

**BANKING SECTOR REFORMS AND THE EMERGING  
INEQUALITIES IN COMMERCIAL  
CREDIT DEPLOYMENT IN INDIA**

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## ABSTRACT

Banking sector reforms, which is a major component of Macroeconomic Adjustment Programme in India, has changed the trends and patterns of banking over the last six to seven years. This paper seeks to analyse the trends in credit deployment by industry, by bank group, by rural and urban areas, and by states over the recent period. The argument of the paper is that serious regional and sectoral inequalities are developing in the deployment of commercial credit in this country.

The economic reasoning for nationalising the major banks in 1969 was the imperfection in the allocation of credit. With bank nationalisation there was a rapid expansion of the banking network into rural and semi-urban areas, and an increase in the share of agriculture and small industry and transport and trade in the total credit deployed. The banking sector reforms have changed this trend. The number of loan accounts has fallen by 60 lakhs in six years, and the fall is largely confined to agriculture, transport operators and trade. The new private banks and foreign banks are increasing their presence in the emerging business of loans for personal and professional services.

There is a striking regional dimension to the developments of the last few years. The emerging banks and the existing ones are competing to expand in South, and North-West India attracted by the growing credit business in a milieu with strong banking habits. This has resulted in a drastic reallocation of total commercial credit from the poorer agricultural states to Delhi, Maharashtra and Tamilnadu. The situation is one where private banks are left to "skim the cream" without investing in the long-term development of banking habits.

**JEL Classification:** G21, G28

**Key Words:** banking sector reforms, nationalisation, directed credit, regional inequalities.

## **1. Introduction**

The 1990s saw India implementing Macroeconomic Adjustment Programme of which the financial sector reform is a major component. The basic principle guiding financial sector reform was that the financial system has a crucial role to play in the mobilisation of savings and their allocation to the most productive uses. The ground for reform was the several distortions which had crept into the financial system rendering it unable to meet the challenges of a competitive environment. The most important factor contributing to this weakness of the system, as argued by the Narasimham Committee, was "the impact of policy induced rigidities such as an excessive degree of central direction of their operations in terms of investments, credit allocations, branch expansion, and even internal management aspects of the business ". The reforms, based on the recommendations of Narasimham Committee, set out to change the policy environment to ease these rigidities.

The financial sector reform has been initiated at a rapid pace since 1992 and has changed the trends and patterns of banking in this country over the last six or seven years. This paper seeks to analyze the trends in credit deployment by industry, by bank group, by rural / urban, and by

states over 1990-91 to 1996-97. The argument of the paper is that serious regional and sectoral inequalities are developing in the deployment of commercial bank credit in this country and a slide back to a situation similar to that existing prior to bank nationalisation in 1969.

The paper is organised in eight sections. Following this introduction, Section 2 discusses the economic principles behind the nationalisation of commercial banks in India and the performance of the banking sector during the two decades since nationalisation. Section 3 takes up the issue of the beneficial impact of bank lending to agriculture and small firms. Section 4 discusses the Financial Sector Reform. The discussion here is confined primarily to banks or depository institutions, which occupy a dominant position on the financial stage. Section 5 attempts at drawing some patterns from the data on the distribution of loan accounts and credit by sectors of the economy. This section also discusses the size of loan per account across the sectors. The discussion of Section 6 deals with bank groups. The differences among State Bank of India and its Associates, Nationalised Banks, Foreign Banks and other Scheduled Commercial Banks are explored in some detail. Section 7 turns to the distribution of banking business in terms of deposits, credit and branch expansion across the states of India. The emerging inequalities in the growth of banking business are noted. The paper concludes by comparing the trends in banking in the 1990s with that prevailing before nationalisation.

## **2. The Nationalisation of Banks in India and Development of Banking in the 1970s and 1980s**

As is well known, the period since 1969, when the major banks in India were nationalised, the functioning of the banking system has come to be highly regulated. Entry into banking came to be restricted, branch expansion was licensed, and the thrust was on opening branch offices in

non-banked and rural areas. The lending policy also came to focus on reaching credit to agriculture, small enterprise, artisans and such segments of population. The first and foremost question in this context is, why were the major commercial banks nationalized in 1969?

Bank nationalisation was a political act and as such the motives for it will have to be found in that sphere. But the policy was founded on economic principles the most influential exponent of which was Raj (1974)<sup>1</sup>. The key arguments of Raj (1974) are presented in this section largely because they are highly relevant today and provide an essential background to the discussion of the later sections.

It is well known that credit markets are imperfect. That is the reason, "monetary authorities always considered it necessary and desirable to fix both the amount of bank credit to be advanced and the rate of interest"(Raj 1974: 303). In an imperfect market leaving the decision to allocate resources to banks will aggravate the imperfections. The market imperfections, together with certain conventions and practices of banking, such as not to finance long term investments, not to lend against the collateral of land etc, "could be seriously in conflict with the larger economic and fiscal considerations which should govern the distribution of the investible resources in an economy" (Raj 1974: 306). The need to nationalise commercial banks followed from this,

" if the dimensions of the problem introduced by market imperfection in the allocation of resources were fully recognised, and the objectives of the development programme kept in mind, one would have expected less hesitation being shown in nationalising all commercial

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1. The lecture on which the paper is based was delivered in 1965, preceding the nationalisation of banks by four years.

banks in the country and in using them directly for a more optimal distribution of finance in the economy. For there are important reasons why banking enterprises seeking to maximise their profits would not venture out into areas and sectors of activity to which high priority needs to be attached from a larger social and economic point of view" (Raj 1974: 308).

