Role of Scheduled Commercial
Banks in the Socio-economic
Development of Nagaland: An
Analytical Study

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I am very excited to present "Role of Scheduled Commercial Banks in the Socio-economic Development of Nagaland: An Analytical Study" to the readers of the subject.

As a special feature of the book, I can claim up-to-date data have been collected from Reserve Bank of India, Guwahati, State Bank of India, Main Branch, Dimapur and from Guwahati University's library and other related institutions.

This book highlights the functioning of Scheduled Commercial Banks in the state of Nagaland and its role in the socio-economic development of Nagaland. Comparisons have been made with respect to all-India levels and problems faced are highlighted with proper remedial measurers to overcome these problems.

This book will be helpful for the banks in Nagaland to formulate policies for further improvement. It will also help the financial institutions of Nagaland to uplift the economic development. It will be also helpful for the students of Commerce, especially in the field of Finance and Banking.

Care has been taken to make the book flawless. In spite of the sincere efforts on my part and also on the part of the printers and publishers, if any error still remains, I beg to be excused for the same.

I am thankful to ICSSR, New Delhi for sponsoring this book.

Once again, I am thankful to M/s Himalaya Publishing House for bringing the book in time.

Suggestions for further improvement of the book will be highly appreciated.

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Dr. Sanjay Chhabra
Author
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## Chapter 1

### Introduction

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Banks are the primary source of channelising the growth with required emphasis on the available resources and sustenance. Commercial banks play a very important role in the socio-economic development of any region. The economic and financial system that India inherited at the time of Independence was not at all suitable for the settlement of the socio-economic problems, which generally the financial sector should achieve. Thus, immediate necessity was the political movement for the Nationalisation of Reserve Bank of India, which was completed in 1949 in the goal that the Central banking institution of the country would have the commitment to serve the social and economic objectives laid down by it. At the same time, the Imperial Bank of India, the premier banking
institution was nationalised in 1955 for the extension of banking facilities on a large scale, more particularly in the rural and semi-urban areas, and renamed as State Bank of India (SBI). The structure of public sector banking was strengthened further in 1959 through the establishment of subsidiaries of State Bank of India.

The banking sector is divided into Commercial banks and Co-operative banks. The modern Commercial banking started in India in the beginning of 19th century. Bank of Hindustan (1770) was the first bank to be established at Calcutta under European management. Other banks set up were Bank of Bengal (1806), Bank of Bombay (1840), and Bank of Madras (1843). These were called Presidency banks. The first purely Indian bank was Punjab National Bank (1894) but in 1881 was formed the first bank with limited liabilities to be managed by Indian board, namely, the Oudh Commercial Bank, the Imperial Bank, by amalgamating the Presidency banks of Bengal, Bombay and Madras was nationalised in 1955. Again fourteen banks were nationalised in 1969 and more six in April 1980. Thus, 28 banks were nationalised. These nationalised banks together with regional rural banks come under the category of public sector commercial bank. The other kinds of commercial banks are the private sector commercial banks.

The Reserve Bank of India, Act 1934 has classified the banks as scheduled banks and non-scheduled banks. The scheduled banks are those, which have a paid-up capital and reserves of an aggregate value of not less than Rs. 5 lakh and which satisfy Reserve Bank of India, that their affairs are carried out in the interest of the depositors. All commercial banks are scheduled banks.

In India, we have all the nationalised banks since 1980, under Reserve Bank of India, which constitutes the National Policy for development taking the guidance from National Planning Commission. In the banking sector, we have various systems in place such as International Banks, Commercial Banks, Industrial Banks, Regional Rural Banks, Co-operative Banks, etc. with particular emphasis, as required. Since nationalisation of major commercial banks in 1969, the banking business has multiplied manifold. Even the geographical spread has expanded from 8,262 branches in June 1969 to nearly 66,000 branches. In September 2002, a vast majority of the people of the country are yet to get the services of the banks particularly in the rural areas. Moreover, after independence of our country, a number of plans and programmes have been adopted and implemented by the Government through commercial banks for their better lifestyle of the people of the nation. Among these, the scheme of bank nationalisation, creation of Lead bank and new Licensing policy are the cornerstone for availability of bank finance to the people for improvement of socio-economic activities of the nation. Therefore, it is observed that commercial bank has occupied an important position towards overall development of the people living in urban as well as in rural India.

