
Venturing Overseas

This period also saw a significant expansion in the number of overseas branches of Indian banks. The Reserve Bank of India is empowered by the Banking Regulation Act to issue licences to commercial banks incorporated in India to open a branch or office either in India or abroad. No branch or office in India, in other words, can operate without the licence. Nor can a foreign bank open a branch or office in India without getting a licence. Indian banks are required to obtain the approval of the Bank before opening offices abroad. Licensing the entry of a bank through a branch or office requires policy-makers to take into account a variety of considerations, not all of which are purely commercial. The process of consideration requires the Bank to consult a number of departments within its own organization and other ministries through the nodal Finance Ministry. Given the multiple considerations, the Bank did not attempt to frame any definitive policy or guidelines in regard to the opening of branches or offices abroad by Indian banks till almost the onset of the 1980s. There was also no clear-cut procedure laid down for the processing of an application in this regard. Nor, in general, did Indian banks show much interest in venturing overseas.

Three major elements influenced the Reserve Bank's policy towards Indian banks opening offices abroad till the early 1970s. First, and overriding all else, there was the question of foreign exchange for meeting the capital requirements and other expenses connected with the setting up of an office. Given the scarcity of foreign exchange reserves, the Bank and the government were concerned about the foreign costs. Foreign exchange was allocated on the basis of potential benefits and costs. Second, there was the issue of business potential. This was related to the number of persons of Indian origin residing in the country in question. The perception was that the branch or office abroad would grow in size if it was supported by a large number of ethnic Indians. Third, there was the principle of 'reciprocity'.

For instance, during 1963–64, Punjab National Bank as well as Bank of India applied for opening offices in the United States but the Bank did not grant them permission on the ground that requests could in turn come from US banks to open offices in India. In 1964, Bank of India sought permission to open offices at Hamburg, Dusseldorf and Milan but these requests too were turned down on the ground of possible application of the reciprocity principle, which, at that time, was considered undesirable from the exchange control angle—i.e. having to permit remittance of profits by branches of foreign banks as well as from the point of view of its adverse effect on the expansion of business of Indian banks within India. The Bank was cautious about allowing foreign banks to expand in India. It expressed its concern about this several times.

Soon after the introduction of social control over banks, in November 1967, foreign bankers met Deputy Prime Minister Morarji Desai. RBI Governor Jha took the initiative of writing to S. Jagannathan, who was the Finance Secretary outlining the policy. Jha foresaw that foreign banks would raise a point about the policy on opening of new branches.

While none of them is being uncooperative in respect of any of the suggestions which we make, by and large they are seeking to be accepted and recognized as Indian banks and to have wider opportunities for opening of branches so that they can mobilize more deposits. As you know, the policy in this respect has been to restrict them to the port towns, and even in respect of port towns for the last few months I have given no new approvals until future policy regarding banking was clearer. Now that there is no proposal to nationalize the banking system, I think it is but fair to tell the foreign banks that we would have a stable long-term policy regarding branch expansion.

Jha also enquired whether foreign banks should be allowed to go outside the strict confines of port towns. At least one of them was anxious for permission to open a branch in Poona on the ground that industrialists in Poona were exporting on a large scale and that, in effect, Poona was an extension of Bombay. Jha said that permission to open branches in other industrial cities like Ahmedabad and Kanpur might also be sought on similar considerations and pointed out that Delhi was already open to them. ‘One idea that I have in my mind, which I confess I have not considered in full, is to link the total amount of sterling which they bring in as a permanent measure not to their volume of business but the number of their branches.’

Jha expressed these views within the Reserve Bank as well. He wondered

whether the view that the deposits that a new foreign bank branch mobilized were mainly at the expense of deposits that would have otherwise gone to other Indian bank branches could be supported by data, in which case the continuing strictness with regard to licensing of foreign bank branches in the country would be justified. Although there is no evidence of any such study having been conducted within the Bank, this policy was followed throughout the period under review.

Much later, on 7 February 1979, Governor I.G. Patel wrote to Manmohan Singh, who was then the Finance Secretary, 'we continue to adopt a restrictive policy in allowing foreign banks to open branches in India', and

within this restrictive policy, we aim at diversifying the presence of the international banking community in India and not enlarging that part of the international banking community which is already represented in the country. Accordingly, the UK and the US banks will not be encouraged to enlarge their presence in India and we would prefer opening of new branches in India by banks from countries not already represented in India but where Indian banks have branches. The principle of reciprocity will be a major consideration in dealing with these cases although it would not be desirable to try and quantify how exactly 'reciprocity' is to be defined. This will naturally vary from region to region.