With nationalisation it was thought that banks could be made to lend to agriculture, small enterprises, and artisans in rural and semi-urban areas.

There is an altogether different economic reason for compelling the banks to carry out a larger social role. It needs to be recognised that the very basis of profit making in banking activity is the development of the habit of deposit money. The profits of commercial banks depend on the proportion of their earning assets to the idle cash reserves they have to hold- their profits being larger the higher this proportion. This is the reason commercial banks show a natural bias, "to advance credit to segments of population which have already developed banking habits, and to be interested in others only to the extent that they offer deposits on a more permanent basis (such as through savings deposits) which would bring cash into the banking system without causing large outflows of cash from it" (Raj 1974: 309). But in the long run this natural bias would not help banks, as banking habits cannot be inculcated without setting up bank offices in non banked areas and advancing credit to segments of population lacking banking habits.

Exactly for the above reason setting up alternative agencies for providing credit to the other segments of population and sectors of activity is also not advisable. In addition,

"By letting private banks continue and only setting up special institutions subsidised by the State, the former are merely permitted to make profits where they can and the whole responsibility of carrying out the less profitable (and perhaps socially more productive) tasks borne by the State at the cost of the general public. There is little economic or social justification for such an arrangement" (Raj 1974: 310).

The solution to these problems was sought in nationalising all the larger banks, with smaller banks allowed to function in a free market. Raj went on to suggest that priority sector advances be charged market interest rates to prevent leakage, "except where there is complete assurance that there will be no such leakage" (Raj 1974: 311).

Having gone into the economic reasoning of bank nationalisation it will be pertinent to investigate how far the objectives of nationalization could be realised during the 1970s and 1980s. Till the end of the 1960s banking was largely an urban/semi urban phenomenon with over 80 percent of the branch offices confined to the urban/semi urban areas (Table 1). Almost 97 percent of the deposits originated in these areas with the rural areas contributing about three percent of the total deposits. Commercial banks were hardly advancing any credit in the rural areas. Even in the semi-urban and urban areas credit business was proportionately lower than deposit collection. While over 45 percent of the total deposits originated in the semi urban and urban areas, only about 30 percent of the total credit was flowing into these areas. The metropolitan areas accounting for less than 20 percent of the number of branch offices, and less than 50 percent of the deposits claimed over two-thirds the total bank credit. Thus, commercial banking bypassed vast segments of the Indian population before nationalisation.

The two decades since nationalisation of the major banks witnessed a transformation of the Indian banking scenario. The total number of branch offices, which was around 8000 in 1969 increased to 60000 by 1990. Such expansion was the most rapid in the rural areas of the country. The share of rural offices in the total increased from 17.6 percent in 1969 to 56 percent by 1989 (Table 1). The share of rural areas in the total deposits rose from about three percent to 15 percent during the period. The rise in the share of credit was more spectacular, from 1.5 percent in 1969 to 16.3 percent in 1989. In the case of bank credit, the gains of the rural areas is entirely explained by the loss of the metropolitan areas. Overall, the two decades since the nationalisation of commercial banking in India saw banking being taken from its urban confines to the vast rural stretches.

The expansion of banking into the rural areas meant a phenomenal expansion in terms of number of deposit and loan accounts. The total number of loan accounts showed a rapid increase from about four million in the early 1970s to over 60 million by 1990 (Table 2). The share of agriculture in this total increased sharply to over 50 percent by 1982 itself. In terms of number of agricultural loan accounts, the increase was from about one million in the early 1970s to over 10 million by the early 1980s and to close to 30 million by the early 1990s. Transport operators and trade also showed significant increases. Hitherto totally neglected segments, such as artisans and craftsmen, and small-scale industries also came to occupy an important place.

Along with the growth and diversification in terms of loan accounts there took place a rapid shift in the composition of the amount of bank credit. Till bank nationalisation in 1969, industry cornered over 60 percent of the total bank credit and agriculture could get hardly 10 percent and small-scale industries about eight percent (Table 3). By the early 1980s,

the share of agriculture had risen to 17 percent and transport operators about five percent, and small-scale industries about 12 percent. With the diversification of portfolio, industry's share came down from over 60 percent in the early 1970s to about 47 percent by the early 1980s and to about 44 percent by the close of the 1980s.

Between 1969 and 1990, the bank branch offices increased by 51,000 with about 80 percent of them having been opened in rural and semi-urban areas. The regional distribution also shifted away from Maharashtra, Gujarat, and South India, which accounted for close to 60 percent of the total branch offices in the late 1960s, to the rest of the country. The share of South India, Maharashtra and Gujarat came down to about 40 percent by the late 1980s and the share of Uttar Pradesh, Bihar, Madhya Pradesh and Rajasthan increased from less than 25 percent to close to 35 percent during this period. The credit deposit ratio also began showing less variation across the states of India during this period.

The phenomenal banking expansion led to a rapid growth in the volume of transactions in relation to gross domestic product (GDP). While in 1969 deposits amounted to 13 percent of GDP and advances to 10 percent, by 1991, deposits had risen to 38 percent of GDP and advances to 25 percent. The growth of bank deposits led to its higher share in total financial assets held by the household sector as well.

