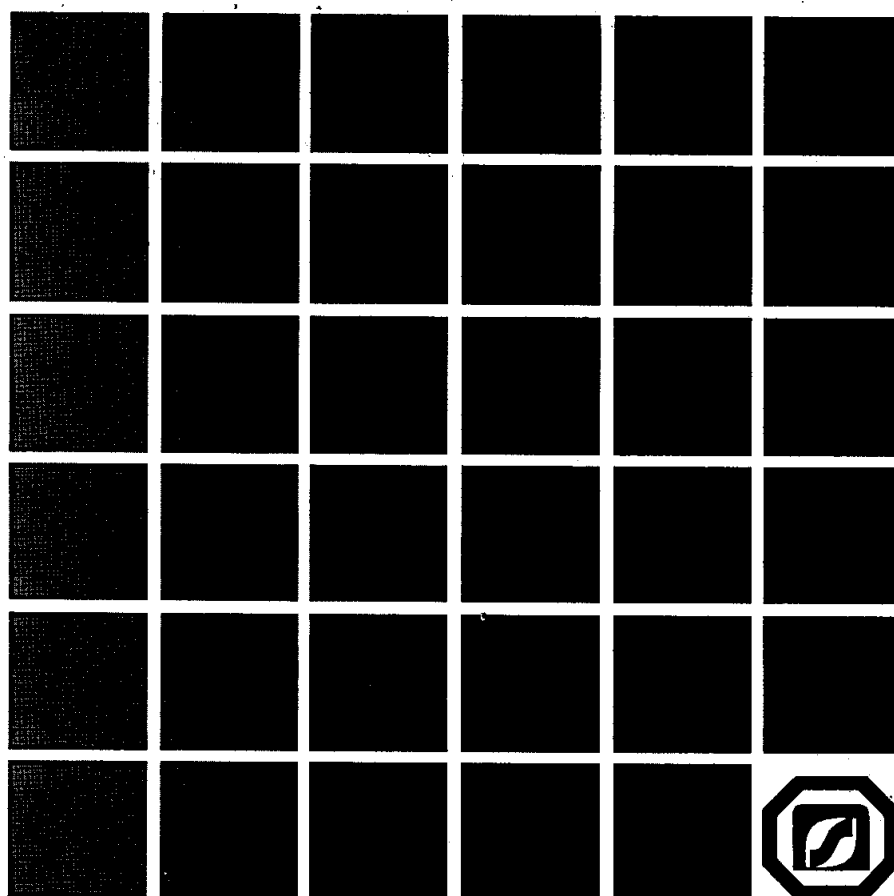


THE FINANCIAL STRUCTURE AND ITS IMPLICATIONS FOR MONETARY POLICY IN THE SEACEN COUNTRIES



**THE SOUTH-EAST ASIAN CENTRAL BANKS (SEACEN)
RESEARCH AND TRAINING CENTRE**

**The South-East Asian Central Banks (SEACEN)
Research and Training Centre**

**THE FINANCIAL STRUCTURE AND ITS IMPLICATIONS
FOR MONETARY POLICY IN THE SEACEN COUNTRIES**

**Kuala Lumpur, Malaysia
November 1986**

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FOREWORD

The philosophy behind the research activities of the SEACEN Research and Training Centre can be described into three aspects. First, the SEACEN Centre has a comparative advantage since it is a regional institution with easy access to data from eight countries and it can devote full-time on research work. Second, it complements the research activities of member central banks and monetary authorities, especially on long-term and exploratory projects which they may find difficult to undertake as their work is directed more to issues that affect day-to-day operations. Third, the research activities of the SEACEN Centre serve as one of the vehicles in training the staff of the member central banks and monetary authorities, particularly those who are seconded to the Centre or those who are involved in its research projects.

This study on "The Financial Structure and Its Implications for Monetary Policy in the SEACEN Countries" is an example of a research undertaking of the SEACEN Centre which adheres with the above general tenets. The study relates the development of the financial structures of the eight SEACEN countries to their conduct of monetary policy. It can be considered as an exploratory research work as existing studies deal mainly on the relationship between financial development and economic growth. Likewise, other previous studies provided only a factual compilation of financial institutions in the region. This collaborative study, therefore, may be of value to the South-east Asian central banks and monetary authorities since it views financial institutions and financial instruments as vital elements in the formulation and implementation of monetary policy. Moreover, the section on financial instruments in the SEACEN countries could add to the scant literature on financial assets in the region.

The researchers involved in the study did not only gain a better understanding of their own country's financial structure and monetary policy but also learned from the experience of the other countries. The workshop held for the researchers at the SEACEN Centre on August 12 to 16, 1985 gave them an opportunity to present their findings and the ensuing exchange of ideas have contributed immensely to the improvement of the final versions of the country studies.

The following staff of the research/economics departments of the South-East Asian central banks and monetary authorities authored or took a major hand in writing the country studies:

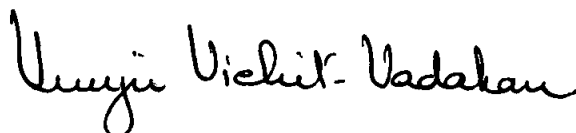
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The overview for the SEACEN region was prepared by Mr. Gerardo S. Tison of the SEACEN Centre. He also coordinated this collaborative research project, edited the country papers and supervised the printing of the final version of the study.

The views in the country papers and regional overview should be considered solely as those of the writers. They do not necessarily reflect the views of the member central banks and monetary authorities nor that of the SEACEN Centre.

Miss Seow Yun Yee, Mrs. Wong Yoke Mei and Miss Sally Ho also provided assistance at various stages of the research project. The contributions made by Mrs. Yeap Gaik Swee, Mr. Bernard Then and Mr. Hassan Sampol in the printing of the study are also highly appreciated.

The support and cooperation given by the member central banks and monetary authorities, especially their research and economics departments, also made possible the completion of another collaborative project of the SEACEN Centre.



Vinyu Vichit-Vadakan

Director

SEACEN Research and Training Centre

Kuala Lumpur
November 1986

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THE FINANCIAL STRUCTURE AND ITS IMPLICATIONS FOR MONETARY POLICY IN THE SEACEN COUNTRIES

by
Gerardo S. Tison

I. INTRODUCTION

Previous studies made on the financial structure are commonly viewed in relation to economic development. This is reflected in the pioneering works on the relationship between financial development and economic growth by Gurley, Goldsmith, Shaw, and McKinnon. This study, on the other hand, may be considered as one which confines itself within the financial sector since it is concerned with the implications on monetary policy of the financial structures of the eight countries represented in the South-East Asian Central Banks (SEACEN) grouping. In short, it does not deal with the relationship between the financial and real sectors of these countries. The study discusses the financial institutions and financial instruments of these countries, provides some indicators of the extent of development of their financial structures and relates them to monetary policy, especially on its scope and the instruments that can be appropriately and effectively used at a certain stage of financial development.

Despite its narrowed scope, this collaborative undertaking of the SEACEN Research and Training Centre and the South-East Asian central banks and monetary authorities still made use of the theoretical and empirical studies of the experts already mentioned. In particular, the degree of development of the financial structure was measured by using the ratios and other indicators devised by them.

2 REGIONAL OVERVIEW

Components of the Financial Structure

The financial structure of any country is made up of financial institutions and financial instruments. Just like in the real sector, the institutions represent the financial sector's industries and markets and they include, among others, commercial banks, finance companies, insurance corporations and money and capital markets. These industries and markets, in turn, produce and sell a range of financial products and services as illustrated by money, deposits, equities, guarantees, loan syndication and underwriting. Likewise, there is a regulatory body which oversees the operation of these institutions to ensure that they operate within accepted norms and standards as well as contribute to the attainment of larger social and economic goals.

The institutions in a financial structure are characterised mainly by their assets which are almost exclusively of financial instruments, primarily, claims against non-financial borrowers while their sources of funds are predominantly in the form of liabilities.^{1/} Hence, financial institutions in this study are classified according to the nature and characteristics of their main assets and liabilities, a classification which could be easily related to monetary policy. However, classifying institutions in the SEACEN countries just like in other countries is not an easy task. Some financial institutions across countries are called differently despite similarities in their functions. On other instances, some financial institutions have the same names although they are into different activities. Moreover, a closer look at the assets and liabilities of financial institutions shows that they are engaged in different financial and allied activities, reflecting the blurring of functional distinction among the various types of financial institutions.

^{1/} Goldsmith, Raymond W. Financial Institutions. (New York: Random House, Inc.), pp. 10-11.

Financial instruments are evidences of transfer of funds between the surplus and deficit units. Their values, either taken as a whole or broken down into components according to common features, when related to other economic aggregates could serve as indicators of the size and importance of the financial structure in an economy. In this study, financial instruments were classified in various ways. One broad classification of financial instruments is to group them into claims and equities. These two types of financial instruments, also collectively referred to as primary securities, are issued by deficit units or ultimate borrowers to generate funds. The difference between them lies in the fact that a firm which issues equities is not under obligation to "buy" them back; it is not borrowing the money for a specified period but acquiring it for permanent use. On the other hand, a claim is a primary security which is being "sold" but subject to a repurchase clause, that is, the money borrowed has to be repaid. Examples of claims issued upon themselves by non-financial units are loans, mortgages and bonds.

Financial institutions which are not ultimate borrowers can also issue claims upon themselves. These claims, otherwise referred to as indirect securities, are issued by financial institutions in return for the savings placed with them by surplus units or ultimate lenders. The particular form that the indirect security takes will depend on the nature of the financial intermediary concerned. Banks, for example, issue deposits while insurance companies provide insurance policies in return for the regular payment of premium of their clients. Thus, an examination of the claims of financial institutions against non-financial units and the claims of non-financial units against the financial sector provides, among others, an indication of the degree of indirect financing and the accumulation of financial assets, respectively, in the economy.

Financial Structure and the Conduct of Monetary Policy

Since the financial instruments and financial institutions serve as the channels of central banks and monetary authorities in conducting monetary policy, it is to be expected that the degree of development of these components of the financial structure will have a bearing on the conduct of monetary policy. As gauged by some ratios and other quantitative indicators, the financial structures of the eight SEACEN countries can be placed at different levels of development. In turn, the existing institutional framework and structure of financial assets will influence the conduct of monetary policy. For instance, with the number and type of financial institutions and financial assets that predominate in a country, what are the monetary policy instruments that can be used by the central banks in pursuing their stabilisation and growth objectives?

On the other hand, the kind of monetary policy pursued by the central bank also has a substantial influence on the financial institutions and instruments of a country. In the SEACEN countries, the types of financial instruments that exist in a country, their yields, maturity structure and currency denominations have been significantly influenced by the monetary policy pursued by the authorities. For instance, the predominance of short or long-term financial instruments may be traced to the interest rate policy of the central bank, the success of the monetary authorities in maintaining domestic price stability and the foreign exchange policy adopted in the country. However, such impact of monetary policy on the financial structure is not part of the scope of this study.

Division of the Study

This study on the financial structure and its implications for monetary policy is divided into two parts. The first part, oftentimes referred to as the regional overview, presents a general picture of the financial structures of the eight countries in the

SEACEN grouping, touching mainly on the extent of their development and their implications for monetary policy. The second part contains the individual treatment of the topic by country, and therefore, presents a more detailed coverage of the situation prevailing in Burma, Indonesia, Malaysia, Nepal, the Philippines, Singapore, Sri Lanka and Thailand.

The regional overview

The first part of this volume is meant to provide an overall view of the financial structures of the eight SEACEN countries rather than present a strictly comparative study. The individual countries are in various stages of financial development and therefore, one country's financial structure is inevitably different from the other. Despite the expected diversity, the regional study aims, firstly, to present the similarities in the various aspects of the financial structures of the eight countries so as to form some patterns that could be linked with monetary policy formulation and implementation. Secondly, the significant differences and uniqueness of the financial structures of these countries were also discussed in so far as these enhance or hamper monetary policy action of the authorities. Furthermore, some issues touching on financial instruments and financial institutions, whether taken individually or as a group, were also raised or highlighted. These issues were related to some targets, objectives or expectations which are usually set when new instruments or institutions are introduced into the financial structure of a country. It is hoped that a focussed view of the similarities, differences, uniqueness and some issues in the financial structures of a group of countries which are in various stages of development could be instructive in further developing their financial institutions and instruments and thereby make them more effective conduits of monetary policy.

6 REGIONAL OVERVIEW

The overview of the financial structures of the SEACEN countries and their implications for monetary policy is presented along the following lines:

1) The types of financial structures in the SEACEN countries are presented in Section II. The types of financial structures discussed here revolved around the ownership of financial institutions which might be expected to be different in a centrally-planned economy or a private enterprise/capitalistic economy. This section, however, showed that even in the other seven countries which have mixed and private enterprise economies, ownership and management control of financial institutions by the state or government is very prominent. Another discussion of the types of financial structures which was based on their degrees of development is subsumed in Section V.

2) Section III is devoted to financial institutions, specifically the various types of institutions in the region. The discussion of this section starts with some historical dates in order to show the emergence of the pioneer financial institutions and then trace their growth (or deterioration) along the financial development path. Moreover, after the descriptive discussion of every type of financial institutions, some issues are raised which have bearings on the development of the financial markets, on the objectives of monetary policy as well as on the supervisory role of the central bank over financial institutions in order to safeguard the stability and soundness of the financial structure. A striking finding in this section is the continued dominance of commercial banks in the financial structures of the SEACEN countries.

3) The discussion on the instruments in the financial structures of the SEACEN countries is contained in the fourth section. It was shown in this section that deposits and loans accounted for the bulk of the financial instruments, be it in the more advanced or just developing financial structures. On the other hand, bonds,

equities and other securities formed a small portion of the total financial assets in the eight countries.

4) The fifth section presents some general indicators of financial development and these include the financial interrelations ratio and the financial intermediation ratio. The ratios obtained for the SEACEN countries were associated with the types of financial structures identified by Goldsmith.

5) Section VI of the regional overview centres on the monetary policy implications of the financial structures of the SEACEN countries. The dominance of commercial banks which are located in the urban areas and the limited range of financial instruments have made the monetary authorities in the region to rely more on direct rather than indirect instruments of monetary policy. There is no doubt that the financial structures of the individual countries have advanced significantly after a decade or two but such degree of development is not yet sufficient to make the use of general and quantitative instruments of credit control effective. A significant portion of the economies of some of the SEACEN countries are still not part of the monetised sector and the elements of perfect competition conducive to the effective implementation of quantitative monetary policy instruments are still lacking. This then leads the authorities to resort to more direct instruments of monetary policy such as selective credit measures which operate under conditions not dictated by market forces.

6) The conclusion part of the study reiterates that since it is obvious that the institutional aspect of financial structure development has been dealt with by the authorities, the agenda at hand now is to develop the staples or products which these financial institutions have to trade or deal with. It was also concluded that the development of financial instruments cannot be legislated as what was done in the establishment of some government financial

institutions in the SEACEN countries. For the non-financial sectors to keep their assets in financial form, the importance of maintaining a positive reward on their savings by keeping a check on inflation cannot be overemphasised. This will, in turn, ensure a continuous flow of funds which financial institutions can intermediate with and make available in the form and volume demanded by deficit-financing units. Equally important as well in the intermediation process is the role of the central bank in ensuring the stability and soundness of financial institutions. In short, the study concluded that the tasks of controlling inflation and maintaining a stable financial system also fall under the scope of responsibilities of the central bank which are not incompatible with its other objective of developing the financial structure.

The country studies

A more detailed discussion of the financial structures of the eight SEACEN countries is covered in the country studies. The writing of the individual country papers was guided by an outline prepared by the SEACEN Research and Training Centre. The outline was not meant to be strictly followed but it could be seen that a fairly uniform treatment of the various areas of the study was made, particularly on the definition of terms, classification of financial institutions and instruments and indicators of financial structure development. The country studies start with an overview of the financial structure, followed by sectional and more detailed discussion and analysis of the financial institutions, financial instruments, policies and measures which affected the financial structure and the tools available to central banks and monetary authorities in pursuing monetary policy.

One important section of the country papers deals with the various quantitative indicators of the degree of development of their respective financial structures. In tracing the development of the financial structure, aggregated data on financial instruments and

institutions were related to other financial and real sector variables such as national product and population.

A separate section is also devoted to examining the existing financial structure of the country and how it has enhanced or hampered the formulation and implementation of monetary policy. The concluding part of the country studies does not only give a summary of the findings but also include some discussion on the areas for further development of financial instruments, institutions and markets in order to enhance their contribution towards more effective central banking operations.

Limitations of the Study

In addition to the difficulty encountered in classifying financial institutions, other limitations of the study can be cited. While the terms, definitions and concepts used in the country papers are basically uniform and consistent, this could not be said on the period covered. In the writing of the country papers, the individual researchers were given the discretion to choose the period to be covered depending on the issues to be analysed and, in most cases, as dictated by data availability.

Data on financial instruments were the most difficult to obtain. Since some of the data are crucial in establishing the degree of development of the financial structure, most of the country researchers have to come up with their own estimations, devise proxies and combine a set of data with another which is based on a different concept. Hence, some of the data on financial instruments and the results of the indicators of financial development do not give an accurate picture of the degree of sophistication of the country's financial structure. Moreover, certain types of financial institutions and instruments were not included as the researchers have no basis in coming up with their own estimates.

On the whole, these limitations were reflected in the individual country chapters as unbalanced treatment of the three major sections of the study, namely, financial institutions, financial instruments and implications on monetary policy. A lengthier discussion of financial institutions can be observed compared to the other two topics. To a certain extent, this reflects the degree of development attained by the financial structures of the SEACEN countries. The initial phases of financial structure development in the individual SEACEN countries were mainly devoted to institutional building or setting up the infrastructures of financial intermediation, a strategy which leans towards the supply-leading phenomenon in financial development. Thus, at this stage of the individual countries' financial development, there already exists substantial literature on financial institutions while much less is devoted to financial instruments which are still confined to three or four financial assets. A much more scanty discussion on the implications of the financial structure on monetary policy is apparent in the country papers. This can be explained by the fact that so far no studies have yet been made on the relationship of the financial structure and monetary policy. Hence, this study represents an initial attempt to delve into the topic, with the individual researchers preparing the groundwork for more in-depth treatment of the implications of financial structure on monetary policy.

Since the individual country papers are the bases of the regional study, the cited limitations are also reflected in the latter. Nevertheless, despite the data constraint and other limitations, some findings and conclusions can still be drawn from the regional overview and the country chapters that may be found useful by others who would like to delve deeper into the relationship of financial structure and transmission of monetary policy.

II. TYPES OF FINANCIAL STRUCTURES IN THE SEACEN COUNTRIES

The discussion of the types of financial structures can be approached in a number of ways. In this study, the discussion of the topic is viewed in two ways. The first, which is contained in this section, relates the type of financial structure to the manner in which the economy operates, that is, whether it is centrally-operated or is left to the hands of the private enterprises. The other approach can be viewed along the degree of development of the financial structure, specifically the classification of financial structure based on the mix of financial institutions and financial assets existing in a country. This second classification is discussed in Section V of this study.

The type of financial structure that emerges in a country is highly related to the type of its economy. ^{2/} The countries in the SEACEN region may be categorised under private enterprise and mixed economies on the one side and centrally planned economies on the other. Under the first category belongs the countries of Indonesia, Malaysia, Nepal, the Philippines, Singapore, Sri Lanka and Thailand. Burma has a centrally planned economy.

The difference in the financial structures of these two types of economies does not lie primarily in the types of financial instruments and financial institutions that are in existence. Both private enterprise and centrally planned economies have similar forms of financial instruments-- currency, demand, savings and fixed deposits, accounts receivable and payable, consumer instalment credit, insurance reserves, short- and long-term loans to business enterprises and government securities. They also have similar types of financial institutions -- central banks, commercial banks, savings banks, development banks, life insurance companies and the like. What

^{2/} Ibid., pp. 30-37.

distinguishes the financial structure of a centrally planned economy like Burma to that of a private enterprise and mixed economy of the other SEACEN countries is the absence of corporate stocks among its financial instruments and the absence of investment banks, investment companies and trust organisations among its financial institutions.

In general, the financial structure of centrally planned economies differ with that of private enterprise and mixed economies in terms of:

"First, the control of financial institutions, all of them being owned and operated by the government in centrally planned economies;

Second, the predominance of claims against the government or government-owned enterprises among financial assets;

Third, the generally smaller size of the financial superstructure in centrally planned economies, which is reflected in the lower value of the financial interrelations ratio at comparable levels of economic development; and

Fourth and most important, a basic difference in function - the fact that the financial system in centrally planned economies serves primarily as an adjunct to the authoritative direction of the real flows of labor and goods instead of acting as an independent factor in the allocation of resources." 3/

The fourth differentiating factor was also mentioned in the introductory part of the country study for Burma which stated that "The budget is the most important instrument for payment flows and the most important component of overall financing. The budget encompasses

3/ Ibid., p. 32.

other financial plans, such as the foreign exchange plan, cash plan and credit plan." Moreover, in pursuance of policies designed to transform the economic structure of Burma into a socialist economy, key sectors including the banking system have been brought under state control since 1962. All private commercial banks, whether foreign-owned or owned by Burmese nationals, were nationalised in February 1963. In short, the banking system of Burma has been amalgamated into a one-bank system with the objectives of effectively mobilising financial resources and to enable the government to exercise effective control over the operations of the financial institutions.

Government-ownership of financial institutions

Although the other seven countries operate under the private enterprise and mixed economic system, the strong presence of the government in terms of ownership of their financial institutions does not clearly set them apart from the centrally planned economic system of Burma. Government ownership of financial institutions including the central bank, range from virtually 100 per cent in Nepal to government equity share in two financial institutions in Singapore.

The equity participation of the government in all of the financial institutions operating in Nepal as of 1983 indicates the leading role it has taken in developing its financial structure. The commercial banks in Nepal represented 45 per cent of the financial systems's assets, the Nepal Rastra Bank contributed 36 per cent and the rest, by other types of financial institutions. Indonesia has the same experience as Nepal since the government has initiated and funded the establishment of almost all types of institutions in the banking sector. In 1984, 75 per cent of the assets of the financial institutions are owned by the government of which Bank Indonesia accounted for 40 per cent and the five state banks, 33 per cent.

In the Philippines, government ownership of financial institutions used to be limited to the development-oriented types.

However, with the conversion into equity of past due loans of private commercial banks owed to government financial institutions, the public sector has acquired a majority controlling interest in six of the 31 commercial banks operating in the country as of June 1984. Thus, the public sector in the Philippines owned about 61 per cent of the total assets of the financial system of which 26 per cent came from the central bank and 15 per cent from the commercial banks.

Insurance and development and savings banking in Sri Lanka are in the hands of the government since the only two insurance companies, the sole credit insurance institution, the only three development banks and the sole savings bank are owned by the government. In addition, the two leading commercial banks in the country are owned by the government. The government's ownership of financial institutions in Thailand is reflected in the four specialised institutions catering to the needs of the agricultural and industrial sectors, housing and small industries. The Thai government also owns the Government Savings Bank and has 95 per cent ownership in a commercial bank, as well as minority shares in other domestic commercial banks.

The Malaysian Government's share in the assets of its financial system was about 34 per cent in 1984 and is reflected mainly in its central bank, the two largest commercial banks, the National Savings Bank and other development-type financial institutions. In Singapore, the government's ownership in financial institutions is seen in the Development Bank of Singapore and the Export Credit Insurance of Singapore.

It can be seen that for the SEACEN countries with private enterprise economic systems, ownership of financial institutions by the government is in pursuance of the institutional-building, economic and social development roles it is expected to perform. Hence, government-owned financial institutions are mainly involved in agricultural and rural development, small and cottage industries,

housing, credit guarantees and employees' welfare. Consequently, the operations of most of these financial institutions are not dictated by normal market forces which, in turn, affect their viability. Moreover, considering the size of government-owned financial institutions in a number of SEACEN countries, it is not uncommon that budgetary appropriations for them constitute a substantial amount and could even be the major cause of the overall budget deficit. This situation seems ironic since they are expected to be mobilisers and sources of funds. Thus, in the case of the Philippines the operations of government financial institutions are being reviewed, if not the whole principle of the government owning and running financial institutions.

III. FINANCIAL INSTITUTIONS IN THE SEACEN COUNTRIES

As mentioned earlier, there is no fundamental difference among the types of financial institutions in centrally planned economies like Burma and in private enterprise and mixed economies like the other seven countries in the region. Thus, it can be said that the SEACEN region has almost all types of financial institutions that can be found in the industrialised countries. This, however, could not be said on an individual country basis. In general, the countries in the region with more advanced economies have a wider range of financial institutions that provide more specialised services than the less developed ones.

Basically, the financial system in the eight SEACEN countries is composed of the central bank or the monetary authority, the banks and the non-bank financial intermediaries. Based on the individual country papers, the following groupings of financial institutions in the SEACEN countries can be drawn:

- 1) Money (M1) generating institutions composed of the central bank and other entities which issue currency and the commercial banks which accept demand deposits;

- 2) Other deposit-type institutions, particularly those accepting quasi-money or savings and fixed deposits, certificates of deposits and other deposit equivalents, and they include savings banks, finance companies, rural banks, merchant banks and cooperatives and credit unions;
- 3) Contractual savings institutions such as insurance companies and provident and pension funds;
- 4) Development-type financial institutions whose assets are composed mainly of medium and long-term loans and investments in the agricultural and industrial sectors;
- 5) Investment-type institutions which collect surplus funds of small savers and invest them in stocks and bonds; and
- 6) Other types.

Money-Generating Institutions

The central bank which issues the country's currency and the commercial banks which are authorised to accept demand deposits constitute the monetary system of the SEACEN countries. In most classification of financial institutions, these two are grouped together due to their money-generating power, specifically narrow money (M1).

Central bank or the monetary authority

All of the eight SEACEN countries have a central bank or monetary authority which is granted not only the authority to formulate and implement monetary and foreign exchange policies but also supervisory and regulatory power over financial institutions. In

connection with their responsibility of controlling money supply, the central banks are also granted the sole authority of issuing currency, except in Singapore where such privilege is vested in its Currency Board.

The monetary authorities in the region were established fairly recently, reflective of the recent attainment of sovereignty of the individual countries. Other financial institutions, notably the commercial banks, existed long before the central banks. As the financial system became more complex, there arose a need for a monetary authority and overseer of financial institutions. The first country to establish its central bank is Thailand, in 1942. Burma followed with its Union of Burma Bank in 1948. The Central Bank of the Philippines first opened its doors in 1949 and a year later, the Central Bank of Sri Lanka started its operations. Three other central banks were formed in the 1950s: Bank Indonesia, in 1953; the Nepal Rastra Bank, in 1956; and Bank Negara Malaysia, in 1959. The Monetary Authority of Singapore was the youngest among its counterparts having been established only in 1971.

Just like in other countries, the South-East Asian central banks were initially one of the largest financial institutions in their respective financial systems. However, through the years their relative magnitude in terms of assets diminished while other types of financial institutions grew much faster, a trend which is viewed as a forward step along the path of financial structure development. In terms of share to total assets of all financial institutions, Bank Indonesia took the biggest share in the region, at 40 per cent in 1984. This was followed by Nepal Rastra Bank at 36 per cent (1983) while the central banks of Sri Lanka and the Philippines accounted for a little more than a quarter of the total assets of their financial systems. The Union of Burma Bank contributed about 22 per cent of the total assets of the financial system in 1983 while the Bank of Thailand's share was 18 per cent in 1984. Belonging to the low side are Bank Negara Malaysia and the Monetary Authority of Singapore

(including the Currency Board) whose shares were at 11 per cent and 13 per cent, respectively, in 1984.

Currency constitutes one of the major liabilities of the central bank and it accounts for a large share of total financial instruments during the early stages of development of the financial structure of a country. As the financial structure becomes more developed, financial instruments issued by other institutions emerge, particularly those which yield interest and other earnings. Even within the liability account of the central bank itself, currency has been tracing a diminishing share. For instance, currency as a percentage of the total liabilities of the Central Bank of the Philippines dropped from 62 per cent in 1970 to 13 per cent in 1984. Currency liabilities of the Central Bank of Sri Lanka also traced a declining share, from 66 per cent in 1960 to 29 per cent in 1984.

Commercial banks

The commercial banks dominate the financial structures of the SEACEN countries, be it in terms of assets, deposits mobilised and credit extended. During the years 1983-1984, they contributed no less than two-fifths of the total assets of the financial systems in the region (see Table 1). This went to as high as 64 per cent in Burma, followed by commercial banks in Thailand, 61 per cent and in Indonesia, 51 per cent. In Malaysia, Nepal and Sri Lanka, the commercial banks accounted for about 45 per cent of their financial systems' aggregate assets. On the low side of the range, but nonetheless a substantial share, are the commercial banks in the Philippines and Singapore which accounted for about 43 per cent of the total assets of their financial institutions.

Commercial banks also dominate the financial structures of the SEACEN countries in terms of head offices and number of branches and other outlets. As shown in Table 2, the number of commercial banks in most of the SEACEN countries have increased from the 1970s to

the 1980s, with the more significant increment registered in their branching network. On an individual country basis, Singapore has the most number of commercial banks, which with the exclusion of the offshore banks total 51 (full and restricted domestic banks) with 250 branches as of the end of 1984. This is followed by Malaysia with 38 head offices and 716 branches and the Philippines, with 34 head offices and 1,913 branches.

Due to their demand deposit liabilities, commercial banks are classified together with the central bank as money-generating institutions. Demand deposits of commercial banks in the SEACEN region accounted for as high as 38 per cent of their total deposit liabilities in Indonesia in 1984 to a low of 6 per cent in Thailand (see Table 3). In Sri Lanka, about a quarter of commercial banks' deposit liabilities was in demand deposits and it was about one-fifth in Nepal. Demand deposits of commercial banks in Burma, Malaysia and Singapore comprised about 17 per cent of their deposit liabilities while it was 12 per cent in the Philippines. These percentage shares of demand deposits to total deposit liabilities of commercial banks, however, reflected the changing deposit structure of commercial banks. Demand deposits have been declining in importance through time while the interest-earning deposits, savings and fixed deposits, have been tracing an increasing share. For instance, in 1980 demand deposits accounted for 52 per cent in Indonesia and 13 per cent in Thailand. On the other hand, by 1984 fixed deposits alone accounted for 72 per cent of Thai commercial banks' deposit liabilities, 64 per cent in Singapore and 55 per cent in Nepal.

The leading role of commercial banks in the region, just like in other countries, could be explained partly by the fact that they are one of the first institutions to emerge in the organised sector of the financial structure. In the SEACEN countries, their beginnings can be traced back to the colonial periods when banks of the colonising country established their branches or banks from their major trading partners extended their operations in these countries.

The oldest commercial banking system in the SEACEN region can be found in Indonesia when the Dutch-owned commercial bank, De Javasche Bank which is the predecessor of its central bank, was established in 1827. Evidence showed that the first commercial bank in Sri Lanka was founded in 1828. The first commercial bank in Singapore was of Indian ownership, established in 1840. In the Philippines, the first commercial bank was a branch of a Spanish commercial bank which was established in 1851 and is today one of the biggest in the country. Malaysia had its first commercial bank in 1859 when the Chartered Mercantile Bank of India, London and China set up a branch in Penang. The history of Burma's organised financial system also started with a branch of a foreign commercial bank, the Presidency Bank of Bengal which was established in 1861. Thailand also had a long commercial banking history as far back as 1888 and although it has never been colonised, the first bank was a branch of the Hongkong and Shanghai Bank. Nepal is another country which has not been subject to foreign powers and its first commercial bank was established by the government in 1936, making Nepal as having the "youngest" commercial banking system in the SEACEN region.

The significance of commercial banks as one of the oldest institutions in the organised financial sector of the SEACEN countries extends beyond its historical value. Their early establishment made them well-entrenched in the financial structures of the region. They were able to reap the benefits associated with the pioneer or the "first comer" in the financial service industry, with no competition from other organised intermediaries. In fact, the monopoly granted them in accepting demand deposits and dealing in international trade financing and foreign exchange is what principally distinguishes the commercial banks from the other financial institutions of the seven countries with private enterprise economies.

There are, however, some exceptions that could be cited in the SEACEN region regarding the exclusive privilege of commercial

banks to accept demand or chequing deposits. These are found in the financial structures of Nepal, the Philippines, Singapore, Thailand and to a lesser extent Burma. The Agricultural Development Bank of Nepal (ADB/N) as its name suggests is not a commercial bank but it is also allowed to accept demand deposits in order to enlarge its deposit base and thereby match its increasing lending operations. In the Philippines, a few rural banks were initially allowed to operate demand deposits in the absence of commercial bank branches in the rural areas. However, with the adoption of the universal banking concept in the 1980s, other types of banks could go into what used to be exclusively commercial banks' domain after meeting certain requirements. At present, only thrift banks, notably savings and private development banks, have joined commercial banks and some rural banks in accepting demand deposits.

In Singapore, a legislative amendment to the charter of the Post Office Savings Bank of Singapore in 1984 authorised it to accept chequing accounts. The Government Savings Bank in Thailand, in addition to functioning as a typical savings institution, has a Banking Department which undertakes normal banking operations including the acceptance of demand deposits. In the case of Burma, the state commercial bank is represented by the Myanma Economic Bank which accepts demand deposits while foreign exchange transactions are handled by the Myanma Foreign Trade Bank.

Their being one of the first and oldest types of financial institutions could also be cited as one reason why some quarters have associated commercial banks with complacency, conservative lending attitude and reliance on their traditional financing transactions, that is, trade and other short-term credit. This criticism gains more importance when viewed on the magnitude of financial and manpower resources that commercial banks have at their command and which could very well meet the needs of other sectors with high social returns. Thus in the assessment of the financial system of the SEACEN countries, local and foreign experts hold the view that commercial

banks have not penetrated the other sectors of the economy and they have lagged in their adaptation to changes in the country's economic structure. Likewise, the contribution of the large number of commercial banks in implementing monetary and economic policies in the SEACEN countries which have large rural sectors is somewhat lessened by the fact that their offices are located in the urban and other developed areas.

Consequently, the authorities in most of the countries in the region have focussed their attention on these issues. For example, in the Philippines and Sri Lanka, the government-owned commercial banks have branches in the rural areas to meet the credit needs of the agricultural sector and small industries. The central banks of Malaysia, Nepal, the Philippines and Thailand require commercial banks to devote a certain percentage of their outstanding loans or deposits to the financing of priority sectors which include agricultural food production, small scale enterprises and housing.

On the whole, the commercial banks, being the dominant institutions in the financial systems of all the SEACEN countries, have spearheaded the development of their respective financial structures. From the point of view of central banking, the prominence and sophistication of this sector is very crucial since they deal on demand deposits and foreign exchange, elements which are very basic in monetary policy formulation. However, there are some attitudes and orientation of commercial banks which when viewed beyond the profit yardstick somehow deflect on their eminent position in the financial system. A positive consequence of the reluctance of commercial banks to go into other areas of financing, as far as financial structure development is concerned, is the emergence of other types of financial institutions, which are discussed in the following sections.

Other Deposit-type Institutions

Deposit-type institutions other than the commercial banks constitute the second largest group of financial intermediaries in the SEACEN region. In this study, they are distinguished from commercial banks because they are not authorised to operate current or chequing accounts but they accept other deposits such as savings and time or fixed deposits, negotiable certificates of deposits and deposit equivalents. In short, this group of financial institutions are commonly bound by their savings mobilisation task. In terms of share to total assets of the financial system, the largest other deposit-type of institutions can be found in Malaysia and Thailand where they contributed 17 per cent, followed by Sri Lanka at 13 per cent. In Singapore, these institutions had an asset share of 10 per cent while they are relatively small in the Philippines and Indonesia with respective asset shares to total of 6 per cent and 4 per cent (see Table 1).

Savings institutions as depositories of surplus funds in the form of savings, fixed and certificates of deposits and deposit equivalents could emerge as important financial intermediaries when viewed from the monetary policy angle because the funds they gather represent the greater portion of the broader definition of money or M2. However, available data as given in Table 4 shows that the other deposit-institutions are still way behind commercial banks in gathering interest-earning deposits. Thus their significance at present lies more on the type of clientele they serve which are the household sector and other non-corporate, non-financial entities. The existence of more deposit-type financial institutions therefore is a contribution towards efforts to increase savings in the form of financial assets and in accelerating the monetisation of the economy.

The utilisation of the accumulated deposits and other sources of funds of other deposit-type institutions reflects a more varied picture for every institution in the grouping. Their lending

activities present a heterogeneous group of financial institutions engaged in medium and long-term loans, housing loans, hire-purchase of motor vehicles, consumer loans and investment in stocks and bonds. This diversity in portfolio could be traced to the fact that most of them were deliberately established to serve specific sectors and activities. Moreover, some of the financial institutions in this group emerged in response to unfulfilled demand for or inadequate financial services.

The other deposit-type of financial institutions in the SEACEN countries include the following:

- 1) savings banks found in Indonesia, Malaysia, Nepal, the Philippines, Singapore, Sri Lanka and Thailand;
- 2) finance companies in Indonesia, Malaysia, the Philippines, Singapore, Sri Lanka and Thailand;
- 3) rural banks in Indonesia, the Philippines and Sri Lanka;
- 4) merchant banks in Malaysia, the Philippines, Sri Lanka and Singapore; and
- 5) cooperative and credit unions in Malaysia, the Philippines and Thailand;

Savings banks

Savings banks in the SEACEN region were established to foster the saving habit among the populace and their main target is the household sector rather than the corporate or business sector. When they were first established in the region, which was as early as 1877 in Singapore and 1888 in Malaysia, they were of the "post office" type, located in almost every locality so as to provide a readily accessible depository for the savings of the people.

The only existing savings banks in Malaysia, Sri Lanka and Thailand are owned by their governments and they all started as post office savings banks. As postal savings banks, their operations were lethargic thus prompting the governments in these countries to absorb or amalgamate them into a single bank. In 1984, the share of the national savings banks of Sri Lanka, Thailand and Malaysia to the total assets of their financial systems were 9 per cent, 5 per cent and 1 per cent. Likewise, in Indonesia and the Philippines, the "post office savings bank" concept was also tried but their operations were later taken over by government-owned commercial banks for the same reason as that of the other countries which transformed their postal savings banks.

Thus as of 1984, only Singapore and Nepal still have post office savings banks in the SEACEN region. The characteristics of these banks in the two countries present a study in contrast. For instance, Singapore has the oldest postal savings bank in the region as it was established in 1877 while Nepal's post office savings scheme was introduced some 100 years later, in 1976. The Post Office Savings Bank in Singapore is now a giant in the country's financial scene, contributing about 5 per cent of the total assets of the financial system in 1984. 4/ It had nearly 2.7 million savings accounts with a value of more than S\$7 billion or a deposit balance of S\$ 2,592 per account. On the other hand, the postal savings scheme in Nepal was described as "yet to catch on and has so far made a slow progress" 5/, with total accounts of 8,550 valued at Rs. 2.5 million, or an average value of Rs. 292 per deposit. The post office savings scheme is largely on the deposit gathering side rather than lending as the bulk of its deposits is redeposited with commercial banks at the same interest rate.

4/ See country chapter on Singapore.

5/ See country chapter on Nepal.

The savings bank networks of Indonesia and the Philippines are composed of head offices and branches in different parts of the countries. These banks are either owned by the government or private sector and in both countries they account for about 2 per cent of their financial sectors' assets in 1984. The Philippines has another type of institution which can be placed under this grouping, the stock and non-stock savings and loan associations. They function very much like the savings banks and post office savings banks in terms of deposit-gathering and lending activities.

Some patterns can be drawn from the experience of countries which still have postal savings banks and from those countries which have transformed them into larger savings bank type.

First is the special privilege given to them. In Singapore and Thailand, as earlier mentioned, the Post Office Savings Bank and the Government Savings Banks were also granted authority to accept demand deposits, side by side with the commercial banks. In addition, in both countries their banks operate more than the typical or traditional post office savings banks. The Post Office Savings Bank of Singapore participates actively in the money market as a supplier of funds and have set up joint ventures with other financial institutions. The Government Savings Bank in Thailand also performs some commercial banking functions such as demand deposit acceptance and selling domestic traveller's cheques and undertakes a small life insurance business. Another privilege given is the tax-exemption (full or partial) of the interest income on deposits placed in these banks in Singapore and Sri Lanka.

The second common feature of savings banks in the region is that their lending activities are specified or subject to some limitations since most of these banks are operated by the government. In Singapore, Sri Lanka and Thailand, the bulk of savings banks' funds goes to the government and other public enterprises either in the form of direct loans or purchases of government securities.

Moreover, they are expressly not allowed or discouraged to extend credit to the private sector. If lending to the private sector is done at all, it usually goes to housing which is a priority lending area.

The transformation of the post office savings banks into bigger government savings institutions in Sri Lanka and Thailand has enabled them to go into more vigorous savings mobilisation activities. Singapore has the most successful experience with its Post Office Savings Bank and this bank ranks as one of the leading mobilisers of savings in the country. The Singapore government has taken several moves to revitalise this former lethargic thrift institution and made it into a giant in the financial scene, something which Thailand and Sri Lanka have also done to their respective banks, although to a lesser extent. The following improvements introduced by the authorities in Singapore, Thailand and Sri Lanka could be emulated by other countries in the region desiring to strengthen their savings banks:

- 1) launching a campaign to encourage savings, especially among school children;
- 2) expanding their scope of activities beyond the traditional post office savings line such as accepting demand deposits, trading in various financial instruments like Treasury bills and money market instruments, selling traveller's cheques, providing Giro payments services and deposit boxes and undertaking life insurance business;
- 3) introducing various innovative savings schemes and instruments such as group savings scheme, save-as-you-earn scheme, special long-term schemes, gift tokens and premium savings certificates with lottery feature;

- 4) increasing the rewards of saving in the form of deposit by offering competitive if not higher interest rates and exempting interest income thereof from taxation; and
- 5) enhancing the convenience feature of transacting with these banks by maintaining a wide network of branches throughout the country, computerising their operations and installing on-line banking terminals.

Finance companies

Finance companies can be found in six SEACEN countries, namely, in Indonesia, Malaysia, the Philippines, Singapore, Sri Lanka and Thailand. In these countries, their asset portfolio is identified with financing of consumer durables, particularly hire-purchase of motor vehicles, installment and cash credit, and short-term credit to manufacturers and merchants. On the liability side, these finance companies can be grouped into two. One group are those found in Malaysia, Singapore and Sri Lanka which raise funds by accepting regular deposits (savings and fixed deposits and certificates of deposit) in addition to issuing their own papers. The other group comprised the finance companies in Indonesia, the Philippines and Thailand whose fund gathering activity is limited to issuing promissory notes and other papers.

The size of finance companies in relation to the entire financial systems of the SEACEN countries can be seen in Table 1. In Thailand, finance companies as a group ranked second to commercial banks as they accounted for 11 per cent of the total assets of its financial system in 1984. In Malaysia, with finance companies contributing 10 per cent of the financial system's total assets, they emerged as the third biggest group, after the commercial banks and the provident and pension funds. In Singapore, they accounted for 5 per cent of its financial system's total assets; in Sri Lanka, 3 per cent; in Indonesia, 2 per cent and in the Philippines, 1.7 per cent.

The role of these institutions in deposit mobilisation and credit extension is reflective of their relative sizes in the SEACEN countries mentioned. Hence, finance companies in Malaysia and Thailand accounted for 16 per cent and 11 per cent, respectively, of their total deposits and deposit-equivalents, or second to commercial banks as deposit mobilisers. They also followed the commercial banks in terms of credit extended, specifically, in 1984 Malaysian finance companies provided 16 per cent of outstanding credit while those in Thailand extended 14 per cent.

One common feature of all the finance companies in the region was their dynamic role in funds mobilisation. To a large extent, this was aided by the higher interest rates they could offer as they were not subject to interest rate ceilings during the time when a number of the SEACEN countries had regulated or controlled interest rates. In fact, the finance companies in these countries were not initially subject to any government regulations as they were established much later than banks so that existing regulations then only apply to banking institutions. In Malaysia, the Philippines, Singapore and Thailand, a number of finance companies were set up by banks themselves as a means of getting away from the regulations imposed on banking institutions. However, as their numbers increased and their activities have expanded and deepened, their existence has become conspicuous and their governments have formally included them into the supervisory and regulatory fold of the central bank and other agencies. Likewise, the need to protect public interest also prompted authorities to regulate them as in the case of finance companies in Singapore and Thailand where they also ventured into risky and speculative activities, notably in the stock and property markets.

Although finance companies are now regulated by the authorities in the SEACEN countries, it can still be discerned that they are treated differently from banking institutions, a treatment which can be said to be less stringent. For instance, in Indonesia,

funds gathered by finance companies are not subject to legal reserve requirements. In Thailand where interest rates are still regulated, finance companies are given higher interest rate ceilings for their deposits. In Singapore, although finance companies are required to maintain the same minimum cash balances as banks (6 per cent of their liabilities base as from mid-1975), they have to observe only a one-tier liquid asset ratio which is 10 per cent as compared to the 20 per cent for commercial banks. Finance companies in Sri Lanka are not subject to credit restrictions unlike commercial banks which have to follow the annual National Credit Plan. Hence, their lending activities have increased considerably.

Rural banks

The main rationale for the establishment of rural banks in three of the eight countries of the SEACEN region is to bring services and facilities of the organised financial sector into the rural areas and countryside. Traditionally, the financial needs of the rural people are met by the informal and unorganised financial sector. However, funds made available by the unorganised financial sector to their customers are usually obtained at usurious rates, are not adequate and have unsuitable lending maturity periods. Moreover, the informal financial market does not provide a facility that could gather the savings of rural households. Hence, savings in the rural areas inevitably take the form of hidden cash, jewelry and other tangible assets which are unproductive, unsafe and even prone to spending. The introduction of rural banks which are single unit banks in a particular locality represents one step of the authorities in Indonesia, the Philippines and Sri Lanka to bring the services of the formal and organised financial market in these areas.

The first bank of such type in the SEACEN region was established in the Philippines in 1952. Under the government's programme to establish a rural bank in every town in the Philippines, the number of rural banks has increased from 18 in 1953 to 1,158 as of

end-June 1984. In Indonesia, rural banks are further classified according to the specific clientele they serve, namely, employees, village, paddy and petty traders banks. As of 1984, there is one employees bank; 3,581 village banks; 2,078 paddy banks; and 172 petty traders bank. The rural bank scheme in Sri Lanka was launched in 1964 when the People's Bank established branches in the rural areas. 6/ After 20 years, 888 branches are operating in the country.

The rural banks in the three countries are comparatively small, accounting for about 1.5 per cent of the total assets of the formal financial sector in the Philippines, 1 per cent in Sri Lanka and less than 1 per cent in Indonesia (see Table 1). They are the main depositories of the savings of the rural populace and hence their main liabilities are in the form of savings and fixed deposits. On the other hand, the bulk of their funds are lent out to agriculture and other rural activities. Another similarity of rural banks in the three countries is the assistance they get from a "parent" bank. In Indonesia, they are supervised by Bank Rakyat Indonesia and in Sri Lanka, by People's Bank. In the Philippines, the Central Bank provides substantial support to the rural banks in the form of special time deposits, preferential rediscounting and technical assistance like sending Central Bank credit extension workers to the areas served by rural banks and training rural bank personnel. Rural banks in Sri Lanka are not required to maintain reserve requirement.

From the foregoing, it is obvious that the rural banks are very much encouraged in the financial sectors of the three countries. institutions. This could be explained by the desire of the

6/ These rural banks which are branches of the People's Bank are different from the regional rural development banks which were established in early 1985. Since the period covered in the Sri Lankan country study ended in 1984, the latter banks were not included.

authorities to bring a large number of the populace who live in the rural areas within the fold of the monetised and organised financial sector. Moreover, these three countries are basically agricultural economies and it is expected that financial services are made available right in the areas where the farmers live, as part of their agricultural development programmes. The assistance provided to them, as others have observed, have made them overdependent on their "parent" banks hence they could not viably operate if left on their own. In the case of the Philippines, the rural banking system is one of the least stable in the financial sector. A number of rural banks have been closed due largely to mismanagement arising from the lack of experience of the stockholders who normally operate these banks. Suggestions have been made to let rural banks operate and compete freely in the open market so that only the viable rural banks would survive. A weak and unstable rural banking system which sees a number of unit banks being closed has a negative impact on the rural people since their establishment is the initial step in bringing the facilities of the organised financial sector to them. A loss of confidence in rural banks will be a serious setback in enlarging the reach of the organised financial sector which also means reduced impact of monetary policy.

Merchant banks

This type of financial institution has a fairly recent existence in the SEACEN region. Their presence represents a certain degree of financial sophistication as they are engaged in specialised financial services which could not be adequately covered by commercial banks. Hence, countries with more developed financial structure would see a greater role for merchant banks.

The merchant banks in Singapore, Malaysia, the Philippines, Sri Lanka and Indonesia were established primarily to engage in fee-based activities such as underwriting of securities, loan syndication, portfolio management and other financial services geared to the

corporate sector. Their fund-based activities-- lending and deposit-taking-- are not highly encouraged by the authorities in the five countries since this is already being undertaken by other bank types. If they have to engage in lending, merchant banks in these countries are preferred to go into the long-term.

The merchant banks in the first three mentioned countries started operations in the early part of 1970 while those in Indonesia and Sri Lanka emerged in the late '70s and early '80s, respectively. In fact, in the Philippines, where they are referred to as investment houses, the first such institution was founded in 1936 but it was also only during the 1970s when most of these institutions emerged in the country. In Indonesia, the so-called investment finance companies are also authorised to perform merchant banking functions such as providing guarantees, extending financial and management consultancy services and underwriting of capital issues. However, since these merchant banking functions are undertaken at a very small scale, this study has classified the investment finance companies of Indonesia under "finance companies". Another common thread among merchant banks in the SEACEN countries is that most of them are joint ventures of domestic and foreign financial institutions. In fact, in Singapore all merchant banks are multinationals.

In terms of share to total assets of the financial system, Singapore has the largest merchant banks in the region where they accounted for 17 per cent. Within the city-state, they are the second biggest group of financial institutions. In Malaysia, they contributed about 4 per cent of the total assets of the financial system in 1984 while in the Philippines, their share was a little over 1 per cent.

The activities of merchant banks in Singapore are now largely fee-based reflecting the degree of financial development it has attained and at the same time the consequence of their not being allowed to accept deposits from the public or issue promissory notes.

In the case of the other four countries, due to the insufficiency of fee-based business and to make their operations viable, merchant banks were allowed to accept deposits other than current account, issue promissory notes and to engage in money market transactions. ^{7/} However, their active roles in fee-based activities and in developing the capital market remain an important concern of the authorities in Indonesia, Malaysia, and the Philippines. In order to restrict the increasing involvement of Philippine merchant banks in the more lucrative money market, funds raised by them were subject to reserve requirement starting in the mid-'70s. In Indonesia, investment finance companies) have to observe limits on their short-term loans/papers and they are not allowed to make direct loans.

Cooperatives and credit unions

This type of savings and credit institution is found in Malaysia, the Philippines and Thailand. There is a dearth of information on cooperatives and credit unions in the Philippines and this precludes their inclusion in this section. The distinguishing characteristic of these cooperatives is that they were formed by groups bound by similar interests, usually along occupation lines or location of residences. As such, they are numerous and they are spread all throughout the countries. However, their resources only accounted for 2.2 per cent and 1.1 per cent of the respective assets of all financial institutions in Malaysia and Thailand in 1984. Although cooperatives were primarily established to foster the habit of thrift and saving among their members, their deposits are not substantial and their main sources of funds are borrowings and members' capital contributions. Funds accumulated by these institutions are invested mainly in loans to members and in the property market.

^{7/} This explains why merchant banks in Malaysia, the Philippines and Sri Lanka were classified under "other deposit-type".

In Malaysia, savings cooperatives were introduced in 1922. They can be grouped broadly into two, based on their location: those operating in the urban areas, and the other, in rural areas. The urban credit cooperative societies are composed mainly of employees credit societies and unions of credit cooperative societies of the public and private sectors. The particular composition of these societies also reflects a specific group or interest, such as the cooperatives for housing and transport. The number of cooperative societies in Malaysia has remained in the vicinity of 2,500 with a membership of some two million and total resources of \$4 billion by the end of 1984.

The cooperative savings scheme in Thailand has a slightly longer history than Malaysia as the movement began in 1916. In terms of number, cooperatives in Thailand almost equal those in Malaysia, at 2,251. They are also formed mainly on an occupational basis, the biggest of which are the agricultural and savings cooperatives. The agricultural cooperatives were organised by farmers for their mutual benefits. The major savings cooperatives were formed by salary earners and these included those organised by school teachers, university employees, provincial policy units, employees of public entities and government departments. Unlike the agricultural cooperatives which get substantial loans from the government-owned Bank for Agriculture and Agricultural Cooperatives, the savings cooperatives have to depend largely on their paid-in capital.

Managing the affairs of cooperatives and credit unions is normally handled by the members through a board of directors which they choose among themselves. There are some cases of mismanagement or improper handling of the cooperatives' business due mainly to the lack of professional banking experience of their managing boards. These developments have precipitated the failure of some cooperatives, and eventually, members shifted their deposits to the more formally organised and professionally-managed banking institutions.

Contractual Savings Institutions

Some financial institutions can be grouped under contractual savings institutions because of the compulsory nature in which their funds are gathered. The participants or members of these institutions enter into some form of a contractual arrangement to make regular payments over a specified period of time. In return, the member or his dependents get a lump sum or stream of income after a certain period and in the case of an insurance policy, protection from casualties and other eventualities as well. Since payments of members are made on a regular basis, the inflow of funds to these contractual savings institutions is predictable. And since the number of members expected to receive a lump sum or stream of payments each year is known, the outflow of funds can also be predicted. Thus, cash flow management does not pose so much a problem for these institutions and their funds are accordingly invested in long-maturing securities.

Institutions falling under this group could either be government or privately administered and they include insurance companies, provident and pension funds and other social security and employees welfare schemes. In the SEACEN countries, the provident and pension fund-type of contractual savings institutions predominate because virtually all employed workers are required to contribute to them. In 1984, they accounted for as high as 16 per cent and 15 per cent of the respective total assets of the financial systems of Malaysia and Singapore. On the other hand, the insurance companies with the highest relative shares to total assets of all financial institutions during the same year were in the Philippines, at about 8 per cent, followed by Sri Lanka, at 4 per cent and Malaysia, at 3 per cent.

Provident and pension funds

These institutions have a captive market in the SEACEN countries since all employees, with a few exceptions, have to

contribute regularly to their funds. In view of this, provident and pension funds gather a sizable amount of funds, the investment of which has a substantial impact in the financial market. More significantly, the regular contributions of the members and the more predictable nature of cash outflows, make the pool of funds they gather ideal for long-term investment.

Combined contributions of the employees and employers to their respective government-administered provident funds is highest in Singapore, at 50 per cent of the workers' monthly income, followed by Malaysia, Nepal and Sri Lanka at 20 per cent and the Philippines at 18 per cent for government employees and 8 per cent for those in private firms. In Singapore and Nepal, both the employer and employee contribute equal shares while in the other countries, the employer contributes more. In Malaysia and the Philippines, a number of public and private firms have their own provident funds as part of their compensation benefits, to supplement the coverage provided by the nationally-administered funds. In Sri Lanka, there is also an employees' trust fund where the employer has to contribute 3 per cent of the government and private employees' earnings to the fund. There is no counterpart contribution from the employees and the fund can be collected upon the member's retirement.

Insurance companies

The financial intermediation role of insurance companies is not as obvious as that of banks or other non-bank financial institutions because they are more associated with minimisation of and compensation from risks. Although the two basic types of insurance companies, life and non-life (casualty and property), differ in the type of risk they insure and the type of investment they tend to make, they nevertheless perform the same intermediation function. They accept funds in the form of premiums from those they insure and stand ready to pay off on the risks they insure. They also invest the funds they receive, thus acting as a lender.

The ownership of insurance companies and the year in which they emerged in the financial structures of the SEACEN countries divide them into two groups. One group comprising Indonesia, Malaysia, the Philippines, Singapore and Thailand, have insurance companies which are mainly in private hands and were established as early as the late 1800s. The first insurance companies in these five countries were foreign-owned and their presence was needed mainly to cover the marine hazards associated with international trade. Their long existence is one reason why insurance companies are greater in number in these five countries. Forming the other group are Nepal and Sri Lanka where the major insurance companies are owned by the government and came into existence during the 1950s and 1960s.

Despite the differences in time of establishment and ownership, insurance companies in all of the SEACEN countries operate similarly. Their liabilities are largely in the form of insurance premiums and they also extend loans for housing and other short-term nature to their policy holders. The government agencies supervising these companies prescribe the minimum ratios and also the form in which their gathered funds could be invested, invariably including government securities since such specifications were meant to ensure the liquidity and security of the funds they have gathered.

Development-type Financial Institutions

Development financial institutions were established in the SEACEN region as an answer to the dearth of medium and long-term funds for the private sector as the leading banks tended to concentrate on short-term lending. They cater primarily to the needs of enterprises that cannot easily raise funds in the domestic or foreign capital market. The bulk of their funds are provided by the government. Since not all development financial institutions in the region accept deposits their other sources of funds include multilateral international financial institutions and to a lesser extent, through issuance of their own securities. Even in countries (Indonesia, Nepal

and the Philippines) where development financial institutions accept deposits, their main source of funds is still the government as deposits gathered are not sufficient. In addition to those set up by the government, there are also privately-owned development financial institutions in Indonesia and the Philippines.

Funds provided by development financial institutions mainly financed the investment needs of the industrial sector. They also have equity shares in private industrial enterprises, provide credit guarantees, administer funds borrowed by the government from international financial institutions and manage projects of the government which were financed from external sources. Development banks in the SEACEN region can be grouped into two: those established to serve the entire country as represented by those owned by the National or Federal Government and those designed to operate at the regional or local level, which are either wholly or partly owned by the public and private sectors.

In Burma, this type of financial institution is represented by the Myanma Agricultural Bank whose main function is to supply the cash and credit needs of the national economic plan in the field of agricultural, livestock and fishery production. It does not lend directly to farmers but only through village banks. Its total assets in 1983 accounted for 1.8 per cent of Burma's banking system.

In Indonesia, the operations of the state development bank is geared to land transportation, maritime, tourism and construction. On the other hand, the only private development bank is yet to fulfil the investment promotion role it was assigned while the regional development banks which were established by Provincial Acts are expected to, among others, encourage development of local governments.

Development financial institutions in Malaysia were organised to serve two broad sectors, agriculture and industry. Three development institutions are owned by the Federal Government while the

rest were established by state governments, notably those in Eastern Malaysia. Their aggregate assets constituted 3 per cent of the financial system's total in 1984.

In Nepal, the two development financial institutions are owned by the Government. In addition to serving their specific sectors, the Agricultural Development Bank has commercial banking activities as well while the Nepal Industrial Development Corporation also underwrite equity shares of public limited companies. These institutions had an asset share of 9 per cent to the financial system's total in 1983.

In the Philippines, the Development Bank of the Philippines (DBP), the Land Bank of the Philippines, the National Investment and Development Corporation (NIDC) and the Agricultural Credit Administration (ACA) are government-owned and operate nationwide. Together with the private development banks, they accounted for 12 per cent of the total assets of the financial system, the biggest share among the development-type financial institutions in the SEACEN area. The two government banks issue their own bonds in addition to raising funds through deposit mobilisation and direct borrowings locally and overseas. The NIDC and ACA gets funding from the government for the purposes of equity investment lending only. The stockholders' equity in private development banks is augmented by their retained earnings, quasi-money deposits and capital contribution from the DBP. The private development banks also get support from the DBP in the form of rediscounting and technical and training assistance.

The development financial institutions in Sri Lanka accounted for 2 per cent of total assets of the financial system in 1984. They are represented by three entities whose main objective is to promote the industrial, commercial and agricultural development of the economy, especially in the private sector. Thus, the Development Finance Corporation of Ceylon, the State Mortgage and Investment Bank

and the National Development Bank are engaged in medium to long-term lending and equity investments in development projects.

The three development financial institutions in Thailand specialise in agriculture, housing and industry. Their combined assets accounted for 4.5 per cent of the total resources of the financial system in 1984, with the Bank for Agriculture and Agricultural Cooperatives contributing 2.3 per cent, the Government Housing Bank, 1.2 per cent and the Industrial Finance Corporation of Thailand, 1 per cent.

While the presence of development financial institutions has no doubt increased the availability of medium and long-term funds for the private sector, the smallness of this group of institutions is the main reason why it has not exerted a profound impact on the capital market. There is therefore a need to look at sources of funds other than the government in order to expand their operations. Another area which needs to be looked into concerns the equity participation of development banks in private enterprises. The equity contributions of development banks in private sector enterprises usually comprise a major share, and since these banks are owned by the government, control of the firms rests on the government. In pursuance of the major objective of the government in establishing development banks, that is, encourage private sector participation in economic development, these banks should divest their shares as soon as private hands could take over.

Investment-type Financial Institutions

These are financial institutions which collect savings from a large number of people by issuing them primary securities in the form of shares. The funds collected are invested in a large portfolio of stocks and/or bonds. Investment institutions pay dividends to their share holders out of the interest, dividends and capital gains earned by their investments. Small savers are attracted

to investment-type institutions for several reasons. Since the funds collected are typically large, they permit diversification that would not be possible if the saver invested directly in securities. They also get more expert management and they save on transactions costs because of the large quantities in which the investment companies trade.

Malaysia and the Philippines have this type of financial intermediaries and in the former, they are known as unit trust institutions while in the latter they are represented by investment companies, fund managers and venture capital corporations. Their total assets in both countries account for only a little more than one per cent of the total assets of their financial institutions.

Other Types of Financial Institutions

Discount houses

The need for the services of discount houses arises as more and more institutions emerge in a country's financial and business corporate structures. This is due to the fact that banks, especially commercial banks, and the corporate sector need temporary investment outlets for their funds, that is, in the interim that they are not used for their main business. Thus, funds placed with discount houses are usually on overnight or on-call basis which in turn are reinvested in short-term government securities and commercial and trade bills. Due to the nature of their transactions, discount houses in effect serve as the link between financial institutions and the monetary authority. In the SEACEN region, discount houses can be found in Malaysia and Singapore where they are patterned after the British model. Assets of Malaysian discount houses accounted for 1.4 per cent of the financial system's total while those in Singapore contributed 1.7 per cent. In Singapore, discount houses are the most active participants in the secondary market for government securities and negotiable certificate of deposit in local company.

Specialised financial institutions

One prominent feature of the financial structures of most of the SEACEN countries is the establishment of specialised financial institutions. They are also engaged in gathering and lending of funds just like any other financial intermediaries but it is difficult to put them into one bank category as most of them have commercial, savings and development banking functions. However, their facilities are geared to develop a specific type of activity, thus making them similar to development banks. In fact, some specialised institutions were classified in this study under the "development-type".

The main reason for their existence is the belief that certain sectors or activities could not compete for funds in the open market, hence the need to establish a special financing agency for them. These institutions are funded by the government and are basically lending institutions, thus they are not as active in savings mobilisation. Likewise, some financial institutions have been organised to reflect certain teachings or practices, notably those religious in nature. In the SEACEN region, there are financial institutions created specifically for agrarian reform (the Philippines), housing (Thailand), for exports credit insurance (Sri Lanka) and small industries (Thailand) as well as to serve particular religious communities (Malaysia and the Philippines). In the case of Burma and Indonesia, their financial systems are so organised so that the leading commercial banks are given specific sectors to serve.

Other types of financial institutions can be found in the SEACEN countries that contribute to greater diversification of their financial structures. Pawnshops are still found in the financial systems of the SEACEN countries although they are not as active and as numerous as before since they are only into lending and have no savings facilities. However, since they still meet the emergency loan needs of the public they are now supervised by the government. In Thailand, the public sector through the Department of

Public Welfare and municipalities operate pawnshops side by side with the private sector.

The financial systems of Singapore, the Philippines and Sri Lanka also have offshore banking units in addition to their domestic banks and branches of foreign banks. The operation of offshore banks in these countries have no doubt added another dimension to their financial systems as well as opened other alternative sources of funds. However, their existence have also raised some issues such as the competition they posed to domestic banks and the impact of their operations on monetary policy.

Lastly, in the SEACEN countries with more developed and complex financial systems, other institutions and facilities which are geared towards the trading and delivery of outstanding financial assets, as distinguished from generating fresh funds, also exist. These include the exchanges (stock market, financial and commodity futures) and securities dealers and brokers. Their presence in the financial system is deemed important as they enhance the liquidity and secondary market of financial assets as well as reduce the risks inherent in investment ventures. In fact, their active involvement in the whole process of financial intermediation is an evidence of the high degree of development of a country's financial structure.

