Chapter VI
CONCLUSIONS

Indian economy experienced growth of national income at an annual compound rate of 3.7 per cent during the period 1951-71. Alongwith the growth of the Indian economy the financial structure has also undergone a change during the same period.

There has been growth of net issues and outstanding stock of primary securities. The net issues of primary securities increased from Rs.568,03 lakhs in 1951-52 to Rs.2,670,32 lakhs in 1970-71, whereas the stock of outstanding primary securities increased from Rs.6,227,94 lakhs to
37,818,62
Rs.3,781,86 lakhs during the same period. The absolute amount of net issues and outstanding stock of primary securities increased by four and a half times and six times respectively in 1970-71 as compared with that in 1951-52.

Issue-income and debt-income ratio are the most important relations in analysing the financial structure and development. They showed upward trend during the period. The issue-income ratio increased from 5.4 per cent in 1951-56 to 9.16 per cent in 1966-71, whereas the debt-income ratio increased from 0.62 in 1950-51 to 1.10 in 1970-71. The upward trend in the issue-income and debt-income ratios during the period understudy conform the hypotheses of rising issue-income and debt-income ratio in a growing economy. The external financing ratio that is the ratio of net primary security issues to net capital formation was 47.8 per cent in 1951-56, increased to 65.1 per cent in 1956-61, then declined to 44.1 per cent in 1966-71. But overall external financing ratio has been on a higher side as the ratio accounted for 51.2 per cent during the period 1951-71.

The study of composition of primary securities from stock dimension has shown that shares of government and corporate sector have increased, while the household sector has shown a decline. It has also brought out that government sector accounts for about half of the total stock of primary securities in India. This reflects the leading role of the government sector in the process of economic development in India. The ratio of government debt for public debt to net national product increased from 0.28 in 1950-51 to 0.54 in 1970-71, reflecting the growing importance of the government sector in Indian economic development.

The composition of government debt, namely, 'internal' and 'external' debt shows the share and significance of external debt which was already important in 1950-51 - 1955-56 period. From that period external debt of the government has assumed even greater proportion as much as one fourth of all government debt during the later period.

The composition of corporate sector into government and non-government non-financial corporate sector has brought out the growth and prominence of the government corporate sector in contradistinction with non-existence in 1950-51.

The composition of government and non-government corporate sector primarysecurities viewed from the stock dimension has revealed the common feature that there has been a decline in the share of stock issues. Trade dues were an important source for both government and non-government corporate sectors.

For the government corporate sector borrowing from 'other sources', mostly from the government was not only significant but its importance grew with time. For the non-government sector borrowing from other sources which include direct public deposits is also quite an important source. But borrowing from the banks and other financial institutions was insignificant for the government corporate sector while it was significant for the non-government corporate sector.

There has been growth of financial intermediaries in India during the period 1951-71. The aggregate assets of all financial intermediaries increased from Rs.3,030,25 lakhs to Rs.17,265,37 lakhs between 1950-51 and 1970-71. The aggregate assets of all financial intermediaries increased more than five and a half times in 1970-71 as compared to that in 1950-51. All financial intermediaries have grown but at different rates. Percentage share of financial institutions has undergone considerable change during the period. The share of the Reserve Bank of India declined from 53.2 per cent in 1950-51 to 31.6 per cent in 1970-71. The share of Commercial Banks remained distinctly stable around 35 per cent to 36 per cent. The shares of insurance organisations, cooperative Institutions and other financial Institutions have increased during the period.

The examination of relative share of assets of monetary and non-monetary intermediaries to the total assets of all financial intermediaries has revealed that the share of monetary intermediaries declined from 88.5 per cent in 1950-51 to 69.9 per cent in 1970-71, whereas that of non-monetary intermediaries increased from 11.5 per cent to 30.1 per cent during the same period. The changes in relative share among monetary and non-monetary intermediaries in favour of non-monetary intermediaries is consistent with our hypothesis that the share of monetary intermediaries tends to decline and that of non-monetary intermediaries tends to increase during the process of financial and economic development in the country.

The analysis of financial intermediaries assets-income ratio has shown that the ratio has gone up from 0.33 in

1950-51 to 0.50 in 1970-71 and this lends strong support to the stated hypothesis of rising financial intermediaries assets-income during the process of financial and economic development.

The analysis of financial institutions from historical perspective has revealed that the structure, character and working of existing financial institutions has undergone significant changes. The older financial institutions have widened the scope of their activities by undertaking the non-traditional activities. Varieties of specialised financial institutions have came up to fill the "gap" in the requirement of long-term finance. The most remarkable thing about these specialised financial institutions is that they undertake innovative financing.

The progress with regard to financing the agricultural sector has been really remarkable. The outstanding loan given by the cooperative Institutions increased from Rs.83,86 lakhs in 1950-51 to Rs.1,577,12 lakhs in 1970-71.[1] There were 1,53,771 active primary agricultural credit societies operating at the village level and covered 82 per cent of the total villages in the country at the end of June 1967.[2]

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[1]See, Column 2, Appendix Table IV-7.

[2]<u>Organisational framework for the Implementation of social objectives</u>, Reserve Bank of India, Bombay, October, 1969, p. 13.