The expansion of the banking system into the rural areas, while expanding the deposit and credit as a proportion of GDP, did result in the cash deposit ratio of the banking system going up. The cash- deposit ratio which was around eight percent at the time of nationalisation of the major banks continued to hover around that rate till 1977, despite the proportion of rural offices and deposits in the total going up. The sharp increase in the cash- deposit ratio from 8.3 percent to 16.8 percent took

place between 1977 and 1987 when the proportion of rural credit increased by almost 10 percentage points.

It is evident that the initial result of taking credit to the rural areas is a larger cash flow out of the bank. It is only much later with the development of the deposit habit that the cash outflow tends to decrease. It is understandable why banks, left to themselves, are hesitant to go to the rural areas. The profitability is bound to be low with the large cash outflow.

### **3. Directed Credit and Investment in Agriculture and by Small Firms**

Following nationalisation of the banks, the policy of directed credit was instrumental in channelling credit to the priority sector consisting of agriculture, small-scale industry and weaker sections. It would be pertinent in this context to inquire whether such flow of commercial credit had a beneficial impact on investment in agriculture and small industry.

As regards agriculture, an influential study sought to quantify the inter-relationship among the investment decisions of government, financial institutions and farmers and their effects on agricultural investment and output. The study used data from 85 randomly drawn districts of India covering the period 1960-61 to 1981-82 and showed that,

- (i) The banks are more likely to locate branch offices in areas where the road infrastructure and the marketing system are improving;
- (ii) The expansion of commercial bank branches accelerated the pace of private agricultural investment; and

(iii) The effects of primary schools, regulated markets and commercial banks are particularly large in increasing fertilizer demand. (Binswanger et al. 1993)

The main finding of the study is that among all the variables,

"Education infrastructure availability and the rural banks play an overwhelming role in determining investment, input and output decisions. Availability of banks is a more important determinant of fertilizer demand and aggregate crop output than interest rates" (Binswanger et al. 1993: 337).

Thus, the expansion of rural branch network and directed credit did have a beneficial effect on agricultural investment and fertilizer demand.

The effect of directed credit on small-scale industry was similar to that on agriculture. In this context two questions are asked,

"First can we find differences in the way in which investment has been determined in small and large firms, in particular, evidence that small firms have faced more severe capital market constraints, and can any such difference be explained? Second, to what extent are the relatively high investment rates observed in small firms in the period attributable to the directed credit policy?" (Eastwood and Kohli 1999: 43).

The analysis, using data for 1965-78, suggests that,

".....directed credit policy in India was, in a narrow sense, well conceived and successful in the case of small modern sector firms: the financial constraint that the policy

was designed to relax does appear to have existed, and the extra bank credit channelled to small firms does seem to have raised their investment appreciably" (Eastwood and Kohli 1999: 57).

Although their analysis referred to the period ending 1978, and desegregated data are not available since then, aggregate data suggest the contrasts identified by them still exist (Ajit and Bangar 1997).

It is evident that branch expansion into rural areas had a definite influence on agriculture and small industry. Bank credit directed into agriculture and small firms have raised their investment appreciably. To that extent the objectives of bank nationalization have been fulfilled. No doubt the expected larger flow of credit into rural areas had a role in adversely affecting the profitability of the banks by raising the cash-deposit ratio as well as by lowering the amount per loan account.

#### **4. The Financial Sector Reform**

The period since nationalisation of the banks witnessed the government increasingly dipping its hands into the resources of the banks. The deposits mobilised from far flung areas was channelled into government and public sector by steadily raising the Statutory Liquidity Ratio (SLR) which reached 38.5 percent of the net demand and time liabilities of the system by 1991. The resources remaining after such pre-emption by the government was channelled into the priority sector consisting of agriculture, small-scale industry and small enterprise. The figure for priority sector lending reached a target of 40 percent of aggregate bank credit by 1990. Consequent to the emphasis on small loans the number of accounts in the priority sector rose from less than half a million in 1969 to over 35 million by 1990. Naturally the average size of credit became rather small.

Along with the regulation of the number and spread of branch offices and the deployment of credit, an elaborate administered interest rate structure also came into being. The coupon rates of government debt were kept very low with long maturity periods in the process preventing the development of a market for these securities. The interest rates of deposit accounts of differing maturity were announced as part of the credit policy. The interest rates of different size class of credit were also regularly announced. By 1990, there were six different administered interest rates, for six size class of credit limits, in addition to a concessional rate for weaker sections of society. Within this structure of interest rates there were differential rates for agriculture, small-scale industry and transport operators with up to two vehicles.

The Narasimham Committee having commended the Indian Banking system for its impressive quantitative achievements during the two decades since nationalisation in 1969 noted the decline in productivity and efficiency of the system and the related erosion of profitability. In the Committee's view the major elements leading to low productivity and profitability were,

Constraints on operational flexibility owing to directed investment in terms of SLR together with cash reserve ratios and directed credit programmes.

Decline in portfolio quality owing to political and administrative interference in credit decision making.

Concessional interest rate on directed investment and credit.

Expansion of branch network into rural and semi-urban areas turning many offices into primarily deposit centres without adequate credit business and income.

In addition to the above, the Committee identified numerous factors such as poor branch reconciliation, lax supervision, and poor quality of staff as responsible for the low productivity and profitability.

The above diagnosis of the maladies of banking led the Committee to recommend,

SLR requirements be related to prudential requirements and be brought down to 25 percent of net demand and time liabilities.

The borrowing rates to be brought closer to market rates.

CRR be turned into an instrument of monetary policy.