IV. FINANCIAL INSTRUMENTS IN THE SEACEN COUNTRIES

The previous section has shown that the SEACEN countries have a variety of institutions in their financial structures, something which could not be easily said of their financial instruments. Financial instruments in the SEACEN countries are not as diversified as their financial institutions and this can be likened to a situation in the real sector where a varied number of industries produce a few, similar products and services.

Financial Claims and Equities

In the SEACEN countries, claims formed the bulk of financial instruments issued (see Table 5). They comprised almost all of the financial instruments in Indonesia, Nepal and Sri Lanka and 98 per cent in the the Philippines. This means that equity issues accounted for a negligible share in the first three countries and 2 per cent in the Philippines. In Malaysia and Singapore equity issues accounted for a respective 26 per cent and 13 per cent (including bonds) of their total instruments in 1984. In Thailand, they comprised 3 per cent in 1980. Nevertheless, claims still formed the bulk of financial instruments in Malaysia, Singapore and Thailand with respective shares of 74 per cent, 87 per cent and 97 per cent. The dominance of financial claims in the SEACEN countries implies that the financing needs of business enterprises, the government and the households, collectively treated in this study as non-financial sectors, were met mainly through loan or debt transactions. They hardly resorted to issuing stock shares in raising funds. Consequently, almost all of the surplus funds of other non-financial units are deposited with financial institutions, that is, as financial claims rather than as ownership shares.

Another evidence of the underdeveloped state of the stock market in the SEACEN countries is seen in the declining share of equities to total financial instruments outstanding. For instance, in Malaysia, the breakdown of financial instruments was 67 per cent for claims and 33 per cent for equities in 1973. This ratio has deteriorated to 74:26 and 1984. In the Philippines, equity shares used to account for 7 per cent of financial instruments in 1970 but this was reduced to 2 per cent in 1980.

Financial Claims, by Sector

A breakdown of financial claims by major sectors of the economy can indicate the general saving and borrowing patterns of an

economy. The non-financial sectors have claims against financial institutions by entrusting their savings to them, as evidenced by the deposits, promissory notes, insurance policies, pension contracts and other indirect securities issued by financial intermediaries. On the other hand, borrowings of the non-financial sectors are given in this study as claims of the financial institutions and they include loans, consumer credit and home mortgages. Non-financial sectors can also lay claim against each other as there exist intrasectoral lending and borrowing. In the SEACEN countries, lending and borrowing among the non-financial sectors is evidenced mainly by government securities. Nevertheless, financial institutions are still the main holders of government securities.

Available data in the SEACEN countries showed the predominance of claims of financial institutions against non-financial units. Viewed from the non-financial units' side, this means that they ended up as deficit spenders, they borrowed more than saved in financial institutions. The more prominent role of the organised financial institutions in lending rather than mobilising savings was most apparent in the Philippines, Singapore and Nepal (see Table 6). In these countries, the financial institutions' claims on the non-financial sectors exceeded the claims (savings) of the non-financial sectors. For instance, in the Philippines as of mid-1984, financial institutions' lendings or claims over non-financial sectors represented about 62 per cent of total claims. On the other hand, claims of non-financial sectors or savings in the financial system went as low as 30 per cent in 1970 in the Philippines.

In Singapore, financial institutions were more of lenders than mobilisers of savings. About 59 per cent of total financial claims in 1975, 1980 and 1984 represented lendings of financial institutions while about 39 per cent was in the form of savings of non-financial sectors in financial institutions. The remaining 2 per cent represented government securities, specifically, claims of non-financial sectors against other non-financial units (government).

The other country which showed a distinct deficit-spending behaviour for the non-financial sectors is Nepal. Available data in this country showed that claims of financial institutions exceeded claims of non-financial sectors, reaching as high as 59 per cent of total financial claims. In Thailand, claims of financial institutions were also higher than claims of non-financial sectors in 1980, at a ratio of 54:46. A different ratio was, however, obtained in 1967 when the non-financial sectors saved more than they borrowed from financial institutions.

The breakdown of financial claims in Indonesia showed the prominent role of the financial sector, specifically the monetary system, in providing funds to the foreign sector. Claims of the financial sector accounted for as high as 56 per cent of total financial claims in 1980 and 1984. Of this, 23 per cent and 31 per cent represented claims of the monetary system against the foreign sector in 1980 and 1984, respectively.

The percentage distribution of financial claims in selected years in Malaysia does not show a clear saving or borrowing pattern. However, based on the number of times their savings exceeded their borrowings, the non-financial sectors tended to be net savers. In 1960, 1973 and 1980, the non-financial sectors of Malaysia saved more than availed themselves of loans from financial institutions. In 1984, they saved as much as they borrowed from financial institutions. In Sri Lanka, the shares of claims of financial institutions to total financial claims exceeded those of non-financial units in 1970, 1975 and 1980, making the latter a deficit-spending sector. However, in 1984, the non-financial sectors ended as net savers as their claims against financial institutions constituted 53 per cent of total financial claims.

Financial Claims, by TypeMoney supply (M1)

In the SEACEN countries, money (M1), which represents a claim of the non-financial sector against the central bank and commercial banks, has been tracing a declining share to total financial instruments through time (see Table 5). This is a typical trend movement for the relative share of narrow money as the financial structure of a country develops. Among the SEACEN countries, money supply as a percentage of total financial instruments outstanding was highest in Indonesia at 19 per cent and in Nepal at 18 per cent in 1984. These shares, nevertheless, already marked decreases over the the 1970 levels. The share of money supply in Singapore was the lowest in the region as it represented only 5 per cent of its aggregate financial instruments in 1984, a further reduction from the 9 per cent registered in 1975. Malaysia follows, at 6 per cent, where M1 used to account for 32 per cent in 1960 and 10 per cent in 1973. The share of M1 in Thailand in 1980 was a little less than 9 per cent as compared to 16 per cent in 1967. In the Philippines, currency and demand deposits represented a little less than 11 per cent of total financial instruments outstanding in mid-1984, a reduction of more than half of what was obtained in 1960, but virtually unchanged from the 11.6 per cent in 1970. The share of M1 to total financial instruments in Sri Lanka has been continuously on the downtrend too, from 25 per cent in 1965 and 19 per cent in 1970 to 13 per cent in 1984. Money supply in Nepal also showed a declining relative share, from 30 per cent and 21 per cent in 1965 and 1975, respectively, to 18 per cent in 1983.

Notwithstanding the declining importance of narrowly-defined money supply, the relative shares of its components, currency and cheques, which are used as means of payment could still be another gauge of the financial development of a country. As the financial structure develops, more and more payments are carried out in the form

of cheques, a transaction which involves the banking system (commercial banks). In contrast, the use of cash or currency is a direct transaction between parties and no financial intermediary is involved.

Table 7 shows the breakdown of M1 in the SEACEN countries. The progressive increase in the share of demand deposits to total M1 in Indonesia is a good illustration of one development which represents an upward movement along the financial development path. In 1970, demand deposits constituted only 38 per cent, then increasing continuously through the years until it accounted for 57 per cent of total money supply in 1984. Demand deposits from the 1970s to the 1980s, with a few exceptions, also formed the greater share of M1 in Singapore, Malaysia and Sri Lanka. In the Philippines, demand deposits were higher than currency from the mid-'70s to the early '80s. The economic and political crisis it experienced in 1983 to 1984, however, led to the preference of the public for currency. On the other hand, currency still formed the bulk of M1 in Burma (92 per cent in 1984), Thailand (68 per cent) and Nepal (66 per cent). In Burma and Nepal, there is a trend for an increasing share of demand deposits through time while in Thailand, demand deposits are losing their share to currency.

Quasi-money

Another type of claim of the non-financial units against the financial institutions are savings and fixed deposits which are preferred for their store of value, that is, as an outlet for saving or investment. In addition to bearing interest rates, these deposits can also be easily converted into cash to meet the general public and business sector's transaction demand for money, hence they are also referred to as quasi-money. Together with M1, they constitute the broader definition of money supply or M2. To a large extent, the declining share of M1 to total financial instruments outstanding is due to the shifting of deposits from the non-interest earning to the

interest-bearing indirect securities. In 1983-1984 and in countries where a breakdown of data is available, savings and fixed deposits constituted the bulk of total claims of the non-financial sectors against the financial institutions (see Table 5). In 1984, savings and fixed deposits in banks and finance companies in Sri Lanka accounted for about 27 per cent of total financial instruments. They accounted for 21 per cent of the total financial instruments outstanding in Indonesia and Malaysia and 17 per cent each in Nepal and the Philippines. The popularity of quasi-money is also seen in Table 3 which gives the percentage distribution of deposit liabilities of commercial banks. In 1984, interest-earning deposits comprised 93 per cent of total deposits of commercial banks in Thailand, 88 per cent in the Philippines and 84 per cent in Burma. The predominance of interest-bearing deposits in the liabilities structure of commercial banks was also evident in the other countries.

A consequence of the popularity of interest-earning deposits was the emergence of other deposit-type financial institutions and the introduction of more attractive features for these instruments. As already mentioned, finance companies in Malaysia and Thailand have emerged as one of the top financial institutions and they ranked second to commercial banks as mobilisers of deposits. In Singapore, Sri Lanka, and the Philippines, their own savings banks are also significant depositories of savings and fixed deposits. More recently, introduction of new features to these deposits such as negotiability and floating interest rates further enhanced their attractiveness.

In terms of annual growth rate, currency and demand deposits or M1 in the SEACEN countries has been experiencing deceleration and registering absolute decreases (see Table 8). On the other hand, the inclusion of interest-earning financial instruments (savings and fixed deposits and negotiable certificates of deposit) to the definition of money, has shown favourable yearly increments (Table 9). In Singapore, M2 grew faster than M1, at an average of 11.9 per cent from 1981 to

1985 as compared to 8.4 per cent for the narrowly-defined concept of money. In Malaysia, the attractiveness of interest-yielding money is reflected in the average growth from 1981 to 1985 of 12.7 per cent for M2 while M1 increased by only 5.6 per cent. The same trends were observed in Thailand, with M2's average increment at 20 per cent as against 4.9 per cent for M1 alone. In the Philippines, the inclusion of savings and time deposits to the definition of money supply means a five-year average growth rate of 17.8 per cent while that for the narrowly defined money was only 5.9 per cent.

The growing significance of M2 can also be seen in its share to GNP. During the same period, the proportion of broadly defined money to total goods and services (GNP) of the individual SEACEN countries has been expanding while that for narrow money was declining (see Tables 10 and 11). In Singapore, the share of M2 to GNP rose from 71 per cent in 1981 to 72 in 1985 while that for M1 declined from 26 per cent to 22 per cent. In Malaysia, broadly defined money took a share of 63 per cent in 1985 while that for narrowly defined money dipped to about 18 per cent. Likewise in Thailand, M2's share to GNP increased from 38 per cent in 1981 to 54 per cent in 1984. In the Philippines, the share of M1 to GNP was declining too, but such trend was not consistently compensated for by the expansion in the share of M2 which showed a wide-ranged fluctuation, from a low of 20 per cent in 1984 to a high of 25 per cent in 1983. This may be partly explained by the existence of another monetary aggregate, the deposit substitute, which together with M2 constitute the broadest definition of money, M3, in the Philippines.

Loans

Viewed from the asset side of financial institutions, that is, their claims against non-financial sectors, loans represented the bulk of their claims (see Table 5). These loans, broadly defined here as comprising of short and long-term loans, bills and hire-purchase instruments, were extended mainly to the private sector. Loans in the

Philippines accounted for more than half (52 per cent) of total financial instruments outstanding in 1984. In 1970, they comprised as high as 54 per cent of total financial instruments, declining to 52 per cent in 1984. Thailand followed, at 38 per cent, an increase in loans' share from the 25 per cent recorded in 1967. In Indonesia, loans to the private sector traced a decreasing share to total financial instruments, from as high as 50 per cent in 1970 and 1975 to the latest 28 per cent in 1984. On the other hand, the shares of loans and bills in Malaysia and Singapore have been gradually increasing since the mid-70s and reached 25 per cent by 1984. Loans to the private sector in Nepal and Sri Lanka accounted for about 20 per cent of total financial instruments in 1984.

A breakdown of bank loans by sector is available for Indonesia, Nepal, the Philippines and Sri Lanka as shown in Table 12. On the whole, the manufacturing and industrial sector has been getting the largest share of total loans from banks, ranging from 48 per cent in Nepal to 25 per cent in Sri Lanka as of 1984. The share of manufacturing loans has been tracing an increasing trend during the ten-year period. Loans for the trading and commercial sector were also substantial and it even accounted for half of total commercial bank loans in Sri Lanka. On the other hand, the share of loans to the agricultural sector did not show very encouraging trends. In Indonesia and Sri Lanka, the share of agricultural loans to total went down to 7-8 per cent during the decade ending in 1984. In the Philippines, loans of banks to the agricultural sector relative to their total loans were maintained while an increase was noted in Nepal. Interlending among banking institutions was significant in the Philippines and Sri Lanka. In the Philippines, interfinancing among banks accounted for about 27 per cent of total loans granted by the banking system, an increase over the shares of 12 per cent and 22 per cent obtained in 1973 and 1981, respectively. In Sri Lanka, intracommercial bank loans comprised 2 per cent of total, a decrease over the 4 per cent and 3 per cent registered in 1975 and 1980, respectively.

Government securities

Unlike in other countries, particularly in the United States, where securities issued by the public sector are also attractive to households and non-financial corporations in view of their competitive yields and safety features, financial institutions in the SEACEN countries are the main holders of government securities. In fact, government securities constituted the second highest financial asset-claim of financial institutions. The apparent popularity of government securities to financial institutions is not due to their attractive yields. On the whole, securities issued by the public sector in the SEACEN countries have below-market yields. Hence, the actual reasons behind the holding of government securities by financial institutions are that they are required to hold part of their legal reserve requirement against their deposit liabilities in this form while others are allowed to invest their funds only or mainly in government securities, as specified in their charters. For instance, in Malaysia and Singapore, their government-administered employees provident funds absorbed the bulk of government securities outstanding. The Employees Provident Fund of Malaysia held as high as 74 per cent of total outstanding government securities in 1960 and 50 per cent in 1984. Another reason is that, apart from loans and government securities, there are no other suitable investment outlets for funds raised by financial institutions as private corporate bond and equity issues are insignificant.

As can be seen in Table 5, government securities traced a declining share to total financial instruments outstanding as well as in terms of total claims of financial institutions in the SEACEN countries. This was due more to the unattractive features of government securities rather than a reduced need for funds of the government sectors of these countries since their fiscal deficits tended to increase through the years. The relative decrease in the holdings of government securities of financial institutions also means that financial intermediation to the government has been declining.

Government securities' share to total outstanding financial instruments was highest in Sri Lanka where they accounted for 26 per cent in 1984. This, however, marked a substantial decline over the more than 40 per cent obtained from 1965 to 1975. Holdings of government securities of financial institutions in Thailand and Malaysia accounted for 13-14 per cent of total outstanding financial instruments, as compared to the shares of 16-18 per cent in the 1960s. In the Philippines, the share of government securities has steadily declined, from 24 per cent in 1950, 18 per cent in 1960, 11 per cent after another ten years and to 8 per cent in mid-1984.

Government securities held by financial institutions in Singapore took a more stable share to total financial instruments. In 1984, they accounted for 14 per cent of total financial assets outstanding. On the other hand, government securities held by other non-financial units traced a declining share.

The exception to the declining importance of government securities to total financial instruments among the SEACEN countries are Nepal and Indonesia. In Nepal, claims of the financial institutions against the government, in the form of government securities, rose through the years. The share of government securities to total financial instruments started at 1 per cent in 1970, rising to 8 per cent and 10 per cent in 1975 and 1980, respectively. In 1984, they comprised a share of 15 per cent. In Indonesia, government securities in financial institutions' portfolio accounted for almost 4 per cent of outstanding instruments in 1984, an improvement over the 0.8 per cent in 1970, less than 2 per cent and 3 per cent in 1975 and 1980.

In Burma, government-guaranteed securities with maturities ranging from 10 to 30 years since 1954 used to be one of the financial instruments in Burma, with the central bank holding the bulk. At present, all of these securities have been redeemed and are no longer issued.

Term Structure of Financial Instruments

The term structure of financial instruments in the SEACEN countries shows that claims of the financial sector against non-financial units, which were largely in the form of loans, have generally short-term maturities while claims of non-financial units against financial institutions, particularly deposits, tend to have longer maturities.

Although there has been a lengthening of maturities of loans in the SEACEN countries over the years, available data still indicate a preponderance of maturity periods in the short-term end. In the Philippines, the commercial banks are the biggest source of domestic credit and the maturity structure of their outstanding credit still showed a bias towards the short-term. Despite the improvement observed in the medium and long-term credit, short-term credit still accounted for 61 per cent of the total in 1984 as compared to the 82 per cent in 1978. In Sri Lanka, commercial banks' advances with less than one year maturity comprised 72 per cent in 1984, a ratio which showed short-term advances increasing through the years as they accounted for only 60 per cent in 1970 and 70 per cent in the early years of the 1980s.

On the deposit side, a broad indicator of the lengthening of their maturities can be seen in the substantial growth in fixed deposits as compared to demand and savings deposits of financial institutions in the region. For instance, the term structure of time deposits in Nepal showed that in 1983 about 80 per cent were placed for two years, an improvement over the 67 per cent in 1975. On the other hand, time deposits placed one year and below have been getting a declining share, particularly in the three months category which experienced absolute decreases. Another indicator is the increased contractual savings of the household sector in provident and pension funds and insurance companies, financial assets which can only be claimed after a specified and relatively long period of time.

Marketability of Financial Instruments

The breakdown of financial instruments in the SEACEN countries as to their marketability or transferability reflects the dominance of the deposit and loan market over the equity and securities market. In this study, the marketability classification is treated broadly as it refers more to transferability of ownership of financial instruments or their negotiability, rather than the strict definition of their being traded in the open market. Based on this definition, currency is classified as a marketable financial asset. However, in view of the declining share of currency to total financial instruments, the broad definition of marketability in this study is not expected to differ much from the usual definition of marketability, especially during the more recent years. In this regard, the marketable instruments in the SEACEN countries are largely in the form of government securities and negotiable certificate of deposit. Moreover the picture for the breakdown of financial instruments as to their marketability in most SEACEN countries is not expected to change even when the assets are confined to securities. The government issues which dominate the securities markets of these countries were held mainly by financial institutions. These financial institutions are compelled to hold on to these securities in fulfilment of statutory reserve ratios. Those securities which were not earmarked for specific purposes cannot be actively traded among the financial institution-holders since they do not have competitive yields. Thus, they have to wait until the full maturity of the issues or for the occasional early redemption by the government.

The bulk of the financial instruments in the SEACEN countries are of the non-marketable type which means that the asset holders have to wait for the full maturity of their instruments before they can be liquified or transferred to other asset holders. In view of this, the volume of financial instruments that can be traded in the SEACEN region is very small and the secondary market for them is likewise underdeveloped. For instance, the most preferred financial

assets by the surplus sector were fixed deposits which do not require secondary markets as they have to be held in these forms up to a specified period. Provident and insurance funds also accounted for a substantial portion of financial instruments but they could not be transferred or traded also in the financial markets. Even the financial intermediaries that obtained the savers' funds by issuing their own indirect securities have to reinvest these funds largely in loans, as bonds and stocks are not sufficient, have unattractive yields and have poor secondary markets.

Among the SEACEN countries, Singapore has the highest share of marketable financial instruments or 44 per cent of total financial instruments (see Table 13). This ratio, however, marked a deterioration from the relatively higher levels of 53 per cent obtained in 1975 and 48 per cent in 1970 and 1980. The distribution of financial instruments as to their marketability in Malaysia was fairly stable in the 1980s, at 40 per cent for the marketable financial assets and 60 per cent for the non-marketable type. In Sri Lanka and Nepal, during the mid-1960s to the mid-1970s marketable financial instruments, largely in the form of currency, comprised more than 50 per cent of their financial instruments. However, with the growth in other types of non-marketable financial instruments in the 1980s such as savings and fixed deposits, provident funds and loans, the shares of marketable instruments were reduced to 38 per cent in Sri Lanka and 32 per cent in Nepal. In the Philippines, the share of marketable financial instruments which were mostly in the form of currency and government securities increased by almost two-fold in about two decades, from 12 per cent in 1960 and 20 per cent in 1984. The improvement in the share of marketable instruments can be traced to the issuance of more government securities, including those issued by the Central Bank, with market-oriented yields and other features.

Currency Denomination of Financial Instruments

The existence of foreign denominated financial instruments in a country is an indicator of the degree of openness of its economy and/or the extent of liberalisation of its foreign exchange policy. Moreover, for the lenders and borrowers, it means greater choices in investment outlets and funds sourcing. If the financial structure gives the surplus units and the deficit spenders more choices in the denomination of their savings and borrowings, it can be said that such financial structure is more advanced as compared to one where financial instruments can only take the local currency denomination. In the SEACEN region, the countries with liberal foreign exchange policies and/or have offshore banking units also have financial instruments denominated in foreign currencies. These are Singapore, the Philippines, Sri Lanka and Indonesia. The first three have offshore banking in their financial systems while in Indonesia, the lifting of all controls on foreign exchange has enabled local residents to maintain foreign currency deposits and contract loans in foreign currencies.

As shown earlier in Table 5 which gives the percentage distribution of outstanding financial instruments in the SEACEN countries, the three countries mentioned have financial assets denominated in foreign currencies. In Singapore, they comprised about 20 per cent of total instruments in 1984 and were largely in the form of foreign securities and bills held by financial institutions. In the Philippines, foreign currency denominated instruments were mainly in deposits and they accounted for a share of 4.9 per cent as of June 1984. Likewise, in Sri Lanka, foreign currency deposits accounted for 2.6 per cent of total instruments in 1984 while loans and advances of foreign currency banking units (FCBUs) accounted for 1.4 per cent. The monetary system of Indonesia has a significant claim on the foreign sector, constituting about a quarter of outstanding financial instruments in 1984. On the other hand, the existence of foreign currency-denominated deposits and loans in Nepal can be explained by

the substantial inflow of foreign loans and grants in the country which were either temporarily deposited with the Nepal Rastra Bank and other financial institutions or lent out in such denominations to borrowers.

Introduction of New Financial Instruments

It can be seen from the foregoing sections that financial instruments are not as diversified as the financial institutions in the SEACEN countries. In this regard, the South-east Asian central banks have taken a lead role in introducing more financial instruments, in the same manner that they have been active in establishing and developing the institutional frameworks of their financial structures. Some of the financial instruments introduced or encouraged by the South-east Asian central banks can be considered innovative in the region, and are discussed below.

Central bank securities

The issuance of securities by the central banks themselves can be considered as a novel way in the SEACEN area. In addition to the traditional function of issuing currencies and coins, the central banks of the Philippines, Indonesia, Malaysia and Sri Lanka have also issued their own securities.

The Central Bank of the Philippines pioneered in this undertaking when it issued in 1970 its Central Bank Certificates of Indebtedness, more popularly known as CBCIs. They were originally issued to mop up excess liquidity in the urban areas and the proceeds were rechanneled to the rural sector, largely through agricultural credit schemes. Through the years, the terms and features of the CBCIs were modified so as to suit different target markets and to fulfil other objectives. Certain CBCI issues are geared to the domestic investors and have market-oriented yields and suitable maturity periods. Other particular issues are designed for foreign investors and are accordingly denominated in foreign currencies, in

particular, in U.S. dollar and Japanese yen. Other types of CBCIs are sold to meet statutory requirements of financial institutions such as substitute lending to the agricultural sector and as part of their legal reserves. In 1984, another central bank paper, the Central Bank Bill, was first issued. These bills have market-oriented features so that they have not only proven themselves as attractive investment outlets but have become the major instruments of the monetary authorities in the conduct of open-market operations.

Bank Indonesia also issued its own securities as early as 1970 and this continued until 1972 for the purpose of encouraging mobilisation of funds. In February 1984, the central bank started to issue again Sertifikat Bank Indonesia (SBI) but for a different purpose. They are intended as temporary investment outlet for the excess funds of banks before they are eventually extended as loans to their customers. When the secondary market for SBI has been developed, these central bank certificates are expected to assist in open market operations.

Bank Negara Malaysia started to float its own securities in 1980 in its effort to provide a wide array of financial instruments that would enhance its monetary management. These certificates were issued with maturities varying from 18 to 36 months and were held mainly by the non-bank private sector.

In June 1984, the Central Bank of Sri Lanka issued its own securities with a view to siphoning off the excess liquidity in the economy. These securities carry a maturity of six months, are fully negotiable and transferable by endorsement. They carry an interest rate of 14 per cent per annum but the yield to the investor will depend on the bid price as these securities are sold by auction.

Negotiable certificates of deposit

In view of the popularity of savings and fixed deposits as financial assets, the introduction by banks of an instrument which has the features of both deposit forms was encouraged by the central banks in the region. This instrument is known as a negotiable certificate of deposit (NCD) which is basically a fixed deposit, that is, with a specified interest rate and a date of maturity. What makes it different from the regular fixed deposit is its negotiability, the owner may sell the certificate to another party before its maturity. This type of deposit can be found in Malaysia, Singapore and Sri Lanka where it is referred to by that name and in Thailand, it was introduced in March 1984 as a transferable certificate of deposit (TCD). In the Philippines, a type of savings account was introduced in 1979 with negotiability feature. It is patterned after the NOW account in the United States and is similarly named, which in full stands for negotiable order of withdrawal (NOW). This order of withdrawal is like a cheque issued by the saver in favour of another party.

Financial instruments with floating rates

In Singapore, floating rate notes and floating rates certificates of deposit (FRCD) denominated in local currency were introduced in April and October 1981, respectively, to raise longer term funds in domestic currency that would match banks' term lendings. The instruments also enabled banks with relatively small deposit bases to resort to floating rate issues as an alternative means of raising funds. Consequently, loans with floating interest rates, mainly with short-term maturities, also emerged in the Singapore financial market to match the variable interest rate feature.

Premyo savings bonds

These are financial instruments first introduced in the Philippines in mid-1970s by the Ministry of Finance. They were issued for two basic objectives: to raise funds for the government at a minimum cost and to inculcate to the public, especially the low income and less sophisticated group, the habit of saving in financial instruments. The novelty of these bonds is found in their features. Premyo savings bonds are marketed by the Central Bank of the Philippines in low peso denominations like 10s and 20s, at no interest rate and with no maturity period, that is, they are redeemable at face value anytime. Every P10 bond is assigned a serial number which has a chance of winning in the daily lotteries held, with prizes ranging from P100 to P100,000. Special lottery draws are also held at cash prizes substantially bigger than the daily draws. This scheme caters to the basic preference of investors to minimise risk since it involves no loss in the nominal principal, in addition to a chance of winning the cash prizes at stake. On the part of the government, substantial revenue is raised, at a cost equivalent to the cash prizes but at a level lower than what could have been incurred had these bonds yielded interest. The same bonds, called Premium Savings Bond, have been introduced in the Sri Lankan financial system by the National Savings Bank.

V. SOME GENERAL INDICATORS OF FINANCIAL DEVELOPMENT

Previous studies on the financial structure have identified some relationships between financial instruments and financial institutions, on the one hand, and economic and monetary aggregates on the other, that give an indication of the degree of development of the financial sector of any country. The size of the financial sector in relation to the real sector can be measured by the financial interrelations ratio (FIR). The ratio is obtained by dividing the total value of financial instruments or assets (partly duplicated) by

the value of the national wealth or GDP. Another indicator of a country's financial sophistication is the financial intermediation ratio. This ratio measures the extent of indirect financing in the economy, or the funds made available by financial institutions to the non-financial sectors. The ratio is obtained by dividing the total funds supplied by financial institutions to non-financial units to the total funds raised by the latter.

Financial Interrelations Ratio

The size of the financial sector in relation to the real sector can be gauged through the financial interrelations ratio (FIR). The value of this ratio in the individual SEACEN countries has been, on the whole, increasing progressively through time (see Table 14). In a period of ten to twenty years, the value of financial instruments exceeded the value of national wealth of a number of SEACEN countries. It is interesting to note that the high FIRs (a total value of financial instruments at least twice the GDP) in Singapore, Malaysia, the Philippines and Burma obtained in 1984 represented a more than double increase in a period of ten years. On the other hand, the growth of financial instruments was relatively slow in Sri Lanka, Thailand, Nepal and Indonesia. It took 20 years for the latest ratios in Sri Lanka and Thailand to increase two-fold. In Nepal and Indonesia, the latest available financial interrelations ratios represented a three times increase over a period of two decades.

Reflective of its highly developed financial structure and its stature as an international financial centre, Singapore has the highest financial interrelations ratio among the eight SEACEN countries. As early as 1970, its FIR, excluding Asian currency deposits, was already at a high level of 2.55, increasing further to 4.34 in 1980, and in 1984, the value of financial instruments in Singapore was more than five times the value of its GDP or an FIR of 5.44. About 12 per cent of the financial instruments outstanding in Singapore in 1984 represented claims of the financial sector against

the rest of the world. In Malaysia, financial assets have been increasing rapidly too; the total value of financial instruments in 1984 is almost four times its national wealth or an FIR of 3.98. This level also reflected a doubling of the FIR after ten years. Compared to the .62 obtained in 1960, the ratio registered in 1984 represented a more than six-fold increase in a span of 14 years. Using the financial interrelations ratio as the indicator, the Philippines has the third largest financial sector in the region in 1984 as the total value of its financial instruments was 2.8 times greater than its GDP. The FIR obtained ten years ago was 1.14. Burma's FIR increased almost five times in a decade, from .45 in 1975 to 2.16 in 1984.

The other four countries, namely, Thailand, Sri Lanka, Nepal and Indonesia have comparatively lower FIRs, ranging from .52 to 1.07 in 1984. The total value of financial instruments in Sri Lanka in 1984 was a little more than its GDP or an FIR of 1.07. This reflected a slow increment when viewed against the .72 registered twenty years earlier. The FIR in Thailand also moved up slowly through the years, from .89 in 1967 to 1.10 in 1980. In Indonesia and Nepal, the respective FIRs register a triple increase in a period of 20 years. The .14 registered in 1966 for Indonesia moved up to .52 per cent in 1984. In Nepal, the value of financial instruments in 1984 was also still less than its national wealth or an FIR of .69.

Types of financial structure based on FIR

Different levels of the financial interrelations ratio in private enterprise and mixed economies were associated by Raymond Goldsmith with fairly distinct types of financial structures. 8/ He characterised the first type of financial structure by a low financial interrelations ratio, or a value ranging from one-fifth to one-half.

8/ Goldsmith, op.cit., pp. 32-35.

This type of financial structure is in its early stage of development, where claims predominate over equity securities, the share of financial institutions in all financial assets is low and commercial banks are the leading financial institutions. Moreover, bank notes and cheque deposits are supplementing and gradually superseding metallic money. This type of financial structure was found in Europe and in North America from the 18th until the middle of the 19th century.

The second type of financial structure identified by Goldsmith has the same characteristics as the first. What distinguishes it from the first type is the greater role of the government and of government financial institutions. The financial structures of Indonesia and Nepal would fall under this type as their respective FIRs had values of .52 and .69 in 1984. The characteristics of the second type of financial structure are all present in both countries -- dominance of claims over equity securities, the pre-eminence of commercial banks (the financial system of Nepal is virtually composed of three commercial banks while Indonesia's state commercial banks accounted for half of total assets of the financial system) and the greater role of the government and government financial institutions.

The third and last type of financial structure is characterised by a higher value of the financial interrelations ratio, starting from unity, that is, the total value of financial assets is equal in size to the national wealth. In terms of structure of financial instruments, equities are beginning to increase their share although claims still account for the bulk of total financial assets. There is an increased diversification among financial institutions, with the share of the banking system declining while the importance of other deposit-type institutions and private and public insurance organisations increases. This type of financial structure is common among industrialised countries since the beginning of the 20th century, particularly when the full complement of financial

institutions and instruments had been established in the United States, former British Dominions, Western Europe and Japan. Singapore, Malaysia and the Philippines have this type of financial structure, where their FIRs in 1984 were equal to or more than three and they have diversified financial institutions and to a lesser extent, financial instruments. The ratios for Sri Lanka and Thailand were slightly over unity which put these countries in the lower range of the third type of financial structure.

Financial Intermediation Ratio

In an economy, the non-financial units can turn to financial institutions and other non-financial units in financing their deficits. If the ultimate borrowers turn directly to ultimate lenders, then there is no financial intermediation involved. On the other hand, indirect financing takes place if the deficit spenders turn to financial intermediaries to augment their funds. The extent of the involvement of the financial institutions in the financing process is measured by the financial intermediation ratio. This is the ratio of the net acquisition during a given period by domestic financial institutions of instruments issued by the non-financial units to total issues of such instruments.

In some of the SEACEN countries where data is available, there has been an upward movement in this ratio through the years, although at an uneven pattern (see Table 15). In Singapore, it started at .77 in 1975, increasing to .83 in 1980 and slightly dropping to .81 in 1984. These figures mean that about 80 per cent of the financing needs of the non-financial units was provided by the financial institutions of Singapore while the remaining 20 per cent represented internal financing and/or direct dealing between the surplus units and the deficit spenders. The estimated financial intermediation ratio for Sri Lanka was even higher, at .87 in 1984, an improvement from the slightly over .60 obtained in 1960 and 1970. The ratio in 1984, however, was lower than the .88 per cent registered in 1975.

The financial intermediation ratios obtained in the Philippines also showed a high involvement of the organised financial sector in supplying funds to the non-financial units. In 1983, this was registered at .76, an improvement over the .69 in 1980 and .59 in 1982.

In Thailand and Nepal, it can be surmised that the bulk of financing was still done internally and/or undertaken directly between the deficit sectors and the ultimate lenders. Only about 30 per cent of the financing needs of the non-financial entities was handled by the financial institutions in both countries. In Thailand, the financial intermediation ratios obtained, at .33 in 1970 and .34 in 1984, indicated an almost static role of financial institutions in providing funds to the economy. Although financial intermediation is still low in Nepal, the movement of the ratio through the years reflects the increasing share of financial institutions in the financing process. The ratio doubled in less than a decade, from .15 in 1975 to .30 in 1983.

Other Indicators of Financial Development

Other quantitative indicators of financial development relate some monetary aggregates like the narrow and broad definitions of money, M1 and M2, to GNP. For instance, the highest M2 to GNP ratios were registered in Singapore and Malaysia at .68 and .62, respectively in 1984. The resulting ratios for the SEACEN countries were already discussed in Section IV of this regional study.

VI. FINANCIAL STRUCTURE AND MONETARY POLICY

Monetary policy works by adjusting to cyclical needs, the volume of and interest on the various financial assets that arise due to indirect financing relationships. Indirect financing is enhanced if the surplus sectors channel more of their savings to the formally

organised financial institutions which, in turn, relend these gathered funds to deficit units. With financial institutions under the supervision of the central bank, their gathering and lending of funds can be easily monitored and regulated. Thus, under this situation, the scope of the conduct of monetary policy by the central bank is enlarged. On the other hand, there is a limited scope for monetary policy when self-financing is involved since no financial assets which can be influenced by central bank measures are involved. Likewise, central bank influence on the availability and cost of funds is minimal or indirect if the surplus sector directly finances the deficit sector.

The foregoing underscores the fact that the financial development of a country has a bearing on the conduct of monetary policy. The instruments of monetary policy that can be used by the authorities are dictated by the variety of financial instruments and institutions existing in a country. As shown in the previous sections on financial institutions and instruments, the individual SEACEN countries are in different stages of financial development. Some countries have a complex financial structure composed of a wide range of financial institutions offering a host of services and issuing a variety of financial instruments. Others have only two or three types of financial institutions, owned and operated by the government.

Despite the differences in their degree of development, the financial structures in any of the eight SEACEN countries may be characterised by the following features:

- 1) The commercial banks are the most dominant institutions in the financial structure. However, despite the principal role of commercial banks in the financial system, other types of financial institutions have emerged and are gradually posing competition.

- 2) Financial claims form the bulk of the financial instruments, particularly deposits and loans.

3) In view of the first two features, the equity and securities market is relatively underdeveloped. Investment-type financial institutions are not as active as there are not enough equity and long-term securities to deal with.

4) The existence of the first three features, however, does not mean that there is a dearth of long-term funds in the SEACEN countries. In fact, there exists a substantial pool of long-term financial savings gathered by commercial banks and provident and pension funds that can be committed to long-term financing.

On the whole, the institution-building part of developing the financial structure has been done with in most of the SEACEN countries. The task that needs to be dealt more by the authorities and the financial institutions is the development of a variety of financial instruments that could meet the needs of savers and borrowers in terms of size, currency denomination, maturity and marketability. The implications on monetary policy of the above-mentioned features of the financial structures of the SEACEN countries are discussed in the following sections.

The Dominance of Commercial Banks

Despite the emergence of other types of financial institutions in the SEACEN countries, commercial banks still dominate in their financial structures. In view of this, the commercial banks continue to be the primary institutions used or targetted by the authorities in implementing monetary policy. Since they are the chief generator or depository of money (narrowly or broadly defined) and they are the largest source of credit, the monetary authorities in the region direct their demand management or savings generation measures principally to the commercial banks.

The relatively high level of sophistication and maturity of commercial banks in most of the SEACEN countries have also given

their financial markets a good degree of integration which helps in the speedy and even transmission of monetary policy. From the commercial banks emerged the interbank funds market where the temporary liquidity needs of individual banks are met. The existence of this sub-market does not only ease the pressure on the central bank as a source of funds but also provides the monetary authorities a good indicator of the liquidity position of commercial banks. In particular, the interest rate from the interbank transactions is a result of the workings of supply and demand for very short-term funds and is therefore a useful indicator for the authorities in formulating monetary policy. Moreover, the volume of activity in the interbank funds market gives the central bank a gauge of the impact of its policies. The existence of an interbank funds market can be related to the degree of development of a country's financial structure in the sense that such a market is more likely to emerge and flourish if there are more participating commercial banks and they are active in the financial intermediation business. The high degree of development of commercial banking in Singapore, Malaysia, the Philippines, Thailand and, to a certain extent, in Sri Lanka has made it possible for an active interbank funds market to emerge which have enhanced monetary policy formulation in these countries.

The dominance of commercial banks in the SEACEN countries also accounts for the greater control of the central bank on their credit operations as compared to other financial institutions. The intervention of the authorities in their operations has been impelled largely by the tendency of commercial banks to concentrate on trade financing and in short-term maturities as well as to their concentration in the urban areas. Because of these, they do not have direct relationship with and immediate impact on the rural segment of the population which comprised the majority in all of the SEACEN countries except Singapore. Thus, the scope of transmitting monetary policy through commercial banks in these countries can be said to be limited up to the extent of the geographical areas and field of financing they cover. That monetary policy conducted through

commercial banks does not have as much impact and coverage than what could be attained is heightened by the fact that the other financial intermediaries dealing with the rural sector, principally the development and rural banks, do not depend on commercial banks for funds.

However, in some SEACEN countries, particularly in the Philippines and Sri Lanka, the strong position of the commercial banks is taken advantage of in developing the rural sector. While it is true that the branches of private commercial banks are hardly found in the rural areas of these countries, government-owned commercial banks which are also the biggest financial institutions in the Philippines and Sri Lanka have pioneered in penetrating agricultural and rural areas. The Philippine National Bank and Sri Lanka's, the People's Bank and to a certain extent, the Bank of Ceylon, extend loans to the agricultural sector through their branches.

A case for a more diversified financial system

Recent developments have shown that as the financial sectors of the SEACEN countries continue to move forward in the path of development, other types of financial institutions are gradually taking a larger share in the task of financial intermediation. In Singapore, Malaysia, the Philippines and Thailand, finance companies are expanding at an accelerated pace, at a rate much faster than it took the commercial banks to reach their prominent stature. This development augurs well for a financial structure which is composed of a variety of equally-strong financial institutions. One consequence of a complex financial network is enhanced competition among financial institutions which will redound to the benefit of the consumers. This can be illustrated with the experience of Singapore on housing loans. Commercial banks used to have an aversion to consumer credit and housing loans and this was reflected in their negligible shares to their total portfolio. However, when the Post Office Savings Bank introduced a housing loan scheme, commercial banks, under the pressure

of competition began to take a more favourable attitude towards housing loans. Singapore also had the same experience with finance companies which used to specialise in hire-purchase finance of motor vehicles and other consumer durables. Due to the competition posed by other financial institutions in the face of a shrinking market, finance companies have no alternative but to diversify their loan portfolio.

The diversification of the structure of the financial systems of the SEACEN countries has enhanced the process of financial intermediation. Surplus units could now turn to a number of financial institutions that could provide them financial instruments that differ from those issued by deficit units. Likewise, borrowers could choose among a number of financial institutions that could satisfy their specific preferences, a situation which is hard to achieve if they turn directly to ultimate lenders. In both saving and borrowing transactions, the transformation of funds made by financial institutions have made it attractive for both parties to pass through an intermediary. Thus, the existence of more financial institutions in the SEACEN countries is a positive contribution towards increasing the access of non-financial units to the organised financial structure. From the point of view of the monetary authorities, the higher the dependence of non-financial units on financial institutions the greater is their influence on the liquidity situation as they could change the mode of operation of these institutions according to intended monetary objective. The number of head offices and branches of financial institutions in the SEACEN countries as shown in Table 2 have increased, more significantly in the rural areas, so that the financial institution to population ratio has improved over the years. In sum, to the extent that a greater number of financial institutions could satisfy the varied needs of a greater number of savers and borrowers, then it can be said that there will be a speedier and more effective transmission of monetary policy.

Concentration of Financial Instruments

Some changes in the structure of financial instruments in the SEACEN countries have led to a closer look of some basic principles underlying monetary management. Growth in currency and demand deposits or M1 has been decelerating or even registering absolute decreases. This means that in an expanding economy, there has been a more efficient use of money, and for the monetary authorities, this amounts to increased velocity of money. To a certain extent, the decline in M1's growth in the SEACEN countries with more developed financial systems could be traced to increasing use of electronic funds transfer systems and the change in payments habit of the general public, that is, more use of credit cards instead of cash. More importantly and this is true for all of the SEACEN countries, there has been a significant shift of preference for interest-earning deposits. The bulk of financial savings in the region are now in the form of savings and fixed deposits. As a result of this, there has been a reexamination of what constitutes money supply in the SEACEN countries and what monetary aggregate is more appropriate for targetting purposes. To date, the broader definition of money or M2 is the preferred aggregate for liquidity control purposes among the South-East Asian central banks. In view of this, an increase in the velocity of M1 is not readily interpreted as a sign of inflationary expectations as this may be brought about by a shift from narrow money to quasi-money, which means a lower velocity for M2. The experience of Malaysia along this line can be cited.

The growing sophistication of the financial system and the increasing monetisation of the economy of Malaysia have made the public in recent years more sophisticated and increasingly more sensitive to interest rate changes and the opportunity cost of capital. 9/ This has made the demand for money function more

9/ Bank Negara Malaysia, Annual Report 1984, p. 18.

interest elastic in the face of the shifts in liquidity preference. In the past, narrow money (M1), had demonstrated a stable and consistent relationship with economic growth. In recent years, however, there had been a definite and unmistakable shift out of non-interest earning M1 to interest-sensitive fixed deposits with commercial banks, finance companies and merchant banks. These near substitutes for narrow money, demonstrated that a broader concept of money is needed to replace M1 as the principal monetary aggregate to manage in the conduct of monetary policy in Malaysia. In this regard, the broader definition of money, namely, private sector liquidity or M2 (M1 plus fixed and savings deposits of the private sector with the banks) and its broader equivalent, M3 (M2 plus fixed and savings deposits with the finance companies, merchant banks and discount houses), have assumed increasingly greater significance in terms of a stable and predictable relationship with underlying economic activity. While the behaviour of all three aggregates, M1, M2 and M3, are being closely monitored, increasing emphasis is being placed on the significance of M2 and M3 as the intermediate "targets" of monetary management.

The concentration of financial assets in the form of bank deposits also raises another monetary policy implication. With only deposits as the most attractive form of financial savings in most of the SEACEN countries, it is to be expected then that wealth owners could easily switch to investing in real assets like land, houses, consumer durables and agricultural commodities, especially in times of inflation. If such a situation predominates, the demand for money in these countries is responsive to the expected rate of inflation. From the point of view of monetary policy formulation, this preference for real assets over financial assets means a limited area for manoeuvring, particularly on the choice of policy tools.

Viewed from the asset side of the financial institutions, the dominance of loans in their claims is a reflection of the unpopularity of issuing equity shares as an alternative means of

financing. This characteristic of the SEACEN countries' financial markets is discussed below.

Underdeveloped Equity Market

The equity market in the SEACEN countries is very small and underdeveloped compared to the loans or borrowed funds market. The seven SEACEN countries with private enterprise and mixed economies have stock exchanges and yet few companies are encouraged to list on these exchanges and only a small portion of the surplus units invests in shares. Even direct public offering or selling of corporate shares directly to investors is rare. The reasons behind the underdeveloped state of the stock market are not within the scope of this study but such degree of development has implications for monetary policy since it points inevitably to the loans market as a source of external and indirect financing. The overdependence on the loans market as a source of financing encourages credit rationing where only established and big business concerns are favoured. Although credit rationing has not been formally undertaken in any of the SEACEN countries, its semblance can be seen in the credit preference given to large and established firms while little access is given to medium and small scale enterprises, especially in times of tight domestic liquidity. The limited access of the agricultural and small sectors to the formal credit market has significantly affected monetary policy formulation in most of the SEACEN countries, and this aspect will be discussed in the latter part of this section.

Moreover, an economy which depends on the loans market in raising funds tends to call for a heavy role of the central bank in providing the credit needs of the economy. This can be seen in the rediscounting windows of most of the South-east Asian central banks which operate in a manner different from those in developed countries, an aspect which is discussed separately in this section of the study.

Harnessing Available Long-Term Funds

Monetary and interest rate policies in the SEACEN countries have been geared, among others, towards increasing the availability of long-term funds to meet the investment demands of the economy. To a certain extent, the monetary authorities have succeeded in attaining this objective as fixed deposits now form the larger portion of the liabilities of financial institutions in the SEACEN region. Even the commercial banks which traditionally have demand deposits as their major liabilities have fixed deposits now as their principal liabilities. Moreover, even without resorting to a high interest rate policy to attract financial savings, the funds gathered by contractual savings institutions like provident and pension funds and insurance companies are substantial. What is stressed here is that the definition of available long-term funds does not rest so much on the legal stipulation regarding maturity but more on the interval between deposit and withdrawal or between issuance and retirement of a funds contract. With this delineation in mind, there exists in the SEACEN countries a core of long-term funds that could be lent to longer periods as required by investors.

It seems that the constraint for long-term funds lies in their disposition. For one, the commercial banks which are the main depository of long-term deposits do not necessarily loan out these funds into long-term maturities. To compel commercial banks and other financial intermediaries to set aside more of their loan portfolios into the long-term, some central banks in the region have required them to lend specific amounts for housing and other productive activities. On the other hand, the government's specification of the form in which gathered funds of contractual savings institutions can take, has also ironically hampered the flow of their long-term funds to the business sector. These contractual savings institutions, be they administered by the government or the private sector, are obliged to invest their funds largely in government securities, which in effect means funding the public sector.

It appears that the government's response to the perceived dearth of long-term funds has leaned more towards establishing development banks and other long-term financing institutions. Almost all of these types of institutions are being funded by the government since their deposit-taking activities, if at all undertaken, are small. Moreover, the performance of some of these institutions in a few of the SEACEN countries has not been satisfactory, particularly in their choices of activities to be provided with long-term funds and in the recovery of loaned-out funds. The mismanagement of some of these intermediaries has threatened the viability of these institutions and to keep them from falling apart, the government has to continually provide them budgetary assistance. In most instances, funding the operations of these institutions have strained government resources, leading to huge budget deficits. The experience of one or two of the SEACEN countries has shown that these budget deficits were directly financed by the central bank as the underdeveloped government securities market cannot raise enough funds to cover such financing gap. This only created a situation where the fiscal and financial sectors continually depend on each other for funds.

A review of this fiscal-monetary chain is worth undertaking if the delivery of long-term funds to the investing sector is to be improved. This may include the use of fiscal measures to increase long-term funds, strengthening the deposit-gathering activities of long-term financial institutions and gearing their operations towards market conditions.

Monetary Instruments Employed

The situations and conditions prevailing in the financial sectors of the SEACEN countries with respect to dominant institutions, preferred financial instruments, and the stage of development of the money and capital markets make their central banks rely extensively on the direct and selective type of monetary policy instruments. These instruments are aimed at controlling the activities of financial

institutions not through the market mechanism but via certain requirements imposed on them, thus directly affecting their capacity to extend credit. The monetary policy instruments employed can be grouped into two: one is regulation of financial institutions' liquidity by imposing reserve requirements thus affecting the money multiplier, and the other, direct credit portfolio regulation and other selective credit controls which affects reserve money.

Reserve requirements

Requiring banks to set aside a fixed percentage of their deposit liabilities as reserves, usually in the form of cash and other acceptable assets, is one of the most common means of controlling bank's liquidity. All of the South-East Asian central banks impose reserve requirements on banks and on some other financial intermediaries. It is a very easy and simple instrument to implement and its impact can be very powerful or ineffective depending on the reserve position of financial institutions. Changing the reserve requirement can have an immediate and powerful impact if the financial system has little cash reserves. This is more applicable to countries with highly-developed money market where banks or other financial institutions have greater choices of investment outlets and therefore they tend to minimise their holdings of non-earning assets. In the case of countries with less developed money markets, banks may hold large amounts of excess liquidity thus making the reserve requirement effective. Moreover, this instrument cannot be used frequently and at a short notice as it entails drastic changes in individual bank's policies and a rearrangement of their balance sheets. In view of its inflexibility, and the relatively high cost of ensuring its compliance, central banks in the region prescribe changes in the reserve requirement sparingly. This infrequent change, in effect, makes reserve requirement more of an instrument in reallocating banks' assets rather than controlling their credit capability.

Illustrative cases of the effectiveness of changing the reserve requirement can be cited in Malaysia and the Philippines which have well-developed money markets. The reserve requirement was actively used for monetary regulation in Malaysia between the period of 1972 and 1978, with the objective of increasing or decreasing loanable funds. The reserve ratio was raised from a level of 5 per cent which had been in force since July 1969 to 8.5 per cent in October 1972. Another upward change was made in January 1974. Since then, the ratio had been reduced in four steps to settle at 5 per cent by December 1978. Based on the experience of Bank Negara Malaysia from 1959 to 1984, the present reserve ratio could precipitate a contraction in the supply of money by about 5 percentage points. In the Philippines, the immediate impact and effectiveness of changing the reserve requirement was made into full use in 1984 and 1985 when the country was faced with very high domestic liquidity and an inflation rate as high as 50 per cent. Thus, as part of the remedial measures, the monetary authorities made relatively big changes in the reserve ratios at successive intervals.

Direct and selective credit controls

The use of direct and selective credit controls by the monetary authorities in the region is very extensive. The dependence of most of the South-East Asian central banks on these instruments is due largely to the limited participation of financial institutions in financing areas deemed desirable by the authorities. To some extent, the reliance of financial institutions on the central bank for funds can also be traced to their underdevelopment, particularly in their role as funds mobiliser. Thus, both factors make financial institutions depend regularly on the rediscounting window of the central bank.

Direct and selective type of monetary policy instruments employed by all of the South-east Asian central banks, except the Monetary Authority of Singapore which no longer makes use of them,

include those which are traditionally viewed as general instruments of monetary policy but are so designed so as have more selective impact. For instance, the rediscounting windows of these central banks do not operate mainly in the orthodox manner, that is, as a "lender of last resort." Instead, the rediscounting or refinancing facility is converted into a source of low cost funds for priority sectors. Another direct and selective type of monetary measure employed is the one requiring banks to set aside a certain percentage of their loan portfolio to selected activities. Lastly, despite the deregulation of interest rates in all the SEACEN countries, with the exception of Burma and Thailand, the monetary authorities in the region still set ceilings on the cost of credit for certain activities. These three selective credit policy instruments of South-east Asian central banks are discussed below.

Preferential refinancing or rediscounting

The refinancing or rediscounting facilities of the central banks of Indonesia, Nepal, the Philippines, Sri Lanka and Thailand also function as credit allocation mechanisms. These credit windows operate under an incentive scheme where preferential or concessional interest rates and higher refinancing values/quotas are given to commercial banks which rediscount papers or collaterals evidencing lending to preferred sectors and activities. On the other hand, Bank Negara Malaysia and the Monetary Authority of Singapore provide rediscounting at preferential rates to export bills only.

The refinancing or rediscounting schemes for priority sectors of the South-East Asian central banks share the following important features:

- 1) Loan values of paper presented for rediscounting are higher for those which financed priority areas, even amounting to 100 per cent of the paper being rediscounted.

2) The refinancing rates for priority lendings are below the prevailing market interest rates.

3) To ensure that the low rates are passed on to the ultimate borrowers, maximum lending rates or permitted margins/spreads of commercial banks are prescribed by the central bank. This means that interest rates on lendings to priority activities are still controlled despite a deregulated interest rate policy adopted in Indonesia, Malaysia, Nepal, the Philippines and Sri Lanka.

4) Refinancing is always made available to priority areas even up to the extent of exempting them from the impact of contractionary credit stance adopted or excluding lendings to these sectors from any credit ceilings imposed on commercial banks.

The financial institutions under the preferential rediscounting scheme essentially seek out, evaluate and accumulate eligible financial assets, and rediscount them with the central bank which holds such assets until maturity. In this situation, rediscount rates charged by the central bank to financial institutions are lower than the rates which the latter charge to their ultimate borrowers. In effect, the central bank remunerates the financial institutions for the service of collecting the rediscountable papers that the central bank will subsequently take over. As long as rediscounting with the central bank is profitable from the point of view of financial institutions, it will tend to be fully or almost fully automatic. In short, an underdeveloped money and capital market tends to promote the use of rediscounting, not for stabilisation purposes as done in more developed countries but more as a primary source of credit at concessional interest rates.

The main objection to preferential rediscounting is that it is inflationary since liquidity coming from the central bank is far more high powered than from any other source. This underscores the fact that rediscounting, particularly in Indonesia, Nepal, the

Philippines, Sri Lanka and Thailand, works at best in increasing credit, not in reducing it. In addition, their central banks have to stand by their announced rediscount rates and quotas for some time before they can be revised again. Furthermore, the preferential rediscounting scheme as borne out by the experience of some central banks does not encourage the funds mobilisation role of financial institutions as the central bank is a more convenient fund source. Another drawback of rediscounting if it is meant as a source of funds for priority areas is that it is a passive credit instrument. Only financial institutions with limited funds, which are usually the small ones, could act as partners of the central bank in providing credit to priority areas. Financial institutions with excess reserves or sufficient funds of their own, like the commercial banks, can choose their own areas of financing which may not be along priority lines. Moreover, preferential rediscounting, together with other selective credit controls represent direct central bank intervention in the financial market. Recent policy moves of the monetary authorities in the region, as reflected in the deregulation of interest rates and blurring of functional distinction among financial institutions, point to their desire to let market forces operate in the mobilisation and allocation of funds. The continued resort to non-market determined policy instruments will only hamper the full attainment of the benefits of financial liberalisation and deregulation. Lastly, direct and selective credit allocation techniques require substantial manpower and involve high administrative cost since they can only be effective if their compliance is carefully monitored and evaluated.

Despite its limitations, preferential rediscounting as a monetary policy tool is still extensively used though not by design or preference of the monetary authorities in the region. It is more of the imperfections existing in their financial markets that make them turn to this non-market oriented monetary policy instrument. As their financial structures become more sophisticated, the monetary authorities would be able to employ rediscounting as a traditional instrument whose impact is more aggregative rather than selective.

Direct regulations on banks' credit portfolio

These take the form of preemptive uses of credit along specified sectors, or requirements to commercial banks to set aside specific portions or amounts of their credit to certain sectors. Direct regulations on the credit portfolio of commercial banks are prescribed in Malaysia, Nepal, the Philippines and Thailand. On some occasions, directives are also issued to commercial banks aimed at restricting credit to specific activities, such as the importation of non-essential commodities.

One of the most prominent direct monetary policy instruments of Bank Negara Malaysia takes the form of annual lending guidelines to commercial banks and finance companies. These guidelines provide that at least a certain percentage of their outstanding loans have to be extended to priority sectors to ensure that they have ready access to credit at reasonable cost. The first set of guidelines was issued in 1974 as part of a package of monetary and fiscal policies to control inflation. The latest lending guidelines which were issued by Bank Negara Malaysia in March 1986 still gave preference to the sectors and activities identified in 1974, namely, the indigenous community, low cost-housing, agricultural food production and small scale enterprises.

In Nepal, commercial banks have to extend at least 25 per cent and 8 per cent of their total loans to the productive and priority sectors, respectively. Moreover, commercial banks have to invest at least 15 per cent of their total investment portfolio to long term-purposes. Considering the fact that the commercial banking system of Nepal is virtually its entire organised financial sector, these directives truly have broad coverage.

All banks in the Philippines are required to allocate at least 25 per cent of their loanable funds for agricultural credit, of which not less than 10 per cent shall be made available for agrarian

reform credit. All banks have to comply also with another measure which requires that at least 75 per cent of the total deposits gathered in a region should be loaned out or invested in the same area.

The Bank of Thailand requires commercial banks to extend credit of at least 13 per cent of their total deposits to the agricultural sector. Two measures with credit allocation impact are also tied up with granting branching permits to commercial banks, namely, at least 60 per cent of total credit of new branches should be extended to residents of that location and, at least 30 per cent of their total credit must be granted to farmers.

The Central Bank of Sri Lanka prepares an annual credit plan and, through moral suasion, expects commercial banks to adhere to the allocation of credit to different sectors which is specified therein. The plan also prescribes ceilings on credit to non-priority activities, particularly on importation of non-essential commodities.

Interest rate ceilings

Apart from the prescribed maximum interest rates to be observed by banks when relending proceeds of central bank refinancing, interest rate ceilings on loans extended by commercial banks to certain sectors and classes of borrowers are also set. The maximum rates apply to loans sourced by the banks themselves and are normally set below the general prescribed rate, in case of a regulated interest rate policy or below the prevailing market rate, for those countries under a floating interest rate regime.

In Indonesia, credit to high priority activities, particularly those extended by the state banks, are obtained below market rates despite the deregulation of interest rates. In addition to extending credit to priority sectors, commercial banks and finance companies in Malaysia have to observe the maximum interest rates

prescribed on such loans by Bank Negara Malaysia. These ceiling rates are, however, reviewed regularly and corresponding adjustments, if warranted, are made.

The Nepal Rastra Bank prescribed 10 per cent and 14 per cent interest rate limits on working capital loans for cottage and rural industries with fixed capital of Rs. 200,000 and over Rs. 200,000, respectively. To boost exports, the cost of credit in financing export trade is kept low. The loss of commercial banks on export loans is being compensated by the Nepal Rastra Bank.

Interest rates in Thailand are regulated. Thus, lending rates of commercial banks to priority sectors like agriculture, industry and exports are kept lower than those prescribed for regular lendings. Adjustments to these ceilings are made from time to time. For example, on March 6, 1984, the Bank of Thailand raised the maximum lending rates of commercial banks and finance companies by 1.5 percentage points to 19 per cent and 21 per cent, respectively. However, the ceiling rate on lending to the three priority sectors was maintained at 17.5 per cent.

On the whole, the direct intervention of the central bank on the credit portfolio of banks and the setting of interest rate ceilings on certain lendings so as to increase the flow of credit to priority sectors is being questioned, not only by the affected banks but by economists as well. The criticisms centre on their effectiveness, their distortion effect, the question of fairness and the high administrative cost involved in their enforcement.

Rediscounting at penalty rates

In some of the SEACEN countries with more developed money markets, if not an active equity or bond market, the financial institutions' dependence on the central bank for funds is less prominent. They would tend to turn to the central bank as a last

resort and funds could be obtained at higher than the market or penalty rate. Thus, the central bank or the monetary authority tends to move from the centre to the periphery of the money market, that is, it fulfils more of its supervisory role rather than as a primary source of funds. It becomes the occasional lender of last resort, at penalty or above-the-market rate, rather than the normal source of credit to the banking system. Under this situation, the rediscounting facility takes its traditional role in the conduct of monetary policy and the central bank's direct involvement in credit extension is relatively small. Other financial markets notably the money market and the interbank sub-market emerges.

The foregoing, again, points to the importance of a diversified financial market in transforming the rediscounting window of the central banks into a lender of last resort. It calls for the existence of a number of developed financial sub-markets offering funds at various maturities and at competitive rates so that financial institutions only turn to the central bank when all other sources have been exhausted. Under this situation, the central bank could move effectively exert its intended impact on the liquidity situation. In the SEACEN region, those countries with more developed financial structures, notably Singapore and Malaysia, have rediscounting windows which operate more as "lenders of last resort" while banks' access to concessional rates to the central bank is limited to export refinancing. In the other countries, the central bank rediscount window also stands ready to meet the temporary liquidity needs of banks but it is more actively used as a primary source of funds in financing a number of priority areas.

Monetary Policy in Singapore

There is no doubt that Singapore has the most developed financial structure among the eight SEACEN countries. This leads to the expectation that monetary policy in Singapore can be conducted more easily and effectively compared to the other seven countries with

less developed financial structures. On the contrary, monetary policy is conducted differently in Singapore not because of the high degree of development that its financial system has attained but more from the fact that it has a very open economy and its financial system does not only serve the republic but also the rest of the world. These, in addition to the relatively underdeveloped state of its capital market, have in fact made it difficult for Singapore to rely on traditional monetary instruments or money/interest rate targetting in demand management. Instead, demand management in Singapore is undertaken mainly through fiscal and financial policies of the government, institutionalised essentially in the Central Provident Fund (CPF). Monetary policy plays a complementary role and is carried out mainly through the exchange rate.

For instance, due to the contractionary impact of CPF contributions and government budget surpluses, foreign exchange interventions of the monetary authorities have generally been geared towards moderating the appreciation of the Singapore dollar and injecting liquidity into the banking system. In this manner, the money supply in Singapore is a result of the exchange rate policy. Moreover, the foreign multinational companies which dominate the Singaporean economy have recourse to foreign financing, thus traditional monetary measures aimed at stemming the inflow of money attracted by exchange and capital gains were largely not successful as experienced during the inflationary period in early 1973. Lastly, the high degree of development that the Singapore financial system has attained has raised problems of insulating the domestic economy from the offshore activities of financial institutions operating in the republic. Due to the absence of exchange control barriers between the domestic money market and the foreign exchange market, domestic interest rates are largely determined by external interest rates. Thus, the Monetary Authority of Singapore has to take steps to limit the internationalisation of the Singapore dollar in order to maintain its control over domestic liquidity.

In short, while a financial structure geared to the rest of the world like Singapore invariably develops into a highly developed and sophisticated one, some difficulties and trade-offs in monetary policy formulation could be encountered by the authorities.

Use of Indirect Monetary Instruments

Indirect type of monetary policy instruments like changes in rediscount rate or open market operations are not actively used in the SEACEN countries because they are more likely to produce less effective results. As shown earlier, the rediscount window in the SEACEN countries operates differently from that of industrialised countries so that no single or dominant central bank discount rate emerges that could give an indication of the monetary policy stance of the authorities. In effect, changing the central bank rate is not one of the major policy instruments of most of the central banks in the region.

Another indirect type of monetary policy instrument is open-market operations which is described as more flexible and "smoother" compared to other intervention tools. In contrast to rediscounting where a central bank trades financial assets with banks only, open-market operations can be conducted with other financial institutions as well. Open-market operations is also deemed more flexible since the central bank can be a seller and buyer, whereas in rediscounting it can only be a buyer. Moreover, the decision to trade in financial papers is taken by the central bank while in rediscounting, the central bank has to passively wait for sellers of financial assets. Lastly, an open-market transaction is concluded at the going rate of the money market while rediscounting is consummated at the central banks's announced rediscount rate. Compared to a change in reserve requirement, open market operations can be conducted in a less disruptive and destabilising manner. It does not have the loud announcement effect of a change in reserve requirement and it can be immediately implemented.

With all the above-cited advantages of open-market operations, the question arises why central banks in the region do not use such monetary tool extensively. The answer to this is highly related to the degree of development of a country's financial structure. An indispensable prerequisite of effective open-market operations is the existence of a broad and active financial market where financial instruments with varying maturities, not only short term, are actively traded. The existence of a sufficient volume of financial instruments is necessary to enable the central bank to sell and buy securities in appropriate amounts in order to exert the desired effect on commercial bank liquidity, and at the same time absorb these transactions without excessive price fluctuations. The results sought by open market policy must be capable of achievement by relatively gentle means, and should not be obtained at the expense of serious disturbances in the money or capital market.

