal, in October 1953 Eugene Black at the World Bank mooted the idea of setting up a privately owned and externally assisted industrial development banking institution in India. The precise antecedents of this proposal are not altogether clear. At a dinner meeting in Washington earlier the same year, the Governor, B. Rama Rau, aired the idea of setting up in India an institution modelled somewhat along the lines of the Commonwealth Development Finance Company in the United Kingdom. The audience included George Woods of the First Boston Corporation who, according to Rama Rau, was 'rather attracted by the idea'. At the same time or shortly thereafter, the US administration came up with the idea of using the counterpart rupee funds of a \$15 million steel loan to set up a development bank in India with assistance from the

World Bank. The proposal appears to have undergone extensive modifications at the World Bank where opinion favoured an institution owned very largely by private Indian investors (with some proportion of the equity held by overseas investors), and which would open a line of credit with the World Bank and confine its assistance to the private sector of Indian industry. It was in this form that the proposal was presented to the Government of India, and Black who, in B.K. Nehru's words, was 'most surreptitiously enthusiastic about the scheme', quickly followed it up by despatching a delegation comprising George Woods, Robert Craft (American Securities Corporation), and Joseph Rucinski (World Bank) to India at the end of January 1954.

As K.G. Ambegaokar, Secretary in the Finance Ministry, confided to the Governor, the Black proposals were based on what would go down best with the US Congress when it discussed American aid to India. The official Indian opinion on them remained divided. B.K. Nehru, who was in Washington at this time, was its most enthusiastic advocate, while Krishnamachari felt it would be difficult in Delhi's prevailing climate to adopt an idea based on American aid 'primarily and secondarily on aid from the IBRD which, though an international institution, has its policies tuned to the prevailing opinion' in the United States. Nor was he convinced that the Indian private sector was in a 'mood to invest ... money in a bank of this nature'. Although the Black proposals may have originated with him, Rama Rau's initial reaction to them was that ad hoc initiatives such as these ran the risk of preventing a unified view being taken of the needs of the private sector and of the means to mobilize private resources for investment. The Governor had good reason to be concerned, since the Black and Krishnamachari proposals threatened between them to dig up the landscape the Bank had entrusted to the Shroff Committee to survey. Misgivings were also expressed at the official level about the relative roles of this bank, the industrial development corporation proposed by T.T. Krishnamachari and approved in principle by the Cabinet, and the Industrial Finance Corporation. In particular, some officials apprehended that a soft loan to the proposed bank from the government may have the effect of diverting available private capital to 'productive industries in which the private sector is ordinarily interested', leaving the industrial development corporation to 'take over all the unproductive' or 'lame-duck' enterprises. However, a committee comprising Ram Nath and Secretaries to the economic departments of the Government of India which considered the proposal agreed generally that there was enough room for all three institutions to exist side by side, with the development corporation initiating and taking up new industries, the private bank assisting industrialists in their schemes, and the Industrial Finance Corporation financing existing industry.

Black's envoys stopped at London on their way to India. It had earlier been expected that the Commonwealth Development Finance Company (CDFC), a privately owned but State-assisted undertaking in the United Kingdom, would pick up part of the equity of the proposed development bank and thus help stimulate investor interest on Wall Street. But the Black proposals received a cool reception in London. Officials there were wary of an arrangement in which the CDFC undertook the risks of equity ownership while the World Bank made guaranteed loans to the development bank. Apart from some nervousness about the consequences for the sterling area balance of payments of higher levels of investment in India, London appears also to have been somewhat protective of its special position in India. These reservations were tempered to some extent by the view that refusal to assist the project might be construed in Washington and elsewhere as proof that Britain preferred to confine its development assistance to countries that were part of the empire. But officials in London steadfastly refused to commit themselves to the project. Krishnamachari was not alone in supposing that the Indian private sector would not subscribe much capital to the project. Opinions in London, which held that Indian businessmen were incapable of cooperating with one another in the public interest, and those of Indian officials such as B.K. Nehru in Washington, also ran along similar lines, so that when the World Bank team arrived in India after having failed to set the Thames on fire, a major unspoken question mark hung over the project for a development bank.

In the event, the delegation's visit to India was an unqualified success. The Government of India was quick to accept the principle of a privately owned institution to finance private sector investment. Differences persisted over the terms on which it would lend the counterpart rupee funds (\$15 million or Rs 7.5 crores) to a private company and over the World Bank's insistence that the chief executive of the proposed institution should be a foreigner capable of establishing its independence from contending business groups in India and facilitating the technical assistance that the international institution hoped to provide to it. But these differences were not allowed to hold up progress which was rapid. Following discussions with the government, it was agreed to set up an investment corporation (the idea of a 'bank' having earlier been abandoned since the term had a restrictive meaning under the Banking Companies Act) to stimulate the creation of new industries and expansion and modernization of existing ones, and promote the participation of private capital, both domestic and foreign, in Indian industries. In order to attain these objectives, it was intended that the corporation would provide capital assistance either in the form of loans or equity, and provide managerial and technical support. The subscribed capital of the corporation was to be of the order of

Rs 5 crores (\$10 million), the majority of which would be Indian. The World Bank agreed to make a long-term foreign exchange loan to the corporation of a similar amount, while the Government of India agreed to lend to the new entity counterpart funds of Rs 7.5 crores (\$15 million). The latter carried no interest, and repayments on the loan were not to begin until fifteen years had passed. The corporation was thus expected to start operations with total resources of Rs 17.5 crores. *Largely at the Bank's instance and in consultation* with Indian business interests, a steering committee with Ramaswami Mudaliar as chairman, and G.D. Birla, Biren Mookerjee, A.D. Shroff, and Kasturbhai Lalbhai as members was formed to help the project get off the ground and propose the initial composition of the corporation's Board of Directors.