The role of financial intermediation in the process of economic development has long since been recognised by distinguished economist like Schumpeter, Kalecki and Keynes. Subsequently, the relationship between financial development and economic growth has been articulated in the pioneering work of Goldsmith (1969), Mackinnon (1973), Shaw (1973) and Fry (1980, 1982, 1988) and lately in the works of the endogenous growth school [King and Levice (1993) Roubini and Sala-i-Martin (1992)]. Two discernible traits emerge from the studies on the relationship between financial development and socio-economic growth.

- Economic growth depends on the dynamism and efficiency of financial sector; and
- Both socio-economic and financial development mutually influences each other in a reinforcing manner.

Given the increasing role of financial markets in developed and emerging economies including India, the role of banks in economic development still remains an actively debated issue. In fact, renowned economist and Nobel Laureate, W.A. Lewis defined economic development as, “the process by which a community which was previously saving and investing 4 or 5 per cent of its national income or less, converts itself into an economy where voluntary saving is running at about 12 to 15
Introduction

- Maturity transformation, i.e., provision of alternate forms of deposits to the savers according to their liquidity preference while at the same time offering the borrowers with loans of desired maturities.
- Risk transformation, i.e., distribution of risks through diversification which substantially reduces risk for savers (depositors), which would prevail while lending directly in the absence of financial transformation.

"In functioning as intermediaries, the banks reduce the: (a) search costs, (b) transaction costs, (c) monitoring costs, (d) verification costs." In the absence of intermediation, savers would have to search for investors and this would entail search costs. By offering standardised products and services to depositors and borrowers, banks also reduce the cost of repetitive searches, i.e., transaction costs. In the process of accepting deposits and extending loans, banks acquire informational advantage over other financial intermediaries and hence can reduce agency costs such as monitoring and verification costs.

The process of financial intermediation supports increasing capital accumulation through institutionalisation of savings and investment and as such, fosters economic growth. The gains of the real sectors of the economy thus depend upon how efficiently the financial sector performs. More specially, the banking sector performs the basic functions of financial intermediation.

1.1 The Role of Banks in Financial Intermediation

Banks are the dominant intermediaries in a developing economy like India. "From the economic point of view, the major tasks of banks are to act as intermediaries channeling savings to investment and consumption: through them the investment requirements of savers are reconciled with the credit needs of the investors and consumers. Banks accept deposits from the public — secured or unsecured," which are usually easily accessible to the depositors and hence become the principal means of making payments. They are, thus, at the heart of the payment system. "Even when corporate or government approach households directly with new instruments, those payments are cleared through the banking system. In deploying the funds (deposits), the banks strike a balance between low yielding, high quality liquid assets and high yielding, riskier investment."

The basic function of bank intermediation can be grouped as:

- Liability-asset transformation, i.e., accepting deposits from the public as liability and converting the same into assets such as loans.
- Size transformation, i.e., providing large loans on the basis of numerous small deposits.

purposive.” Hence, to ensure financial discipline and the end-
use of credit, the Reserve Bank of India (RBI) introduced the
Credit Authorisation Scheme in 1965. The scheme was
introduced for regulating directly bank credit to large borrowers
in both the private and public sectors. The main feature of the
scheme is the requirement of prior authorisation of the RBI or
later reporting to it in respect of large credit facilities given by
banks. However, in actual practice, the banking system and
more so the banking policies failed to operate in a manner
consistent with the ideas indicated in the First Plan document.

The chief method of lending by commercial banks in India
had been the cash credit system, of which the banks could
control only the credit limits and not their actual utilisation.
This resulted in excessive financing of inventories and
receivables of the industrial sector at the expense of other
sectors. A study group was constituted by the RBI under the
Chairmanship of V.T. Dehejia in 1968 to examine the extent to
which the credit needs of industry and trade were inflated and
suggest necessary remedial measures. The committee
observed that:

- Banks credit to industries had grown at a higher rate
  vis-à-vis the industrial output.
- Credit appraisal by banks were not adequate.
- Short-term credit was utilised to finance long-term
  current assets.

Consequently, the committee suggested that credit
appraisal be done on the basis of financial situation of the
borrower and cash credit component be segregated into two
components — hard core component representing minimum
current assets required for maintaining a given level of
production and the other short-term component. It also advocated
introduction of the bill financing by banks.

Despite the well meaning suggestion advocated by the
Committee not much could be achieved in the sphere of bank
lending. It was only after the setting up of the National Credit
Council (NCC), in the year 1968, that a new beginning was made
in the direction of evolving positive plans for deposit growth and
for credit allocation according to social priorities. The Council
had indicated three sectors — agriculture, small-scale
industries and exports as deserving treatment in the matter of
bank credit. But social control was not effective in socialising
the banking process in the country. The existence of “credit
gaps” and their growth constituted the principle of economic
justification for the nationalisation of major commercial banks.