The financial instruments available in the SEACEN countries are not as varied yet, be it in terms of forms, maturities and marketability. The financial instruments have not attained a sufficient level so as to allow the central banks in the region to actively make use of open market operations. The government securities market which usually serves as the medium through which open market operations can be conducted is narrow and limited in the SEACEN countries. As already cited, these government securities are held by "captive" financial institutions, mainly in fulfilment of certain statutory requirements. Despite this, the central banks in the Philippines, Sri Lanka and Malaysia have been making use of open-market operations in their conduct of monetary policy. In particular, the issuance of central bank securities in the financial markets of the Philippines and Sri Lanka was aimed at providing their monetary authorities with instruments through which open market operations could be conducted. The central bank securities in these two countries were first issued in 1970 and 1984 to mop up the excess liquidity brought in by export earnings during those years. With the passage of time, the terms and other features of Central Bank

Certificates of Indebtedness (CBCIs) in the Philippines have been designed so as to reflect changes in market conditions, and thereby make them suitable open market instruments. Moreover, open market operations of the Central Bank of the Philippines were not confined to selling securities to mop-up excess liquidity. On appropriate situations, it has also entered into repurchase transactions with banks, that is, buying back the securities it has previously sold before their maturity, in order to inject liquidity into the financial system.

VII. CONCLUSION

The extent of the development of the financial structures of the SEACEN countries and their experience in monetary policy formulation was seen in the preceeding sections of this study. From the institutional infrastructure side, it was observed that the SEACEN countries present some differences in orientation and development - from the monolithic banking system of Burma and the virtually one-office-for-every-basic-type of financial institution in Nepal to the complex network of highly specialised financial intermediaries with strong international links in Singapore. Falling within this wide spectrum of development are, on the one hand, the financial structures of Malaysia, the Philippines and Thailand and on the other, those of Indonesia and Sri Lanka. The first group have almost the same types of financial institutions that exist in Singapore. In Singapore, Malaysia, the Philippines and Thailand other financial institutions which do not raise or lend funds but are engaged in services which enhance and improve on the process of financial intermediation can also be found. These consisted of the brokers and dealers in financial instruments and the financial and commodity exchanges which make financial instruments more attractive asset-holdings, particularly in terms of their distribution or delivery, liquidity and marketability. The financial infrastructures of Indonesia and Sri Lanka were not as complex and they reflected the heavy role of the

government in running the financial institutions themselves or in setting up the foundation of the financial structure. However, in all the countries, the position of the central bank in terms of concentration of assets, has been declining. This indicates the presence and emergence of other types of financial institutions whose resources have been increasing and points to their expanding role in financial intermediation through time.

The active role of the South-east Asian central banks in establishing and promoting new financial institutions also speaks of the adherence to the supply-leading approach in financial structure development. While the emergence of commercial banks and finance companies in the SEACEN countries may be generally categorised as a demand-following phenomenon, that is, the expansion in their economies led to increased needs for the services of these types of institutions, a more deliberate approach was followed in the development of other financial institutions. Thus, rural banks, development banks and other long-term financial institutions in the SEACEN countries were introduced by their governments or central banks to exert a causative influence on economic growth.

On the financial instruments side, all of the SEACEN countries have evolved from the dominance of currency as the major financial asset to the popularity of interest-earning deposits. However, there is a need for variety in the types of financial instruments in order to give financial savers and borrowers more choices in terms of maturity, marketability or negotiability. Specifically, the issuance of more bonds and other long-term securities will add breadth to the financial markets of the SEACEN countries.

On the whole, the degree of development that has been attained in the institutional set-up of the financial structures of the SEACEN countries can be said to be suited to their economic circumstances and desired orientation of their financial markets. The

next imperative in the task of developing the financial structures of the SEACEN countries is, therefore, to make available more financial instruments, particularly those with long maturities and secondary markets. The underdevelopment of the financial instruments has influenced the conduct of monetary policy in the region. Monetary policy instruments which have more general or aggregative impact are used in a more limited manner in view of this. The impact of open market operations, if used at all, is not expected to be transmitted widely in view of the limited availability of financial instruments that can be traded. Thus, a number of central banks in the SEACEN region still rely on more direct type of monetary policy instruments to influence the availability and cost of funds. However, such direct instruments as selective credit policies and interest rate and credit ceilings are not without welfare cost, not to speak of their actual efficacy. Thus, it can be said that the monetary authorities in the SEACEN region would like to see a further development of their financial structure so that they can rely more on the general and market-oriented type of monetary policy instruments.

The central banks in the region have taken an active part in financial instruments development. This can be illustrated by the central banks of Indonesia, Malaysia, the Philippines and Sri Lanka which issued their own bonds in their financial markets. These central bank bonds were issued not only to increase the financial instruments available in the market but also to serve as tools in achieving stabilisation goals. The South-East Asian central banks have also taken a liberal and more receptive attitude on the new financial instruments issued by private financial institutions. Some central banks have also provided incentives to banks to mobilise long-term deposits by imposing a lower reserve requirement on these liabilities and in the case of countries with administered interest rates, by prescribing higher interest rates for them.

The important role of interest rates in increasing and diversifying financial instruments in the SEACEN countries has been

recognised as reflected in the deregulation of interest rates in six of the eight countries in the region. Thus, the monetary rewards to investing in financial assets as well as the cost of regular borrowing are determined by market forces in Indonesia, Malaysia, Nepal, the Philippines, Singapore and Sri Lanka. The Bank of Thailand, on the other hand, is constantly reviewing its administered interest rates and revisions on the prescribed ceilings have been made to keep them in step with international developments as well as to achieve certain economic and financial objectives. In other words, the central banks in the region have the statutory power to influence the level of financial savings and the volume of funds borrowed through financial institutions. An active use of interest rate policy by the central bank could have far-reaching effects in promoting the development of their financial sectors.

Another aspect which is important to the development of financial instruments and which is within the sphere of responsibility of central banks is the control of inflation. Inflation eats up on the nominal interest rates of financial savings and to the extent that savers do not get positive real returns on their financial assets, investment in them will be significantly affected. This brings to the fore the importance of the price stabilisation objective of the central bank. A stable price level provides a conducive environment for economic development and from a limited point of view, it augurs well for increased savings in financial assets, particularly those with longer maturities.

The supervisory role of the central bank over financial institutions also exerts a crucial influence on the development of the country's financial structure. The business of financial intermediation rests on a very sensitive foundation, public confidence, and an erosion of this confidence is a serious setback not only to the financial sector but to the larger economic system as well. Thus, the financial development of a country and the effectiveness of monetary policy are inextricably linked to the

soundness and stability of the financial institutions. The able performance of the overseer role of the central bank means that surplus units will confidently entrust their savings to financial institutions, thereby ensuring the continuous flow of less inflationary funds to the investors.

In sum, while it is true that there are other factors that bring about the development of a country's financial structure, a number of the more crucial ones are within direct control and influence of the central bank. This then calls for the central bank to take the centre stage in the efforts to achieve greater financial sophistication and thereby make the financial structure an effective channel of its monetary policy measures.

Table 1
ASSETS OF FINANCIAL INSTITUTIONS IN THE SEACEN COUNTRIES
(Percentage Distribution)

	Burma				Indonesia			
	1976	1980	1983		1970	1975	1980	1984
A. Money - generating	76.0	81.4	86.2		95	96	93	91
1. Central bank	54.0	21.7	21.7		47	43	46	40
2. Commercial bank	22.0	59.7	64.5		46	53	47	51
(Myanma Economic Bank)								
B. Development - type	3.9	2.7	1.8		-	1	3	4
1. Myanma Agric. Bank					-	-	1	2
2. Rural banks					-	-	-	-
3. Finance companies					-	1	2	2
C. Others								
1. Foreign Trade Bank	20.1	16.0	12.0		5	3	3	5
TOTAL	100.0	100.0	100.0		-	-	1	-
					-	-	1	-
D. Contractual savings								
1. Insurance companies					-	-	-	-
E. Others (Leasing companies)					-	-	-	-
Total					100	100	100	100

Note: Data or insurance companies not available

Note: A dash (-) sign indicates negligible share.

Table 1 (cont'd.)
ASSETS OF FINANCIAL INSTITUTIONS IN THE SEACEN COUNTRIES
(Percentage Distribution)

Malaysia					Nepal					
	1960	1970	1980	1984		1965	1970	1975	1980	1983
A. Money generating	66.1	59.2	60.9	56.4	A. Money generating	92.0	90.1	84.7	82.6	81.8
1. Central bank	31.4	20.8	17.5	10.8	1. Central bank	71.1	61.9	46.8	39.5	36.5
2. Commercial banks	34.7	38.4	43.4	45.6	2. Commercial banks	20.9	28.2	37.9	43.1	45.3
B. Other deposit-type	7.8	10.1	13.9	17.3	B. Development type	5.5	6.0	10.2	10.0	9.2
1. Finance companies	0.3	4.6	7.6	10.3	1. Agric. Devt. Bank of Nepal	0.6	1.6	6.1	6.4	5.9
2. Merchant banks		-	3.0	3.8	2. Nepal Ind. Devt. Corp.	4.9	4.4	4.1	3.6	3.3
3. Savings bank and cooperatives	7.5	5.5	3.3	3.2	C. Contractual savings	2.5	4.0	5.0	7.4	8.9
C. Development type financial institutions	-	1.1	3.0	2.6	1. Provident Fund Corp.	2.5	3.8	4.6	6.6	7.9
D. Investment type financial institutions	-	0.1	1.1	1.4	2. National Insurance Corp.		0.2	0.4	0.8	1.0
E. Contractual savings	23.5	27.2	18.7	19.1	D. Others			0.1	0.1	0.1
1. Insurance companies	2.9	3.8	3.3	2.9	1. Credit Guarantee Corp.			0.1	0.1	0.1
2. Provident and pension funds	20.6	23.4	15.4	16.2	TOTAL	100.0	100.0	100.0	100.0	100.0
F. Others (discount houses etc.)	2.6	2.3	3.4	3.2						
TOTAL	100.0	100.0	100.0	100.0						

Note : A dash (-) sign indicates negligible share.

Table 1 (cont'd.)

ASSETS OF FINANCIAL INSTITUTIONS IN THE SEACEN COUNTRIES
(Percentage Distribution)

	Philippines					Singapore*				
	1950	1960	1970	1975	1980	June 1984	1970	1975	1980	1984
A. Money generating	100.0	98.3	65.1	64.6	65.1	69.3	78.4	71.1	60.9	55.5
1. Central bank	46.3	44.7	19.5	21.2	20.9	26.1	3.4	14.3	14.7	9.5
2. Commercial banks	53.7	53.6	45.6	43.4	44.2	43.2	10.0	6.5	4.5	3.5
B. Other deposit type	-	0.4	4.8	10.6	11.2	6.2	65.0	50.3	41.7	42.5
1. Finance companies	-	-	-	2.8	3.8	1.7	7.6	7.0	7.5	9.7
2. Savings and Mortgage banks	-	0.3	2.3	1.2	2.3	1.2	6.7	5.0	3.8	4.7
3. Stock SLAs	-	-	0.2	0.3	0.5	0.5	0.9	2.0	3.7	5.0
4. Non-Stock SLAs	-	-	0.1	0.1	0.1	0.1	-	-	-	-
5. Rural banks	-	0.1	2.2	2.3	1.8	1.5	-	-	-	-
6. Investment houses	-	-	-	3.9	2.7	1.2	-	-	-	-
C. Contractual savings	-	-	18.3	9.7	8.7	7.6	14.0	13.8	13.7	16.4
1. Private insurance co.	-	-	5.4	3.4	3.2	2.2	3.3	2.1	1.6	1.5
2. Government insurance co.	-	-	12.9	6.3	5.5	5.4	10.7	11.7	12.1	14.9
D. Development type	-	1.2	10.9	10.4	11.5	12.2	-	-	-	-
1. Devt. Bank of the P'pines	-	1.2	10.1	7.8	8.9	10.0	-	-	-	-
2. Land Bank of the P'pines	-	-	-	1.7	1.9	1.4	-	8.1	17.8	18.4
3. Private devt. banks	-	-	0.5	0.3	0.5	0.8	-	6.4	16.6	16.7
4. Agric. Credit Admin.	-	-	0.3	0.6	0.2	-	-	1.7	1.2	1.7
E. Investment type	-	-	-	-	-	-	100.0	100.0	100.0	100.0
1. Investment companies	-	-	-	3.0	2.2	1.2	-	-	-	-
2. Fund managers	-	-	-	0.9	1.6	0.7	-	-	-	-
3. Venture Capital Corp.	-	-	-	2.1	0.6	0.5	-	-	-	-
F. Others	-	0.1	0.9	1.8	1.2	3.5	-	-	-	-
TOTAL	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0

Note : A dash (-) sign indicates negligible share.

* Excluding ACUS

Note : A dash (-) sign indicates negligible share.

Note : A dash (-) sign indicates negligible share.

Table 1 (cont'd.)

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ASSETS OF FINANCIAL INSTITUTIONS IN THE SEACEN COUNTRIES
(Percentage Distribution)

Sri Lanka

	1950	1955	1960	1965	1970	1975	1980	1984
A. Money generating	84.0	82.0	74.0	66.0	71.0	67.0	80.0	72.0
1. Central bank	34.0	33.0	34.0	32.0	36.0	34.0	37.0	27.0
2. Commercial banks	50.0	49.0	40.0	34.0	35.0	33.0	43.0	45.0
B. Other deposit type	14.0	16.0	15.0	10.0	9.0	13.5	10.0	13.0
1. National Savings	14.0	16.0	15.0	10.0	8.0	12.0	9.0	9.0
2. Rural banks	-	-	-	-	-	0.5	-	1.0
3. Finance companies	-	-	-	-	1.0	1.0	1.0	3.0
C. Development type	2.0	2.0	4.0	2.0	2.0	1.0	1.0	2.0
1. Long term lending institutions	2.0	2.0	4.0	2.0	2.0	1.0	1.0	2.0
D. Contractual savings	-	-	7.0	22.0	18.0	18.5	10.0	14.0
1. Insurance companies	-	-	1.0	7.0	5.0	4.5	2.0	4.0
2. Provident funds	-	-	6.0	15.0	13.0	14.0	8.0	10.0
TOTAL	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0

Note: A dash (-) sign indicates negligible share.

Thailand

	1965	1970	1975	1980	1984
A. Money generating	90.5	89.0	89.3	78.2	76.2
1. Central bank	44.3	36.4	28.7	24.9	17.9
2. Commercial banks	46.2	52.6	60.6	53.3	58.3
B. Other deposit type	8.6	8.7	7.3	16.3	17.0
1. Govt. Savings Bank	8.6	8.7	7.3	4.9	4.9
2. Finance and sec. co.	-	-	-	11.4	10.6
3. Credit finance co.	-	-	-	-	0.4
4. Savings cooperative	-	-	-	-	1.1
C. Development type	1.0	2.3	3.5	5.5	5.1
1. BAAC	0.7	1.7	2.7	3.0	2.3
2. IFCT	0.3	0.6	0.8	0.7	1.0
3. GHB	-	-	-	1.8	1.2
4. Agric. Coop.(ACCOOP)	-	-	-	-	0.6
D. Contractual savings	-	-	-	-	-
1. Life Insurance co.	-	-	-	-	-
E. Others	-	-	-	-	-
1. Pawnshop	-	-	-	-	-
TOTAL	100.0	100.0	100.0	100.0	100.0

Note: A dash (-) sign indicates negligible share.

All data were taken from BOT monthly bulletins of various years, except for 1984 which were based on the country paper.

Table 2

NUMBER OF FINANCIAL INSTITUTIONS IN THE SEACEN COUNTRIES

BURMA

INDONESIA
(Head Office)

1982/1983

	1982/1983			1989				March 1974				March 1979				March 1985			
	Head Office	Branches	Total																
TOTAL	4 ===	152 ===	156 ===																
A. Money - generating	2	1	53																
1. Central bank	1	-	1																
2. Commercial bank (Myanmar Economic Bank)	1	51	52																
B. Development-type (Myanmar Agricultural Bank)	1	101	102																
C. Other bank (Foreign Trade Bank)	1	-	1																
D. Contractual saving (Insurance companies)	n.a.	n.a.	n.a.																
E. Others (Leasing companies)																			

Table 2 (cont'd)
NUMBER OF FINANCIAL INSTITUTIONS IN THE SEACEN COUNTRIES

		PHILIPPINES (Head Office and Branches)				THAILAND 1984		
		1960	1970	1975	1980	June 1984	Head Office	Branches Total
TOTAL					5089	5989	1561	3837
					=====	=====	=====	=====
A. Money-generating					1507	1918	31	1773
1. Central bank	3	4	4	4	4	5	1	4
2. Commercial banks	159	643	996	1503	1913		30	1769
B. Other deposit-type					2279	2299	1196	1660
1. Finance companies	164	556	1407	531	541		104	133
2. Investment houses (merchant banks)	n.a.	n.a.	40	62	49		26	26
3. Savings and mortgage banks	4	56	92	268	210		1065	1065
4. Stock savings and loan ass'n	-	28	69	251	267		1	436
5. Non-stock savings and loan ass'n	-	65	67	71	74		4	436
6. Rural banks	160	507	820	1096	1158		4	74
C. Development-type					239	313	4	74
1. Development Bank of the Phil.	9	84	149	65	67		1	68
2. Land Bank of the Philippines	1	27	57	18	22		1	4
3. NIDC	-	1	1	1	1		1	1
4. Private development banks	1	1	1	1	1		1	1
5. Agricultural Credit Admin.	6	54	86	154	222		1	1
D. Contractual saving					169	169	1	1
1. Private insurance companies	157	174	178	137	136		330	330
2. GSIS	147	150	149	22	23		-	-
3. Social Security System	n.a.	14	19	10	10		-	-
E. Investment-type					74	94	-	-
1. Investment companies	10	10	217	62	65		-	-
2. Fund managers	n.a.	n.a.	23	194	12		-	-
3. Venture Capital Corporation	n.a.	n.a.	-	-	17		-	-
F. Others (brokers, pawnshops etc.)	-	-	-	-	-		-	-
	7	7	630	821	1196		-	-

n.a. - not available

Table 2 (cont'd)

NUMBER OF FINANCIAL INSTITUTIONS IN THE SEACEN COUNTRIES

SINGAPORE

	1970			1975			1980			1984		
	Head Office	Branches	Total	Head Office	Branches	Total	Head Office	Branches	Total	Head Office	Branches	Total
TOTAL	181	215	396	303	290	593	399	383	782	519	480	999
A. Monetary Authorities and commercial banks	===	===	===	===	===	===	===	===	===	===	===	===
1. MAS	39	139	178	72	173	245	99	212	311	131	250	381
2. BCCS	1		1	1		1	1		1	1		1
3. Commercial banks	37	139	176	70	173	243	97	212	309	129	250	379
Full banks	37	139	176	37	173	210	37	212	249	37	250	287
Restricted bank				12		12	13		13	14		14
Offshore banks				21		21	47		47	78		78
B. Other deposit type	36	76	112	37	117	154	35	171	206	35	230	265
1. Finance companies	35	34	69	36	55	91	34	66	100	34	99	133
2. Post Office Savings Bank	1	42	43	1	62	63	1	105	106	1	131	132
C. Contractual saving	88		88	79		79	81		81	90		90
1. Central Provident Fund	1		1	1		1	1		1	1		1
2. Insurance companies	87		87	78		78	80		80	89		89
D. Others	18		18	115		115	184		184	263		263
1. Merchant banks	2		2	21		21	37		37	54		54
2. Discount houses				4		4	4		4	4		4
3. Asian Currency Units	16		16	66		66	115		115	172		172
4. Stock brokers				19		19	21		21	25		25
5. Money brokers				5		5	71		71	8		8

Table 2 (cont'd)

NUMBER OF FINANCIAL INSTITUTIONS IN THE SEACEN COUNTRIES

SRI LANKA

	1970			1975			1980			1984		
	Head Office	Branches	Total	Head Office	Branches	Total	Head Office	Branches	Total	Head Office	Branches	Total
TOTAL	17	259	276	49	1033	1082	67	1323	1390	103	1659	1762
	==	===	===	==	====	====	==	====	====	==	====	====
A. Money-generating	12	166	178	12	563	575	21	616	637	26	651	677
1. Central bank	1	1	2	1	1	2	1	1	2	1	3	4
2. Commercial banks	11	165	176	11	562	573	20	615	635	25	648	673
B. Other deposit-type		90	90	32	467	499	41	683	724	67	943	1010
1. Finance companies				31	-	31	40	-	40	64	-	64
2. Rural banks		90	90		447	447		641	641		888	888
3. National Savings Bank				1	20	21	1	42	43	1	52	53
4. Merchant banks										2	3	5
C. Development-type	3	3	6	3	3	6	3	6	9	3	6	9
D. Contractual saving	2	-	2	2	-	2	2	-	2	4	34	38
1. Insurance Corporation	1	-	1	1	-	1	1	-	1	2	34	36
2. Provident funds (major)	1	-	1	1	-	1	1	-	1	2	-	2
E. Others							-	18	18	3	25	28
1. Leasing companies										3	-	3
2. Foreign Currency Banking Units							-	18	18	-	25	25

Table 3

DEPOSIT LIABILITIES OF COMMERCIAL BANKS
IN THE SEACEN COUNTRIES, 1980 AND 1984
(Percentage Distribution)

	Burma		Indonesia		Malaysia		Nepal	
	<u>1980</u>	<u>1984</u>	<u>1980</u>	<u>1984</u>	<u>1980</u>	<u>1984</u>	<u>1980</u>	<u>1984</u>
TOTAL	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0
Demand	23.4	15.6	52.0	37.6	22.0	17.2	23.6	21.3
Savings	54.3	54.0	5.3	5.1	17.2	11.8	17.0	18.9
Fixed	22.3	30.4	22.3	44.7	57.0	61.7	59.5	55.4
NCDs					3.8	9.2		
Others			20.5	12.6				4.4
- import and government								

	Philippines		Singapore		Sri Lanka		Thailand	
	<u>1980</u>	<u>1984</u>	<u>1980</u>	<u>1984</u>	<u>1980</u>	<u>1984</u>	<u>1980</u>	<u>1984</u>
TOTAL	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0
Demand	25.6	12.5	21.3	17.1	38.2	25.7	13.0	6.1
Savings	42.0	42.3	10.3	17.2	14.4	68.3	13.0	21.2
Fixed	32.4	45.3	65.9	64.2	46.5		72.6	71.6
NCDs			2.0	1.1				
Others			0.4	0.4	0.9	6.0	1.4	0.8
- non-residents								

Table 4

DEPOSIT LIABILITIES OF OTHER DEPOSIT-TYPE INSTITUTIONS, 1984

	<u>Savings Bank</u>	<u>Finance Co.</u>	<u>Rural Bank</u>	<u>Merchant Bank</u>	<u>Co-op</u>	<u>Pte. Devt. Bk.</u>	<u>Specialised Govt. Bk.</u>
Malaysia (\$m)							
TOTAL		12,647.3		4084.8			
Savings		728.3					
Fixed		11,918.6					
NCDs							
Others							
Philippines (mill pesos)					(Stock SLAs)		
TOTAL	6,446.0		3,360.4		1,886.7	2,773.8	9,370.9
Savings	2,993.9		1,960.4		975.3	1,035.8	2,573.5
Fixed	2,810.5		1,377.4		863.1	1,231.9	6,622.9
Deposit Substitutes	547.2					394.5	
Others - demand	94.4		22.6		28.3	111.6	174.5
Singapore (\$m)							
TOTAL	7,287.3	5,278.3					
Savings		209.2					
Fixed		4,655.4					
NCDs							
Others		413.6					
Sri Lanka (Rs. mill)							
TOTAL	10,565.7	2,452.5					
Savings	2,846.9						
Fixed	7,678.2						
NCDs							
Others							
Thailand (mill B)					(BAAC)		(Housing)
TOTAL	43,655.1				13,903.7		5,481.5
Savings	9,966.5				1,126.0		2,953.8
Fixed	32,449.2				3,239.16		2,206.9
NCDs							
Others	1,239.4				9,538.1		320.8

Table 5

FINANCIAL INSTRUMENTS OUTSTANDING IN THE SEACEN COUNTRIES
(Percentage Distribution)

	INDONESIA				MALAYSIA			
	<u>1970</u>	<u>1975</u>	<u>1980</u>	<u>1984</u>	<u>1960</u>	<u>1973</u>	<u>1980</u>	<u>1984</u>
I. Claims	99.9	99.8	99.9	99.7	100.0	67.4	77.9	73.9
A. Claims against financial institutions	49.2	45.7	44.0	43.8	67.5	37.5	40.9	36.3
1. Currency	22.4	13.5	11.0	8.3	20.3	4.8	4.1	2.5
2. Demand deposits	13.7	13.5	14.5	10.9	11.2	5.3	4.3	3.1
3. Other deposits	11.7	15.9	14.0	21.5	17.9	16.4	22.7	21.1
4. Life insurance	-	-	0.4	n.a.				
5. Import deposits	1.1	1.8	1.9	0.5	18.1	11.0	9.8	9.6
6. Borrowings								
Domestic sector	0.9	0.9	0.9	0.9				
Foreign sector	0.3	-	-	-	32.5	29.9	37.0	37.6
7. Securities	0.1	0.1	1.3	1.7				
B. Claims against non-financial sectors	50.7	52.5	23.1	31.4	13.7	13.5	20.6	23.1
1. Loans					1.1	1.4	2.6	1.7
2. Bills					17.7	15.0	13.8	12.8
3. Government securities								
II. Equities	49.8	50.6	20.5	27.6	-	32.6	22.1	26.1
2. Government securities	0.8	1.9	2.6	3.8				
III. Total					100.0	100.0	100.0	100.0
C. Claims against foreign sector	-	1.6	32.8	24.5				
II. Equities	0.1	0.2	0.1	0.3				
III. Total	100.0	100.0	100.0	100.0				

Table 5 (cont'd)

FINANCIAL INSTRUMENTS OUTSTANDING IN THE SEACEN COUNTRIES
(Percentage Distribution)

	NEPAL				PHILIPPINES			
	1965	1970	1975	1980	1984	1950	1970	June 1984
I. Claims	98.8	99.8	99.6	99.7	99.7	100.0	100.0	97.8
A. Claims against financial institutions	40.8	38.5	41.7	44.7	46.3	42.0	41.0	37.6
1. Currency	23.8	19.7	14.6	12.6	12.4	15.3	11.7	5.0
2. Demand deposits	6.3	5.4	6.4	5.6	5.3	18.0	14.1	6.7
3. Other deposits	2.9	6.0	9.9	14.8	16.6	6.7	12.8	13.9
Savings deposits at commercial banks	0.9	2.0	2.7	4.0	5.0	5.8	9.8	9.5
Time deposits at commercial banks	2.0	3.8	7.1	10.5	11.4	0.9	3.0	3.7
Deposits at ADB/N	-	6.2	0.1	0.3	0.1	0.1		0.1
4. Margin deposits	-	0.6	0.6	0.6	1.2			7.4
5. Deposits at MFB	5.1	3.3	2.1	2.3	1.5	1.9	2.2	1.5
Foreign deposits	-		0.8	0.5	0.2	-	-	0.4
Other deposits	5.1	3.3	1.3	1.8	1.2	-	0.2	0.3
6. Other foreign denominated claims	1.3	1.0	4.9	3.8	2.8			-
7. Insurance premiums	-		0.1	0.3	0.5	58.0	59.0	60.1
8. Provident funds	1.4	2.5	3.1	4.7	6.0			
B. Claims against non-financial sectors	58.0	61.3	57.9	55.0	53.4	33.8	40.8	54.5
1. Loans to private sector	15.8	18.6	26.1	24.6	20.4	-	-	44.2
2. Government securities	0.5	1.0	8.4	9.9	15.4	-	-	7.8
3. Other credit to government	5.6	4.1	0.9	0.8	5.4	24.2	18.2	10.8
4. Foreign currency denominated claims	36.1	37.6	22.5	19.7	12.2	-	-	0.2
II. Equities	1.2	0.2	0.4	0.3	0.3			0.5
III. Total	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0

1/ Includes consumer credit

2/ Includes claims of non-financial sectors against other

3/ non-financial sectors

Table 6

FINANCIAL CLAIMS IN THE SEACEN COUNTRIES
(Percentage Distribution)

	<u>Claims of Financial Institutions Against Non-Financial Sectors</u>	<u>Claims of the Non- Financial Sectors Against Financial Institutions</u>	<u>Total</u>
Indonesia			
1970	50.7	49.3	100.0
1975	54.2*	45.8	100.0
1980	55.9*	44.1	100.0
1984	56.0*	44.0	100.0
Malaysia			
1960	32.5	67.5	100.0
1973	44.3	55.7	100.0
1980	47.7	52.3	100.0
1984	50.9	49.1	100.0
Nepal			
1965	58.7	41.3	100.0
1970	60.4	39.6	100.0
1975	58.1	41.9	100.0
1980	55.1	44.9	100.0
1984	53.6	46.4	100.0
Philippines			
1950	58.0	42.0	100.0
1960	59.0	41.0	100.0
1970	70.5	29.5	100.0
1984 June	61.5	38.5	100.0
Singapore			
1975	58.8	38.2**	100.0
1980	59.0	38.7**	100.0
1984	58.7	40.6**	100.0
Sri Lanka			
1965	48.3	51.7	100.0
1970	54.4	45.6	100.0
1975	54.3	45.7	100.0
1980	53.5	46.5	100.0
1984	47.3	52.7	100.0
Thailand			
1967	42.5	57.5	100.0
1980	53.5	46.5	100.0

* Include claims against the foreign sector: 1975 - 1.6; 1980 - 23.1; and 1984 - 31.4.

** Include claims against other non-financial sector (government): 1975 - 3.0; 1980 - 2.3; and 1984 - 0.7.

Table 7

COMPOSITION OF MONEY SUPPLY (M1) IN THE SEACEN COUNTRIES
(In Per cent)

	1970		1975		1980		1984	
	<u>Currency</u>	<u>Demand Dep.</u>	<u>Currency</u>	<u>Demand Dep.</u>	<u>Currency</u>	<u>Demand Dep.</u>	<u>Currency</u>	<u>Demand Dep.</u>
Burma								
Indonesia	62.0	38.0	50.0	50.0	92.1	7.9	91.7	8.3
Malaysia	49.2	50.8	51.5	48.5	43.1	56.9	43.3	56.7
Nepal	69.6	30.4	68.5	31.5	48.7	51.3	44.7	55.3
Philippine	51.3	48.7	46.0	54.0	63.6	36.4	66.4	33.6
Singapore	41.8	58.2	43.7	56.3	45.1	54.9	64.8	35.2
Sri Lanka	47.5	52.5	52.1	47.9	47.4	52.6	48.7	51.3
Thailand	61.0	39.0	63.7	36.3	44.3	55.7	50.9	49.1
					64.2	35.8	68.1	31.9

Table 8
ANNUAL GROWTH RATE IN M1 IN THE SEACEN COUNTRIES
(In Per Cent)

Country	M1					
	Average (1981-85)	1981	1982	1983	1984	1985*
Burma <u>1/</u>	12.7	15.7	7.5	13.0	15.3	12.2
Indonesia	14.9	29.8	9.8	6.3	13.4	15.2
Malaysia	5.6	12.8	13.3	7.7	-0.6	-5.4
Nepal	14.2	11.9	15.3	18.1	13.2	12.6
Philippines	5.9	4.4	0.0	38.3	3.5	-16.8
Singapore	8.4	18.0	12.6	5.5	3.0	2.9
Sri Lanka	16.1	6.3	17.3	25.4	14.1	17.4
Thailand	4.9	2.6	6.8	6.1	11.4	-2.6

* 1985 figures are based on 12 months ending June.

1/ All figures are based on 12 months ending March.

Table 9

**ANNUAL GROWTH RATE IN M2 IN THE SEACEN COUNTRIES
(In Per Cent)**

Country	M2					
	Average (1981-85)	1981	1982	1983	1984	1985*
Burma <u>1/</u>	16.4	20.9	12.9	15.8	17.6	14.7
Indonesia	24.3	26.3	13.9	32.4	22.3	26.8
Malaysia <u>2/</u>	12.7	17.1	16.3	9.4	11.4	9.5
Nepal	18.6	19.1	21.4	20.4	13.0	19.2
Philippines	17.8	20.3	17.7	21.8	14.7	14.1
Singapore	11.9	22.4	15.9	11.9	6.2	2.9
Sri Lanka	20.6	23.1	24.8	22.1	16.6	16.5
Thailand	20.0	16.1	24.1	24.1	20.1	15.8

* 1985 figures are based on 12 months ending June.

1/ All figures are based on 12 months ending March.

2/ M2 is broadly defined to include fixed and savings deposits with the banking system and holdings of negotiable certificates of deposits and central bank deposits.

Table 10
 SHARE OF M1 TO GNP IN THE SEACEN COUNTRIES
 (In Per Cent)

Country	1981	1982	1983	1984	1985
Burma <u>1/</u>	20.9	21.5	21.8	22.9	23.9
Indonesia	12.4	12.3	10.8	10.6	
Malaysia	19.7	20.9	20.5	18.0	17.7
Nepal <u>2/</u>	11.8	11.6	12.1	12.8	13.2
Philippines	7.7	7.0	8.6	6.3	
Singapore	26.2	26.4	24.6	22.3	22.5
Sri Lanka	12.9	12.9	13.6	11.5	
Thailand	9.6	9.6	9.3	9.7	8.9

1/ Data based on period 12 months ending March.

2/ Data based on period 12 months ending June.

Table 11

SHARE OF M2 TO GNP IN THE SEACEN COUNTRIES
(In Per Cent)

Country	1981	1982	1983	1984	1985
Burma <u>1/</u>	26.3	28.3	30.0	32.1	34.3
Indonesia	18.6	19.2	20.9	22.2	
Malaysia	58.0	63.0	62.9	61.7	63.0
Nepal <u>2/</u>	22.6	23.9	26.0	26.8	29.3
Philippines	21.6	23.5	25.3	20.5	
Singapore	71.1	73.8	73.0	68.1	72.2
Sri Lanka	31.6	33.4	34.3	30.3	
Thailand	38.3	44.5	50.4	53.8	

1/ Data based on period 12 months ending March.

2/ Data based on period 12 months ending June.

Table 12

BANK LOANS, BY SECTORAL DISTRIBUTION
(Per cent)

	Indonesia			Nepal *			Philippines			Sri Lanka **		
	1975	1980	1984	1977	1980	1984	1973	1981	1984	1975	1980	1984
Agriculture	8	7	7	27	38	41	6	9	9	14	13	8
Manufacturing and Industry	26	28	35	28	33	48	22	32	29	22	22	25
Trade and Commerce	40	25	34				48	22	16	47	51	50
Services and Utilities	8	12	17	45	29	11	3	5	8			
Finance							12	22	27	4	3	2
Mining	1	24	2				2	5	6			
Others	17	4	5				7	5	5	13	11	15
Total	100	100	100	100	100	100	100	100	100	100	100	100

* Commercial banks' credit to priority sectors

** Commercial banks' credit only

Table 13
FINANCIAL INSTRUMENTS IN THE SEACEN COUNTRIES
BY MARKETABILITY
(Percentage Distribution)

	<u>Marketable</u>	<u>Non-Marketable</u>
MALAYSIA		
1960	38	62
1973	52	48
1980	40	60
1984	41	59
NEPAL		
1965	59	41
1970	56	44
1975	38	62
1980	37	61
1983	32	68
PHILIPPINES		
1960	12	88
1970	24	76
1984	20	80
SINGAPORE		
1970	48	52
1975	53	47
1980	47	53
1984	44	56
SRI LANKA		
1965	58	42
1970	56	44
1975	52	48
1980	44	56
1984	38	62

Table 14

FINANCIAL INTERRELATIONS RATIO IN THE SEACEN COUNTRIES

	<u>1960</u>	<u>1965</u>	<u>1970</u>	<u>1975</u>	<u>1980</u>	<u>1984</u>
Burma				.45		2.16
Indonesia		.14 <u>a/</u>	.21	.37	.43	.52
Malaysia	.62			2.06 <u>b/</u>	2.42	3.98
Nepal		.20	.28	.38	.61	.69
Philippines	.58			1.14		2.81 <u>c/</u>
Singapore			2.55	2.84	4.34	5.44
Sri Lanka	.47	.72	.87	.79	1.12	1.07
Thailand		.89 <u>d/</u>			1.10	

a/ 1966
b/ 1973
c/ June 1984
d/ 1967

Table 15

FINANCIAL INTERMEDIATION RATIO IN THE
SEACEN COUNTRIES

	<u>1960</u>	<u>1965</u>	<u>1970</u>	<u>1975</u>	<u>1980</u>	<u>1984</u>
Indonesia					.47	.61
Nepal				.15	.24	.30*
Philippines					.69	.76*
Singapore				.77	.83	.81
Sri Lanka	.63	.71	.64	.88	.85	.87
Thailand			.33	.39	.35	.34

* 1983

THE FINANCIAL STRUCTURE AND ITS IMPLICATIONS FOR MONETARY POLICY IN BURMA

by
Myint Myint Tin

I. INTRODUCTION

Historical Perspective of the Financial System

Burma's economy is centrally planned. A wide range of economic activities such as agricultural and industrial production, distribution, transportation, external trade and banking are influenced by the public sector. Productive forces are geared according to the socialist plan laid down by the State. In a planned economy, the budget plays a key role in the allocation of resources on a yearly basis among different productive and social sectors, and between consumption and investment. The budget is the most important instrument for payment flows and the most important component of overall financial planning. The budget encompasses other financial plans, such as the foreign exchange plan, cash plan and credit plans.

Burma aims to achieve the targets of the Four-Year Economic Plan within the framework of a long-term 20 year economic plan. The main objectives of the Plan are to achieve growth with stability and equity, to transform the dominantly agricultural economy into an agro-based industrial economy and to double the per capita income during the twenty-year period. Plan implementation and performance have been improving under the leadership of the Burma Socialist Programme Party.

The Union of Burma Bank was established in February 1948 under the Union Bank of Burma Act of 1947. It took over the central banking functions of the Rangoon branch of the Reserve Bank of India which had served as the central bank in Burma since 1935. But it was not until July 1952 when the new Union Bank of Burma Act (1952) came

into effect, that the Union Bank of Burma became a full-fledged central bank. Under the new Act, the Union Bank took over the sole right of note issue from the Burma Currency Board which had its head office in London. It gave wide powers of credit control, inspection and licensing over commercial banks. It defined the Central Bank's relationship with the Government in the management of public debt and loan facilities, as adviser on the monetary implications of fiscal operations, and in measures to be taken to meet balance of payments difficulties.

The banking system at that time consisted of the Union of Burma Bank as the central bank with the commercial banks confining their activities mostly to short-term financing of foreign trade and to the seasonal financing of rice processing. Out of 20 commercial banks existing in 1948, 18 were foreign banks, with head offices abroad. There were then no specialised credit institutions for agriculture or industry or cooperative societies. Since 1952, the banking sector has expanded gradually. Four new commercial banks and the State Agricultural Bank were established. The most important of these new banks was the State Commercial Bank (1954) which filled an important gap in the country's financial system by making capital available to local industries. Up to February 1963, there were 25 commercial banks of which 14 were foreign-owned.

The State Agricultural Bank was established in 1953 to cater to the needs of agricultural finance, and in 1961, the Industrial Development Bank was established to cater to the needs of industrial finance.

Since 1962, Burma has pursued policies designed to transform the economic structure of the country into a socialist economy and many enterprises in key sectors of the economy, including the banking system and important segments of the trade and distribution sectors, have been brought under state control. In accordance with the needs and requirements of the socialist economy all private commercial

banks, owned by foreigners as well as those owned by Burmese nationals, were nationalised in February 1963.

It was found necessary to pool the financial resources of the state financial institutions, such as the State Commercial Bank, the insurance agencies, the Industrial Bank, the State Agricultural Bank, the Small Loans Corporation and the Treasury in order to mobilise all available domestic financial resources of the country.

The process of amalgamation of the banking system into one monolithic bank was carried out in five different stages. The creation of a one-bank system enabled effective mobilisation of financial resources and enabled the Government to exercise effective control over the operations of the financial institutions. The People's Bank of Burma which was established in November 1969 under the People's Bank of the Union of Burma Act, 1967, functioned not only as a central bank but also engaged in commercial, industrial, saving, insurance and agricultural-financing operations through specialised divisions.

The People's Bank of Burma was reorganised on April 1, 1976, on a functional basis under the Bank Law of 1975. This new banking set-up consists of the Union of Burma Bank, the Myanma Economic Bank, the Myanma Agricultural Bank, and the Myanma Foreign Trade Bank. All major decisions on monetary matters, credit expansion, interest rates, foreign borrowing, exchange rate and reserve management policies continue to rest with the Ministry of Planning and Finance. The responsibilities of the new banking system have been enlarged. The Union of Burma Bank as the central bank, advises the Ministry of Planning and Finance on the fiscal and monetary implications of the Government's internal and external financial operations. The Myanma Economic Bank, as the state commercial bank, became a financier of state economic enterprises and assumes greater responsibility in exercising financial control over these enterprises while the Myanma Agricultural Bank expanded its activities beyond that of seasonal

financing. The insurance function was transferred to the newly created Myanma Insurance Corporation which now operates outside the banking system.

II. INSTITUTIONS IN THE FINANCIAL STRUCTURE

The Union of Burma Bank

The Union of Burma Bank acts as the central bank of the country and also acts as adviser on financial matters to the Government and other specialised banks. It directs, supervises and co-ordinates the operations and audits the accounts of each bank in order to have an effective banking system.

The Bank monitors economic and monetary trends with a view to giving timely warning or signals to the authorities for any divergence from the monetary targets and plans. The Bank in the early stages financed the public sector deficits mainly through purchase of Treasury bills and bonds and securities guaranteed by the Government. However, since 1976 with the adoption of economic and financial reforms, the Myanma Economic Bank lends directly to the State Economic Enterprises within the limits prescribed in the Budget.

The Myanma Economic Bank

The Myanma Economic Bank (MEB) is the state commercial bank whose capital is eighty million Kyats paid up by the State and the Union of Burma Bank. The main functions of the Bank are:

(1) to undertake savings business such as issuing cash certificates, savings certificates, savings stamps and other instruments;

(2) to advance loans to economic enterprises and the co-operatives as well as private enterprises and personal loans to individuals;

(3) to maintain the Government accounts such as Ministries and the Departments Accounts, Boards and Corporations Accounts, and Local Authorities Accounts;

(4) to maintain Cooperative accounts as well as private individual accounts; and

(5) to issue small loans secured by pledge of movable property;

At the end of 1982/83, the network of branches of the Myanma Economic Bank totalled 51 branches, 158 township branches and 35 sub-treasuries throughout the whole country.

The Industrial Finance Division of the MEB maintains the accounts of State-Economic Enterprises (SEEs) and grants loans for working capital, term loans and financial loans to them. The progress of the State Corporations financed by the Bank is constantly monitored by the Bank. The Industrial Finance Division keeps watch over the programmes of projects and performance of enterprises so that remedial measures can promptly be taken in case of projects facing difficulties. Field trips are also undertaken from time to time to appraise economic projects particularly in the co-operative sector, in which the research staff of the Union of Burma Bank also takes an active part.

As a matter of policy all term loans to cooperative enterprises are secured by a sufficient pledge, mortgage or hypothecation of movable and immovable assets. In addition, the Cooperative Ministry guarantees the repayment of loans taken by cooperative enterprises.

The Myanma Agricultural Bank

The Myanma Agricultural Bank (MAB) is the only agricultural bank in the country having 101 branches, while in 106 townships the MEB acts as its agent. The MAB operates through 11,587 village banks throughout the country mainly to disburse seasonal crop loans to the farmers. The main objective of MAB is to supply the cash and credit needs of the national economic plans in the field of agricultural, livestock and fishery production.

The MAB has an original capital of forty million kyats, paid up by the State and the Union of Burma Bank. The MAB acts as lender to state-owned agricultural organisations, cooperative agricultural organisations, partnerships in agriculture and livestock breeding, animal husbandry enterprises, and village banks. The MAB grants short-term loans up to one year, medium-term loans from one to four years and long-term loans from four to twenty years.

The Bank does not lend directly to farmers but only through banks. The Bank charges an interest rate of 8 per cent and the village banks in turn charge at the rate of 12 per cent per annum. The interest differential of 4 per cent represents village banks' profits and is used to finance running expenses of the village banks.

Cultivation loans for paddy are granted at the rate of K 70 per acre. Since 1981/82, it has been raised to K 140 per acre particularly in areas where High Yield Variety (H.Y.V) of paddy are grown. Medium term loans for purchase of drought cattle was introduced in 1978/79 at the average rate of K 1,000 per head of cattle. The H.Y.V programme for other crops such as wheat, groundnut, jute, sugarcane, potatoes was introduced in 1979/80.

The MAB recovers its loans from the farmers at the time paddy is sold to buying depots of the State-owned Agricultural Farm

Produce Trade Corporation. Recovery rate of seasonal credit for various types of crops during 1982/83 was 91.65 per cent achieved through the co-operation of village banks and personnel from People's Village Councils and Township Councils.

The Myanma Foreign Trade Bank

The Myanma Foreign Trade Bank (MFTB) has an original capital of thirty million kyats paid-up by the State and the Union of Burma Bank. It has a Reserve Fund consisting of initial contributions by the State and the Union of Burma Bank and other funds that may be transferred to it from the operating surplus. It is authorised to conduct foreign exchange operations arising out of both external trade as well as non-trade activities of the state. It may borrow money in or outside the country for the purpose of development of foreign trade. Exchange control is administered by the Exchange Control Board through MFTB in accordance with instructions from the Ministry of Planning and Finance.

The main office of the MFTB is situated in Rangoon and agencies of this bank operate at hotels and the Rangoon Airport.

Developments Affecting Financial Institutions

Since 1954, the Union Bank has granted long term loans for economic development by purchasing debentures issued by state enterprises and guaranteed by Government. An overall limit to debenture issues was fixed annually taking into consideration the prevailing and expected economic and monetary conditions. The Union Bank purchased three-month Treasury bills and two- and five-year Treasury bonds from the Government. A ceiling was fixed for the purchase of three months Treasury bills during any fiscal year. Since March 1981, however, the Union of Burma Bank no longer holds these Treasury bills and bonds. The Government now lends directly to State Economic Enterprises through the Myanma Economic Bank.

A major development has been the nationalisation of banking business in 1963 when all the private banks became State-owned and came under the control of the Ministry of Planning and Finance. The systems of accounting, pay scales, interest rates on loans and deposits were standardised in accordance with the one used by the State Commercial Bank.

As the specialised banks opened more branches and agencies in the townships and rural areas, the magnitude of the unorganised market, which was associated with high interest rates, was reduced. At the same time, through the process of financial intermediation, rural savings were mobilised and monetisation of the economy expanded.

The number of village banks under the MAB increased from 11,159 in April 1976 to 11,621 at the end of September 1984. Every new member who wishes to join the village banks have to pay K 5 each and these members' subscriptions amounted to K 4.3 million in the above period. Moreover, 1 per cent of every loan taken by members is retained as compulsory savings and these savings amounted to K 61.7 million while profits of the village banks amounted to K 88.2 million in the same period. These profits arise out of the 4 per cent interest differential because the MAB charges 8 per cent on its loans to village banks while the village banks in turn charge 12 per cent to its members. Thus, mobilisation of rural savings through MAB amounted to K 154 million from April 1976 to September 1984.

III. INSTRUMENTS IN THE FINANCIAL STRUCTURE

Financial Claims

Claims in the form of loans and deposits are the main financial instruments in Burma.

1. Loans. In Burma, credit plays an important role in that it assists in the financial needs of various sectors. Up to March 1981, the Union of Burma Bank handled the public debt of the Union Government comprising mainly of Treasury bills and Treasury bonds, the bulk of which was held by the central bank itself. The purpose of Government borrowing from the central bank was mainly to finance operations of the State Economic Enterprises (SEEs). Since then, however, these bills and bonds were redeemed and the SEEs are now financed directly by the Myanma Economic Bank (MEB). Credit, except for agriculture, is disbursed by the MEB namely loans to and local bodies, cooperative loans, small and other personal loans. Loans to SEEs comprise a significant portion of the total credit.

Credit to the cooperative sector has been sluggish in recent years because the cooperatives have been able to pay back their loans and were able to accumulate substantial cash balances due to better management. These cooperative loans amounted to about 3.7 per cent to 12.5 per cent of total credit during the last 10 years.

The MEB grants loans to local authorities for building schools and bazaars, providing water supply, etc. These loans went up by 28 per cent in 1982/83 compared to the previous year and accounted for only 0.7 per cent of total credit as of March 31, 1983.

Loans are also granted to private institutions such as private small scale industries registered under the Right of Private Enterprises Law.

Small loans are granted to the private individuals through the branches of the MEB all over the country. The rate of interest is 24 per cent annum. The small loan branches accept movable property like gold as security.

The Myanma Agricultural Bank (MAB) grants loans to farmers through village banks. The MAB advances annual, short-term and long-

term loans to the state-owned agricultural organisations, cooperatives and farmers. Agricultural loans outstanding amounted to about 2.3 per cent to 4.6 per cent of total credit during 1974 to 1983. This was because the recovery rate of these loans was very good.

The MAB extends loans to 29 types of crops. Paddy is the major crop, and oil seeds such as groundnut, sessamum, sunflower are also eligible. Recovery of these loans is made by a door-to-door system of collection by the village bank committees at the time of harvest. Term loans for drought cattle, pumpsets, power tillers and bullock carts are available to farmers who have no overdue loans from the Bank. Cattle and other equipment require insurance with the policy being assigned to the Bank. Paddy makes up 82 per cent of the total volume of lending and the recovery rate for that crop is 98 per cent.

The recovery procedure for paddy has been tied-in with the farmers' sale of paddy to the State purchasing depots. During the year 1981/82, total agricultural loans extended by the Bank was K 5,922 million, and the amount of repayment being about K 5,445 million, bringing the recovery rate to 91.95 per cent.

The Myanma Foreign Trade Bank (MFIB) has borrowed medium and long-term loans from foreign institutions. These funds are used in turn to buy capital goods, auxiliary parts, raw materials, etc. for the state economic enterprises. Project loans are loans given out for projects for these enterprises. These loans are about 8.6 per cent of the total credit at the end of the fiscal year 1982/83 as compared to 2.8 per cent in 1973/74.

In Burma, all the banks are state-owned and all extend loans to the public sector including the State Economic Enterprises, and to the cooperative and private sectors. State Economic Enterprises receive loans according to budget provisions set by the Ministry of Planning and Finance.

Bank credit to the public sector was 92.8 per cent of the total credit while loans to co-operative sector and private sector include 3.7 per cent and 3.5 per cent of the total credit. Changes in the structure of bank credit by sectoral user are shown in Table 1.

Table 1

CHANGES IN THE STRUCTURE OF BANK CREDIT, BY USER

(As a percentage of total credit)

	1976/77	1979/80	1982/83
1. Credit to the Public Sector	80.7	84.5	92.8
2. Credit to the Co-operative Sector	11.8	8.4	3.7
3. Credit to the Private Sector	7.5	7.1	3.5
Total Credit	100.0	100.0	100.0

All State boards and corporations have accounts under Government deposits (Union Government Consolidated Fund). All excess cash holdings of the public sector are transferred to the Union of Burma Bank through a unified Government Accounting System.

The banking system is the only source of domestic credit. There are no financial markets and bank liabilities are not subject to reserve requirements. The advance of credit, interest rates, foreign borrowing, exchange rates and reserves policies are determined by the Government within the framework of the annual and four-year plans.

2. Deposits. In Burma, savings bank deposits are considered safe and liquid and the rate of interest paid on such deposits make investments in them worthwhile.

Before the nationalisation of the banks in 1963, interest paid on such deposits ranged from 1 per cent to 3 1/2 per cent per annum. After nationalisation, the uniform rate of 2 per cent per annum was used in the whole country. With effect from 1st January 1973 it became 3 1/2 per cent per annum. But it was changed to 6 per cent plus 2 per cent premium on 3 year minimum balances starting from 1st April 1975. But since 1st November 1977, the interest rate on saving deposits was changed to 8 per cent per annum plus 2 per cent premium rate on three-year minimum balances.

The rate of increase on savings deposits was about 30 per cent. One can open a savings account with two kyats at any branch of the Myanma Economic Bank. There is no limit on the amount a depositor may withdraw. But interest will be paid only if the minimum balance amounts to 10 kyats.

Another type of savings are the savings certificates with a maturity of twelve years. They are issued in denominations of K 5; K 10; K 50; K 100; K 500; K 1,000; K 10,000; and K 100,000. No interest will be received during the first year. Withdrawals are allowed after one year-time period. The rate of interest on saving certificates is 10.9 per cent compounded annually.

Saving deposits which consist of 66 per cent of total savings increased by 24.6 per cent in 1982/83 while savings certificates which form 34 per cent of total savings increased by 37 per cent in the same year.

No interest is paid on demand deposits but interest on time deposits varies according to their period. Three-, six-, and twelve-month and two-year time deposits obtain 1, 1.5, 2.5, 3.5, per cent interest rates per annum, respectively, but these deposits are not widely used, the total outstanding being only K 2 million.

Other Instruments

Currency. One of the indicators of the structure of financial instruments is the share of currency to money. The currency in circulation forms a major part of the money supply consisting 90 per cent of the money supply (M 1) whereas it was about 65 per cent of total money supply (M 2) which includes the savings in the banking system.

Government securities. Since 1954, issue of Government Guaranteed Securities was one of the financial instruments in the economy. The Union Bank held the bulk of these securities while some were taken up by public and private bodies. At present, these securities ranging from 10 - 30 years maturity have been redeemed and are no longer issued.

IV. INDICATORS OF FINANCIAL DEVELOPMENT

Financial Interrelations Ratio

The financial interrelations ratio (FIR) which is defined as the ratio of the total value of financial assets and the national wealth has increased rapidly in Burma. It was 215.7 per cent in

1983/84 compared to 45.2 per cent in 1975/76. The marginal rates of financial assets as well as the GDP growth rates for 1971/72 to 1983/84 are shown in Table 2. The marginal rate of financialisation of national wealth fluctuated during the 13 years under review. The ratios were highest in 1981/82 and 1983/84 on account of increases in the financial assets. The growth rates of the financial assets varied from 7.5 per cent to 58 per cent whereas the increase in Gross Domestic Product at current prices varied from 2.8 to 31.6 per cent. The above increase in financial assets was due to the increase in the financial assets of the Myanma Economic Bank and the Myanma Foreign Trade Bank. On the other hand, the growth in GDP was mainly due to overfulfilment of the plan targets in the agriculture sector which is the basis for economic development and productive supporter of other important economic sectors.

Degree of Concentration of Financial Institutions

Before the nationalisation of private banks and enterprises, Burma had a substantial number of private banks, of which only a few maintained offices outside Rangoon. Total assets of the Union Bank of Burma and private commercial banks were K 1,109 million and K 456 million, respectively, in December 1952. After the nationalisation of private banks in February 1963, the total assets of Union Bank of Burma was K 2,244 million while that of commercial banks amounted to K 1,454 million in December 1963. These assets increased to K 7,190 million in December 1973 when all the banks came under one monolithic bank named The People's Bank of Burma.

Table 2

FINANCIALISATION OF NATIONAL WEALTH

(In per cent)

	Marginal Rates of Total Financial Assets (March)	GDP* Growth Rates	Marginal Rate of Financialisation of National Wealth
1971/72	8.1	2.8	4.0
1972/73	11.8	8.0	5.8
1973/74	20.5	25.3	9.0
1974/75	27.5	31.6	11.0
1975/76 ^{a/}	7.5	21.3	3.2
1976/77	36.5	16.8	14.1
1977/78	36.6	8.0	17.9
1978/79	58.6	7.4	36.5
1979/80	35.4	11.1	31.4
1980/81	24.3	9.3	26.8
1981/82	38.9	11.0	47.9
1982/83	19.6	8.4	30.9
1983/84	22.3	7.0	39.4

*At Current Prices

^{a/} Since April 1976 the accounts of the Myanma Insurance Corporation were excluded from the banking system.

When the new banking set-up came into existence in April 1976, the total assets of the Union of Burma Bank amounted K 7,349 million. The other 3 banks (MEB, MAB, and MFTB) had K 1,630 million, K 471 million and K 2,223 million, respectively. At the end of December 1983, the total assets were K 20,476 million, K 60,782 million, K 1,721 million and K 11,298 million, respectively. Total assets of the 4 banks increased by K 92,859 million over the past 18 years.

The ratio of total assets of the central bank to the total assets of financial institutions was 54.04 per cent in December 1976 whereas it was 21.71 per cent in December 1983.

Myanma Economic Bank is the only domestic commercial institution authorised to accept all kinds of deposits in Burma. Its branches, township branches, sub-treasuries and savings agencies mobilise savings and accept deposits. It also advances loans to economic enterprises, cooperatives, private enterprises and to individuals. This Bank has the largest assets compared to the other three banks, comprising 64.47 per cent in December 1983 which was more than half of the total assets of the four banks.

The Myanma Agricultural Bank's head office is represented at the grass roots by 207 township credit outlets located all over Burma. At the village level, there are 11,587 village banks at the end of 1983/84. The MAB's share of total assets contributed about 1.82 per cent in December 1983.

The Myanma Foreign Trade Bank conducts the foreign exchange operations arising out of both external trade as well as non-trade activities of the State. Its share of assets contributed about 11.98 per cent out of the total financial assets of the 4 banks. The ratios can be seen in Table 3 which shows the changing structure of the financial institutions.

Table 3

DISTRIBUTION OF TOTAL ASSETS OF THE BANKING SYSTEM: 1977-1983

(in per cent)

	Union of Burma Bank	Myanma Economic Bank	Myanma Foreign Trade Bank	Myanma Agricul- tural Bank
1976 Dec	54.0	22.0	20.1	3.9
1977 Dec	41.9	36.4	18.6	3.1
1978 Dec	31.3	45.4	19.1	4.2
1979 Dec	24.1	56.1	16.6	3.2
1980 Dec	21.7	59.6	16.0	2.7
1981 Dec	22.0	58.8	16.6	2.6
1982 Dec	20.2	61.3	16.4	2.1
1983 Dec	21.7	64.5	12.0	1.8

V. THE EFFECTIVENESS OF MONETARY POLICY

Policies Affecting of the Financial Structure

The financial structure of Burma is geared to serve the socialist economic system and to assist in the implementation of State economic plans. Before nationalisation, most of the financial institutions were privately owned enterprises with the main objective of achieving maximum profits. The Union Bank's policies were formulated in order to promote the development of the productive resources of the country and to achieve a rising level of real income in addition to internal and external stability of the currency. This implies that the Bank should help to mobilise and direct domestic capital for the nation's economic development by establishing suitable financial institutions and fostering the growth of the banking sector, at the same time keeping domestic prices and the foreign exchange rate reasonably stable.

According to the Bank Act of 1947, the reserve requirement to hold international reserves at 25 per cent of the amount of currency in circulation plus bank deposits was applied to control credit of private banks. There was also minimum reserve requirement to be maintained by each bank, 8 per cent of its demand liabilities and 3 per cent of its time liabilities which may be changed from time to time. That instrument of control was used to curb the creation of further credit which might add to inflationary pressures.

After nationalisation, all the private banks and enterprises came under Government control. Key manufacturing, banking, transportation and international trade activities were also controlled and operated by the State. As Burma is based on a planned economy with a twenty-year long term plan broken down into five four-year and annual plans, all the State-owned financial institutions are responsible for achieving these targets of the plans. While the Ministry of Planning and Finance has control and supervision over the

entire economic system as well as the banking system, the Union of Burma Bank acting as a central bank has to direct, control, supervise and co-ordinate the functions of the remaining banks whose basic functions are to assist in the successful implementation of the objectives indicated in the annual, short-term and long-term state economic plans.

The principal objectives of the Twenty-Year Economic Plan (1974/75 - 1993/94) are to achieve growth with stability and equity, to transform the dominantly agricultural economy into an agro-based industrial economy and to double the per capita income of the people. The State financial institutions play a close and co-ordinated role with the planning and fiscal authorities in the implementation of economic plans. As Burma's economy is centrally planned, this includes the management of money and credit involving the use of the cash plan, credit plan, interest rate policy and selective credit control.

Implications on the Effectiveness of Monetary Policy

The financial structure of a country differs according to the economic system. In Burma, the banking institutions have played an effective role as an intermediary in channeling resources for development purposes.

Since credit is extended under the credit plan and currency is issued under the cash plan, the amount of money and credit to be injected into the economy is accordingly planned. The actual implementation by the specialised banks is carried out according to the monetary plans, and the Central Bank keeps a close monitoring of actual implementation of the plan. The effectiveness of monetary and financial policies is ensured by a close co-ordination between the financial institutions, the central bank and the Ministry of Planning and Finance at the policy level and other financial institutions at the technical and implementation levels.

VI. CONCLUSION

In the Burmese experience, monetary policy has been effective in raising financial savings and consequently, in contributing to growth and stability in recent years. Private financial savings increased by 22 per cent in 1983/84 due to adequate incentives given to savers and are expected to increase further. The growth rate in GDP in 1983/84 was 5.6 per cent as against 5 per cent of the annual plan, and the plan performance exceeded the plan target.

In general, the Burmese experience has indicated that close coordination between financial institutions and state economic enterprises is necessary to implement monetary and fiscal policies in order to achieve the targets of the national economic plans.

THE FINANCIAL STRUCTURE AND ITS IMPLICATIONS FOR MONETARY POLICY IN INDONESIA

I. INTRODUCTION

Prior to 1966, Indonesia faced a deteriorating economy characterised by high inflation rates, declining production and shortage of all kinds of goods. With those problems, the New Order Government began to proceed with a programme of rehabilitation and stabilisation covering the period 1966-1969. This programme is aimed at fostering a suitable environment to start economic development in the country. The general direction of development efforts is specified in the Five-year Development Plans or REPELITA.

The financial sector was likewise expected to provide efficient services in supporting the REPELITA. Accordingly, the Government also concentrated its efforts towards improving banking and other financial institutions by introducing fundamental financial reforms. The reforms were embodied essentially in Act No. 14 of 1967 on Banking Principles, Act No. 3 of 1968 on Foreign Banks and Act No. 13 of 1968 on the Central Bank. These three statutes have served as the legal bases for the banks' regulatory frameworks under which banking activities have rapidly expanded along with the economy.

In terms of supervision, financial institutions in Indonesia may be classified into three categories: banks, non-bank financial institutions and others. Banking institutions are under Central Bank (Bank Indonesia) supervision while non-bank financial institutions (NBFIs) and other financial institutions composed of insurance and leasing companies, fall within the ambit of the Ministry of Finance.

As of end March 1985, the financial system of Indonesia is comprised of Bank Indonesia, 85 commercial banks, 29 development banks, two saving banks, 5,832 rural banks, 14 non-bank financial institutions (NBFIs), 89 insurance companies and 47 leasing companies.

This study aims to analyse the changes in the financial structure and their implications for monetary policy in Indonesia from the period of REPELITA I to REPELITA III.

The specific coverages of the REPELITAs are as follows:

REPELITA I	April 1st, 1969 - March 31st, 1974
REPELITA II	April 1st, 1974 - March 31st, 1979
REPELITA III	April 1st, 1979 - March 31st, 1984
REPELITA IV	April 1st, 1984 - March 31st, 1989

Indonesia is currently under the second year of REPELITA IV.

Limitations in the availability of data for earlier periods confined the coverage of this study largely to the period of December 1972 to December 1984. However, the qualitative analysis of the major developments in the financial structure will be presented by tracing the events and policies from 1966 up to the succeeding REPELITA periods.

Section II focusses on the development of each type of financial institutions since the beginning of the economic rehabilitation in 1966 up to the present, during the implementation of REPELITA. Section III concentrates on the financial instruments available in Indonesia while Section IV presents the various indicators and measurements of financial structure development.

Section V is devoted to the analysis of the policies on the financial structure and their implications on the effectiveness of monetary policy while the last section gives the summary of the findings and some conclusions.

II. INSTITUTIONS IN THE FINANCIAL STRUCTURE

After the New Order Government took over in 1966, some measures to stabilise the economy began to be implemented. This included the reform of the financial system in recognition of its important role in accelerating economic recovery. With the three regulations mentioned earlier as framework, the financial system in Indonesia evolved to its present position (see Chart 1).