Generally in the advanced countries the experience has been one of evolution of financial institutions and financial system through the market forces.[3] Evolutionary development of financial system is a continuing consequence of the passive, sweeping process of economic development. What may be called "demand-following" phenomenon in which creation of financial institutions, their financial assets and liabilities and related financial services are in response to the demand for these services by the investors and savers in the economy. Thus, the financial intermediaries of the demand-following nature plays permissive and passive role in the process of economic development.[4]

Our analysis has shown that the creation of new financial institutions and their role and changing mode of working of the existing financial institutions are very close to the financial intermediaries of the "supply-leading" nature. What may be called the "supply-leading" phenomenon is one in which creation of financial institutions and supply of their financial assets, liabilities and related services take place in advance of demand for them,

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[3]Edward Nevin, Capital funds in underdeveloped countries, Macmillan and Co. Ltd., London, 1961, pp.72-73.

[4]Huge T. Patrick. "Financial Development and Economic growth in Underdeveloped countries", Economic Development and cultural change. January, 1966, pp.174-75.

especially the demand of enterpreneurs in the modern growth-inducing sectors. Financial intermediaries of the "supply-lending" nature performs two functions: (1) to transfer resources from traditional (non-growth) sectors to modern sectors.[5] (2) and to promote and stimulate an entrepreneurial response in the modern sectors. Thus the most important function of the financial intermediaries of the "supply-leading" nature is to induce the growth. Our analysis brings out that financial intermediaries have played active and strategic role in the process of capital formation in the country. They have stimulated entrepreneurial response in the modern industrial sector by providing entrepreneurial advice, other managerial services and skills. Thus, the financial intermediaries after Independence have played more active and stretagic role in inducing the growth process.

Along with the growth of primary securities, there also takes place growth issues of indirect finance. The net issues of indirect finance increased from Rs.81,34 lakhs in 1951-52 to Rs.1,488,66 lakhs in 1970-71. So also outstanding issues of indirect finance increased from Rs.1,373,74 lakhs to Rs.12,785,30 lakhs during the same period. However, indirect finance-issue-income ratio has not shown clear

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[5] Ibid., p.175.

and decisive trend during the period.

Analysis of financial intermediation ratio revealed upward trend in the ratio. The ratio has increased from 33.25 per cent in 1951-56 to 43.53 per cent in 1970-71. Thus, our findings support the hypothesis of rising indirect finance ratio during the process of financial and economic development.

The extent of indirect finance according to sector has shown that it was higher with regard to household sector. It was 43.5 per cent for the government sector during the period 1951-71. Thus, the financial intermediaries purchased sizeable portion of government domestic securities. The extent of indirect finance with regard to corporate sector was 25.48 per cent during the period 1951-71.

The indirect finance by the type of financial intermediaries has revealed that the percentage of net issues of domestic primary securities purchased (27.9 per cent) by the monetary intermediaries has been relatively more than that purchased (12.83 per cent) by the non-monetary intermediaries during the period 1951-71. Thus, the monetary intermediaries dominated the purchase of primary securities. However, it should be noted that the purchase of net issue of domestic primary securities by the non-monetary intermediaries increased from 10.99 per cent in 1951-56 to 14.63 per cent in 1966-67.

Thus, our findings confirm the hypothesis that the monetary intermediaries tend to purchase relatively large proportion of primary securities in the initial process of financial intermediation and the purchase of primary securities by the non-monetary intermediaries tends to increase along with the upward trend in the indirect finance during the process of financial development.

On the side of monetary development in India, there has been continuous expansion of stock of money in India during the period. The stock of money increased from Rs.1,828,85 lakhs in 1951-52 to Rs.7,139,97 lakhs in 1970-71. The stock of money increased nearly four times in 1970-71 as compared to that in 1951-52. The percentage composition of stock of money has shown that the major constituent in the stock of money is the currency with the public, as the percentage share of currency with the public averaged 67 per cent per annum during the period. In contrast to the composition of stock of money in mature and advanced economies where major constituent is the deposit with the public. Though the composition of money has changed marginally, but it has not altered the composition radically.

The money-income ratio has strikingly remained around 0.20 to 0.22 during the period. The observed money-income ratio has not shown upward tendency, but it remained steady at a higher level. Thus, the observed money-income ratio during the period 1951-71 does not lend support to our hypothesis of rising money income ratio in the earlier stage of economic development. The underlying the hypothesis is that the ratio tends to rise from lower to higher level. If we examine the ratio from the broader perspective, then the money-income ratio seems to be consistent with the hypothesis. The observed money-income ratio can be considered higher one and the ratio would have increased from low level in the earliest stage of economic development. Although the money-income ratio has not shown a tendency of upward movement, the observed ratio fits well with the hypothesis.

The money-debt ratio has declined from 0.29 in 1951-52 to 0.19 in 1970-71. The reason for the decline in the proportion of money to the debt is not that the non-financial assets have been substituted for money. But it is that primary securities have gained more weightage in the assets portfolio of the non-financial spending units due to the growth of primary securities by itself.

Our finding broadly confirms the theoretical model and structure of financial development. India has became richer in financial assets and markets.

The two decades of development examined in our thesis exhibit, in remarkable proximity to the models of financial development and its role in economic development, the key role of financial intermediation in facilitating and accelerating developmental process in the Indian economy. What is striking in the Indian experience with regard to the various ratios examined during the period conform to the observed pattern. The financial structure has changed over time in conformity with the known behaviour elsewhere. The Indian economy has witnessed the 'supply leading' function in its institutional development. The role of the state (government) in all these can hardlybe exaggerated. This combination of 'institutional changes' and the 'supply leading' financial intermediation dovetailed with the growth of the corporate sector - governmental and non-governmental - ushers in the changes that would now put the economy on par with those development and advanced countries. Perhaps a major weakness of the Indian economy could be the slow process of monetization. Indeed, the process of monetization could be a pace-setter.

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