This viewpoint was accepted by the government.

THE QUESTION OF RECIPROCITY

This view about reciprocity was probably appropriate. The fact is that, notwithstanding the legal position relating to the licensing of banking companies in India and of branches abroad, as given in Section 22 of the Banking Regulation Act of 1949, the principle was not spelt out in detail. But reciprocity, in practice was not viewed as a rigid position. It was applied flexibly in the early years of the period covered by this volume. For example, in June 1969, under the aegis of the Indo–Iran Commission for Economic, Trade and Technical Cooperation, the two countries explored the possibilities of closer cooperation between their banking systems. When the Reserve Bank examined the legal position in Iran, it found that no foreign bank could open a branch in Iran and that only joint ventures were permitted, provided at least 51 per cent of the capital was held by Iran or Iranians. Opening a branch also involved remittance in foreign exchange of about

Rs 15 lakh to comply with the minimum capital requirement under the laws of Iran, which amounted to one hundred million rials, with 50 per cent of it forming the paid-up capital. As regards an Iranian bank opening an office in a port town in India, the Bank saw no objection, even though it meant a relaxation of the practices followed till then. There was, however, one precedent to cite in favour of allowing an Iranian bank to open an office, namely, the grant of licence to Bank of America. This exception had been made in consideration of the role that Bank of America had played in financing Indian enterprises.

Another example was of Indian Overseas Bank, which had a branch in Thailand at the time of nationalization. As the Thai government did not, as a matter of policy, permit branches of nationalized banks of other countries to function in Thailand, the Indian Overseas Bank branch was converted into a branch of a private bank in September 1973. The newly created bank was named Bharat Overseas Bank Ltd, to make it distinct from Indian Overseas Bank. It took over the assets and liabilities of the Bangkok branch of the erstwhile Indian Overseas Bank Ltd and commenced business from 26 October 1973. No foreign exchange remittance from India was required for meeting the preliminary expenses of the Bangkok branch. The new branch had, however, to invest 10 million baths as additional capital. The Reserve Bank allowed Bharat Overseas Bank Ltd to open the branch at Bangkok under Section 23 of the Banking Regulation Act, 1949.

This flexibility did not mean that the RBI was not concerned about the possible demand for application of the reciprocity principle by other countries. In general, the offices of Indian banks abroad performed well in terms of earnings, notwithstanding the temporary setback to the process of increasing the presence of Indian banks in the United Kingdom on account of the fraud at the Central Bank of India's London branch in the Sami Patel case.

The working arrangement was that the Reserve Bank would consult the Finance Ministry on applications from banks to open branches or offices abroad. An important reason for this was the need to ascertain the views of the Ministry of External Affairs and the Commerce Ministry. This often created tensions.

Nationalization added a new dimension. The first problems arose when the Reserve Bank made a routine reference to the government, in June 1972, regarding the opening of a representative office by Bank of India in Jakarta. The Bank had earlier approved the State Bank of India's application to open a branch in London's West End. The government was critical of the Bank giving approval to SBI without consulting it. D.N. Ghosh, Joint Secretary in the Department of Banking, wrote to Hazari on 23 November that the

opening of a branch or a representative office by an Indian bank in a foreign country has political overtones. The government will have to keep in view the mutual relations between India and the country concerned, and also the future prospects. Therefore, he suggested, whenever any application from any bank is received for opening a branch or a representative office in a foreign country, whether for the first time or not, a reference may be made to Department of Banking; it would in turn consult the Ministry of External Affairs and the Department of Economic Affairs, and communicate the views of the government to the Bank. He further wrote that it would be greatly appreciated if this was followed as a convention in the future, and that this had the approval of the Finance Minister.

Governor Jagannathan was irked by this. He asked the Department of Banking Operations Division (DBOD) to see if any recommendation had been received in recent years from the Ministry of External Affairs or Foreign Trade through the Finance Ministry. DBOD confirmed that the Reserve Bank had received a reference in August 1967 from the government calling for comments on a suggestion made by the Indian Ambassador in Indonesia to open an office of an Indian bank in Jakarta. As the proposal involved a remittance of US\$ 1 million and SBI had expressed its inability to provide the requisite funds from its overseas branches, the government was informed that it might not be worthwhile to pursue the matter. However, at a meeting between Hazari and Bakshi, the Secretary in the Banking Department, Hazari was given to understand that the government had no objection to Bank of India opening a branch in Djakarta. Hazari, in reference to Ghosh's letter, said it would be better to get a general approval from all the ministries concerned rather than accept a procedure of formally consulting the government on each proposal. The latter procedure, he said 'would be time-consuming, ad hoc and in terms of perspective, unsatisfactory'.