BANKING INSTITUTIONS

Bank Indonesia

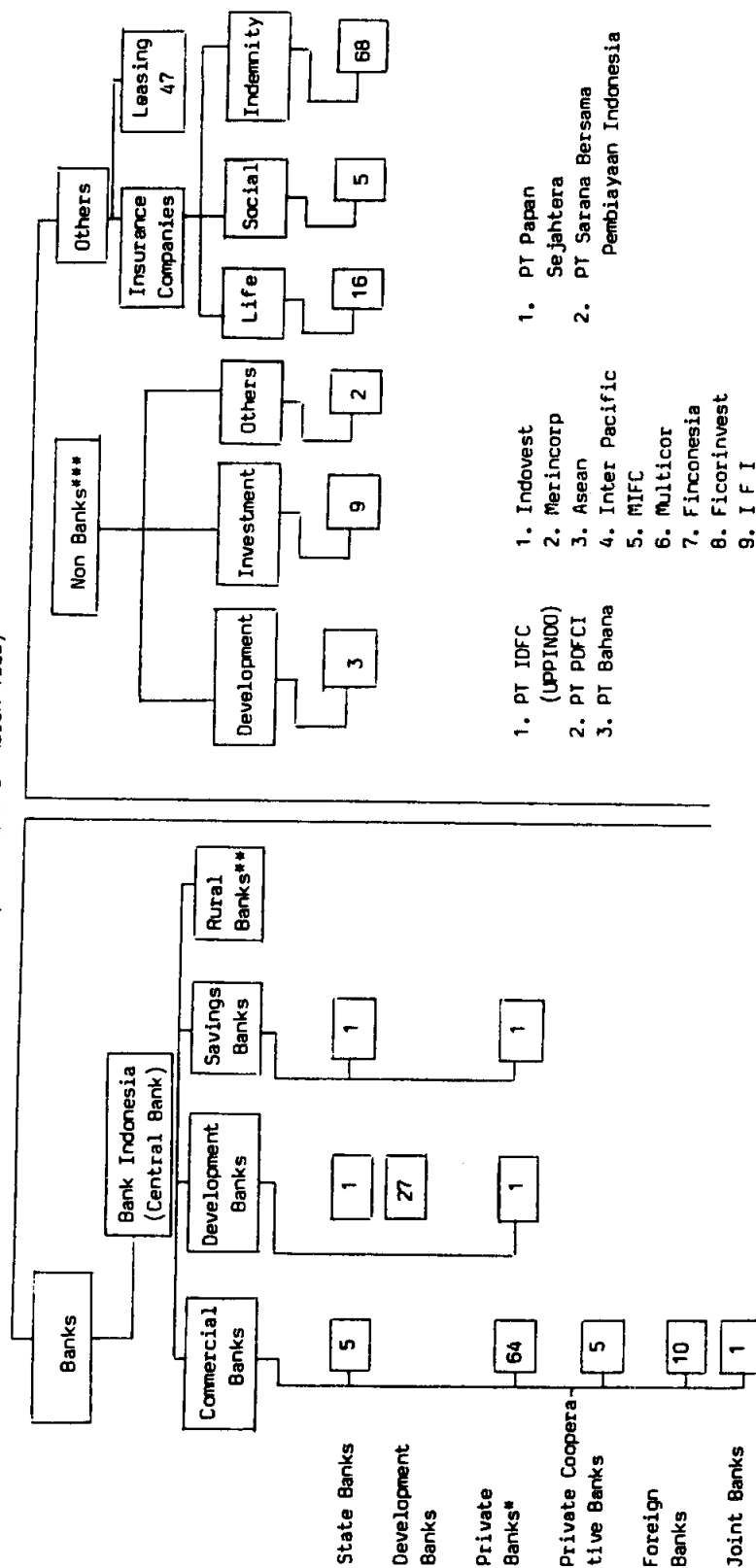
Bank Indonesia is the central bank of Indonesia. It was founded in 1953 as a result of the nationalisation of De Javasche Bank N.V. established in 1928. Prior to 1966 when Bank Indonesia was named as Bank Indonesia Unit I, it was given the power to control directly the financial system and also acted as a commercial bank. As stipulated in Act No. 13 of 1968, Bank Indonesia has ceased its commercial activities and concentrated on its original central bank functions, which are primarily:

1. to regulate, safeguard and maintain the stability of the value of the rupiah; and
2. to promote and to serve as a financial vehicle to achieve the development of domestic production as well as to expand employment opportunity.

As a central bank, Bank Indonesia is the sole issuer of Indonesia's currency, manages the nation's external reserves and acts as the depository of the Treasury and as the cashier of the Government. As the authority over the banking system, Bank Indonesia is empowered to inspect, supervise and regulate the operations of the banking system. The Monetary Council, which is composed of the Governor of

Chart 1

THE FINANCIAL SYSTEM OF INDONESIA
(As of End of March 1985)



=====Under Finance Department Supervision=====

* Ten of which are eligible to deal in foreign exchange transactions and are called Foreign Exchange (F.E.) private banks, the rest are called non-F.E. private banks

** Supervision and promotion of these banks are executed by Bank Rakyat Indonesia (BRI), under Bank Indonesia guidance. These banks consist of:

1. Village Banks	3,581
2. Paddy Banks	2,078
3. Petty Traders Banks	172
4. Employees Banks	1
	----- 5,832

*** Before September 1, 1982, supervision and promotion were carried out by Bank Indonesia

Bank Indonesia, the Minister of Finance and the Minister of Trade, is the financial advisory body of the Government.

Bank Indonesia also performs an important role with respect to the economic development of the country. As an agent of development, Bank Indonesia provides direct credit needed to finance several Government programmes and projects. Aside from those direct Government credit extensions, Bank Indonesia also extends credit to commercial banks to finance government credit schemes. However, since the adoption of the Monetary Policy Reforms of June 1, 1983, Bank Indonesia curtailed its direct credit gradually and limited such credit to the highest priority sectors.

The head office of Bank Indonesia is located in Jakarta. It has 39 branches and five representative offices abroad: in Kuala Lumpur, London, New York, Singapore and Tokyo. It has also opened correspondent relations with 233 overseas banks.

Commercial Banks

The main functions of commercial banks are to mobilise funds from the public and to extend credit for working capital and investment purposes.

Among the 85 commercial banks currently in operation, five are state banks which play a dominant role in terms of loans and deposits. There are also 64 private national banks in Indonesia, and 10 foreign banks and one joint-venture bank (Table 1). Commercial banks comprised the largest group of financial institutions in Indonesia. As of end-1984, they accounted for 51 per cent of the total assets of its financial system (see Table 2).

State banks. The importance of the state commercial banks can be viewed from their assets, deposits and loans (Tables 3, 4 and 5). It can be seen from Table 3 that since 1966 total assets of state

commercial banks is the largest among the banks. In 1984, the share of state commercial banks' assets to total was 72 per cent. The same impression can be gathered in terms of deposits and loans, in 1984 the shares of state banks deposits and loans to total were 64 per cent and 69 per cent, respectively (Tables 4 and 5). Historically, the operations of all the state commercial banks represent a continuation of that of foreign banks which operated in Indonesia prior to its independence in 1945. Since ownership of banks is vested with the Government, the commissioners and boards of directors of these institutions are appointed by the Government. All of the five state commercial banks are licensed to deal in foreign exchange transactions. In accordance with their enabling Acts, each state commercial bank is assigned to serve a specific sector of the economy. However, due to structural and technical difficulties, such specific assignments have to be implemented gradually along with the expansion and development of each bank.

The June 1, 1983 Monetary Policy Reforms gave much more freedom to the state banks with respect to their lending activities and fund mobilisation. The deregulation of state banks gave them the freedom to set their interest rates, leading to the narrowing of the differential between these rates and the unregulated rates prevailing at national private banks and the determination of the maturity structure of deposits which, however, led to the shortening of the average maturity of their deposits.

Private national banks and cooperative banks as at the end of March 1985 aggregated to 69 as compared with 138 in the beginning of REPELITA I. This decline indicated the success of the government's policy in encouraging banks to merge. Ten of these private commercial banks are licensed to deal in foreign exchange transactions. Such eligibility to transact foreign exchange is tied up to the soundness of the banks, to certain capitalisation and preferably merger requirements.

The role of private national banks is relatively small compared with the state banks. However, their total assets, funds mobilised and loans extended have increased significantly from year to year. The average annual growth rates of private national bank' assets, funds mobilised and loans extended during the period of REPELITA III (1979-1984) were 48 per cent, 59 per cent and 57 per cent, respectively. The shares of these components to the banking system also increased significantly during the same period (Tables 3, 4 and 5).

Foreign banks. In addition to a joint venture bank established in 1953, ten foreign banks were granted permission to establish branches and engage in commercial banking activities under the provisions of Government Regulation No. 3, 1968. The objective of this permission is to encourage foreign investment, exports, development of domestic industries and production as well as to increase national productivity. In view of these objectives, all foreign banks are authorised to deal in foreign exchange transactions. However, their operations are restricted to the Province of Jakarta Raya only. Services to customers outside the Province of Jakarta Raya can be rendered only through cooperation with national banks.

Although few in number and restricted in their area of operations, the share of foreign banks to the country's banking business is quite significant. During the period of REPELITA III (1980-1984) the average shares of foreign banks' assets, deposits and loans to the banking system were 7.5 per cent, 10.4 per cent and 6.8 per cent, respectively (Tables 3, 4 and 5). In addition, there are 68 representative offices of foreign banks in Jakarta performing special liaison role for their head offices abroad and their local customers. Indonesia.

Development Banks

Development banks in Indonesia rely heavily on the

Government and Bank Indonesia for the bulk of their resources. However, they also mobilise funds in the form of deposits and medium and long term securities and extend medium-and long-term credit. Development banks' shares to total assets, deposits and loans of the whole banking system in 1984 were at 8 per cent, 5 per cent and 5 per cent, respectively. These shares were more or less maintained since 1966. Compared to total assets of the financial system, that is, including non-bank financial intermediaries, development banks resources accounted for 5 per cent in 1984.

The emergence of development banks as an important source of investment credit has been even more striking. Investment credit provided by development banks has been generally of longer maturities, five to ten years on the average, as compared with maturities of three to five years in commercial banks.

There are three types of development banks in Indonesia, namely, one state development bank called BAPINDO, one private development bank and 27 regional development banks.

BAPINDO was established on May 25, 1960. On August 16, 1960, the Industrial State Bank which was founded in 1951, was amalgamated with BAPINDO. The main task of this bank is to provide medium- and long-term loans for the financing of projects to develop the industrial sector with emphasis on land transportation, maritime, tourism, and construction sectors. BAPINDO also extends investment credit with a maturity of 15 years, including six years grace period. Other activities of BAPINDO include participating in the equity of enterprises, extending guarantees, and administering government projects whose funds are derived from foreign borrowing.

The only private development bank in Indonesia was founded in 1962. Its primary sources of funds are deposits and medium-and long-term securities. The issuance of securities by the private development bank is envisaged by the Banking Act of 1967 to provide

long-term credit and to act as an investment promoter. However, up to the present, the investment role assigned to it has not been performed due to technical difficulties and lack of funds.

The regional development banks are established by Provincial Acts. They commence operations after a license from the Minister of Finance has been obtained. The Minister grants the license only after having received positive consideration from the Board of Directors of Bank Indonesia and the Minister of Internal Affairs. The establishment of the development banks is designed to assist the government in accelerating local development by mobilising potential funds and resources in the region, and to encourage the private sector to participate in the financing of projects. All 27 provinces have already established their regional development banks while 162 branch offices and 12 sub-branch offices have been opened. In order to manage their funds more efficiently, regional development banks are allowed to invest their funds in securities issued by non-bank financial institutions.

Saving Banks

The activities of savings banks are restricted to accepting deposits and investing in securities. They are also authorised to extend loans but this is confined to specific purposes such as house ownership and loans to its own depositors.

There are only two saving banks in the country: the state savings bank and the private savings bank. The state savings bank was established in 1968 as a continuation of Bank Tabungan Pas which had its origin from the nationalisation of the Postspaarbank in 1950. The Bank is engaged in collecting deposits especially from the public, and investing these funds in securities or extending loans for house ownership.

Private saving banks are allowed to operate after having received a license, which the Minister of Finance only issues after obtaining a positive consideration from Bank Indonesia. At present, as already mentioned there is only one private savings bank. At the end of REPELITA III the share of saving banks to the total assets of the financial system was about 2 per cent (Table 2).

Rural Banks

Another type of bank in Indonesia is the rural bank. Unlike the other banks, the rural banks are supervised by one of the state commercial banks, Bank Rakyat Indonesia, under Bank Indonesia guidance. Rural banks can be further classified into employees, village, paddy and petty traders banks. As of the end of March 1984, there is only one employees bank, while village, paddy and petty traders banks numbered to 3,581, 2,078 and 172, respectively. Most of these banks are located in Java and Bali and they collect funds in the form of time and savings deposits. Although the assets of these banks was less than 1 per cent of total financial institutions' assets, the average annual growth since 1979, showed a substantial annual increase of 54.2 per cent (Table 2).

NON-BANK FINANCIAL INSTITUTIONS

Since 1972, the Government permitted the establishment of NBFIs in Indonesia to encourage the development of the money and capital markets and to assist the business sector in their capital needs.

Finance Companies

The finance companies in Indonesia fall into three categories, namely, the development type, the investment type and the others type.

Development type. The main function of the development type institution is to provide medium-and long-term loans and invest in equities. They also issue short-term promissory notes and deal in commercial paper and long term securities. They are permitted to hold equity investments of not more than 50 per cent of their paid-up capital. Two of these three institutions are of joint ventures with Indonesian banks. The investment type have functions similar to those of the development type. However, they are not allowed to make direct loans.

Investment finance type. Since 1979, the investment finance type have been encouraged to participate in the ownership of companies in Indonesia. They are permitted to participate in equities of both Indonesian companies and joint foreign ventures up to 25 per cent of their paid-up capital. Ownership of shares in a joint venture by investment type finance companies is permitted for up to five years, with the long-term objective that the shares be transferred to their Indonesian partners. In addition to participating in the equity of joint foreign ventures, the investment type financial institutions are expected to assist foreign investors in finding local partners and to provide investment services and advice.

Others type. The others type of NBFIs was established to meet the needs of certain sectors such as the provision of loans to the medium-income group for house ownership. They meet their long-term funding requirements by issuing medium-and long-term bonds in the stock market. The NBFIs have the advantage over banks of not being subject to legal reserve requirements. However, the competitiveness of NBFIs against banks is hampered by the fact that the interest paid on their papers is subject to income tax, whereas interest on bank's time deposits is currently not taxable.

The gross assets of NBFIs accounted for about 1 per cent of the total assets of the financial system in 1973, about 2 per cent at

the beginning of 1980, 3 per cent at the end of REPELITA III in March 1984 and 2 per cent as of end-1984 as shown in Table 2.

Insurance Companies

Insurance companies in Indonesia have grown rapidly during the last few years. There are three categories of insurance companies operating, namely, those engaged in indemnity insurance, life insurance and social welfare insurance. The average annual growth rate in assets for the period 1979-1983 was 26 per cent for non-life insurance companies and 28 per cent for life insurance companies. However, their assets still represent a small fraction of the financial system's total assets, about 2 per cent as of end 1983 (Table 2).

At the end of March 1985, there were 68 companies, dealing in indemnity insurance, 15 companies, in life insurance and five companies, in social welfare insurance.

Leasing Companies

The leasing business in Indonesia started in 1974. Currently 47 leasing companies operate in Indonesia, of which 28 are joint venture companies, one state company, and 18 domestic companies, while eight more companies are holding provisional licenses. The number of leasing companies rose rapidly in 1982 and 1983, reflecting the liberal licensing policy of the Government. Their activities are geared towards providing financial leases, mostly for industrial machinery, automobiles and office management. A large part of their funding comes from the interbank market and from foreign borrowing, the latter usually covered by a swap arrangement.

III. INSTRUMENTS IN THE FINANCIAL STRUCTURE

During the period of 1966-1984, the total value of financial instruments increased by 47 per cent annually, that is, from only Rp 44.3 billion in 1966 to Rp 44,522.4 billion in 1984 (Table 6). The highest increase was registered during REPELITA I, with an annual average increase of 166 per cent. For REPELITA II and III, the annual average increase was 32 per cent and 30 per cent, respectively.

From Table 6, it can be seen that almost all of the financial instruments consisted of claims against financial institutions, while equities comprised only a small portion of total instruments. This indicates the underdevelopment of the capital and money markets in the country. Although the share of equities to total instruments was less than 1 per cent, its average annual increase from 1969 to 1984 was, however, significant at 47 per cent. This increase is primarily due to government efforts to encourage the development of the capital and money markets. These included the establishment of non-bank financial institutions since 1973 and the permission given them to acquire ownership of private companies.

The annual average increase of claims against financial institutions amounted to 46 per cent, that is, from only Rp 22.5 billions in 1966 to Rp 19,537.0 billion in 1984. This expansion was not only due to the increase of existing financial claims but also due to the introduction of other types of claims (Table 6). This is an indication of the ability of financial institutions to mobilise funds from the public and likewise reflected the introduction of varied financial instruments in Indonesia.

Claims against non-financial institutions in 1984 amounted to Rp 13,957.8 billion, increasing at an average of 43 per cent annually since 1966. This increase was primarily due to the expansion of loans extended which registered an annual increase of 42 per cent.

Net claims against the foreign sector also increased significantly, although its share to total claims was less than 1 per cent. In the period of 1971-1984, claims against the foreign sector increased by 78 per cent annually. This increase showed the growing involvement of financial institutions in the foreign sector.

IV. INDICATORS OF FINANCIAL DEVELOPMENT

Economic development and monetary policy in Indonesia had a positive impact on the performance of the financial structure. The growth in Gross Domestic Product was accompanied by an expansion in assets in the form of financial instruments. Two indicators of the relative importance of the financial sector to the national economy are the marginal rate of financialisation of national wealth (MRF) and the financial interrelations ratio (FIR) which are discussed below.

Marginal Rate of Financialisation of National Wealth

The marginal rate of financialisation of national wealth (the ratio of the changes in financial assets to GDP) has been tracing an irregular trend from 1967 to 1984. It started at about 11 per cent in 1967 but ended up at a lower rate of 8 per cent in 1984. The highest MRF was obtained in 1972 and 1973 when it reached 13 per cent. (Table 7). These figures reflected that the financialisation of the Indonesian economy proceeded at a slower pace. This could be attributed to the vast area of Indonesia, particularly the rural area, which are still not fully within the monetised sector.

Financial Interrelations Ratio

Table 7 also shows another indicator of the extent of financialisation of the Indonesian economy. The financial interrelations ratio (FIR) is nothing but the share of total financial instruments or assets to the Gross Domestic Product. The ratios

obtained from 1966 to 1984 revealed a more progressive path for the financial development of Indonesia as compared to those indicated by MRF. Although the value of financial assets has not exceeded that of the national wealth, it is interesting to note that the share of the former to GDP has been increasing through the years. From .14 per cent in 1966, the FIR increased by almost three times ten years after, in 1976. By the early 1980s, total financial assets in Indonesia accounted for about half of the national wealth.

Financial Intermediation Ratio

The financial intermediation ratio in Indonesia was computed as the ratio of the claims of financial institutions against non-financial units (NFUS) to total credit for consumption purposes plus gross fixed capital formation of the NFUs (Table 8). During the period of 1980 through 1984, the ratio improved from .47 in 1980 to relatively low role of financial institutions in the financial intermediation process may be ascribed to the dominant role of the government sector in financing economic activities. Thus loans of financial institutions do not play as much role in financing economic activities.

Degree of Concentration of Financial Institutions

Commercial banks play the most important role among the groups of financial institutions. The share of their assets to total financial assets was the highest, more than 50 per cent, compared with that of other institutions (Table 2). From 1972-1984, assets of commercial banks increased at an average rate of 29.3 per cent, by 29.8 per cent and 34.2 per cent, respectively. On the other hand, there is a tendency for share of assets of the monetary authority to decrease, as it only grew by 45 per cent annually and its share to total financial assets of other banking and financial institutions did not change much relative to commercial banks. It can be summed up that commercial banks benefited from banking policies more than other

financial institutions. This is due to the fact that most of the banking measures promulgated in the past encouraged the growth and development of commercial banks. However, current policies are also aimed at expanding the role of other financial institutions.

Foreign-currency Denominated Instruments

Among all financial instruments, the share of foreign currency instruments which consist of foreign currency deposits, net foreign assets of the monetary system and bank credits in foreign exchange currencies, increased from 0.20 in 1972 to an average of 0.29 during REPELITA II.

For REPELITA III, the ratio rose to an average of 0.33 and remained at that level at the end of 1984 (Table 9). These indicators reflected a fairly significant share of foreign denominated financial instruments and showed the relatively high degree of the openness of the Indonesian economy. This only reflected positively the impact of the removal of several restrictions on trade and foreign exchange payments and the adoption of a flexible exchange rate system in Indonesia.

Securities

Prior to 1973, the bulk of securities was held by commercial bank which mainly consisted of draft and promisory notes. However, with the emergence of non-bank financial institutions in the early 1970s and the introduction of other financial instruments, securities held by these institutions reached 60 per cent. This can be traced to the fact that non-bank financial institutions not only invested their funds in the form of securities but also issued securities to absorb funds from the public. As a result, from 1973 through 1984, total securities of financial institutions increased by 48 per cent while securities of non-bank financial institutions rose markedly by 88 per

cent. At the same time, the share of securities of the latter type of institutions rose to about 80 per cent during REPELITA III (Table 10).

Bank Credit and Other Monetary Indicators

In line with the development and growth of the economy, credit extended by the banking sector rose by 30 per cent annually since 1973. This increase is due largely to credit to the manufacturing and trade sectors (Table 11). Manufacturing and trade credit accounted for 33 per cent and 28 per cent of total, respectively. Meanwhile, during the same period, there was an improvement in the ratio of demand deposits to money supply (Table 12) and the ratio of broad money to GDP (Table 13). These indicated that there was also an improvement in the monetisation rate of the economy and increased bank consciousness on the part of the general public.

V. IMPLICATIONS FOR MONETARY POLICY

Developments and innovations in the financial sector were primarily due to policies and reforms introduced by the Government. The strong Government influence in the financial system was dictated mainly by the requirements called for by an ever-changing environment which could not be provided solely by the private sector.

Since 1966, restoration of financial stability became a primary goal and the Government carried out a stabilisation programme consisting of a set of fiscal, monetary and foreign exchange policies. The stabilisation objective of fiscal policy was geared towards a balanced budget designed to alleviate domestic price increases. This was achieved by reducing government expenditure to the level that could be financed by domestic revenues and supplemented by external resources. In the monetary field, the inflationary financing of budget deficits was stopped and the growth in money supply was moderated. Restrictive trade and foreign exchange controls were

gradually removed and a new foreign exchange rate system was implemented.

In the banking sector, the Government adopted two important banking regulations, namely, Act No.14 of 1967 on Banking Principles and Act No.13 of 1968 on the Central Bank. These two principal regulations were designed to provide the framework for the creation of a uniform system in regulating the banking system and implementing monetary policy as well as mobilising and channelling of domestic resources through the banking system. Under the 1967 Banking Act, a foreign bank is permitted to operate only in Jakarta and it should be established in the form of a branch.

The total number of banks up to 1969 was 179 consisting of seven state banks, 138 national private banks, 23 regional development banks and 11 foreign banks.

At the end of 1969, their total assets amounted to Rp 290.7 billion, funds mobilised totalled Rp 185.2 billion while outstanding credit aggregated to Rp 158.2 billion.

In order to mobilise financial savings in the economy that could be channelled to productive investment, a policy of increasing the nominal level of interest rates was adopted. This policy was not only aimed at gathering funds from the public but also at reducing the pressure on prices. In practice, the high interest rate policy was implemented by the reintroduction of time deposit in 1968 which offered very high nominal interest rates ranging from 4 to 6 per cent per month for deposits of three to twelve months. In addition to time deposits, a national savings programme with a lottery feature was introduced in 1969. The private sector responded positively to the high nominal interest rates.

The beneficial effects of all these measures have been registered during their period of implementation. The inflation rate

which reached 635 per cent in 1966 was reduced to about 112 per cent in 1967, 85 per cent in 1968 and 10 per cent in 1969. Annual economic growth rates averaged 6 per cent between 1967-1969 compared with only 2.8 per cent in 1966. In other words, the stabilisation programme initiated during this period turned out to be successful and provided the necessary condition to embark with the economic development plan for the next period.

REPELITA I

During the period of REPELITA I, a healthy pace of economic growth continued and basic monetary stability was maintained despite the resurgence of inflation. This inflationary push was due to price adjustment arising out of the de facto devaluation of the Rupiah by over 23 per cent in terms of the US dollars on January 15, 1968, the food supply shortage, the worldwide commodity price boom and the oil shock in 1974.

Since the new government recognised that the banking system had to be viewed as an integral part of the Indonesian economy and its performance is a reflection of its development, a number of regulations to implement the Banking Act 1967 were adopted during this period. Government Regulation No. 8 of 1969 stipulated the terms and condition for national private commercial banks to operate as foreign banks. Meanwhile, the Ministry of Finance issued Decision No. 800/MK/IV/II of 1969 to regulate the establishment of cooperative development banks, cooperative savings banks and cooperative commercial banks. In order to develop state banks, the Ministry of Finance in its Decision No. 562/MK/IV/1970 stipulated the conditions and procedures for the establishment of branches, sub-branches and representative offices of state banks, including state development banks and state savings banks. For secondary banks, the government issued a regulation on the establishment of rural banks in 1970.

To create a better banking climate, particularly for the national private commercial banks, in November 1969 Bank Indonesia issued guidelines on banking supervision. This action involved two fundamental objectives: firstly, to improve the banking structure by persuading and encouraging banks to merge and secondly, to provide assistance to the banking system in the form of refinancing facilities and technical assistance related to the reorganisation of banks. Merger among national private banks was designed to reduce their number while improving their financial soundness by granting some tax allowances. To allow foreign banks to operate outside Jakarta, Bank Indonesia required these banks to operate on the basis of joint activities with national banks.

In the course of 1973 and 1974, operating licenses were granted to nine investment finance companies (IFCs) to begin money market operations in Jakarta. The IFCs were supported by approximately 30 foreign companies with joint venture commitments.

In general terms, an operating license granted to an IFC allows this financial corporation to do the following:

- a) to act as broker or dealer of securities;
- b) to provide guarantees;
- c) to obtain funds from the public through assistance, acceptance, endorsements, and assignment of debt instruments;
- d) to extend services in the form of financial and management consultancy;
- e) to provide medium-to long-term financing; and
- f) to act as underwriter of capital instruments.

At the end of REPELITA I, the total number of banks was 162, consisting of seven state banks, 118 national private banks, 26 regional development banks and 11 foreign banks. The total volume of banking activities during REPELITA I increased significantly. Their

total assets, deposits and loans at the end of REPELITA I reached Rp 1,722 billion, Rp 1,002 billion and Rp 1,080 billion, respectively.

The annual GDP growth rate during the period of REPELITA I reached 8.4 per cent or much higher than what were ever achieved in the past decades. Associated with this rapid growth rate is the expansion in gross domestic capital formation which increased at an annual average of 23.8 per cent, mostly induced by the increase in public investment. Development expenditures increased from 5 per cent of GDP in 1970 to 10 per cent in 1971 and 12 per cent in 1972, of which approximately half was spent on transportation and communication as well as on agriculture and irrigation.

REPELITA II

With the reemergence of high inflation in 1974 which exceeded 33 per cent, the Government launched a series of anti-inflation measures. The 1974 policy package had for its main thrust the control of domestic credit creation since domestic credit expansion by the banking system was the main cause of inflation late in this period .

Accordingly, Bank Indonesia made great efforts to improve its policy instruments to regulate bank credit activities. First, and the most important among a number of policy instruments implemented to moderate money supply increase, was the imposition of specific bank-wide ceilings on credit expansion. In addition, Bank Indonesia devised and imposed a new minimum liquidity ratio (defined as the ratio of liquid assets to current liabilities) which was to be maintained at 30 per cent both in respect of the Rupiah and foreign exchange liabilities. Up until then, although the minimum cash ratio requirement existed, it was ineffective in controlling domestic credit creation. The bank lending ceilings and the minimum liquidity ratio requirement until the end of REPELITA II remained as the two most important and effective means of credit control by Bank Indonesia.

Second, the interest rate level was also moved upward, together with the introduction of a new two-year negotiable certificates of deposits (CDs) scheme. The high interest rate policy adopted at that time, however, had an interesting twist to it: to prevent high-cost time deposits from increasing banks' funding costs that would lead to high lending rates, and thereby, discourage bank credit-financed investments, Bank Indonesia decided to provide interest subsidies to banks which accepted time deposits.

Third, it was also during this period that Bank Indonesia further developed the rediscounting or refinancing credit facility as an important part of its policy instruments. Two major refinancing schemes have been operating since the beginning of the 1970s. One is an agricultural credit scheme for the financing of fertiliser and other inputs used by farmers primarily for rice production, and these credits were provided as part of the Government's agricultural extension programme and are refinanced by Bank Indonesia. The other, the medium-term investment credit scheme, was introduced in 1969 to provide medium-term credit for investment purposes. These refinancing facilities, provided at preferential rediscount rates, represented Bank Indonesia's attempt to direct credit flows in favour of the high priority sectors. In 1974, Bank Indonesia introduced new special refinancing schemes for indigenous small-and medium-scale industries, including the Small Investment Credit Programme (KIK), the Permanent Working Capital Programme (KMKP), the Mini Credit Programme and the Vendors' Credit Programme. In having added these refinancing schemes, Bank Indonesia's credit policy was further oriented towards assisting the Government in its objective of equitable distribution of development gains.

The year 1975 served as the first meaningful year of operations for the nine investment finance companies (IFCs) that were established in the previous year to do business in Indonesia. It was during this year that saw the reorganisation of most of the said institutions and their recovery from operating losses.

Financial services offered by the IFCs were limited to dealer note transactions, i.e., the sale of IFCs' own short-term obligations. Despite the desire of the IFCs to accelerate the development of the market, industry expansion was not dramatic and secondary trading of primary issues remained to account for a minimum share of the total trading volume. Securities were acquired and remained in the dealer's portfolio, while dealer notes were traded actively as a means of funding this portfolio. Thus, in effect, the IFCs operated very much like banks.

The role of the IFCs started changing with the opening of the new Jakarta Stock Exchange in 1977. The IFCs, together with P.T. Danareksa, were involved in the development of the new Jakarta Stock Exchange by acting as underwriters.

In view of the increasing need for international transactions, it was considered necessary to ease the requirements on national private banks to become foreign exchange banks. In April 1974, Bank Indonesia introduced regulations governing the appointment or addition of foreign exchange banks. The requirements on national private non-foreign exchange banks to be eligible as foreign exchange banks, among others, are the felt need to establish or expand a foreign exchange bank in the requested region, the bank involved must have been in operation for at least five years, and it must have undergone merger.

To stimulate banking activities, at the end of 1977 the Government reduced the minimum reserve requirement both in Rupiah and foreign exchange from 30 per cent to 15 per cent of current liabilities. Furthermore, Bank Indonesia decided to grant interest on bank deposits placed with it whenever they exceed the required level.

To develop rural banks, starting from September 1977 Bank Indonesia delegated its supervisory functions of the rural banks to

Bank Rakyat Indonesia. However, the general guidance remains with the central bank.

At the end of REPELITA II, the total number of banks was further reduced to 127, consisting of seven state banks, 83 national private banks, 26 regional development banks and 11 foreign banks. Total assets, deposits and loans of banks amounted to Rp 5,322 billion, Rp 3,337 billion and Rp 3,674 billion, respectively.

Due to all of these efforts and measures, REPELITA II succeeded in achieving its major objectives. GDP at constant prices grew at an annual average of 7 per cent. The annual rate of inflation declined significantly from that prevailing in REPELITA I. However, since the rate of inflation in Indonesia was significantly higher than in her trading partners, the competitiveness of Indonesian exports gradually deteriorated. In November 1978, the Government initiated devaluation in response to the continued weakness of Indonesia's major export commodities in the world market.

The devaluation was aimed at providing a competitive base for the long-term development of the non-oil sectors and at assuring the long-run viability of the balance of payments. To moderate and smoothen price movements during the post devaluation period, the Government adopted several measures comprising, among others, exemption from and reduction of import duties and sales taxes levied on raw materials and spare parts used by domestic industries. Indonesia's balance of payments showed an overall surplus of \$708 million in 1978/79 compared with \$651 million in the preceding year.

REPELITA III

During the period of REPELITA III, efforts to improve the climate for banks to operate showed some interesting results. The Government not only enhanced and supported measures already taken in

REPELITA I and II, but also introduced a fundamental reform known as June 1, 1983 Monetary Policy Reforms.

This policy was essentially intended to establish a stronger foundation towards a healthier development of the banking sector in the years to come. The major feature of this policy was deregulation in the banking sector involving both credit activities and mobilisation of funds. In the field of credit, the policy stressed on reduced dependence of state banks on Bank Indonesia's refinancing facility (liquidity credit) by allowing the state banks to establish their own credit policies and by removing credit ceilings. Prior to June 1, 1983, bank credit was regulated by numerous requirements, such as, the share of financing from the implementing banks and of self-financing from the borrowers, interest rates, feasibility studies and the appropriate financial reports. Since June 1, 1983, most of the above regulations were removed and henceforth, banks were free to determine their own policies. In the mobilisation of funds, state banks were free to set their own interest rates on time deposits, which in the past were regulated by Bank Indonesia.

One of the objectives of the June 1, 1983 Monetary Policy Reforms was to encourage banks to maximise their fund mobilisation from the public and thereby reduce their dependence on the central bank for low cost funds in their lending activities. The liquidity credit provided since the past 15 years had succeeded in boosting development efforts. However, it had some unfavourable effects on prices, balance of payments and foreign exchange reserves, and it did not encourage banks to actively mobilise funds from the public.

Prior to June 1, 1983, the Government in controlling money supply utilised credit ceilings as a direct instrument. After June 1, 1983, the Government stressed the use of indirect instruments, such as reserve requirements, open market operations, discount facilities and moral suasion. In this connection, since February 1, 1984 Bank Indonesia introduced the Bank Indonesia Certificate or

Sertifikat Bank Indonesia (SBI) and created a discount facility. It should be noted that this new SBI differed from those issued in 1970-1972, since the latter were introduced only as instruments to encourage mobilisation of funds. The present SBI could be utilised by banks as a temporary outlet for their excess funds before extending them as loans to their customers. When the secondary market for SBI has been developed, the SBIs could be utilised more effectively to influence monetary developments in accordance with the economic policies of the Government.

In order for banks to be more efficient and effective in managing their liquidity, adjustments were made on the interest rates on rupiah and foreign exchange demand deposits of banks placed at Bank Indonesia. Immediately after the June 1, 1983 Monetary Policy Reforms, the increase in funds mobilised was faster than that of the extension of loans, leading to excess liquidity to some banks. To ease the burden of the cost of funds encountered by banks, the interest rate on rupiah demand deposits placed at Bank Indonesia was raised from 10 per cent to 13 per cent per annum. Following the introduction of Certificate of Bank Indonesia (Sertifikat Bank Indonesia/SBI), this interest rate was reduced from 13 per cent to 7 per cent per annum and the maximum amount of demand deposits eligible for this interest rate was set at 1 per cent of total current liabilities of the respective bank. The interest rate on foreign currencies demand deposits held with Bank Indonesia, previously fixed at 10 per cent, was abolished in February 1, 1984.

Merger among national private banks continued to be encouraged. However, tax incentives granted to these banks had been abolished since September 1981.

At the end of REPELITA III, the total number of banks was 117, consisting of seven state banks, 72 national private banks, 27 regional development banks, and 11 foreign banks. In addition, there were also 5,823 rural banks. The banks' total assets, deposits and

loans amounted to Rp 22,118 billion, Rp 10,097 billion and Rp 13,827 billion, respectively.

REPELITA IV

In 1984/85 the Government continued to make adjustments and consolidation to prevent backsliding on the major structural reforms in the financial sector, taxation and exchange rate management. Along with improved growth rate and the improvement in the balance of payments position, the price fluctuations were also placed under control.

Mobilisation of private savings is one of the principal objectives of the banking sector in the period of REPELITA IV. In view of this government policy, it is important that the financial institutions are well prepared to undertake this task. Accordingly, in REPELITA IV, greater emphasis is placed on improving the organisation and management of banks and non-bank financial institutions. Bank supervision by monetary authorities will therefore be focused on these areas.

As far as the national private banks are concerned, the government will still emphasise the policy of encouraging merger among national private banks and opening new branch and sub-branch offices. For regional banks, the emphasis is on supporting them with financial and technical assistance and training.

In the first year of this period (1984-1985), macro economic indicators in 1984/85 pointed towards remarkably good performance. The economic growth in 1984 was higher than the preceding year. The balance of payments surplus in 1984/85, although not as high as the previous year, amounted to \$667 million. As a result, the central bank foreign exchange reserves increased from \$5.144 million to \$5.811 million at the end of March 1985. It is also encouraging to note that the deficit on current account declined significantly.

V. CONCLUSION

The financial structure in Indonesia has gradually improved and expanded during the period of the study. Although the number of private national banks decreased due to mergers promoted by the Government, the Indonesian financial structure has nevertheless expanded in terms of branches, institutions, activities and instruments. In line with the improvement of the economy, the overall financial system expanded as can be seen from the increase in its total assets, loans, deposits and securities.

Among the five groups of financial institutions, deposit type institutions particularly commercial banks play the most important role. The share of their assets to total financial assets was the highest among the groups of institutions. On the other hand, the ratio of foreign currency denominated instruments of commercial banks which accounted for a third of their total instruments indicates the relatively high degree of openness of the economy.

The expansion of the branches has increased the financial system's coverage of the economy. Innovations in financial instruments and the introduction of new institutions have increased the sophistication of the financial structure of the country. All of these changes in the financial structure of Indonesia have improved the effectiveness of monetary policy and increased the speed of the monetary transmission process.

However, Indonesia's financial structure still faces many problems such as under-developed capital and money markets, high concentration of state banks, inefficiency in state banks, and lack of sufficient long-term lending institutions. The need for efficient banking operation and the improvement of capital and money markets has become very urgent in Indonesia especially since the June 1, 1983 monetary policy reforms which led to the gradual liberalisation of the financial system.

Table 1

NUMBER OF FINANCIAL INSTITUTIONS

	<u>1969</u>	<u>1st Repelita</u> (end of March 1974)	<u>2nd Repelita</u> (end of March 1979)	<u>3rd Repelita</u> (end of March 1984)	<u>1st year of 4th Repelita</u> (end of March 1985)
Total	8,849 =====	5,990 =====	6,087 =====	6,089 =====	6,099 =====
A. <u>Banks</u>	<u>8,849</u>	<u>5,990</u>	<u>5,999</u>	<u>5,941</u>	<u>5,949</u>
1. Central Bank	1	1	1	1	1
2. Commercial Banks	<u>142</u>	<u>123</u>	<u>94</u>	<u>85</u>	<u>85</u>
- State Banks	5	5	5	5	5
- National Private Banks	126	107	78	69	69
- Foreign Banks	10	10	10	10	10
- Joint-Venture Banks	1	1	1	1	1
3. Development Banks	<u>25</u>	<u>28</u>	<u>28</u>	<u>29</u>	<u>29</u>
- State Banks	1	1	1	1	1
- Regional Development Banks	23	26	26	27	27
- Private Banks	1	1	1	1	1
4. Savings Banks	<u>12</u>	<u>11</u>	<u>5</u>	<u>3</u>	<u>2</u>
- State Banks	1	1	1	1	1
- Private Banks	11	10	4	2	1
5. Rural Banks	<u>8,669</u>	<u>5,827</u>	<u>5,871</u>	<u>5,823</u>	<u>5,832</u>
- Village Banks	5,091	3,505	3,564	3,574	3,581
- Paddy Banks	3,317	2,212	2,154	2,079	2,078
- Petty Traders Banks	261	110	152	169	172
- Employees Banks	-	-	1	1	1
B. <u>Non-Bank Financial Institutions</u>	-	-	<u>12</u>	<u>14</u>	<u>14</u>
- Development type	-	-	3	3	3
- Investment type	-	-	9	9	9
- Others	-	-	-	2	2
C. <u>Others 1)</u>	n.a.	n.a.	<u>76</u>	<u>134</u>	<u>136</u>
Insurance Companies			<u>76</u>	<u>97</u>	<u>89</u>
- Life Insurance	n.a.	n.a.	13	14	16
- Social Insurance	n.a.	n.a.	5	5	5
- Indemnity Insurance	n.a.	n.a.	58	68	68
Leasing Companies	-	-	n.a.	47	47

Source: Bank Indonesia

1) Note: 1 life, 5 social, and 3 indemnity insurance companies, and 1 leasing company are state companies; the rest are private.

Table 2
ASSETS OF FINANCIAL INSTITUTIONS
(Billions of Rupiah)

Institutions	1966	1967	1968	1969	1970	1971	1972	1973	1974	1975	1976	1977	1978	1979	1980	1981	1982	1983	1984
Monetary Authority Share (\$)	23.1 (61)	162.6 (81)	273.1 (70)	384.2 (57)	439.2 (47)	540.4 (45)	666.7 (40)	856.0 (35)	1299.7 (37)	2145.1 (43)	2801.6 (44)	3300.0 (44)	5002.0 (48)	6636.0 (47)	9245.0 (46)	10561.0 (42)	13254.0 (41)	14783.0 (38)	19848.0 (40)
Commercial Banks Share (\$)	13.4 (36)	35.0 (18)	115.9 (29)	283.7 (42)	443.9 (48)	611.1 (51)	917.5 (56)	1452.4 (60)	2040.1 (58)	2557.0 (53)	3273.5 (51)	3741.6 (50)	4875.9 (46)	6322.4 (45)	9423.0 (47)	12199.0 (49)	15470.0 (48)	19075.0 (49)	25492.0 (51)
Development Banks* Share (\$)	1.2 (3)	2.0 (1)	3.3 (1)	7.0 (1)	43.0 (5)	47.4 (4)	65.6 (4)	80.5 (4)	143.9 (4)	167.6 (3)	235.0 (4)	288.4 (4)	400.1 (4)	466.6 (3)	699.0 (3)	954.0 (4)	1336.6 (4)	1757.0 (5)	2276.0 (5)
Savings Banks Share (\$)	0.1 (0)	0.3 (0)	0.5 (0)	0.9 (0)	2.4 (0)	3.1 (0)	2.8 (0)	3.6 (0)	7.2 (0)	9.3 (0)	17.5 (0)	27.6 (0)	37.3 (0)	63.0 (1)	129.0 (1)	256.0 (1)	452.0 (1)	683.0 (2)	946.0 (2)
Rural Banks Share (\$)	-	-	-	-	-	-	-	-	-	-	-	-	-	22.0 (0)	31.0 (0)	60.0 (0)	70.0 (0)	104.0 (0)	177.0 (0)
Non-Bank Financial Institutions Share (\$)	-	-	-	-	-	-	-	22.0 (1)	44.0 (1)	69.0 (1)	98.4 (1)	125.0 (2)	194.7 (2)	277.0 (2)	404.0 (2)	557.0 (2)	805.0 (3)	1108.0 (3)	1327.0 (2)
Insurance Companies Share (\$)	-	-	-	-	-	-	-	-	-	-	-	-	-	242.0 (2)	312.0 (1)	413.0 (2)	566.0 (2)	812.0 (2)	-
Leasing Companies Share (\$)	-	-	-	-	-	-	-	-	-	-	-	-	-	28.0 (0)	35.0 (0)	60.0 (0)	114.0 (1)	368.0 (1)	-
Total (\$)	37.8 (100)	199.9 (100)	392.8 (100)	675.8 (100)	928.5 (100)	1202.0 (100)	1652.6 (100)	2414.5 (100)	3534.9 (100)	4948.0 (100)	6426.0 (100)	7482.6 (100)	10510.0 (100)	14057.0 (100)	20278.0 (100)	25060.0 (100)	32067.6 (100)	38690.0 (100)	50066.0 (100)

* Including state development bank

Table 3
ASSETS OF BANKING INSTITUTIONS
(Billions of Rupiah)

Group of Banks	1966	1967	1968	1969	1970	1971	1972	1973	1974	1975	1976	1977	1978	1979	1980	1981	1982	1983	1984	1985
State Commercial Banks Share (%)	10.6 (73)	26.7 (72)	86.2 (72)	209.9 (72)	335.3 (69)	465.8 (71)	712.8 (73)	1127.3 (74)	1632.6 (75)	2113.3 (78)	2688.4 (77)	3034.8 (75)	3890.0 (74)	5123.2 (75)	7630.0 (77)	10152.9 (77)	11937.9 (76)	15293.5 (73)	19805.0 (72)	23708.9 (71)
National Private Banks Share (%)	2.8 (19)	8.3 (22)	21.2 (18)	37.1 (13)	45.7 (10)	57.6 (9)	79.1 (8)	111.5 (7)	161.5 (8)	183.7 (7)	265.9 (8)	337.2 (8)	480.8 (9)	569.2 (8)	870.0 (9)	1128.1 (9)	1475.5 (9)	2085.5 (10)	3495.0 (13)	4856.1 (14)
Development Banks Share (%)	1.2 (8)	2.0 (6)	3.3 (3)	7.0 (2)	43.0 (9)	47.4 (7)	65.6 (7)	80.5 (5)	143.9 (7)	167.6 (6)	235.0 (7)	288.4 (7)	400.1 (8)	466.6 (7)	699.0 (7)	954.0 (7)	1336.6 (8)	1757.0 (9)	2276.0 (9)	2702.0 (8)
Foreign Banks ^{1/} Share (%)	-	-	8.5 (7)	36.7 (13)	62.9 (12)	87.7 (13)	125.6 (12)	213.6 (14)	246.0 (10)	260.0 (9)	319.2 (8)	369.6 (10)	505.1 (9)	630.0 (10)	723.0 (7)	918.0 (7)	1172.0 (7)	1696.0 (8)	2192.0 (7)	2245.0 (7)
T o t a l (%)	14.6 (100)	37.0 (100)	119.2 (100)	290.7 (100)	486.9 (100)	658.5 (100)	983.1 (100)	1532.9 (100)	2184.0 (100)	2724.6 (100)	3508.5 (100)	4050.0 (100)	5276.0 (100)	6789.0 (100)	10122.0 (100)	13153.0 (100)	15922.0 (100)	20832.0 (100)	27768.0 (100)	33512.0 (100)

^{1/} Including joint-venture bank.

Source: Bank Indonesia

Table 4

DEMAND, TIME AND SAVINGS DEPOSITS OF BANKS
By Group of Banks

(Billions of Rupiah)

	1972	1973	1974	1975	1976	1977	1978	1979	1980	1981	1982	1983	1984
State Commercial Banks Share (%)	363 (69.4)	505 (66.7)	846 (71.1)	1,122 (72.7)	1,537 (73.9)	1,760 (72.9)	2,141 (70.8)	3,168 (74.6)	4,897 (76.4)	5,982 (74.7)	6,100 (68.8)	8,299 (66.9)	9,934 (64.1)
National Private Banks Share (%)	36 (6.9)	50 (6.6)	72 (6.1)	104 (6.7)	159 (7.6)	208 (8.6)	275 (9.1)	385 (9.1)	583 (9.1)	861 (10.8)	1,284 (14.5)	2,119 (17.1)	3,020 (19.5)
Development Banks Share (%)	33 (6.3)	57 (7.5)	85 (7.1)	115 (7.5)	161 (7.7)	189 (7.9)	275 (9.1)	232 (5.5)	377 (5.9)	401 (5.0)	479 (5.4)	580 (4.7)	801 (5.2)
Foreign Banks Share (%)	91 (17.4)	145 (19.2)	187 (15.7)	203 (13.1)	224 (10.8)	256 (10.6)	333 (11.0)	459 (10.8)	554 (8.6)	765 (9.5)	1,004 (11.3)	1,398 (11.3)	1,743 (11.2)
Total	523	757	1,190	1,544	2,081	2,413	3,024	4,244	6,411	8,009	8,867	12,396	15,498
(%)	(100.0)	(100.0)	(100.0)	(100.0)	(100.0)	(100.0)	(100.0)	(100.0)	(100.0)	(100.0)	(100.0)	(100.0)	(100.0)

Source: Bank Indonesia

Table 5

OUTSTANDING LOANS OF BANKS 1/

(Billions of Rupiah)

	1976	1977	1978	1979	1980	1981	1982	1983	1984
State Commercial Banks Share (%)	1,904 (80.8)	2,149 (79.4)	2,689 (77.7)	3,075 (75.0)	4,059 (74.9)	5,501 (73.2)	7,436 (72.5)	8,981 (69.4)	12,348 (68.8)
National Private Banks Share (%)	159 (6.8)	205 (7.6)	299 (8.6)	406 (9.9)	566 (10.4)	834 (11.1)	1,197 (11.7)	1,883 (14.5)	3,042 (17.0)
Development Banks Share (%)	142 (6.1)	170 (6.2)	209 (6.1)	276 (6.7)	331 (7.1)	627 (8.4)	952 (9.3)	1,217 (9.4)	1,507 (8.4)
Foreign Banks Share (%)	150 (6.3)	183 (6.8)	262 (7.6)	342 (8.4)	414 (7.6)	548 (7.3)	666 (6.5)	862 (6.7)	1,046 (5.8)
Total	2,355	2,707	3,459	4,099	5,420	7,510	10,251	12,943	17,943
(%)	(100.0)	(100.0)	(100.0)	(100.0)	(100.0)	(100.0)	(100.0)	(100.0)	(100.0)

1/ Do not include loans extended by Bank Indonesia.

Source: Bank Indonesia

Table 6

FINANCIAL INSTRUMENTS OUTSTANDING

	1966		1967		1968	
	(Billion Rp)	%	(Billion Rp)	%	(Billion Rp)	%
I. Claims						
A. Claims against financial institutions	44.3	100.0	136.5	100.0	190.0	100.0
	22.5	51	53.9	40	126.0	66
1. Money ^{1/}	22.2	50	51.5	38	113.9	60
2. Time and Savings deposits ^{2/}	0.3	1	2.4	2	12.1	6
3. Insurance reserves	-	-	-	-	-	-
4. Borrowings	-	-	-	-	-	-
5. Import deposits	-	-	-	-	-	-
6. Securities	-	-	-	-	-	-
B. Claims against non-financial institutions	21.5	48	69.8	51	63.8	34
1. Loans	21.4	48	69.8	51	63.5	34
2. Securities	0.1	0	0.1	0	0.3	0
C. Net Claims against foreign sectors ^{3/}	(0.3)	1	(12.7)	9	(0.2)	0
II. Equity	-	-	-	-	0	0
Total Financial Instruments	44.3	100	136.5	-	190.0	100

^{1/} Consists of Currency + Demand deposit

^{2/} Consists of time and savings deposits held by monetary system, savings banks and rural banks

^{3/} Net-foreign assets of monetary system; figures in brackets mean a negative sign which indicate that monetary system has a net borrowing to foreign sector.

Source: Bank Indonesia

Table 6 (cont'd)

FINANCIAL INSTRUMENTS OUTSTANDING

	1974	1975	1976	1977	1978
	(Billion Rp) %	(Billion Rp) %	(Billion Rp) %	(Billion Rp) %	(Billion Rp) %
I. Claims	<u>3854.1</u>	<u>4607.8</u>	<u>6096.7</u>	<u>7401.8</u>	<u>10064.4</u>
A. Claims against financial institutions	1765.8	46	2111.0	46	4163.8
1. Money ^{1/}	937.5	24	1250.1	27	2488.0
2. Time and Savings deposits ^{2/}	517.7	13	733.0	16	1337.6
3. Insurance reserves	-	-	-	-	-
4. Borrowings	27.8	1	42.8	1	61.1
5. Import deposits	282.8	8	78.6	2	174.0
6. Securities issued	-	-	6.5	0	103.1
B. Claims against non-financial institutions	<u>1435.6</u>	<u>37</u>	<u>2424.8</u>	<u>53</u>	<u>4237.6</u>
1. Loans	1381.8	35	2337.6	51	4023.8
2. Securities	53.8	2	87.2	2	213.8
C. Net Claims against foreign sectors ^{3/}	652.7	17	72.0	1	1663.0
II. Equity	<u>3.3</u>	<u>0</u>	<u>8.2</u>	<u>0</u>	<u>11.5</u>
Total Financial Instruments	<u>3857.4</u>	<u>100</u>	<u>4616.0</u>	<u>100</u>	<u>10075.9</u>

1/ Consists of Currency + Demand deposit

2/ Consists of time and savings deposits held by monetary system, savings banks and rural banks

3/ Net-foreign assets of monetary system; figures in brackets mean a negative sign which indicate that monetary system has a net borrowing to foreign sector

Source: Bank Indonesia

FINANCIAL INSTRUMENTS OUTSTANDING

	1969	1970	1971	1972	1973
	(Billion Rp)	(Billion Rp)	(Billion Rp)	(Billion Rp)	(Billion Rp)
	%	%	%	%	%
I. Claims	472.4	691.7	1011.1	1614.4	2512.2
A. Claims against financial institutions	235.2	338.9	481.2	748.4	1119.2
1. Money ^{1/}	183.4	250.3	320.8	474.6	669.0
2. Time and Savings deposits ^{2/}	50.1	81.0	149.5	221.7	320.4
3. Insurance reserves	-	-	-	-	-
4. Borrowings	-	-	-	-	14.1
5. Import deposits	1.7	7.6	10.9	52.1	115.7
6. Securities	-	-	-	-	-
B. Claims against non-financial institutions	219.7	350.8	523.9	862.4	1104.3
1. Loans	218.7	345.1	520.2	840.1	1071.7
2. Securities	1.0	5.7	3.7	12.3	32.6
C. Net Claims against foreign sectors ^{3/}	(17.5)	(2.0)	6.0	213.6	288.7
II. Equity	0.3	0.7	0.2	1	1.6
Total Financial Instruments	472.7	692.4	1011.3	1615.4	2513.8

1/ Consists of Currency + Demand deposit

2/ Consists of time and savings deposits held by monetary system, savings banks and rural banks

3/ Net-foreign assets of monetary system; figures in brackets mean a negative sign which indicate that monetary system has a net borrowing to foreign sector

Source: Bank Indonesia

Table 6 (cont'd)

FINANCIAL INSTRUMENTS OUTSTANDING

	1979	1980	1981	1982	1983	1984
	(Billion Rp) %	(Billion Rp) %	(Billion Rp) %	(Billion Rp) %	(Billion Rp) %	(Billion Rp) %
I. Claims	<u>13694.5</u>	<u>19545.4</u>	<u>24054.8</u>	<u>29095.2</u>	<u>37184.7</u>	<u>44422.8</u>
A. Claims against financial institutions	<u>5816.9</u>	<u>8612.5</u>	<u>10795.4</u>	<u>12536.9</u>	<u>16712.8</u>	<u>19537.0</u>
1. Money ^{1/}	3385.5	4995.0	6485.0	7121.0	7569.0	8581.0
2. Time and Savings deposits ^{2/}	1865.5	2744.9	3308.7	4043.9	7228.9	9567.6
3. Insurance reserves	58.8	79.2	107.3	121.6	144.3	-
4. Borrowings	163.7	174.7	248.0	453.6	904.8	394.9
5. Import deposits	213.0	365.0	298.0	300.0	242.0	216.0
6. Securities issued	130.4	253.7	348.4	496.8	623.8	777.5
B. Claims against non-financial institutions	<u>4559.6</u>	<u>4513.9</u>	<u>6602.4</u>	<u>11429.3</u>	<u>12311.9</u>	<u>13957.8</u>
1. Loans	4211.1	4009.4	5964.3	10533.0	10933.8	12276.6
2. Securities	348.5	504.4	638.1	896.3	1378.1	1681.2
C. Net Claims against foreign sectors ^{3/}	3318.0	6419.0	6657.0	5129.0	8160.0	10928.0
II. Equity	14.7	18.7	53.2	72.6	88.0	99.6
Total Financial Instruments	13709.2	19564.1	24108.0	29167.8	37272.7	44522.4

1/ Consists of Currency + Demand deposit

2/ Consists of time and savings deposits held by monetary system, savings banks and rural banks

3/ Net-foreign assets of monetary system; figures in brackets mean a negative sign which indicate that monetary system has a net borrowing to foreign sector

Source: Bank Indonesia

Table 7

MARGINAL RATE OF FINANCIALISATION (MRF) OF NATIONAL WEALTH
AND FINANCIAL INTERRELATIONS RATIO (FIR)

Year	Total Financial Instruments (Billion Rp)	Change in Financial Instruments (Billion Rp)	G D P (Billion Rp)	MRF (%) FIR	
				3/4	2/4
1966	44.3	-	315.9	-	.14
1967	136.5	92.2	847.8	10.9	.16
1968	190.0	53.5	2096.7	2.6	.09
1969	472.7	282.7	2718.3	10.4	.17
1970	692.4	219.7	3340.2	6.6	.21
1971	1011.3	318.9	3672.0	8.7	.28
1972	1615.4	604.1	4564.0	13.2	.35
1973	2513.8	898.4	6753.0	13.3	.39
1974	3857.4	1343.6	10708.0	12.6	.36
1975	4616.0	758.6	12643.0	6.0	.37
1976	6105.4	1489.4	15467.0	9.6	.39
1977	7411.6	1306.2	19011.0	6.9	.39
1978	10075.9	2664.3	22746.0	11.7	.44
1979	13709.2	3633.3	32025.0	11.4	.43
1980	19564.1	5854.9	45446.0	12.9	.43
1981	24108.0	4543.9	54027.0	8.41	.45
1982	29167.8	5059.8	59633.0	8.48	.49
1983	37272.7	8104.9	73698.0	11.00	.51
1984	44522.7	7249.7	85257.0	8.50	.52

Table 8
FINANCIAL INTERMEDIATION RATIO

Year	Claims of Financial Inst. on non-financial units (Bill. of Rp) (1)	Consumption Credit + Gross Fixed Capital Formation (Bill. of Rp) (2)	Financial Intermediation ratio 1/2 (3)
1980	4,513.9	9,513.0	.47
1981	6,602.4	11,785.6	.56
1982	11,429.3	13,667.6	.84
1983	12,311.9	21,933.4	.56
1984	13,957.8	22,854.2	.61

Table 9
FOREIGN EXCHANGE (Fx) DENOMINATED INSTRUMENTS

Year	Fx Instruments (Bill. of Rp) (1)	Total Financial Instruments (Bill. of Rp) (2)	Ratio* (3)= (1):(2)
1972	319.1	1,615.4	0.20
1973	461.4	2,513.8	0.18
1974	959.3	3,857.4	0.25
1975	1,111.5	4,616.0	0.24
1976	1,738.1	6,105.4	0.28
1977	2,270.4	7,411.6	0.31
1978	3,773.2	10,075.9	0.37
1979	4,425.0	13,709.2	0.32
1980	7,995.0	19,564.1	0.41
1981	8,260.0	24,108.0	0.34
1982	7,213.0	29,167.8	0.25
1983	11,546.0	37,272.7	0.31
1984	14,487.0	44,522.4	0.33

* A measure of the degree of economic openness of the financial structure.

Table 10

SECURITIES HELD AND ISSUED BY FINANCIAL INSTITUTIONS

(Billion of Rupiah)

	1973	1974	1975	1976	1977	1978	1979	1980	1981	1982	1983	1984
Commercial Banks Share (%)	14.3 (44)	18.3 (34)	34.3 (37)	39.2 (33)	45.3 (27)	46.0 (15)	97.0 (21)	132.0 (18)	116.0 (12)	113.0 (8)	296.0 (15)	471.0 (19)
Savings Banks Share (%)	-	-	-	-	-	-	1.0 (0)	6.0 (1)	15.0 (1)	49.9 (4)	89.0 (4)	109.0 (4)
Non Bank Financial Institutions (NBFIs)* Share (%)	18.3 (56)	35.5 (66)	59.4 (63)	79.5 (67)	120.4 (63)	270.9 (85)	369.1 (78)	597.2 (80)	824.5 (85)	1185.2 (86)	1565.3 (79)	1878.7 (77)
Insurance Companies Share (%)	-	-	-	-	-	-	6.1 (1)	11.0 (1)	16.7 (2)	25.9 (2)	37.7 (2)	
Total (%)	32.6 (100)	53.8 (100)	93.7 (100)	118.7 (100)	165.7 (100)	316.9 (100)	473.2 (100)	746.2 (100)	972.2 (100)	1373.1 (100)	1988.0 (100)	2458.7 (100)

* Some were issued by non-bank financial institution to absorb funds from the public.

Table 11

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BANK CREDIT ACCORDING TO MAJOR ECONOMIC SECTOR 1/

(Billion of Rupiah)

	1973	1974	1975	1976	1977	1978	1979	1980	1981	1982	1983	1984
1. Agriculture Share (%)	87 (8)	116 (7)	220 (8)	266 (8)	270 (7)	345 (6)	414 (7)	539 (7)	813 (8)	1025 (8)	1226 (8)	1318 (7)
2. Mining Share (%)	8 (1)	11 (1)	741 (27)	1036 (29)	1062 (27)	1699 (32)	1893 (30)	1867 (24)	1693 (17)	1472 (11)	806 (5)	384 (2)
3. Manufacturing Share (%)	278 (26)	359 (23)	719 (26)	990 (28)	1156 (29)	1624 (30)	1721 (27)	2213 (28)	2762 (27)	3923 (30)	5207 (34)	6667 (35)
4. Trade Share (%)	428 (40)	627 (40)	766 (28)	858 (24)	911 (23)	1114 (21)	1320 (25)	1976 (25)	3062 (30)	4129 (32)	5132 (34)	6344 (34)
5. Service Share (%)	79 (7)	121 (8)	172 (6)	260 (7)	319 (8)	389 (7)	656 (11)	946 (12)	1385 (14)	1867 (14)	2277 (15)	3169 (17)
6. Others Share (%)	179 (17)	340 (21)	132 (5)	156 (4)	219 (6)	223 (4)	258 (4)	333 (4)	444 (4)	606 (5)	651 (4)	931 (5)
Total	1059 (100)	1574 (100)	2750 (100)	3566 (100)	3937 (100)	5394 (100)	6262 (100)	7874 (100)	10159 (100)	13022 (100)	15299 (100)	18813 (100)

1/ Excludes loan extended to central government

Source: Bank Indonesia

Table 12
MONEY SUPPLY 1/
(Billions of Rupiah)

End of Period	Money Supply		Currency		Demand Deposits	
	Total	Change (%)	Outstanding	% of Total	Outstanding	% of Total
		Annual				
1969	183	61.1	116	63.1	67	36.9
1969/1970	211	61.1	126	59.9	85	40.1
1970	250	36.4	155	62.0	95	38.0
1970/1971	270	28.2	167	61.9	103	38.1
1971	321	28.4	199	62.0	122	38.0
1971/1972	360	33.3	210	58.3	150	41.7
1972	475	48.0	272	57.3	203	42.7
1972/1973	530	47.2	291	54.9	239	45.1
1973	669	41.8	375	56.0	294	44.0
1973/1974	784	47.9	421	53.7	363	46.3
1974	938	40.2	494	52.7	444	47.3
1974/1975	1,027	31.0	538	52.4	489	47.6
1975	1,250	33.3	625	50.0	625	50.0
1975/1976	1,428	39.0	659	46.2	769	53.8
1976	1,603	28.2	781	48.7	822	51.3
1976/1977	1,815	27.1	853	47.0	962	53.0
1977	2,006	25.1	979	48.8	1,027	51.2
1977/1978	2,111	16.3	1,036	49.1	1,075	50.9
1978	2,488	24.0	1,240	49.8	1,248	50.2
1978/79	2,800	32.6	1,369	48.9	1,431	51.1
1979	3,385	36.1	1,552	45.9	1,833	54.1
1979/80	3,797	35.6	1,774	46.7	2,023	53.3
1980	4,995	48.0	2,153	43.1	2,842	56.9
1980/81	5,214	37.3	2,229	42.8	2,985	57.2
1981	6,486	29.8	2,557	39.4	3,929	60.6
1981/82	6,775	30.0	2,542	37.5	4,233	62.5
1982	7,121	9.8	2,934	41.2	4,187	58.8
1982/83	7,379	8.9	3,001	40.7	4,378	59.3
1983	7,569	6.3	3,333	44.0	4,236	56.0
1983/84	8,055	9.2	3,554	44.1	4,501	55.9
1984	8,581	13.4	3,712	43.3	4,869	56.7

1/ Fiscal year ends March 31.