The institution, finally christened the Industrial Credit and Investment Corporation of India Ltd., came into existence in January 1955, barely sixteen months after the first proposals for the institution were put forward. P.S. Beale, a former Secretary of the Bank, was appointed its first *General Manager*. The issued capital of Rs 5 crores was taken up by Indian banks and insurance companies, directors of the corporation and their associates (Rs 2 crores), British exchange banks and UK and other commonwealth insurance companies (Rs one crore), and American nationals and corporations (Rs 50 lakhs). Shares aggregating Rs 1.5 crores were offered to the Indian public in February 1955. The issue was oversubscribed.

T.T. Krishnamachari's proposal for an industrial development corporation, too, became a reality in October 1954 with the formation of the National Industrial Development Corporation as a *private limited company* with an authorized capital of Rs one crore, and a paid-up capital of Rs 10 lakhs provided entirely by the Government of India. The NIDC was authorized to issue shares and debentures, and to provide finance to industries related to planned development, in particular those manufacturing capital goods, machinery, and equipment. As well as taking up plans to study industrial schemes and manufacturing possibilities, the NIDC, it was expected, would also set up *greenfield projects involving ancillary linkages* with the private sector.

THE BANK'S SCHEME FOR A DEVELOPMENT BANK

If the institutional developments of the 1950s arrested some of the momentum towards setting up a fully-fledged development banking institution in India, the success of the Refinance Corporation for Industry in the early 1960s drew attention to the latent demand for long-term funds to finance industrial investment. Krishnamachari had mooted the idea of an industrial development bank to the Governor, H.V.R. Jengar, and others in 1956-57, and he resumed

his close interest in the subject early in his second stint as Finance Minister. He apparently felt the Industrial Finance Corporation of India (IFCI) was hampered in its operations because of being government-owned, and that a new development bank owned by the Reserve Bank, and thus free from political pressures, should be set up. According to some accounts, he brought up this subject almost without warning during a meeting with the Governor, P.C. Bhattacharyya, and after some discussions the latter communicated to the Finance Minister the general outline of the proposed development bank towards the middle of November 1963.

According to the Governor, the 'general conception of the new institution' was that it should be able to take a 'coordinated view of the problem of industrial finance in all its aspects in the context of planned industrial development'. Existing institutions financing industry were short of resources and were finding it difficult to raise resources on their own. Increasingly, therefore, they required access to the government or 'some central financing or refinancing institution'. The new institution, the Governor argued, should be able to provide additional finance through 'commercial banks and ... existing long-term lending agencies on a coordinated basis', after taking account of plan priorities and the relative needs of small-, medium-, and large-scale industries for medium- and long-term loans. The government, for its part, should discontinue its practice of lending to term-lending institutions except through this apex development bank.

In addition to refinancing, the proposed institution was expected directly to finance investments in strategic sectors that were beyond the abilities of 'normal lending institutions'. It would also undertake a 'positive promotional role' by commissioning research and techno-economic surveys to evaluate investment prospects in relation to plan programmes, and thereby stimulate investment and entrepreneurship in new lines of activity. It would engage a central pool of technical consultants to service term-lending institutions, particularly state financial corporations, which might not otherwise be in a position to engage such specialist advisers.

The Governor proposed that the new bank should have an authorized share capital of Rs 50 crores and a paid-up capital of Rs 5 crores distributed to existing shareholders of the Refinance Corporation and other financial institutions such as state financial corporations, the Industrial Finance Corporation, and the ICICI. The Bank, he suggested, could contribute any unsubscribed part of the capital offered to these institutions and the balance of the increased capital.

Bhattacharyya envisaged five sources of finance for the new bank. Funds under the P.L.480 programme would be routed through this

institution. Secondly, the government was to make an initial interest-free loan of Rs 10 crores to the development bank along the lines of that given to the ICICI. In addition, it would place new funds intended as special assistance for priority projects in a Development Assistance Fund which the development bank would administer as an agent of the government. For its part, the Bank might set up out of its profits a National Industrial Credit (Long-term Operations) Fund from which advances could be made to the development bank for long-term lending and to acquire shares and debentures of both industrial borrowers and long-term lending agencies. The Reserve Bank, the Governor proposed in a significant departure from past policy, should also rediscount eligible paper based on the development bank's loans to direct lending institutions for periods up to five years. Remarking that the Bank had not felt compelled to extend this step to the Refinance Corporation since it had access to other resources, the Governor pointed out that other central banks too had taken 'quite unorthodox initiatives in the field of industrial finance, and this departure from orthodox central banking canons is clearly justifiable in our conditions'. Finally, the development bank could raise funds of its own in the market with or without government guarantee.

The management of the new institution, the Governor suggested, should be integrated at the top with the structure of the Bank to ensure better policy coordination. To this end, he proposed that the Bank Act should be amended to provide for an additional Deputy Governor who would be the ex-officio Chairman of the development bank. Finally, although there was something to be said for calling the new institution the Development Corporation for Industry owing to the indirect character of its lending, the Governor said he preferred calling it the Industrial Development Bank of India to highlight its close association with the Reserve Bank. The Industrial Development Bank of India, the Governor stressed, would 'indeed be the reserve or apex bank of industry'.

