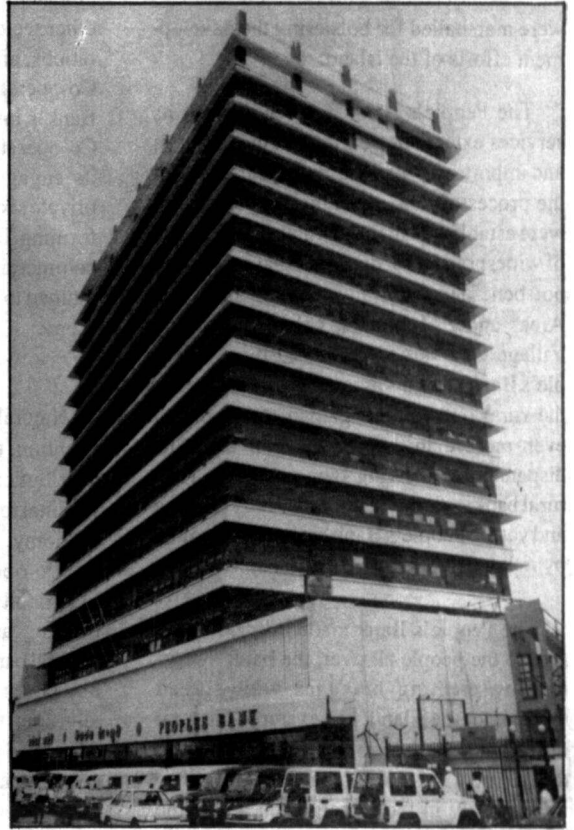


THE PEOPLE'S BANK THIRTY YEARS AFTER: RETROSPECT

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Since independence in 1948, Sri Lanka (Ceylon) has experienced many changes in the economy and more emphatically especially since the late Seventies, in the eighties and the early nineties. The banking sector of the country too has expanded during this period to sustain the economic progress and development in post-independent Sri Lanka. In this widening role of the banks and active participation of the banks in fostering the island's economic and social development, the People's Bank has figured as a significant and important actor. Indeed, the People's Bank has been closely involved with the development of the island in an overall sense particularly by its tremendous contribution to the economy, both rural and urban.

The People's Bank has taken a leading, and at times even an exclusive, part in supplying credit to the poorer people in rural and urban areas. The People's Bank weaned the poverty-stricken from their dependence for credit on undesirable non-institutional sources and brought a neglected lot of the island's inhabitants into the local banking mainstream. It catered specially to the impoverished agricultural sector of the rural areas and gave to those of this sector the means and wherewithal to emancipate themselves from the clutches of the exacting

money lenders, on whom they had been much dependent.

The People's Bank was the outcome of legislation presented to the House of Representatives in May 1961. As the name of the bank itself implies, the People's Bank was meant to be a democratic institution established not solely to render financial assistance to a select group only, such as the co-operative societies but also to answer the needs for credit of those outside them—it was to have a wider reach. Furthermore, the People's Bank by establishing a network of rural banks, granting financial aid to individual farmers, and even venturing to fund enterprises for developing entire areas within the ambit of local government, *ab initio* itself ventured beyond the scope of co-operative banking and directly into a real all inclusive rural sector.

True to its name, the People's Bank became the pioneer in making the banking habit really popular in practice. In addition, this bank took a principal part in "the redistributory function of transferring resources from the surplus to the deficit sectors". Over the years although the People's Bank had as a vital target the Co-operative Movement, now this bank is more acclaimed for its contributions in commercial banking.

But it is clearly evident that the People's Bank was correct in setting its sights on a broader field than in limiting its concern solely to the Co-operative sector. Now the People's Bank is little known among many for its incipient role in the fostering of the Co-operative Movement and it is better known instead for its successful intrusion into a wider range of avenues properly falling within the scope of a Commercial bank that functions within a competitive commercial arena. It is now taking on an even more versatile role as a bank in a fast growing economy.