Source: Bank Indonesia

Table 13
SELECTED INDICATORS OF MONETARY DEVELOPMENT*
1965 - 1984

Unit	Money Supply			Annual Change of Total %	G D P		Ratio	
	Currency + Demand Deposits M1	Quasi Money Rp.bill.	Total M2		Current Prices Rp.bill.	Annual Change %	M1/GDP	M2/GDP
1965	2.6	0.1	2.7	-	24	-	0.11	0.11
1966	22.2	0.3	22.5	733.3	316	1216.7	0.07	0.07
1967	51.5	2.3	53.8	139.1	848	168.4	0.06	0.06
1968	113.9	12.0	125.9	134.0	2,097	147.3	0.06	0.06
1969	183.4	49.9	233.3	85.3	2,718	29.6	0.07	0.09
1970	250.3	80.1	330.4	41.6	3,340	22.9	0.07	0.10
1971	320.8	148.1	468.9	41.9	3,672	9.9	0.09	0.13
1972	474.6	220.4	695.0	48.2	4,564	24.3	0.10	0.15
1973	669.0	318.4	987.4	42.1	6,753	48.0	0.10	0.15
1974	937.5	514.7	1,452.2	47.1	10,708	58.6	0.09	0.14
1975	1,250.1	728.0	1,978.1	36.2	12,643	18.1	0.10	0.16
1976	1,603.0	1,028.3	2,631.3	33.0	15,467	22.3	0.10	0.17
1977	2,006.4	1,124.8	3,131.2	19.0	19,011	22.9	0.11	0.17
1978	2,488.3	1,320.4	3,808.7	21.0	22,746	19.6	0.11	0.17
1979	3,385.0	1,837.0	5,222.0	34.5	32,025	45.2	0.11	0.16
1980	4,995.0	2,695.5	7,690.5	47.6	45,446	41.9	0.11	0.17
1981	6,485.5	3,230.6	9,716.1	26.3	54,027	18.9	0.12	0.18
1982	7,121.4	3,954.0	11,075.4	14.0	59,633	10.4	0.12	0.19
1983	7,569.1	7,093.6	14,662.7	32.4	71,215	19.4	0.11	0.21
1984	8,581.2	9,355.8	17,937.0	22.3	85,914	20.6	0.11	0.22

* At 1983 Market Price

Source: Bank Indonesia

THE FINANCIAL STRUCTURE AND ITS IMPLICATIONS FOR MONETARY POLICY IN MALAYSIA

by
Cheng Yoke Chang

I. INTRODUCTION

The financial system in Malaysia has undergone a radical transformation over a span of 125 years, from a single foreign bank in 1859 to over 30 financial institutions and a variety of financial services in 1984. Following the establishment of the foreign bank, the Currency Board was set up in 1897, to issue currency. Later, other financial institutions like provident funds and insurance companies were formed. The public on their own also set up cooperative societies as early as the 1920s. To mobilise savings from the small savers, the Government formed the Post Office Savings Bank. To encourage industrial development in East Malaysia, industrial development institutions were set up.

All these institutions were already in existence when the Central Bank opened its doors in 1959. This marked a new era in the development of the financial system in Malaysia as the Central Bank was set up specially to promote and develop financial services to effectively channel savings for investment. In order to create the basic financial infrastructure for effective management, the Central Bank began to assist in institution building. More domestic banks were encouraged and their branch network increased significantly, while the opening of foreign bank branches was gradually prohibited. To assist in the intermediation process in the short-term money market, the first discount house was established in 1963. In recognition of the important role played by the agricultural sector in the economy, an agricultural bank was established in 1969, to promote agricultural development. To further encourage the development of small-scale enterprises, the Central Bank helped set up the Credit

Guarantee Corporation in 1972, which provides guarantee up to 60 per cent of designated loans of commercial banks. In line with the Government's New Economic Policy to restructure society, a development bank was set up in 1974 with the objective of promoting the participation of Bumiputera community in commerce and industry. In addition, a National Unit Trust Scheme (Amanah Saham Nasional) was launched in 1981 to help the Government achieve its New Economic Policy.

These financial institutions performed a significant role in providing for the surplus funds of some economic units to be rechannelled to those who need them.

This study only covers the major financial institutions and excludes the money and foreign exchange brokers, pawnshops, private money lenders, capital and commodity market institutions, some smaller co-operatives and unit trust companies due to data limitations. The time frame being analysed is from 1960, after the setting up of the Central Bank, up to 1984. In the analysis of the sources and uses of funds of the financial institutions, the balance sheets of all the financial institutions are combined. Therefore, transactions among the institutions are not eliminated.

This study begins with the evolution of the financial system which is contained in this introductory section, followed by an analysis of the assets of the financial institutions, with the changes in the size of the five major groups and their sources and uses of funds discussed at length in section II. The types and relative importance of financial instruments are discussed in section III while some measures of development of the financial structure are given in section IV. In section V, the monetary instruments available to the Central Bank are briefly explained together with the policies undertaken during the period under study, 1960-1984. A discussion on the weaknesses of the existing financial structure with regard to

the use of certain monetary instruments is included in this section, with a conclusion in Section V.

HISTORICAL PERSPECTIVE OF THE FINANCIAL SYSTEM

The Central Bank

In the early years before the Currency Board was established in 1897, the common medium of exchange in the country was coins which were introduced by foreign traders. With the opening of banks, bank notes were also issued during those times when there was shortage of coins. It was only after the establishment of the Commissioner of Currency in 1897 that currency was solely issued by the Government and became the principal medium of exchange. However, by only issuing currency, the Currency Board did not play a positive role in economic development. As a result, the World Bank Mission in 1955 recommended the establishment of a Central Bank. The Central Bank would then replace the Currency Board as the currency-issuing authority and it was to preside over the financial system to ensure financial stability and at the same time to promote and develop financial services to effectively channel savings for investment.

The establishment of a Central Bank eventually took place in 1959, marking a new era in the history of the development of the Malaysian financial structure. To enable the Bank to perform its functions effectively, the Central Bank is vested with comprehensive legal powers to regulate and supervise the financial system under the Central Bank of Malaysia Ordinance Companies Act, 1958, the Banking Act, 1973 and the Finance Companies Act, 1969. These powers bestowed upon the Central Bank placed it at the heart of the financial system. When the Central Bank opened its doors in January 1959, the financial structure was dominated by the commercial banks.

Commercial Banks

The origin of commercial banks in Malaysia dated as far back as 1859, when the first commercial bank, a branch of Chartered Mercantile Bank of India, London and China was set up in Penang, mainly to service trade (see Table 1). Soon after, in 1875, Chartered Bank established a branch in Penang and later with the discovery of tin in Taiping and Kuala Lumpur, more branches were opened. The operations of the commercial banks originally fell within the ambit of the Companies Ordinance, 1948. After the establishment of the Central Bank in 1959, the activities of the commercial banks were brought under its supervision through the Banking Ordinance, 1958, which was later amended to become the Banking Act, 1973. Under the Banking Ordinance, the commercial banks are required to comply with statutory reserve and liquidity requirements which the Central Bank varies to influence the volume of money and credit in the economy.

With the rapid development in the economy, more banks, particularly domestic banks were set up and their branch network began to spread, such that by 1960 there were already 24 commercial banks with 131 offices. The commercial banks experienced a steady growth over the years and by the end of 1984, there were 38 commercial banks (of which 22 are domestic) and 716 offices (with 570 offices of domestic bank). With assets of \$66.7 billion, they remained the largest group of financial institutions in the country.

National Savings Bank

Another type of bank that has a history of about 100 years is the savings bank. The first Government-owned postal savings bank began operations in 1888 but it was only in 1948 that the Post Office Savings Bank (POSB) was formed. The functions of POSB were then passed on to a more dynamic national savings institution, the National Savings Bank which was established in 1974. POSB expanded steadily in the 1950s and up to 1967 was the second largest deposit-taking

institution in the country, after the commercial banks. However, when finance companies' branch network became more extensive and more competitive interest rates were offered, POSB lost ground to finance companies in mobilising deposits from the lower income group. Its position deteriorated further with the emergence of other specialised institutions like merchant banks and discount houses.

By the end of 1984, the bank has 15 branch offices and there were 519 post offices with saving bank facilities. The number of depositors has increased to 5.4 million at the end of 1984 and total deposits mobilised amounted to \$1.3 billion.

Provident Funds

A financial institution that has a history as early as some of the commercial banks in Malaysia is the provident fund. Generally, provident funds are designed to provide members with a measure of security in the form of retirement or death benefits. They also act as mobiliser of funds through contributions paid by the employer and employees.

The oldest known provident fund in Malaysia is the Penang Municipal Provident Fund which was established in 1898, with the employers and employees contributing 7.5 per cent of the members' monthly wages. This was followed by the setting up of the Rubber Research Institute of Malaysia Provident Fund in 1925 and the Federated Malay States Railway Provident Fund in 1936. Subsequently in 1947, a statutory funds was established for plantation workers, namely the Malayan Estates Staff Provident Fund, which is one of the largest provident fund in Malaysia. By 1949, the establishment of provident funds in the country amongst the plantation and mining companies for their employees was sufficiently widespread for the Joint Wages Commission to consider it timely to introduce a contributory scheme for daily-rated employees. This impetus led to the enactment in 1951 of the Employees Provident Fund (EPF) Ordinance

which created the Employees Fund Board, to provide some measure of social security for the lower-paid workers. Initially, the enactment covered only employees in certain types of employment who earned not more than \$400 per month. The rates of contributions by the employer and employee were 5 per cent each of the employee's wages.

Over the years, by a series of amendments to the original enactment, the conditions of the coverage of the EPF were relaxed to cover all employees except for certain categories such as nomadic aborigines, fishermen, household-employed domestic servants, non-residents and temporary residents. The wage ceiling of \$400 per month was also raised and by 1970, all Malaysian employees irrespective of monthly income were made liable to contribute to the EPF. The rates were also raised from 10 per cent of the employee's total wages (at 5 per cent of the employee's total monthly wage) to 13 per cent (7 per cent for employer and 6 per cent for employee) in 1975. With effect from December, 1980, the rate of contributions was further raised to 20 per cent of the employee's monthly wage (11 per cent for employer and 9 per cent for employee).

Over the years, the forced savings mobilised by the provident funds increased by leaps and bounds, from \$0.7 billion in 1960 to \$23.9 billion in 1984.

Co-operative Societies

Besides established institutions like commercial banks and government savings bank, the public has been saving through the co-operative societies. The co-operative movement was introduced in Malaysia as early as 1922. The co-operatives can be divided into two groups: those which operates in the urban areas and the other in the rural areas. The urban credit co-operative societies are made up mainly of employees credit societies and unions of credit co-operative societies of the public and private sectors. In 1958, the urban co-operative societies formed a bank, the Co-operative Central Bank to

mobilise savings from member societies and individuals and to provide credit facilities to members. In addition, there are other urban co-operatives such as housing, transport (and taxi) and multipurpose co-operative societies. On the other hand, the rural co-operatives, also formed a rural co-operative apex bank, Bank Rakyat, in 1954. In the early years, the co-operative societies were covered under separate enactments in the different states of the country. By 1948, however, all the co-operative societies were covered under the Co-operative Societies Ordinance, 1948.

The number of co-operative societies remained at about 2,500 since 1960 while membership has increased to more than two million with total resources amounting to about \$4 billion by the end of 1984.

Insurance Companies

One of the earliest types of financial institution in Malaysia are life and general insurance companies. They provide financial services to their clients in the form of financial protection against loss of property, income or life. The first indigenous insurance company in Malaysia was established in the 1950s. Before that, the bulk of the insurance business was dominated by foreign companies. Through their acceptance of premia from their clients, life insurance companies also act as mobiliser of savings which is long-term. On the other hand, premia paid on general insurance policies are not savings, as premia paid constitute service payments. These insurance companies play a significant role in national development by rechanneling their funds to the capital market, in the form of investment in Government and corporate securities.

Building Societies

A pioneer institution specialising in the provision of housing credit in Malaya, Singapore, Sabah and Sarawak, namely the

Malaysia Building Society Berhad (MBSB), was set up by the Commonwealth Development Corporation in 1950, at a time when the commercial banks preferred to concentrate on providing short-term loans for trade. In 1954, the building society was sold to the Malaysian Government. A few years later (1958) another building society was set up (Borneo Mortgage Housing Finance) to take over its activities in Sabah and Sarawak. Malaysia Building Society Bhd. became publicly quoted in 1963 by issuing MBSB shares to the public.

The operations of these building societies were principally funded by loans from the Employees Provident Fund, a source which has gained increasing importance over the years while their shareholders' funds and deposits mobilised showed a diminishing role. Total deposits outstanding of these two building societies amounted to about \$150 million at the end of 1984, as compared to \$1.4 billion of loans received.

Finance Companies

About a century after the establishment of the first commercial bank, the first finance company was established in 1959, to complement the credit operations of commercial banks. They specialise in providing loans for the purchase of consumer durables such as motor vehicles, machinery and equipment on hire purchase terms. They are also allowed to accept deposits but not demand deposits. Since their deposit rates were subject to ceilings prescribed by the Central Bank (it was only after October, 1978 when interest rates are freely determined by the banks), the commercial banks, in order to attract more deposits, began to establish wholly-owned finance companies which could compete for deposits through variation in their interest rates.

The first wholly bank-owned finance companies were established in 1960. The operations of the finance companies were originally regulated by government agencies directly responsible for policing the provisions of the Money Lenders Ordinance, 1951, the

Companies Act 1965, and the Hire Purchase Act, 1967. However, with their rapid growth, finance companies emerged as one of the largest mobilisers of deposits. Since this has a growing impact on the domestic monetary situation, their activities came under the supervision of the Central Bank in 1969, through the enactment of the Finance Companies Act, 1969. Under this Act, specific restrictions were imposed on their use of funds and the Central Bank is bestowed the power to prescribe statutory reserves and liquidity ratio.

By the end of 1984, there were 43 finance companies (of which 11 were subsidiaries of banks) with a branch network of 303 offices. Their deposit liabilities amounted to \$12.6 billion, and they continued to be the second largest deposit-taking institutions next to commercial banks.

Discount Houses

By early 1960s, with the existing financial institutions progressing rapidly, there arose a need for a convenient and reliable channel for those institutions particularly the commercial banks and the corporate sector, to "invest" their temporary surplus funds and to deal in money market papers so as to help financial institutions to adjust their asset holdings into the desired range of maturities. To assist this intermediation process in the short-term money market, the first discount house was established in 1963.

Together with the growth of financial institutions and the corporate sector, more discount houses were set up and by the end of 1984, there was a total of five discount houses. Total deposits of the discount houses rose from \$19 million at the end of 1964 to \$2 billion at the end of 1984.

Unit Trusts

The first investment company in Malaysia, the Malayan Unit Trusts Ltd., was established in 1959. However in 1963, the shares of this company were transferred to the Singapore management. Thus, the oldest unit trust company in existence today is the Asia Unit Trusts Bhd. which launched the Malaysian Investment Fund in 1966. By the end of 1980, there were five unit trust companies, managing 21 unit trusts funds, which issued 79.8 million units with a market value of \$162.2 million. In April 1981, to help the Government achieve the New Economic Policy in restructuring the society, the National Unit Trust Scheme (Amanah Saham Nasional) was launched. These unit trust companies are regulated under the Trustee Act, 1949 and part of Companies Act, 1965. As stipulated in the first Act, most of their investments are in "approved securities" which refers to public companies listed on the Kuala Lumpur Stock Exchange that have paid dividends in the preceding five years.

Funds mobilised by the unit trusts have grown tremendously since then. By the end of 1984, the National Unit Trust created a total of 1.1 billion units. At the end of 1984, there are seven unit trust companies managing 28 unit trusts funds. The accumulated investment of the 1.8 million unit holders amounted to \$2.4 billion.

Merchant Banks

In July 1970, another type of financial institution, the merchant bank, was established to provide specialised financial services which the commercial banks were not adequately equipped to perform. These included services such as underwriting, loan syndication, portfolio management, management advice and restructuring of ownership.

Merchant banks were originally incorporated under the Companies Act, 1965. Prior to 1979, the merchant banks operated under

a set of operational guidelines prescribed by the Central Bank, one of which was to maintain a statutory reserve of 1.5 per cent with effect from 1975. They are also allowed to accept deposits which exceed a certain amount (as determined by the Central Bank) from certain financial institutions. From January 1979, they were brought under the ambit of the Banking Act, 1973, whereby the merchant banks were required to comply with certain prescribed reserve requirement and liquidity ratio. This has enabled the Central Bank to have a direct influence on the availability of credit by varying statutory reserve and liquidity requirements. Subsequently, in March 1979, the merchant banks were permitted to accept fixed deposits from corporations and this relaxation boosted their resources.

As at the end of 1984 there are 12 merchant banks with 15 branches. Total deposits increased by 40 times from about \$100 million in 1973 to \$4 billion in 1984, of which one-third was placed by corporations.

Malaysian Industrial Development Finance

In West Malaysia, the first Government development finance institution, Malaysian Industrial Development Finance (MIDF), was established in 1960, following recommendations by the World Bank Mission that an industrial credit institution be set up to provide medium to long-term capital for private industrial enterprises to promote industrialisation. This need arose as the commercial banks traditionally focused their loan operations on essentially short-term lending to finance working capital only.

Total loans outstanding of MIDF was \$404.4 million at the end of 1984 and is the largest industrial finance institution to provide loans to the industrial sector.

Agricultural Bank

To promote agricultural development in the country, the Agricultural Bank was established in 1969. The Bank provides credit for the development of all aspects of agriculture, a large proportion of which is granted at a preferential rate and for the purpose of eradication of poverty, no interest rates are charged. The oldest form of lending is to the padi production credit scheme. Other forms of loans include tobacco production and marketing credit scheme, palm oil production, and land purchase and development. To mobilise funds for its loan operations as well as to encourage the savings habit, especially among the rural folks, the Bank introduced its fixed and savings deposits scheme in 1972.

Over the years, the Bank expanded its branch network such that by the end of 1984, it has 52 branches. Total deposits mobilised also increased rapidly from \$0.1 million in 1972 to \$1 billion by the end of 1984, reflecting in part, the money market operations of the banks, through which the bank accepted deposits of short to medium term from public authorities. Since the deposits mobilised far exceeded loans extended, the bank has been reinvesting the surplus funds with finance companies and merchant banks to generate additional income to support its lending operations.

Development Bank of Malaysia

Besides the MIDF and Agricultural Bank, a number of other development finance institutions were established in the mid 1970s. The Development Bank of Malaysia was set up in 1974 by a Government-owned commercial bank with the objective of promoting the participation of Bumiputera community in commerce and industry. The Bank provides medium and long-term loans for the purchase of fixed assets in approved projects as well as equity participation. At the end of 1984, total loans outstanding to the industrial sector amounted

to \$133.3 million. The main source of funds of the Bank is in the form of long-term loans from the Government.

Industrial Development Bank

In 1979, another development bank, the Industrial Development Bank was established by the Government to provide long-term finance to promote and help finance the expansion of productive capacity in capital-intensive and high-technology industries, especially those which are export-oriented, with a long gestation period. The operations of the Bank are mainly funded by long-term funds from the Government. At the end of 1984, total loans outstanding amounted to \$67.7 million. The bulk of the loans was directed to shipyards and shipping companies in the form of working capital credit facilities and purchase of vessels.

Credit Guarantee Corporation

Recognising the importance of the small-scale enterprises in economic development, the Central Bank helped set up the Credit Guarantee Corporation (CGC) in 1972. About 20 per cent of the capital was financed by the Central Bank while the balance, by the commercial banks. The corporation provides 60 per cent guarantee cover to commercial banks for designated loans extended to small-scale enterprises. In addition, loans extended under this CGC scheme is at a preferential rate of interest. To ensure that small-scale enterprises have ready access to bank credit at reasonable cost, the Central Bank imposed lending guidelines on commercial banks and finance companies to extend a certain proportion of its loans to small-scale enterprises.

Since its inception, the cumulative total of loans approved by the CGC amounted to \$2.4 billion at the end of 1984, as compared with \$11.8 million in 1973.

Sabah Credit Corporation, Borneo Development Corporation,
Sabah Development Bank

To assist in the economic diversification of the predominantly agricultural economies in East Malaysia, industrial development finance institutions in this area were set up, namely the Sabah Credit Corporation in 1956, Borneo Development Corporation in 1958, and the Sabah Development Bank in 1978. Most of the loans of these institutions was directed to the development of residential, industrial and commercial properties. Since 1979, the Sabah Development Bank has expanded its activities to trade financing, loan syndication and corporate finance and management services. The main sources of funds of these institutions are loans and deposits from the Sabah State Government.

II. INSTITUTIONS IN THE FINANCIAL STRUCTURE

The total assets of financial institutions included in this study increased by 36 fold from \$3.6 billion in 1960 to \$147.2 billion in 1984 (see Table 2). Out of the 31 institutions presented in this study, only 15 were in operations in 1960. Subsequently, seven began operations in the 1960s, six in the 1970s and three in the 1980s. While their total assets in 1960 was equal to a little over half of the Gross National Product, by 1984 they are two times the national product. During the period 1973-1984, they held over three-quarters of all financial instruments.

Generally, the Malaysian financial system may be divided into five groups of institutions, namely, monetary authorities (currency), deposit-type institutions, contractual savings, investment-type and others (see Chart 1). The Monetary Authorities is comprised of the Currency Board and the Central Bank. Prior to 1967, the Currency Board was the sole currency-issuing authority and since then, the Central Bank took over the Currency Board authority.

Chart 1: THE FINANCIAL SYSTEM OF MALAYSIA

Structure as at December 31, 1984

I MONETARY AUTHORITIES

CENTRAL BANK OF MALAYSIA

Total assets: \$15,927.2

of which:

Foreign Exchange Reserves: \$3,866.8m

8 branch offices in:

1 Kuala Lumpur 5 Kota Kinabalu

2 Penang 6 Kuching

3 Kuantan 7 Alor Setar

4 Johor Bahru 8 Ipoh

II DEPOSIT-TYPE INSTITUTION

ISLAMIC BANK

Total assets: \$160.8m

Total deposits: \$274.8m

Credits: \$74.8m

Investment: \$29.1m

COMMERCIAL BANKS

Total assets: \$86,727.4m

Total deposits: \$48,007.8m

Notes and balances: \$41,014.7m

of which:

77 Domestic (Total assets: \$47,397.4m)

18 Foreign (Total assets: \$19,000.0m)

218 Bank branches

of which:

970 Domestic banks

148 Foreign banks

91 Foreign banks' representative offices

FINANCE COMPANIES

Total assets: \$15,224.2m

41 Finance companies

393 Finance company offices

MERCHANT BANKS

Total assets: \$8,447.8m

12 Merchant banks

18 Merchant banks' offices

of which:

12 in Kuala Lumpur

1 in Johor Bahru

1 in Kota Kinabalu

1 in Penang

DISCOUNT HOUSES

Total assets: \$2,108.3m

8 Discount Houses

SAVINGS INSTITUTIONS

National Savings Bank

Total assets: \$1,430.7m

18 Branch offices

11 Regional Public Relations and Marketing Offices

818 Post offices with savings facilities

Urban Credit Co-operative

Total assets: \$2,013.7m

Co-operative Central Bank

Total assets: \$1,050.8m

Rural Credit Co-operative

Total assets: \$1,030.8m

Bank Rakyat: \$766m

III CONTRACTUAL SAVINGS INSTITUTION

PROVIDENT AND PENSION FUNDS

Total assets: \$23,947.0m

Employees Provident Fund

Total assets: \$20,642.0m

No. of contributors: 4.8m

Employees Provident Fund

Total assets: \$1,688.0m

No. of active contributors: 12

Armed Forces Fund

Total assets: \$1,600.0m

No. of contributors: 120,000

Other Statutory and

Private Provident and

Pension Funds

Total assets: \$1,700.0m

No. of contributors: 78,000

INSURANCE COMPANIES

Total assets: \$4,276.8m

of which:

1 Life Insurance companies

\$2,848.8m

General Insurance companies

\$1,278.0m

of which:

88 Domestic

13 Foreign

48 General Insurance companies

4 Life Insurance companies

14 Composite life and general

1 Reinsurance company

1 6-asset credit insurance company

IV INVESTMENT-TYPE INSTITUTION

UNIT TRUSTS

7 Unit trust companies

28 Unit trust funds

Size of funds: \$2.5bn

No. of unit holders: 1.8m

DEVELOPMENT FINANCE INSTITUTIONS

Total assets: \$7,894.9

Salah Development Bank

Agricultural Bank of Malaysia

Malaysian Industrial Development Finance

Development Bank of Malaysia

Industrial Development Bank of Malaysia

Subah Credit Corporation

Mersey Development Corporation

V OTHER

OTHER FINANCIAL INTERMEDIARIES

Malaysian Refining Society

Mersey Investing Mortgage Finance

Pilgrimage Management and Fund Board

Credit Guarantee Corporation

MONEY & FOREIGN EXCHANGE MARKET

7 money and foreign exchange brokers

STOCK EXCHANGES

Kuala Lumpur Stock Exchange

No. of companies listed: 281

Malay Stock Exchange

Division of the Kumpulan Keangsaan Malaysia Bhd

No. of companies listed: 8

Deposit-type institutions consist of commercial banks, finance companies, merchant banks, discount houses, agricultural bank, post office savings bank, and co-operatives. The group of contractual savings institutions includes the provident and pension funds and insurance companies. Investment-type institutions are the unit trusts companies. The main representatives of "other" types of institutions are industrial finance institutions, development banks and housing credit institutions.

In 1960, the largest group of financial institutions was the deposit-type institutions, which represented 42.5 per cent of total financial institutions' assets. The group was dominated by the commercial banks and finance companies. With rapid development, particularly the commercial banks and finance companies, this group continued to be the largest group up to 1984, and its asset share has increased to account for two-thirds (65.2 per cent) of all financial institutions. In view of the underdevelopment of the financial structure in 1960, the Monetary Authorities accounted for one-third (31.4 per cent) of all financial institutions' assets while contractual savings institutions represented 23.5 per cent. Over the years, both these 2 groups declined in importance to account for 10.8 per cent and 19.1 per cent of total assets of all financial institutions. Besides these 3 main groups of financial institutions, the "other" group mainly comprising of development institutions and investment-type institutions only represent about 3 per cent and 1 per cent of total assets of financial institutions.

In 1960, the total assets of financial institutions was approximately \$3.6 billion consisting mainly of gold and external reserves held by Central Bank (\$1.1 billion or 30.2 per cent, see Table 3), claims against non-financial units particularly in the form of Government securities and Treasury bills (\$0.7 billion or 21.2 per cent), loans to private sector (\$0.6 billion or 16.4 per cent) and corporate stock (\$0.02 billion or 0.6 per cent). By 1984, the total assets of financial institutions rose to \$147.2 billion, of which gold

accounted for only 6.1 per cent (\$9 billion). On the other hand, reflecting the rapid growth of banking institutions and proliferation of industrial finance institutions, loans to the private sector (including commercial bills) increased, to present about half (43.2 per cent or \$63.5 billion) of total assets. Government papers continued to make up about 20 per cent of total assets (\$33.6 billion) arising from the growth of institutions such as insurance and provident funds, which are required by statute to invest mainly in Government securities and the growth of commercial banks which are required to hold 20 per cent of their assets in liquid assets. As a group, financial institutions' holdings of Government securities accounted for more than 85 per cent of total Federal Government domestic debt during the period 1960-84. By the end of 1984, the share of corporate stocks also rose to 3.6 per cent (\$5.3 billion) of total assets of financial institutions.

Financial institutions, in turn, have been able to acquire these claims against certain households, business enterprises, Governments, and foreigners as a result of using funds placed by households, business enterprises and Government units, primarily by issuing currency, by accepting deposits and by incurring liabilities under insurance and pension contracts. In 1960, total deposits placed with financial institutions amounted to \$1.3 billion or 36.4 per cent of total liabilities. Commercial banks alone accounted for 73.2 per cent of total deposits mobilised. Over the years, deposits mobilised by financial institutions as a source of funds became more important, rising to 51.9 per cent (\$76.4 billion) of total liabilities by 1984. Due to the growth of other financial intermediaries, commercial banks' contribution declined slightly to 62.2 per cent of total deposits mobilised.

In 1960, currency issued by the Monetary Authorities (Currency Board), represented 24.3 per cent (\$0.9 billion) of total sources of funds. However, arising from the growth of other financial intermediaries as well as the public's increasing consciousness of the

cost of holding money, currency only represented 4.5 per cent (\$6.6 billion) of total liabilities by 1984.

In 1960, insurance premia and provident funds represented 21.6 per cent of total funds (\$0.8 billion). However, by 1984, its share to total source of funds declined to account for 17.2 per cent (\$25 billion).

Deposit-type Institutions

The largest group of financial institutions is the deposit-type institutions which is becoming increasingly important, with total assets rising from 42.5 per cent of the financial system in 1960 to 65.2 per cent at the end of 1984. Total assets of the group rose from \$1.5 billion in 1960 to \$95.9 billion in 1984 (see Table 4). As the name suggests, during the period 1960-1984, about three-quarters of the liabilities of this group of institutions is short or medium term deposits from the public (increasing from \$1.1 billion in 1960 to \$70.1 billion by end of 1984) being supplemented by capital and reserves (averaging about 7 per cent of total funds during the period 1960-84) and some placement of funds by other financial institutions. The resources of these institutions are utilised in providing credit to the deficit units. Loans which accounted for 37.7 per cent (\$0.5 billion) of their total assets in 1960, increased to 67.6 per cent (\$60.4 billion) of total assets by 1984. On the other hand, both deposits with other financial institutions and securities (mainly Government securities) declined from 34.6 per cent and 13.7 per cent in 1960 to 12.4 per cent and 8.7 per cent in 1984, respectively.

The major deposit mobilising institutions are the commercial banks and finance companies which made up nearly 90 per cent of the assets of the group. By the end of 1984, there are 38 commercial banks and 43 finance companies with a total of 1,019 branch offices, of which 716 are operated by commercial banks. The average population to banking office ratio used as an indicator of financial deepening

(excluding finance companies) improved from 62,800 back in 1960 to about 21,000 in 1984. Including finance companies, the average population to banking office ratio improved from 21,300 in 1969 to 14,800 in 1984.

Commercial banks There was an increase in the importance of commercial banks as proxied by the total assets of commercial banks as a ratio of assets of all financial institutions. In 1960, the commercial banks represented about one-third of the total assets of all financial institutions (\$1.2 billion). By 1984, half of the assets of all financial institutions was held by the commercial banks (\$67.1 billion). Being the sole institution that has current accounts, together with the Central Bank, they dominate the supply of narrow money (M1). As at the end of 1984, total demand deposits placed by the private sector with the commercial banks amounted to \$7.4 billion or 55.3 per cent of M1. Their deposit liabilities also dominate the other broader money supply concepts of M2 (currency, demand, fixed and savings deposits and net NCDs of the Central Bank and commercial banks) and M3 (which includes deposits of finance companies and merchant banks). Including fixed and savings deposits and net NCDs issued (quasi-money), commercial banks deposit liabilities accounted for 86.9 per cent of the M2 concept at the end of 1984 (\$39.9 billion). However, with the much more rapid growth of finance companies, the share of their deposit liabilities in the broader money supply concept was eroded, representing 65.9 per cent (\$38.5 billion) of M3, with another 20.7 per cent (\$12.1 billion) being represented by finance companies. As a proportion of total deposits mobilised by all financial institutions, about two-thirds (\$47.5 billion) was through the commercial banks at the end of 1984.

The importance of commercial banks was also reflected in their role as a major source of credit to the private sector. At the end of 1984, total loans to the non-financial private sector by the commercial banks amounted to \$41.3 billion or about two-thirds of the total credit provided by the financial institutions to the private

sector. The nature of lending was mainly in the form of advances under the overdraft system of lending, mainly for working capital of businesses. Based on data available, in 1969, more than three-quarters of total loans of banks was in overdraft and short-term advances. However, following advice from the Central Bank to change the granting of credit to term lending in order for them to have greater control over their borrowers, the proportion of overdraft to total loans was on a decline since 1971 to about 50 per cent in the 1980s (see Table 5). Most of the commercial banks loans were directed to finance trade (general commerce) and manufacturing companies. In addition, commercial banks are one of the major sources of financing for the purchase of houses, accounting for one-third of total loans to housing in the past 20 over years.

With about 10 per cent (\$6.9 billion) of its total assets invested in Government securities, commercial banks are the second major financial institutions that hold Government securities, increasing from 12 per cent in 1960 to 20 per cent in 1970s and thereafter. Together with the Central Bank and other institutions that are directly under the jurisdiction of the Central Bank, such as finance companies, merchant banks and discount houses, the group accounts for nearly half of the domestic Federal Government debt.

Finance companies. Finance companies are one of the fastest growing financial institutions in the country and their relative importance has been increasing, accounting about 0.3 per cent of total assets of all financial institutions in 1960 to about one-tenth by the end of 1984. In comparison to the commercial banks, the size of finance companies with total assets of \$15.2 billion at the end of 1984 is one-fifth the size of banks, a significant improvement from a mere size of 1 per cent in 1960. In 1960, the second largest deposit-taking institution next to the commercial banks was the National Savings Bank. However, the size of finance companies has already overtaken the National Savings Bank as early as 1967. Including leasing (which is another form of lending rather similar to

hire-purchase), total loans of the finance companies totalled \$10.2 billion at the end of 1984. The finance companies growth has also been impressive from the view point of being a mobiliser of deposits, specially after the freeing of interest rates for commercial banks in 1978 which enabled the finance companies to compete for funds with commercial banks by offering higher interest rates. By the end of 1984, about 16 per cent (\$12.6 billion) of total deposits mobilised by the financial institutions was through the finance companies, mainly in the form of fixed deposits. Similarly, total credit provided by finance companies accounted for 16 per cent (\$10.2 billion) of total loans by the financial institutions to the non-financial private sector.

To illustrate the contribution by the commercial banks and finance companies in mobilising deposits and extension of credit to the non-financial private sector, Table 6 provides data for selected years of 1960, 1970, 1980 and 1984 on deposits and loans of commercial banks and finance companies. This table shows that during the period, more than three-quarters of total deposits mobilised and loans extended to the private sector in the financial system was channelled through the commercial banks and finance companies. Moreover, the commercial banks and finance companies have become more important as mobilisers of deposits over the years, their total deposits rose from 73.8 per cent of total deposits of the financial system in 1960 to 78.7 per cent at the end of 1984. In terms of disbursement of credit, the finance companies gained tremendous progress over the same period to account for 16 per cent of total credit to the non-financial private sector by the end of 1984. On the other hand, the role of the commercial banks slackened. Therefore, the commercial banks and finance companies as a group continued to account for a greater share of credit generated through the financial system, increasing to 81 per cent by the end of 1984, as compared with 75.7 per cent in 1960.

Contractual Savings Institutions

Provident, pension and insurance funds formed the second largest group of financial institutions in the country, next only to the commercial banks. After the setting up of the first provident fund in 1898 for the workers of Penang Municipal Corporation, other provident funds were also set up to cover certain category of workers. Eventually by 1970, all Malaysian employees (with the exception of some workers such as domestic servants, and nomadic aborigines) have to contribute to the Employees Provident Fund. As a result of the growth in labour force and the spread in coverage, the contribution of the members of the Fund rose from about one-half of a million dollars in 1952 to \$4.4 million at the end of 1984, covering virtually all employees in the country. Total amount of 'forced' savings mobilised by the group increased from about \$20 million in 1952 to \$20.4 billion in 1984. As a proportion of GNP, savings through provident and pension funds rose from about 12 per cent in 1960 to about 30 per cent by 1984. In fact, up to 1972, savings mobilised by provident, pension and insurance funds exceeded deposits placed by the private sector with the financial institutions (excluding demand deposits which is basically for transaction purposes). During 1984, total contributions increased by \$3.4 billion, accounting for nearly one-fifth of gross national savings.

This development is reflected in the share of the assets of the group as a proportion of total assets of the financial system which increased from 23.5 per cent in 1960 to a peak of 29 per cent in 1967 then declining to 19.1 per cent in 1984, partly as a result of more rapid growth of other financial institutions. Moreover, the contractual nature of the provident and pension funds precluded the attraction of new savings through higher interest rates, and their growth depended very much on the increase in coverage brought about by legislation, the natural growth of the workforce, and any increase in contribution rates. Total assets of the group increased from \$0.8 billion in 1960 to \$28.2 billion in 1984 (Table 7). The bulk of their

funds (about 70 per cent) continued to be invested in Government securities, as required by statute. However, their importance in providing funds to the Government has declined over the years, from a share of 78 per cent of total Government securities held by financial institutions in 1960 to 55.3 per cent in 1984. This is in contrast to the Central Bank and commercial banks which when combined, increased their holdings of Government securities, from 13.2 per cent in 1960 to 35.1 per cent in 1984 (see Table 8).

The mobilisation of resources through the provident, pension and insurance funds has enabled Malaysia to deploy these funds for development, particularly for the financing of the development programmes of the Federal Government. The holdings of Government securities as a percentage share of total assets rose from 70.3 per cent in 1960 to a peak of 76.2 per cent in 1973 but declined subsequently to 65.8 per cent in 1984. This shift of assets away from Government securities reflected partly the search for higher returns in the form of direct loans and investments in corporate securities. Loans rose from 2.7 per cent in 1960 to 9.4 per cent in 1984 while corporate securities which constituted 1.5 per cent in 1960 increased to 7 per cent in 1984. The largest in this category is the Employees Provident Fund (EPF), which alone represented 73.3 per cent (\$20.6 billion) of total assets of the group at the end of 1984.

Monetary Authorities

The third sub-group is the Monetary Authorities of the country whose assets increased from \$1.1 billion in 1960 to \$15.9 billion in 1984. Within the Monetary Authorities, the Currency Board contributed the major portion in 1960, representing about a quarter of the total assets of the financial system. However, after passing on its function of sole currency-issuing authority to the Central Bank in 1967, its assets declined significantly to account for 3.7 per cent of total assets of the financial system at the end of 1967. With effect from November 1979, the Currency Board ceased to function and its

assets were distributed to the participating Governments of Malaysia, Singapore and Brunei.

The Central Bank, which only represented about 5.2 per cent of the total assets of the financial system in 1960, expanded to account for 20 per cent of total assets of the financial system in the late 1960s after taking over the function of sole currency issues. However, reflecting the more rapid growth of other financial institutions in the 1970s and early 1980s, the percentage share of the Central Bank dwindled to 10.8 per cent of the total assets of the financial system in 1984. The liabilities of the Monetary Authorities are basically currency issued, making up 77.6 per cent of total liabilities in 1970 (Table 9). Over the years, even though currency issued remained to be the predominant liability, its share diminished to 41.2 per cent by the end of 1984. This was due mainly to the higher deposits placed by the public sector which rose from 9.3 per cent in 1960 to account for 18.2 per cent in 1984. Reflecting the rapid expansion of commercial banks, finance companies and merchant banks, deposits placed by them with the Central Bank as statutory reserves also increased from 4.7 per cent of total liabilities in 1960 to 16.1 per cent in 1984. In 1960, almost the entire fund of the Monetary Authorities was in the form of gold (96.3 per cent). Over the years, its proportion declined, such that by 1984, gold represented 56.8 per cent of total assets. The balance of the funds was held mainly in the form of Government securities, whose share rose from 0.8 per cent in 1960 to 30.2 per cent in 1984.

Other Financial Institutions

The fourth major group of financial institutions is the "other" which comprised mainly Government-owned development financial institutions and housing credit institutions. This sub-group made up about 2.6 per cent (\$0.1 billion) of the system's total assets in 1960. By 1984, they constituted 3.4 per cent (\$5 billion) of total assets of all financial institutions (Table 10). Their main sources

of funds are capital injected and loans from the Government. In turn, these funds are channelled as loans to the private sector. In 1960, 93.4 per cent of the assets was loans extended to the private sector, but its proportion declined to 73.4 per cent by 1984, when a larger portion of funds is placed with other financial institutions and invested in corporate securities. Deposits placed with other financial institutions which accounted for 3.6 per cent in 1960 rose to 7.2 per cent in 1984, while investment in corporate securities increased from 0.3 per cent in 1960 to 9 per cent in 1984. The largest institution in the group is the Malaysian Building Society Berhad, which is funded by the Government to provide financing for the purchase of residential properties, in line with the Government policy of encouraging house ownership.

Investment-type Institutions

In this study, investment-type institutions only cover 2 institutions, namely, Mara Unit Trust and National Unit Trust which were set up in 1966 and 1980, respectively. The Mara Unit Trust accounted for 0.1 per cent of total assets of financial system all these years. With the addition of National Unit Trust in 1980, total assets of these unit trust companies amounted to \$2.1 billion in 1984, representing 1.4 per cent of total assets of the financial system (Table 11). These institutions received funds from the Government in the form of capital subscription and also through the sale of their own common stock to individuals and these funds are used primarily to acquire corporate securities. Even though investment type institutions only represent 1 per cent of total assets of the financial system, they accounted for more than one-third of the total holdings of corporate securities by the financial system (Table 12). The portfolio of investment of National Unit Trust comprised largely of shares of blue-chip companies purchased from the National Equity Corporation. The total number of unit holders amounted to 1.8 million at the end of 1984.

Summary

The rapid expansion in the banking system, which had already been of importance before 1960, and the development of new financial intermediaries contributed to the sharp increase in the importance of financial institutions. The Malaysian financial system is characterised by the pre-eminence of commercial banks among financial institutions. In 1960, the commercial banks accounted for more than one-third of the total assets of the financial system (34.7 per cent). During the period 1960-84, the assets of commercial banks rose by 54 times. By the end of 1984, the commercial banks represented about half of the total assets of the financial system (45.6 per cent).

On the other hand, the Employees Provident Fund which constituted about one-fifth of the assets of financial institutions in 1960, now only holds 14 per cent. The Monetary Authorities which was the second largest group of financial institution in 1960, with a share of 31.4 per cent of total assets, took a share of 10.8 per cent and ranked below Employees Provident Fund.

One of the most notable changes was the rise in the asset share of finance companies, from only 0.3 per cent in 1960 to 10.3 per cent in 1984. As a result, finance companies emerged to be the fourth largest financial institutions in 1984 from the 10th position in 1960. Together with the commercial banks they accounted for more than three-quarters of deposits mobilised and loans extended to the private sector that is channelled through the financial system. Since both the commercial banks and finance companies are under the direct jurisdiction of the Central Bank, the dominance of commercial banks and finance companies in the financial system would have implications for the role of monetary policy.

Merchant banks, although a relatively young institution (being set up in 1970), rose rapidly to account for 3.8 per cent of total assets by the end of 1984. On the other hand, the share of Post

Office Savings Bank (NSB) declined, reflecting tough competition for deposits from other deposit-taking institutions. Growth of life insurance companies was also unimpressive, contributing about 2 per cent of total assets in 1984 (2.3 per cent in 1960), such that total insurance premia as a proportion of GNP remained relatively low at 3.7 per cent in 1984 (1.2 per cent in 1960).

The Unorganised Money Market

There are no national estimates of the size of the unorganised money market (informal credit institutions). However, studies of certain regions of the rural sector between 1964-74 indicated that informal lenders in Peninsular Malaysia are the principal sources of credit of small farmers growing padi, rubber, coconut and pineapple.

These unorganised sources of finance are dealers, middlemen, provision shops and money lenders. However, with the establishment of specialised credit agencies such as the Agricultural Bank, Farmers Organisation Authorities and Bank Rakyat (rural cooperative bank) it is conjectured that the proportion of informal (unorganised) sources of credit to the agricultural sector would be reduced over the past few years.

III. INSTRUMENTS IN THE FINANCIAL STRUCTURE

Financial institutions have an important function in providing a market mechanism for the transfer of surplus funds of savers to the deficit units, the more efficient investors. This is because not all savers are entrepreneurs, and entrepreneurs cannot save enough to finance their desired investment expenditures. This deficiency could be remedied without recourse to financial intermediaries if the securities market is perfect, where savers are willing to purchase securities from efficient entrepreneurs. However,

the characteristics of primary securities do not always coincide with the preferences of savers, especially in terms of liquidity, safety, divisibility, and the special services specific financial assets provide (e.g., money as a medium of exchange, insurance, etc).

The mechanism whereby financial institutions effect this transfer is to issue their liabilities to savers, in exchange ultimately for their monetary claims upon such assets, and to provide the assets so accumulated to investors by purchasing their primary securities.

In Malaysia, as shown in Table 13, of the total financial instruments, about one quarter (25.7 per cent) was in the form of equity securities during the period, while percentage share of total claims as a proportion of all claims accounted for the balance of 74.3 per cent. It should be cautioned that the data compiled for equity securities is the market value, which probably have fluctuated depending on market conditions in the stock exchange, declining from 32.5 per cent of total financial instruments in 1973 to as low as 20.5 per cent in 1977 before reaching its peak of 32.9 per cent in 1983. Subsequently, equity securities dropped to 26.1 per cent of total financial instruments in 1984, when share prices were in its doldrums.

One of the most important characteristics of a country's financial structure and development is the extent to which the issues of domestic non-financial and of foreign issues are absorbed or held by domestic financial sectors rather than domestic non-financial sectors or by foreigners.^{1/} In Malaysia, the domestic financial institutions have absorbed or held an increasing proportion of issues of domestic non-financial institutions, from about 30 per cent in 1973 to 37.6 per cent in 1984. Of the claims against non-financial sectors, loans to the private sector (including commercial bills) had risen considerably from about 14 per cent of all financial instruments in 1973 to 23 per cent in 1984. On the other hand, claims against the

Government (Government papers) have declined from 15 per cent in 1973 to 12.7 per cent in 1984.

Over the years from 1973-1984, about slightly less than half of the financial instruments are liquid in the sense that they are marketable in the open market. The marketable financial instruments included currency, Treasury bills, Government securities and corporate securities. As a proportion of all financial instruments, the share of marketable financial instruments has declined from 52 per cent in 1973 to as low as 41.3 per cent in 1984.

The share of narrow money (currency and demand deposits), i.e., the non-yielding assets to all financial instruments has been on a declining trend from 10.2 per cent in 1973 to 5.6 per cent in 1984. Interest-bearing instruments, on the other hand, have become increasingly more important reflecting a shift in preference for interest-bearing instruments such as fixed and savings deposits, partly due to the increased accessibility to branch offices of deposit-type institutions. The percentage share of interest-bearing deposits (fixed and savings and negotiable certificates of deposits) over all financial instruments rose from about 16 per cent in 1973 to about 21 per cent in 1984.

The maturity structure of fixed deposits issued by commercial banks ranged from 1 month, 3 months, 6 months, 9 months, 12 months and over 12 months. The finance companies are allowed to issue fixed deposits of similar maturity but of a longer nature of 3 months and above. The maturity structure of fixed deposits placed with merchant banks are very much more flexible in order to gear them towards the depositors' needs, for example, it could be from 1 month to less than 3 months, 3 months to less than 6 months, 6 months to less than 9 months, 9 months to less than 12 months, 12 months and more.

1/ Raymond William Goldsmith, Financial Structure and Development, New Haven: Yale University Press, 1969, p.317.

Other financial institutions that are allowed to issue fixed deposits are the Agricultural Bank, Bank Rakyat (rural cooperative bank), and the Cooperative Central Bank. In the case of National Savings Bank, it is only allowed to issue fixed deposits in 1984. All the deposit-type institutions have savings accounts.

The share of insurance premiums, provident and pension funds to total financial assets declined from 11 per cent in 1973 to 9.6 per cent in 1984. Their share to total claims against financial institutions also showed a downward trend, from about 29 per cent in 1973 to about 26 per cent in 1983.

Two new financial instruments were introduced in 1979 to further develop the money market, namely, negotiable certificates of deposits and bankers acceptances. The negotiable certificate of deposit (NCD) is a relatively new instrument introduced in May 1979 to further develop the money market. It is a special kind of fixed deposit which is negotiable. NCDs are issued at multiples of 3 months, from 3 months to 3 years, in denominations of \$50,000 to \$1 million. This type of negotiable fixed deposit is popular, especially among corporate clients, as reflected by its significant increase from \$200.3 million in 1979 to \$4.3 billion in 1984.

A new form of short-term trade financing, bankers acceptance (BAs) was introduced in 1979 together with the NCDs. A BA is a bill of exchange drawn on and accepted by either a commercial bank or merchant bank for periods of 30 to 200 days. These BAs (to a certain amount) can be taken as liquid assets in the computation of liquidity ratio by banks and can be discounted with the Central Bank.

IV. EFFECTIVENESS OF MONETARY POLICY

It is widely believed that the lack of institutional features, such as diversified financial institutions, banking habits

as reflected by high currency/money ratio and well-knit money and capital markets posed constraints on the effectiveness of monetary policy. In the case of Malaysia, as shown in the earlier sections, there has been an increase in the number and variety of financial institutions as well as in the proportion of total financial assets relative to Gross National Product. The marginal rate of financialisation of national wealth, one of the measures of the development of the financial structure, which is derived by dividing the change in financial assets over the Gross Domestic Product, has increased in Malaysia, from 6 per cent in 1961 to 30 per cent in 1984 (Table 14).

In section III, the importance of financial institutions in providing a mechanism for the transfer of surplus funds of savers to the deficit units was also discussed. It is argued that the more perfect the financial markets are, the more optimum allocation of funds to investment can be achieved. In this way, the financial system accommodates economic growth. On the other hand, to the extent that the financial system is underdeveloped and/or inefficient, it restricts growth, lower than could be optimally achieved.^{2/}

The banking habit in the country has also become more widespread with the increased number of financial institutions and varieties of financial instruments. One of the proxies of these banking habit is the share of currency to money supply. In Malaysia, the ratio has declined over the past 20 years, particularly currency to the broader measure of money (M2 and M3). The ratio of currency to M1 was about 40-50 per cent during 1960-84, while the ratio of currency to M2 dropped drastically from 41.4 per cent in 1960 to 13 per cent in 1984. In terms of the broader measure of money supply (M3), the ratio fell from 19.9 per cent in 1973 to 10.2 per cent in 1984.

^{2/} H.T.Patrick, Financial Development and Economic Growth in Underdeveloped Countries, p. 46.

All these indicators indirectly point to the fact that the progressive development in the financial structure in Malaysia is conducive for the Central Bank to conduct its monetary policy. Nevertheless, to determine the effectiveness of monetary policy by the financial structure, one would also need to examine the transmission mechanism of a change in monetary policy (instrument) and to assess whether, the ultimate targets are achieved. However, a study of the transmission mechanism is not in the scope of this paper. This paper, besides examining the institutional features as discussed earlier, attempts to look at what are the ultimate targets of monetary policy and whether monetary instruments used were able to achieve the targets over the past 25 years.

In the conduct of monetary policy in Malaysia, the choice of monetary instruments available to Bank Negara Malaysia are statutory reserve requirement, liquidity ratio, direct regulation on the availability of credit (for e.g., lending guidelines to priority sectors and credit ceiling), interest rates and open market operations. It is through these instruments that, via the cost of capital and availability effects, aggregate demand and ultimately economic growth are influenced, which is the main object of monetary policy. Besides this objective, others include maintaining price stability, bridging the savings-investment gap, achieving a viable balance of payments position and to restructure society as contained in the New Economic Policy.

During the early stages between 1959-68, the emphasis of the Central Bank was on interest rates to stimulate bank credit while at the same time being cautious to prevent possible capital outflows. In the export boom of 1969, the Central Bank raised the statutory reserve ratio of commercial banks from 3.5 per cent to 5 per cent in order to dampen growing liquidity of the banking system. This has resulted in higher economic growth without inflation. In 1971-72, with the onset of recessionary tendencies, monetary policy was gradually eased to stimulate expansion in business activity and private investment,

through reducing lending and borrowing rates of commercial banks. Since the commercial banks and finance companies had significant excess liquidity, the statutory reserve ratio of commercial banks was raised from 5 per cent to 8.5 per cent, while a new statutory reserve ratio of 2.5 per cent was introduced for finance companies, to provide these institutions with a gauge for the desirable minimum liquidity levels and so that they could step up their lending operations.

By late 1972 to 1974, there was a cyclical upswing in economic activity being spurred off by a boom in export prices. The Central Bank was then faced with inflationary pressures. Consumer prices began to rise at an average of 3.2 per cent in 1972 to 10.5 per cent in 1973 and reached its peak of 17.4 per cent in 1974 (the highest recorded in the last 25 years). Growth in M1 was close to 40 per cent in 1973 and M2 growth was about 30 per cent. To solve such economic ills, the Central Bank introduced a series of monetary measures from 1972-74. Deposit and lending rates were increased in 1972. In 1973, both statutory and liquidity ratios were raised. Since the money supply growth was extremely high up to the end of 1973, credit ceilings of 20 per cent and 25 per cent were imposed in 1974 for commercial banks and finance companies, respectively. With the moderation of monetary growth, the credit ceilings were subsequently relaxed later in the year. From 1975 to 1977, monetary measures were more easy as credit ceilings were abolished and the bank deposit and lending rates and statutory reserves ratio were lowered.

In mid-1978, when liquidity was tight due to more rapid growth in loans than deposits, the Central Bank relieved the tight liquidity situation by reducing the statutory reserve ratio. From 1978 to 1984, the statutory reserve and the liquidity requirement of banks, finance companies and merchant banks remained unchanged. The Central Bank also deregulated interest rates as commercial banks were allowed to fix their own interest rates in October 1978. From then onwards, the Central Bank conducted open market operations and moral suasion to regulate interest rates. The priority of monetary policy

continued to be price stability and monetary discipline. Generally, the objective of price stability has been achieved as reflected by the low rate of increase in consumer price index, averaging about 5.6 per cent during 1979-84. However, the financial structure does impinge on the effectiveness of monetary policy to a certain extent as shown in the following sections on interest rate policy and open market operations:

(i) Interest Rate Policy

Prior to 1978, the deposit and lending rates of commercial banks were fixed by the Central Bank in consultation with the Association of Banks. In October 1978, the Central Bank freed the deposit and lending rates of commercial banks, leaving rates to be determined by competition among financial institutions. The Central Bank's influence on interest rates continued, but indirectly through intervention in the money market to smoothen out fluctuations in the inter-bank market, thereby ensure that rates can attract savings while not discouraging investment. In the past few years, the freeing of lending and deposit rates did not promote the desired competition, as illustrated below:

Interest rates tended to be rigid downwards. There were banks which after reducing their deposit rates, did not adjust their lending rates. Thus in November 1981, the Central Bank asked the banks to peg their lending rates to their base lending rates, which in turn were based on their cost of funds. All the banks are required to display their deposit and base lending rates and their lending rates should move in consonance with their deposit rates.

Circumstances have arisen in which the smaller banks have raised their deposit rates to attract deposits while the bigger banks with larger deposit base have not followed the change thereby resulting in bigger banks losing out in the competition.

These events highlight the fact that the institutional framework in Malaysia is not conducive enough for effective competition among financial institutions, stemming from the large differential in the size of banks.

Currently, studies are being made as to the appropriate changes in the financial structure that will be conducive for greater and more effective competition among financial institutions.

(ii) Open Market Operations

The Central Bank influences interest rates and liquidity in the system through buying and selling of securities in the open market. However, in Malaysia, as discussed in the earlier sections on sources and uses of funds, the major institutions such as provident funds that hold Government securities hold the securities till maturity. Therefore, with these underdeveloped money and capital markets, there is limited scope for the Central Bank to conduct its open market operations.

The Central Bank acts as buyer and seller of last resort of Government papers. This has also made the Central Bank's tasks of managing liquidity more difficult. When the Central Bank intends to affect liquidity in the system by reducing statutory reserves, instead of utilising the new excess reserves as loans, the commercial banks sometimes come back to the Central Bank to purchase Government papers as was done in April 1985. Since there are no other means of short term investment for the commercial banks, they turned to the Central Bank for Government securities. As a result, the originally-intended expansionary efforts of the Central Bank were offset on this occasion. They liquidated their Government securities only when the banks gradually stepped up their lending operations.

V. SUMMARY AND CONCLUSION

The financial structure in Malaysia has undergone a remarkable transformation in terms of range of institutions in the system from commercial banks to unit trusts, merchant banks and discount houses. In terms of financial instruments or range of services offered, the change was also tremendous - from fixed and savings deposits to negotiable certificates of deposits, bankers acceptances and lately, automatic teller machines and the onset of electronic transfer of funds. The progress in the development of the Malaysian financial structure as also reflected by improved banking habit and diversified financial institutions seemed to be conducive to the implementation of monetary policy. So far, the Central Bank has successfully maintained price stability and allocated credit to the priority sectors. However, due to imperfections in the financial system and the underdeveloped nature of the money and capital markets, the Central Bank faces shortcomings in the promotion of market-determined interest rates and the use of open market operations as a monetary instrument.