Jagannathan agreed with this and during his subsequent discussions with N.C. Sen Gupta, who was Additional Secretary in the Department of Banking, he set forth what he termed as the Reserve Bank's 'ideas'. He said it would be advantageous to have branches opened in Germany for 'trade reasons', and in France because a French bank was already functioning in India and it could be, therefore, expected to reciprocate. Referring to the branches to be opened in West Asia, the Governor added that it would be advantageous for one more bank, namely, SBI, to open a branch in Tokyo and Indonesia or reconstitute the existing branch in Thailand, and to consider especially the question of opening branches in Africa.

The Bank's 'ideas' went down poorly with the government. Sen Gupta

wrote to Hazari on 13 July 1973 that the 'decision to open banking offices abroad' is a 'complex matter involving various aspects—political relations, trade prospects, foreign exchange release, etc.' The government felt it necessary to state that while overseas banking had so far been confined to the UK, East Africa and Southeast Asia, it would be desirable to have a chain of branches of Indian banks opened in Afghanistan, Iran and the Persian Gulf area right up to Lebanon, and another chain from Singapore to the Philippines, because of the expected growth of India's exports to these areas. The government also felt that profitability should be a vital consideration and, as such, it was necessary to weigh the volume of business that was likely to accrue against the overhead expenses of branches, which would be especially high in Western Europe, the US and South America, before deciding on the opening of branches. The government also recognized to keep in view the possible use of the reciprocity principle by foreign countries, and the need to give thought to issues of logistics relating to training of personnel and control of branches by the head offices.

It is not clear whether the government's caution influenced the Reserve Bank but it did give the impression, from then on, that it took the government view seriously. Hazari convened a meeting on 18 April 1974 with the chairmen of selected commercial banks. D.N. Ghosh was present at the meeting. The bankers wanted the restriction on Indian branches abroad for drawing an overdraft from their head offices to be removed because of the difficulties these branches faced in getting adequate lines of credit from foreign banks for financing their business. They also felt that where branches were not allowed to be opened by law, Indian banks might be allowed capital participation either with local banks or with other foreign banks already operating there. In this connection, they wanted guidelines to be issued regarding the quantum of capital participation and the remittance of funds that would be permitted towards capital requirements, initial expenses and working capital requirements, till the branch became viable.

The bankers also favoured suitable amendment of the law to protect Indian bank branches abroad from any legal action that customers or constituents abroad might take. They were of the view that, to enhance the incentives for non-residents to keep their funds with banks in India, it would be necessary to permit banks to maintain foreign currency accounts in India with some protection provided for against fluctuations in exchange rates. (This idea led to the Non-resident (External) Account Scheme.) Besides eliciting the bankers' views, the meeting took the decision that Punjab National Bank and Syndicate Bank could explore the possibility of opening a branch each in London.

Hazari forwarded the summary record of the discussions to N.C. Sen Gupta on 7 May. In Jagannathan's opinion, the Reserve Bank's view was reasonably liberal in facilitating the setting up of branches abroad of Indian banks. In reply, Sen Gupta, while appreciating the Bank's efforts, conveyed his intention to convene a meeting on 25 May at the government level, and raised a poser as to whether it would be worthwhile from the country's point of view to allow new banks like Punjab National Bank and the Syndicate Bank, which had no branches abroad, to open a branch each in the UK, instead of permitting existing banks to expand. Hazari countered on 17 May that unless the banks opened branches abroad, they would never acquire the necessary competence in international finance, and that getting a licence or its equivalent from a foreign monetary authority depended not so much upon a bank having or not having a foreign branch already but upon its credit standing, its size and management.

At the 25 May meeting, B.K. Sanyal, who was Secretary in the Ministry of External Affairs, pointed out that Bank of Baroda had delayed opening branches in Dubai and Abu Dhabi, and had not utilized the licence obtained to open a branch at Muscat. He wanted such situations to be avoided and the highest priority to be accorded to the opening of branches in the Gulf region, as well as in Panama, Afghanistan, Lebanon, Zaire, Moscow and South Korea. Narasimham, representing Economic Affairs, while favouring the generally restrictive policy in respect of remittance of foreign exchange to meet the expenditure and capital requirements of newly opened branches, observed that this policy would have to be applied on the merits of each case and that he was not in favour of framing specific guidelines. Deputy Governor Shiralkar agreed with Narasimham. On the opening of branches in the Gulf region, Sen Gupta felt that creating a base in London would help banks to open branches there both in terms of funds and expertise. Punjab National Bank and Syndicate Bank were to be asked to send concrete proposals about opening branches in the UK for consideration by the Reserve Bank and the Finance Ministry.