“An institution such as the banking system which touched and
should touch the lines of millions has necessarily to be inspired by
a larger social purpose and has to subserve national priorities and
objectives”, announced the then Prime Minister Late Smt. Indira Gandhi in her broadcast to the nation when she nationalised
fourteen major commercial banks on July 19, 1969 and made
it an epoch-making event in the history of Indian banking. The
main objective of the nationalisation was to control the heights
of economy and to meet progressively and serve better the needs
of the development of the economy in conformity with the
national policy and the objectives and for matter connected
therewith or incidental thereto (Preamble to the Banking
Companies Act, 1970).

The central objective of nationalisation, thus, was to make
banking an effective instrument and catalytic agent of socio-
economic development. In terms of operation, this essentially
meant widening of banking facilities, spreading banking habit
among people, mobilising savings of the community on a
massive scale and deploying the resources thus mobilised in a
purposeful manner for all productive activities irrespective of
the size and social status of the borrower.

Besides the regional disparities in spread of banking
network prior to nationalisation, there existed widespread
disparities in the distribution of sectoral credit as well. The
integration of credit planning with economic planning since
the nationalisation of banks in 1969, in tune with the
requirements of five-year plans and national priorities has been
the important step in deciding the credit allocation for different
sectors.

The branch expansion programme of banks in the post-
nationalisation phase was interwoven with the Lead Bank
Scheme (LBS), of the RBI, adopted in December, 1969 as per
the recommendations of the Gadgil Group of NCC. Given the diversity of conditions all over the country, it was felt that an area approach was essential for appropriate credit arrangements on the basis of local conditions. Accordingly, all the districts in the country were adopted by the major Indian commercial banks which were then made responsible for playing a lead role in the expansion of banking facilities, identify and study the local problems and evolve credit plan for the overall economic development of the district. Under the scheme, the District Credit Plans (DCPs), with time bound credit targets for institutional credit agencies in the district block-wise, sector-wise, scheme-wise and bank basis are prepared and implemented.

1.3 Policy Initiatives and Financial Sector Reforms in the Post-nationalisation Era

The extension of formal financial (credit) coverage to the rural sector in India received a great impetus following the nationalisation of banks. However, vast areas of rural India still remain outside the ambit of formal credit institutions. The situation aggravates further in case of underdeveloped regions within the economy. Regional imbalances have been a marked feature of India’s development process. Thus, on one hand, there exist pockets of extremely underdeveloped regions within a developed state in India as well as pockets of highly developed centres in a backward state.

The initial euphoria of bank nationalisation was thus, broken when it was observed that the entry of commercial banks in the field of agricultural finance led to certain problems in the supply of institutional credit in the rural areas — stemming from the high cost structure of the branches operating in rural areas and the lack of effective manpower to deal with rural clientele and problems of agricultural finance.

Hence, with a view to improve the banking structure in the rural areas, the Banking Commission in 1972 made the recommendation for the creation of Rural Banks. Realising that the primary credit society had been the weakest link in the co-operative system, the Banking Commission felt that the primary ties had to be replaced by a network of Rural Banks.

Thus, a ‘Rural Bank’ is described by the Commission as “a primary banking institution set up to serve compact group of villages generally, working as a co-operative bank or as a subsidiary of commercial bank.” However, it was only after the recommendation of the Working Group on Rural Banks under the chairmanship of M. Narasimhan in 1975 that the Government of India set up the Regional Rural Banks under the Regional Rural Banks (RRB) Ordinance, 1975. Despite the setting up of the RRBs, the rural agrarian sector of the economy still remained outside the ambit of rural credit supply. Most of the banks in the rural areas turned out to be deposit branches. Consequently, in 1975, the Government of India set before the public sector banks the targets of providing one-third of their credit outstanding to all priority sectors including exports. In March 1980, this target was revised upward to 40% to be attained by 1985. With respect to directed credit programmes, as this, despite considerable unproductive lending, there has been clear evidence that the contribution of bank credit to the growth of agriculture and small-scale industry has made an impact.

It is worth mentioning, that the way the RRBs have evolved was quite different from what the Working Group which had suggested their formation had in mind. RRBs were conceived as low-cost institutions with a separate (and lower) wage structure but that hope belied by subsequent events. Nor did that Group envisage that the RRBs should confine their activities only to small farmers and small industries as they were later enjoined to do. In the process, the RRBs, have become the victims of the policy induced distortions and have turned out to be unprofitable ventures. The RRBs have now been permitted to deploy their resources in non-target avenues: for instance, they can invest in commercial banks, shares and debentures of corporate bodies and in bonds of financial institutions and of public sector units. This has only led to encouraging the reverse flow of funds from the rural to the urban areas.

