

## A SOURCE OF FINANCE FOR INDUSTRIAL DEVELOPMENT

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The structure of an underdeveloped export economy which Sri Lanka inherited at its political independence remained virtually intact for about a decade afterwards. A change in this structure required more than anything else, a sustained relative expansion, in general, of industrial activity, and in particular of manufacturing activity. There were periods in the past when the country experienced spurts of industrial growth but some sustained development in this respect can be considered to have started only around the turn of the 1950's decade. This was essentially due to import restrictions, introduced during this period and further tightened as time passed, and consequent opening up of market opportunities for import substitution industry. These developments which led to some sustained industrial progress since the early 1960's were partly attributable to adverse contemporary conditions affecting the external sector of the economy. These adverse conditions were reflected in deteriorating terms of trade and import capacity, the run down of previously accumulated external reserves during the free trade regime of the preceding decade and the generally worsening overall balance of payments position. These conditions in the context of no foreign capital inflow created the unavoidable need for gradual closing up of doors for a wide variety of imports which in turn provided the required market stimulus for domestic industrial activity to manufac-

ture restricted imports.

Developments around the turn of the 1950's in the country's industrial scene were also partly attributable to contemporary politico-ideological changes in the country. The regime which had come to power in the General Elections of 1956 and remained in power till 1965 (with the exception of a few months in 1960 when there was a minority government of the same party which was in power during 1948-56) was ideologically committed to changing the colonial export economy structure, to the promotion of greater industrial activity in the country and generally to greater diversification of the economy. It was partly this policy commitment to structural readjustment away from primary activity dominance, partly the socialist rhetoric of the new regime and its isolated nationalization exercises in certain economic activity areas, which made private and official foreign capital shy away from Sri Lanka during this period.

This conjuncture of the contemporary objective conditions affecting particularly the country's external economy and the politico-ideological conditions looking for some planned diversification of the economy away from the traditional primary product dominance was behind the spurt of manufacturing activity since the early 1960's. Domestic private capital at the time, however, was not ready to take up the wide range of

industrial activity it was expected to undertake by prevailing conditions, despite all the incentives which were present. The regime therefore also widely used capital, supported by aid from Socialist countries, in order to expand industrial activity.

Among various institutional additions to the system during this period within the public sector, the People's Bank established in 1961 can be seen as a major one within the country's banking and financial sector. Given the fact that its establishment and early growth coincided with the early industrial progress of the country as described above, one is tempted to raise the question as to what role this Bank played in promoting contemporary industrial development. This paper contributed to a volume being published on the occasion of the People's Bank's silver jubilee tries to examine one aspect of the above question, namely the role of the Bank during the period of its existence as a source of industrial finance. Even within this narrow focus, however, the paper does not go into micro details pertaining to individual industrial loans given by the Bank but restricts itself to an examination of the overall structure of the Bank's lending activity in relation to the structure of total commercial bank and "development bank" lending in the country.

Lest some of the research questions raised in the foregoing paragraph create wrong initial impressions and expectations, a few cautionary comments are called for here. As will be explained in detail subsequently, "industrial finance" in its broadest sense was not an objective of the

People's Bank. It has gone into this area of finance as a natural banking development and anyway, in spite of the general exclusion of industrial finance from its originally stated objectives and functions. Thus one ought to try to find the People's Bank's position among the institutions which promoted industrial development of Sri Lanka since about 1960 bearing in mind clearly that "industrial finance" was not one of the 'functions' it was established for. We should not try to see any special role for the People's Bank in this sphere. It has come to do what it has actually done in this respect simply as a normal commercial bank response to changing credit needs of the economy, which at this time were naturally being influenced more than during preceding times by the contemporary industrial development drive.

#### Background to Establishment and Objectives

It is now part of well-researched history that the development of banking institutions in Sri Lanka in the colonial period was dictated by the needs of the plantation economy and the related trade and commerce activities. In the words of the foremost monetary historian of this period" ... the entire monetary system of Ceylon was an adjunct to her export economy" (Gunasekera, 1962, p. 299). The banking structure which existed in 1934 was well summarised by the Pochkhanawala Commission (Imperial Government, 1934, p.26) as follows:

"Upon the existing banks in Colombo falls the main burden of supplying the credit wants of the country. Not only do they finance trade, which is

their principal business, but they also assist industry and agriculture. Being commercial banks, they prefer dealing in short-term credit."