A MINOR SKIRMISH

What was perhaps most vexatious for the Reserve Bank was the government issuing a letter on 6 June to all leading banks, informing them about the 25 May meeting. This should have emanated from the Bank. The situation was exacerbated by the government conveying its intention to hold inter-departmental committee meetings to consider applications from the public sector banks to open branches abroad.

The Finance Minister got involved in this little scuffle, apparently at the instance of N.C. Sen Gupta, who had by that time become Secretary in Department of Banking. He conveyed to the RBI Governor the following message from the Finance Minister:

In the matter of opening branches in foreign countries we would be generally guided by the RBI who should have the expertise with them to advise Government in this matter. Let me discuss this with the Governor of the Reserve Bank before we take a final decision. Governor may be requested to come prepared to speak to me when he comes to Delhi next.

But when the Governor met the Finance Minister, the latter indicated that as a normal rule it would be desirable for the government to accept and act on the recommendations of the Bank, and to pass on to the Bank any facts and suggestions that would enable it to consider and take a final decision on the matter. This, however, was not to be.

On 21 April 1975, the Governor wrote to Sen Gupta giving a gist of his discussions with the Finance Minister and added that the Minister's decision/approval could be sought wherever necessary after the Bank had finalized its views. Jagannathan thought that 'this arrangement will be quite satisfactory'. He reiterated the case for a branch each of Punjab National Bank and Syndicate Bank in the UK, as already recommended by the Bank and pending with the Finance Ministry. He thought that banks should be allowed to open branches in the UK, where entry was free, and felt that this would 'in no way interfere with or be allowed to affect our efforts to open banks/branches in the Middle East/West Asia, in countries such as Iran, Lebanon (where there were legal restrictions) or in other countries'. Finally, he requested Sen Gupta to confirm the facts he cited in favour of the opening of branches by Punjab National Bank and the Syndicate Bank. There was no reply.

On 12 May, Jagannathan again took up the issue with Sen Gupta, citing the healthy growth of deposits in the UK branches of India-based banks, and pointing out that branches opened in the middle of 1974 had begun to attract deposits even before the end of that year without cutting into the deposits of other Indian branches. But the government delayed taking a final decision in regard to Punjab National Bank and Syndicate Bank, presumably waiting to implement some changes in the procedure. Jagannathan pressed for a decision, even offering to work out some kind of an accepted procedure for arriving at one. The government seized the opportunity with both hands and decided to make the Finance Ministry the focal point for

dealing with applications for opening branches abroad. Thus was the Reserve Bank's role diminished.

Jagannathan retired on 19 May and N.C. Sen Gupta succeeded him for a three-month period. But he left this issue well alone and returned to Delhi. On 22 August 1975, two days after K.R. Puri took over as Governor of RBI, M.G. Balasubramanian, Additional Secretary in the Department of Banking, conveyed to Puri the decision taken by the Finance Minister about the revised procedure, in order to expedite decisions. The procedure was that individual proposals to open branches or offices abroad by the public sector banks should be sent directly to the government, with a copy to the RBI, and these were to be considered by a committee consisting of officials of different ministries and the Bank. This, in effect, meant that the Department of Banking, through this committee, took over the powers vested in the Reserve Bank, under Section 23 of the Banking Regulation Act. The letter also stated that the proposals of Punjab National Bank and Syndicate Bank would be placed before the said committee for its consideration.

The letter so surprised K.S. Krishnaswamy, who was by then an Executive Director of the Bank, that he wrote on it: 'One more encroachment on the RBI's territory! Why?' Why, indeed? Chief officer of the DBOD, P.N. Khanna, in his note of 12 September 1975, traced the background of the impasse and remarked that the RBI's image in the eyes of the banks had been lowered in the process.

On 22 September, the first Inter-Departmental Committee meeting was held at Delhi, with N.C. Sen Gupta in the chair. Khanna represented the Reserve Bank at the meeting. Economic Affairs and the Banking Department opposed the granting of licences to Punjab National Bank and Syndicate Bank on the usual grounds. Khanna countered that without a base in London it would not be possible for these banks to operate elsewhere abroad, and that remittances were in the nature of working funds that could be sent back to India within three years. The External Affairs Ministry strongly supported Khanna. Ultimately, it was decided to allow the two banks to open branches in London subject to the approval of the Finance Minister and on a clear understanding that the banks would repatriate within three years the amounts remitted from India for their establishment in London. The Committee also discussed other proposals of banks for opening branches/offices and took decisions thereon. The Finance Minister eventually approved the recommendations of the Committee.