Table 1

COMMENCEMENT OF BUSINESS OF FINANCIAL INSTITUTIONS
IN MALAYSIA

<u>Financial Institution</u>	<u>Year of Commencement of business</u>
Commercial banks - Chartered Merchantile	1859
Board of Commissioners of Currency	1897
Penang Municipal Provident Fund	1898
Co-operatives	1920s
National Savings bank (previously POSB)	1948
Insurance Companies	1950s
Malaysian Building Society	1950
Employees Provident Fund	1951
Sabah Credit Corporation	1956
Borneo Development Corporation	1958
Borneo Housing Mortgage Finance	1958
Central Bank of Malaysia	1959
Finance Companies	1959
Malaysia Industrial Finance Bhd.	1960
Bank Rakyat (rural co-operative bank)	1960
Cooperative Central Bank	1961
Teachers Provident Fund	1962
General Insurance Company	1962
Discount Houses	1963
Pilgrim Management Fund Board	1963
Unit Trust	1966
Agricultural Bank Malaysia	1969
Merchant Bank	1970
Armed Forces Fund	1973
Credit Guarantee Corporation	1973
Development Bank of Malaysia	1974
Sabah Development Bank	1978
Industrial Development Bank	1979
National Unit Trust	1980
Farmers Organisation Authority (rural-co-operatives)	1981
Islamic Bank of Malaysia	1983

Table 2
ASSETS OF THE FINANCIAL SYSTEM

	Outstanding (\$m)				% Composition			
	1960	1970	1980	1984	1960	1970	1980	1984
I) MONETARY AUTHORITIES	1114.3	2421.5	12994.1	15920.9	31.4	20.8	17.5	10.8
i) Bank Negara Malaysia	184.2	2226.7	12994.1	15920.9	5.2	19.2	17.5	10.8
ii) Currency Board	930.1	194.8	0.0	0.0	26.2	1.7	0.0	0.0
II) DEPOSIT TYPE INSTITUTIONS	1509.4	5688.0	44617.2	95931.3	42.5	49.0	60.2	65.2
i) Commercial Banks	1232.0	4460.2	32186.1	67097.2	34.7	38.4	43.4	45.6
ii) Finance Companies	10.0	531.0	5635.5	15224.1	0.3	4.6	7.6	10.3
iii) Merchant Banks	0.0	0.1	2228.7	5542.6	0.0	0.0	3.0	3.8
iv) Discount Houses	0.0	41.7	1291.6	2106.3	0.0	0.4	1.7	1.4
v) Bank Pertanian Malaysia	0.0	10.2	812.6	1376.5	0.0	0.1	1.1	0.9
vi) National Savings Bank	156.9	296.0	1279.0	1539.7	4.4	2.5	1.7	1.0
vii) Bank Rakyat	0.0	25.0	386.5	766.3	0.0	0.2	0.5	0.5
viii) Cooperative Societies	110.5	316.1	675.9	963.2	3.1	2.7	0.9	0.7
ix) Farmers' Organisation Authority	0.0	0.0	0.0	264.9	0.0	0.0	0.0	0.2
x) Cooperative Central Bank	0.0	7.7	121.3	1050.5	0.0	0.1	0.2	0.7
III) CONTRACTUAL SAVINGS INSTITUTIONS	835.6	3157.1	13846.3	28172.6	23.5	27.2	18.7	19.1
i) Employees' Provident Fund	632.6	2265.5	9480.9	20642.0	17.8	19.5	12.8	14.0
ii) Teachers' Provident Fund	0.0	78.1	131.5	167.8	0.0	0.7	0.2	0.1
iii) Other Provident Fund	100.0	374.0	1129.1	1938.5	2.8	3.2	1.5	1.3
iv) Life Insurance	83.0	324.0	1657.5	2948.9	2.3	2.8	2.2	2.0
v) General Insurance	20.0	115.5	818.8	1276.6	0.6	1.0	1.1	0.9
vi) Armed Forces	0.0	0.0	628.5	1198.8	0.0	0.0	0.8	0.8
IV) INVESTMENT TYPE INSTITUTIONS	0.0	8.4	108.9	2122.6	0.0	0.1	0.1	1.4
i) Unit Trust	0.0	8.4	76.4	158.8	0.0	0.1	0.1	0.1
ii) Amanah Saham Nasional	0.0	0.0	32.5	1963.8	0.0	0.0	0.0	1.3
V) OTHERS	93.5	342.8	2586.5	5037.9	2.6	3.0	3.5	3.4
i) Malaysian Industrial Devt. Finance Bhd.	0.0	98.4	354.4	530.0	0.0	0.8	0.5	0.4
ii) Borneo Development Corporation	0.0	20.8	53.0	65.9	0.0	0.2	0.1	0.0
iii) Sabah Development Bank	0.0	0.0	589.8	1080.7	0.0	0.0	0.8	0.7
iv) Sabah Credit Corporation	1.1	4.5	97.0	162.5	0.0	0.0	0.1	0.1
v) Development Bank of Malaysia	0.0	0.0	154.0	522.7	0.0	0.0	0.2	0.4
vi) Bank Kemajuan Perusahaan Malaysia	0.0	0.0	132.0	194.8	0.0	0.0	0.2	0.1
vii) Borneo Housing Mortgage Finance Bhd.	4.5	51.8	241.0	622.6	0.1	0.4	0.3	0.4
viii) Malaysia Building Society Berhad	87.9	150.8	758.3	1363.0	2.5	1.3	1.0	0.9
ix) Pilgrims Management & Fund Board	0.0	16.5	196.8	465.1	0.0	0.1	0.3	0.3
x) Credit Guarantee Corporation	0.0	0.0	10.2	30.6	0.0	0.0	0.0	0.0
TOTAL	3552.8	11617.8	74153.0	147185.3	100.0	100.0	100.0	100.0

Table 3
SOURCES AND USES OF FUNDS OF THE FINANCIAL SYSTEM

	Outstanding (\$m)				% Composition			
	1960	1970	1980	1984	1960	1970	1980	1984
SOURCES								
Capital and Reserves	287.6	979.5	4231.1	11315.0	8.1	8.4	5.7	7.7
Currency	364.7	1131.7	5104.6	6554.7	24.3	9.7	6.9	4.5
Demand Deposits	477.0	1068.1	5326.2	8088.3	13.4	9.2	7.2	5.5
Other Deposits	816.7	3970.2	34232.9	68340.7	23.0	34.2	46.2	46.4
Public Sector	217.7	1222.8	6777.4	10791.6	6.1	10.5	9.1	7.3
Other Financial Intermediaries	53.4	302.9	5832.4	12859.1	1.5	2.6	7.9	8.7
Private Sector	545.6	2444.5	21623.1	44690.0	15.4	21.0	29.2	30.4
Loans	47.1	252.0	1667.2	3295.0	1.3	2.2	2.2	2.2
Domestic	47.0	232.0	1648.6	3292.0	1.3	2.0	2.2	2.2
Foreign	0.1	20.0	18.6	3.0	0.0	0.2	0.0	0.0
Funds from Other Fin. Inst.	131.0	679.0	3914.7	8647.4	3.7	5.8	5.3	5.9
Domestic	58.0	426.2	1188.7	3117.1	1.6	3.7	1.6	2.1
Foreign	73.0	252.8	2726.0	5530.3	2.1	2.2	3.7	3.8
Life Insurance & Provident Funds	767.9	2882.0	12210.6	25378.3	21.6	24.8	16.5	17.2
Other Liabilities	160.8	655.3	7465.7	15565.9	4.5	5.6	10.1	10.6
Domestic	153.8	556.1	6937.5	15031.0	4.3	4.8	9.4	10.2
Foreign	7.0	99.2	528.2	534.9	0.2	0.9	0.7	0.4
TOTAL	3552.8	11617.8	74153.0	147185.3	100.0	100.0	100.0	100.0
USES								
Currency	80.4	97.2	419.8	688.9	2.3	0.8	0.6	0.5
Deposits with Other Fin. Inst.	527.0	1242.8	8831.1	15422.3	14.8	10.7	11.9	10.5
Domestic	204.2	1035.1	7603.1	13889.2	5.7	8.9	10.3	9.4
Foreign	322.8	207.7	1228.0	1533.1	9.1	1.8	1.7	1.0
Bills	87.4	829.5	4600.6	7346.2	2.5	7.1	6.2	5.0
Treasury	40.6	545.4	1416.4	2769.1	1.1	4.7	1.9	1.9
Commercial	46.8	284.1	3184.2	4577.1	1.3	2.4	4.3	3.1
Loans	632.3	2999.7	26821.5	66719.1	17.8	25.8	36.2	45.3
Public Sector	0.1	55.1	795.5	1957.4	0.0	0.5	1.1	1.3
Other Financial Intermediaries	50.7	403.3	937.8	5802.0	1.4	3.5	1.3	3.9
Private Sector	581.5	2541.3	25088.2	58959.7	16.4	21.9	33.8	40.1
Securities	966.0	3631.2	17992.3	36120.2	27.2	31.3	24.3	24.5
Malaysian Government	712.5	3091.4	15959.5	30791.2	20.1	26.6	21.5	20.9
Foreign Government	233.4	194.6	31.3	46.6	6.6	1.7	0.0	0.0
Corporate	20.1	345.2	2001.5	5282.4	0.6	3.0	2.7	3.6
Gold and Reserves	1072.7	2229.1	9708.6	9041.1	30.2	19.2	13.1	6.1
Other Assets	187.0	588.3	5779.1	11847.5	5.3	5.1	7.8	8.0
Domestic	159.1	566.5	5124.5	10825.5	4.5	4.9	6.9	7.4
Foreign	27.9	21.8	654.6	1022.0	0.8	0.2	0.9	0.7
TOTAL	3552.8	11617.8	74153.0	147185.3	100.0	100.0	100.0	100.0

Table 4
SOURCES AND USES OF FUNDS OF DEPOSIT TYPE INSTITUTIONS

	Outstanding (\$m)				% Composition			
	1960	1970	1980	1984	1960	1970	1980	1984
SOURCES								
Capital and Reserves	103.6	417.6	1936.4	5783.0	6.9	7.3	4.3	6.0
Currency	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Demand Deposits	477.0	1068.1	5326.2	8088.3	31.6	18.8	11.9	8.4
Other Deposits	644.8	3124.3	28680.5	62034.2	42.7	54.9	64.3	64.7
Public Sector	114.2	585.1	4078.6	7819.7	7.6	10.3	9.1	8.2
Other Financial Intermediaries	0.8	104.0	4232.4	10265.5	0.1	1.8	9.5	10.7
Private Sector	529.8	2435.2	20369.5	43949.0	35.1	42.8	45.7	45.8
Loans	19.1	80.6	384.7	593.5	1.3	1.4	0.9	0.6
Domestic	19.0	80.6	384.7	593.5	1.3	1.4	0.9	0.6
Foreign	0.1	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Funds from Other Fin. Inst.	131.0	679.0	3900.4	8647.4	8.7	11.9	8.7	9.0
Domestic	58.0	426.2	1174.4	3117.1	3.8	7.5	2.6	3.2
Foreign	73.0	252.8	2726.0	5530.3	4.8	4.4	6.1	5.8
Life Insurances & Provident Funds	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Other Liabilities	133.9	318.4	4389.0	10784.9	8.9	5.6	9.8	11.2
Domestic	126.9	283.5	4181.1	10276.7	8.4	5.0	9.4	10.7
Foreign	7.0	34.9	207.9	508.2	0.5	0.6	0.5	0.5
TOTAL	1509.4	5688.0	44617.2	95931.3	100.0	100.0	100.0	100.0
USES								
Currency	72.0	97.2	353.5	599.9	4.8	1.7	0.8	0.6
Deposits with Other Fin. Inst.	471.0	1104.6	7170.2	11907.1	31.2	19.4	16.1	12.4
Domestic	155.0	914.0	5942.2	10374.0	10.3	16.1	13.3	10.8
Foreign	316.0	190.6	1228.0	1533.1	20.9	3.4	2.8	1.6
Bills	87.4	829.3	4580.3	7323.2	5.8	14.6	10.3	7.6
Treasury	40.6	545.2	1416.4	2769.1	2.7	9.6	3.2	2.9
Commercial	46.8	284.1	3163.9	4554.1	3.1	5.0	7.1	4.7
Loans	522.2	2534.7	24132.8	60370.3	34.6	44.6	54.1	62.9
Public Sector	0.1	41.7	795.5	1957.4	0.0	0.7	1.8	2.0
Other Financial Intermediaries	40.7	323.5	494.5	4883.0	2.7	5.7	1.1	5.1
Private Sector	481.4	2169.5	22842.8	53529.9	31.9	38.1	51.2	55.8
Securities	206.9	749.9	5349.7	8349.9	13.7	13.2	12.0	8.7
Malaysian Government	116.6	622.5	4647.2	7417.7	7.7	10.9	10.4	7.7
Foreign Government	82.8	2.9	15.0	39.1	5.5	0.1	0.0	0.0
Corporate	7.5	124.5	687.5	893.1	0.5	2.2	1.5	0.9
Gold and Reserves	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Other Assets	149.9	372.3	3030.7	7380.9	9.9	6.5	6.8	7.7
Domestic	139.9	355.0	2982.3	6974.4	9.3	6.2	6.7	7.3
Foreign	10.0	17.3	48.4	406.5	0.7	0.3	0.1	0.4
TOTAL	1509.4	5688.0	44617.1	95931.3	100.0	100.0	100.0	100.0

COMMERCIAL BANKS' OVERDRAFTS AS A PROPORTION OF
TOTAL LOANS

(Million Ringgit)

<u>Year</u>	<u>Overdrafts</u>	<u>Total loans of Commercial banks</u>	<u>Overdraft/ Total loans (%)</u>
1969	1,584.7	1,998.9	79.3
1970	1,917.0	2,359.6	81.2
1971	2,073.7	2,667.2	77.7
1972	2,314.1	3,179.3	72.8
1973	3,539.7	4,867.1	72.7
1974	3,775.1	5,575.6	67.7
1975	4,228.3	6,468.4	65.4
1976	4,835.8	8,061.4	60.0
1977	5,570.5	9,557.8	58.3
1978	7,109.2	12,288.4	57.9
1979	8,438.9	15,384.6	54.9
1980	11,876.6	21,031.1	56.5
1981	13,604.0	25,521.4	53.3
1982	15,382.7	29,665.6	51.9
1983	18,627.9	36,781.8	50.6
1984	22,276.7	43,504.3	51.2

Table 6

DEPOSITS AND LOANS OF COMMERCIAL BANKS
AND FINANCE COMPANIES

	1960	1970	1980	1984	1960	1970	1980	1984
	Outstanding (\$m)				As a proportion of all financial institutions(%)			
Commercial Banks								
Total deposits	947.0	3400.2	24257.4	47506.6	73.2	67.5	61.3	62.2
Total loans to non- fin. pte. sector	470.3	2049.4	20059.0	41252.9	74.9	72.5	70.9	64.9
Finance Companies								
Total deposits	7.7	433.0	4873.7	12616.3	0.6	8.6	12.3	16.5
Total loans to non- fin. pte. sector	5.1	241.1	3632.1	10178.8	0.8	8.5	12.8	16.0
Commercial Banks and Finance Companies								
Total deposits	954.7	3833.2	29131.1	60122.9	73.8	76.1	73.6	78.7
Total loans to non- fin. pte. sector	475.4	2290.5	23691.1	51431.7	75.7	81.1	83.8	80.9
All Financial Institutions								
Total deposits	1293.7	5038.3	39559.1	76429.0				
Total loans to non- fin. pte. sector ^{1/}	628.3	2825.4	28272.4	63536.8				

^{1/} Including commercial bills

Table 7

SOURCES AND USES OF FUNDS OF CONTRACTUAL SAVINGS INSTITUTIONS

	Outstanding (\$m)				% Composition			
	1960	1970	1980	1984	1960	1970	1980	1984
SOURCES								
Capital and Reserves	48.2	162.2	763.0	1023.4	5.8	5.1	5.5	3.6
Currency	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Demand Deposits	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Other Deposits	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Public Sector	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Other Financial Intermediaries	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Private Sector	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Loans	0.0	0.1	0.0	0.0	0.0	0.0	0.0	0.0
Domestic	0.0	0.1	0.0	0.0	0.0	0.0	0.0	0.0
Foreign	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Funds from Other Fin. Inst.	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Domestic	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Foreign	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Life Insurance & Provident Funds	767.9	2882.0	12210.6	25378.3	91.9	91.3	88.2	90.1
Other Liabilities	19.5	112.8	872.7	1770.9	2.3	3.6	6.3	6.3
Domestic	19.5	112.8	872.7	1770.9	2.3	3.6	6.3	6.3
Foreign	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
TOTAL	835.6	3157.1	13846.3	28172.6	100.0	100.0	100.0	100.0
USES								
Currency	0.0	0.0	66.2	86.2	0.0	0.0	0.5	0.3
Deposits with Other Fin. Inst.	30.0	126.9	1152.0	3063.5	3.6	4.0	8.3	10.9
Domestic	23.2	109.8	1152.0	3063.5	2.8	3.5	8.3	10.9
Foreign	6.8	17.1	0.0	0.0	0.8	0.5	0.0	0.0
Bills	0.0	0.2	0.0	0.0	0.0	0.0	0.0	0.0
Treasury	0.0	0.2	0.0	0.0	0.0	0.0	0.0	0.0
Commercial	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Loans	22.8	182.2	999.2	2648.8	2.7	5.8	7.2	9.4
Public Sector	0.0	13.4	0.0	0.0	0.0	0.4	0.0	0.0
Other Financial Intermediaries	10.0	79.8	443.3	919.0	1.2	2.5	3.2	3.3
Private Sector	12.8	89.0	555.9	1729.8	1.5	2.8	4.0	6.1
Securities	750.4	2726.7	10704.6	20533.0	89.8	86.4	77.3	72.9
Malaysian Government	587.5	2345.1	9622.1	18547.1	70.3	74.3	69.5	65.8
Foreign Government	150.6	191.7	16.3	7.5	18.0	6.1	0.1	0.0
Corporate	12.3	189.9	1066.2	1978.4	1.5	6.0	7.7	7.0
Gold and Reserves	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Other Assets	32.4	121.1	924.3	1841.1	3.9	3.8	6.7	6.5
Domestic	14.5	116.6	924.3	1841.1	1.7	3.7	6.7	6.5
Foreign	17.9	4.5	0.0	0.0	2.1	0.1	0.0	0.0
TOTAL	835.6	3157.1	13846.3	28172.6	100.0	100.0	100.0	100.0

Table 8

HOLDINGS OF GOVERNMENT SECURITIES

	1960	1970	1980	1984	1960	1970	1980	1984
	Outstanding (\$m)				As a proportion of all financial institutions(%)			
I Monetary Authorities	8.4	123.8	1680.8	4808.6	1.1	3.4	9.7	14.3
Central Bank	8.4	123.8	1680.8	4808.6	1.1	3.4	9.7	14.3
Currency Board	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
II Deposit-type instn.	157.2	1167.7	6063.6	10186.8	20.9	32.1	34.9	30.4
Commercial banks	91.0	833.0	3648.1	6980.7	12.1	22.9	21.0	20.8
Finance companies	0.1	9.5	215.3	198.3	0.0	0.3	1.2	0.6
Merchant banks	0.0	0.0	161.5	336.2	0.0	0.0	0.9	1.0
Discount houses	0.0	41.5	1090.2	1724.4	0.0	1.1	6.3	5.1
Agricultural Bank	0.0	0.0	20.4	27.7	0.0	0.0	0.1	0.1
National Savings Bank	66.1	283.7	924.3	919.4	8.8	7.8	5.3	2.7
Bank Rakyat	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Urban Credit Co-op.	0.0	0.0	3.3	0.0	0.0	0.0	0.0	0.0
Rural Credit Co-op.	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Cooperative Central Bk.	0.0	0.0	0.5	0.1	0.0	0.0	0.0	0.0
III Contractual Savings Inst.	587.5	2345.3	9622.1	18547.1	78.0	64.5	55.4	55.3
Employees Provident Fund	553.9	2071.9	8581.6	16738.2	73.5	57.0	49.4	49.9
Teachers Provident Fund	0.0	76.2	60.3	53.9	0.0	2.1	0.3	0.2
Other Provident Fund	19.0	130.7	443.2	1067.2	2.5	3.6	2.6	3.2
Life insurance	12.8	48.9	327.5	421.0	1.7	1.3	1.9	1.3
General insurance	1.8	17.6	175.3	232.3	0.2	0.5	1.0	0.7
Armed Forces	0.0	0.0	34.2	34.5	0.0	0.0	0.2	0.1
IV Investment-type Inst.	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Mara Unit Trust	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
National Unit Trust	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
V Others	0.0	0.0	9.4	17.8	0.0	0.0	0.1	0.1
MIDF	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Borneo Devt. Corp.	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Sabah Devt. Bank	0.0	0.0	0.0	8.1	0.0	0.0	0.0	0.0
Sabah Credit Corp.	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Devt. Bank M'sia	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Industrial Devt. Bank	0.0	0.0	9.4	9.7	0.0	0.0	0.1	0.0
BMMF	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
MBSB	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Pilgrim Mgt. Fund Bhd.	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Credit Guarantee Corp.	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Total	753.1	3636.8	17375.9	33560.3	100.0	100.0	100.0	100.0

Table 9

SOURCES AND USES OF FUNDS OF THE MONETARY AUTHORITIES

	Outstanding (\$m)				% Composition			
	1960	1970	1980	1984	1960	1970	1980	1984
SOURCES								
Capital and Reserves	90.3	259.8	797.7	1275.9	8.1	10.7	10.7	8.0
Currency	864.7	1131.7	5104.7	6554.7	77.6	46.7	46.7	41.2
Demand Deposits	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Other Deposits	156.1	825.6	5038.4	5607.5	14.0	34.1	34.1	35.2
Public Sector	103.5	637.2	2425.8	2891.8	9.3	26.3	26.3	18.2
Other Financial Intermediaries	52.6	188.4	1406.0	2556.1	4.7	7.8	7.8	16.1
Private Sector	0.0	0.0	1206.6	159.6	0.0	0.0	0.0	1.0
Loans	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Domestic	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Foreign	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Funds from Other Fin. Inst.	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Domestic	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Foreign	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Life Insurance & Provident Funds	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Other Liabilities	3.2	204.4	2053.4	2482.8	0.3	8.4	8.4	15.6
Domestic	3.2	140.1	1733.1	2456.1	0.3	5.8	5.8	15.4
Foreign	0.0	64.3	320.3	26.7	0.0	2.7	2.7	0.2
TOTAL	1114.3	2421.5	12994.1	15920.9	100.0	100.0	100.0	100.0
USES								
Currency	8.4	0.0	0.0	0.0	0.8	0.0	0.0	0.0
Deposits with Other Fin. Inst.	22.6	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Domestic	22.6	0.0	0.0	0.0	2.0	0.0	0.0	0.0
Foreign	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Bills	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Treasury	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Commercial	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Loans	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Public Sector	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Other Financial Intermediaries	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Private Sector	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Securities	8.4	123.8	1680.8	4808.6	0.8	5.1	5.1	30.2
Malaysian Government	8.4	123.8	1680.8	4808.6	0.8	5.1	5.1	30.2
Foreign Government	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Corporate	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Gold and Reserves	1072.7	2229.1	9708.6	9041.1	96.3	92.1	92.1	56.8
Other Assets	2.2	68.6	1604.7	2071.2	0.2	2.8	2.8	13.0
Domestic	2.2	68.6	998.5	1455.8	0.2	2.8	2.8	9.1
Foreign	0.0	0.0	606.2	615.4	0.0	0.0	0.0	3.9
TOTAL	1114.3	2421.5	12994.1	15920.9	100.0	100.0	100.0	100.0

Table 10
SOURCES AND USES OF FUNDS OF OTHER INSTITUTIONS

	Outstanding (\$m)				% Composition			
	1960	1970	1980	1984	1960	1970	1980	1984
SOURCES								
Capital and Reserves	45.5	135.6	638.1	1342.7	48.7	39.6	24.7	26.7
Currency	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Demand Deposits	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Other Deposits	15.8	20.3	513.7	681.4	16.9	5.9	19.9	13.5
Public Sector	0.0	0.5	273.0	80.1	0.0	0.1	10.6	1.6
Other Financial Intermediaries	0.0	10.5	194.0	37.5	0.0	3.1	7.5	0.7
Private Sector	15.8	9.3	46.7	563.8	16.9	2.7	1.8	11.2
Loans	28.0	169.0	1277.5	2701.5	29.9	49.3	49.4	53.6
Domestic	28.0	149.0	1258.9	2698.5	29.9	43.5	48.7	53.6
Foreign	0.0	20.0	18.6	3.0	0.0	5.8	0.7	0.1
Funds from Other Fin. Inst.	0.0	0.0	14.3	0.0	0.0	0.0	0.6	0.0
Domestic	0.0	0.0	14.3	0.0	0.0	0.0	0.6	0.0
Foreign	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Life Insurance & Provident Funds	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Other Liabilities	4.2	17.9	142.9	312.3	4.5	5.2	5.5	6.2
Domestic	4.2	17.9	142.9	312.3	4.5	5.2	5.5	6.2
Foreign	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
TOTAL	93.5	342.8	2586.5	5037.9	100.0	100.0	100.0	100.0
USES								
Currency	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Deposits with Other Fin. Inst.	3.4	11.2	490.4	363.9	3.6	3.3	19.0	7.2
Domestic	3.4	11.2	490.4	363.9	3.6	3.3	19.0	7.2
Foreign	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Bills	0.0	0.0	20.3	23.0	0.0	0.0	0.8	0.5
Treasury	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Commercial	0.0	0.0	20.3	23.0	0.0	0.0	0.8	0.5
Loans	87.3	282.7	1686.6	3700.0	93.4	82.5	65.2	73.4
Public Sector	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Other Financial Intermediaries	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Private Sector	87.3	282.7	1686.6	3700.0	93.4	82.5	65.2	73.4
Securities	0.3	28.2	207.8	470.4	0.3	8.2	8.0	9.3
Malaysian Government	0.0	0.0	9.4	17.8	0.0	0.0	0.4	0.4
Foreign Government	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Corporate	0.3	28.2	198.4	452.6	0.3	8.2	7.7	9.0
Gold and Reserves	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Other Assets	2.5	20.7	181.4	480.6	2.7	6.0	7.0	9.5
Domestic	2.5	20.7	181.4	480.6	2.7	6.0	7.0	9.5
Foreign	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
TOTAL	93.5	342.8	2586.5	5037.9	100.0	100.0	100.0	100.0

Table 11

SOURCES AND USES OF FUNDS OF INVESTMENT TYPE INSTITUTIONS

	Outstanding (\$m)				% Composition			
	1960	1970	1980	1984	1960	1970	1980	1984
SOURCES								
Capital and Reserves	0.0	4.3	95.9	1890.0	0.0	51.2	88.1	89.0
Currency	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Demand Deposits	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Other Deposits	0.0	0.0	0.3	17.6	0.0	0.0	0.3	0.8
Public Sector	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Other Financial Intermediaries	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Private Sector	0.0	0.0	0.3	17.6	0.0	0.0	0.3	0.8
Loans	0.0	2.3	5.0	0.0	0.0	27.4	4.6	0.0
Domestic	0.0	0.0	5.0	0.0	0.0	27.4	4.6	0.0
Foreign	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Funds from Other Fin. Inst.	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Domestic	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Foreign	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Life Insurance & Provident Funds	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Other Liabilities	0.0	1.8	7.7	215.0	0.0	21.4	7.1	10.1
Domestic	0.0	1.8	7.7	215.0	0.0	21.4	7.1	10.1
Foreign	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
TOTAL	0.0	8.4	108.9	2122.6	0.0	100.0	100.0	100.0
USES								
Currency	0.0	0.0	0.1	2.8	0.0	0.0	0.1	0.1
Deposits with Other Fin. Inst.	0.0	0.1	18.5	87.8	0.0	1.2	17.0	4.1
Domestic	0.0	0.1	18.5	87.8	0.0	1.2	17.0	4.1
Foreign	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Bills	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Treasury	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Commercial	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Loans	0.0	0.1	2.9	0.0	0.0	1.2	2.7	0.0
Public Sector	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Other Financial Intermediaries	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Private Sector	0.0	0.1	2.9	0.0	0.0	1.2	2.7	0.0
Securities	0.0	2.6	49.4	1958.3	0.0	31.0	45.4	92.3
Malaysian Government	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Foreign Government	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Corporate	0.0	2.6	49.4	1958.8	0.0	31.0	45.4	92.3
Gold and Reserves	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Other Assets	0.0	5.6	38.0	73.7	0.0	66.7	34.9	3.5
Domestic	0.0	5.6	38.0	73.6	0.0	66.7	34.9	3.5
Foreign	0.0	0.0	0.0	0.1	0.0	0.0	0.0	0.0
TOTAL	0.0	8.4	108.9	2122.6	0.0	100.0	100.0	100.0

HOLDINGS OF CORPORATE SECURITIES

	Outstanding (\$m)				Proportion Held (%)			
	1969	1970	1980	1984	1969	1970	1980	1984
I) Monetary Authorities	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Central Bank	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Currency Board	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
II) Deposit-type inst.	7.5	124.5	687.5	886.2	37.3	36.1	34.3	16.8
Commercial Banks	7.0	51.6	281.3	405.3	34.8	14.9	14.1	7.7
Finance Companies	0.5	16.9	10.7	10.3	2.5	4.9	0.5	0.2
Merchant Banks	0.0	0.0	23.8	90.6	0.0	0.0	1.2	1.7
Discount Houses	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Agricultural Bank	0.0	0.0	13.9	10.1	0.0	0.0	0.7	0.2
National Savings Bank	0.0	0.0	190.3	206.8	0.0	0.0	9.5	3.9
Bank Rakyat	0.0	2.7	76.9	64.5	0.0	0.8	3.8	1.2
Urban Credit Co-op	0.0	52.5	81.8	60.2	0.0	15.2	4.1	1.1
Rural Credit Co-op	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Cooperative Central Bank	0.0	0.8	8.8	38.4	0.0	0.2	0.4	0.7
III) Contractual Savings Inst.	12.3	193.6	1066.2	1990.3	61.2	56.1	53.3	37.7
Employees Provident Fund	0.0	0.0	29.5	494.4	0.0	0.0	1.5	9.4
Teachers Provident Fund	0.0	0.0	38.0	0.0	0.0	0.0	1.9	0.0
Other Provident Fund	1.0	90.4	211.0	384.4	5.0	26.2	10.5	7.3
Life Insurance	9.2	83.1	364.1	419.7	45.8	24.1	18.2	7.9
General insurance	2.1	20.1	98.0	152.2	10.4	5.8	4.9	2.9
Armed Forces	0.0	0.0	325.6	539.6	0.0	0.0	16.3	10.2
IV) Investment-type Inst.	0.0	4.0	49.4	1958.3	0.0	1.2	2.5	37.1
Mara Unit Trust	0.0	4.0	36.3	138.5	0.0	1.2	1.8	2.6
National Unit Trust	0.0	0.0	13.1	1819.8	0.0	0.0	0.7	34.5
V) Others	0.3	23.1	198.4	447.6	1.5	6.7	9.9	8.5
MIDF	0.0	9.0	37.9	19.7	0.0	2.6	1.9	0.4
Borneo Devt. Corp.	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Sabah Devt. Bank	0.0	0.0	12.2	109.8	0.0	0.0	0.6	2.1
Sabah Credit Corp.	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Devt. Bank M'sia	0.0	0.0	24.2	44.6	0.0	0.0	1.2	0.8
Industrial Devt. Bank	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
BMMF	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
MBSB	0.3	0.0	0.0	0.0	1.5	0.0	0.0	0.0
Pilgrim Mgt. Fund Bhd.	0.0	14.1	124.1	273.5	0.0	4.1	6.2	5.2
Credit Guarantee Corp.	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Total	20.1	345.2	2001.5	5282.4	100.0	100.0	100.0	100.0

Table 13

FINANCIAL INSTRUMENTS IN MALAYSIA

	Outstanding (\$m)				% Composition			
	1960	1973	1980	1984	1960	1973	1980	1984
I) CLAIMS AGAINST FIN. INSTRS.								
A) Marketable Instruments								
Currency Issued	2872.9	14468.3	51041.9	95502.9	67.5	37.5	40.8	36.3
	864.7	1870.2	5104.6	6554.7	20.3	4.9	4.1	2.5
B) Non-Marketable Instruments								
Demand Deposits	2008.2	12598.1	45937.3	88948.2	47.2	32.7	36.7	33.8
Deposits From Public Sector	477.0	2030.3	5326.2	8088.3	11.2	5.3	4.3	3.1
Deposits From Private Sector	217.7	1685.2	6777.4	10791.6	5.1	4.4	5.4	4.1
Life Insurance & Provident Funds	545.6	4624.7	21623.1	44690.0	12.8	12.0	17.3	17.0
	767.9	4257.9	12210.6	25378.3	18.0	11.0	9.8	9.6
II) CLAIMS AGAINST NON-FIN. INSTRS.								
A) Marketable Instruments								
Treasury Bills	1381.5	11529.6	46443.8	99054.5	32.5	29.9	37.1	37.6
Government Securities	753.1	5793.0	17375.9	33560.3	17.7	15.0	13.9	12.7
	40.6	625.4	1416.4	2769.1	1.0	1.6	1.1	1.1
	712.5	5167.6	15959.5	30791.2	16.7	13.4	12.7	11.7
B) Non-Marketable Instruments								
Loans to Public Sector	628.4	5736.6	29067.9	65494.2	14.8	14.9	23.2	24.9
Loans to Private Sector	0.1	193.6	795.5	1957.4	0.0	0.5	0.6	0.7
Commercial Bills	581.5	5002.6	25088.2	58959.7	13.7	13.0	20.0	22.4
	46.8	540.4	3184.2	4577.1	0.0	0.5	0.6	0.7
TOTAL CLAIMS	4254.4	25997.9	97485.7	194557.4	100.0	67.4	77.9	73.9
III) EQUITY SECURITIES								
A) Marketable Issues								
Corporate Issues	0.0	12555.4	27709.9	68882.1	0.0	32.6	22.1	26.1
B) Non-Marketable Issues								
Preferred Issues	0.0	25.3	9.9	9.8	0.0	0.1	0.0	0.0
IV) TOTAL FINANCIAL INSTRUMENTS	4254.4	38553.3	125195.6	263439.5	100.0	100.0	100.0	100.0
GMP	3096.0	18723.0	51838.0	66389.0	143.3	46.9	40.0	27.2
CORPORATE SECURITIES	69.8	205.9	241.5	396.8	0.5	1.7	1.6	2.0

Table 14

FINANCIAL INTERRELATIONS RATIO (FIR)

	<u>Total Financial Instruments</u> <u>(Million Ringgit)</u>	<u>GDP</u> <u>(Million Ringgit)</u>	<u>FIR:1/2</u>
	(1)	(2)	
1960	4254.4	6837	0.62
1973	38553.3	18723	2.06
1980	125195.6	51838	2.42
1984	263439.5	66389	3.98

Table 15
SELECTED ECONOMIC AND MONETARY INDICATORS

	CPI	Nominal	Nominal	Real	Real	M1	M2	M3	Minimum statutory reserve require- ment	Commercial Banks Liquidity ratio		
		GDP	GNP	GDP	GNP					Minimum require- ment	Actual	Excess liquidity ratio
		(current prices)								% growth		
1959									4.0	20.0		
1960						5.4	11.6					
1961	-0.2	0.0	7.0			2.3	6.7					
1962	0.1	-9.8	6.0			4.7	5.9			25.0		
1963	3.1	23.9	6.3			7.0	9.7					
1964	2.7	6.7	6.4			5.6	8.2					
1965	-	9.9	9.9			6.8	10.6		3.5	20.0	23.0	3.0
1966	1.4	6.7	6.8			9.1	11.7				28.3	8.3
1967	4.1	3.7	5.2			-7.7	3.2				38.3	18.3
1968	-0.2	4.4	4.3			11.3	15.6				41.7	21.7
1969	-0.4	10.6	9.0			10.9	14.1		5		35.2	15.2
1970	1.9	5.9	5.9			8.0	10.9				30.1	10.1
1971	1.6	8.2	8.4			4.3	13.2				33.5	13.5
1972	3.2	9.8	9.9	9.4	9.8	28.1	23.4		8.5		33.3	13.3
1973	10.5	31.7	30.5	11.7	10.5	37.6	31.1			25.0	31.6	6.6
1974	17.4	22.1	21.0	8.3	7.7	8.6	15.4	16.8	10.0		34.9	9.9
1975	4.5	- 2.3	-1.2	0.8	2.2	7.2	14.5	16.0	7.0		36.2	11.2
1976	2.6	25.8	24.9	11.6	10.7	20.9	27.7	28.1	6.0		39.6	14.6
1977	4.7	15.2	15.1	7.8	7.6	16.6	16.2	17.0			41.8	16.8
1978	5.0	17.1	16.4	6.7	5.9	18.2	17.9	19.9	5.0		36.0	11.0
1979	3.6	19.0	19.1	9.3	9.3	17.2	23.8	31.8		20.0	25.8	5.8
1980	6.7	15.0	16.1	7.8	8.6	15.0	27.9	20.8			23.4	3.4
1981	9.7	8.2	8.6	7.1	7.5	12.8	17.1	13.6			27.0	7.0
1982	5.8	9.2	7.7	5.6	4.7	13.3	16.3	16.8			26.4	6.4
1983	3.7	11.1	9.0	5.9	3.5	7.7	9.4	14.5			23.2	3.2
1984	3.9	12.5	11.8	7.3	6.2	-0.6	11.4	15.1			23.3	3.3
1985												
Average												
1971-75						17.2	19.5					
76-80		18.4	18.3	9.8	8.4	21.2	22.7	23.5				
81-84		10.3	9.3	6.5	5.5	8.3	13.6	15.0				
79-84				7.2	6.6	10.9	17.7	18.8				

THE FINANCIAL STRUCTURE AND ITS IMPLICATIONS FOR MONETARY POLICY IN NEPAL

by

Mukti Prasad Upadhyay

I. INTRODUCTION

The evolution of the ~~organised~~ financial system in Nepal has a more recent history than in other countries of the SEACEN region. The financial structure of a country reflects the relative position of the financial system vis-a-vis the non-financial sector of the economy. It also has a bearing on the propensity to save, the inducement to invest, on the structure of production and other important economic factors. A general view of these factors may be obtained with reference to the degree to which the process of financial intermediation has been stretched and through a ramification of the process. In a developed country, the financial system is fully integrated so that the rates of return on alternative financial assets tend toward equality except in so far as they differ with respect to maturity and liquidity and to the people's perception of their riskiness. The benefits of intermediation like increase in liquidity, reduction in risk and resource flow into high-yielding investments

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follow naturally in the development process even as the financial system merely responds to development impulses originating elsewhere.

These are not, however, the natural consequences of the development process a country like Nepal. The financial system in such a country is fragmented into an organised part and a much larger unorganised one. The latter may be further divided into small but numerous financial markets. The whole structure is characterised by apparently limited intercourse between its constituent parts. This hinders the responsiveness of the financial structure to the financial demands of real infrastructure. But the problem only begins there. Nepal faces a more crucial task of releasing growth impulses through the financial sector. Some idea on how the task can be accomplished can be obtained by studying the different aspects of the financial structure. Important aspects of such a study would include (1) how the structure has evolved in the past, (2) what stage is the present structure in and what are the ramifications of this structure in terms of the importance of various institutions and instruments, and (3) what direction is the structure moving in.

Objectives of the Study

The objectives of the study are:

1. to have an in-depth knowledge of the growth pattern of financial institutions and financial instruments;
2. to get insights on how financial development has fared vis-a-vis, and interacted with, the growth of the economy;
3. to evaluate how the development of the financial structure has facilitated the effectiveness of monetary policy; and

4. to derive some policy implications for enhancing the effectiveness of monetary policy.

Period Covered, Methodology and Scope of the Study

The study encompasses a nineteen-year period from 1964/1965 to 1983/1984. The selection of the starting point is prompted mainly by data availability. Another consideration is that 1965 could serve as the base or reference points from which successive development of the financial system could be properly evaluated. This was the year when the main existing institutions were well-established and a few others were in the process of inception. The methodology followed in this study was supplied by the SEACEN Research and Training Centre. It is non-quantitative in nature but it incorporates the extensive use of ratios, percentages, growth rates, etc.

This paper is organised along the following lines: Section I is the introductory part and includes a brief background on the Nepalese economy and an overview of the financial system. An account of the development of the financial structure in terms of institutional diversification and an assesment of the relative position of institutions is presented in Section II. This section also presents some indicators of the size of the financial system vis-a-vis the rest of the economy. The development and diversification of financial instruments in the economy are analysed in Section III. Section IV explains the major concerns of the policies on financial structure. The policy tools used by authorities to influence relevant targets are also described therein. This section then attempts to evaluate in non-quantitative terms the implications for monetary policy of the growth and direction of the financial structure; and analyses the constraints imposed by various factors on its development. Finally, Section V summarizes the main findings of the study and concludes with a few policy recommendations.

Economic Background of Nepal

Nepal's economy is a slow-growth economy. Real GDP increased at the rate of 2.7 per cent per annum over the past two decades. Most of this growth was, however, absorbed by a 2.5 per cent annual increase in population (see Table 1). Agriculture remains the mainstay of the economy, although its contribution to GDP has been slightly receding over time - from 67.6 per cent in 1964/65 to 53.7 per cent in 1983/84. Some diversification of the economic structure is noticeable in terms of the growth of construction and services, while industrial development has lagged far behind. Domestic saving has fluctuated around 10 per cent of GDP over the past decade. Investment as a percentage of GDP has been on the rise and has remained well above the savings ratio. The discrepancy is met by foreign aid, whose contribution to the growth of GDP is apparently very limited.

Nepal is an open economy because of an 800-mile long free open border with India. This is not fully reflected in the total foreign trade which is only around 20 per cent of GDP. The unrestricted movement across the border with India and unlimited convertibility of Nepali rupees with Indian rupees renders most of domestic goods and even services as tradeable. This dichotomy between actually traded and tradeable goods is of paramount importance for Nepal as it considerably weakens the influence of exchange rates and other macro policies on relative prices of tradables and nontradables. Sectorally-oriented policies to expand the export sector have met with repeated failure in the absence of a coherent strategy to influence relative rates of return on alternative investments. The external sector is thus characterised by high growth of imports and stagnating exports. Garments and woollen carpets have emerged as significant earners of export revenue but in the mean time, traditional export items like rice and jute have deteriorated as a result of productivity losses and of competition from synthetic fibers, respectively. The trade deficit is partly covered with surpluses on the services and

transfers accounts of which foreign grants occupy a significant share. The adverse balance of payments has reduced external reserve to the equivalent of less than three months imports. Government expenditure has been increasing rapidly without a corresponding growth of public revenue. The deficit is traditionally met by soft loans from multilateral financing agencies. Of late the banking system, and the Nepal Rastra Bank in particular, have been financing an increasing proportion of the fiscal deficit. Six development plans have been executed in the past and a Seventh Plan has now begun. Significant achievements have been made in building infrastructure, but the country is yet to find a respectable long term growth path.

AN OVERVIEW OF THE FINANCIAL SYSTEM OF NEPAL

The Organised Sector

The monetary system. The year 1937 stands out as a most remarkable year in the history of the Nepalese financial system. The first formal financial institution, namely, Nepal Bank Ltd. (NBL), was established in that year. With it began the business of modern banking in Nepal. NBL was set up under a special act as a commercial bank but it went on to perform some of the functions of a central bank as well. In those days in Nepal the only important source of livelihood, except for a few traders and for a handful of autocratic ruling elite, was agriculture (farming and animal husbandry). Retail trade was concentrated in a few towns. The external trade of the country was confined with India and, to a very small extent, with Tibet. The principal export items were rice (even paddy), ghee (clarified butter) and animal skin. The industrial and service sectors had marginal contributions to national income and employment. Naturally, therefore, foreign trade was the principal area of business for the first bank of Nepal. NBL gradually opened branches at the towns which had developed near the Indian rail-heads across the border. By the time the Nepal Rastra Bank, the central bank of the

country, was established in 1956, NBL had a network of 13 branches. It operated in those places as the banker of the government, taking over from Mal Addas (government revenue offices) the function of keeping the 'books' as well as the revenue.

Before the Rastra Bank came into existence, the note issuing function was performed directly by His Majesty's Government of Nepal. Nepalese currency was, however, in limited demand as it circulated mainly in the Kathmandu valley and a few adjoining hilly districts. The principal medium of exchange as well as the unit of account in other places was the Indian rupee (IRe). The modicum that Nepal earned in foreign exchange (other than international reserves IRs) was also kept in Indian banks. There was no official mechanism to stabilise the value of Nepalese rupee vis-a-vis Indian rupee. The market exchange rate, therefore, fluctuated widely which hindered the use of Nepalese rupee (NRe) as the sole legal tender. As of mid-July 1957 the Nepalese currency in circulation outside the Rastra Bank amounted to Rs 84 million. 1/

Judging from this background the establishment of Nepal Rastra Bank (NRB) in 1956 may be considered as a watershed in the evolution of the organised financial system in Nepal. NRB was entrusted by the Nepal Rastra Bank Act promulgated in 1955, with the main task of bringing about order in the monetary system of the country and in the exchange rate of the rupee. Specifically, the functions of NRB were stated as "to manage the issuance of Nepali notes, to endeavour to bring Nepali currency into circulation throughout the Kingdom, to stabilise the exchange rate of Nepali rupee, to induce capital mobility so as to encourage enterprise, and

1/ The first notes issued by Nepal Rastra Bank came out in February 1960.

to develop the banking system in the country." ^{2/} The development of money and capital markets was thus made one of the responsibilities of NRB.

During its initial years of operation, NRB, however, remained preoccupied with the twin objectives of providing the Nepalese rupee universal acceptability and ensuring exchange rate stability. NRB was mostly successful in bringing a measure of stability in the exchange rate following the enforcement of the Foreign Exchange Control Act 1960 and the Foreign Exchange Regulation Act 1962. Private money-changers could no longer operate currency exchange business without obtaining a license from NRB. The NRB opened its own branches in various parts of the country and guaranteed unlimited convertibility between IRe and NRe at a fixed rate at its offices, at the branches of NBL, at a few Mal Addas and through licensed moneychangers. Branch expansion was pursued concomitantly to increase the circulation of NRe.

The dual currency system could not, however, be abolished until as late as 1966. This was the year when IRe was devalued by 36.5 per cent. Nepal's official holdings of international reserves (IRs) had grown to a relatively respectable level of NRs 238 million as of mid-May 1966 from an abysmally low level of NRs 56.6 million at mid-July 1959. Buoyed by this remarkable growth, the authorities decided not to devalue NRe. They allowed the rupee to be overvalued by 57.5 per cent vis-a-vis IRe following the devaluation of the latter. The new exchange rate came to be set at NRs 1.0125 as against the previous rate of NRs 1.60 per IRe. The authorities' perception that NRe had attained a higher degree of independence from IRe was, however, shortlived. The official exchange rate was clearly out of line with the effective exchange rate as evidenced by a

^{2/} Nepal Rastra Bank Act, 1955, in Collection of Nepali Acts, Part 4(b) (in Nepali) 1984, p. 89.

considerable drop in IRe reserve in the two-month period ending mid-July 1966. From NRs 238 million, the NRB holding of IRe decreased to NRs 100.1 million (a one-third drop in terms of IRs), which further dwindled to Rs 63 million over the following fiscal year. Only when the pound sterling was devalued in November 1967 did the overdue devaluation of NRe materialise. There have been occasional swings (sometimes large) in the movement of IRe reserve since then but only two minor adjustments have been made in the exchange rate against IRe.

By mid-Sixties NRe had attained wide acceptance as a medium of exchange. It was now possible to effectively enforce the law making transactions in IRe illegal. In the year 1966, it was officially stated that IRe was successfully driven out of circulation. A major shift was noticeable in the central banking policy since the mid-Sixties. The shift was in terms of institution-building and a progressively greater monetisation of barter transactions so as to create a congenial atmosphere for the operation of monetary policy. Before the establishment of Rastriya Banijya (National Commercial) Bank in January 1966, Nepal Bank Ltd. was the lone commercial bank in the country. NBL had its branches operating at 32 places ^{3/} of which 26 branches were either in the plain Terai or in Kathmandu Valley. As the profit incentive was little, NBL was reluctant to set up its office in the hilly districts and also in some relatively prosperous places elsewhere. NRB had not enforced any regulation on the interest rate or NBL's other terms of contract with the general public. NBL was controlled by the government as the latter owned 51 per cent of its share capital. Interest rates were kept low. Consistent with the prevailing line of economic thinking, it was felt that low interest rate would help promote banking habit and increase the investment rate in the economy. To supplement the intermediation services of NBL and also to introduce an element of competition in the banking industry, another bank, Rastriya Banijya Bank (RBB) was established in 1966.

^{3/} As of mid-July 1965.

RBB was owned fully by the government. It was entrusted the responsibility of opening new branches in the remote and the seemingly unprofitable areas. The branches of NRB set up mainly for extending the circulation of the rupee were also to be handed over to RBB. So far (by early 1984) Nepal's banking system has only comprised these two banks besides the Rastra Bank.

Development banks. Development of the commercial banking structure in Nepal was important for various reasons. However, the scope for generalised banking had its own limitations. Deposit growth was lagging far behind the demand for bank credit until as late as the middle of the Seventies. The banks had a natural bias toward the financing of trade and other activities in the urban areas. Commercial bills provided the only attractive source of the bank funds. In the evolutionary phase, innovations like term lending were not considered fit to be a part of the banking business. In order to facilitate an economic transformation, it was necessary to make capital, among others, available to modern sectors of the economy. Capital for private sector industry was, therefore, considered as the rationale behind the establishment of Nepal Industrial Development Corporation (NIDC) in 1959. Even now NIDC remains the only public sector (or any for that matter) institution serving as an industrial development bank.

For the provision of credit to agriculture, a cooperative bank was set up in 1964. The bank, however, dealt only with cooperatives which relent the amount (mainly in kind) to the farmers. The cooperatives were formed out of inducement by the government, not out of overly felt need by the farmers. They were misplanned, hence mismanaged. The support services in terms of input supplies and marketing were conspicuously lacking. A comprehensive organisation was, therefore, needed to supply credit to cooperatives and also directly to individual agriculturists. The answer was the Agricultural Development Bank (ADB/N) which was established in 1968. The Cooperative Bank was merged with this bank. Agricultural credit

requirements were, and still are, immense in the country. An agricultural credit survey conducted by NRB for the first time in Nepal in 1970-71 showed that the financing of agricultural operations at the prevailing technology required a sum of Rs 80.5 million per annum. The introduction of modern technology would raise the figure up to Rs 1 billion. ADB/N is owned by the government (which holds a major part), by NRB and by the borrowers from ADB/N. In the course of time, this institution has evolved as the single most important organisation influencing agricultural life in Nepal.

ADB/N and NIDC comprise the development banking segment of the organised financial structure in Nepal. They differ from commercial banks not only in terms of specific purposes (areas) of their lending but also due to the fact that deposits from the public are not an important source of their funds.^{4/} In recent years, particularly since 1974 when commercial banks were asked to step into the business of "priority sector financing", the distinction between commercial banks and development banks (especially ADB/N) has become less sharp. Beginning in 1984, ADB/N has also been allowed to directly enter the general banking business (with certain restrictions), plagued as it was from the ever acute shortage of funds.

Contractual savings institutions. The rest of the organised financial system includes two institutions of the contractual savings type, and two other smaller organisations. Those dealing in the contractual savings are the Employees' Provident Fund (EPF) and the National Insurance Corporation (NIC). The EPF was established in 1962 under the Employees' Provident Fund Act of 1962. Previously, provident funds were directly run by the government for its employees.

^{4/} NIDC does not accept deposits and ADB/N accepts them (as of early 1984) only at places where commercial banks do not have an office.

The assets and liabilities of these funds were now transferred to the EPF. The resources of the EPF comprise (1) a 10 per cent monthly deduction from the salary of the employees of government and corporate institutions having an agreement with it, (2) an equivalent amount deposited by the employers, and (3) the interest earned on loans and investments. The EPF works as the trustee of employees' provident fund, manages it, extends loans to the contributing employees for various purposes and refunds the contribution and the interest to them upon termination of their service for any reason whatsoever. The assets of EPF have crossed a billion rupees mark by 1982, increasing enormously in recent years by a compound annual rate of about 25 per cent over the five years ending mid-September 1982. The EPF has grown into one of the major institutions for savings mobilisation in the country, although of late the structure of its asset portfolio has tended to have some adverse implications for the banking industry.

The other institution, viz., National Insurance Corporation (NIC), was set up in December 1967 as a private limited company under the Company Act, 1964. Its main objectives were stated as resource mobilisation for economic development and preventing the outflow of the country's foreign exchange. The history of indigenous insurance institutions dates back to 1946 when the Nepal Insurance and Transport Company Ltd. was established under the ownership of Nepal Bank Ltd. However, the insurance business was concentrated in the hands of a few Indian companies. The National Insurance Corporation Act was promulgated in 1968 which then came to govern the business of NIC. The NIC is also a public sector undertaking, shared by the government, the NRB and the NBL. The NIC's activities were originally limited to non-life insurance. In February 1973, it entered the life insurance business, previously the exclusive field of the Life Insurance Corporation (LIC) of India. Effective mid-July 1977, following an agreement between the NIC and the LIC of India, the LIC-held life policies of Nepali citizens have been transferred to the NIC, subject to the agreement of the policy holder.

Other institutions. By 1974, the NRB's efforts in evolving and strengthening the financial institutions in Nepal had succeeded in making available a wider array of financial services in the country. In that year, a priority sector lending programme was launched for commercial banks. The banks were urged to advance loans at lower rates of interest to small scale agricultural, industrial and service sectors. According to the directive, the total of such lending should amount to not less than 5 per cent (increased to 7 per cent since 1976/77 of their deposit liabilities). The banks were, however, experiencing an increasingly tighter liquidity situation for years by then. 5/ They had to depend on NRB funds for a significant portion of their trade credit. 6/ Added to this was a total lack of experience in non-traditional banking. In these circumstances, the priority credit programme had little prospect for success.

To persuade the banks to increase their lending, it was considered essential to provide for reduction in risks associated with rural lending. The Credit Guarantee Corporation (CGC) was thus established in September 1974. The banks were guaranteed compensation (up to 80 per cent of unrecovered amount) against default. The CGC had an initial paid-up capital of Rs 3 million of which two-thirds were subscribed by NRB and one-third was shared equally by NBL and RBB. In the year 1981/82, its paid-up capital was raised to Rs 7.5 million to accomodate greater bank lending to priority sectors. Incorporated under the Company Act 1964, it is in fact a subsidiary company of NRB. The latter holds 73 per cent of its shares and has

5/ The liquidity ratio as of mid-July 1974 had been squeezed to 31 per cent. For the first time in the preceding six years the ratio had come down from 45 per cent.

6/ The ratio of borrowing from NRB to total deposits had shot up to 32.4 per cent as of mid-July 1974 as compared to insignificant figures in earlier years.

three members in its board of directors. Initially, CGC guaranteed the disbursed amount on which it charged a guarantee fee of 0.25 per cent once for all. The guarantee was applicable until the loan was recovered by the bank or the documents placed before CGC for compensation. Beginning 1980/81, the CGC started guaranteeing, for a period of three months, the outstanding amounts. The guarantee fee was revised at 0.36 per cent of the loan outstanding. The new provision requires renewing the guarantee every three months.

The Corporation has recently completed a decade of its operations. Its activities are, however, dependent on those of commercial banks. A number of factors have led the banks to go slow on the priority sectors lending programme. The provision of rural credit is itself an apparently risky venture for the banks. The disposal of collateral in the event of default is a difficult proposition to begin with. The interest rate that could compensate for the risk involved is set at a low level. Then there is the cost of supervision that is incurred to prevent or reduce the potential misuse of loans. No doubt the NRB assures refinance at concessional rates. It also plays the dominant part (in terms of capital subscription) in compensating for the bad debts through CGC. The incentives on these accounts are, however, too little against expected losses by banks in the priority business. Cheaper availability of refinance hardly provides an inducement when the banks are flush with their internal funds, a usual banking scenario after 1975. ^{7/} As for CGC, the compensation fund it has created stands too low to provide adequate guarantee cover. The fund comprises an amount which has been typically around two per cent of outstanding credit of banks guaranteed with the CGC. Clearly, CGC has been unable to ensure compensation for expected losses by banks. It has been reported by

^{7/} For a brief review of the priority credit programme, see also Study on Rural Savings Mobilisation in Nepal, APROSC, Kathmandu, October 1984.

CGC officials that the banks have tended to show apathy toward the entire guarantee scheme. Many cases have been recorded where the banks have refrained from demanding compensation despite clear evidences of loans having gone bad. Indeed, CGC has itself played a part in the inching forward of priority credit programme. But the role of other factors independent of CGC has been adequate enough to keep CGC's operations at a low level. The assets of CGC as of mid-July 1983 stood at Rs. 14.7 million which accounted for less than one-tenth of one per cent of total assets of all financial institutions in the organised sector. The percentage share has not shown any growth during the nine years of its existence (1974-83). The CGC's scope of guarantee has remained confined to the priority credit of commercial banks. At present, however, the NRB is contemplating a widening of the guarantee coverage to pre-export credit.

Finally, the Securities Exchange Centre (SEC) was set up in 1977. Opened under the initiative of NRB and owned jointly by NRB and NIDC, its main objective is to develop a stock exchange in the country. In the beginning, it dealt exclusively in government securities. But after a few years it started to sell shares and debentures of public limited companies as well. Recently, it has completed the indexing of shares of a few organisations and beginning 1984, it has assumed the role of a recognised stock exchange in the country.

Unorganised Financial Sector

Information on the unorganised financial sector is both scanty and imprecise. An important source of information is the Agricultural Credit Review Survey which was conducted by the Nepal Rastra Bank in 1977/78. This report also contains the figures for 1969/70 when the first survey was carried out. Table 2 shows that in the span of seven years between the two surveys, institutional sources of agricultural credit gained considerable importance and private sources registered corresponding decline. Of the total of 41 per cent

share of institutional credit in 1976/77, ADB/N alone contributed 28 per cent. The share of commercial banks was low at 6 per cent. Among private sources of farm credit, village moneylenders and friends and relatives supplied the bulk (46 per cent of total from all sources).

While the formal financial institutions seem to be financing an increasing proportion of agricultural debt in Nepal, there is no indication of how fast their importance has grown within the overall financial system of the country. An estimate of agricultural credit from non-formal credit agencies is presented in Appendix Table 2.1 to give an indication of the relative magnitude of these sources vis-a-vis the formal institutions.

II. INSTITUTIONS IN THE FINANCIAL STRUCTURE

The institutions comprising the financial structure of Nepal may be classified (as indicated in the preceding section) for the purpose of analysing the growth of individual institutions vis-a-vis the overall structure. The classification followed in the present study (and which may be seen from Chart 1) is as follows:

1. Central bank or monetary authorities, viz., Nepal Rastra Bank;
2. Commercial banks, which conduct the general banking business;
3. Development banks, which are the specialised term lending institutions;
4. Contractual savings institutions, which deal in savings that mature upon fulfilment of certain contracts; and

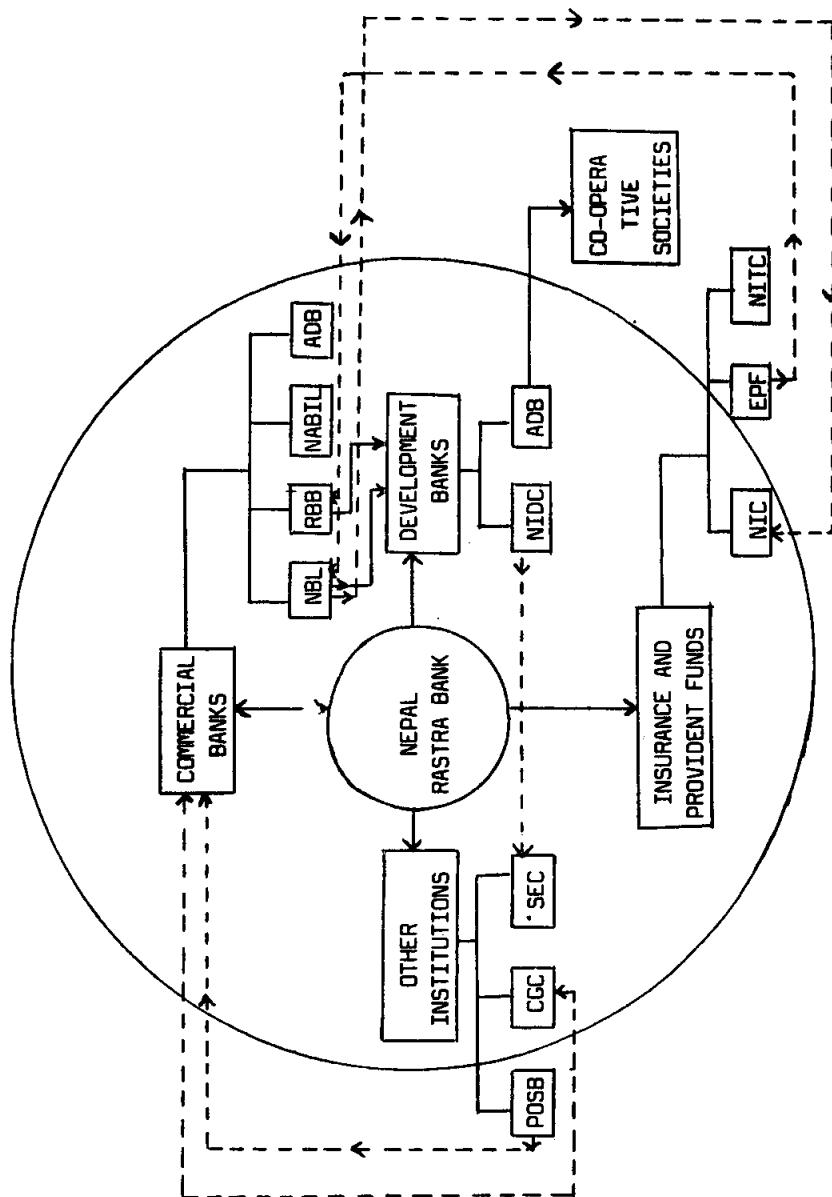
Chart 1

THE FINANCIAL SYSTEM OF NEPAL
(Mid-July 1984)

- NBL : Nepal Bank Limited
- RBB : Rastriya Banijya Bank
(National Commercial Bank)
- NABIL: Nepal Arab Bank Limited
- ADB : Agricultural Development Bank
- NIC : National Insurance Corporation
- EPF : Employees' Provident Fund
- NITC : Nepal Insurance and Transport
Company
- * : a subsidiary company of NBL
- CGC : Credit Guarantee Corporation
- SEC : Securities Exchange Centre
- POSB : Post Office Savings Bank

Note: 1. Institutions outside the circle are not under direct supervision of NRB.

2. The arrows show the direction of flow of funds.



5. Others, which guarantee (repayments of) bank credit to certain priority areas and which aim at serving both the primary and the secondary markets for securities. There are about 700 small cooperative credit societies dispersed throughout the country. The Post Office Savings Bank is also functioning through its 75 branches, one in each district of the country.

There is a large informal money market that includes, among others, village money-lenders and agricultural traders. The present study limits itself to the study of formal financial institutions. Even amongst the latter, three insurance companies which are in the private sector, and the cooperative societies are left out because of data constraints.

Nepal Rastra Bank

Nepal Rastra Bank (NRB) is the central bank of the country. It was established under the Nepal Rastra Bank Act 1955. NRB commenced operation on April 27, 1956. Its responsibilities were immense then. It had to widen the circulation of Nepal Rupee throughout the Kingdom to make it the principal and eventually the sole medium of exchange. It had to stabilise the exchange rate vis-à-vis Indian rupee. It had become necessary to avoid sharp and irregular fluctuations in the exchange rate arising from heavy speculation. The speculation was destabilising because the exchange market was characterised by uncertainty and high information cost. Other stabilisation objectives of NRB as outlined in the Preamble of its Act are to induce mobility of capital to encourage enterprises in the country; and to initiate the development of the banking and financial system. The authorised capital of the Bank is Rs 10 million which is all subscribed and paid up by the government.

Beginning 1962, Nepal had practised a system of multiple exchange rates. The system owed itself to a scheme called the

Exporters Exchange Entitlement Scheme which was introduced with a view to secure geographic diversification for Nepal's foreign trade. ^{8/} In March 1978, when the multiple exchange system was replaced by a dual exchange system, Nepal ushered in a process of gradual elimination of distortion created by unrealistic exchange practices. The exchange rates were unified in October 1981 and in June 1983, the system moved from a single currency peg to a basket peg. ^{9/} At the end of FY 1983/84 the gross foreign exchange reserve of Nepal stood at Rs. 2,349.7 million which was hardly enough to pay for 4.3 months' imports. The rupee has depreciated, vis-a-vis the US dollar, the intervention currency, by about 30 per cent over the last 20 months (June 1983-January 1985). As the exchange rate has largely depended on the value of the dollar in the international exchange market, the recent surge in dollar appreciation has showed itself up in the rupee-dollar rate.

This dependence on US dollar has been possible because the rupee is also simultaneously pegged to Indian rupee. The exchange rate vis-a-vis IRe has remained stable (at NRs. 1.45 per IRe) since March 1978 (see also Section IV). The NRB guarantees free and unlimited convertibility between the two currencies.

^{8/} For the ramification of this scheme in some detail and for some of its consequences on the Nepali economy, see P.K. Kafle "Foreign Trade and Regional Co-operation" in Nepal's Economy: an Overview, edited by Mahesh Banskota and Nirmal Bista, Kathmandu, CEDA, 1980.

^{9/} The rupee was pegged to the US dollar in respect of transactions in convertible currencies. It was also pegged simultaneously to IRe which made it imperative for NRB to have caution in setting exchange rates so as to avoid broken cross rates between US dollar-NRe-IRe and the consequent instability in foreign reserve movements.

The relationship of NRB with commercial banks and non-bank financial intermediaries is governed mainly by the Nepal Rastra Bank Act 1955, the Commercial Bank Act 1974, and separate Acts under which specialised financial institutions (FIs) have been created. The Nepal Rastra Bank monitors and supervises the operations of FIs in general and commercial banks in particular, thereby enhancing its regulatory power over the banks. It is empowered to fix the interest rates on the deposits the FIs accept and loans they advance. Since 1971, NRB has been actively regulating the interest rate structure of FIs. NRB has created development funds to provide refinance for the purpose of lending to priority sectors. Interest rate on refinance is generally lower by 4 percentage points than the corresponding loan rates of the banks. The lower rate is necessary for the operation of selective credit policy especially when the banks are urged to enhance the flow of lending in risky rural projects. The banks may also borrow by pledging government bonds at NRB, or they may readily sell out the Treasury bills, traditionally to the bank but now to its agent, namely, the Securities Exchange Centre.

The total assets/liabilities of the monetary authorities are shown in Table 3. The total resources increased at an annual rate of over 17 per cent in the 1960s and by 14 per cent in the 1970s. In the respective periods, the external assets of the NRB increased by 21 per cent and 9 per cent. In sharp contrast, the growth in internal assets accelerated from 9 per cent in the 1960s to 25 per cent in the 1970s. The scenario in the 1980s has reinforced this trend. This sharp turnaround in the NRB's asset structure has left the external reserve at a small 29 per cent share in the total assets of the Bank at the end of 1983/84 against 68 per cent a decade ago. It has also resulted in a severe decline in the relative share of NRB in aggregate assets of financial system. From 53 per cent at mid-July 1974, this share has gone down to 34 per cent at mid-July 1984.

On the liabilities side, growth of monetary base closely followed the rate of growth of total liabilities in the 1960s, but

has outpaced the latter in the 1980s. The expansion of base money in the Eighties has come about despite an absolute decline in the external assets in terms of rupees (whose value has fallen by 37 per cent). The expansion owed itself mainly to a 36 per cent annual increase in the NRB credit to government.

Commercial Banks

There are three commercial banks operating in Nepal as of the end of 1984, namely Nepal Bank Ltd., Rastriya Banijya (National Commercial) Bank and Nepal Arab Bank Ltd. (NABIL). The last of these is a joint venture with 50 per cent share of Arab Bank of Dubai and the other 50 per cent of two public sector FIs and individuals in Nepal. NABIL commenced operation in the second week of July 1984. The Act which governs the organisation and the business of commercial banking in Nepal is the Commercial Bank Act, 1974 promulgated on October 21, 1974 and three amendments in it effective January 2, 1978, October 20, 1982 and November 12, 1984.

The paid-up capital of NBL is Rs 15 million and of RBB Rs 20 million (Table 4). The government owns 52 per cent of shares of NBL and all shares of RBB. The Commercial Bank Act provides that the government may nominate the chairman and all other directors of a bank fully owned by it and more than half of the directors of a bank where it holds a majority of shares. The government may empower the NRB to nominate up to two directors in the former category of bank and one director in the latter category. This provision has been strictly carried out and it has facilitated NRB's regulation of the banking industry. Table 4 also shows that the government has four members in the Board of Directors of either Bank while NRB has two in RBB and one in NBL.

The Commercial Bank Act delineates the functions a bank may perform. Apart from the usual banking functions of accepting deposits, advancing loans and several others, the Act recognises the

role of banks in introducing innovations in banking practices. Article 12 (d) of the Act provides that the banks may advance loans for agriculture, industry, irrigation or power generation for a period of two years for working capital and for up to ten years for fixed capital. The banks may extend loans to a maximum of Rs. 50,000 to a Nepali national without any security if the project (of any of these sectors) is found feasible. The banks, are, however, authorised to invoke conditions necessary to protect their interest while making transactions with any person. They may supervise the use of loans and make inquiry to ensure their utilisation.

The banks may work as an agent of NRB on conditions prescribed by it and perform banking functions on behalf of the government. The license which must be obtained before starting banking business is issued by NRB after taking consent from the government. The nature of the relationship between NRB and the banks is explained in both the Commercial Bank Act and the Nepal Rastra Bank Act. Article 38 of the former stipulates that the banks shall comply with all such directives as are issued by NRB from time to time in respect of currency, credit and the banking system. The banks must regularly submit financial and other returns as prescribed by NRB. The NRB may inspect or get inspected any office of the banks at any time. It shall be the duty of the bank concerned to submit information as demanded by NRB. The NRB may issue directives deemed appropriate by it after the inspection and the banks shall comply with such directives.

Over the past two decades (1964-84), the total resources of the banks increased from Rs. 132.1 million to Rs. 8541.2 million - a rise of about 65 times in nominal terms and about 18 times in real terms. Before 1966, NBL was the only commercial bank in the country and it had altogether 32 branches. An element of competition in the banking industry was introduced only in January 1966 with the establishment of RBB. By July 1984, the commercial banks had expanded their services through a network of 357 branches. An average branch

served about 46 thousand persons in 1984 compared to 321 thousand in 1966. The urban-rural division of total branches yields a ratio of 65:35. The urban-based commercial banks have indeed penetrated the rural areas even though the deposits mobilised by rural bank offices accounts for only 20 per cent of the total.

In order to examine the course of banking operations, it would be better to divide the whole period into two sub-periods of nine years each, i.e., 1966/67-1974/75 and 1975/76 - 1983/84. In both sub-periods, NRB regulated interest rates on deposits and loans. But during 1966-75, the instrument was used more to influence the direction of lending whatever loanable resources were available. A complicated rate structure was maintained with shades of differences in interest rates for deposits of various maturities and for loans of all sorts of purposes. Lending business of banks was characterised by severe rationing of credit. The second period stands in marked contrast. Now, the rationale for regulating interest rate drew more upon the desirability of augmenting loanable resources and less on influencing sectoral demand for credit. Credit rationing became an exception. However, the interest rate structure, which remains simplified as compared to the first period, came to include in 1976 and 1977, a number of rate differentials.

Table 5 reveals comparative trends in the major components of commercial bank assets and liabilities. All the important components are observed to have moved faster during 1966-75 than during 1975-84. This is, however, principally due to the fact that the banks had started with a very low base in 1966. Total assets and liabilities during 1975-84 increased annually at the rate of 18.7 per cent compared to 28.1 per cent growth during the earlier nine years (Table 5.1). If growth rates were compared during 1960-70 and 1970-80, however, the corresponding figures would be 24.3 per cent and 19.8 per cent which would show a better performance during the Seventies. As compared to the growth rate of GDP which averaged 9 per cent in

nominal terms during 1966-84, the growth of the banking industry is impressive indeed.

Development Banks

There are two development banks in Nepal, Agricultural Development Bank (ADB/N) and Nepal Industrial Development Corporation (NIDC). The operations of these institutions display, in a sense, the structure of the Nepali economy. Agriculture contributes about 60 per cent to the GDP while corporate industrial units account for not more than 5 per cent. The share of cottage industry is almost double the share of other industries but the former is not covered by financial operations of NIDC. In terms of lending operations, therefore, ADB/N is a much larger institution than NIDC.

Agricultural Development Bank. The ADB/N was established in 1968 under the Agricultural Development Bank Act, 1967, by incorporating the assets and liabilities of the Cooperative Bank set up in 1963. Its paid-up capital as at mid-July 1984 was Rs. 190.6 million of which the government held Rs. 147.2 million, the NRB Rs 30 million, and individual land cooperative societies, Rs. 13.4 million. The General Manager and all directors except three are appointed by the government from various ministries. The NRB, the cooperative societies and other shareholders have one representative each.