Drawing attention to the major weakness of the existing banking structure in promoting national development the same Commission presented the following argument (p.9).

"It was considered essential for the attainment of this goal of economic freedom that the public should have adequate financial assistance, so as to enable indigenous capital and enterprise to participate more actively in the trade and industries of the country, and, in particular, to cultivate and expand the home market in preference to the export markets. The prevailing banking system primarily designed to foster economic development by requisitioning the aid of non-indigenous capital and enterprise proved to be ill-adapted, by the very nature of its structure, to offer such facilities."

It was in order to cater for the credit needs of domestic capital in the agricultural, industrial and trade fields that the Banking Commission of the early 1930's proposed the establishment of a State-aided national bank for Sri Lanka combining within it both "commercial bank" and "development bank" functions. The State-aided bank which was established in pursuance of these proposals in the name of the Bank of Ceylon, however, also turned out to be yet another purely commercial bank. By the early 1960's this Bank had existed over a period of about thirty years but the type of results expected by the Banking Commission of 1934 from the State-aided bank it proposed, could not be considered

to have been fully achieved by the actual operations of this Bank. The plantations and trade bias of commercial bank lending persisted and the rural agricultural and rural industrial activities remained generally outside the orbit of formal banking institutions. These latter activities were being catered to predominantly by informal sector money lenders with a set of rather ineffective co-operative credit societies also operating at the fringe.

At the apex of this structure of co-operative credit agencies was a Co-operative Federal Bank which, according to the then Governor of the Central Bank (as cited in Gunawardena, 1959, p. 421), did not appear "to be of much use to the co-operative movement or to the public". A draft bill to replace this Co-operative Federal Bank with a Co-operative Development Bank thus emerged by 1959 as a result of joint work at the Central Bank, the Ministry of Agriculture and other related agencies, according to which the new bank's activities would combine the "co-operative banking" function with more lucrative "commercial banking" functions. (ibid., p.430). In the words of the Minister who was responsible for this draft bill, "the new Co-operative Bank.. aims at sweeping away the semi-feudal credit system which still prevails in the villages..and thereby releasing the...peasant from the clutches of the village boutique-keeper and the professional money-lender" (ibid.,p.433).

Firm legislative action on this proposal was delayed till 1961. In the late fifties the proposed bill gave rise to an intense political debate and brought up certain intra-Cabinet conflicts, which existed already at the time to a climax leading ultimately to throwing the Minister responsible for the proposal out of the

Cabinet of Ministers. After two intervening General Elections, this proposal emerged again in the Parliament in 1961 and gave rise to the People's Bank (People's Bank Act No. 29 of 1961). The change of name from "Co-operative Development" to "People's" bank was intended to give the new bank "a democratic and socialist appeal" and to indicate that it "was being established not merely to furnish financial assistance to co-operative societies but also to provide the credit needs of those outside them" (Government of Sri Lanka, 1966, p.7).

The People's Bank Act stipulated the objectives of the bank which it set about establishing as "the development of the country's co-operative movement, rural banking and agricultural credit facilities. According to the rather controvertible section 4 of the Act, the bank was called upon to furnish financial and other assistance to co-operative societies, approved societies, cultivation committees and other persons. The actual behaviour of the bank in its formative stages has raised serious doubts as to whether the bank functioned and developed in line with spirit of the law so much so that even a Commission of inquiry was appointed in 1965 "...to determine the extent to which the Bank has carried out or failed to carry out the purposes for which it was established" (Government of Sri Lanka, 1966, p. 3). The Commission interpreted section 4 of the People's Bank Act rather narrowly so that even the problematic cover-all words "other persons" in that section were also taken "...to refer to such persons only as are engaged in a type of activity cognate, to that in which the other classes enumerated in the section are occupied" (ibid., p.3). Thus the Commission examined the activities of the bank upto 1965 as an institution "...intended to be no more and no less than an agency to provide

credit needs of the rural economy", whose primary objectives were viewed as those of "transforming the rural economy" and "promoting economic growth among the peasants" (ibid., p.6).