The second meeting of the Inter-Departmental Committee was held on 1 March 1976, to consider proposals to open four branches in the UK, one in Abu Dhabi and a representative office in Toronto. The Committee

approved the proposals to open branches in the UK, two each by Bank of Baroda and Bank of India, as also a representative office at Toronto by SBI. It also considered two proposals for opening an agency: one at San Francisco by Bank of India and the other at Los Angeles by SBI. It turned down Bank of India because under California's banking laws, an agency working there was not immediately allowed to mobilize deposits from the local population and the applicant bank had asked for a remittance of \$560,000. But the SBI proposal was approved as it did not require any foreign exchange remittance from India. Besides, the Los Angeles agency could mobilize deposits on behalf of the New York and Chicago branches of SBI.

Strangely, however, the Committee took exception to the Reserve Bank permitting a representative of a private sector bank, Bank of Madura, to visit Kuala Lumpur for more than a year to canvass deposits. It ruled that requests for such long stays should be put up to it for clearance! But when the minutes of the meeting arrived, the Bank was informed that the Minister for Revenue and Banking had approved the recommendations of the Committee, and the Department of banking was advising the banks to submit formal applications to the Bank for seeking the necessary permission. This was a welcome departure from the earlier position wherein the Reserve Bank was asked to initiate action on the basis of the Committee's recommendations by getting in touch with the banks.¹

In November 1976, by which time Narasimham had become Secretary in the Department of Revenue and Banking, three policy guidelines were set before the Committee:

- (i) Applications for opening of branches should be examined with reference to the constraints of foreign exchange and manpower.
- (ii) Ordinarily, only one bank might be permitted to open a branch in a new area, although in international financial centres like London and

¹ There is an interesting little interlude here. N.C. Sen Gupta, Secretary, Department of Banking, had specifically invited Hazari to attend the two meetings. But on both the occasions, Hazari could not attend on account of his commitments elsewhere. Sen Gupta himself held the post of Governor in the three-month period between 19 May and 19 August 1975. When Jagannathan relinquished the Governorship, Hazari, who was then the seniormost Deputy Governor, was rumoured to succeed him. It is not clear why the Bank chose to send its senior officers but not Heads of Departments to the meetings. It is likely that this level of representation had placed it at a disadvantage vis-à-vis the government. This position, however, was sought to be corrected when M. Narasimham, on becoming Secretary, Department of Revenue and Banking, in November 1976, specifically requested Governor Puri to attend a meeting of the Inter-Departmental Committee he convened on 28 December 1976. Puri, however, deputed P.N. Khanna, by then the chief officer of DBOD, to the meeting.

New York, there could be more than one Indian bank in operation.

- (iii) If a bank did not open a branch within a year of getting approval, the licence would not be renewed.

Against this background, the Committee considered applications for opening of branches abroad. Of these, two proposals are worth mentioning. Bank of India and Indian Overseas Bank applied for opening a branch each in Seoul and the Committee felt that, given the presence of IOB in Southeast Asia, it should be allowed to open a branch in Seoul.

At the fourth meeting, held on 15 March 1977, R. Vijayaraghavan, joint chief officer, DBOD, was present. The simmering differences between the government and the Reserve Bank surfaced at this meeting in four instances. First, the Bank was not inclined to support the application of Punjab National Bank to open branches in the UK at Wolverhampton and Gravesend, because of that bank's presence in London. But Narasimham had had a prior discussion with the chairman of the bank. He felt that the application could be considered because a large number of Punjabi businessmen and other Indians were residing in these places. The Committee approved the proposal subject to repatriation of the foreign exchange remittance from India within three years.

Second, the RBI felt that State Bank of India's request to open a representative office at Vancouver need not be considered in view of its new office in Toronto. Narasimham, again, justified the request on the ground that the chairman of that bank was satisfied with its critical significance. The Committee agreed with his view.

Third, RBI did not support the State Bank's presence in Tokyo on the ground that Bank of India already had branches in Tokyo and Osaka. The Bank also pointed out that there was already a proposal under consideration, of Bank of India opening a branch at Kobe. However, the chairman over-ruled that Tokyo and Hong Kong should be regarded as important financial centres in the same way as London and New York. The Committee again concurred with this view.