ADB/N provides short, medium and long-term loans to individuals, cooperatives and corporate bodies for agricultural development. Since the middle of the Seventies, agro-based industries and, in the Eighties, other cottage industries have been made eligible for ADB loans. Short-term loans are advanced to finance seasonal operations of inputs like seeds, fertilizers and labour services. Medium-term loans are extended for the purchase of farm machines and tools and those for industries. Loans for livestock raising and some warehousing loans are also due for repayment in the medium-term (which

covers a period from over 1 1/2 years to 7 years). Projects of long gestation period like tea cultivation are given long-term finance.

Besides granting loans, ADB/N's other functions include accepting demand, savings and time deposits at places where no commercial bank is operating. Since 1984, however, ADB/N has been given permission to open branches that would perform, or introduce in existing branches, commercial banking business irrespective of whether a commercial bank has an office. Twenty-five branches in urban areas have been approved to conduct general banking business which would, however, not cover financing of import trade and credit against gold and silver. ADB/N was allowed to operate like a commercial bank in view of its growing deficit to meet increasing lending operations. This had made ADB/N increasingly more dependent on NRB credit, inducing thereby a greater monetary expansion through a rise in monetary base. ADB/Ns's entry into the general banking industry is likely to help finance a greater part of agricultural and industrial activities out of domestic savings. Some amount of transfer of urban savings into rural investment seems inevitable in the process, but more than that, the mixed type of banking undertaken by an institution like ADB/N is likely to increase the rural savings rate as well (APROSC, study on Rural Savings Mobilisation in Nepal, Kathmandu, 1984).

During the decade 1974-84, the total resources of ADB/N increased annually at a rate of 20 per cent and aggregated Rs. 1,298.6 million at mid-July 1984 (Table 6). The structure of ADB/N's liabilities has undergone a vast change in respect of the two principal components, viz., paid-up capital and borrowings. In 1974, the equity accounted for 27 per cent of its total funds while borrowings supplied 23 per cent. Over the following decade, the respective shares changed dramatically and stood at 15 per cent and 60 per cent on mid-July 1984. Among the sources of borrowings, NRB retained up to 1983 the leading position (accounting for 45 per cent of total) it had in 1974. However, foreign suppliers of ADB/N's debt,

notably Asian Development Bank, have grown in importance too. They contributed 43 per cent to ADB/N's outstanding borrowings in 1983. In 1984 the shares of these two sources were equal - 43 per cent.

The asset structure of ADB/N is naturally biased toward loans proper. In 1984, the loans absorbed 70 per cent of total assets, gaining 34 percentage points since 1974. Investment in government securities has remained a nominal fraction of total assets (0.6 per cent in 1983). The unclassified assets accounted for 26 per cent of total in 1984. This relatively high proportion is mainly because of the holding of immovable property and office equipment necessitated by the operation of a huge number of branches spread throughout the country.

The lending operations of ADB/N as seen in Table 6.1 are more or less evenly spread out over production of agricultural crops; farm mechanisation including, other forms of irrigation; raising of livestock, etc; industry, marketing and warehousing; and tea plantation and horticulture. Loans with the maximum turnover are those for crop production, as they are mostly due for repayment by the lapse of one year.

Demand for ADB/N credit has considerably increased in recent years even in areas where the traditional money lenders are rooted firmly as the principal supplier of credit. This is attributable principally to vigorous expansion of numerous innovations in its lending practices. Project viability remains the cornerstone of advancing loans in ADB/N's offices, as the principal collateral it has to accept is land, the marketability of which is poor due to various reasons. Liberal valuation of collateral for sound projects introduced in the late Seventies has provided more favourable terms of contract to borrowers. Mobile teams are sent to vilcages to assess credit requirements for crop production, thus lowering information and transaction costs of borrowing for the small farmers.

Another innovation, probably the first of its kind in Asia, was the Small Farmers Development Project (SFDP) introduced in 1975. As of 1984, SFDPs have, their own functioning offices at 121 places spread out in 46 districts of the country. The characteristic feature of the projects is that groups must be formed among small farmers and landless labourers to enable them to borrow from the project office. Lending may be made to an individual of the group or to the group itself but the entire group stands as the guarantor against nonrepayment of the loan. Loans disbursed through SFDPs during 1982/83 amounted to Rs.42.4 million, constituting 9.4 per cent of total disbursements of ADB/N in that year.

Nepal Industrial Development Corporation (NIDC). The NIDC was established in 1959 with the objective of promoting industrial growth in the private sector through financial and technical assistance. It was created by a special charter, viz., the NIDC act. The paid-up capital as of mid-July 1984 was Rs.190.3 million of which the government has subscribed Rs.181.3 million and NRB, the residual of Rs.9.0 million. Traditionally, the technical assistance of NIDC included, among others, preparation and dissemination of industrial feasibility reports, providing consultancy services to potential investors and development and management of industrial districts in Kathmandu and Hetauda. With the inception of Industrial Services Centre, also in the public sector, NIDC has functioned more like an industrial bank, principally concerned with advancing medium and long term credit to industries and with equity participation. Its other forms of financial assistance are guarantee arrangement with commercial banks which provide direct loans to its clientele industries, and underwriting equity shares of public limited companies. Between 1973, when the Small Industries Development Corporation was dissolved, and 1976, when commercial banks took over the business, NIDC was also engaged in the promotion of cottage industries.

Any industrial enterprise which is above the scale of cottage industry (defined as having investment on fixed assets not exceeding Rs. 800,000) is eligible for NIDC assistance. There is no such restriction for an enterprise established in an industrial district. All enterprises under the industrial classification of Industrial Enterprises Act 1982, with the exception of hotels in Kathmandu valley, may apply for financial assistance. The terms of the loan contract include a maturity period which may extend up to 15 years depending on the nature of the project and its prospective ability to service the debt. Security against the loan comprises the client's fixed assets and the assets which may subsequently be added in the project. Interest rates are as set by NRB. The present structure is composed of altogether three rates: 12 per cent on basic industries, 15 per cent on service industries, and 17 per cent on other industries producing luxurious or semi-luxurious goods.

The principal sources of funds of NIDC are, as shown in Table 7, paid-up capital (31.1 per cent of total funds in 1984) and borrowings (46.3 per cent). Borrowings from NRB constitute all of domestic borrowing. NIDC also negotiates loans with foreign institutions (governments or government-sponsored agencies and the World Bank). Foreign borrowings formed a major part of total borrowings before 1977 and after 1982.

Loans to different industries comprise the bulk of the assets of NIDC. As at mid-July 1984, direct loans outstanding amounted to Rs.336.9 million and guarantee for loans Rs.70.8 million, which together filled 68.7 per cent of total assets. Principal categories of debtor industries were hotels (47 per cent of direct loans) and manufacturing enterprises (29 per cent). The other financial use of assets is investment in the equity of industrial units, in industrial districts and to a smaller extent in government securities. No major shift in the components of asset portfolio is noticeable except that with the abandonment of the policy to finance hotels in Kathmandu, lending to manufacturing units has shown some

indications of growth in 1983 and into 1984. Between 1974 and 1984, annual growth rates in the total outstanding loans averaged 18.6 per cent. This relatively high growth is principally due to larger disbursements in the Seventies to hotels while recovery of loans has lagged far behind the targets. In the Eighties the slow recovery was accompanied with lower demand for industrial investment. Industrial policy of the government has provided successive increases in tax concessions and other inducements to industry. But the spurt in investment is yet to come, which reflects itself in NIDC's lending operations.

Contractual Savings Institutions

Employees' Provident Fund (EPF). EPF was established in 1962 under the Employees Provident Fund Act promulgated in that year. It is managed by a Board of Directors consisting of eleven members who are all appointed by the government from various services (administrative, agricultural and others). EPF collects from government employees and from those of corporate bodies entering into an agreement with it, 10 per cent of their monthly salary deducted at the source. An equivalent amount is contributed by the employer institution and transferred to EPF. The EPF manages the accumulated fund, advances loans to contributing employees for various purposes and refunds the principal and the interest on termination of their service for whatever reason.

Provident fund constituted about 95 per cent of total sources of EPF funds in 1974 and 97 per cent in 1984. From Rs.166 million at mid-July 1974, the fund increased by about 10 times to Rs. 1,580.9 million over the following decade. The occasional revisions in the monthly pay of employees and increase in the number of employees are, of course, the main factors responsible for the rapid upswing of the fund's total. Among the principal uses of the EPF resources, investment in the time deposit accounts at commercial banks accounted for about 70 per cent in 1983 (Table 8). Loans to the fund-

supplier employees constituted only 27 per cent of the fund. EPF has begun diversifying its asset structure by placing larger amounts on government securities. It has thus contributed to an expansion of non-inflationary sources of financing the government deficit. At the end of 1983/84, the asset portfolio of EPF has only 49 per cent in the form of time deposits and 18 per cent in the form of government securities.

National Insurance Corporation (NIC). National Insurance Corporation was set up in 1968 under the NIC Act. It started functioning with an authorised capital of Rs.10 million and paid-up capital of Rs.2.4 million. Life insurance business at that time in Nepal was conducted by the Life Insurance Corporation of India. Beginning 1971/72, this part of insurance was included in the activities of NIC for which an amount of Rs.1.8 million was paid in as equity. The shareholders are the government, the NRB and the Nepal Bank Limited. A majority of the directors are appointed by the government.

The total assets and liabilities of NIC amounted to Rs.3 million at mid-July 1970 and, with successive increments each year, reached Rs. 204.3 million at mid-July 1984 (Table 9). The primary source of its assets is the insurance fund constituting 61.5 per cent of total in 1984. Since 1977, life insurance fund has overtaken the non-life fund and their relative shares in the total insurance fund in 1984 stood at 73 per cent and 27 per cent, respectively.

Assets portfolio of NIC contains mainly government bonds which comprise 62 per cent of total and 87 per cent of investments and loans (1983 figures). A modicum (9 per cent of assets) is held in the form of time deposit certificates.

Other Institutions

Credit Guarantee Corporation (CGC). Credit Guarantee Corporation was established in 1974 under the Company Act 1964 with the joint investment of NRB, the Nepal Bank Ltd. and the Rastriya Banijya Bank. Its paid-up capital at present is Rs.7.5 million of which NRB's subscription is Rs.5.5 million and that of the commercial banks, Rs. 1 million each. The main objective of CGC is to compensate the loss incurred by commercial banks or other FIs while investing in agriculture, cottage or small scale industries and other employment-generating activities. It provides guarantee on loans extended by the member institutions in agriculture, industry, services and other sectors. In order to be eligible for guarantee, the individual loan amount must not exceed Rs. 200,000 in the field of agriculture and services and Rs.800,000 in industry. The compensation ceiling is 80 per cent of unrecovered loans in agriculture and industry, 70 per cent in services and 60 per cent in other sectors. The guarantee fee to be paid by lender institutions was set initially at 0.75 per cent of loan disbursement and was revised in 1979/80 to be 0.36 per cent of the amount outstanding. Previously, the fee was to be paid once and for all. As per the revision, the guarantee covers a period of three months and therefore it has to be renewed through the payment of the fee every successive quarter.

Sources and uses of CGC funds are as shown in Table 10. Following the increase in its equity in 1981/82, paid-up capital came to supply the bulk of its resources. At mid-July 1984, the capital accounted for 45 per cent of its total funds and reserve and surplus, 33 per cent. Considering the nature of business of CGC, it is only to be expected that the Corporation would build up a sizable fund in meeting its compensation obligations. At mid-July 1983, however, the compensation fund stood at Rs.2.7 million constituting less than 20 per cent of its total funds of Rs.14.7 million. The amount guarantees totalled Rs.94.4 million as of the same date. The compensation fund thus covered just about 3 per cent of loans under guarantee cover. In

view of the poor recovery rate of bank lending in guarantee areas, the fund could be regarded too small. However, probably because of this, CGC has received very few compensation claims. Authorities are contemplating to expand the scope of guarantee operations of CGC. ^{10/} For the success of guarantee schemes in inducing greater flow of financial resources to priority sectors it seems more urgent to increase its resources and to effect a greater diversification of the liability structure of CGC.

Securities Exchange Centre (SEC). The Securities Exchange Centre was set up in April 1977 with a view to develop a stock exchange in the country. It is owned by the NRB and the Nepal Industrial Development Corporation. In the beginning, activities of the Centre were confined to dealing in government securities. But after a few years of operation, it started selling shares and debentures of public limited companies. Given the slow growth of industrial investment in the country, this aspect of SEC's operations is likely to move in a slow gear for some time to come. In terms of the value of transactions, government securities provide an overwhelmingly large portion of its operations. The Centre was incorporated under the Company Act but in 1983 a Securities Exchange Act has been promulgated. The operations of SEC now fall under this latter Act. With the passage of this Act every public limited company must have the issues of its common stock and other securities indexed. This would, of course, imply an increase in the activities of SEC and is likely to help promote a fullfledged stock exchange in the country.

Post Office Savings Scheme. Savings accounts in post offices were introduced in 1976/77. By 1983/84 there were altogether

^{10/} K.B. Ahikari, "Contribution of NRB in National Development", NRB News (in Nepali), 29th Anniversary Issue, April 28, 1985, p.5.

75 offices with the savings scheme, one each in as many districts. Post office savings banks are known for ease of operations like depositing and making withdrawals and for their ready accessibility. In Nepal, the scheme is yet to catch on and has so far, made only slow progress. By 1982/83, the number of accounts totalled 8,500 and the amount mobilised, Rs. 2.5 million. Much of this amount has been reinvested by post offices in deposits of commercial banks though interest rate on savings deposits at either type of institution is the same.

CONCENTRATION OF ASSETS AMONG FIS

It may be seen from the analysis so far in this section that some institutions, notably the monetary system, have a dominant position in the organised financial system and some others, a weak one. The magnitude of their relative position may be measured in terms of the concentration of assets according to each type of institution. The asset concentration ratios are presented in Table 11. The first thing that can be noted from the table is that between 1965 and 1984, the distribution of assets has gone against the NRB, and in favour of other institutions. At mid-July 1965, as much as 74 per cent of aggregate assets of the financial system was concentrated in the NRB. In the following 19 years, this share dropped to 37 per cent, to almost half of what it was before. With the development of the financial structure, a gradual weakening of the central banks's relative position is very much expected. Not only new institutions emerged as the demand for some sort of specialised intermediation became large enough to sustain a new institution, but innovations in the existing institutions also took place through introduction of new instruments and greater sophistication of the previous instruments.

This has been most obviously the case with commercial banks. From 19 per cent at mid-July 1965, the asset concentration in banks

has gone deeper with 46 per cent at mid-July 1984. This large concentration with the banks is not without reason. Commercial banks in Nepal are a blend of a banking institution proper and a thrift institution. Since there is no other savings bank in Nepal, the savings and time deposits they have mobilised are a several multiple of demand deposits, whose acceptance and creation are traditionally the function peculiar to commercial banks. The deposits expanded rapidly in the Seventies, especially during the second half following the adoption of a high interest policy in April 1975. At mid-July 1970, the banks accounted for about 26 per cent of all assets of formal financial institutions. In the following four years, the concentration ratio rose to 35 per cent (at mid-July 1974). In another six years, the ratio went up further to 46 per cent. The longer-term trend of increase in asset concentration at the banks was of course, the outcome of deposit expansion. The movements in individual years, however, are related with changes in the major components of assets across institutions. The highest gain (of 7 percentage points) in the concentration ratio was recorded for banks in 1974/75. In this year, the average deposit rate of interest (11 per cent) was lower than in the succeeding years, and the inflation rate was higher (17 per cent). Consequently, the deposit mobilisation was at a low key. In the mean time, the lower real interest rate on credit raised the return on inventory of goods and investment in real estate. This caused heavy pressure on the allocation of bank resources. The banks attempted to adjust by squeezing their reserve down to a minimum and by borrowing from NRB. In the process, the burden was shouldered by the external trade sector in terms of reserve losses of NRB. The domestic assets of commercial banks increased while the external assets of NRB declined. The asset concentration ratio thus went in favour of the banks at the expense of NRB. During the Eighties (1980-84), the assets of commercial banks have kept pace with those of the financial system as a whole. The ratio for the banks thus stood at 46 per cent in 1984, the same level as in 1980.

Another important reason for the strong position of commercial banks is their branch expansion. From 32 branches at mid-July 1965, their network expanded to 129 branches in 1975 and 357 branches in 1984. The corresponding figures for population served by an average branch declined from 280 thousand in 1965 to 99 thousand in 1975 and 45 thousand in 1984. This expansion of banking services has facilitated resource mobilisation into banks considerably and has helped maintain the dominance (in terms of overall size) of the banks within the financial system.

A look at the combined degrees of concentration for the monetary system, will show that the gains made by the banks have been more offset by losses of NRB. The concentration ratio thus stood in 1984 at 83 per cent as compared to 94 per cent in 1965, 92 per cent in 1970, and 85 per cent in 1975 and 1980.

Reduction of concentration ratio for the banking system implies an institutional diversification of the asset structure of the financial system. In Nepal, this diversification, has reflected itself in the growth of assets of all categories of non-bank financial institutions. Among the development banks, ADB/N recorded high growth rate during the first decade (from 0.3 per cent in 1965 to 7.2 per cent in 1975). In the second decade, ADB/N has somehow maintained its pace of expansion as shown by the concentration ratio which is more or less stable at 7 per cent since 1975. NIDC has, however, lost ground in the Eighties after having kept a stable growth rate during 1965-80 at around 5 per cent. ADB/N has kept pace with the overall financial system because of continued government support to increase capital resources, in addition to borrowings from the Asian Development Bank as well as from the NRB. These sources have enabled ADB to meet part of the rising demand for agricultural loans in the country. As for NIDC, which is established to support private industrial investment, the decline in its relative position reflects, among others, a general

lack of entrepreneurship as well as (or due to) a low rate of return in industry (above the cottage scale).

The share of other institutions in the total assets of financial institutions is generally on the rise. The case of Employees Provident Fund is interesting. Table 11 shows that EPF accounted for 2.4 per cent of total assets in 1966 and only 2.7 per cent of total after seventeen years (i.e., in 1983). In fact, well over 95 per cent of the total Liabilities of EPF are concentrated in the provident fund which has grown remarkably high (25.3 per cent a year in 1973-83). The low figure for its share in total assets of all institutions is due to its inability to diversify its assets well. It has placed a large proportion of its total assets in time deposits at the banks. Since these deposits constitute a claim over banks which are themselves the financial institutions, they have been excluded from the assets of EPF in the calculation of concentration ratio.^{11/}

SIZE AND DEVELOPMENT OF FINANCIAL INSTITUTIONS VIS-A-VIS THE ECONOMY

In this sub-section the assets of financial institutions are analysed in relation to the overall growth of the economy. This is intended to provide some meaningful idea on how the growth of the financial structure is linked to economic activities in general. The indicators chosen for the purpose are as follows:

^{11/} Inclusion of the deposits of EPF at banks would lead to double counting as the banks have been advancing loans or making other uses of these deposits and appears in the appropriate components of the bank assets.

Financialisation of National Wealth and Related Measures

The marginal rate of financialisation (MRF) of national wealth is one such indicator. It measures the change in total financial assets in the economy as a proportion of Gross Domestic Product. In the early stage of financial development, the degree of penetration of the financial system into the economy is likely to rise at an increasing rate. Hence, it should be expected that the MRF of national wealth will rise too. Data on the total financial assets in the country are, however, not available. The ratios shown in Table 12 are based on proxy variable, viz., total liabilities of financial institutions. These liabilities, chosen for want of a better alternative, are expected to constitute a major part of the total financial assets held by the rest of the economy.

Table 12 shows the MRF, as defined here, at selected points in time. Between 1969/70 and 1983/84, it rose from 2.6 per cent to 5.6 per cent. MRF has increased over time but the increase is not systematic. A look at the annual figures shows that since 1976/77 the percentages show a regular opposite swing every year. This annual fluctuation is mainly due to change in assets of commercial banks and the source of such change is bank deposits. Deposits at the banks presumably depend more on the income of the people and the real return on deposits. Both these determinants have fluctuated considerably during the period concerned.

The lower portion of the table is presented to eliminate this bias. The five-year averages reveal that the MRF of national wealth rose from 3.6 per cent during 1970-74 to 5.7 per cent during 1980-84. Whether individual data or the average figures are examined, the conclusion is inescapable that over time the national wealth has been increasingly financialised. This may be explained by the vigorous drive towards expansion of commercial bank branches undertaken in the Seventies under the aegis of Banking Promotion

Board. The second half of the Seventies also witnessed a rapid expansion of Agricultural Development Bank's branch network. Together, the number of branches of the banks and the ADB increased from 172 at mid-July 1974 to 402 at mid-July 1979, lowering the population per branch ratio from 72 thousand to 35 thousand. The expansion of financial services in the country is one major reason for the growth of financial assets at a faster rate than GDP. Secondly, the organised financial market offered more competitive rates of return to the suppliers of savings. This was aided by lower general rates of inflation during 1974-79 (6.5 per cent).

However, once the institutions has attained some degree of penetration into the rural areas, further demand for financial services would have to be backed by increases in income. As income continued to grow at a slow pace, scope for further branch expansion decreased in the 1980s. Inflation rates were higher (averaging 10.8 per cent during 1979-84), yet no noticeable adjustments could be made on interest rate on deposits. Consequently, the intermediation process of financial institution was not able to continue the momentum of latter half of the Seventies.

The rise in MRF also implies that the income elasticity of the assets of FIs is above unity. The elasticity values are shown in Table 13. For the 19-year period (1965-84) the income elasticity is recorded at 1.79. This implies that every percentage growth in GDP is observed to be associated with an increase in financial institutions' assets in the multiple of 1.79. For 1975-80 and 1980-84, however, the elasticity shows dramatic changes, rising to 2.47 in the first period and then sharply falling to 1.03 in the second. Changes in the assets of financial institutions have remained fairly stable. But similar percentage changes in assets during various periods were associated with varying rates of economic growth. Hence, the fluctuation in elasticity. Of late, and particularly in the Eighties, the elasticity has witnessed a declining trend. This is to be expected in countries where the financial structure has attained a certain momentum of

growth. Viewed in terms of commercial banking in Nepal, the sector does seem to have picked up a respectable, and perhaps a self-sustained, growth path. There is, however, a vast scope for expansion of activities of other (specialised) intermediaries even at the present level of GDP. The income elasticity of their assets is very likely to go up in the coming years. The movement of overall elasticity will, therefore, depend on the relative strength of the banking system vis-a-vis non-bank financial intermediaries.

Degree of Financial Intermediation

If each individual or firm were to spend exactly what he or it earned, or else, if the deficit spending units found it easy to meet their deficit by borrowing directly from surplus units, there would be no place for financial intermediation. Intermediation occurs only because of indirect financing. The preference of individual savers varies with respect to safety, yield and liquidity of their money and with respect to other specific terms of contract. The borrowers in turn will have their own valuations of the terms of the borrowing contracts such as maturity, cost and repayment schedule.

Financial institutions (FIs), by pooling funds from a myriad of sources, are able to meet divergent requirements of the lenders as well as borrowers. FIs only acquire a part of these instruments as there is always an element of direct financing involved. To what extent FIs participate in financing these instruments becomes crucial in understanding the relative importance of the country's financial structure. This can be measured by the financial intermediation ratio as suggested by Goldsmith. ^{12/}

^{12/} Raymond W. Goldsmith, Financial Structure and Development, Yale University Press, 1969, p. 317.

Financial intermediation ratio is defined in flow terms as the ratio of the net acquisition (during a given period) by financial institutions of instruments issued by non-financial economic units to the total issues of such instruments. A rise in this ratio would signify a growing role of the organised financial system in influencing economic activity. This would also indicate that the intermediaries have grown more important than before vis-a-vis the dealers in direct finance. The estimation of this ratio for Nepal was, however, beset with a number of difficulties. In Nepal, the flow-of-funds account is not available for any sector. A rudimentary form of this account may be compiled for the financial system and for the government. The problem is almost insurmountable in the case of households and of the non-financial corporate sector. The figures presented in Table 14 are based on the balance sheets of FIs and on national accounts statistics. Several simplifications have been made while estimating the relevant variables. ^{13/} However, the estimated values of the financial intermediation ratio (FIR) that appear in

^{13/} The bases for estimation are described at the foot of each table. Nevertheless, a few points may be noted here. First, credit to the external sector has been omitted from gross credit extended by FIs which perhaps implies that the ratio shown in Table 14 is, in fact, the domestic intermediation ratio. Second, estimation of change in consumption credit, which appears as a proxy for (net) instruments issued by non-financial economic units for consumption is mainly based on the researcher's own judgment. This is so with respect to non-government sector. For the government, the proportion of 'development' (i.e., total minus "regular") expenditure that actually goes into real investment is officially assumed to be 60 per cent and that for consumption to be 40 per cent. Third, it is the 'gross' figure for the fixed capital formation that has been regularly published since 1974/75. The date on depreciation is available only since 1978/79. The net capital formation for the previous years is thus based on extrapolation of depreciation figure.

Table 14 raise some interesting points. Between 1974/75 and 1983/84, FIR has fluctuated widely within a range from 17.3 per cent in 1975/76 to 52.0 per cent in the preceding year. The average ratio works out at 29.7 per cent and the standard deviation at 9.8 per cent. Of greater importance is the observation that FIR does not seem to follow any medium or longer-term trend. It stood at 24.4 per cent in 1983/84 compared to 52 per cent in 1974/75 and 25.9 per cent in 1979/80.

The formal financial-sector finances an average of 30 per cent of total instruments issued by non-financial sector. The role of financial infrastructure of Nepal is, thus, still very limited in the intermediation process. Especially net fixed capital formation has increased apace over the last decade. The financial system has contributed significantly to the financing of public expenditure, which is clear from Table 14.1. Most of the government securities are held by FIs in Nepal (see Col.7 of that Table). The ratio has gone up to 96 per cent at mid-July 1983 against 83 per cent a decade before. Apart from the sale of securities the government has heavily overdrawn its account at NRB during 1981-84. All this has led to a severe crowding-out of private sector (including government) enterprises. The government (excluding public enterprises) has absorbed, as of 1984 mid-July, over 50 per cent of outstanding gross credit of FIs, as compared to about 15 per cent at mid-July 1974.

Thus, the monetary authorities' heavy extension of credit to government mainly accounted for the rise in FIR in 1982/83 (Table 14.1). In 1974/75, commercial banks had also borrowed heavily from NRB, which had raised the FIR to record levels. In the wake of substantial increases in the interest rate on time and savings deposits effected in April 1975 and a similar drop in inflation rates in the following years, the banks had acquired large and rising volume of deposits. This had caused the M2/GDP ratio to rise swiftly. It had generated optimism that an investment boom was around the corner, that it would be financed by domestic non-inflationary resources. Findings of the lower and unchanging FIR shows that instead the

opposite has taken place. Investment has been certainly rising as revealed by over five-fold increase in net fixed capital formation (Table 14). However, a large part of it has been financed by external resources, mainly foreign aid. ^{14/} The aggressive branch banking expansion which could have contributed to increase the FIR has not materialised.

To sum up, the general indicators of the development of the financial structure display a mixed picture. The indicators based on the number of offices of FIs and those dealing on the liability side of FIs' balance sheets like deposits and total resources show encouraging results. In contrast, the indicators that reveal the degree of financial intermediation in terms of financing the instruments of deficit units, do not signify an increasing role of FIs in influencing economic activity. Sectoral classification of deficit units suggests that intermediation to government has grown enormously at the cost of intermediation to the rest of the economy (Table 14.1).

III. INSTRUMENTS IN THE FINANCIAL STRUCTURE

The process of financial intermediation involves a greater degree of sophistication in financial instruments as economic activities expand. With the rise in demand for financial intermediation, newer instruments are placed before different categories of lenders as well as borrowers. An indication of the relative importance of financial instruments to the economy as measured by the Financial interrelations ratio FIR is shown in Table 15. Tables 16 and 17 trace the movement of this structure over the

^{14/} About 61 per cent of development expenditure during the Sixth Plan (1980-85) was expected to be covered by foreign aid. See Sixth Plan, National Planning Commission, Kathmandu, 1981.

period 1974-1983. The tables include the instruments issued and held by the Nepal Rastra Bank as well.

Instruments Reflecting Main Characteristics of FIs

The sources side of the funds of FIs reveals interesting trends. Currency, demand and time deposits in banks, provident funds, and capital and reserve are the principal instruments issued by FIs and held by the rest of the economy. In 1974, financial intermediation and monetisation of the economy were at a much less advanced stage than they were in 1984. This is manifested partly in the share of currency in total financial instruments. Currency comprised 23 per cent of total sources of financial funds in 1974 and with successive diminutions fell to 17 per cent in 1983. Substitution of other financial assets for money is also apparent from a large reduction in the share of demand deposits from 18 to 9 per cent.

Time and savings deposits have become considerably more important. As against 15 per cent in 1974, these deposits increased at a faster rate than total sources to account for 23 per cent of the total in 1984. Savings deposits are highly liquid; for allowing withdrawals up to Rs. 1,000 a day, these are like demand deposits with the difference that savings deposits earn 8.5 per cent interest. Time deposits are not as liquid but certificates of time deposits are eligible as sound security for borrowing from the respective banks up to 90 per cent of their face value. Yield and liquidity considerations have apparently encouraged economising on money and induced substitution of non-financial assets in favour of deposits.

Provident and insurance funds are other sources of diversification of financial instruments in Nepal.[†] It is difficult to make a clear-cut distinction between economic features of these two types of instrument. Pension funds contain an element of insurance and insurance funds (life funds, in particular), an element of

pension. It is even more difficult to establish clear links between factors like yield and liquidity and the volume of these funds. The importance of these two funds in all instruments is still limited, but it has grown between 1974 and 1984, from their contribution of 4.3 per cent in aggregate financial resources to 8.9 per cent.

For the instruments held by FIs and issued by non-financial sectors of the economy and rest of the world, a more meaningful classification than what the Tables 16 and 17 and .1 exhibit, could have been made but for data constraints. From what has been presented, holdings of foreign-currency denominated instruments has suffered a heavy decline from 41 per cent of the value of all instruments in 1974 to a mere 17 per cent in 1984. This sharp downswing is mainly explained by the movements in the components of external trade and balance of payments, a consequence of poor internal growth performance and a more liberal trade regime. This has also resulted in a decline in the relative position of NRB, as explained in Section II. On the other hand, domestic financial instruments have gained considerably in the portfolio of asset instruments of FIs. Government securities improved their share from 11 to 21 per cent during the ten years under review while other loans to government (mostly overdraft from NRB in 1984) gained 6 points. Holdings of instruments issued by non-governmental sector of the economy (inclusive of public enterprises) for consumption and investment was virtually static (30 per cent in 1984 against 29 per cent in 1974). This shows that claims on FIs against this sector have kept pace with the total claims of FIs, but have not grown quite rapidly. A part of this slower growth is more apparent than real because of the points of time selected. In 1974 and 1975, credit to the private sector has grown rapidly following higher rates of expected inflation vis-a-vis lower interest rate on credit. In marked contrast, the year 1983/84 was characterised by high real interest rates and a tightening of monetary policy on trade credit. The credit expansion was therefore restricted, which lowered the relative share of private sector credit.

Instruments Classified by Marketability

In the previous paragraphs, an account of financial instruments classified according to distinctive features of the types of FIs was presented. The instruments may be further classified in various ways. For instance, the financial structure of a country may be considered to have achieved a greater degree of sophistication if more financial instruments are marketable. The instruments are broadly of two principal types, equity and claims. Their marketability has been shown separately in Tables 16 and 17. Table 16 displays the claims of non-financial units against FIs and Table 17 traces the claims of FIs against the non-financial units (NFUs).

Of the various claims of NFUs against FIs, currency stands as the only true marketable instrument. Banks in Nepal have not yet issued negotiable certificates of deposit that could be freely tradeable in the market. The Negotiable Instruments Act was legislated in 1978 and a stock exchange in a semi-functional form now exists in the country. The exchange is somewhat busy transacting government securities but not other instruments (including common stock). A small exception to what is exhibited in the table is the equity shares of Nepal Bank Ltd. that are held by the private sector. These shares are sold at a high premium but the part of equity that is owned by private sector adds up to only Rs 15 million which is less than 1 per cent of the marketable instrument, currency. Any indication as to the volume/value of sales of these shares in a year is also not available. The common share and recently, debentures, issued by other FIs till mid-July 1984 are either fully owned by FIs or by the government, and are therefore non-marketable. The currency held by the private sector at mid-July 1965 constituted the bulk (58 per cent) of all claims of NF units against FIs. With the growth of deposit institutions and other FIs in the financial structure, deposits and the rest of the non-marketable instruments grew in importance and currency underwent corresponding declines. In 1970, non-marketable instruments at their face value rose to 49 per cent.

These instruments further went up to 65 per cent in 1975, 72 per cent in 1980 and finally 73 per cent in 1984. The rising relative share of non-marketable instruments of financial institutions may be attributed to the underdeveloped state of the secondary market for financial instruments. The instruments are normally held by owners until maturity. In the Eighties, the nonmarketable instruments have maintained their volume, but their relative position seems to have approached a plateau by 1984.

Demand deposits in Nepal have not yet attained a high degree of acceptability as a medium of exchange. For the sake of simplicity, therefore, they are treated as part of non-marketable instruments. As the economy expands, it is expected that the use of demand deposits would be enhanced considerably, and currency would suffer declines. If, however, the economy is not monetised enough, the expansionary forces would perhaps lead to a rise in demand for currency. Consequently, the ratio of currency to demand deposits should increase. In Nepal during the 1980s, currency has been on the rise vis-a-vis demand deposits. The process of monetisation does seem to have had such an influence in Nepal. But there are other reasons too. The balance the public keeps in the form of demand deposits and also the change in this balance reflect, among others, the general condition of domestic and foreign trade, and the price of its substitutes. Since 1982/83, the authorities have tightened restrictions on credit for imports with a view to preventing reserve losses. Business through banks became less favourable as import credit constitutes the largest segment of the total bank credit. The people therefore attempted to adjust by switching to other instruments which yielded some rate of return, or otherwise placed deposits to other uses. Since 1982/83, the NRB financing of the government deficit has increased substantially, causing heavy currency injections into the economy. Hence, the decline in the relative position of marketable instrument (viz. currency) was mostly held in check during the 1980s.

Of the non-marketable instruments issued by FIs and held by non-financial units of the economy, deposits at commercial banks and provident fund at EPF constitute the major forms. Together, these two broad categories accounted for 62.6 per cent of the total non-marketable instruments (deposits 49.6 per cent and the provident fund 13 per cent) at mid-July 1984. As elaborated earlier, these are also the types of instruments recording substantial growth over the past two decades.

The claims of FIs against NFUs and the external world reveal a similar pattern in terms of marketability (see Table 17). Between 1970 and 1984, marketable instruments as a percentage of total instruments decreased from 63 per cent to 50 per cent. The decline notwithstanding, marketable instruments held by FIs stood at each point in time higher than those issued by FIs. Of the two components of marketable instruments, foreign exchange assets have remained in a dominant position throughout the sample period. ^{15/} The importance of government securities (the other marketable instrument) is a recent phenomenon. The changes in relative shares have therefore gone in favour of government securities. In 1974, the holding of government securities comprised 12 per cent of the value of marketable instruments. During the following decade fiscal deficits went on soaring. As even the primary market for government securities is not well developed in Nepal, the financial system has to finance most of these securities. Consequently, government securities-foreign exchange claims ratio increased by 1983 to 15:55. In 1984, increase in the financing of government debt by financial institutions was

^{15/} All foreign assets except SDR holding and IMF Reserve Tranche has been included in marketable instruments. This would seem to be arbitrary; lack of adequate information on types of foreign assets precluded a more appropriate division into marketable and non-marketable instruments. In fact, there would be various degrees on the marketability of instruments.

associated with a sharp decline in the foreign exchange reserve of the country. There was thus a complete turnaround in the ratio which stood at 55:45 at mid-July 1984.

Equity

The equities issued by NFUs and held by FIs are presented in the last column of Table 17. The amount held by FIs totalled Rs 82.9 million at the end of 1983/84, reflecting a slow growth from Rs 14.2 million in 1965. The amounts referred to are the book values rather than the market values as these equities are a part of non-marketable instruments (issued by the non-financial units of the economy). As a percentage of total claims, the equities were, in 1984, well below the equivalent of one per cent. This indicates that financial institutions have not come forward to promote the new industrial or commercial enterprises in the country. This is also a reflection of general underdevelopment of the industrial sector in the country.

Deposit and Asset Instruments of Banks

The commercial banks have clearly dominated the formal financial structure of Nepal. The deposits mobilised by them are the most important source of their funds. In 1984, deposits contributed 82.7 per cent to the total liabilities reflecting an increase of 12 percentage points in 1970 and 9 points since 1980. In addition, the bank deposits constitute approximately one-half of all claims on NF units against the overall financial system. It would therefore be pertinent to discuss in some detail the deposit structure of commercial banks.

In 1970, demand deposits (DD) were the leading type of deposits with a share of 42 per cent, (Table 18). The respective shares of savings and time deposits stood at 14 per cent and 40 per cent. By 1974, TD had overtaken the DD. observed. The decline had to do with the availability of banking services in wider geographical

areas, causing time and savings deposits to increase faster. Comparing the interest rates between 1965-69 and 1970-74, both savings deposits and time deposits were found to offer, in the second period, more than double the interest rates prevailing in the first period. The higher interest rates had probably contributed in a significant way to the growth of time and savings deposits or, through substitution process, to the diminution of the strength of DD. The positive real interest policy introduced in 1975 has continued and strengthened this trend. Consequently, in 1984 the relative shares stood at 55 per cent for TD as against 21 per cent for DD. Savings deposits have also gained 4.4 percentage points at the expense of DD during 1970-84.

The declining importance of DD has contributed to raise the overall cost of funds of the banks. The rise in interest rates on the interest-bearing deposits in 1971, 1974, 1975 and 1982 has apparently increased the cost of funds in two ways: by having to pay depositors more than before for a given amount of deposits, and by inducing a substitution of interest-bearing deposits for the DD. There is, however, another aspect of it which is more favourable to the banks. This is in terms of the use of funds. A bank whose major source of funds is the DD, will find it necessary to apportion larger amounts into cash and other liquid assets than one whose principal source is the TD. The latter position allows the bank to invest more in high interest-earning assets. In normal circumstances, the aggregate demand deposits are also inherently stable so that a small proportion of DD will suffice to cover deposit withdrawals. Nevertheless, from depositors' point of view, time deposits are locked in the bank for a specified period. Hence, TD will require the banks to keep liquid assets as they must stand ready to honour individual deposit contracts that are regularly maturing.

Another form of liquidity the banks must maintain is the mandatory reserve at the central bank. Given the required reserve ratio, a rise in total deposits (which serve as the base for the

ratio) leads to a proportionate increase in the compulsory balances with NRB. The value of cash and the NRB balances comprise the cash reserve of the banks. They also comprise the domestic component of liquid funds. The foreign component includes the foreign currency in hand and balances held abroad. Change in the deposit structure is partly responsible for a reduction in the bank holding of cash reserve from 22 per cent of aggregate deposits in 1970 to 13 per cent in 1975, 11 per cent in 1980 and 10 per cent in 1984. Other factors presumably are increased cash availability assured by NRB's maintenance of currency chests at principal branches of commercial banks, and improvement in communication. To these may be added the ready convertibility of government Treasury bills into cash.

These improvements have enabled the banks to place larger amounts into earning assets. Including investment in government securities, the total earning assets (ex-post) stood at 61 per cent of total assets at mid-July 1970, and rose to 72 per cent in 1975. A fall in this ratio is to be observed in the following years. In 1980, the earning assets accounted for 70 per cent, and in 1984, 67 per cent of the total assets. However, some of the balances held abroad (a part of liquid funds) seem in recent years to have gone into interest-bearing foreign assets, which somewhat weakens the comparison.

The asset structure of commercial banks has undergone a greater diversification in the post-1975 period. The diversification is in terms of both the type of debtors and of the period of lending. As indicated at various sections in this study, the government has become a larger debtor of the banks in recent years. At mid-July 1970, its share in total loans and advances was 6 per cent. It rose to 8 per cent in 1975, 12 per cent in 1980 and then accelerated rapidly to 26 per cent in 1984. This rapid accumulation of liquid assets in the asset portfolio of the banks has been of some concern to the banking industry. For the more liquid the assets, the lower return they will yield and the smaller the profit for the shareholders.

This will be more so if a larger portion of the debt incurred by the banks is in the form of time deposits, and secondly, if the longer maturities predominate the TD structure. This is exactly applicable to Nepali bankers. Table 19 presents the term structure of time deposits. Unfortunately, the figures are available only since 1974. At mid-July 1975, i.e., about two and a half months after the 50 per cent increase in interest rates was effected, the two-year deposits comprised two-thirds of total time deposits. Nine-years later in 1984, this proportion rose further to 79.5 per cent. Three-month deposits (bearing only 4 per cent interest) decreased from 8.2 per cent to 0.1 per cent. Six-month deposits carried 9 per cent interest but nevertheless lost their share and stood at 1.4 per cent in 1984.

The data on maturity structure of loans and advances other than government securities is not available. However, due to gradual increase in term lending in agriculture and industry, the average maturity of loans is likely to have increased to some extent. These loans again come under priority sector credit which would imply a lower (to the extent the loans are advanced to cottage scale enterprises) average return and involve greater risk. The end result is, therefore, the diminution of profit rates. The earnings and costs of banking operations are as shown in Table 20. Column 18 of the table shows net profit that includes amount allocated to reserve and other funds and a small amount for dividend distributed. The interest payments increased from 7 per cent of total deposits in 1974/75 to about 10 per cent in 1982/83. Interest plus discount fees and commissions received also rose correspondingly from 11 per cent to 14 per cent of total loans and advances thus maintaining a 4-point differential over the years. However, other operating expenses have shown a rising trend to reduce net profit as a per cent of equity and reserve.

Priority sector credit is seen in Nepal as one of the indicators of the developmental role of commercial banks. The

outstanding credit to priority sector is reported in Table 21. Against the target of 7 per cent of total deposits (as of preceding year's mid-July) the actual performance of the priority sector credit has stood consistently low in all the years (except 1977/78). Since 1982/83, the credit requirement was raised to 10 per cent of deposits. At the end of 1983/84, credit to priority sector amounted to Rs 119.5 million or 4.6 per cent of the total deposit liabilities. The obvious reasons for the heavy shortfalls are high cost of managing the priority loans, lower return on them and their greater riskiness of repayment. There has been an increasing pressure on the banks in the last few years to bring about a more appropriate diversification in their asset structure. Beginning 1984/85, the banks have again been urged by NRB to make adjustments in their lending operations such that productive sectors of the economy which include priority sectors, among others, receive at least 25 per cent of their aggregate loans and advances.

Financial instruments available in Nepal are characterised by the dominance of claims over equities and by a low degree of marketability. Secondly, the diversification of the institutional structure of the financial system has not been able to bring forth a diversification in terms of instruments. Innovations have rarely taken place in terms of features of existing instruments or the introduction of new instruments. A few prominent innovations like the practice of group guarantee at Small Farmers Development Project of ADB/N and the intensive banking programme of commercial banks (mentioned in Section II) account for a small proportion of total activities of the respective institutions. There is thus a considerable scope for introducing new instruments in the financial system so as to cater to the varying preferences of actual or potential savers/investors.

IV. THE FINANCIAL STRUCTURE AND ITS IMPLICATIONS FOR MONETARY POLICY

The financial structure of Nepal has remained evolutionary in the past two decades. There are a number of types of financial institutions which have not yet emerged, such as finance companies and private sector pension funds. Even among the institutions that exist, the rate of diversification from the banking system to the specialised intermediaries has been slow. The specialised agencies work more in an environment of monopoly as there are no two institutions serving identical or similar purposes and also, all of them operate in the public sector. The monopolistic tendencies also pervaded the commercial banks until recently when a third commercial bank opened its doors. There is a vast unorganised financial sector which has an unknown degree of interaction with the organised system.

The limited number of financial institutions has had its own implication for the development of financial instruments. There are not only a limited number of instruments for the public to choose from but the instruments mostly suffer from lack of marketability. Rarely has an innovation been introduced in the financial system to upgrade customer services, for instance.

While the financial structure of the country is thus not well-developed, a number of policies have indeed been taken from time to time with the explicit objective of affecting the structure. There were policies which did not have such objective but they nevertheless affected the financial structure. These policies are discussed briefly in the next section.

POLICIES ON THE FINANCIAL STRUCTURE

The First Decade (1965-74): The Foundation Years

During the first decade of the period, the major policy thrust was on promotion of new institutions, rather than on the use of monetary policy instruments to regulate them. Institutions like the Rastriya Banijya Bank (the second commercial bank), the Agricultural Development Bank, the National Insurance Corporation and the Credit Guarantee Corporation were added to the financial structure of the country during this period. By the end of the Sixties, the commercial banks had expanded their services to wider geographical areas through a network of 80 branches. The Nepalese rupee had also settled as the currency in circulation and the banks were no longer permitted to offer the Indian rupee deposit account. The exchange rate vis-a-vis the Indian rupee had been stable for some years now.

The Rastra Bank found the situation suitable enough to launch a more comprehensive regulation on the interest rates on bank deposits and loans. This was in the year 1971. The interest rates were increased slightly but they were still at a low level. The rationale behind having a low interest regime was that it would promote real investment. The banks, however, continued to restrict themselves to the financing of trade, especially exportable agricultural items like rice and jute. Other activities which the banks supported through lending were the hire purchase business and lending against some industrial commodities. The low interest rates encouraged demand for credit to grow much faster than what the deposit expansion could sustain. Even though the Rastra Bank stood ready to provide refinance for the favoured sectors, the refinance was not used on a large scale except in 1974. Credit was rationed heavily, consistent with the financially repressed regime. Since the banks formed an overwhelmingly large part of the organised financial structure, the low interest policy suppressed the growth of the overall structure.

The fiscal year 1974/75 marked a turning point for the financial system of the country. Two policy decisions were taken in that year which substantially influenced the intermediation process of financial institutions. The first was taken in 1974 and was geared at reforming the asset structure of commercial banks. A 'small sector' was defined to cover agriculture, industry and the services sub-sectors in which the banks were urged to lend an amount equivalent to at least 5 per cent of their total deposit liabilities. This was done to induce a more competitive financial structure since there were other institutions specialising in agricultural or industrial loans. For the banks it amounted to practising a more generalised type of banking. The small sector financing programme was renamed the priority credit programme in 1977 and the minimum lending requirement was raised to 7 per cent of total deposits. In 1982/83, the banks were again asked to intensify efforts to make the programme a success and lend an amount to the equivalent of 10 per cent of deposits.

Except for this policy of initiating a diversification of credit instruments for the banks, the first decade was mainly a period of building the infrastructure for the operation of monetary policy instruments to be used in the years ahead.

The Second Decade (1975-84): The Period of Halting Growth

The period under review started with a turmoil in the money market. Under the impact of higher (around 18 per cent) inflation and lower interest rates the deposit growth slowed down considerably. The OPEC-shock of 1973-74 also contributed to the acceleration of credit demand. To adjust to the increasing demand pressure, the banks resorted heavily to borrowing from the Rastra Bank. For the private sector, and especially for the small borrowers, this meant a high dose of credit rationing.

This situation did not, however, last long. In 1974/75, the Rastra Bank stepped in with a series of policy measures. The

important measure for the present purpose was taken in April 1975 when the interest rate structure was revamped for all the deposit and credit institutions. On deposits, both the savings and the fixed accounts would now carry a much higher interest rates than before. The rate structure was simplified too. On loans, the interest rates were also fixed higher. There were fewer lending rates now and their range was narrowed down. 16/

The high interest rate policy was aimed at raising the sagging growth of financial savings, meeting the rising investment and credit needs of the economy, and thus bringing financial intermediation on to a more efficient level. Later adjustments in the interest structure have all followed the policy of keeping the real interest rate at a positive level. The policy is to facilitate an increase in the overall financial intermediation rather than to influence the relative strength of individual institutions within the financial structure.

Liquidity and reserve requirements constitute another policy instrument that have affected financial intermediation, particularly to the government. This instrument has been in effect throughout the period under review except for two years (1975-77) when high liquidity at banks had made the liquidity restrictions redundant. At present the required liquidity ratio is equal to 32 per cent of total deposits. The liquidity ratio (which includes the 9 per cent mandatory reserve ratio) has come in handy for the authorities to finance public debt from private savings. This has led to some substitution of central bank financing of government borrowing by commercial banks.

16/ See for details: (1) SEACEN Research & Training Centre, Monetary Policy in SEACEN Countries, Petaling Jaya, 1980. (2) Agricultural Projects Services Centre, Study on Rural Savings Mobilisation in Nepal, Kathmandu, 1984, pp. 34-43.

Since 1983, however, the government has adopted the policy of going directly to the market for private savings and compete for them along with the financial institutions. It issues National Savings Bonds which yield 13 per cent rate of interest compared to 13.5 per cent on two-year fixed deposits in the banks. The income from bonds is tax-free. The banks are not, however, allowed to buy them. In the past two years the government has mobilised over one billion rupees through these bonds. The marketability of government bonds has shown some improvement as a result of the policy of issuing bonds for the non-bank sector at attractive rates. Together, with this, the establishment of Securities Exchange Centre (in 1977) and the legislation of Negotiable Instruments Act have in a sense led to the emergence of a semblance of securities market in Nepal.

The policy of refinancing the loans for agriculture, industry and exports has made the ADB/N relatively stronger in the financial structure of Nepal. Of the total agricultural credit instruments held by the financial system, the share of ADB/N has remained well over three-fourths during the past decade. Commercial banks have been flush with their own funds for most of the period, obviating the use of the refinance facility. The banks also subscribed to debentures issued by ADB/N to meet its chronic fund shortage. The imbalance in the asset and the liability structure of the ADB/N was visible on two counts. Firstly, it advanced loans in amounts far in excess of the deposit it mobilised from the public or what it financed from its capital base. It was dependent more on foreign resources and the Rastra Bank refinance. Secondly, it charged interest rates (on loans) which were well above what it had to pay on its borrowings. To remove the complacency arising from easy availability of low-cost money, the ADB/N has been recently brought to compete for funds in the open market. A total of 25 branches of ADB/N are allowed to operate as commercial banks.

The policy of expanding the banking services remains one of the important aspects of NRB policies. During the Sixth Plan (1980-

85), the target was to increase the number of branches such that the population served by an average branch is lowered down to 30,000. The achievement of the Sixth Plan fell short of target by a considerable margin. The population-branch ratio dropped only to 43,000 by the end of the Plan. The earlier target has now been carried into the Seventh Plan (1985-90).

The expansion of branch network in rural areas is aimed to help realise three objectives: enhancing the rate of saving mobilisation, improving the allocation of credit, and in the process, assisting further monetisation of the economy.

The policies discussed above have had a direct bearing on the size and growth of the financial structure. The policies were taken to increase the financialisation of national wealth and to influence the overall and sectoral financial intermediation. A few other policies were pursued to help restore stabilisation of the economy. Ceilings on the total outstanding credit to non-government sectors have been imposed for some years in the late 1970s. The purpose of the ceiling was to prevent import acceleration and avert decline in the external reserve. A second objective was to check inflationary pressures generated by rapid expansion of bank credit.

IMPLICATIONS FOR MONETARY POLICY

The purpose of this section is to briefly evaluate two things: whether monetary policies on financial structure have been effective in achieving the stated objectives, and whether the financial structure of Nepal has been conducive enough to facilitate the achievement of other objectives of monetary policy. The problem with the separate evaluation arises when a given instrument of policy influences both sets of objectives. In the following paragraphs, therefore, an attempt is made to discuss the combined effects of monetary policy.

Financial Deepening

One way of assessing the extent in which monetary policy has been effective in contributing to the growth of the financial structure, is to see the level of financial deepening the economy has attained. This can be measured by some ratios like $M1/GDP$, $M2/GDP$, and $M2/M1$. These indicators are shown in Table 22.

$M1$ was 6.5 per cent of GDP in 1964/65 and 7.9 per cent in 1974/75. The growth of money stock accelerated in the latter half of the 1970s causing $M1/GDP$ ratio to rise to 11.4 per cent. This substantial growth was due to a greater attraction of the public towards monetary assets.

The incentive to hold money was higher during 1975-80 because of a more stable price situation. The increase in the rate of return was much more pronounced for $M2$ than for $M1$, after the interest rates on time and savings deposits were increased by NRB in April 1975. The $M2/GDP$ ratio rose from 7.1 per cent to 11.7 per cent during 1965-75. Over the following nine years it came to stand more than doubly higher, 24.8 per cent in 1983/84. The growth of time and savings deposits has dominated the expansion in $M2$. The $M2/M1$ ratio thus went up from 1.1 on mid-July 1965 to 2.1 on mid-July 1984.

The extent of financial deepening in Nepal can be gauged by the ratio just analysed, i.e., $M2/GDP$. The commercial bank sector is the largest contributor to the size as well as growth of the financial system in Nepal. The banks also hold a substantial amount of another form of financial saving, viz. the provident fund. The only diversification for Employees' Provident Fund in recent years was noticed in 1983/84 when it put a modest fraction of its resources in the newly-issued high-interest National Saving Bonds. The aggregate monetary resources measured by $M2$ thus covers most of the principal liabilities of financial institutions to the public.

The above measure of financial deepening may be supplemented with the indicator of holding of real money supply in per capita terms. The per capita ^{17/} broad money at 1974/75 prices, increased from Rs. 231 in 1969/70 to Rs. 544 in 1983/84 (see Table 22).

All the chosen indicators suggest that the financial system has indeed attained a certain depth. These measurements also seem to have responded to changes in monetary policy like changes in the real rate of return on money and quasi-money. They have apparently been influenced by the policy for expansion of bank branches. The question is, given the success in mobilising financial savings, have the same policies been able to lead to a higher level of financial intermediation? The financial intermediation ratio, analysed in Section II, casts severe doubts on this. The degree of intermediation is found to move up whenever NRB injects more money into the economy through other financial institutions. Because of its stated refinancing and discounting policy, NRB is normally compelled to supply credit to them. So the public demand for higher intermediation may be the cause of NRB injections of money rather than the other way round. Whichever way we look at it, it seems fair to conclude that the financial system has not been able to increase significantly the extent of financial intermediation. Sectoral division suggests, of course, that the intermediation to the government has been pushed high, largely at the cost of intermediation to other sectors.

Credit Allocation and Credit Control

Allocation of credit is sought to be done through the maintenance of a differential interest rate structure and credit ceiling. When in 1977 interest rates were realigned by unifying the rates applicable to a given purpose across all financial institutions,

^{17/} In terms of economically active population aged 15 years and above.

it was hoped that the measure would help integrate the markets of formal finance. The unification had become necessary because the commercial banks were given the extra responsibility of lending in areas in which the specialised institutions were functioning before. Specialisation reduces transactions cost for the borrowers. ADB/N was experienced in project lending in the field of agriculture. For this reason the commercial banks turned out to be no match against ADB. Secondly, the resource cost of ADB/N as explained elsewhere, was smaller than the cost of deposits for the banks. The interest realignment was thus in favour of ADB/N. The banks in recent years have attempted to adjust by lending in areas where the effective competition with the other institutions is little, traditionally. These areas mainly comprise the cottage industry. The banks are, however, wide off the mark in making adjustments so as to meet the minimum quantitative requirements for priority sector lending.

Attempts to set quantitative restrictions are likely to fail when at the same time prices are also set monopsonistically by the authorities. Controlling only one of the two variables, viz., interest rate and the volume of lending, and letting the other to be determined by market forces, are most likely to succeed. Regarding the interest rate, it must be said that the NRB stands ready to refinance the priority loans at rates normally 4 per cent lower than the lending rates of the banks. Yet the programme is short of being a success as the banks have frequently experienced difficulty in managing their own excess reserves.

Instead of the minimum imposed as on the priority credit, a ceiling is occasionally enforced on credit to non-government sector. This is done especially when the external reserve position threatens to go out of hand. The ceilings were imposed in 1974/75 (suspended because of abnormal conditions arising from the OPEC shocks of 1973/74) and in 1977/78 through 1979/80.

It may be mentioned here that there are at least two aspects of the financial structure having implications for the effectiveness of credit ceiling. First, where the objective is to control the gross credit of commercial banks, the ceilings tend to work effectively. The structure of bank loans is such as to keep the banks away from competition with other financial institutions. Also, the fact that EPF largely holds financial assets that are issued by the banks, leaves only development banks outside the purview of ceiling on bank credit. The Gurley-Shaw hypothesis that the purpose of monetary policy would be thwarted when the non-bank financial intermediaries are not covered, does not seem to be true in the case of Nepal. The financial structure is not advanced enough to ensure the process of substitution between institutions. For better or for worse, this tends to make monetary policy more effective.

Second, if the objective of the ceiling is to help control diminutions in foreign exchange reserve, the quantitative ceiling alone may well be inadequate. As the ceiling is announced months earlier, there is time for the banks to adjust their asset portfolio. Plans to finance working capital of industries may be postponed in favour of import credit and so on.

To take care of this possibility, the monetary policy has of late focussed more on sectoral distribution of credit rather than on the total amount. In 1982/83, for instance, margin rates were increased on credit for the imports of certain luxury and semi-luxury goods to cent per cent. This measure helped discourage the respective imports, although the policy of issuing import licenses by the government was also tightened at the same time.

To conclude, the instruments aimed at regulating the asset/liability portfolio of commercial banks tend to influence the portfolio of the overall financial system. The effect is not, however, quick or automatic. As the secondary market in financial instruments is not developed, NRB is not able to engage in the open

market operations when for instance there is a need to mop up excess liquidity. The instruments of direct control like credit ceiling seem to have been moderately successful in the past. But they have not been adequately tested in the sense that it is hard to say what would have happened in their absence. Selective credit policy is found to work normally when the authorities intend to squeeze on credit. Where the aim is to promote a virgin sector, the use of minimum credit restrictions at specified rates of interest does not produce the desired effect.

PROBLEMS

From the indicators discussed in Sections II and III, it may be seen that Nepal's financial structure has developed to some extent vis-a-vis the economy in general. The important indicators like the MRF of national wealth and the financial intermediation ratio show, however, that the modest growth achieved is characterised by severe oscillations. The slow growth of the financial structure may be attributed to a number of factors as discussed below.

Growth of the Economy

So far the authorities have pursued a policy of supply-leading financial system. Bank branches have been opened in places which at present do not show enough potential to support a banking office. This leads us directly to a major problem for the development of financial structure in Nepal. The problem is that the economy is not growing satisfactorily as the rate of growth has stayed well below the modest targets set by national plans. So long as demand remains static, there is a limit to the expansion of the supply of financial services if the institution providing these services is not to undergo losses.

The authorities have attempted to find ways to overcome the constraint that is holding back the expansion of financial services in the country. The policy of merely extending loans for productive sectors was replaced by a new policy that would cater to all the economic and social needs of the rural population. A programme called the Intensive Banking Programme was launched in 1981. The banks are called upon to assess credit requirements for all genuine activities in a given area, provide loans and closely supervise the credit. For the banks the adjustment to these programmes has been rather slow since these new areas involve a high degree of risk for them. The Credit Guarantee Corporation has been unable, due to its small capital base, to induce a desired diversification of the asset structure of commercial banks.

Trade and Exchange Policies

The interest rate policy pursued over the last decade has been successful in mobilising resources at a higher rate. The same is not, however, true of the allocation of credit. Quite frequently in the recent past, the banks faced difficulties in finding the borrowers and they took to investment in government securities as a last resort to reduce the holding of non-earning assets. As a further adjustment to excess liquidity, they have sought to promote large business loans in the form of overdraft. But such credit extension apparently conflicts with the balance of payments objective as it unduly stimulates imports.

The high propensity to import in Nepal is more due to inadequate enforcement of trade policies that are adopted without giving due consideration to its open border with India, than it is due to GDP growth. The policy pursued by India of severe import restrictions on luxurious consumer goods induces the trading community of Nepal to engage in illegal entrepot trade which have adverse BOP implications. A lax enforcement of the trade policies of Nepal aggravates this process. The situation may deteriorate further

because of the fact that Nepal has been following a fixed exchange regime without exchange control vis-a-vis Indian rupee. On the other hand, the exchange rates with the major currencies of the world are quoted daily, accommodating day-to-day fluctuations in the value of US dollar (the intervention currency) in international markets. Consequently, the Nepalese authorities have to watch against a break in cross rates arising from the triangular exchange rates. The shocks from India are readily transmitted to Nepal and these are allowed to be absorbed by the movements in Indian rupee reserve but not by exchange rate changes.

The problem with the adoption of a flexible exchange regime vis-a-vis Indian currency lies in the characteristics of the traded goods sector. The proportion of actually traded goods to GDP is rising gradually but it still is within 25 per cent. The tradeable goods sector is, however, considerably larger. Because of ease of mobility of all factors of production (as well as goods) across the border, there is little in Nepal that cannot be traded. The high ratio of tradeables to non-tradeables makes it unlikely for measures like devaluation to affect the relative prices. In such a case the effect of exchange rate changes would mostly be absorbed by changes in price level. Improvement in balance of payments would still be possible provided the movements in exchange rate leads to a decline in real absorption in the economy. In the short run, the presence of money illusion might reduce absorption to a certain extent. But there would be little permanent advantage when price rise tends to nullify the potential benefits of devaluation. Alternatively, enforcing credit crunches to check BOP deficit keeps intermediation at a lower key.

Political and Bureaucratic Interference

This factor is of great importance in the development of financial structure. As almost all the financial institutions in Nepal are either owned or controlled by the government, they are

susceptible to interferences from politicians in power and from bureaucracy. Where work evaluation is not based wholly on the amount and quality of work one has performed, there will be lack of motivation to attain high standards. This is reinforced by monopolistic practices followed by the institutions which is again a consequence of public ownership. This explains why consumer services are poor in Nepali banks and non-bank financial institutions. It is rare that an institution goes out to sound investment outlets, usually it will merely wait for a customer rather reluctantly. No wonder the priority sector lending programme has made little progress despite emphasis on it in official pronouncements.

To sum up, there are problems in the development of financial structure in Nepal. The problems themselves suggest areas where improvements must be made so as to make the financial system flexible and responsive to the needs of the economy.

CONCLUSION

This study aimed to analyse the process of development of financial structure in Nepal. It then attempted to examine, in a non-quantitative manner, how far the policies on the structure were effective in achieving their objectives, and also, whether the structure has been conducive enough to help attain goals of other monetary policies.

The findings of the study reflect a mixed pattern of the growth of financial structure. Between 1937, when the first bank was organised, and 1984, when the study ends, a number of institutions were created to cater to the needs of a growing economy. The indicators of the growth of financial institutions, like the financialisation of national wealth, income elasticity of financial assets etc., show that the structure of Nepalese finance has grown faster than the economy as a whole. Other indicators like the

financial intermediation ratio reveal that the financial system has not yet been tailored well to meet the consumption and investment needs of the economy. The diversification of institutional structure has lagged behind the growth of financial system where the monetary system and especially commercial banks enjoy a predominant position. Diversification in terms of instruments is at a low key since currency, bank deposits and provident fund continue to rule the roost.

Policies to influence the growth of liability instruments of commercial banks were generally successful in the past. In contrast the policies on the asset instruments that aimed to influence the allocation of credit did not do as well. While identifying constraints, it was found that the slow growth of the economy, the nature of the trade and exchange policies and the monopolistic practices of the institutions (most of which are in the public sector) were constraining the development of financial structure in Nepal. The non-bank financial intermediaries, except for Employees Provident Fund, were found to record slower growth which tended to enhance the effectiveness of conventional instruments of monetary control.

Table 1

SELECTED INDICATORS ON THE ECONOMY OF NEPAL

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	<u>1964/65</u>	<u>1969/70</u>	<u>1974/75</u>	<u>1979/80</u>	<u>1983/84</u>
1. a. Gross Domestic Product (Current, Rs. Million)	6271	9816	16571	23351	38184
b. Gross Domestic Product (At 1974/75 prices, Rs. Million)	13328	15148	16571	18606	22172
2. Share of Agriculture in GDP (%)	67.6	70.0	69.7	58.6	53.7
3. Domestic Savings/GDP (%)	NA	NA	10.0	11.1	10.4
4. Investment/GDP (%)	NA	NA	14.5	18.3	19.4
5. Population (Million)* <u>1/</u>	10.2	11.3	13.5	14.6	16.2
6. Economically Active Population (Million) <u>1/</u> <u>2/</u>	4.5	4.7	5.6	6.7	7.7
7. Rate of Inflation (based on CPI,%)	NA	10.5	16.7	9.8	6.2
8. Exports <u>3/</u> /GDP (%)	7.0	5.0	5.4	4.9	4.5
9. Imports <u>3/</u> /GDP (%)	13.1	8.7	11.0	14.9	17.1
10. Foreign <u>4/</u> /GDP (%)	2.3*	2.6	2.3	5.7	6.7
11. M1/GDP (%)	6.5	7.5	7.9	11.4	12.2
12. M2/GDP (%)	7.1	9.2	11.7	20.6	24.8
13. No. of Commercial Bank Branches <u>1/</u>	32	80	129	241	357
14. Govt. Expenditure/GDP					
15. Govt. Revenue (Excl. For. Grants)/GDP					

Source: Publications of Central Bureau of Statistics and Nepal Rastra Bank,
and Government Budgets.