The next steps were taken with the utmost despatch. The government's intention to establish the Industrial Development Bank of India was signalled in the *Economic Survey* for 1963-64, while the Finance Minister's budget speech for 1964-65 included a proposal to introduce the necessary legislation for bringing the bank into being. The Industrial Development Bank of India Bill was introduced in the Lok Sabha on 30 April 1964 and passed the same day. It was passed by the Rajya Sabha on 7 May, and secured Presidential assent on 16 May. The Industrial Development Bank of India Act came into effect on 30 June 1964, and the IDBI came into existence on 1 July 1964, i.e. within eight months of the Governor submitting the blueprint for such an institution to the Finance Minister.

Organization and Early Operations

The IDBI was a fully owned subsidiary of the Bank, with an authorized share capital of Rs 50 crores which could be raised to Rs 100 crores with the prior approval of the central government. In a departure from the original blueprint, the issued capital of Rs 10 crores was wholly contributed by the Reserve Bank. At the IDBI's instance, the Bank made a further subscription of Rs 10 crores to the share capital of the IDBI in June 1967, and its resources were also augmented by an interest-free loan of Rs 10 crores from the government. Apart from its own resources and the interest-free loan from the government, the IDBI was allowed to raise resources from the market by selling its own bonds and debentures with or without the guarantee of the government, and accept deposits from the public for periods of not less than one year, borrow from the Reserve Bank for periods up to ninety days against trustee securities and up to five years on the security of bona fide commercial bills or promissory notes of industrial concerns, and receive gifts, grants, donations, and benefaction from the government or any other source. It was also empowered to borrow, with the previous consent of the central government, foreign currency loans from any bank or financial institution in a foreign country.

The affairs of the IDBI were vested in a Board of Directors which was identical with the expanded Central Board of the Bank. The Governor of the Bank became the ex-officio Chairman of the IDBI, and a Deputy Governor was nominated by the Central Board as Vice-Chairman. (B.K. Madan was nominated the first Vice-Chairman of the Board of Directors of the IDBI.) The Bank also provided the bulk of senior staff for the IDBI in its early years. In June 1967 the IDBI comprised five main departments—Appraisal, Economic and Planning, Operations, Refinance, and Administration and Board. The Legal Department of the Bank attended to the legal needs of the IDBI. Considering the size of projects which required the IDBI's assistance, particularly in core sectors such as fertilizers, petrochemicals, machinery manufacture, cement, etc., the need was felt to strengthen the bank's technical staff to evaluate projects and better monitor the end-uses to which its assistance was being put. The Bank took charge of recruiting the necessary technical staff either directly from the market or on deputation from the government.

The IDBI took over the business of the Refinance Corporation for Industry from the beginning of September 1964. It also acquired the shares of the government and the Bank in the Industrial Finance Corporation, and together with a fresh issue to it of shares worth Rs 1.34 crores, the IDBI came to acquire 50 per cent of the shares of the latter corporation in August 1964. The

IDBI was also given financial and supervisory powers over the Industrial Finance Corporation. These powers had earlier vested in the central government. The Bank's Industrial Finance Department too, transferred some of its work to the IDBI. As the apex institution in the field, the IDBI was now given primary responsibility for providing financial assistance to other term-lending institutions and to individual medium and large industrial units. The needs of small industries, the study of industrial finance in its different aspects, and of gaps in its structure continued to be looked after by the Industrial Finance Department of the Bank.

Simultaneously with the founding of the IDBI, a new long-term fund known as the *National Industrial Credit (Long-term Operations) Fund*, as proposed by Bhattacharyya, was established by the Bank with an initial contribution of Rs 10 crores. The Bank made annual allocations to the Fund out of its surplus profits before these were transferred to the government. This Fund was utilized to finance the IDBI's subscriptions to the shares, bonds, and debentures of the Industrial Finance Corporation of India, state financial corporations, and other financial institutions notified by the central government such as the ICICI, and purchase by the Bank of bonds and debentures issued by the IDBI. The total contribution to the Fund at the end of June 1967 was Rs 30 crores, out of which the IDBI availed loans of over Rs 5 crores.

The explanatory memorandum to the IDBI Bill drew attention to the practice followed in other countries of governments placing at the disposal of their development banks counterpart, trust, or other funds for supplementing resources normally available to them. Accordingly, the IDBI was appointed the agency for administering and applying the Development Assistance Fund which the central government instituted in March 1965 to assist essential *industrial concerns* which were not attractive to commercial banks and other financial institutions, but were nevertheless of strategic national importance. The resources of this fund comprised contributions from the central government or any other source by way of loans, gifts, grants, and donations. Losses arising out of the fund's operations were to be charged to it, while the IDBI was reimbursed expenses of operating the fund. The total assistance sanctioned and disbursed since the inception of the fund and up to the end of June 1967 amounted to Rs 33 crores and Rs 26 crores respectively, the beneficiaries being two fertilizer companies. The latter amount also represented the IDBI's total borrowing from the government towards this fund which showed a profit of Rs 40 lakhs over these three years.