Directed credit programme be phased out in the long run; redefine priority sector in the shortrun, and review the concessional interest rate. Use fiscal instruments rather than the credit system to help the weaker sections.

Dismantle the administered interest rate structure and allow interest rates "to perform their main function of allocating scarce loanable funds to alternative uses".

Numerous other recommendations were made on capital adequacy norms, accounting policies and related matters, structural organisation of the banking system and other matters, the details of which are not relevant here. Another strong recommendation was that freedom of entry into the financial system should be liberalised and that there should not be any difference in treatment between the public and private sector banks. A related recommendation regarding branch expansion was that branch licensing be abolished and full freedom be given to banks to open and close branches.

The government accepted most of the recommendations of the Committee on directed investment, administered interest rate structure, privatization and on branch licensing, and modified the ones on directed credit. Implementation began soon after. And the last six to seven years have seen the banking system being turned from a highly regulated to one with a remarkable degree of freedom.

## **5. Sectoral Deployment of Credit Following Reforms**

One of the reasons attributed by the Narasimham Committee to the poor profitability of the banking system is the phenomenal growth of borrower accounts. It was said that, "by 1990, the number of such (priority sector) accounts had risen to over 35 million and with this the average size of credit has come down sharply with its obvious and corollary implications of rising unit costs of administering such loans". How has the Reform changed such a situation?

A concerted effort seems to have been made in the banking system to bring down the total number of loan accounts. The total number of loan accounts has come down from 620 lakhs in 1990-91 to 556 lakhs in 1996-97 (Table 4). The fall in the number of loan accounts has not been uniform across industry groups. The fall is confined to agriculture, transport operators and trade- largely those activities coming under the priority sector. Although industry has also reported a reduction in the total number of accounts, this is almost entirely on account of the reduction in "other industries". Industry, other than "other industries", has in fact, shown a slight increase in the number of loan accounts. The sharpest increases have however, been reported from the category of personal loans and professional services, a whopping 36 percent increase. Thus, in terms of the distribution of loan accounts there is a perceptible shift away from agriculture, trade, other industries and small-scale industry to large and medium industry and personal loans and professional services.

Distribution of outstanding credit across industry groups follows the distribution of loan accounts. The share of agriculture, other industries, trade and transport operators has all come down, and the share of industry and personal loans and professional services has gone up (Table 5). The sharpest fall in the credit share has been those of agriculture (3.8 percentage points) and other small-scale industries (three percentage points). The significant gainers are, industry- other than "other industries"- and personal loans and professional services, whose shares have gone up from 40 percent to 44 percent and 10.68 percent to 13 percent respectively.

The reduction in the number of loan accounts in agriculture, small-scale industry and trade has not been able to raise the average size of loan amount in these categories (Table 6). The average size of loan amount in the above industry groupings has, in fact, come down relative to the size of loan amount in industry, or overall average loan amount. At the same time, the size of loans in industry has been going up. The reason for such a situation becomes evident when one analyses the distribution of loan accounts by size class of loan amounts. In agriculture, trade and other industries, over 95 percent of the loans are of size less than Rs.25000 and this has hardly changed during the last seven years. Obviously, there are constraints in raising the size of loan amount in these industry groups. In the face of such constraints the strategy to raise the size of average loan amount overall seems to be to focus on industry, personal loans and professional services and financial institutions where the size of loan amounts are higher.

## **6. Local Banks and Emerging Business**

Narasimham Committee visualized that, "given the freedom of entry into the financial system, there could be strong possibility that several new banks with a predominantly local character would be set up

and existing local banks would find the environment congenial for increasing the size and scope of their operations". The Committee also favoured a level playing field for Foreign Banks (FB).

The developments of the last six or seven years have gone as visualized by the Committee. The FB and other scheduled commercial banks (OSCB) have been able to increase their shares of deposit and credit. The State Bank of India and its associates (SBI) have been able to maintain their share of deposits and credit in the new environment (Table 7). But the Nationalised Banks (NB) as a group have been losing out their share of deposits and credit. Their share in total credit business has come down by almost 10 percentage points (from 58 percent to 49 percent) between 1990-91 and 1996-97. The share of NB in total deposits has come down slowly from 61 percent to 55 percent. The gainers are FB and OSCB. The Foreign Banks have increased their share in total deposits and credit by around 1.5 percentage points each. In comparison the gains of OSCB have been considerably higher at around 5.5 percentage points each. The Regional Rural Banks have not shown much of a change. Thus, the FB and OSCB seem to be gaining at the expense of NB.

Industry being one of the sectors gaining in terms of credit share, it would be of interest to analyse the shares of bank groups in the aggregate credit to industry (Table 8). Again, SBI has been able to maintain its share of credit to industry at about 31 percent of the total. The NB has lost about 10 percentage points in its share of total credit to industry. The gainers are mainly FB and OSCB, with the gains of the latter being significant. The share of OSCB has improved from less than three percent in 1990-91 to close to nine percent by 1996-97.

While in the area of bank credit to industry OSCB has made significant gains in relation to FB, in the case of PL&PS, the FB has

gained significantly. The total number of loan accounts (PL&PS) has increased by about 36 lakhs between 1990-91 and 1996-97 (Table 9). Of this increase, about 10 lakh accounts have been cornered by FB, 13 lakh by NB, four lakh each by SBI and OSCB. Interestingly, PL&PS loan accounts formed almost 90 percent of the total loan accounts of FB through out this period whereas their share in the total loan accounts of OSCB has increased from around 20 percent to 40 percent. Thus, it is evident that the private banks and foreign banks are emerging as highly specialised in certain areas of banking whereas the NB and SBI continue to be highly diversified. But one characteristic that distinguishes all bank groups, including Regional Rural Banks (RRB), is their effort at curtailing their exposure to agriculture.

