Abstract

The politics of bank nationalization, 1969-76

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Indira Gandhi announced the nationalization of fourteen banks in 1969. Even though this decision was subsequently challenged in the Supreme Court, which declared the order void, the judicial order was circumvented subsequently by an ordinance, which overcame the disabilities mentioned by recasting the original order. Though bank nationalization was established through parliamentary legislation only later, for all practical purposes, the fourteen banks began functioning as nationalized entities in 1969 itself, alongside the State Bank of India and its subsidiaries, in the public sector.

What this paper seeks to do is to examine, first, the politics surrounding Indira Gandhi's sudden decision to nationalize the banks (alongside the far less momentous decision to abolish privy purses for the erstwhile royals of British India) and, second, examine what in effect bank nationalization achieved in comparison with the stated objectives of policy and, not least, the politics surrounding the performance of the nationalized banks.

Nationalization of banks as a political issue had been part of the agenda of the Congress party from earlier times. The demand from the 'radical socialist' sections of the Congress party had been gathering momentum through the 1960s and had acquired a critical mass since the death of Jawaharlal Nehru or more specifically the ascension of Indira Gandhi to the prime ministerial chair after the death of Lal Bahadur Shastri, not least because of the perception within and outside the party that under the latter's stewardship the Congress government had started drifting from its 'Nehruvian socialist' moorings in a rightward direction.

Some hope had been pinned on Mrs Gandhi that a course correction would follow. But in her early years as prime minister, Mrs Gandhi seemed clearly unable to grapple with the considerable problems of managing the economy, far less point the way to a decisive return to the Nehruvian groove: that the post-Nehruvian rightward drift was well on its way to becoming the new orthodoxy seemed to be abundantly signalled by the prime minister's decision to devalue the rupee almost on the heels of a 'successful' tour of the United States in conjunction with the decision to suspend the planning process, which led in the immediate term to the by now notorious three-year 'plan holiday' of 1966-69.

The Congress party's disastrous electoral performance in the general elections of 1967 (when it lost power in a number of states and found its majority in the Lok Sabha shaved to the thinnest of margins) renewed calls for a return to the Nehruvian, socialist policy frame, especially because of the electoral losses suffered

by the old guard (the infamous Syndicate) widely, if not entirely fairly seen as the bastion of ‘reaction’ as opposed to Mrs Gandhi’s youthful commitment to change. By 1969, the cleavage between her and the old guard had sharpened to what seemed an unsustainable depth and was concretely symbolized by the policy and political gulf between her and Morarji Desai, the deputy prime minister and finance minister foisted on the prime minister by her Syndicate mentors, who opposed socialist measures by and large and the nationalization of banks in particular. In an uneasy compromise, in 1968, Mrs Gandhi, egged on towards nationalization by radical sections of the party and a group of equally radical advisors, settled for the utterly vague compromise that came to be known as social control of banks.

Though Mrs Gandhi had promised to give ‘social control’ a two-year trial, the rapidly escalating tensions between her and the old guard forced her hand in a year and bank nationalization was announced as a measure that would take the economy in a new socialist direction. Desai was unceremoniously dumped as a signal, more than anything else, to Mrs Gandh’s antagonists in the party, principally the old guard, spearheaded by the Syndicate. As is well known, events proceeded apace thereafter leading to the split in the Congress in 1969, ostensibly over the presidential elections.

Bank nationalization, in effect promised a redistribution of credit away from large and medium industrial and business houses to what came to be known as the priority sector: small-scale industry, small traders and entrepreneurs and, supposedly most crucially, agriculture. It was promised early on that this would be effected primarily through two instruments: the expansion of branches to previously unbanked or underbanked rural, semi-urban, backward areas, which would speed up both the mobilization of hitherto unbanked savings in the form of deposits and the dispensation of credit to sections of people who previously had had no or severely restricted access to credit; and, further, that credit would be provided to priority sectors (or borrowers) at differential (meaning lower than commercial) rates of interest.

Before proceeding to a brief statement of the actual operation of nationalized banking, a brief note on its political significance is necessary. Without question those who had advised Mrs Gandhi to speedily announce the move, had reckoned brilliantly in political terms. And, again in political terms, Mrs Gandhi had shown immense sagacity in acting decisively on this advice. Close to half a century on, it seems somewhat incredible that a move that sounds so arcane in the context of mass politics even in today’s world, would have proved a winner in the calculus of mass politics of the time. But all evidence suggests that it provided the post-split Congress (R, for requisition), immense electoral and popular traction not just in the immediate aftermath of its announcement, when crowds spontaneously thronged the prime minister’s residence in support, but even over a year later when Mrs Gandhi decided to call early parliamentary elections in 1971 and won a resounding victory, though by then the ‘garibi hatao’ slogan had acquired more significance. The available evidence also suggests that even in 1972, when elections were held in a number of states, though overtaken by the Bangladesh war and the promise of the eradication of poverty, bank nationalization remained in public memory.

But a close examination of bank nationalization in action shows that it failed to, or perhaps was never meant to, fulfil its stated populist, radical promise of contributing to either the eradication of poverty or, more realistically, scaling down inequalities of income, wealth and entitlements, especially in rural India. Though an impressive expansion of branches ensued, as statistics show, nationalized branches performed on par if not worse in comparison with private (excluding foreign) banks in this respect. In a couple of years, too, as the pace of expansion slowed down, new branches came increasingly to be located in urban and metropolitan areas. A similar point can be made about the mobilization of deposits if one compares the banks that were nationalized with the ones that were not.

But most crucially, nationalized banks failed to energize the 'priority sectors' by providing easy and accessible credit for a number of reasons, which will be comprehensively dealt with in the paper. At this point, it is important to note that medium and big industry and business continued to dominate the credit profile of nationalized banks and lending to priority sectors never took off on any significant scale, and, even when it did, say in the agricultural sector, the beneficiaries were, overwhelmingly, rich peasants who produced at least in part for the market. This was no surprise, since the operation of the nationalized banks in their formative years coincided with the apogee of the years of the new agricultural strategy. On the whole, however, bank credit, which expanded massively in the first half of the 1970s, helped rich peasants, big traders and big industrial houses to hoard, stockpile and build inventories of critical commodities (including foodgrains) at a time of acute economic crisis marked by continuously rising prices and scarcities. For the present, I will forbear from belabouring obvious, or not so obvious, points about the class character of the state.

I will end with one crucial point. Though failing in its immediate and stated objectives, bank nationalization certainly did one thing: it provided the central government, especially, with a massive access to resources, without which, in the extreme crises of the early 1970s, it would have been hard put to survive financially. The burgeoning indebtedness of the government to the banking sector (the Reserve Bank of India, the State Bank of India group and the nationalized banks) and the steadily spiking graph of budgetary deficits and deficit financing bears testimony to this fact.

That, this contributed to the worsening economic crisis, including soaring inflation, while bailing out the government is a point I shall dwell on at greater length in the course of the paper.