Finally, the RBI had reservations, on two counts, about the External Affairs Ministry's proposal to support State Bank of India's request to open a branch or subsidiary in Zurich. Firstly, it felt that the Swiss laws insisted on strict secrecy of accounts and the Bank would not be able to inspect them. Secondly, a large remittance (equivalent of Rs 4.12 crore), towards minimum capital and preliminary expenses, would have to be made for the purpose. The chairman intervened to say that secrecy laws should not deter India from considering the proposal since in any case foreign branches of Indian banks would have to comply with the rules and regulations of the

respective countries of operation. He pointed out that relatively small banks, like Habib Bank of Pakistan, had an office in Switzerland and did good business. He hoped that SBI would remit the funds from its other overseas establishments if it were to set up branch/subsidiary in Switzerland. On the question whether it should open a branch or establish a subsidiary in Switzerland, the Committee felt that this was a general policy issue, and therefore could be referred to the Minister. Eventually, it was decided that the Department of Banking would take up the request in greater detail with the Reserve Bank and, subject to the latter's approval, the Committee would agree to the entry of SBI. This meeting once again proved that the real decisions would be taken by the government through the Inter-Ministerial Committee, although for the sake of form and compliance with the law, the Reserve Bank's approval would be sought.

DIFFERENCES PERSIST

The sudden change in the government at the centre in March 1977 led to a marked shift in the perceptions on the subject. At the behest of Deputy Governor Krishnaswamy, the DBOD prepared a note on the perspective plan on the opening of branches abroad, and on the relative responsibilities of RBI and the government in the matter. The note was helpful when the next meeting of the Inter-Ministerial Committee was convened on 28 July by Manmohan Singh, Secretary, Economic Affairs. Krishnaswamy saw an opportunity to normalize relations between the government and the Bank. The meeting proceeded on the familiar lines of considering applications of banks for opening of foreign branches/offices. In four out of the six applications, the Committee's views were in line with those of the Bank.

In one case, however, the application was approved notwithstanding the Bank's recommendation for its rejection. In another case, involving SBI's application to open a joint venture bank at Jeddah, the Bank wanted deferment and the Committee felt that the proposal required to be examined in further detail and after consultation with the Indian embassy. As a policy departure, however, the Committee took the view that where joint ventures and finance companies were to be established in foreign countries, it would be preferable to set them up on a consortium basis by associating one or two Indian banks rather than on the basis of participation of only one Indian bank. SBI was asked to re-examine the proposal and come up with a concrete scheme spelling out the financial details before the Committee.

The thaw in the relationship was in evidence in the subsequent two

meetings as well, held on 26 November and 21 July 1978. In general, the Committee's decisions on banks' applications were in line with the perceptions of the Reserve Bank. However, before the 21 July meeting, the Department of Banking, which by that time had been downgraded as the banking division, raised a discordant note by trying to empower the Committee to decide on applications of foreign banks wanting to open offices in India.

Baldev Singh, Joint Secretary, in his letter of 2 February 1978 to Governor I.G. Patel, argued:

Under the Banking Regulation Act, 1949, grant or refusal of a licence for banking business to a bank, including a foreign bank, is a function exclusively assigned to the Reserve Bank of India. A convention has, however, developed over the years for the Reserve Bank to consult the Ministry of Finance and for the Ministry of Finance to consult the Ministry of External Affairs before any decision is taken either to give or to refuse a licence to a foreign bank for conduct of banking business, mainly due to the political angle involved in such a decision. Of late, both the Government and the Bank have received a number of requests from the foreign banks operating in India for expansion of their branch network in India and from other foreign banks for their entry into India. Some canvassing by the banks concerned in support of their applications has also been noticed.

He said that the applications received from foreign banks for establishing representative offices or branches in India would be placed for consideration before the existing Committee (which considered proposals by Indian banks wanting to open branches abroad). In his eagerness to formalize the arrangement, Baldev Singh proposed, if the RBI agreed, to place such applications received thus far before the next meeting of the Committee. But this time the Bank was alert and managed to stave off the attempt to erode its authority further and even made an effort, albeit only partially successful, to retrieve the powers that had been taken over by the government in the case of Indian banks opening branches abroad.

The Reserve Bank responded with a long note on 24 February, which examined the implications of the government's move. After narrating the determined manner in which the erstwhile Department of Banking had succeeded in usurping the statutory powers of the Bank, the note said that its suggestion would further erode its authority and dwelt on the political implications involved in dealing with such applications. Finally, it said that

the present procedure, which had been unilaterally decided by the government, had *executively abrogated* (the Governor italicized the two words) the powers that were lawfully vested in the Bank. The note cautioned that the revised procedure might open itself to allegations of lack of transparency at a later date.