This interpretation of the objectives and functions of the People's Bank could be considered tenable if such interpretation is based only on section 4 of the Act which established it.<sup>1</sup> The Act itself did not restrict the Bank's activities to rural sector credit in its other provisions. As shown by the Commission itself: "above all, the new Bank was to be given the normal powers and functions of a commercial Bank..." (ibid., p.8). In the words of the Minister who originally developed the idea of a Co-operative Development Bank into a draft Bill:

"The critics of the Bill contend that the Bank should confine itself purely to the grant of small loans to co-operative societies for agricultural and marketing purposes. The adoption of this proposal would certainly ensure the quick liquidation of the new Bank. Small-scale loans to co-operatives are among the most risky forms of credit. The Co-operative Federal Bank failed because it confined itself to such loans and did not extend its activities to the more lucrative and profitable field of normal commercial banking. The experts of the Central Bank were well aware of this fact. That is why the Central Bank.....strongly urged that the new bank should be a 'mixed bank' which would undertake not only pure co-operative banking functions but also the more profitable functions of a commercial bank" (Gunawardena 1959, p.425).

Irrespective anyway of what the critics wanted the new bank to do, the top managers of the newly

formed People's Bank seem to have developed it on the broad lines enunciated by those who pioneered its establishment. What gradually emerged as a result was essentially a "commercial bank" with some priority placed on rural credit. Although it had been used, along with the Bank of Ceylon, as an instrument in the implementation of various agricultural and rural credit schemes of the state, in its actual development the People's Bank gradually became another commercial bank catering for whatever credit needs the environment produced.

The contemporary environment as shown earlier, was one where some industrial development was taking place on the stimulus provided by import and exchange restrictions. This industrial progress was taking place within both private and public sectors. Naturally the system produced a demand for long, medium and short-term industrial credit, which should have been met partly by "development banks" and partly by "commercial banks". Although there were a couple of institutions of the "development bank" type, their traditional preoccupation was naturally in agricultural (mainly plantation) investments and real estate. Thus even some of the "development bank" type functions had to be undertaken by commercial banks in respect of industrial finance. In the formative stages, the People's Bank seems to have undertaken such financing activities, sometimes even perhaps disregarding what were considered to be "sound" security-based lending practices of orthodox commercial banking. It probably got into difficulties at times as a result of such unorthodox lending practices, but the growth of the bank over time shows that on the whole and in net terms the combination of "commercial banking", development

1/ Even here whether the Commission's interpretation of "other persons" correctly interprets the expectations of those who founded the bank is subject to doubt.

"co-operative banking" and "rural banking" as incorporated in the law and practice of the People's Bank was quite an achievement.

Thus very narrowly defined, the People's Bank would have remained a co-operative bank catering to the rural sector needs, which would essentially have been agricultural. In this narrow definition of functions, the only industrial finance it could have carried out would have been restricted to the finance of small-scale rural industry, including cottage industries.<sup>2</sup> In actual practice however, its "commercial banking" function was given priority and within an environment of nascent industrial growth over a wider front, the bank seems to have emerged as a supplier of credit even to non-rural industrial ventures. This, however, does not at all mean, as will be shown later, that the People's Bank's major function in the past had been industrial finance. Being a commercial bank, its loan portfolios were to be determined by the pattern of changing economic environment, which could hardly be said to have become a predominantly industrial one.

### Commercial Banks and Industrial Finance

Industrial development of a primary-producing underdeveloped country (like Sri Lanka) would be the net result of the combined operation of a complex of factors and processes. Some of these causative factors and processes may be briefly mentioned here:

- the market conditions for locally produced or locally producible industrial goods;
- the level and the rate of development of industrial entre-

- preneurship;
- accumulation of industrial capital;
- endowment of natural and other resources;
- the level and the rate of technological development;
- the quality of infrastructural facilities and so on.