Despite various studies and suggestions on the credit delivery system of Indian banking system, serious distortions continued to exist. This necessitated an evaluation of the

existing credit delivery. A Study Group to frame guidelines for follow-up of bank credit under the chairmanship of P.L. Tandon was constituted by the RBI, in 1974. The Committee observed that:

- Cash credit system of lending wherein the borrower can draw freely within limits sanctioned by the banker hinders sound credit planning on the part of the banker and induce financial indiscipline on the borrower.
- The security-oriented approach to lending favoured the borrowers with strong financial base and also led to diversion of funds.
- Working capital finance though theoretically short-term finance, tended to be long-term finance.

The committee made comprehensive recommendations in four broad areas:

- Norms for inventories and receivables for fifteen major industries were suggested based *inter alia* on company finance studies made by the RBI.
- The Group took the view that a banker’s role in financing a borrower is to supplement the latter’s resources in carrying reasonable level of current assets in relation to his production requirement and not to meet the whole of his working capital requirement. Three methods for determining permissible amount of bank finance were suggested. It was of the view that this amount should not exceed 75% of the working capital gap and should be reduced progressively.
- Having laid down the norms for determining the quantum of bank credit for individual, the Group suggested a new style of credit — (a) a loan component, comprising the minimum level of borrowing throughout the year and (b) a demand cash credit component to take care of fluctuating requirement, both being reviewed annually.

Despite the fact that the recommendations of the Tandon Committee were pragmatic and sought to rectify the inherent malaise in the credit system, the flexible application of the norms defeated the very aims of the recommendations. The James Raj Committee7 (1978) evaluated the performance of the banking industry in the post-nationalisation period and made a number of suggestions on a wide-ranging subjects seeking to apply societal goals of banking policies in a flexible manner.

While committees were instituted as periodic political responses to the system’s ailments, the implementation of the substantive reforms suggested were either never implemented or if implemented were in a so-called flexible manner as and when necessary.

The 1980s was the most crucial period for the banking sector in India. The quantitative achievements in respect of credit plans became increasingly ritualistic, but the goals stood the test of time and required reinforcement through greater focus on the quality of delivery. It was during the 1980s that the first attempt at reforming the banking sector came with the submission of the report of the committee set up to review the working of the monetary system (popularly referred to as the Chakravarty Committee Report, 1985).8 The Committee advocated the necessity of moving away from quantitative controls which it felt led to distortions in the credit market and resulted in curbing the growth of the economy. As regards administered interest rates, the Committee pointed out that:

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The administered interest rate system has grown to be unduly complex and has reduced the ability of the system to promote the effective use of credit.

Concessional rates of interest appear to have allowed projects of doubtful viability to be undertaken.

The low yields on Treasury Bills and Government securities have, on the other hand, led to considerable monetisation of public debt, fuelling monetary expansion, and on the other hand, have adversely affected bank profitability and the growth of capital market.

The administered system of interest rates has been found to be lacking the flexibility necessary for augmenting the pool of financial savings by affecting suitable changes in the deposit rates as the low profitability of banks has made banks wary of increasing the average cost of deposits.

The policy of insulating banks from price competition and confining competition to consumer service has not served to promote high standards of customer service.

With the introduction of New Economic Policy (NEP), in 1990, reforms and liberalisation have been brought about in the real sectors of the Indian economy. Simultaneously, under the impact of NEP, there has been continuing deregulation and liberalisation of the banking system as well. The impetus to reforms in the financial sector received a major thrust with the submission of the Report of the Committee on the Financial System (1991), popularly referred as the Narasimhan Committee. The Committee recommended wide-ranging reforms which included among other the reduction in pre-emption of bank resources (in the form of reserve requirements) and the directed credit programmes. It also recommended deregulation of interest rates so as to reflect market conditions and complete abolition branch licensing policy which regulated entry into banking. As regards Statutory Liquidity Ratio (SLR), the Committee was of the view that it should be used as prudential requirement and not as an instrument for financing public sector and recommended that the SLR be brought down to 25 per cent over a period of 5 years and Cash Reserve Ratio (CRR), to be gradually reduced and recommended the interest rate on these instrument be raised. The Committee also recommended various remedial measures to strengthen the viability of the banking system which included inter alia capital adequacy norms, income recognition and provisioning for bad debts. Hence, the need to improve the performances in terms of profitability, productivity and efficiency has assumed great significance for the Indian banking sector today.9