As already indicated, total loan accounts (agriculture) have come down by about 50 lakhs. This reduction in total number of accounts is distributed among SBI, NB, FB and RRB according to their share in total number of loan accounts (agriculture) in 1990-91. The FB had negligible exposure to agriculture and OSCB had about 20 percent of its loan accounts in agriculture. Both FB and OSCB continue in the same situation.

Along with the shift in business composition, there has come about a perceptible change in the composition of credit by duration. The share of long term loans in the total credit deployed has steadily been coming down and that of medium term loans going up (Table 11). The share of demand loans has also been increasing rather significantly. Another notable trend has been the increase in export related credit (packing credit, export bills discounted/purchased, etc.). The share of all other types of credit (mainly inland bills purchased/discounted) has come down significantly.

There are two distinct trends observable in the banking sphere during the last six to seven years. Firstly, a definite shift away from agriculture, trade and transport operators to industry- that too large and medium industry- and personal loans and professional services is taking place. Secondly, an increasing presence of OSCB and FB is visible in the emerging businesses. These trends have serious implications for the regional distribution of bank credit. This is the subject we turn to in the next section.

## **7. The Regional Distribution of Banking Business**

One of the arguments advanced against branch licensing by the Narasimham Committee was that "most of the rural branches are unremunerative and lack viability in their operations". The poor profitability of rural and semi-urban branches, the committee argued, was on account of them being primarily deposit centres without adequate credit business and income. Following the abolition of branch licensing it would be pertinent to analyse the trends in branch expansion and deployment of credit across the states of India.

At the all-India level the number of branch offices of commercial banks increased by 3387 (5.49 percent) during 1990-91 to 1996-97. The percentage increase showed considerable variation across the states of India. The highest percentage increase in the number of branch offices was observed in Punjab, Haryana (over 10 percent), and Delhi (eight percent) followed by South India and Maharashtra (Table 12). Their share in the total number of branch offices opened was two-thirds. The rest of the region showed significantly lower percentage increase in the number of branch offices opened. Thus, the abolition of branch licensing has led the banks to focus their attention on some selected regions of the country, especially South and North-West parts.

The regional concentration of branch expansion is also related to the privatisation of banking. Significant increases in the number of branch offices were reported by the foreign banks (22.67 percent) and other scheduled commercial banks (17.24 percent), while the overall increase remained at just 5.49 percent. Both SBI and NB groups have shown low percentage increases, 6.91 percent and 6.14 percent respectively, but have been able to maintain their shares in the total as RRBs have shown no growth. The FB have expanded their branch network in the metropolitan areas, with the exception of Calcutta. The OSCB are basically concentrated in South India and Maharashtra, with 75 percent of the branches concentrated in this region as of 1990-91. The branch expansion of OSCB was also mainly confined to this region. Thus, the OSCB are focusing their business activity in the areas of their origin.

Given the freedom of choice, why is it that the banks focus on some states and neglect others? A partial answer to that question has been provided in terms of the location of origin of private banks. A fuller answer needs, however, to be found in terms of the variation in deposit and credit business across the states. Taking up deposit business first, it may be seen that the deposit per branch in rural areas varies widely across the states of India. The coefficient of variation (percent) of the per branch deposit (rural) of states varied between 70 to 78 percent during 1990-91 to 1996-97. For an all-India average of Rs. 1.01 crores of deposit per rural branch office, the amount was Rs. 3.47 crores in Goa, Rs. 2.76 crores in Punjab and Rs. 1.74 crores in Himachal Pradesh. The deposit amounts in Maharashtra, Karnataka, Andhra Pradesh or Tamilnadu were not significantly higher than the amounts in Bihar or Uttar Pradesh. In the urban areas, the deposit per branch office did not show any significant variation at all. The coefficient of variation was just around 30 percent in all the seven years. Given that only about 15 percent of the total deposits

are accounted for by the rural areas, and that the deposit per branch office in the urban areas did not vary much from state to state, there is no reason to expect that the attraction of deposits take banks to any particular state to the neglect of others.

The story is very different when it comes to the credit business per branch office across the states of India. The coefficient of variation is fairly high and has been steadily increasing in the 1990s (Table 13). As regards credit business, there are a few distinct patterns across the states of India. At one end is Delhi and Chandigarh, where the per branch credit business amounts to over three times the all-India average. In Maharashtra, it is over twice the national average and has been increasing. In Gujarat, Tamilnadu, Goa, Kerala, Karnataka and Andhra Pradesh the credit business is close to the all-India average and is growing. In Punjab, Haryana and West Bengal credit business was higher than the all-India average in the early 1990s, but the growth has been rather slack and they have lost considerable ground in the 1990s. In the rest of the states, the credit business per branch office is less than 50 percent of the all-India average and there has been a decline in the 1990s.

With the discussion of the credit business per branch office across the states of India, an attempt may be made to answer the question regarding the attraction of banks to some regions. Banks are basically attracted by the growing credit business, in a milieu where banking habit has already developed and the cash outflow is minimised. As the credit business is increasingly getting concentrated in South, West and North-West parts of India, the banks are focusing attention in these regions.