In any given combination of these factors and processes affecting industrialization, industrial credit or finance performs a dual role. Sometimes this role would be stimulative and promotive of industrial progress in a causative way. It is usually and often the so called "development banks" which are expected to perform this stimulative role of industrial finance. The role of industrial finance would, in other instances, be one of merely passively responding to changing credit needs emerging from industrial progress caused by a favourable combination of other causal factors. A purely commercial bank would in general, be performing this second type of role in respect of industrial finance, although a state-owned commercial bank might be guided by State policy to perform also the stimulative and promotive role of industrial finance at least in a marginal way.

The above a priori observations regarding the behaviour of commercial banks in general can be verified by examining the changing pattern of purpose-wise distribution of commercial bank advances in Sri Lanka over time. The relevant data for selected years after 1960 are presented in Table 1. Many analysts have referred to the fact that commercial banks in Sri Lanka during the colonial and early post-colonial periods had concentrated their lending activities within the plantation and trade sectors. The continuing

bias of commercial banks towards lending for commercial activities is made clear by the data in Table 1. There was, however, a lessening of this bias to some extent over the period after 1960. The plantation sector bias in commercial bank lending, however, does not come out from the data in this Table even for a relatively early year like 1960. This is really a complication arising out of the system of classification adopted in this breakdown of lending purposes. Most of the lending to plantation-related activities is classified into "commercial" and "industrial" advances. The low proportion of "agricultural" loans in 1960 and 1965 (and also prior to these years) therefore need not be taken as evidence disproving the widely-held view that commercial banks have, in the colonial and early post-colonial era, given preference to the plantation sector in their lending practices. The growing share of agricultural loans in the commercial bank lending activities over the post-1960 period, reflects the increasing bias in State policy towards non-export agriculture and the increasing use of commercial banks to implement numerous State-sponsored rural credit schemes.

The very low proportion of "industrial" loans in 1960 among commercial bank advances reflects the very little development of industrial activity even a decade after political independence. The gradual expansion in industrial activity after this year and the natural commercial bank response to the resulting growth of industrial credit needs produced a sharp increase in the share of industrial advances within the decade after 1960. What is classified as industrial advances in Table 1 was as low a proportion as 3.6 per cent in 1960 but this gradually increased to 26.9 per cent in 1970. Although at a lower level than that reached in 1970, this proportion remained at around

2/ As explicitly stated by the People's Bank Commission, the above narrow definition of functions meant that "the development of industry is not specifically mentioned as one of the main objectives of the People's Bank (ibid, p. 24).

3/ Processing of tea, rubber and coconut is traditionally classified in Sri Lanka as an industrial/manufacturing activity.

22-25 per cent over the subsequent period covered in Table 1.

among a number of other well-established commercial banks. In order to

Table 1  
Purpose-wise Distribution of Advances by Commercial Banks in  
Sri Lanka, Selected Years (Per Cent)

PURPOSE OF ADVANCE	1960 <sup>a/</sup>	1965	1970	1975	1980	1984
Commercial	68.7	58.4	41.7	47.1	51.2	49.7
Financial	18.1	11.9	8.9	4.1	2.6	2.3
Agricultural	1.9	4.5	13.1	14.1	13.2	9.7
Industrial	3.6	9.7	26.9	22.4	22.4	24.6
Tourism	—	—	—	—	—	2.0
Consumption	6.3	8.5	6.4	4.2	2.1	1.4
Housing	—	—	—	4.0	4.5	7.2
Other	1.5	7.0	2.9	4.1	4.0	3.1
Total:	100.0	100.0	100.0	100.0	100.0	100.0

<sup>a/</sup> As at end of September 1960. For other years, the data refer to conditions as at end of December.

Source: Central Bank.

This passivity in the behaviour of commercial bank accommodation to economic activities is quite natural and understandable as the primary objective of any commercial bank is profit making. As such it has to be focussing in its credit practices on relatively well developed areas of activity which are capable of generating a demand for credit backed up by assurances of repayment with interest.

### Role of the People's Bank

Whether the People's Bank conformed to the general behavioural pattern of a commercial bank in its lending practices or significantly deviated from that pattern is a useful question to raise here. On *a priori* reasoning one would find forces which must have compelled the People's Bank both to conform and to deviate.