As anticipated, the IDBI quickly became the *pre-eminent* industrial term-financing institution in India. In 1966-67, for example, over Rs 62 crores of the total assistance disbursed by industrial term-financing institutions that

year of Rs 134 crores, was accounted for by the IDBI.⁴ The IDBI's dominance was particularly pronounced in respect of rupee loans (Rs 48.6 crores out of Rs 89.1 crores). It disbursed, besides, Rs 6.5 crores by way of subscriptions to shares and debentures of industrial concerns and Rs 7.1 crores as subscriptions to shares and bonds of other financial institutions in 1966-67. The setting up of the IDBI also marked a sharp upswing in refinancing operations. The total volume of refinancing made available by the Refinance Corporation for Industry since it was founded in 1958 and merged with the IDBI in September 1964 was about Rs 39 crores. Refinancing disbursed by the latter institution, on the other hand, averaged over Rs 20 crores in each of the first three years of its existence. Direct assistance sanctioned too was substantial, amounting to Rs 33.8 crores during the year ending June 1967, of which nearly Rs 10 crores were by way of underwriting assistance and guarantees. Total direct assistance sanctioned was of the order of Rs 75 crores during the three years ending June 1967, while the volume of underwriting assistance sanctioned during the same period aggregated Rs 16.3 crores. The total financial assistance outstanding to the IDBI as at the end of June 1967 amounted to Rs 144 crores.

THE UNIT TRUST OF INDIA

The Shroff Committee, it will be recalled, recommended the establishment of investment trusts in the public and private sectors to promote industrial investment. At the time when the proposal was first made, the Bank was distinctly unenthusiastic, preferring initiative in this respect to come from the private sector. In reporting to the Central Board on the recommendations of the Shroff Committee, Rama Rau acknowledged that the 'unit form of investment' would help small investors who had 'little or no knowledge of the investment market'. But there was little that either the Bank or the government could do about setting up unit trusts, he suggested, except perhaps to give 'consent to the issue of the capital applied for'.

The Central Board endorsed this position, and there the matter rested for some years. However, at the staff level the Bank never completely lost interest in the idea of unit trusts, some of which was reflected in two studies conducted by its Economic Department in January 1959 and June 1960. The latter study by K.M. Hanifa, which was published in the Bank's *Bulletin* in October 1960, reviewed the progress of investment trusts in Britain and the USA. Incomes of unit trusts, it pointed out, commonly enjoyed immunity from taxation

⁴ Industrial term-financing institutions here include, apart from the IDBI, the Industrial Finance Corporation, the ICICI, and state financial corporations.

provided they were overwhelmingly distributed among unit-holders. In the United States, for example, a trust had to distribute 90 per cent of its income before it could claim tax immunity. Tracing the evolution of ideas about *investment trusts in India*, the study recalled Manu Subedar's minority report as member of the Indian Central Banking Enquiry Committee (1931) in which he urged the creation of these trusts as vehicles for financing investment in industry. Manu Subedar's plea was not altogether wasted, as the colonial government soon decided to exempt investment companies from super-tax. Despite this concession, there were only a handful of such companies in India; and only two of them could be regarded as investment companies in the proper sense of the term. Many investment companies were promoted 'only to collect public money ... for employment to the advantage of the *management and directors in their speculative activities*'. Investments of several such companies, the study emphasized, were concentrated in the shares of a few joint-stock companies which were often either 'private companies' or those whose shares were 'not quoted on the Stock Exchanges'. Many investment companies, moreover, also counted direct loans and advances among their assets. The study found that the investments of a majority of these companies were not, by and large, 'sufficiently diversified ... or strictly disinterested'. Only two investment companies, the *Industrial Investment Trust* associated with the stock-broking firm of Premchand Roychand and the *Investment Corporation of India* (controlled by the Tatas) held reasonably large and well-diversified portfolios of securities, the former having deployed over Rs 1.25 crores in 200 different securities and the latter Rs 3.5 crores in twice as many securities. Echoing the recommendation of the Shroff Committee, the article noted the wide scope that existed for large industrial or financial houses to form unit trusts. The State, it suggested, should encourage the process and regulate the functioning of these intermediaries from the point of view of *safeguarding the interests of their investors*. Unit trusts, the article concluded, would help mobilize the resources of small savers for industrial investment and democratize industrial share-ownership as envisaged in the directive principles of the Indian Constitution.

Both while in Commerce and Industry and as Finance Minister in 1956-57, TTK had been casting about for ways to boost public confidence in the stock markets. He was an enthusiastic advocate of the newly-established Life Insurance Corporation playing a more active role in promoting the demand for industrial equities. TTK's unfortunate decision to invest the organization's funds in the concerns of Haridas Mundhra partly reflected this wider motivation, but he also appears to have given some thought to setting up a mutual fund in the public sector. This idea had not taken any concrete shape

when TTK resigned as Finance Minister in February 1958; while the circumstances attending his departure rendered inopportune any effort to press ahead with the formation, particularly in the public sector, of institutions designed to mobilize and move large resources into securities offered largely by privately owned enterprises.

Two factors appear to have come together in the early 1960s to give fresh impetus to the formation of unit trusts. The accelerated pace of public investment and industrialization during the second plan and the early years of the third plan created conditions for stepping up private investment in industry. At the same time, the dust raised by the Mundhra affair, following which investment decisions of the public-owned Life Insurance Corporation of India came under intense public scrutiny, had begun to settle. With little prospect in sight of private interests establishing genuine investment companies, the government decided in the early part of 1963 to take the initiative to form a unit trust in the public sector. TTK was once again the moving spirit. As Minister for Economic Coordination, he is said to have sent the proposal to the Prime Minister who, in turn, pressed it on the Finance Minister, Morarji Desai. Intervening in the debate on the 1963–64 budget, Finance Minister Morarji Desai disclosed to the Lok Sabha his intention to set up an investment trust which would afford the ‘common man a means to acquire a share in the widening prosperity based on steady industrial growth’, that combined ‘security and a reasonable return’.