The expansion of the branch network and credit business in selected states and regions has led to some disturbing trends in the shares of states in total commercial credit. As is evident from Table 14, in the 1980s, Maharashtra, Delhi, Gujarat, Kerala, and West Bengal were losing

their shares in total commercial credit. The rest of the states were improving their position steadily. Some notable gainers were, Assam (0.70 percent point), Madhya Pradesh (1.10 percent), Orissa (0.50 percent), and Uttar Pradesh (1.01 percent). The period beyond 1991 witnessed a reversal of this process. Those who improved their shares in the 1980s were all losing steadily in the 1990s. The losers were, Assam (0.64 percent), Bihar (0.57 percent), Madhya Pradesh (0.28 percent), Orissa (0.38 percent), Uttar Pradesh (1.53 percent), and West Bengal (1.50 percent). The numbers clearly show that all the states which had improved their shares in the 1980s were pushed back to the situation prevailing before 1980. This is a great fall. The gainers were just three, Delhi (1.96 percent), Maharashtra (3.56 percent), and Tamilnadu (1.02 percent). Karnataka and Kerala had only made marginal gains.

## **8. Summary and Conclusion**

The economic reasoning behind nationalisation of large commercial banks in India is the imperfection in the credit market and the natural bias of the banks against expanding into the rural areas, and lending to agriculture and small firms. The two decades since nationalization in 1969 has seen the expansion of branch network into the rural and non banked areas and lending to agriculture, small industry and weaker sections. Studies show that directed lending had a beneficial impact on investment in agriculture and small firms. The nationalisation of banks and the directed credit policy is well conceived is borne out by such findings.

The post-Reform banking trends are slowly reversing the trends of the two decades since nationalisation. The liberalisation of banking has aggravated the imperfections in the credit market. The natural bias of banks has come to the fore and they are increasingly withdrawing from lending to agriculture, small enterprise and such activities. Branch

expansion into rural and non banked areas has also stopped. Such withdrawal would have an adverse impact on the investment and output in agriculture and small industry was evident from the studies referred to in Section 3 above.

The new private banks and the already existing ones are competing to expand in South and North West India attracted by the growing credit business in a milieu with strong banking habits. This has resulted in a drastic reallocation of total commercial credit from the poorer agricultural states to Delhi, Maharastra and Tamilnad. The situation is exactly similar to the one referred to by Raj (quoted on page 5 above), where private banks are let to "skim the cream" without investing in the long term development of banking habits. Should the monetary authorities allow this to go on?

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**Table 1. Distribution (%) of Offices, Deposits & Credit of Scheduled Commercial Banks by Population Groups 1969-1989**

	1969	1974	1979	1984	1989
Offices					
Rural	17.6	36.1	43.3	53.7	55.7
Semi Urban	40.8	30.5	26.8	20.4	19.3
Urban	23.3	18.3	16.8	15.1	14.7
Metro	18.3	15.1	13.1	10.8	10.3
Deposit					
Rural	3.1	7.8	10.6	14.4	15.0
Semi Urban	22.0	22.7	22.5	20.7	21.4
Urban	25.9	24.8	24.9	26.0	25.1
Metro	49.0	44.8	42.0	38.9	38.6
Credit					
Rural	1.5	5.3	8.4	14.8	16.3
Semi Urban	11.3	14.7	15.6	16.4	17.3
Urban	20.0	22.9	22.7	23.5	23.0
Metro	67.2	57.1	53.3	45.3	43.5

Source: *Reserve Bank of India*. Banking Statistics 1972-1995.

**Table 2. Distribution (%) of Loan Accounts by Organisation  
1972-1992**

	1972	1977	1982	1987	1992
Agriculture	31.61	40.77	50.53	47.87	42.11
Industry	5.13	3.77	4.51	6.95	9.56
Transport Operators	1.21	1.75	2.10	2.48	2.20
Prof. Services & Personal Loans	27.03	19.64	17.01	14.90	16.78
Trade	6.75	6.46	9.87	14.29	17.94
Others	28.27	27.61	15.98	13.49	11.41
Artisans & Craftsmen	0.68	1.36	3.67	3.61	5.41
OSSI	3.98	3.34	2.29	6.24	3.32
Total	100	100	100	100	100
(accounts in millions)	(4.34)	(10.75)	(23.52)	(43.44)	(65.86)

Source: Same as Table 1.

Note: Others include Financial Institutions and miscellaneous.

OSSI- other small scale industries.

**Table 3. Distribution (%) of Loans Outstanding by Organisation  
1972-1992**

	1972	1977	1982	1987	1992
Agriculture	9.02	10.40	17.15	17.29	14.80
Industry	61.16	47.94	47.35	44.46	47.70
Transport Operators	1.58	2.70	5.15	4.01	2.62
Prof. Services & Personal Loans	4.96	4.89	6.19	10.74	11.02
Trade	14.85	28.45	18.51	18.75	14.76
Artisans & Craftsmen	0.09	0.21	0.31	0.62	0.69
OSSI	11.87	10.87	11.95	11.96	12.00
Total	100	100	100	100	100

Source: Same as Table 1., Note: OSSI- Other Small Scale Industries.

**Table 4. Distribution of Loan Accounts by Industry (100,000)**

Industry	1990-91	1991-92	1992-93	1993-94	1994-95	1995-96	1996-97
Agriculture	273	277	262	255	248	242	222
Industry	52	63	55	52	49	46	44
Other Industries	46	57	48	45	43	39	37
Transport Operators	14	15	14	12	12	11	11
Personal Loans and Professional services	100	110	109	106	105	122	136
Trade	106	118	107	103	99	92	89
Financial Institutions	0.16	0.18	0.19	0.20	0.22	0.22	0.22
Other Small Scale Industries	21	22	21	20	19	18	17
Total	620	659	621	597	581	567	556

Source: CMIE, Money and Banking, October 1999.