The People's Bank forged ahead, as the years went by, keeping pace with Sri Lanka's economic growth; and in fact there was a healthy mutual interaction between these two phenomena which consequently accounted in a noteworthy manner to improve the standard of living of the people. The banking habit was inculcated in a sector of people who usually would have been non-banking; and many of them saw through the People's Bank the only way of bettering their economic position. When the habit of banking spread among people hitherto unreached by banks, following the expansion of branches of the People's Bank then as a result the monetization of economic activities also in turn increased, and more and more resources

were marshalled for bolstering the development efforts of the island.

The People's Bank in spreading out its services extended itself into all the districts, and importantly over the remoter districts. In the process, branches of the People's Bank were established in the townlets in the centre of widespread rural divisions that earlier had not benefited from any banking facilities. Areas under Municipal, Urban, Town and Village Councils were served by the People's Bank and thus as much as urban centres the rural outback too gained, to an extent even more than the urban sector from the dispersion of banking facilities. As a rule, rural banking is not so commercially alluring and yet the People's Bank broke fresh ground by risking advent into the rural sphere.

The People's Bank made it its policy to take to the people all over, the bank's services by creating branches wide-spread throughout the island. For example the total of 158 branches in 1975 was steeply increased to 293 by 1985. Although these branches were mostly in the remote rural areas, the People's Bank continued to maintain its grip on the urban areas too.

Easily it surpassed other banks in providing banking outlets and services to Sri Lanka's public. Significantly, the People's Bank was able to mobilize a notable volume of deposits from the rural sector, town and village council areas; and in 1985 out of the entire amount of the deposits drawn into the Bank, a little over thirty three per cent of it came from the rural areas; the Bank was remarkably successful in involving the rural group of the people in the banking enterprise.

The People's Bank contributed to the furtherance of rural banking also, through the role it played vis-a-vis the Co-operative Rural Bank. The Co-operative Rural Bank acted as a banking agent of the People's Bank, and accepted savings and fixed deposits, and financially covered activities in village and small town areas, such as agricultural production, animal husbandry, cottage industry, debt redemption, electrification, consumption and supply of credit during times of hardship. By providing financial aid to Co-operative societies, regarding this as one of its principal obligations, the People's Bank supplanted more efficiently and skilfully the Co-operative Federal Bank. In fact, the People's Bank stretched itself to the extent of utilising the funds generated from

other sectors such as the government, corporations, and the private clients for financing Co-operatives. But in the last few years, the Bank's involvement in the financing of the Co-operative sector decreased while in turn its engagement in providing credit to the private sector increased—the Bank was transforming itself more and more into a truly commercial organisation and keeping itself attuned to the wants of a changing economic scene.

Naturally, the People's Bank shifted its attention toward financing the trade and distribution sectors; enterprises that were cordinal to the improvement of the country's economy. Originally, the development of the Co-operative movement, the provision of agricultural credit, the promotion of rural banking and engagement in normal commercial banking activities were the prescribed objectives of the People's Bank. But, actually over the years, the People's Bank got converted more and more into "yet another commercial bank on the conventional pattern."

The People's Bank, soon after it was created, recognised that the collection of deposits from the rural and Co-operative sectors was too restricted and largely restrained the extent of credit that could be distributed to these sectors. In fact, the Bank had to take to commercial business for raising funds for financing the Co-operative sector. Moreover, there were problems of recovery from the Co-operative sector and then the sector itself lost its significance as either an economic or popular unit. Additionally, the Bank encountered difficulties in recovering loans given out for agricultural purposes. In such a context the Bank had to avert itself from facing liquidity problems which threatened its own commercial viability, and the inevitable slide towards becoming yet another losing enterprise.