As a follow-up of the Chakravarty and Narasimhan Committee recommendations, various policy initiatives were taken by the Reserve Bank of India to move away from direct monetary policy instruments to indirect monetary controls. Firstly, the level and structure of interest rates have been rationalised in a phased manner culminating in the abolition of minimum lending rate in 1988 and letting the banks to determine their prime lending rates (PLR). In 1995, all controls were phased out to bring down CRR to 10 per cent and reduce SLR to 25 per cent on an incremental basis. Thirdly, prudential norms and regulations were introduced to ensure the safety and soundness of the financial system and at the same time to encourage market forces to play an increasing role.

However, insofar as the recommendations with respect to directed credit programmes were concerned, the government policy have continued with the existing norms for the Indian commercial banks and have also made it mandatory for the foreign banks operating in India to ensure that at least 32% of their net bank credit is directed to priority sector inclusive of SSI and exports. Within the priority sector lending also, agriculture has to account for at least 18% of net bank credit. However, the newly set up private sector banks have been permitted to substitute the agricultural lending requirements by contributions to deposits with SIDBI/NABARD* for a period of three years from the date of inception. Since then, major

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* SIDBI: Small Industries Development Bank of India.
  NABARD: National Bank of Agriculture and Rural Development.
changes have been affected in the domestic, economic and institutional scene and these developments have reinforced the importance of building a strong and efficient financial system. The second Narasimhan Committee Report on Banking Sector Reforms\(^\text{10}\) set up by the United Front Government to review the progress of reforms in financial sector in 1991, which was submitted in 1998, spelt out the course for second generation reforms in terms of three broad interrelated issues:

- Actions that need to be taken to strengthen the foundations of the banking system.
- Related to this, streamlining procedures, upgrading technology and human resource development.
- Structural changes in the system.

These would cover aspect of banking policy, institutional, supervisory and legislative dimensions. The committees have observed that, an attempt at strengthening the foundation of the banking system would involve improving the quality of bank assets and nothing is more indicative of the quality of assets than the quantum and incidence of Non-performing Assets (NPAs), in relation to the total portfolio. The causes for a high proportion of NPAs are varied. Poor credit decisions by bank management, difficult recovery environment represent some of the micro and macro aspects of life. This is not all. Often, as international experience has shown, a high incidence of NPAs could be traced to policies of directed credit, not to speak of cruder forms of directed lending. Social banking need not conflict with canon of sound banking but when banks are required has shown the danger of erosion of the quality of the loan portfolio. An important aspect of the continuing reform process is thus to further reduce the high level of NPAs as a means of institutional strengthening.

In respect of the directed credit programme, it was observed by the committee that proportionately higher share of NPAs were in this category which has been one of the factors for erosion in the quality of bank assets. The Committee is of the view that the interest subsidy component should be eliminated in respect of priority sector credit and what is important is the ‘timely and adequate availability of credit rather than its cost which is material for the intended beneficiaries’.

In the process, the RBI has overhauled lending norms for priority sector advances. The central bank has amended the NPA classification norms for agricultural loans and also changes rules for directed lending in SSIs. The RBI has created subclasses of small-scale industries for the purpose of directed lending by banks. The changes are a part of the ongoing process of reforms in the agricultural sector and SSI sector conducted by the RBI. Consequently two committees, one on agriculture headed by Mr. R.V. Gupta, (former Deputy Governor RBI) and the other on SSI headed by Mr. S.L. Kapoor (former Secretary, SSI Government of India) had been set up. This clearly indicates that in pursuit of higher profitability banks will not be allowed to shy away from their social responsibilities in the development of the backward sectors of the economy.

Endorsing the report of the Gupta Committee set up on December, 1997, on Agricultural Credit, the RBI has directed all the scheduled commercial banks to work on its recommendations which have aimed at streamlining the credit delivery system by ensuring pre-sanction appraisal of the borrower focusing on his income, his capability of taking up the activity, integrity and technical viability of the project and disbursal of all agricultural loans in cash which will facilitate dealer choice to borrowers and foster an environment of trust.\(^\text{11}\)

The Kapoor Committee report on credit to SSI sector which was submitted to RBI on June 1998, made 126 recommendations of which 35 had been accepted by the RBI and the commercial banks have been directed to introduce tri-lingual loan application forms in Hindi, English and the local language; disposal of applications for amount up to Rs. 25,000 within a fortnight and those above Rs. 25,000 within 8-9 weeks. It has also directed to enhance the limit of composite loans from Rs. 2 lakh to Rs. 5 lakh so that entire requirement of such units is met by a single document; and also to assess the flow of credit to SSI by using data on disbursement rather than outstanding balances.