Events thereafter moved swiftly, at any rate within the Bank to which the task of preparing the blueprint for the unit trust and the draft legislation was, naturally enough, entrusted. As it happened, the Economic Adviser, V.G. Pendharkar, Hanifa, and other officials at Mint Road had been working on just such a scheme, and following discussions between Bhattacharyya, the Deputy Governor, M.V. Rangachari, the Executive Director, B.K. Madan, and the Legal Adviser, B.N. Mehta, a draft bill called the Unit Investment Trust of India Bill was drawn up as a basis for discussion, and sent to the government in July 1963. Unlike elsewhere such as in the United Kingdom, the proposed trust was designed both to manage its business and hold securities. It was to have an initial capital of Rs 5 crores, half contributed by the Bank and the other half by the Life Insurance Corporation, the State Bank of India and its subsidiaries, the Industrial Finance Corporation, the ICICI, and scheduled banks. The Board of Trustees was to have six members, with a Chairman and one trustee nominated by the Bank and the remaining trustees nominated by the other subscribing institutions. The proposal envisaged the trust having powers to borrow from the Bank against government and trustee securities. The income of the trust, it was proposed, would be allocated between

unit holders and subscribing institutions in the proportion the face value of the unit capital bore to the original fund. The actual cost of managing the unit scheme was not to exceed 5 per cent of the income allocated to the unit capital. Other costs, such as interest charges on any sums borrowed by the trust and any other necessary provisions, were also limited to 5 per cent, so that at least 90 per cent or more of the notional income allocated to unit capital was available for distribution to unit holders. The blueprint also suggested a number of tax concessions to assist the new institution and enhance the attractiveness of units as a form of investment. As a 'conduit company', the trust was to be exempted from paying any tax on its income or capital gains. This was done to avoid double taxation. More importantly, members' dividends were not to be subject to tax at source since the average unit holder, who was likely to be a small saver, would find it irksome to claim credit for the deduction; as a further incentive to small unit holders, incomes on units up to Rs 1,000 were to be free from tax; and finally, *transfers of units did not attract stamp duty.*

The Government of India decided to discuss the blueprint with an expert on unit trusts whom the World Bank proposed to depute. This meant some delay, but in the meantime, the committee of economic Secretaries of the Government of India approved the essential elements of the Bank's plan in October 1963 and decided to press ahead with it. Besides venturing a few suggestions of its own the committee also took decided views on issues which the Bank's plan had steered clear of. Chambers of Commerce, for example, had suggested to the government that the proposed unit trust legislation should be of a permissive character applicable to trusts both in the public and the private sector. The committee dismissed this suggestion on the plea that privately run unit trusts might, much in the manner of investment companies before them, come under the influence of managing agency houses and business groups. Intense competition between trusts for the limited amount of business that was likely to be available, it was feared, would also affect the viability of all of them. Besides, it would be necessary to provide for appropriate supervision and control over privately managed unit trusts. The committee also balked at the prospect of extending tax concessions to privately owned institutions whose business was not effectively 'supervised and directed by agencies acceptable to Parliament and the public'. Except for that relating to viability, the committee's other concerns regarding privately run unit trusts could have been addressed through appropriate regulatory and supervisory measures. But it appears to have rejected the latter approach, preferring instead to establish the Unit Trust of India as a de facto public sector monopoly. The Bank, on the other hand, preferred the more open stance of first watching the

working of the proposed trust before determining whether other similar public or privately owned institutions should be allowed into the business. The World Bank consultant, one Mr Sullivan as the Bank's records refer to him everywhere, also apprehended that the government intended to create a public sector monopoly, but the Indian authorities maintained that while unit trusts could exist in the private sector, they should not expect to receive the tax concessions proposed to be granted to the Unit Trust of India.

The committee of Secretaries was also in favour of the government having the power to nominate two trustees, issue directions to the trust on matters of policy involving the public interest, and approve regulations framed by the trust. Senior officials at the Bank, including Pendharkar, believed these provisions excessive in relation to the concerns they might be intended to address. The bill provided for the trust being run along business lines and it was unlikely, in their view, that the objectives of the trust would conflict with the public interest. The Bank managed to bring the government round to its point of view, with the committee of economic Secretaries clarifying subsequently that directives would be issued to the trust in consultation with the Bank and

that in its administration the Trust should not function like a Department or like a statutory Corporation; it should be run more like a Company, and the best available talents in the investment field should be secured to maximize the efficiency and profitability of the Trust.

As a further step towards ensuring that the trust functioned according to business principles, the committee wanted it explicitly clarified that it was not intended to promote 'the cooperative movement or the development of backward areas'. The committee also rejected the idea of placing any ceiling on the number of units owned by any single individual since such restrictions might militate against the objective of promoting savings in the community. The trust, the committee agreed, would invest its funds only in listed securities, and could underwrite issues of new capital with the prior permission of the Bank. Units, it proposed, should have the status of trustee securities and their ownership should be confined to individuals.