It was a commercial bank created

survive and prosper, its lending practices had to be sound in the sense that it should have gone for a share of the most lucrative and profitable commercial banking business that was available. In spite of the fact that it was expected to be a commercial bank with a difference - a commercial bank established mainly to cater for the co-operative sector credit needs and to rejuvenate the rural sector - it was doomed to fail if it had completely ignored trade and other lucrative areas of commercial bank business. Thus there clearly were forces in operation on the new bank calling for conformity to make it also just another commercial bank.

There were also other forces contributing to an element of deviant behaviour on the part of this bank. It was totally State-owned, the only commercial bank of its kind at the time of its establishment. The contemporary State policy was pursuing

an aim of economic diversification in general and industrialization in particular. This general thrust of State policy, whether deliberately or otherwise, would have influenced the practices of a new financial agency established under State ownership and patronage. The State patronage of the People's Bank in its early stages can quite clearly be seen. The State sector agencies of both enterprise and non-enterprise type, which increased in their number during this period, were often deliberately promoted to do business with the People's Bank. Among such State enterprises of the time quite a large number had come up in the manufacturing sector and the People's Bank was naturally made their bank and the source of credit for them. In addition the well-established economic organisations in existence at the time of creation of the People's Bank were already committed to be in business with those commercial banks which already existed. The People's Bank could therefore have been expected or compelled to cater more to emerging types of new business activities, among which manufacturing formed a large proportion. All the above factors makes one argue, on *a priori* grounds, that the People's Bank would have been forced to somewhat deviate from the existing pattern of commercial bank lending.

The examination of the actual behaviour of the People's Bank in the past within the institutional credit scene in Sri Lanka clearly brings out the operation of the above conflicting forces on the Bank's progress over time. Given the theme of this paper, we do not propose to go into details of all lending activities of the People's Bank here. The focus will be solely on industrial lending. One sees a certain degree of deviant behaviour of the People's Bank vis-a-

vis other commercial banks but it is doubtful whether this was a very significant extent of deviation from the norm. It had given a little greater emphasis to industrial lending than the other commercial banks. It also occasionally stimulated new industrial ventures. Yet in fundamental respects it also acted just like another commercial bank going into credit areas which were thought to be remunerative and profitable under prevailing conditions. Particularly in more recent times, as the People's Bank has gradually become a well-established mature institution, conformity rather than deviation can be seen to have become the norm of its operation.

In the above background, there is not much point in raising the question as to what extent the People's Bank has stimulated (i.e. as a casual force) industrial progess in the country. The more valid question concerns the extent to which the People's Bank responded to changing credit needs within a system in which other dynamic developments were leading to an expansion in industrial activity.

The controversy which the People's Bank's operations had given rise to in the mid 1960's and the consequent appointment of even a commission of Inquiry on the subject may well be referred to here. All this is likely to make one wonder whether this Bank adopted a lending policy of fundamental divergence from normal commercial banking practice in respect of industrial credit. This controversy, however, seems to have emerged more as a result of a few clearly identified loans of questionable prudence rather than as a result of any significant overall policy deviation from normal commercial bank practice which was accepted to be sound. As indicated in Table 2, the proportion of industrial loans from the People's Bank

has not been significantly higher than the relevant proportion for all commercial bank loans. The former proportion was in general marginally higher than the latter but there were also years when it was lower. The years excluded from the Table in order to save space also do not adversely affect this general conclusion. With the passage of time the demand for credit for industrial purposes increased with growing industrial activity in the country and the commercial bank as whole expanded their role in industrial finance in a relative sense from 9.2 per cent in 1964 to 27 per cent in 1970. The People's Bank too had followed the same path and increased its proportion of loans for industry from 6 per cent in 1961 to 34 per cent in 1970. There has been a general decline in this ratio after the early 1970's in the case of all commercial banks, as well as the People's Bank.