and accordingly fix disbursement targets along with outstanding balances. Regarding the overall interest rate payable by the SSIs, it has been decided to limit it within the existing parameters fixed, which is the PLR, plus four per cent.\footnote{Reserve Bank of India (1997), “The Report of the Committee on Credit to SSI Sector”, (Chairman: S.L. Kapoor), Mumbai.}

In the pioneering task of marshalling, the capital and credit resources in the planned economy of India and directing them to the best advantage of the society, the contribution of the commercial banks have been praiseworthy. Indian economy presents paradoxical picture of poverty in the midst of plenty. The commercial banks can be the only viable agency which can mop up the excess resources of the economy and direct them towards investments in the relatively poorer or less developed sectors of the economy.

1.4 Scope of the Study

Today, the commercial banks have cumulatively financed majority of loans and advances in the Wood, Handloom, Plastic, Paper, Agriculture, Food Processing, Formal Education, Vocational Training, Human Resource Development, etc. So also, it has helped in maintaining the savings of the individuals as well as societies. With the cease-fire in place between the insurgents and the Government of India and the globalisation with the advent of Internet, it is imperative to study the new challenges faced by the State for the socio-economic development and the positive role that the commercial banks can play in the changed circumstances. Particularly, Nagaland has a pool of talented unemployed youths with English fluency, technical and Western orientation which can be very handy for Human Resource Development. The study is essential to highlight the potential growth areas, the constraints and solutions for the all-round socio-economic development of this backward state of Nagaland with the assistance of the Scheduled Commercial Banks.

1.5 Need and Contribution of the Study

The state of Nagaland was carved out of the erstwhile Assam as the 16th state of the Indian Union, forming a part of the seven sisters of the North-Eastern states connected to the mainland with a narrow strip of 23 kms at West Bengal. The state touches an International border, i.e., Burma and three State borders, viz., Manipur, Assam and Arunachal Pradesh. The state encompasses almost 20 lakh population within a geographical area of 16,579 sq.km*. Its population has one of the highest growths in the country, i.e., more than 64%. The general population resides in the villages with as high as 83% whereas the overall tribal population stands at almost 88%.

Agriculture constitutes the major occupation of the Nagas since time immemorial, with the uniqueness of Jhum cultivation in particular. Agriculture is the backbone of the state economy where about 75% of the population engaged themselves in agriculture and depends on agricultural products but fails to make any headway due to inadequate infrastructure, lack of work culture and laziness and lack of knowledge amongst the villagers regarding borrowing and lending policies of commercial banks as well as financial institutions.

Nagaland is an industrially backward state. Till date, the state is industrially represented by 10 medium and large-scale industries, 1900 SSI units, 22 Cottage Industries, 3 Industrial Estates and 10 District Industrial Centres. Lately, a political will is being observed in formulating a Medical and an Engineering College. Community Information Centres have been set in 52 Blocks along with 3 Polytechnics including Institute for Communication Technologies at Mokokchung. All the earlier 8 Districts boast of a District Computer Centre. Since both the Central Government as well as State Governments of the state and also North Eastern Council (NEC) is desperately trying for the development of small and medium size industries in the state, commercial banks are expected to provide adequate and timely assistance. In view of the backwardness of the state, both commercial banks as well as financial institutions are also expected to offer adequate concessions through relaxing various conditions and norms, for working capital and term loans.

We cannot think of any social and economic changes and development without a good network of transport and

communication. But in this state, the transport and communication facilities are far below the desired level and thereby retarded the growth because of financial constraints. It is worth mentioning that the agriculture and industry cannot make any headway in this state if the present scenario of power generation is allowed to continue. Nagaland is already in debt with the neighbouring state in relation to the power. The term social overhead capital is widened to include health, skills, education and other qualities of the people which are essential pre-condition of development of a region or a state. In this connection, commercial banks and financial institutions can play a vital role towards socio-economic development of the state like Nagaland. But inspite carious efforts made by the Government on different direction the expected benefit from the commercial banks and other financial institutions have not trickled down to the poor and needy people living in urban as well as rural of this state.