**Table 5. Distribution of Outstanding Credit by Industry (Percent in total credit)**

Industry	1990-91	1991-92	1992-93	1993-94	1994-95	1995-96	1996-97
Agriculture	14.95	14.80	13.58	13.00	11.83	11.31	11.12
Industry	47.58	47.70	48.60	48.15	45.61	48.00	49.34
Other Industries	7.17	7.46	6.83	6.16	5.92	5.72	5.69
Transport Operators	2.93	2.62	2.30	2.14	1.88	1.80	1.83
Personal Loans & Prof. Services	10.68	11.02	10.98	11.29	11.29	12.83	13.06
Trade	14.73	14.26	15.31	15.79	17.13	13.88	13.17
Fin. Institutions	2.26	2.93	2.44	2.59	3.77	3.54	3.97
Other Small Scale Industries	12.49	12.00	11.24	11.33	10.30	10.14	9.42
Total	100	100	100	100	100	100	100

Source: Same as Table 4.

**Table 6. Average Amount per Loan Account by Industry (Rs. 1000)**

	1990-91	1991-92	1992-93	1993-94	1994-95	1995-96	1996-97
Agriculture	6.81	7.30	8.41	8.96	10.05	11.91	14.04
Industry	114.57	103.57	143.59	164.38	194.44	264.46	316.88
Other Industries	19.59	18.02	22.95	24.24	29.29	37.01	43.61
Transport Operators	25.28	24.70	26.98	30.25	33.98	41.48	46.36
Personal Loans & Prof. Services	13.21	13.64	16.40	18.74	22.70	26.77	27.29
Trade	17.34	16.50	23.16	26.92	36.51	38.22	41.85
Financial Institutions	1704.90	2195.35	2085.80	2290.73	3668.05	4088.49	5140.39
Other Small Scale Industries	74.03	75.00	88.19	99.88	111.57	147.39	154.19
Total	20.05	20.76	26.16	29.49	36.31	44.94	51.13

Source: Same as Table 4.

**Table 7. Distribution of Credit and Deposit by Bank Groups (% share in total deposits in parantheses)**

	1990-91	1991-92	1992-93	1993-94	1994-95	1995-96	1996-97
SBI and Associates	27.95 (26.58)	27.44 (27.03)	30.83 (26.76)	32.45 (26.80)	29.15 (25.36)	29.15 (26.09)	29.20 (24.95)
Nationalised Banks	57.49 (60.97)	55.94 (58.95)	54.30 (58.30)	52.72 (57.10)	53.42 (57.28)	51.05 (56.12)	48.92 (55.29)
Foreign Banks	7.54 (5.68)	9.22 (6.88)	7.44 (7.52)	6.51 (7.81)	7.62 (7.48)	9.01 (7.05)	9.32 (7.12)
Regional Rural Banks	3.02 (2.42)	3.06 (2.46)	2.82 (2.49)	2.95 (2.84)	2.90 (2.97)	2.88 (3.22)	3.04 (3.54)
Other Scheduled commercial Banks	4.01 (4.35)	4.33 (4.69)	4.61 (4.92)	5.37 (5.45)	6.91 (6.91)	7.91 (7.52)	9.51 (9.12)
Total	100	100	100	100	100	100	100

Source: Same as Table 4.

**Table 8. Distribution of Credit (Industry) by Bank Groups (Rs.100 Crores)**

	1990-91	1991-92	1992-93	1993-94	1994-95	1995-96	1996-97
SBI	183	191	266	311	294	379	443
NB	330	355	417	428	511	605	659
FB	59	83	78	69	97	150	174
RRB	3	4	4	5	5	6	7
OSCB	16	20	25	35	54	84	120
Total	591	652	790	847	962	1223	1403

Source: Same as Table 4.

**Table 9. Distribution of Loan Accounts (PL&PS) by Bank Groups (1000)**

	1990-91	1991-92	1992-93	1993-94	1994-95	1995-96	1996-97
SBI	3352	4096	3944	3752	3512	3333	3821
NB	4899	5195	5154	4933	4916	5417	6110
FB	153	155	117	99	154	1190	1091
RRB	1077	1031	1036	1049	1074	1339	1587
OSCB	566	572	617	761	834	926	1000
Total	10046	11049	10868	10595	10491	12205	13610

Source: Same as Table 4.

**Table 10. Distribution of Loan Accounts (Agriculture) by Bank Groups (100000)**

	1990-91	1991-92	1992-93	1993-94	1994-95	1995-96	1996-97
SBI	75	79	73	71	68	64	61
NB	126	126	118	114	110	109	101
FB							
RRB	67	67	66	65	65	64	58
OSCB	5	5	5	5	5	5	6
Total	273	277	262	255	248	242	225

Source: Same as Table 4.