At this juncture, in the post 1977 period, liberalised economic policies were vigorously pursued by the government, and as a result noteworthy structural changes in the economy occurred. The agriculture sector itself became more market oriented; there was greater activity in manufacturing; a growth in the service sector, and the wholesale and retail trade picked up thereby substantially enhancing the island's economic activity since 1977. Simultaneously, foreign exchange transactions grew steeply following

the adoption of a liberal policy governing trade and payments. The People's Bank could not escape the effect of such basic changes and more of its resources had to be used in those sectors which could meet the wants of a changing economic environment. Innovative attitudes toward development and banking had to be taken by the People's Bank if it were to play a meaningful role in the rapidly altering economic landscape.

The People's Bank can justly claim to have been a pioneer in several respects. In attempting to relieve rural people from the weight of indebtedness, and since those unfortunate people often could not provide proof of their incomes or supply normal securities against bank loans, the Bank introduced a unique loan scheme based on pawning. A number of pawning centres were established and pawning advances multiplied quickly in volume. Apart from the recognition that the People's Bank was fair and secure most borrowers falling into this scheme were attracted to it since the interest rates charged by the Bank were lesser than those of the private pawn brokers. The initiation of this scheme also drew away the poorer borrowers from depending on more burdensome and demanding sources of credit for meeting their urgent financial needs. It is singular and creditable that among the commercial banks, the People's Bank alone continued to function as the sole institution that provided this facility; and this was no doubt a popularly availed of service.

If in more recent times the People's Bank had grown to be more commercial in character and comparable to other similar commercial banks there were imperatives that accounted for this inescapable transformation. Since 1977, a relaxation of the eligibility criteria compelled the Bank to grant loans liberally. At the same time the Bank was forced to make the borrower become conscious that loans are not donations and that the repayment of advances is a contractual obligation. It was necessary to tighten up so as to usher in the right atmosphere for expanding the banking habit which also implies as a concomitant the fostering of a faith in and adherence to formal lending and borrowing procedures and practices.

The People's Bank, in addition, has functioned as a source of furnishing finance for industrial development especially after

about 1960. A lack of foreign capital inflow owing to certain conditions then affecting the island led to a shutting out of a wide range of imports and then there arose the needed market stimulus that accounted for the growth of domestic industrial enterprise bent on manufacturing the goods which were restricted from being imported. Moreover, at this period, there was a commitment to replace the inherited colonial export economy structure with the encouragement of enhanced industrial activity, and the creation of a greater diversification of the economy. However, domestic private capital in Sri Lanka was not in a position to undertake the range of industrial activity it had to, in spite of the provision of incentives. State capital buttressed with aid from some of the socialist states had to be deployed so as to expand industrial activity in the country. But even though the People's Bank did not consider industrial financing to be one of its initial specific aims yet it had to venture into this sphere and respond to the challenges that the country's changed policy then posed. The People's Bank could not but answer the call as any commercial bank had to in meeting changing credit requirements of the economy affected by the island's industrial development venture. After all, the People's Bank was in practice and in a wider sense yet another commercial bank meeting the credit needs, whatever they be, that arose according to the circumstances prevalent in the country.

While several conditions from prerequisites for engendering industrial development, industrial credit or finance is a vitally necessary element. It is industrial credit that, stimulates and fosters industrial development, and generally the banks provide such finance thereby playing a development role. The People's Bank as a state-owned institution was even more obliged to be supportive of state policy and had to provide finance for affording an impetus to and for promoting industrial growth. Consequently, the industrial credit lent by the People's Bank which was as low as 3.6 percent in 1960 gradually increased to 26.9 percent by 1970, and thereafter in the early eighties ranged from 22 to 25 percent.

The People's Bank had already been lured to fund trade and other more profitable areas that come within the ambit of commercial bank practices. It had to make its own gains and be viable, and naturally had turned its attention in

giving advances early enough to developed areas of activity that call for credit and also assure return of it with interest. Now the People's Bank rose to meet the needs of economic diversification and industrialization because it had to be responsive as a state sponsored Bank to the calls arising from the new turn in state policy.