Though perhaps not very significantly in a statistical sense there was, however, some measure of deviation too in this respect. The

forces listed above as leading to such a deviation were in fact powerful forces. The result of their operation was therefore to make the People's Bank deviant from while being conformist to accepted commercial bank practice. Hence the generally larger proportion of credit in the case of People's Bank compared to that of all commercial banks. The above pattern of behaviour can be seen from a alternative ways of analysing available data too.

Whether as a result of State patronage or the greater dynamism of its initial managerial leaders, the People's Bank grew rapidly since its inception, much more rapidly than the rest of the commercial banking sector - so that by the early 1970's it had come to be supplying about half of total commercial bank advances in the country. Within this overall credit scene, its share in commercial bank advances for industrial purposes usually exceeded its share in total such advances (Table 3). People's Bank was thus showing a greater bias towards industrial finance than was

**TABLE: 2**  
Proportion of Commercial Bank Advances for Industrial Purposes:  
All Commercial Banks and the People's Bank - Selected Years

	Per Cent	
	All Commercial Banks	People's Bank
1961	-	5.9
1964	9.2	8.0
1965	9.7	10.9
1967	12.2	14.4
1970	26.9	34.2
1972	27.3	31.4
1975	22.4	20.9
1977	23.4	27.5
1980	22.4	27.7
1982	24.4	28.7
1984	24.6	24.5

Note: - not available.

Sources: Government of Sri Lanka (1966) Central Bank and People's Bank.

4/ This was also, to a certain extent, a political matter. The People's Bank was established by a SLFP government in 1961 and had its initial development under that government. This controversy came to prominence and the consequent appointment of a Commission of Inquiry took place under a UNP government which came to power in 1965.

shown by other commercial banks in the country. It is probable that a greater proportion of the country's new industrial capitalist class found in the People's Bank, a source of bank services and bank credit, which was more willing to accommodate them than the well established traditional commercial banks which found the greater proportion of their clientele among entrepreneurs in plantation, trade and such traditional lines of business.

Table 3 also shows certain interesting time trends. Till about 1978-79, the People's Bank appears to have dominated the scene in respect of commercial bank credit to industry<sup>5</sup>, by accounting for half or more of the total such credit. After this period, however, its share in commercial bank advances for industrial purposes gradually declined. This was true of its share in total commercial bank advances as well and shows the impact of new competitive forces introduced in to the commercial bank arena by way essentially of the growing presence of foreign banks. In addition, it can be suspected that a growing proportion of industrial credit needs during the more recent period has come from foreign (industrial ) investors who probably have preferred to seek accommodation from foreign banks. Another factor behind these recent trends was perhaps the drying up of credit demand from public industrial corporations whose activities declined in a relative sense due to greater sector orientation in industrial policy since 1977. As can be seen from Table 4 the People's Bank was by far the largest and the most dominant commercial bank financier of public sector industrial corporations upto about 1980 and these corporations were responsible for about half of the demand for industrial credit from commercial

banks till 1979. Although the People's Bank remained the major supplier of credit to these industrial corporations supplying more than half of their credit needs till 1983, those corporations ceased by about 1979 to occupy the dominant position they used to occupy as sources of demand for industrial credit from commercial banks. This partly explains the drop in the People's Bank's share in commercial bank advances for industrial purposes since 1980 (Table 3).

ties. Even such a narrow definition of its functions however allowed some business for the bank in the industrial arena but this would have been in respect only of cottage industries and non-urban small industries. Without implying any judgemental opinion about its past behaviour, one must point out here that the Bank had quite obviously interpreted its role in a much wider sense than the above narrow interpretation in original functions implied.

**TABLE: 3**  
Total Commercial Bank Advance and those for Industrial Purposes with  
Comparable Data for People's Bank: Selected Years

	Proportion of People's Bank in All Com- mercial Bank Advances (%)	All Commercial Bank Advances To Industry Rs. Million	Peoples Bank Advances to Industry Rs. Million	Proportion of People's Bank in Advances to Industry (%)
1970	38	416	202	49
1972	54	483	299	62
1975	48	786	348	44
1978	45	2396	1546	64
1980	36	3838	1714	45
1982	34	6171	2478	40
1984	31	8605	2646	31