Yet another aspect is the need for keeping the records straight of both government and the Reserve Bank of India so that at a future date, one will be able to correctly interpret the circumstances and factors taken into account while taking a particular decision. The absence of formal communications between the Bank and the government wherein the grounds on which a particular view is supported or otherwise are clearly spelt out in the notes or letters exchanged may lead to possible suspicion or view that the decisions were taken arbitrarily.

On a milder note, the note added that the Finance Ministry was at liberty to obtain the opinion of the Ministry of External Affairs or any other ministry before communicating its final view to the Bank. Besides, it could pass on to the Bank any facts or information that any government department might have and any of its own suggestions as well, which the Bank would take into consideration. The note asserted that the Bank was not in favour of the Committee considering such applications, so that 'the autonomy of the Reserve Bank of India is preserved'.

Krishnaswamy, in his noting, summed up the position vis-à-vis autonomy of the central Bank thus:

In my view, this is a matter on which the present position is quite unsatisfactory. Every time we put up a memorandum to our Board regarding opening of foreign branches by Indian banks or of Indian branches of foreign banks, we are merely asking the central Board to endorse a government decision. This is not right for either the RBI or the government. Since, under the statute, RBI is the authority to grant the licences the process should in both form and substance, conform to the statutory provisions. Hence, we should take up the matter with government and set right the machinery. To do so does not, clearly, imply any reduction in RBI having to consult with, and generally respect the views of, government.

Governor Patel, while concurring with the contents of the note, instructed that a copy of the note be sent to the government. Krishnaswamy did so

on 28 February. In his covering letter to M.R. Shroff, he conveyed the opposition of the Reserve Bank not only to the proposal made by Baldev Singh but also to the functioning of the Inter-Departmental Committee, and called for retracting the steps already taken.

We are not in favour of the Committee considering applications received from foreign banks for establishing representative offices or branches in India. We are also not in favour of the Committee taking decisions on the applications received from Indian banks for opening branches abroad. We are of the view that both these categories of applications should be received by the Reserve Bank who will refer to the Ministry of Finance, which may consult other ministries or departments as expeditiously as possible and convey the views of the Government to the Reserve Bank... If Government agrees, appropriate instructions will have to be issued to the public sector banks requiring them to submit the applications for opening branches abroad to the Reserve Bank direct. I have also discussed this with the Governor.

Manmohan Singh, while sending out invitations for convening the meeting of the Inter-Departmental Committee on 17 April 1978, informed Krishnaswamy that he was having the matter examined and that, in the meanwhile, 'I thought we should not hold up the various proposals we have received.' Significantly, the agenda for the meeting included applications received from five foreign banks to open branches in India. A few days later, the Bank's strong resistance paid off and the government climbed down by modifying that the agenda for the meeting would be confined only to the proposals of Indian banks for opening branches/representative offices abroad.

On 7 February 1979, I.G. Patel wrote a detailed letter to Manmohan Singh that the Committee's approach was far from desirable since it could not avoid placing the Reserve Bank in an embarrassing position. He referred to the discussions between himself, Manmohan Singh and the Finance Minister in the first week of February 1979, regarding the policy for foreign banks opening branches in India, and the practice followed for processing applications from Indian banks for opening branches abroad. Patel expressed the view that only the bigger banks with the expertise needed to open branches abroad and joint efforts for opening of branches/offices abroad of a few of the nationalized banks should be encouraged, wherever feasible, rather than make them compete with each other for the sake of so-called

'prestige'. He also said that, instead of taking decisions under pressure or persuasion from individual banks, a perspective plan for the next few years should be drawn up for Indian banks desiring to open branches abroad. He wanted Manmohan Singh to confirm whether the general approach set out by him was acceptable to the Ministry and mentioned that he intended to ask for a meeting with select banks to discuss the general approach. The letter concluded by highlighting the key issues in the whole controversy, which touched on the relations between the Bank and the Finance Ministry:

I would be grateful if you could let me know whether the general approach in this letter is acceptable to the Ministry of Finance and also that we may not act at cross-purposes—and what is more important, do not encourage our own banks to play us one against the other. Between the Ministry and the RBI there should, in fact, be informal discussion and agreement on individual cases before we discuss them at a general meeting, as otherwise the danger I apprehend would be difficult to avoid. That is why we had earlier suggested a reconsideration of the present procedure which, to say the least, puts the RBI in an awkward position; and I hope that it would be still possible for us to evolve something better than the present procedure which puts us more in the role of, at best, a public prosecutor rather than at least a member of the judiciary.