The People's Bank became the lending bank of a number of state enterprises that sprang up and engaged themselves in manufacturing; and the People's Bank inevitably catered more to the rising new business ventures of which quite a few were devoted to manufacturing. At an early stage of the new focus on industrialisation, the People's Bank paid somewhat more emphasis on industrial lending than other commercial banks and at times provided a much needed impetus to new industrial enterprises. During the years from the sixties to 1970, the demand for advances for industrialising grew, and in response the People's Bank increased its quantum of loans for buttressing industry.

The People's Bank's growth since its creation till the seventies was particularly noteworthy as it came to provide about half of the total commercial bank advances. It demonstrated a greater propensity towards industrial financing too. The new industrial entrepreneurship discovered in this institution easier avenues of bank services and credit for building up industry. But from around 1980 the People's Bank's supply of credit for industrial ventures declined probably because of the competition posed by foreign banks as suppliers of credit and because of the fall in demand for advances from public industrial corporations which were yielding place to the private sector following the new character imported to the economy in the post 1977 era. Interestingly, nevertheless, the average industrial loan given by the People's Bank was large, and much of the loans had aided industries more so in the urban settings.

The People's Bank indubitably did contribute through its enterprise to better the rural economy and to help the disadvantaged and poorer clients but from the start it yielded to the temptations that

beset any bank. It furnished credit assistance for the urban big timer, the larger industry, and the ambitious businessmen. Nevertheless, the Bank supported the small and rural industrialists simultaneously, especially in the area of small industry in venturing into project oriented lending in collaboration with the Industrial Development Board in the early seventies, which of course entailed big risks. Then another venture in which the People's Bank engaged itself was the Small and Medium Scale Industry Scheme but here again the bias of the Bank in lending was tilted more in favour of the medium scale enterprise. Additionally, through Rural Banks too, the People's Bank assisted but to a smaller extent by advances the setting up of rural industry.

Definitely and evidently, in the early stages, the People's Bank did lend support to industrial development within the island. As a new financial institution it played a significant part in meeting new credit needs such as in providing financial aid for nascent industry although to a rather limited extent. It never functioned as a development bank at the cost of shedding its character as a commercial bank which it had assumed *ad initio*, whatever its primary aims be.

The People's Bank was not rigidly restricted by the prescription that it should employ funds and aid to develop the co-operative movement, rural banking, and furnish credit for traditional agriculture. Like other commercial banks, the People's Bank while not losing sight of objectives accredited to it, yet had got lured into the more profitable, less risky other banking activities. We surprise then, that the Bank should take on a fair portion of banking activity connected with foreign trade. By 1986 the Bank could legitimately participate in the profitable task of financing foreign trade which entailed *inter alia* the attractive business of dealing in foreign exchange. Indeed from the inception of the Bank, profitable fields of banking were not lost sight of notwithstanding the constraints laid by founding objectives because of the foreign branch that was established for strengthening the Bank's opportunity to generate income. The People's Bank however could undertake fairly such

business since it had been empowered "to engage in the kinds of business similar to the business of the Bank of Ceylon".

During the early years, till the mid sixties, the foreign branch of the People's Bank groped its way seeking for business and more importantly acceptance by the international banking community. It gained initially the significant import business and the lesser notable export business of the Co-operative Wholesale Establishment. Then it cottoned on to the import business of the Petroleum Corporation, and thereafter followed an acquisition of foreign business from other state corporations and from a number of private business ventures and individuals. Imports of government departments too came to be done *via* the foreign branch of the People's Bank. With the onset of industrialisation in the post 1960 era, the foreign branch of the Bank provided banking services, advice and guidance in regard to technical, financial and managerial matters to many of the new industrialists. The Bank certainly had expanded its services.

