REVIEWS

Studies in Indian Financial System. V. A. Avadhani. Bombay, Jaico, 1978. 375p. Rs. 70.00

While the word 'studies' at the start of the title may lead the reader to anticipate in-depth analytical treatment of various aspects of the institutional structure of finance in India, Dr. Avadhani himself acknowledges in the Preface that the book is intended only to provide an 'integrated picture' and a 'factual account' of the Indian Financial System. The sixteen chapters of the book do cover a very wide spectrum of topics like merchant banking and agricultural finance, corporate finance and the new issue market, flow of funds in the capital market and financial institutions and so on. The space devoted to various chapters is fairly uniform. In many cases latest available statistics have been incorporated to highlight gaps and achievements. It is thus a good 'updating' book for any student of the subject.

The first chapter on 'Financial System and Real System' has a laudable purpose. However, the reader at times could be wondering about the import of certain observations. For instance, "In traditional theory, finance was supposed to take the form of either circulating capital or fixed capital, and the concept of finance as distinct from capital was not well conceived and well-developed. In modern theory, finance is different from capital. While the former relates to money and near-money assets......capital relates to the physical plant and capital goods such as machinery etc. which are capable of further production" (p.2). If this were held to be true, then what is to be the fate of 'cost of capital' and 'capital structure' — the core of financial management theory ? A statement like "The growth objective of the financial system is to achieve the structure and rate of growth of various financial assets and liabilities in consonance with the optimal characteristics of real capital stock" (p.6) does not convey any clear message to the reader.

However, it agrees with this reviewer's view that supply-leading and demand-following phenomena are more realistic in less developed economies for generating industrial growth (p.10). This seems to give the lie to the argument often raised by banks about low absorptive capacity in backward regions to explain the extremely low credit-deposit ratios in those pockets. Pump-priming is what is necessary in the first place.

The chapter on 'Reserve Bank and Financial System' is purely descriptive. Not even the history of the bank rate changes is provided here, although this appears much later in chapter 11. In the chapter on 'Money Market' the twin institutional weaknesses of poor integration and insignificant specialisation have been highlighted (pp.34-35). The author later attributes to the factor of seasonality of demand for and supply of bank funds the effort of banks to keep excess reserves. This leads to the development of an inter-bank money market, loosening somewhat the grip of the RBI (p.37). It would have been useful to know at the end of this chapter the proportion of the money market controlled by the unorganised sector in the non-rural areas.

The next chapter is entitled 'Capital Market — Demand for Fund'. But it deals for good measure with 'supply of funds' too. The author rightly stresses the fact that in the Indian capital market the demand for funds from the public sector far outstrips the demand from the private sector (p.53). Some of the terms in this chapter deserved definitional clarity for many readers e.g., treasury bills, unfunded debt etc.

While writing on 'Private Corporate Demand' the author remarks that preference shares redeemable after 12 years are considered as debt capital (p.92). This is not correct. Preference shares redeemable within 12 years are treated as debt capital by the Controller of Capital Issues, and those after 12 years as equity. According to the author, more debt capital for gearing effect is in order after the take-off stage of growth is reached (p.93). While this may be true of existing enterprises, the recent examples of new enterprises indicate a very high debt — equity (via loans and not debentures) ratio right from the start. The author may have usefully touched on this issue. On p.103 the author argues that lower rates of capital gains tax (compared to tax on dividend income) is an inducement for more retained earnings because this will entitle the company to a lower tax rate. This inference appears to indicate a confusion. The question of tax advantage for capital gains vis-a-vis dividend income is relevant for shareholders, and not for the company. On p.95 the author observes that high D/E ratio is undesirable because it might encourage concentration of income and wealth, but on p.105 he argues that self-financing shall also increase concentration of economic power. Where is the way out then out of this impasse? Besides, the meaning of the expression 'cost benefit analysis of funds flowing into the company' is in need of explicit clarification (p.105).

On p.115 the author presents us with the regional distribution of assistance by all all-India financial institutions in 1976-77. The Eastern Zone secured the lowest share at 16.5% only. The author might have considered elaborating on this a little in the light of his quotation from Patrick on p.10.

The chapter on 'All-India Financial Institutions' is a fairly comprehensive descriptive account of various agencies. Once again the reader would have been benefitted by some analytical writing on aspects like the insertion of 'convertibility clauses', the working of the 'soft loan scheme' etc. This chapter could also have immensely profited by the inclusion of a discussion of inter-institutional coordination — especially from the viewpoint of the aid-seeking organisations who are brought under consortium arrangements. Only a passing reference is made to this issue on p.198.

It is towards the end of the chapter on 'Other Financial Institutions' that the author presents us with some of his evaluative comments. For example, he argues that banks still provide the major part of investment finance to the corporate sector, despite the existence of many special financial institutions, and that this is not right for banks may not use the right appraisal techniques (p. 199). (By investment finance the author probably means long term finance for capital expenditure). His argument needs to be substantiated by data. There is substance in this point that financial institutions should do more of equity financing. It is also a meritorious point that at times interest rates charged might have been negative in real terms during periods of high inflation. That the unorganised, small entrepreneurial sector has not benefitted much by such institutional innovations is also a tenable criticism.

In the 'Interest Rates' chapter there seems to be an inadvertent imprecise statement that interest rates are influenced by fiscal policy (p. 221). The chapter on 'Corporate Finance Studies' is based very largely on periodic RBI surveys on the subject. It presents an organised picture of corporate sector financial performance. However, the author's observation that "the pattern of deployment of funds influences the capital efficiency", followed by "capital efficiency can be measured by the ratio of net fixed assets or current assets to total net assets" (pp. 255–256), seems to convey little meaning to the reader. The chapter on 'New Issue Market' is one of the best written chapters of the book. With respect to the future of Stock Exchanges in India, the reader would have liked to know the author's views about launching public sector company shares into the new issue market, as well as for getting them quoted on the stock exchanges on a widespread and consistent footing.

Dr. Avadhani's book is thus a useful compendium of the current features and highlights of the financial system of India. Lack of enough analysis should not come in its way of being considered a good first-entry work on the subject.

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Rural Development and Social Change.
J. M. Heredero. New Delhi, Manohar, 1977.

There are many people working for rural development and their approaches differ widely. The true meaning of rural development is helping the people to attain at least a minimal economic standard which would enable them to have the necessities of life. The aim of most of the studies on rural development is research-oriented, while the main aim of this work is education-oriented. The present approach to rural development is based on the understanding of rural society. It is also based on the understanding of education. It is not the formal education imported in the schools and colleges, which covers a very small fraction of man's reality. Education should enable a person to deal more effectively with others, with his work, and also with himself (his needs, his feelings, his motives, his past history). Thus, education means training the intelligence of the participants to deal effectively with these problems (p.7). Therefore, the approach to rural development here is to inculcate the non-formal education in to the rural people.

The objective of this project was twofold : (i) to help villages in their development and (ii) to study the effect on them of both material help and psychological education. The meaning of psychological education is to foster self-reliance and to highten their achievement motivation. The aim of this education is the whole man : his feelings, needs, motives, his intelligence and, if necessary his spiritual powers. The ultimate purpose is to increase the participants' awareness and to prepare them to be more effective in dealing with other members of the community, and with their own work. Since