Sources: Central Bank and People's Bank

#### People's Bank and Small Scale Industry

In any rigorous interpretation of People's Bank objectives as laid down in the Act of Parliament which established it, its primary task was to promote rural sector economic activities. Large scale located in urban areas would have fallen outside its purview had the above interpretation of its objectives been rigorously adopted by its managers and, being a State-owned bank, also by its supervisory political authori-

In quantitative terms, the People's Bank's industrial advances amounted generally in more recent times to over a quarter of its total advances (Table 2). But in terms of the number of advances, those given to industry by the People's Bank remained consistently in the range of 1-3 per cent except in some exceptional years like 1978-80 when this ratio had just merely exceeded 5 per cent. What all this implies is that the average People's Bank industrial Loan was large. In its practice of industrial finance, the Bank had not

5/ The corresponding People's Bank proportion for 1979, not given in Table 3, was 56

at all favoured the cottage industry and small-scale industry. Available material also indicates that the bulk of its industrial loans had gone into industries located in the urban sector.

schemes intended to support the small and the rural industrialists. One of the earliest of this type was the one started in 1972 jointly with the Industrial Development Board (IDB) an experimental scheme in project-

of Ceylon and the Development Finance Corporation-also participated in this scheme in collaboration with the IDB. As at 31 March 1980, the People's Bank had granted 649 loans amounting to Rs.20.4 million guaranteed by the Central Bank under this scheme as against the 56 loans of Rs. 4.4 million given by the Bank of Ceylon. The former, itself being a commercial bank, seems to have more actively pursued a commitment to support small industry than other commercial banks, thereby also taking greater risks in the process. It may also be noted here that the average size of a People's Bank loan in this scheme was Rs. 35,452 while that of a Bank of Ceylon was more than double that figure at Rs.79,590.

The latest programme in the area of assisting small industry in the country is known as the Small and Medium Scale Industry (SMI) loan's scheme, which is going through its second phase now. Along with some other commercial banks and a development bank, the People's Bank has been involved in this scheme as a major implementing agency. In the first phase of the SMI scheme the People's Bank had granted 905 loans of Rs.117.1 million and under the second phase 282 loans of Rs. 123.3 million (i.e. upto the end of 1985). Although the scheme was expected to cover both "small" as well as "medium" scale industry, a large proportion of money lent appears to have gone into the later type, again underlining the difficulty a commercial bank, working in an underdeveloped background in a highly competitive area of finance, is faced with in carving out the assigned task of helping the "small". The average size of a loan under both phases of the SMI scheme was Rs.203,000.

Another method whereby the People's Bank attempted to carry out the functions assigned to it in rural upliftment and helping small industry was the establishment and expansion of the Rural Banks

**TABLE: 4**  
**Commercial Bank Advances for Industrial Purposes**  
**to Government Corporations and others with Relevant People's Bank Shares**

	All Commercial Bank Advances to Industry - Rs. Million		Peoples Bank Share in	
	Government Corporations (% of total within brackets. i.e. 1/1 + 2)	Other	Credit to Government Corporation	Credit to others
	(1)	(2)	(3)	(4)
1975	365 (46.4)	422	67.9	23.8
1976	567 (50.5)	557	70.5	27.1
1977	734 (52.9)	653	69.1	42.1
1978	1130 (47.2)	1266	73.6	56.4
1979	1471 (47.7)	1612	69.8	43.6
1980	1044 (27.2)	2793	73.4	47.6
1981	1478 (32.0)	3146	51.9	42.2
1982	1636 (26.5)	4536	53.9	35.2
1983	2045 (25.4)	5988	58.8	32.1
1984	1959 (22.8)	6646	33.2	30.0

Sources: Central Bank and People's Bank.

This again indicates the kind of conflict referred to earlier as was present throughout the existence of this Bank. It was no doubt set up to promote the rural economy but was required to survive as a commercial bank in competition with other well-established entities of the same kind. Even with the State patronage it received during most of its existence, its survival and growth as a commercial bank, catering solely to predominantly to the financially risky rural credit needs was, from its inception, quite a doubtful proposition. Thus it was quite obvious that whatever it did to improve the rural economy and to help the small man had to be combined with credit support for the urban, rich, big industry and the big trader.