The consultant from Washington, Mr Sullivan, was a close friend of the World Bank President, George Woods, and the former head of a medium-sized US mutual fund. Sullivan and his wife arrived in India in October 1963. Apart from indulging the amateur interest he and his wife had in archaeology, Sullivan had two comments to offer on the Bank's unit trust

plan. Confining the ownership of units to individuals, he suggested, was unnecessary and restrictive, and he urged India to adopt the practice of small US pension funds in this respect. The trust, Sullivan also suggested, should have powers to suspend its repurchasing obligations in the event of emergencies, such as stock exchange closures, when it might not be in a position to realize its investments.

Neither suggestion found much favour with the Bank. Pendharkar, who played the major part in giving practical shape to the idea of a unit trust, was inclined to make light of the particular threat Sullivan apprehended, since the proposed trust was to have the power to borrow from the Bank for up to eighteen months. Nor did he see any advantage in allowing corporate bodies to hold units. Not only would the latter's motives for doing so have little in common with the trust's objective of promoting a new vehicle for household savings, their operations might be such as to promote instability in the price of this asset. While such risks were negligible in the case of small firms, Pendharkar felt there was little point in partners of such firms being allowed to own units in that capacity, rather than as individuals. In the end, however, the government decided to overrule the Bank and not to restrict the ownership of units to individuals. This freedom became a source of some embarrassment to the Unit Trust within three years of its coming into existence, and on other occasions thereafter.

The Unit Trust of India Bill, 1963, as drafted by the Bank and amended in line with the views of the committee of economic Secretaries and in some other respects, was introduced in Parliament on 26 November 1963 by T.T. Krishnamachari who in the meantime had become the Finance Minister. In the debate on the bill, members expressed apprehension that the investment policy of the trust might come under the control of large business houses or the Finance Ministry, or that 'pro-government companies' might walk away with a lion's share of its investments. Some members expressed concern for small investors who might suffer capital losses and adverted to the possibility of speculative transactions in the absence of limits on the ownership of units. Questions were also raised about the trust becoming a state monopoly and the possibility of establishing similar institutions in the private sector. Replying to the debate, the Finance Minister clarified that the government did not intend to interfere in the investment policy of the trust and that it was not practical to limit the holding of units by individuals. The question of unit holders being represented on the Board of Trustees of the trust was raised in both houses, with the government holding to the view that the nomination of such representatives was best left to the Bank. An amendment to add 'or Calcutta' after Bombay in the clause dealing with the location of the head

office of the trust was not accepted on the ground that the new institution would be managed by the Bank which had its head office in Bombay. The bill, which passed the Lok Sabha on 5 December and the Rajya Sabha on 12 December, received the President's assent on 30 December 1963. It came into effect on 1 February 1964 on which date the Unit Trust of India came into existence as an offshoot of the Bank. Soon after its inception the Trust opened branch offices in Calcutta (1964), Madras (1965), and Delhi (1967).

Set-up and Organization

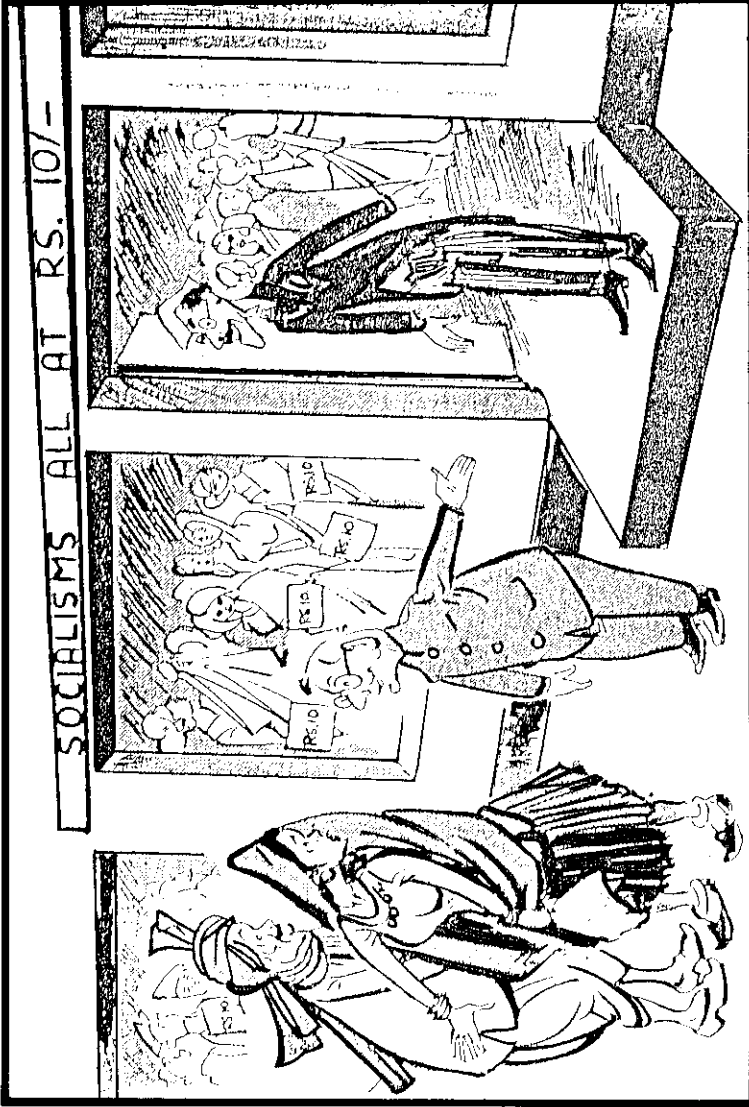
The Unit Trust of India came into existence with an initial capital of Rs 5 crores allocated between the Reserve Bank (Rs 2.5 crores), the Life Insurance Corporation (Rs 75 lakhs), and the State Bank of India and its subsidiaries (Rs 75 lakhs). Scheduled banks and other financial institutions were allocated Rs one crore, despite their subscriptions exceeding this amount by about 10 per cent. Almost all foreign scheduled banks in India contributed to the initial capital. The Industrial Finance Corporation (Rs 25 lakhs), the ICICI (Rs 15 lakhs), and the Bank of India (Rs 10 lakhs) between them accounted for half the contribution from scheduled banks and other financial institutions. The Trust was allowed to raise resources by borrowing from any person or institution in or outside India other than the government or the Bank. It was also authorized to borrow from the Bank for short periods up to ninety days against trustee securities and for the medium-term up to eighteen months against the security of its bonds, with the approval and guarantee of the central government. The Unit Trust Act, as originally passed, allowed the organization to float only one unit scheme. However, in 1966 this limiting provision was relaxed to enable it to borrow against any other securities specified by the Bank for schemes other than the first unit scheme, subject to a ceiling of Rs 5 crores for each such scheme and Rs 10 crores in all.