Manmohan Singh replied on 15 February in a typically disarming manner. He clarified that the government was not wedded to any particular procedure and was willing to consider any alternative procedure that the Reserve Bank would suggest. Patel responded on 1 March apologizing for the 'insinuation' and conceded that he did not see any reason 'for making a change in the present practice', which, however, seemed like a climbdown from the high moral ground that his letter of 7 February 1979 had assumed. He requested that a representative from the banking division be present at the meeting arranged by Krishnaswamy with the banks. The meeting was for discussing the Bank's plans for the next two or three years, to 'avoid ad hoc decisions'.

In June, the government told the RBI that it would be necessary first to draw up a set of guidelines regarding the future approach towards permitting branches abroad by Indian banks and thereafter prepare a perspective plan for such expansion. The government said it wanted the guidelines to be discussed at the next meeting of the Inter-Departmental Committee.

Accordingly, on 6 September, the Bank forwarded the guidelines to the government.

The meeting of the Inter-Departmental Committee was held on 5 November. The agenda was heavy. It included twenty proposals from banks for expansion overseas, as also the draft guidelines prepared by the Bank. Krishnaswamy said that the Bank could only process five proposals and that it needed more time for making its recommendations. The Committee agreed and the discussion on the draft guidelines ended with the conclusion that the guidelines would have to be more specific so that banks became aware of the policy in precise terms.

In the meantime, another interesting development came to the notice of the government. Certain public sector banks had been submitting applications to the central banking authorities of foreign countries for permission to open branches/representative offices even before obtaining the prior approval of the authorities in India. The Finance Ministry asked the chairmen and managing directors of the public sector banks to stop this. Governor Patel, on the copy of the letter endorsed to the Reserve Bank, was quick to instruct that it should be made clear that the prior approval referred to 'approval of both and not of either'. Some of the banks were annoyed by all this and there was some heat generated.

The revised draft guidelines were presented and approved on 11 June. One of these was intended to ensure that the opening of a new branch in an area where an Indian bank was already established should be justified on the basis of creation of potential for 'additional' business. It was also decided that representative offices should not be allowed to be opened unless full justification was provided by the banks because these offices did not directly conduct banking business and as such did not earn profit. But the guidelines took a long time to be issued—almost a year and four months.

The basic objective in permitting banks to expand abroad was to enable them to enlarge their international business, act as catalysts in the development of India's foreign trade and to raise resources abroad. As there were implications for the Reserve Bank's approach to foreign banks opening offices in India, Indian banks were asked to be fairly certain that the host country was willing to permit them to operate there on terms equal to those of other foreign banks. Each bank was expected to formulate the proposal for establishing or enlarging its business abroad in the context of its overall development plan. Small banks were advised not to venture into international money and capital markets because of severe competition and market volatility.

However, the government, at whose instance the guidelines had been

prepared and circulated to banks, did a sudden about-turn on realizing that it amounted to a dilution of its powers. While deciding on the countries/areas where Indian banks are to be permitted to establish/increase their presence, the following aspects had to be taken into account:

- (i) India's political relations with the concerned country and the political conditions obtaining there.
- (ii) The extent of existing/potential trade between India and the foreign country concerned.
- (iii) The population of Indian origin in that country.
- (iv) The financial importance of the centre from an international point of view.
- (v) The projected business and profitability estimates of the proposed branch, particularly in the context of local laws relating to liquidity, credit control and taxation.
- (vi) The Foreign exchange remittance required for establishing the branch and the source from which this will be met.

Every bank had to keep the Reserve Bank of India informed of its programme for surveys, before these were taken up, in order to establish better coordination in bank surveying.

On 12 August 1981, the Finance Ministry wrote a letter to Patel that practically ended any hope of the Bank's autonomy: in view of political, foreign exchange and other factors, it said, it would be desirable to obtain the government's approval 'in principle' for opening of branches/offices, etc., abroad, and for participation in the equity capital of foreign banks or institutions. The letter went on to say that the Inter-Departmental Committee would continue to carefully examine the proposals and make suitable recommendations to the government, and that the government's approval, with or without modifications, would be communicated to the Reserve Bank. The Indian banking companies should not, however, normally submit formal applications for licences to the central banking authorities of other countries without first obtaining the approval of the RBI/Government of India.