In the industrial credit field, the People's Bank was no doubt involved from its early stages, in numerous

oriented lending as opposed to the traditional security-oriented commercial bank lending (Fernando, 1979, p.99). From 1973 to 1975 the amount of loans granted by the Bank under this scheme was restricted to a meagre Rs.2.5 million on 146 loans. Individual loans granted were subject to unrealistically low ceilings and therefore ineffective. Moreover as high a proportion of these loans as 46 per cent (in terms of the number of loans) were granted within the Colombo region. The scheme was modified by the Bank in 1976 jointly with the IDB, but with no appreciable change in general directions the scheme had taken so far. In 1978 a credit guarantee scheme for small industries was introduced whereby 75 per cent of credit granted by a lending bank was guaranteed by the Central Bank. In addition to the People's Bank, two other financial institutions- the Bank

Scheme from 1964. The number of these rural banks increased from 3 in 1964 to 403 in 1974 and 888 in 1984. Throughout their operation these rural banks have however earmarked only less than 5 per cent of their total advances for rural industry.

All the above schemes, operated sometimes single-handedly by the People's Bank and sometimes jointly with other financial institutions, clearly show that the Bank did not lose sight of or, to put it in different words, the supervisory political authorities did not allow it to lose sight of, its mission of the upliftment of the small man. Yet the underlying underdeveloped setup and the competitive environment created conflicts in objectives which were resolved perhaps by giving prominence to helping the large and the powerful while trying to do something to help also the poor and the vulnerable. In the industrial credit field in particular, statutory objectives would have made the People's Bank a financial agency catering to the credit needs of rural and small industry but reality made it, to a large extent, yet another commercial bank to look after the needs of the rich, large and predominantly urban industrialists. According to impressionistic evidence one sees that in comparison to their commercial banks on the scene, the People's Bank has retained some of its appeal as a "people's bank" but the compulsions generated by the environment seem to have made it sacrifice a large part of its original "people's bank" role.

### Concluding Comment

Whether so originally intended or not the People's Bank has in the past played a supportive role in Sri Lanka's industrial development, particularly in the early phases of that process. This can hardly be described as an initiating role as no commercial bank would be in a position to support the initiation of large numbers of new industrial and other projects.

Security, stability and growth considerations of any commercial bank require that it does the bulk of its business with established enterprises which would provide the necessary conditions of security, repayability and profitability to funds loaned out by the bank. This is why governments depend on the so-called "development banks" to provide the required long-term credit support for new and emerging enterprises. The People's Bank was established not as a "development bank" but as a "commercial bank" though, perhaps, with an element of development banking added to it.

The analysis of available data shows a greater involvement of the People's Bank in industrial finance than the other competing commercial banks which were in operation in the country. As shown already, this was because it responded more strongly to credit demands from emerging industry, which included a substantial number of public corporations. What it has achieved in this respect was not a "development bank" function per se but a normal commercial bank function of responding to newly emerging credit needs. Being a relatively new commercial bank, it did this perhaps with greater vigour, sometimes disregarding accepted norms of security of loan funds.

Although easy bank credit is absolutely vital to promote a vigorous process of industrial develop-

ment, a commercial bank can perform only a part of this vital role, the other part requiring a well developed "development banking" sector. In the field of promoting small scale industry hoping that it would provide the training ground for industrial entrepreneurs and a source of saving for further industrial accumulation commercial banks have been extensively used in the past by various regimes in power in Sri Lanka. The results so far achieved perhaps raise doubts as to whether these were the most suitable agencies to provide the credit needs of small-scale industry. Commercial banks, whether they are in the public sector or in the private sector have to be aiming at profits and the small industry sector (or any other small enterprise sector) is hardly the most attractive sector of financial entities guided by such aims and objectives. Even if they get involved in such activities to be in line with overall State policy or because of refinancing and other facilities provided by the Central Bank, commercial banks can devote only a small share of their advances portfolios to such small enterprise financing. It would thus be more effective to assign the development task of promoting new enterprises to "development banks" while assigning the usual of suitably responding to changing credit needs of the economy to "commercial banks".

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