In Nagaland, the function of scheduled commercial banks has been started with State Bank of India in the year 1962, 28th May in Dimapur, a year before Nagaland was granted the status of a full-fledged state of the Indian Union in the year 1963. In due course of time, various other banks came up such as Allahabad Bank, Vijaya Bank, Bank of Baroda, etc. So also, need was felt for regional banks as a result of which Nagaland State Co-operative Bank, Nagaland Industrial Development Co-operation, Marco fed, Nedfi, etc. were established to meet the particular needs of the State. But it is noticed that only few commercial banks namely State Bank of India (SBI), United Bank of India (UBI), Vijaya Bank, Central Bank of India (CBI) and Allahabad Bank (AB) have number of branches and accordingly, they operate from almost all the district of the State. Even though the banking industry in the State has attained noticeable achievement and credit expansion, etc., their performance with regard to credit deposit ratio has been unsatisfactory. The credit deposit ratio for the state is the lowest one as compared to the other parts of the country. Recently, RBI admonished the commercial bank to improve their credit deposit ratio which was far below the national average due to the perceived insurgency, thereby making the investment risky and jeopardising the stability.

From the above discussion, it is ascertained that the state of Nagaland is still backward as compared to the other parts of the country and could not develop much industrially despite of having vast natural resources. It should be mentioned here that, when the State was created, it was fully recognised that Nagaland would be economically non-viable and would depend almost entirely on central assistance for its economic development. But the growth of development depends on a complex interaction of large number of variables, not all of which are amenable to Government control and therefore, there is an urgent need to examine the role of scheduled commercial banks towards socio-economic development of the State of Nagaland and enough research, establishes the truth and suggest measures thereof to deal with the problem. It is with this background that the present piece of research is conceptualised and taken up. The present study will be highly significant to the State of Nagaland where several problems (such as social, economic, and political) and lack of finance (income) is a hurdle for development. This study will be helpful to the State itself for taking necessary steps and remedial measures for successful performance of banking sectors towards overall development.

1.6 Structure of Banking System in Nagaland and Rationale for the Study

In an underdeveloped or a developing economy like Nagaland, where banks constitute a crucial part of the economic infrastructure — both for mobilising investible resources as also for channeling the same for investment purposes these set of reforms assume greater significance. At the same time of nationalisation, Nagaland had 2 banks offices out of a total of 90 banks offices in the North East Region (NER), which were approximately 2% of the region's total. However, the region as a whole shared only 13.5% of the total bank branches in the country. Nagaland's share in the country's total bank offices stood at a merge 0.02%. The share of deposits and credit of the commercial banks in the State out of the country's total was negligible, i.e., less than 0.05%. From the given statistics, one can easily infer the state of banking habit and business existing in the State at the time of nationalisation. It may be noted here that the N.E. Region was not only underbanked but there
also existed high level of intra-regional disparity in spread of bank coverage. Within the NER, Assam enjoyed a place of privilege claiming a share of 82% of bank branches, 64% of deposit and 63% of credit at the time of nationalisation. Thus, among the four states and two Union territories, Nagaland accounted for only 2% of bank offices and less than 1% of deposit and credit.

Twenty-six years after nationalisation, the banking network in the State and the region has witnessed vast changes. Apart from expansion of branches, both mobilisation of deposits as well as credit has increased. The population coverage of branches too has improved since then. From coverage of 1,53,044 persons per bank office in the State against all-India coverage of 65,000 persons per bank office in 1969, the population coverage per bank office in 2002 stood at 28,010 persons for Nagaland against all-India figure of 13,169.

However, it may be noted here that despite the increase in both credit and deposit share of commercial banks in the State, the flow of credit to the different sector of the State have been meager. An approximate estimation of the credit flow vis-à-vis the deposit mobilisation is the Credit Deposit (CD) ratio. The CD ratio in Nagaland has not only been consistently below the national average but is also having a declining trend. Compared to the national benchmark of 60 per cent stipulated by the RBI, the credit deposit ratio was 12.8% for 2002, 43.87% in 2008.

<table>
<thead>
<tr>
<th>Year</th>
<th>Credit Deposit Ratio (India)</th>
<th>Credit Deposit Ratio (N.E. Region)</th>
<th>Credit Deposit Ratio (Nagaland)</th>
</tr>
</thead>
<tbody>
<tr>
<td>1969</td>
<td>55.78</td>
<td>47.04</td>
<td>27.44</td>
</tr>
<tr>
<td>1992</td>
<td>57.65</td>
<td>46.67</td>
<td>43.40</td>
</tr>
<tr>
<td>1995</td>
<td>55.60</td>
<td>35.55</td>
<td>37.80</td>
</tr>
<tr>
<td>2000</td>
<td>56.00</td>
<td>28.05</td>
<td>15.30</td>
</tr>
<tr>
<td>2002</td>
<td>58.40</td>
<td>27.17</td>
<td>12.80</td>
</tr>
<tr>
<td>2007</td>
<td>74.9</td>
<td>31.86</td>
<td>29.05</td>
</tr>
<tr>
<td>2008</td>
<td>73.9</td>
<td>40.69</td>
<td>43.87</td>
</tr>
</tbody>
</table>

Source: Calculated by the Researcher on the Basis of Deposit and Credit as per Quarterly Handout (March) RBI.