In the latter half of the sixties there was a change in economic policy. Rigid import control was loosened by the liberalisation of the issue of Open General Licences, and exchange control was relaxed by the introduction of a dual exchange rate *via* the Foreign Exchange Entitlement Certificate Scheme. Consequently, new entrepreneurs embarked on undertaking the import trade, and they were aided by the People's Bank's foreign branch to venture into the import business. A noteworthy record in this respect is that the People's Bank aided small and medium level local businessmen to break into import business and international trade thus assisting the development of a new trend in Sri Lanka's foreign trade.

By 1970 a change in economic policy placed a huge responsibility on the public sector for economic enterprise; and state corporations largely played the role of engaging in industry and commerce. These corporations utilised the foreign branch of the People's Bank, and in turn the foreign business of the Bank flourished. The foreign branch assisted the corporations in strengthening their

capabilities, and building up their experience in the area of international trade and business. However, the years upto 1977 were rather lean years in international trade owing to the adverse foreign exchange position of Sri Lanka. In such a difficult context the People's Bank played a crucial and vital role through influencing the international banking community to lend their support for servicing foreign banking business which included some of the island's most indispensable imports.

Thereafter, the post 1977 years witnessed radical changes in the island's economic policy. The economy was deregulated, and the economy, in its operation, was left to be governed by market forces. Import and export controls were jettisoned, and Sri Lanka's economic liberalization earned the support of the international financial bodies, the International Monetary Fund and the World Bank, and of the international financial and banking communities. As a result of this sea change in the economic sphere several foreign banks cropped up on the local banking scene; foreign exchange was left to a free market; and exchange control governing trade and industry was almost lifted and even control on capital transfers was curtailed. These wholesale economic changes took the People's Bank by surprise, which now had to adjust to and acquaint itself with such changes. The newly christened International Division of the Bank proved adapt in quickly gearing itself to meet the new demands. Furthermore, the Bank acquired sophisticated knowledge and upto date expertise in banking skills, operations and marketing to compete with foreign banks. Once more, the People's Bank and its International Division proved to be quick on the uptake, and caught up with competitive business. Modernisation and honing of technology, skills and services made the People's Bank to retain its place as one of the leading commercial banking organisations in a sharply competitive banking atmosphere. Even though it changed substantially in this manner it still did not lose much of its bent towards the co-operative movement and the rural section.

The "open economy" and the competitive environment in business, trade and

banking of contemporary times contributed to the honing of the capability and capacity of the People's Bank. The Bank had to adopt modern techniques, automated operations, aggressive advertising and marketing; and in short radically innovate itself as a banking institution. It had to keep abreast of new changes and approaches in and attitudes to banking. The Bank had to plan businesslike better, and implement prudent and economical measures if it was to remain viable in the free market provoked competitive atmosphere of the contemporary times; and also it had to undertake these formidable tasks despite the constraints inevitable owing to the state's pervasive and vigilant influence on the Bank.

In a brief span of little over 30 years, the People's Bank had taken impressive strides and made its impact felt for the economic betterment of the island. It had provided greater assistance to the important rural sector, identifying viable projects, furnishing infrastructural support and imparting technical know how to this sector. Loans granted had been followed up so as to ensure prompt repayment, although not with even and remarkable success. Allocation of resources was made to the informal sector and the individual small scale borrower who had been ignored by other commercial banks. Credit was being given through an institutionalised set-up to the urban and rural poor often without scrupulous insistence on strong collateral, and a new entrepreneurship within the country was encouraged. The People's Bank demonstrated competence to engage in a type of agency banking funding agents.

It still is, in spite of such a record, able to project the image of a competitive commercial bank which has the capacity and capability to undertake competently off shore banking; to manage foreign currency banking units; and to supply foreign currency for financing imports and for investment. Furthermore, understanding merchant banking, engaging in financial consultancy, managing investment portfolios and preparing feasibility reports for entrepreneurs are now all grist to the banking mill of the People's Bank as, it has vigorously flourished as a commercial bank of the island's post independence era.