**Table 11. Distribution of Total Credit by Type (%)**

Type of Credit	1990-91	1991-92	1992-93	1993-94	1994-95	1995-96	1996-97
Cash Credit/Overdraft	43.42	43.78	46.80	47.62	44.42	43.12	38.99
Demand Loans	3.47	4.50	5.08	6.42	6.03	8.00	12.25
Medium Term Loans	5.83	6.05	5.58	6.24	8.35	10.33	10.17
Long Term Loans	24.74	24.29	23.02	22.21	21.99	19.83	21.03
Export Related Credit	8.15	8.89	9.58	10.17	11.93	12.39	11.93
Others	14.39	12.49	9.93	7.34	7.28	6.33	5.67
Total	100	100	100	100	100	100	100

Source: Same as Table 4.

**Table 12. Distribution of Bank Offices by State**

	1990-91	1991-92	1992-93	1993-94	1994-95	1995-96	1996-97	Increase (%)
India	61724	62121	62774	63358	63817	64456	65111	3387 (5.49)
Uttar Pradesh	8591	8654	8723	8760	8992	8854	8897	306 (3.56)
Maharashtra	5775	5807	5868	5919	5951	6057	6179	404 (7.00)
Andhra Pradesh	4703	4745	4781	4879	4918	4969	5022	319 (6.78)
Bihar	4903	4929	4959	4976	4985	5003	5016	113 (2.03)
Tamilnadu	4434	4460	4522	4593	4653	4728	4782	348 (7.85)
Karnataka	4407	4419	4463	4494	4523	4589	4644	237 (5.38)
Madhya Pradesh	4414	4444	4496	4504	4491	4490	4517	103 (2.33)
West Bengal	4303	4329	4359	4376	4391	4423	4444	141 (3.28)
Gujarat	3471	3484	3518	3546	3585	3575	3619	148 (4.26)
Rajasthan	3105	3120	3160	3202	3219	3275	3306	201 (6.47)
Kerala	2912	2925	2966	3043	3119	3161	3198	286 (9.82)
Punjab	2178	2184	2218	2247	2285	2353	2415	237 (10.88)
Orissa	2103	2129	2158	2174	2179	2187	2187	84 (3.99)
Haryana	1280	1290	1316	1336	1365	1384	1413	133 (10.39)
Delhi	1204	1210	1224	1230	1252	1273	1310	106 (8.80)
Goa	263	264	268	273	278	286	293	30 (10.24)

Source: Same as Table 4.

Table 13. Credit per Branch Office (Rs. crores) by State

	1990-91	1991-92	1992-93	1993-94	1994-95	1995-96	1996-97
Delhi	7.38	7.89	12.56	17.67	14.64	19.05	19.70
Chandigarh	6.32	6.60	6.03	9.78	18.61	14.42	13.43
Maharashtra	4.54	5.19	6.37	6.55	9.05	11.11	11.88
Tamilnad	2.98	3.16	3.66	3.88	4.81	5.81	6.77
Haryana	2.37	2.41	2.73	2.66	3.07	3.51	4.00
Punjab	2.28	2.40	2.57	2.78	3.39	3.73	3.99
West Bengal	2.22	2.46	2.90	2.87	3.32	3.76	3.95
Gujarat	2.13	2.28	2.70	2.66	3.25	4.04	4.31
Andhra Pradesh	1.91	2.13	2.37	2.49	3.06	3.60	4.10
Karnataka	1.80	2.04	2.08	2.34	2.84	3.65	4.17
Goa	1.76	1.92	1.85	1.65	2.52	2.94	3.33
Kerala	1.59	1.71	1.92	2.14	2.50	2.84	3.31
Jammu & Kashmir	1.33	1.34	1.36	1.35	1.28	1.32	1.48
Assam	1.24	1.57	1.63	1.40	1.49	1.57	1.67
Madhya Pradesh	1.17	1.23	1.36	1.43	1.54	2.14	2.34
Uttar Pradesh	1.14	1.21	1.33	1.37	1.53	1.65	1.92
Rajasthan	1.09	1.21	1.40	1.43	1.68	1.69	2.19
Orissa	.95	1.06	1.16	1.18	1.35	1.61	1.61
Himachal Pradesh	.80	.82	.88	.85	1.13	1.19	1.25
India	2.01	2.20	2.59	2.78	3.31	3.95	4.38
CV(%)	44.60	45.94	48.57	47.22	55.42	57.92	56.37

Source: Same as Table 4

**Table 14. Distribution of Commercial Credit by States in India, 1980-1996**

	1980	1985	1991	1994	1996
Delhi	12.16	8.28	6.51	8.11	8.47
Maharashtra	22.16	24.72	20.52	23.84	24.08
Tamilnad	9.60	8.96	9.60	9.91	10.62
Haryana	1.90	1.88	2.12	1.85	1.85
Punjab	3.42	3.64	3.58	3.43	3.16
West Bengal	10.11	7.93	7.26	6.46	5.76
Gujarat	6.03	5.15	5.43	5.15	5.11
Andhra Pradesh	5.59	6.68	6.89	6.66	6.75
Karnataka	5.86	6.53	6.15	5.68	6.35
Goa	0.52	0.42	0.35	0.31	0.32
Kerala	3.97	3.86	3.42	3.45	3.47
Jammu & Kashmir	0.48	0.60	0.73	0.46	0.39
Assam	0.63	0.90	1.33	0.83	0.69
Madhya Pradesh	2.64	3.26	3.74	3.07	3.46
Uttar Pradesh	6.12	7.05	7.13	5.95	5.60
Rajasthan	2.30	2.60	2.57	2.40	2.38
Orissa	1.03	1.58	1.53	1.31	1.15
Himachal Pradesh	0.28	0.40	0.42	0.36	0.32
India	100	100	100	100	100

Source: Same as Table 4.

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