Introduction

While the socio-economic scenario of the state is rural and agrarian in nature, it is only natural that massive expansion of bank branches was taken up in the rural areas as a deliberate policy to develop the rural section of economy through credit flow. However, the fact remains through the bank branches have been opened, these could not effectively meet the desired social obligations in the state. Despite the fact that the per capita availability of both credit and deposit in Nagaland has increased at a faster pace during the decade, however the disparity with the all-India level has further aggravated.

The raises a pertinent question as to whether the banks have failed to participate in an effective manner in the development process of the state by providing adequate credit to the different sectors of the economy. Or is there some other factor hampering the flow of credit into the different sectors of the economy? The study aspires to analyse this interrelation in a comprehensive manner.
APPENDIX-I

Glossary of Terms Used:

**Capital Market:** Capital market is the market for the purchase and sale of shares, debentures, etc. with a view to raise long-term loans.

**Cash Reserve Ratio:** As per the Reserve Bank of India Act, scheduled commercial banks are required to maintain with RBI, some minimum cash reserve which has some relationship with bank’s time and demand liabilities. Cash Reserve is an important instrument of RBI’s monetary policy for regulating the liquidity in the economy.

**Credit Authorisation Scheme:** This scheme was introduced by the RBI, in 1965, as a means to regulate bank credit. Under the scheme, banks were required to obtain RBI’s Authorisation before disbursement of sanctioned loans which are more than the prescribed limits. The scheme has now been abolished and in its place a new scheme name as ‘Credit Monitoring Arrangement’ has been introduced.

**Credit:** This term generally refers to the time allowed for payment for the goods and/or services by the seller to his buyer. It is also used in banking parlance to mean loans and advances offered by the banks to the borrowers.

**Deposit:** Money placed in a bank for safe keeping or to earn interest. Deposits in a bank are of three types — fixed deposits also known as term deposits for a fixed period of time with a fixed rate of interest depending on the time period for which the deposit is kept; saving deposits bearing a fixed rate of interest lower than the term deposits and the accounts are freely drawn upon by the depositors; current deposits bearing no interest rate and are used for making payments in business and transaction purposes.

**Credit Deposit Ratio:** This is a ratio which is used to measure the proportion of credit as percentage of deposit. In other words, the CD Ratio shows the quantum of loan or advances per hundred rupees of deposits collected and is an approximate indicator of banking performance.

**District Credit Plan:** A district credit plan is a blueprint of activities undertaken by banks to bring about overall development of the districts. The plan includes identification of economic activities which could be financed by credit institutions, preparation of bankable schemes covering these activities and estimation of the credit demand likely to arise under these schemes. These plans are formulated by the Lead Banks for their respective lead districts.

**Financial Intermediation:** The process by which the financial institutions act as intermediary between savers of funds and users of funds.

**Financial Intermediaries:** Financial institutions that serve as financial intermediary between savers and users of funds. (e.g., Commercial banks, Development banks).

**Lead Bank Scheme:** The Lead Bank Scheme was introduced by RBI in December, 1969, to make an important instrument of local development by entrusting individual banks with the lead role to locate growth centres, assess deposit potential, identify credit gaps and to evolve a co-ordinated programme for development of each district allotted to them in consultation with other bank credit agencies.

**Non-performing Assets:** The RBI introduced prudential accounting standards for banks in April, 1992. The essence of the new system is recognition of the record of recovery as the basis of classification of the advances portfolio of the bank. Thus, if interest/installment of principal remained unpaid for a specified number of quarters, an advance had to be classified as a non-performing assets and depending upon the period for which it remained as NPA, it had to be classified as substandard or doubtful asset.

**Role of Banks:** The term is used to define the purposive actions of banks in any sphere of economic activities. The term ‘role of banks’ has been used here in the study to define the activities of deposit mobilisation and credit dispensation.

**Statutory Liquidity Ratio:** As per the RBI Act, each commercial bank in India is required to statutorily maintain a prescribed minimum portion of its daily total demand and time liabilities in the form of designated liquid assets. These liquid assets consist of: (a) excess reserves, (b) unencumbered government and ‘other approved’ securities and (c) current account balances with other banks.