According to the Unit Trust of India Act, the general superintendence and management of the Trust was vested in a board of ten trustees, of whom the Chairman, the executive trustee, and four other trustees were nominees of the Bank. While the Life Insurance Corporation and the State Bank of India would each nominate a trustee, two others were to be elected by the other contributing financial institutions and scheduled banks. The first Board of Trustees was constituted on 1 February 1964 with R.S. Bhatt, who was then the Executive Director of the Indian Investment Centre, as the whole-time Chairman. Bhatt narrates a business meeting in October 1963 with Bhattacharyya at the end of which he was asked his opinion on the best person to head the new Trust. Bhatt apparently named himself and H.T.

Parekh, at that time General Manager of the ICICI, as the 'only two persons who can handle the job'. The Governor confessed to Bhatt that he had these two names in mind but that every time he mentioned them to G.L. Mehta, who was chairman both of the ICICI and the Indian Investment Centre, 'he hits the roof'. Apparently at Bhattacharyya's instance, Krishnamachari spoke to Mehta about sparing Bhatt's services. Mehta, according to Bhatt, relented under pressure from a 'firm and determined' Krishnamachari who was insistent that his nominee 'should take charge of the Unit Trust in Bombay' right from its inception.

Bhatt served as the Chairman of the Trust for a little over eight years, until the end of April 1972. The Bank's Economic Adviser, V.G. Pendharkar, was appointed the first executive trustee on a part-time basis till the end of July 1964 after which he became a trustee in place of B.K. Madan who was elevated as Deputy Governor. Pendharkar was succeeded by R.C. Sachdeva, and he in turn by S.D. Deshmukh. The Chairman, the executive trustee, and two other trustees constituted the executive committee of the Trust. Competent to deal in all matters handled by the Board, the executive committee functioned practically as the investment committee of the Trust. The general regulations of the Trust, which were framed by the Bank, laid down that the Trust's investment in any one company should not exceed the lower of 5 per cent of its total investible funds or 10 per cent of the securities issued and outstanding of the company. Debentures were, however, excluded from the purview of this regulation in August 1964. As it had done for the Refinance Corporation and the Industrial Development Bank of India, the Bank once again provided the new institution with trained and experienced staff, particularly in its early years. The Bank arranged to undertake 'integrated recruitment' of personnel *for itself and the Trust*. This practice, of the Trust's officers and staff coming to it on deputation from the Bank, continued beyond the end of the period covered by this volume. As Bhatt acknowledged on the eve of laying down office as Chairman at the end of March 1972, this arrangement placed at the Trust's disposal 'highly trained and experienced officers and personnel from the ... Bank' and enabled it to cope successfully with a 'growing and diversified volume of work'. More broadly, as Bhatt pointed out to the government in 1970 in the course of representing to it that the Trust should not be brought under the jurisdiction of the Comptroller and Auditor General of India, although a 'statutory corporation' the Unit Trust worked 'in fact ... nearly as a department of the Reserve Bank and directly under its control'. Sponsoring the Trust as part of the Bank's family of financial institutions, Bhatt maintained, gave it a sound start and enabled the relatively new concept and institution to get off the ground smoothly.

Salesmanship



Mr. Krishnamachari said, the Unit Trust scheme aims at ushering in socialism.

- Shankar's Weekly, 12 July 1964

Business Activities

The first scheme of the Unit Trust of India, called the Unit Scheme 1964, was launched in July 1964. Prepared following a study by Pendharkar of the operation of similar schemes in the United Kingdom, it was framed more or less on the lines of a Trust Deed issued by unit trusts in the United Kingdom defining and regulating the rights and obligations of trustees and unit holders. Gazetted on 30 May 1964, the scheme came into operation on 1 July 1964 when it was inaugurated by the Finance Minister. Adopting the technique of block offer, units were offered at a face value of Rs 10 for a period of four weeks initially. Bowing to public demand, the Trust extended this period by another two weeks up to 14 August 1964. Thereafter, units were available at prices which reflected earnings on them since July. Contributions amounting to Rs 17.37 crores were received during the initial offer period, while contributions during the rest of the first year of the scheme amounted to Rs 1.77 crores.

Unit sales which amounted to Rs 19.14 crores in the first year, declined to Rs 2.15 crores in the next year, but picked up in 1966–67 to reach Rs 9.24 crores. The principal reason for the decline in 1965–66 was that the dividend of 6.1 per cent declared by the Trust for the first year appeared low against the background of a rising trend in yields which followed the hike in the Bank rate from 5 to 6 per cent in February 1965. The Trust declared a higher dividend of 7 per cent in 1965–66, and sales of units responded almost immediately. Besides, with the merger of super tax and income tax, the tax benefits available on incomes from units up to Rs 1,000 also became available more widely.

At the Bank's instance, participating commercial banks agreed to act as selling agents of the Trust. Later, post offices were brought into the picture, and registered brokers of stock exchanges and scores of individuals were appointed agents. A study by the Bank revealed that nearly two-thirds of the units sold up to the end of 1965 were concentrated in the five major cities of Bombay, Madras, New Delhi, Calcutta, and Ahmedabad. Further the bulk of the applications came from middle-income investors for lots of one hundred units or less. Salary and wage earners accounted for about half the applications received.

The Trust's repurchase operations commenced in November 1964. Prices of units were fixed daily, based on the net asset value of the underlying securities with reference to the closing stock exchange quotations of the preceding day and the income flowing into the Trust's coffers each month. There was a difference of 5 per cent between the sale and repurchase price of units. Repurchases in the early years were of the order of 4.5 per cent of units sold, compared with track averages of 6 to 7 per cent in the United States and

the United Kingdom. There was some speculation in the press about the price of units rising when the index of share prices was nudging downwards. Clarifying this seeming paradox in a letter to the Editor of the *Financial Express* which commented upon it, Bhatt pointed out that the value of the Trust's portfolio fluctuated much less than the index of share prices because the former was dominated by cash, rather than cleared, securities. Besides, unit prices reflected not only the underlying value of securities (less expenses) but also the accumulated income of the Trust.

Investment Policy

The Trust's investment policy was based on the need to balance security of capital and that for an adequate return 'including reasonable capital appreciation'. At their first meeting, the trustees decided to invest about 15 per cent of the initial corpus in government securities or other trustee securities and in cash, a quarter in debentures or cumulative preference shares, and not more than 60 per cent in first-class equities of companies. Since a considerable length of time might elapse before they managed to distribute the initial corpus along the intended lines, the trustees wished to invest the entire corpus immediately in short-dated securities and requested the Bank to extend to their institution the same facilities (of buying back securities at the prices at which it sold them) available to the Deposit Insurance Corporation and other organizations. The Bank demurred, feeling that the Trust should function on commercial and business lines and that it should not benefit from hidden subsidies such as a waiver of commission or the cushioning of investments from the ordinary fluctuations of the market. However, it agreed to charge the Trust for a limited period of three months commission at one-sixteenth of one per cent on sales and no commission on repurchases. The Trust also entered into an arrangement with the Bank to buy and sell government securities at the prevalent market rates.

The Unit Trust of India decided to invest not less than a fifth of the capital of the first unit scheme in government and other trustee securities and cash or debentures, and the remainder in equities and cumulative preference shares of sound companies with good dividend record and growth prospects. In order to achieve a balanced portfolio, it also decided to invest 55 to 60 per cent of the unit capital in fixed interest bearing assets and the rest in variable dividend securities or equities. The executive committee approved the list of eligible securities and implemented the investment policy of the Trust. The depressed conditions of the stock market in 1965-67 proved a blessing in disguise as it provided the Trust with an opportunity to build a sound portfolio of stock at attractive prices. The Trust's total investments at the end of March 1967

aggregated Rs 29.8 crores. Of this, ordinary shares of corporate enterprises accounted for Rs 13.4 crores (44.8 per cent), preference shares for Rs 3.6 crores (12.1 per cent), debentures for Rs 12.1 crores (40.7 per cent), and bonds of financial corporations and electricity boards for Rs 72 lakhs (2.4 per cent).

Floating New Schemes

Early in 1965, the Trustees began thinking about formulating other unit schemes and amending the Unit Trust of India Act which, as originally framed, limited the Trust's activities to the one scheme. The committee of Trustees set up for the purpose recommended that the Trust should be enabled to float new unit schemes. This was approved by the Bank. But other recommendations of the committee, such as utilizing P.L.480 funds for augmenting the Trust's capital and declaring units as trustee securities, did not find much favour. The committee also proposed a reserve fund to provide for possible future losses arising out of a fall in security prices while the Trust continued to repurchase units at a price not lower than their face value. The Bank, for its part, endorsed the idea and volunteered to contribute to the fund out of the income it received from the initial capital subscribed by it. In February 1966 Parliament passed the bill amending the Unit Trust of India Act allowing it, among other things, to float other unit schemes. Following this, the Trust announced a 'Reinvestment Plan' in July 1966 offering unit holders the facility of automatically reinvesting the income they earned from units. At the Trust's urging, the Bank appointed a working group in June 1966 under Pendharkar to formulate a scheme offering both savings and insurance benefits. This group, which also comprised representatives from the Posts and Telegraphs Board and the Life Insurance Corporation, formulated the Unit Linked Insurance Plan which the Trust introduced in October 1971.

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