- 1/ End-of-period figures
2/ aged 15 years and above
3/ merchandise trade
4/ Grants + loan
* for 1965/66

Table 2
AVERAGE DEBT PER INDEBTED FARM FAMILY

Credit Agency	<u>1969/70</u>		<u>1976/77</u>	
	Amount (Rs)	Per cent	Amount (Rs)	Per cent
<u>Institutional</u>	113	17.0	620	41.1
Cooperatives	6	0.9	103	6.8
Ward/Village Committees	61	9.2	5	0.3
Agricultural Devt. Bank	30*	4.5*	422	28.0
Commercial Banks	16	2.4	90	6.0
<u>Private</u>	552	83.0	890	58.9
Village Moneylenders	266	40.0	373	24.7
Professional Moneylenders	17	2.6	70	4.6
Landlords	30	4.5	33	2.2
Agricultural Traders	14	2.1	75	5.0
Friends and Relatives	218	32.8	325	21.5
Others	7	1.1	14	0.9
Total	665	100.0	1,510	100.0

* Includes the figure for Land Reform Savings Corporation which was subsequently merged with the ADB/N.

Source: Agricultural Credit Review Survey, Nepal, Vol. 1 (Summary and Recommendations), Nepal Rastra Bank, 1980.

Table 2.1

ESTIMATED AGRICULTURAL CREDIT IN THE INFORMAL SECTOR

303

	<u>Unit</u>	<u>Amount (1976/77)</u>
A. Indebted Households in the Sample	No.	1,654*
B. Average Debt per Household from Informal Sources	Rs.	890
C. Total Debt of Sample Households (A x B)	Rs.	1,472,060
D. Total Households in the Sample	No.	2,655
E. Average Debt per Household (C/D)	Rs.	554.45
F. Total Farm Households in Nepal+	No.	1,715,049
G. Total Debt of All Farm Households in Nepal (= E x F)	Rs. Million	950.9
Memorandum Item:		
Gross Credit of Organised Financial System	Rs. Million	2,611.4

* 62.99 per cent of sample households

+ Assumed to be 91 per cent of all households in Nepal (the average size of households consisting of 7.11 members, one of the Survey findings).

Source: Agricultural Credit Review Survey, Nepal, Vol. 1
Nepal Rastra Bank, 1980

Table 3

ASSETS AND LIABILITIES OF MONETARY AUTHORITIES
(In Millions of N. Rupees)

<u>Mid-July</u>	<u>External Assets</u>	<u>Internal Assets</u>			<u>Total Assets = Total Liabilities</u>	<u>External Liabilities</u>	<u>Internal Liabilities</u>		
		<u>Govt.</u>	<u>Others</u>	<u>Total</u>			<u>Monetary Base</u>	<u>Others</u>	<u>Total</u>
1960	137.9	63.2	26.5	89.7	227.6	-	125.6	102.0	227.6
1965	431.3	69.9	51.8	121.7	553.0	-	319.0	234.0	553.0
1970	924.4	111.6	94.7	206.3	1130.7	-	617.7	513.0	1130.7
1975	1173.2	431.9	650.9	1082.8	2256.0	275.3	1098.1	882.6	1980.7
1980	2223.3	1050.1	870.9	1921.0	4144.3	476.6	2215.3	1452.4	3667.7
1983	2340.7	2928.6	940.0	3868.6	6218.3	448.3	3668.8	2101.2	5770.0
1984	2006.2	3545.8	1381.6	4927.4	6933.6	463.5	4299.0	2177.1	6470.1
(%)	(28.9)	(51.1)	(19.9)	(71.1)	(100.0)	(6.7)	(62.0)	(31.4)	(93.3)
<u>Average Annual Growth (%)</u>									
1960-1975	15.3	13.7	23.8	18.1	16.5		15.6	15.5	15.5
1975-1984	6.1	26.4	8.7	18.3	13.3	6.0	16.4	10.6	14.1
1960-1984	11.8	18.3	17.9	18.2	15.3	-	15.9	13.6	15.0
1960-1970	21.0	5.9	13.6	8.7	17.4	-	17.3	17.5	17.4
1970-1980	9.2	25.1	24.8	25.0	13.9	-	13.6	11.0	12.5
1980-1984	-2.5	35.6	12.2	26.6	13.7	-0.7	18.0	10.6	15.2

Table 4

EQUITY AND CONTROL OF FINANCIAL INSTITUTIONS

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Present Position (1983)									
	Year of Incep- tion	Paid-up Capital				No. of Members in the Board			
		Total	Govt.	NRB	Finan- cial Sector	Total	Govt.	NRB	Finan- cial Sector
1. Nepal Rastra Bank	1956	10.0	10.0	-	-	7	2	3	3
2. Nepal Bank Ltd.	1937	15.0	7.5	-	-	9	4	1	2
3. Rastriya Banijya Bank	1966	20.0	20.0	-	-	7	4	2	3
4. Nepal Industrial Development Corp.	1959	177.8	168.8	9.0	9.0	7	4	1	2
5. Agricultural Develop- ment Bank	1968	169.7	129.7	30.0	30.0	7	3	1	2
6. Provident Fund Corp.	1962	-	-	-	-	9	8	-	1
7. National Insurance Corporation	1968	4.2	1.8	1.8	2.4	7	4	2	3
8. Credit Guarantee Corporation	1974	7.5	-	5.5	7.5	6	-	3	6
9. Securities Marketing Centre	1977	3.7	-	2.0	3.7	5		1	

* A Co-operative Bank was established in 1963 but was merged in 1968 with the ADB/N.

Table 5

SOURCES AND USES OF COMMERCIAL BANK FUNDS: PERCENTAGE DISTRIBUTION AND GROWTH RATE

	Percentage Distribution					Growth Rate (in per cent)				
	1960	1966	1970	1975	1980	1984	1960-70	1970-80	1980-84	1966-75 1975-84
<u>Sources</u>										
1. Total Deposits	85.5	63.5	70.7	63.9	73.6	82.7	17.6	24.8	20.7	28.2 22.2
1.1 Demand Deposits	54.1	38.5	29.4	24.0	18.9	17.6	12.7	18.9	15.3	21.5 14.7
1.2 Savings Deposits	5.1	7.7	10.3	9.5	12.6	15.6	28.5	26.9	23.6	31.0 25.5
1.3 Fixed Deposits	26.3	17.3	27.9	28.4	40.1	45.8	20.6	28.8	21.2	35.3 25.2
1.4 Margin Deposits	-	-	3.1	2.0	2.0	3.7	-	-	-	- -
2. Borrowings from NRB	-	14.9	4.1	20.2	5.8	1.8	-	28.9	-12.9	32.5 -9.4
3. Foreign Liabilities	-	-	-	0.5	-	-	-	-	-	- -
4. Other Sources	14.5	21.6	25.2	15.4	20.6	15.5	26.7	21.8	5.2	23.4 18.8
5. Sources = Uses	100.0	100.0	100.0	100.0	100.0	100.0	19.8	24.3	17.2	28.1 18.7
<u>Uses</u>										
6. Liquid Funds	59.1	9.4	29.7	19.9	17.1	20.8	11.9	17.6	23.1	39.2 19.3
6.1 Cash in Hand	6.2	5.8	4.0	2.6	2.4	3.3	-	18.1	26.6	17.2 21.7
6.2 Balance with NRB	12.7	1.4	11.3	5.7	5.6	5.3	-	15.8	15.7	49.3 17.8
6.3 Foreign Currency in hand	10.5	1.2	3.0	1.0	1.1	1.2	-	12.4	19.8	24.9 21.5
6.4 Balance held abroad	29.7	1.0	11.4	10.6	8.0	11.0	-	20.0	27.0	68.2 19.2
7. Loans and Advances	38.2	84.3	61.2	72.5	70.0	67.6	25.6	26.0	15.9	25.9 17.7
7.1 Claim on Government	-	1.7	3.5	5.5	8.2	17.4	-	35.4	41.4	46.2 34.9
7.2 Claims on Govt. Enterprises	-	6.2	5.3	23.7	16.8	12.2	-	39.4	8.3	48.7 10.3
7.2.1 Financial	-	0.7	1.3	0.1	1.4	1.1	-	24.8	11.7	6.2 50.8
7.2.2 Non-Financial	-	5.5	4.0	23.6	15.4	11.1	-	42.3	12.9	50.6 9.2
7.3 Claims on Pvt. Sector	38.2	76.4	48.9	41.8	41.3	36.1	-	22.3	13.3	19.8 16.8
7.4 Foreign Bill Purchased & Discounted	-	-	3.5	1.5	3.7	1.9	-	24.9	-1.3	- 22.0
8. Other Uses	2.7	6.3	9.1	7.6	12.9	11.6	35.2	28.7	14.2	30.8 24.4

Table 6

SOURCES AND USES OF FUNDS OF AGRICULTURAL DEVELOPMENT BANK
(AS ON MID-JULY)

	1964	1965	1966	1967	1968	1969	1970	1971	1972	1973	1974	1975	1976	1977	1978	1979	1980	1981	1982	1983	1984
(In Millions of N. Rupees)																					
1. Paid up Capital	2.9	4.1	4.5	4.8	7.4	12.5	17.6	22.9	33.1	44.8	58.2	66.0	96.8	107.7	113.7	120.2	131.2	141.8	154.4	169.7	190.6
1.1 Government	2.8	4.0	4.4	4.6	4.7	9.7	14.7	19.8	29.7	38.7	48.7	54.3	84.5	74.5	79.5	84.5	94.5	104.5	116.1	129.7	147.2
1.2 Nepal Rastra Bank	-	-	-	-	2.5	2.5	2.5	2.5	2.5	5.0	8.3	10.0	30.0	30.0	30.0	30.0	30.0	30.0	30.0	30.0	30.0
1.3 Individuals, Cooperatives & Others	0.1	0.1	0.1	0.2	0.2	0.3	0.4	0.6	0.9	1.1	1.2	1.7	2.3	3.2	4.2	5.7	6.7	7.3	8.3	10.0	13.4
2. Reserves and Surplus	-	0.3	0.4	0.8	1.7	1.7	1.7	1.8	1.9	2.4	16.1	17.7	20.6	23.3	3.4	4.1	35.1	35.3	56.8	4.2	4.2
3. Deposits	-	-	0.4	1.9	3.3	4.6	5.4	5.3	4.8	5.0	6.3	7.4	9.3	51.4	49.1	40.7	35.1	31.1	35.0	35.2	37.9
3.1 Current	-	-	-	-	-	-	-	3.6	4.2	4.6	6.0	7.1	8.6	29.7	19.1	15.4	14.5	13.3	14.7	15.6	17.9
3.2 Savings	-	-	-	-	-	-	-	0.2	0.2	0.2	0.2	0.1	0.4	19.6	28.4	24.4	19.2	15.9	16.4	13.7	15.3
3.3 Fixed	-	-	-	-	-	-	-	1.5	0.4	0.2	0.1	0.2	0.3	2.1	0.6	0.9	1.4	1.9	3.9	5.9	4.7
4. Borrowings	-	-	0.7	1.8	-	2.2	3.1	8.0	7.5	22.3	49.4	122.0	88.1	132.6	220.6	321.4	343.1	362.7	459.9	570.2	780.2
4.1 Government	-	-	-	-	-	-	-	-	-	-	0.2	0.2	-	-	-	-	-	-	21.2	-	-
4.2 Nepal Rastra Bank	-	-	-	-	-	-	2.0	6.6	6.5	12.5	24.6	98.2	50.8	89.4	127.2	200.3	214.0	218.9	242.0	256.0	332.2
4.3 Commercial Banks	-	-	0.7	1.8	-	0.2	1.1	1.4	1.0	1.0	2.7	2.1	0.5	0.9	46.0	61.6	60.0	55.1	50.5	68.7	113.8
4.4 Foreign	-	-	-	-	-	-	-	-	-	8.8	21.9	21.5	36.8	42.3	47.4	59.5	69.1	88.7	146.2	245.5	334.2
5. Compulsory Savings	-	-	-	-	-	-	-	-	-	-	50.3	58.9	88.8	74.2	58.1	45.6	41.9	38.2	34.8	33.8	36.6
6. Other Liabilities	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
7. Total Liabilities =	0.1	-	0.1	0.2	0.2	0.3	0.8	1.5	2.4	5.1	32.7	23.8	25.9	35.7	41.4	52.7	83.3	84.8	114.5	196.0	249.1
Total Assets	3.0	4.4	6.1	9.5	12.6	21.3	28.6	39.5	49.7	79.6	213.0	295.8	329.5	424.9	486.3	584.7	669.7	693.9	855.4	1009.1	1298.6
8. Loans	0.8	1.2	2.7	4.6	4.8	9.2	18.2	31.4	41.3	56.7	121.1	226.7	221.9	290.6	355.9	426.9	458.2	474.7	566.7	698.4	914.3
8.1 Crop Production	0.5	0.7	1.6	2.7	2.7	-	0.7	2.6	6.6	13.5	20.7	34.1	49.2	58.7	72.1	82.8	91.3	98.3	119.9	163.7	218.5
8.2 Mechanisation and Irrigation	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
8.3 Livestock, etc.	-	-	-	-	-	-	3.4	8.2	13.3	16.5	22.9	35.4	50.0	70.0	93.5	113.9	116.7	114.9	122.5	160.5	202.8
8.4 Industry, Marketing, Warehousing	-	-	-	-	-	-	0.4	1.8	3.5	4.6	8.1	11.8	17.6	32.3	54.5	75.7	85.3	88.0	104.8	142.6	184.2
8.5 Tea, Horticulture, etc.	0.3	0.5	1.1	1.9	2.1	5.2	7.2	9.3	10.2	10.6	29.6	109.1	68.4	85.3	84.8	88.8	90.4	94.8	133.1	133.2	206.3
9. Investment	-	-	-	-	-	-	0.2	0.3	2.7	3.4	27.3	31.4	36.7	44.3	51.0	65.7	74.5	78.7	86.4	98.4	102.5
9.1 Shares	-	0.8	1.8	2.7	2.6	9.2	6.0	2.1	2.1	2.1	41.5	20.5	21.8	19.0	19.1	19.8	18.7	18.2	18.6	20.7	17.8
9.2 Govt. Securities	-	-	-	-	-	-	-	-	-	-	0.4	4.1	4.5	4.5	4.8	4.9	4.9	4.9	5.3	5.9	7.8
9.3 Fixed Deposits	-	-	-	-	-	-	-	-	-	-	16.4	16.4	16.3	13.3	13.3	13.3	13.8	13.3	13.3	13.3	8.3
10. Cash and Bank Balances	1.3	2.3	1.3	1.7	4.5	1.4	2.3	2.8	2.3	6.6	9.2	8.4	13.9	18.0	15.1	10.9	11.7	13.4	19.6	27.9	25.8
11. Other Assets	0.9	0.1	0.3	0.5	0.7	1.5	2.1	3.2	4.0	14.2	41.2	40.2	71.9	97.3	96.2	127.1	181.1	187.6	250.5	262.1	340.7

1/ Breakdown by type of deposit (as on and before mid-July 1970) is not available.

Table 6.1

AGRICULTURAL DEVELOPMENT BANK OF NEPAL'S OUTSTANDING LOANS, BY TYPE*

Mid-July	Loans and Investment										Loan Amounts in Millions of N. Rupees		
	Total Loans	Crop Production (10%) ^{1/}	Mechanisation & Irrigation (100%)	Livestock (15% for Sheds)	Industry Marketing (50%) ^{2/}	Tea Horticulture Etc. (25%)	Total	Col. 8 as Per Cent of Col. 2	Consumption Loans	Investments other than Claims on FIs	Consumption Credit to HMG/N (40 Per Cent of Inv. on HMG Securities) ^{3/}	Total Consumption Credit (10+12) ^{4/}	
	1	2	3	4	5	6	7	8	9	10	11	12	13
1965		1.2	0.1	-	-	0.3	-	0.4	33.3	0.8	0.8	0.3	1.1
1970		18.2	0.1	8.2	0.3	3.6	0.1	12.3	67.6	5.8	2.0	0.8	6.7
1973		56.7	1.4	22.9	0.8	5.3	1.1	31.5	55.6	25.2	2.0	0.8	26.0
1974		121.1	2.1	35.4	1.2	14.8	6.8	60.3	49.8	60.8	16.8	6.6	67.4
1975		226.7	3.4	40.3	1.8	54.6	7.9	108.0	47.6	118.7	20.5	6.6	125.3
1976		221.9	4.9	50.0	2.6	34.2	9.2	100.9	45.5	121.0	20.8	6.6	127.6
1977		290.6	5.9	70.0	4.8	42.7	11.1	134.5	46.3	156.1	17.8	5.3	161.4
1978		355.9	7.2	93.5	8.2	42.4	12.8	164.1	46.1	191.8	18.1	5.3	197.1
1979		426.9	8.3	113.9	11.4	44.4	16.4	194.4	45.5	232.5	18.2	5.3	237.8
1980		458.2	9.1	116.7	12.8	45.2	18.6	202.4	44.2	255.8	18.7	5.5	261.3
1981		474.7	9.8	114.9	13.2	47.4	19.7	205.0	43.2	269.7	18.2	5.3	275.0
1982		566.7	12.0	122.5	15.7	66.6	21.6	238.4	42.1	328.3	18.6	5.3	333.6
1983		698.4	16.4	160.5	21.4	66.6	24.6	289.5	41.5	408.9	19.2	5.3	414.2
1984		914.3	21.9	202.8	27.6	103.2	25.6	381.1	41.6	533.2	16.1	3.3	536.5

* All investments (including those on shares) have been excluded.

1/ Most of the loans for crop production help meet short-term (and recurring) expenses.

2/ Of late, loans for cottage industries (mainly for equipment purchases) have been growing and those for warehouse construction declining.

3/ The proportion of development expenditure going for investment is presumed by government to be 60 per cent of total.

4/ Total investment credit = col. (2 + 11 - 13).

Table 7

SOURCES AND USES OF FUNDS OF NEPAL INDUSTRIAL DEVELOPMENT CORPORATION
(As at mid-July)

	1984	1985	1986	1987	1988	1989	1970	1971	1972	1973	1974	1975	1976	1977	1978	1979	1980	1981	1982	1983	1984
	(In Millions of N. Rupees)																				
1. Paid-up Capital	13.6	16.2	21.2	23.6	25.7	34.1	34.4	37.4	79.8	99.3	119.3	129.3	139.3	157.8	157.8	157.8	157.8	157.8	157.8	177.8	190.3
1.1 MRB	9.0	9.0	9.0	9.0	9.0	9.0	9.0	9.0	9.0	9.0	9.0	9.0	9.0	9.0	9.0	9.0	9.0	9.0	9.0	9.0	9.0
1.2 Govt	4.6	7.2	12.2	14.6	16.7	25.1	25.4	28.4	70.3	90.3	110.3	120.3	130.3	148.8	148.8	148.8	148.8	148.8	148.8	168.8	181.3
2. Reserve and Surplus ^{1/}	0.2	0.7	1.2	1.5	1.6	1.5	1.8	2.0	2.6	3.3	4.0	2.4	3.0	5.8	8.5	6.7	10.6	21.3	28.5	16.8	19.4
3. Borrowings	7.1	15.8	21.1	25.1	27.0	25.5	28.0	40.0	39.1	39.2	42.0	52.9	70.4	86.7	130.1	156.9	161.9	179.6	215.0	260.4	274.6
3.1 Government	2.0	-	-	-	-	-	-	2.8	2.5	2.3	2.0	1.7	1.4	1.1	0.8	0.6	0.2	-	-	-	-
3.2 Nepal Rastra Bank	-	-	-	-	-	-	-	-	0.8	-	-	-	6.0	29.4	71.4	93.9	98.4	119.5	147.5	95.5	181.6
3.3 Commercial Bank	5.1	15.8	21.1	25.1	27.0	25.5	28.0	37.2	35.8	36.9	40.0	51.2	63.0	56.2	57.9	62.4	63.3	60.1	67.5	164.9	93.0
3.4 Foreign	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
4. Other Liabilities	2.8	5.0	2.7	10.4	17.3	15.0	16.9	7.4	9.3	8.1	10.5	10.9	15.9	34.7	46.4	47.0	49.7	50.9	94.3	105.8	109.1
5. Total Liabilities =	23.7	37.7	46.2	60.6	71.6	76.1	81.1	86.8	130.9	149.9	175.8	195.5	228.6	285.0	342.8	368.4	380.0	409.6	495.6	560.8	593.4
6. Loans	13.1	21.9	29.2	34.8	35.4	35.2	42.4	52.0	51.1	57.6	76.5	127.1	152.8	179.8	221.3	252.2	251.2	281.8	299.3	315.9	336.8
6.1 Hotel	3.5	7.1	9.7	10.8	11.0	10.7	11.5	15.4	18.5	18.5	22.9	38.8	49.1	70.1	93.2	112.1	118.5	144.7	157.8	156.6	158.6
6.2 Manufacturing	8.0	11.2	13.9	15.0	14.4	14.9	19.0	20.6	16.9	21.4	30.4	47.7	48.0	47.8	49.7	59.6	51.8	57.3	62.3	90.3	97.9
6.3 Transport	-	1.1	1.4	3.9	4.4	4.0	6.4	6.6	7.3	7.5	7.0	14.4	12.4	10.7	8.7	7.1	7.1	6.6	6.4	5.9	4.9
6.4 Services	0.5	0.9	2.2	2.2	2.2	1.9	1.6	1.5	1.0	1.4	2.1	2.6	2.7	3.4	3.2	3.6	3.6	4.1	4.1	5.5	12.5
6.5 Electricity	1.0	0.9	0.9	1.0	1.0	1.3	1.2	4.5	3.8	3.0	2.7	2.5	1.6	1.0	0.8	0.6	0.2	-	-	1.0	2.0
6.6 Miscellaneous	0.1	0.7	1.1	1.9	2.4	2.4	2.7	3.4	3.6	5.8	11.4	21.1	39.0	46.8	65.7	69.2	70.0	69.1	68.7	56.6	60.9
7. Guarantee for Loans	0.3	0.1	0.7	3.0	4.4	4.4	4.0	4.1	4.4	4.6	4.9	1.1	1.9	11.0	19.6	22.9	22.9	23.3	26.8	75.7	70.8
8. Investment	4.8	6.0	9.4	10.2	11.8	13.0	13.6	14.2	21.2	23.4	28.8	33.0	39.7	44.5	46.4	46.6	48.3	48.5	54.0	51.8	102.2
8.1 Shares	2.3	1.8	3.1	3.6	4.0	4.2	4.8	5.4	11.6	13.8	19.2	21.1	28.0	32.7	33.9	34.8	36.5	36.7	42.2	39.5	67.2
8.2 Industrial Estates	2.5	4.2	6.3	6.6	7.8	8.8	8.8	8.8	9.6	9.6	9.6	9.6	9.4	9.4	9.4	9.4	9.4	9.4	9.4	9.4	9.4
8.3 Govt. Securities	-	-	-	-	-	-	-	-	-	-	-	2.3	2.3	2.4	3.1	2.4	2.4	2.4	2.4	2.4	25.6
9. Cash and Bank Balance	3.4	3.7	2.2	3.1	3.0	4.4	2.5	7.0	12.5	25.2	27.6	5.6	0.5	16.6	14.0	9.4	17.0	6.5	28.2	15.8	16.8
10. Other Assets	2.1	6.0	4.7	9.5	17.0	19.1	18.6	9.5	41.7	39.1	39.0	28.7	33.7	33.1	41.5	37.3	40.6	47.5	87.3	101.6	66.8

^{1/} Include subsidies and grants

Table 9
SOURCES AND USES OF FUNDS OF NATIONAL INSURANCE CORPORATION
(In Millions of N. Rupees)

	1970	1971	1972	1973	1974	1975	1976	1977	1978	1979	1980	1981	1982	1983	1984
1. Paid up Capital	2.4	2.4	4.2	4.2	4.2	4.2	4.2	4.2	4.2	4.2	4.2	4.2	4.2	4.2	9.5
1.1 Life	-	-	1.8	1.8	1.8	1.8	1.8	1.8	1.8	1.8	1.8	1.8	1.8	1.8	1.8
1.2 Non-life	2.4	2.4	2.4	2.4	2.4	2.4	2.4	2.4	2.4	2.4	2.4	2.4	2.4	2.4	7.7
2. General & other Reserves	0.3	0.3	0.8	1.3	3.8	5.4	2.2	3.6	4.3	5.0	5.6	9.1	10.8	11.3	11.8
3. Insurance Fund	-	0.2	0.6	1.4	3.0	4.9	8.0	14.2	24.3	33.1	45.4	55.3	73.5	98.5	125.6e/
3.1 Life	-	-	-	-	0.6	1.4	3.0	7.5	15.3	22.1	29.8	36.4	50.5	71.0	91.6e/
3.2 Non-life	-	0.2	0.6	1.4	2.4	3.5	5.0	6.7	9.0	12.0	15.6	18.9	23.0	27.5	34.0e/
4. Other Liabilities	0.3	3.6	6.2	7.0	6.7	6.0	16.5	21.1	24.9	23.7	33.5	42.6	42.8	50.3	57.4
5. Total Sources = Total Uses	3.0	6.7	11.8	13.9	17.7	20.5	30.9	43.1	57.7	67.0	88.7	112.2	131.3	164.3	204.3
6. Investment & Loans	2.6	4.0	7.7	9.4	13.2	13.2	16.9	22.2	33.5	45.6	62.3	77.2	93.0	118.6	151.3
6.1 H.M.G. securities	2.6	3.4	7.4	9.1	12.9	12.9	16.6	17.4	23.0	35.8	55.8	74.4	89.1	102.6	130.9e/
6.2 Time deposits at banks	-	0.4	-	-	-	-	-	4.5	10.0	9.1	5.8	1.9	2.9	14.5	18.5e/
6.3 Equity participation	-	0.2	0.3	0.3	0.3	0.3	0.3	0.3	0.3	0.3	0.3	0.3	0.3	0.3	0.4e/
6.4 Loans	-	-	-	-	-	-	-	-	0.2	0.4	0.4	0.6	0.7	1.2	1.5e/
7. Cash & Bank Balance	0.1	1.0	0.7	0.5	0.7	1.6	5.9	6.3	3.9	5.7	3.3	3.8	6.4	4.7	5.7
8. Other Assets	0.3	1.7	3.4	4.0	3.8	5.7	8.1	14.6	20.3	15.7	23.1	30.2	31.9	41.0	47.3

e/ Estimated

Table 10

SOURCES AND USES OF FUNDS OF CREDIT GUARANTEE CORPORATION
(In Millions of N. Rupees)

	<u>1975</u>	<u>1976</u>	<u>1977</u>	<u>1978</u>	<u>1979</u>	<u>1980</u>	<u>1981</u>	<u>1982</u>	<u>1983</u>	<u>1984</u>
<u>Mid-July</u>										
1. Paid-up Capital	3.0	3.0	3.0	3.0	3.0	3.0	3.0	7.5	7.5	7.5
1.1 Nepal Rastra Bank	(2.0)	(2.0)	(2.0)	(2.0)	(2.0)	(2.0)	(2.0)	(5.5)	(5.5)	(5.5)
1.2 Commercial banks	(1.0)	(1.0)	(1.0)	(1.0)	(1.0)	(1.0)	(1.0)	(2.0)	(2.0)	(2.0)
2. Reserve and Surplus	0.1	0.3	0.5	0.9	1.1	1.7	2.3	3.0	4.0	5.4
Of which: Compensation Fund	(0.1)	(0.2)	(0.2)	(0.4)	(0.6)	(0.9)	(1.5)	(2.0)	(2.7)	-
3. Borrowing from Banks	-	0.9	0.9	0.9	0.9	0.9	-	-	-	-
4. Other Liabilities	0.1	0.1	0.6	0.7	0.8	0.6	2.5	2.6	3.2	3.6
5. Total Liabilities = Total Assets	3.2	4.3	5.0	5.5	5.8	6.2	7.8	13.1	14.7	16.5
6. Investment	0.3	4.1	4.6	5.0	5.5	5.8	6.3	11.4	12.8	11.7
6.2 Time Deposit Certificates	(2.0)	(1.4)	(1.9)	(2.3)	(2.8)	(3.1)	(5.3)	(10.4)	(11.8)	(11.7)
6.2 Government Securities	(1.0)	(2.7)	(2.7)	(2.7)	(2.7)	(2.7)	(1.0)	(1.0)	(1.0)	-
7. Cash and Bank Balances	0.1	-	-	0.1	0.1	0.1	0.1	0.1	0.1	0.2
8. Other Assets	0.1	0.2	0.4	0.4	0.2	0.3	1.4	1.6	1.8	4.6

Table 11

CONCENTRATION OF ASSETS AMONG FINANCIAL INSTITUTIONS

Mid-July	Total	NRB	Total Assets* (in Million Rs.)		Degree of Concentration (in per cent)											
			Com.Banks	ADB	NIDC	EPE	NIC	CGC	Total	NRB	Com.Banks	ADB	NIDC	EPE	NIC	CGC
1965	737.1	548.6	141.1	2.1	34.0	11.3	-	-	100.0	74.4	19.1	0.3	4.6	1.5	-	-
1966	841.7	591.4	181.1	4.8	44.0	20.4	-	-	100.0	70.3	21.5	0.6	5.2	2.4	-	-
1967	901.1	621.2	188.5	7.8	57.5	26.1	-	-	100.0	68.9	20.9	0.9	6.4	2.9	-	-
1968	1157.5	791.2	264.6	8.1	68.6	25.0	-	-	100.0	68.4	22.9	0.7	5.9	2.2	-	-
1969	1405.5	976.1	320.0	14.5	71.7	23.2	-	-	100.0	69.4	22.8	1.0	5.1	1.7	-	-
1970	1662.5	1097.9	429.5	22.3	78.6	31.3	2.9	-	100.0	66.0	25.8	1.3	4.7	1.9	0.2	-
1971	1907.8	1263.9	483.1	36.6	79.8	39.1	5.3	-	100.0	66.2	25.3	1.9	4.2	2.0	0.3	-
1972	2239.7	1368.9	644.5	47.5	118.4	49.5	11.1	-	100.0	61.1	28.8	2.1	5.3	2.2	0.5	-
1973	2702.2	1600.7	829.8	72.9	124.7	60.7	13.4	-	100.0	59.2	30.7	2.7	4.6	2.2	0.5	-
1974	3407.7	1806.0	1183.0	179.1	148.2	74.4	17.0	-	100.0	53.0	34.7	5.3	4.3	2.2	0.5	-
1975	4009.8	1752.4	1670.2	287.4	189.9	89.9	18.9	1.1	100.0	43.7	41.7	7.2	4.7	2.2	0.5	-
1976	4681.3	2202.2	1806.0	314.6	228.1	102.5	25.0	2.9	100.0	47.0	38.6	6.7	4.9	2.2	0.5	0.1
1977	5522.2	2404.3	2291.4	405.7	268.4	117.0	32.3	3.1	100.0	43.5	41.5	7.3	4.9	2.1	0.6	0.1
1978	6444.8	2644.2	2815.6	470.2	328.8	139.1	43.8	3.1	100.0	41.0	43.7	7.3	5.1	2.2	0.7	-
1979	7925.8	3288.9	3481.7	572.2	359.0	168.9	52.2	2.9	100.0	41.5	43.9	7.2	4.5	2.1	0.7	-
1980	8925.2	3512.8	4102.3	658.0	363.0	206.5	79.6	3.0	100.0	39.4	46.0	7.4	4.1	2.3	0.9	-
1981	10387.7	3745.6	5194.6	680.5	401.1	258.0	105.5	2.4	100.0	36.1	50.0	6.6	3.9	2.5	1.0	-
1982	12217.2	4843.7	5624.9	835.8	467.4	320.8	122.0	2.6	100.0	39.6	46.0	6.8	3.8	2.6	1.0	-
1983	14648.8	5660.2	6925.9	979.7	545.0	390.1	145.1	2.8	100.0	38.6	47.3	6.7	3.7	2.7	1.0	-
1984	16770.2	6210.1	7712.3	1271.3	576.6	416.2	179.3	4.6	100.0	37.0	46.0	7.6	3.4	4.9	1.1	-

* Excluding the claims of each on other financial institutions.

Table 12

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MARGINAL RATE OF FINANCIALISATION OF NATIONAL WEALTH
(Amounts in Millions of N. Rupees)

Year	Total Assets of Financial Institutions ^{1/}	Annual Change in Total Assets	Gross Domestic Product ^{2/}	MRF of National Wealth ^{3/}
1	2	3	4	5
1964/65	737.1	-	6272	-
1969/70	1662.5	254.5	9816	2.6
1974/75	4015.6	547.7	16571	3.3
1979/80	9017.7	954.5	23351	4.1
1983/84	16770.2	2121.4	38184	5.6
5-Year Averages				
1970-74	2438.3	412.0	11386	3.6
1975-79	5794.3	919.1	18638	4.9
1980-84	12531.0	1741.4	30546	5.7

^{1/} Sum of the total assets of eight financial institutions included in Table A.10, adjusted for the inter-institution net claims.

^{2/} Source: Central Bureau of Statistics.

^{3/} MRF = Marginal Rate of Financialisation, defined here as the percentage of column 3 to column 4.

Table 13

INCOME ELASTICITY OF ASSETS OF FINANCIAL INSTITUTIONS

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Period	<u>Annual Percentage Change in</u>		Income Elasticity (2:3)
	Total Assets of FIS*	GDP at Current Prices	
1	2	3	4
1965-70	17.66	9.37	1.88
1970-75	19.29	11.04	1.75
1975-80	17.56	7.10	2.47
1980-84	16.78	16.29	1.03
1965-75	18.47	10.20	1.81
1975-84	17.21	9.72	1.77
1965-84	17.87	9.97	1.79

* Outstanding amounts at mid-July adjusted for net inter-FI claims.

Table 14

FINANCIAL INTERMEDIATION RATIO (FIR)

Year	FIR 1/	Net Acquisition by FIs of Instruments Issued by NFEUs 2/	Gross Credit Extended by FIs 3/ To NF sector	Extended by To Govt.	Total Instruments Issued by NFEUs 4/	Consumption Credit Extended by FIs 5/	Change in Consumption Credit	Net Fixed Capital Formation in the Economy	
1	2	3	4	5	6	7	8	9	10
1973/74			1245.7	1051.1	184.6		823.1		
1974/75	52.0	760.0	2005.7	1671.2	334.5	1460.3	1313.4	490.3	970
1975/76	17.3	211.2	2216.9	1665.0	551.9	1220.3	1373.7	60.3	1160
1976/77	25.1	394.5	2611.4	1810.5	800.9	1570.1	1551.8	178.1	1392
1977/78	36.9	798.8	3410.2	2387.8	1022.4	2165.4	2081.2	529.4	1636
1978/79	24.8	665.4	4075.6	2877.8	1197.8	2687.3	2593.5	512.3	2175
1979/80	25.9	826.3	4901.9	3553.8	1348.1	3189.4	3182.9	589.4	2590
1980/81	25.2	940.9	5842.8	4474.7	1368.1	3740.7	3907.6	724.7	3016
1981/82	24.3	1018.1	6860.9	4682.5	2178.4	4188.5	4269.1	361.5	3827
1982/83	40.9	2622.7	9483.6	5268.1	4215.5	6412.7	5513.8	1244.7	5168
1983/84	24.4	1484.8	10968.4	5474.9	5493.5	6081.4	6430.2	916.4	5165

1/ FIR is defined here in percentage terms as the proportion of column 3 to column 7.

2/ As proxied by annual change in column 4.

3/ Outstanding as at the end of the fiscal year (Source: Appendix Table 1)

4/ Sum of cols. 9 and 10.

5/ Source: Appendix Table 2

Table 14.1

FINANCIAL INTERMEDIATION TO GOVERNMENT
(In Millions of N. Rupee)

Mid-July	Govt. Securities outstanding	Govt. Securities held by FIs	Other NRB		Total (3+4)	Gross credit of FIs	Ratios (in%)					
			Net Claims on Govt.	4			5	6	7	8	9	
1	2	3										
1965	-	12.8	-61.1	-48.3	166.8	-	-	-29.0				
1970	-	85.7	-242.5	-156.8	360.1	-	-	-43.5				
1973	359.4	293.6	-228.9	64.7	978.9	81.7	18.0	6.6				
1974	476.4	409.8	-225.2	184.6	1245.7	86.0	38.7	14.8				
1975	604.8	527.3	-192.8	334.5	2005.7	87.2	55.3	16.7				
1976	742.6	660.2	-108.3	551.9	2216.9	88.9	74.3	24.9				
1977	1013.8	916.1	-115.2	800.9	2611.4	90.4	79.0	30.7				
1978	1224.6	1126.9	-104.5	1022.4	3410.2	92.0	83.5	30.0				
1979	1395.2	1291.9	-94.1	1197.8	4075.6	92.6	85.9	29.4				
1980	1502.8	1402.0	-53.9	1348.1	4901.9	93.3	89.7	27.5				
1981	1443.8	1339.2	28.9	1368.1	5842.8	92.8	94.8	23.4				
1982	1900.0	1781.7	396.7	2178.4	6860.9	93.8	114.7	31.8				
1983	2878.1	2741.7	1473.8	4215.5	9483.6	95.3	146.5	44.5				
1984	4337.1	4069.2	1424.3	5493.5	10968.4	93.8	126.7	50.1				

See Appendix Table 3 for details.

Table 15

FINANCIAL INTERRELATIONS RATIO (FIR)

	Claims (Million N. Rupees)		Equities (Million N. Rupees)		GDP (Million N. Rupees)	FIR = TFI/GDP	
	Against Financial Institutions	Against non- Financial Institutions	Corporate Shares	Total Financial Instruments (TFI) (Claims + Equities) (Million N. Rupees)			
							Total
1965	508.9	722.9	1231.8	14.7	1246.5	6272	.20
1966	604.6	1022.4	1627.0	24.7	1651.7	7090	.23
1967	688.4	876.4	1564.8	24.7	1589.5	7650	.21
1968	774.1	1131.5	1905.6	25.1	1930.7	7174	.27
1969	910.8	1379.6	2290.4	25.3	2315.7	7986	.29
1970	1040.7	1657.3	2698.0	4.8	2702.8	9816	.28
1971	1209.1	1919.6	3128.7	5.6	3134.3	10006	.31
1972	1402.4	2241.8	3644.2	11.9	3656.1	11608	.31
1973	1677.5	2688.1	4365.6	14.1	4379.7	11160	.39
1974	2202.4	3068.4	5270.8	19.9	5290.7	14339	.37
1975	2616.2	3626.8	6243.0	28.0	6271.0	16571	.38
1976	2864.1	4196.7	7060.8	36.8	7097.6	17394	.41
1977	3780.0	4961.4	8741.4	41.5	8782.9	17280	.51
1978	4414.0	5664.3	10078.3	45.0	10123.3	19732	.51
1979	5173.7	7008.6	12182.3	47.0	12229.3	22215	.55
1980	6365.4	7812.0	14177.4	48.7	14226.1	23351	.61
1981	6929.6	8991.0	15920.6	48.9	15969.5	27307	.58
1982	8251.2	10710.9	18962.1	51.8	19013.9	30265	.63
1983	10743.0	12691.2	23434.2	52.7	23486.9	33621	.70
1984	12190.1	14089.7	26279.8	82.9	26362.7	38184	.69

Table 16

CLAIMS OF NON-FINANCIAL UNITS AGAINST FINANCIAL INSTITUTIONS
(Amounts in Million N Rupees)

Year	Non-Marketable Instruments															Percentage of market-able to Total	
	1	2	3	4	Comm.Bank (CB) Deposits2/					10	11	12	13	14	15		16
					Total	Demand	Saving	Time	Margin								
			Foreign Deposits at NRB	Other Deposits at NRB						Deposits at ADB/N Fund (total)	Provident Fund (PFC)	Insurance Premium at NTC	Foreign Currency Denominated Claims (NRB+CB+ADB+ NIDC) 3/	Sub-Total (3 through 5 and 10 through 13)	Total (Col. 2+14)	Total	
1965	296.2	-	-	63.6	115.3	78.8	10.9	25.6	-	-	18.0	-	15.8	212.7	508.9	58.2	
1966	345.7	-	-	100.0	113.5	70.3	15.2	28.0	-	0.4	23.9	-	21.1	258.9	604.6	57.2	
1967	368.6	-	-	91.1	170.7	101.8	19.1	40.4	9.4	1.9	31.0	-	25.1	319.8	688.4	53.5	
1968	419.1	-	-	85.6	200.4	106.3	26.1	59.2	8.8	3.3	38.7	-	27.0	355.0	774.1	54.1	
1969	470.1	-	-	103.3	257.6	131.2	37.8	78.6	10.0	4.6	49.7	-	25.5	440.7	910.8	51.6	
1970	531.4	-	-	89.5	317.6	145.9	52.9	103.0	15.8	5.4	68.8	-	28.0	509.3	1040.7	51.1	
1971	576.1	-	-	50.7	395.5	166.6	68.6	143.1	17.2	5.3	90.3	0.2	91.0	633.0	1209.1	47.6	
1972	601.2	-	-	67.4	531.3	192.1	88.5	229.3	21.4	4.8	112.0	0.6	85.1	801.2	1402.4	42.9	
1973	694.7	47.4	-	88.1	650.6	216.0	121.5	277.0	36.1	5.0	136.7	1.4	53.6	982.8	1677.5	41.4	
1974	878.6	48.0	-	112.2	865.4	282.6	157.5	364.3	61.0	6.3	166.0	3.0	122.9	1323.8	2202.4	39.9	
1975	916.5	49.6	-	80.8	1054.9	404.3	170.1	443.0	37.5	7.4	195.2	4.9	306.9	1699.7	2616.2	35.0	
1976	963.6	29.1	-	101.4	1413.9	486.3	197.1	660.4	70.1	9.3	237.4	8.0	101.4	1900.5	2864.1	33.6	
1977	1193.2	34.7	-	139.9	1925.9	661.6	268.5	918.0	77.8	51.4	318.7	14.2	102.0	2566.8	3780.0	31.6	
1978	1351.9	50.9	-	131.5	2274.7	652.9	360.7	1149.1	112.0	49.1	416.8	24.3	114.8	3062.1	4414.0	30.6	
1979	1615.2	71.5	-	164.0	2597.9	831.4	454.0	1222.5	90.0	40.7	527.1	33.1	124.2	3558.5	5173.7	31.2	
1980	1799.3	68.6	-	253.3	2954.1	799.3	570.9	1493.8	90.1	37.0	666.8	45.4	540.9	4566.1	6365.1	28.3	
1981	2065.7	61.0	-	210.8	3526.0	960.3	716.3	1670.8	178.6	33.0	820.4	55.3	157.4	4863.9	6929.8	29.8	
1982	2436.7	50.4	-	225.0	4123.3	942.0	876.6	2098.6	206.1	37.0	1048.5	73.5	256.8	5814.5	8251.2	29.5	
1983	2752.0	59.5	-	343.8	5319.0	1262.8	1067.9	2567.4	420.9	35.2	1303.7	98.5	831.3	7991.0	10743.0	25.6	
1984	3273.4	65.3	-	325.1	6045.2	1395.8	1329.4	3016.3	313.7	37.9	1580.9	125.6g/	736.7	8916.7	12190.1	26.9	

1/ Currency outside FIs & Govt.

2/ Includes foreign deposits.

3/ Excluding foreign deposits.

g/ Estimated.

Table 17

CLAIMS OF FINANCIAL INSTITUTIONS AGAINST NON-FINANCIAL UNITS
(In Millions of N. Rupees)

Mid-July	Non-Marketable Instruments														
	Marketable Instruments					Non-Marketable Instruments									
	Govt. Securities	Govt. Securities	Govt. Securities	Govt. Securities	Govt. Securities	Foreign Currency Denominated Claims 1/	Govt. Securities at NR8 2/	Govt. Securities at PFC 2/	Other Credit to Govt. Sector 3/	Loans to Private	Foreign Currency Denominated Claims	Total 7-11	Total of Marketable & Non-Marketable Claims (2 & 12)	Percentage of Marketable to Total	Equities
	1	2	3	4	5	6	7	8	9	10	11	12	13	14	15
1965	451.6	4.1		447.5	429.3	18.2	-	2.7	69.9	196.7	2.0	271.3	722.9	62.5	14.7
1966	565.7	5.1		560.6	556.4	4.2	-	7.3	82.2	580.0	6.8	456.3	1022.0	55.4	24.7
1967	407.7	6.0		401.7	375.3	26.4	-	1.7	85.4	374.8	6.8	468.7	876.4	46.5	24.7
1968	658.5	6.9		651.6	615.6	36.0	-	4.0	67.0	393.0	9.0	473.0	1131.5	58.2	25.1
1969	895.1	13.8		881.3	780.7	100.6	-	3.1	67.0	389.8	24.6	484.5	1379.6	64.9	25.3
1970	1014.4	22.5		991.9	899.3	92.6	-	3.3	111.6	503.3	24.7	642.9	1657.3	61.2	4.8
1971	1137.4	41.0		1096.4	999.9	96.5	94.3	0.8	50.6	598.5	38.0	782.2	1919.6	59.3	5.6
1972	1271.0	88.6		1182.4	1063.9	118.5	127.3	0.1	7.7	779.7	56.0	970.8	2241.8	56.7	11.9
1973	1520.7	123.0		1397.7	1230.1	167.6	164.4	6.5	47.4	890.5	58.6	1167.4	2688.1	56.6	14.1
1974	1724.2	205.0		1519.2	1309.5	209.7	195.4	11.4	50.8	1031.6	55.0	1344.2	3068.4	56.2	19.9
1975	1646.7	293.3		1353.4	1114.6	238.8	221.8	12.3	53.8	1633.6	58.6	1980.1	3626.8	45.4	28.0
1976	2270.1	430.9		1839.2	1466.7	372.5	217.1	12.2	47.0	1618.1	31.5	1926.6	4196.7	54.1	36.8
1977	2900.3	696.8		2203.5	1780.1	423.4	208.3	11.3	52.7	1759.6	29.2	2061.1	4961.4	58.5	41.5
1978	3026.9	917.0		2109.9	1653.1	456.8	199.1	10.8	74.2	2333.4	19.9	2637.4	5664.3	53.4	45.0
1979	3820.2	1082.2		2738.0	2071.5	666.6	199.6	10.2	89.6	2821.4	67.6	3188.4	7008.6	54.5	47.0
1980	3931.8	1216.0		2715.8	2133.1	582.7	177.3	10.2	106.8	3495.7	90.2	3880.2	7812.0	50.3	48.7
1981	4203.2	1160.6		3042.6	2243.6	799.0	168.3	10.2	100.6	4416.4	92.3	4767.8	8991.0	46.7	48.9
1982	5422.5	1600.2		3822.3	2959.0	863.3	174.5	7.0	396.7	4618.3	91.9	5288.4	10710.9	50.6	51.8
1983	5686.1	2532.8		3153.3	2251.3	902.0	202.6	20.0	1478.1	5206.0	98.4	7005.1	12691.2	44.8	52.7
1984	6989.7	3872.1		3117.6	1910.2	1207.4	197.1	-	1424.3	5382.6	96.0	7100.0	14089.7	49.6	82.9

1/ Excluding SDR Holdings and IMF Reserve (Gold) Tranche in Monetary Authorities Accounts.

2/ Special bonds.

3/ Includes loans to public non-financial enterprises.

Table 18

STRUCTURE OF DEPOSITS, BY TYPE*
(Amount In Million N Rupees)

Mid-July	Demand		Savings		Time		Margin		Total	
	Amount	Percent	Amount	Percent	Amount	Percent	Amount	Percent	Amount	Percent
1970	151.6	41.6	52.9	14.5	143.9	39.5	15.8	4.3	364.2	100.0
1974	305.8	32.6	158.1	16.9	412.0	44.0	61.0	6.5	936.8	100.0
1975	438.6	37.6	172.7	14.8	517.4	44.4	37.5	3.2	1166.2	100.0
1976	524.8	32.8	198.0	12.4	807.7	50.5	70.1	4.4	1600.6	100.0
1977	725.1	34.0	269.2	12.6	1060.8	49.7	77.8	3.6	2132.9	100.0
1978	694.1	27.6	361.1	14.3	1350.5	53.6	112.0	4.4	2517.8	100.0
1979	880.0	30.3	454.5	15.7	1477.7	50.9	90.0	3.1	2902.2	100.0
1980	853.5	25.6	571.2	17.2	1814.9	54.5	90.1	2.7	3329.7	100.0
1981	1019.6	24.6	716.7	17.3	2228.3	53.8	178.6	4.3	4143.2	100.0
1982	1033.7	21.1	877.4	17.9	2789.8	56.9	206.1	4.2	4907.0	100.0
1983	1379.0	21.9	1068.7	17.0	8417.9	54.4	420.9	6.7	6286.5	100.0
1984	1507.1	21.3	1333.9	18.9	3912.3	55.4	313.7	4.4	7067.0	100.0
<u>Annual Percentage Growth</u>										
1970 - 1975	23.7		26.7		29.2		18.9		26.2	
1975 - 1980	14.2		27.0		28.5		19.2		23.3	
1980 - 1984	15.3		23.6		21.2		36.6		20.7	
1974 - 1984	17.3		23.8		25.2		17.8		22.4	
1970 - 1984	17.8		25.9		26.6		23.8		23.6	

* Including deposits denominated in foreign currency

Table 19

TERM STRUCTURE OF TIME DEPOSITS*
(In Millions of N. Rupees)

<u>Mid-July</u>	<u>3 Months</u>	<u>6 Months</u>	<u>1 Year</u>	<u>2 Years</u>	<u>Total</u>
1975					
Amount	42.3	19.3	111.2	344.6	517.4
% Distribution	8.2	3.7	21.5	66.6	100.0
1980					
Amount	5.8	47.4	341.4	1420.3	1814.9
% Distribution	0.3	2.6	18.8	78.3	100.0
1984					
Amount	5.4	54.1	744.4	3108.4	3912.3
% Distribution	0.1	1.4	19.0	79.5	100.0
<u>Percentage Growth</u>					
1975 - 1980	-32.8	19.7	25.2	-2.0	28.5
1980 - 1984	-1.8	14.1	21.5	21.6	21.2
1975 - 1984	-20.4	12.1	23.5	27.7	25.2

* Including foreign deposits

Table 20
EARNINGS FROM AND COSTS OF COMMERCIAL BANKS' OPERATIONS
(In Million of N. Rupees)

Fiscal Year	Deposits				Loans and Investments				External Interest earned				Discount & Commission		Total Amount (Interest) of Col.5 Expenses		Net earnings			
	Total	Amount	Interest Payments of deposit	percent	Total (6 through 9)	Private Govt. Sector]	Securities	Bills	External balances held abroad	Total	on Loans	investment	received	+ Discount	Percent of Col.5	Other Expenses	Other2/ Income	Account	Total Earning	Percent of Total Assets
1	2	3	4		5	6	7	8	9	10	11	12	13	14	15	16	17	18	19	20
1964/65	112.4	N.A.	N.A.		107.5	91.5	3.0	-	13.0	N.A.	N.A.	N.A.	N.A.	N.A.	N.A.	N.A.	N.A.	N.A.	N.A.	N.A.
1969/70	295.4	10.8	3.7		291.3	195.3	10.0	23.6	62.4	21.9	N.A.	N.A.	3.9	25.8	8.9	10.8	0.7	4.9	1.7	1.7
1972/73	613.3	28.7	4.7		571.5	398.2	65.8	20.4	86.1	45.0	N.A.	N.A.	7.4	52.4	9.2	19.0	2.1	6.8	1.1	1.2
1973/74	764.4	36.7	4.8		747.6	491.9	100.9	28.8	126.0	59.9	N.A.	N.A.	8.4	68.3	9.1	23.6	2.0	10.0	1.3	1.3
1974/75	936.9	65.0	6.9		1066.1	766.9	98.3	24.1	106.8	102.4	N.A.	N.A.	12.3	114.7	10.9	35.6	2.7	16.8	1.8	1.6
1975/76	1166.2	134.1	11.5		1515.7	1194.3	100.4	27.3	193.7	194.2	N.A.	N.A.	12.7	206.9	13.7	54.2	2.6	21.2	1.8	1.4
1976/77	1600.6	148.9	9.3		1616.8	1144.6	119.6	46.5	305.9	187.9	N.A.	N.A.	20.5	208.4	12.9	51.9	3.3	10.9	0.7	0.7
1977/78	2132.9	171.4	8.0		2035.3	1157.5	479.9	54.0	343.9	208.5	171.3	37.2	22.5	231.0	11.3	61.1	4.4	2.7	0.1	0.1
1978/79	2517.8	224.1	8.9		2424.2	1646.9	351.5	78.8	347.0	277.3	243.0	34.3	35.5	312.8	12.9	86.3	8.1	10.2	0.4	0.4
1979/80	2902.2	259.8	9.0		3020.4	2025.7	371.8	185.2	437.7	339.1	303.0	36.1	42.8	381.9	12.6	101.5	9.2	29.6	1.0	1.0
1980/81	3329.7	300.3	9.0		3530.7	2626.5	371.2	171.5	361.5	419.9	391.2	28.7	50.0e/	475.3	13.5	111.7	9.9*	31.0	0.9	0.9
1981/82	4143.2	373.0	9.0		4481.5	3441.2	324.8	162.0	553.5	528.7	494.0	34.7	68.0	596.7	13.3	57.6	10.6	50.7	1.2	1.1
1982/83	4907.0	474.4	9.7		4883.6	3469.9	641.8	111.6	660.3	579.0	514.6	64.4	106.4	685.4	14.0	76.3	19.5	40.3	0.8	0.8

Notes: Outstanding amounts are as at the beginning of the fiscal year.

1/ Including claims on government enterprises (both financial and non financial)

2/ Including discounts and commissions

g/ The data on components are not available.

Table 21

COMMERCIAL BANK CREDIT EXTENDED TO PRIORITY SECTORS
(In Millions of N. Rupees)

Mid-July	Total Deposits*	Credit Extended to				Required Disbursement+	Percentage of 6 to 2
		Agriculture	Industry	Services	Total		
1	2	3	4	5	6	7	8
1977	1530.5	18.8	19.9	31.7	70.4	107.1	4.6
1978	2055.1	60.5	31.9	35.5	127.9	143.9	7.0
1979	2405.8	55.6	44.9	35.3	135.8	168.4	5.6
1980	2902.2	61.4	53.1	47.5	162.0	203.2	5.6
1981	3329.7	67.3	60.4	38.4	166.1	233.1	5.0
1982	4143.2	57.1	57.2	41.7	156.0	290.0	2.8
1983	4907.0	74.0	81.0	19.4	174.4	490.7	3.6
1984	6286.5	119.5	138.6	31.0	289.1	628.7	4.6

* Total deposits excludes inter-bank deposits and margin deposits up to 1979, and excludes only inter-bank deposits thereafter. The deposits which serve as the base for required minimum credit to priority sectors are (as shown here) deposits at the preceding year's mid-July.

+ 7 per cent of total deposits (upto 1982)

+ 10 per cent of total deposits (1983 and 1984)

Table 22

INDICATORS OF FINANCIAL DEEPENING

F.Y.	M1	1/	M2	1/	M2/M1	M1/GDP 2/	M2/GDP 2/	Consumer Price Index 3/	M1/P	M2/P	M1/P to 4/	M2/P to Popn.
						(%)	(%)				Popn.	Popn.
1964/65	446.3		489.7		1.097	6.5	7.1	-	-	-	-	-
1969/70	763.3		959.5		1.257	7.5	9.2	61.3	1245.2	1565.2	184	231
1974/75	1337.7		2026.9		1.515	7.9	11.7	100.0	1337.7	2026.9	176	266
1979/80	2830.4		5195.2		1.836	11.4	20.6	128.7	2199.2	4036.6	255	469
1983/84	4931.5		10141.5		2.056	12.2	24.8	195.5	2522.5	5187.5	264	544
Growth Rate (%)												
1970/75	11.9		16.1		3.8			10.3	1.4	5.3	-0.9	2.9
1975/80	16.2		20.7		3.9			5.2	10.5	14.8	7.7	12.0
1980/84	14.9		18.2		2.9			11.0	3.5	6.5	0.9	3.8
1970/84	14.3		18.3		3.6			8.6	5.2	8.9	2.6	6.3

Note: End of period figures

1/ M1 = Currency + Demand Deposits; M2 = M1 + Time and Saving Deposits.

2/ M1 and M2 used here are averages of figures for the beginning and the end of fiscal year.

3/ National urban consumer price index, the only available aggregative price index (apart from GDP deflator).

4/ Per capita real money supply for the economically active population (aged 15 years and above).

Appendix Table 1

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GROSS CREDIT EXTENDED BY FINANCIAL INSTITUTIONS
(In millions of N. Rupees)

Mid-July	Private Non-financial*			Government	Others (Industrial Estate)	Gross Credit (4+5+6)	Per Cent of Govt. to Gross Credit
	Claims	Equity	Total				
1	2	3	4	5	6	7	8
1965	196.2	14.7	210.9	-48.3	4.2	166.8	-29.0
1970	503.3	4.8	508.1	-156.8	8.8	360.1	-43.5
1973	890.5	14.1	904.6	64.7	9.6	978.9	6.6
1974	1031.6	19.9	1051.5	184.6	9.6	1245.7	14.8
1975	1633.6	28.0	1661.6	334.5	9.6	2005.7	16.7
1976	1618.8	36.8	1655.6	551.9	9.4	2216.9	24.9
1977	1759.6	41.5	1801.1	800.9	9.4	2611.4	30.7
1978	2333.4	45.0	2378.4	1022.4	9.4	3410.2	30.0
1979	2821.4	47.0	2868.4	1197.8	9.4	4075.6	29.4
1980	3495.7	48.7	3544.4	1348.1	9.4	4901.9	27.5
1981	4416.4	48.9	4465.3	1368.1	9.4	5842.8	23.4
1982	4618.3	54.8	4673.1	2178.4	9.4	6860.9	31.8
1983	5206.0	52.7	5258.7	4215.5	9.4	9483.6	44.5
1984	5382.6	82.9	5465.5	5493.5	9.4	10968.4	50.1

* Includes credit to non-financial public enterprises

Appendix Table 2

CONSUMPTION CREDIT EXTENDED BY FINANCIAL INSTITUTIONS
(In Millions of N. Rupees)

Year	Total	Government1/ Total	P R I V A T E S E C T O R						Percentage Distribution	
			NRB2/ Total	CB3/ ADB	NIDC	PFE4/ NIC	CGC	Govt./ Total	Pvt./ Total	Total
1965	199.1	58.7	140.4	1.3	136.8	0.8	-	1.5	-	-
1970	469.7	208.2	261.5	2.7	247.1	5.9	-	5.8	-	-
1973	362.6	-111.5	474.1	3.5	434.7	25.2	-	10.7	-	-
1974	688.0	-61.3	749.3	7.3	668.1	60.8	-	13.1	-	-
1975	1197.1	17.5	1179.6	8.0	1036.3	118.7	-	16.6	-	-
1976	1298.7	138.6	1160.1	8.4	1011.0	121.0	-	19.7	-	-
1977	1483.1	251.7	1231.4	23.9	1027.8	156.1	-	23.6	-	-
1978	2018.7	346.5	1672.2	17.3	1434.5	191.8	-	28.4	0.2	-
1979	2537.0	422.6	2114.4	12.8	1834.4	232.5	-	34.3	0.4	-
1980	3150.3	506.3	2644.0	19.3	2325.3	255.8	-	43.2	0.4	-
1981	3921.8	562.0	3359.8	23.8	3010.7	269.7	-	55.0	0.6	-
1982	4501.4	1103.7	3397.7	4.7	2994.3	328.3	-	69.7	0.7	-
1983	6391.6	2564.0	3827.6	6.4	3323.7	408.9	-	87.4	1.2	-

1/ 40 per cent of all government securities held by financial institutions

2/ Internal bills purchased

3/ 85 per cent of total credit

4/ 25 per cent of total loans

Appendix Table 3

INVESTMENT/CONSUMPTION CREDIT OF FINANCIAL INSTITUTIONS TO GOVERNMENT
(In Millions of N. Rupees)

Mid-July	Investment in Government Securities ^{1/}							Total	Investment Credit to Government ^{2/}	Consumption Credit to Government ^{3/}	Adjusted Consumption Credit to Government ^{4/}	
	Commercial Banks			ADB/N	NIDC	PFC	NIC					CGC
	NRB	3	4									
1	2	3	4	5	6	7	8	9	10	11	12	
1965	6.0	3.3	0.8	-	2.7	-	-	12.8	7.7	5.1	58.7	
1970	59.9	17.9	2.0	-	3.3	2.6	-	85.7	51.4	34.3	208.2	
1973	170.2	100.9	2.0	-	11.4	9.1	-	293.6	176.2	117.4	-111.5	
1974	266.8	98.3	16.4	-	15.4	12.9	-	409.8	245.9	163.9	-61.3	
1975	378.0	100.4	16.4	2.3	16.3	12.9	1.0	527.3	316.4	210.9	18.1	
1976	486.5	119.6	16.3	2.3	16.2	16.6	2.7	660.2	396.1	264.1	155.8	
1977	385.1	479.9	13.3	2.4	15.3	17.4	2.7	916.1	549.7	366.4	251.2	
1978	718.5	351.5	13.3	3.1	14.8	23.0	2.7	1126.9	676.1	450.8	346.3	
1979	851.6	371.8	13.3	2.4	14.3	35.8	2.7	1291.9	775.2	516.8	422.7	
1980	941.0	371.2	13.8	2.4	14.3	55.8	2.7	1402.0	841.2	560.8	506.9	
1981	909.0	324.8	13.3	2.4	14.3	74.4	1.0	1339.2	803.5	535.7	564.6	
1982	1023.0	641.8	13.3	2.4	11.1	89.1	1.0	1781.7	1069.0	712.7	1109.4	
1983	1454.8	1161.0	13.3	2.9	6.1	102.6	1.0	2741.7	1645.0	1096.7	2570.5	
1984	2121.5	1482.9	8.3	25.6	300.0	130.9	-	4069.2	2441.5	1627.7	3052.0	

1/ As shown in the balance sheet of financial institutions

2/ 60 per cent of col. 9: the government-presumed proportion of development expenditure going to investments

3/ Col. 9 minus 10

4/ Total credit to government as per Table 14.1 minus col. 10 of this table

Appendix Table 4

MONETARY POLICY INSTRUMENTS OF NEPAL RASTRA BANK

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	<u>1965-69</u>	<u>1970-74</u>	<u>1975-79</u>	<u>1980-84</u>
1. <u>Interest Rate for Commercial Banks</u> (Period Averages)				
1.1 Interest Rate on Deposits:				
Savings	2.5	5.2	8.0	8.3
Fixed:				
3-months	-	4.6	4.0	4.3
6-months	-	3.9	9.4	9.3
1-year	3.5	7.6	13.0	12.3
2-years (and above)	4.5	8.5	14.0	13.3
1.2 Interest Rate on loans (Period Averages)				
Export Bills	7.6	7.5	12.6	12.9
Gold and Silver	8.5	10.0	16.5	16.6
Agriculture	-	2.0	3.0	7.5
Industry	-	2.0	11.4	12.3
Trade	8.5	9.8	16.6	16.8
Services	-	-	-	1.5
Overdue (any loan)	-	-	-	-
Others (Import Bills & L.C.)	8.0	11.0	16.5	16.6
2. <u>Refinance Rates</u> (Period Averages)				
Export Bills	-	5.6	11.6	11.9
Agriculture	-	6.0	8.2	7.9
Industry	5.0	6.0	9.4	10.3
Services	-	-	9.6	11.4
Development Bonds	7.8	6.0	14.2	14.2
Others	5.0	5.3	2.0	2.3
3. <u>Cash Reserve and Liquidity</u>				
Cash Reserve Ratio (Per cent of deposits)	-	8 <u>e</u> /	7 <u>e</u> /	9 <u>e</u> /
Liquidity Ratio (Per cent of deposits)	-	32 <u>e</u> /	-	25 <u>e</u> /
4. <u>Credit Ceiling</u>	-	-	1927.0 <u>e</u> /	-
5. <u>Sectoral Lending Requirements</u>				
Priority Sector	-	5	7	10

e/ - End of the period

Appendix Table 5

FACTORS AFFECTING MONETARY BASE
(In Millions of N. Rupees)

Mid-July	Monetary Base					Claims on					Ratios to Monetary Base (in per cent)				
	Total	Currency outside Banks	Commercial Bank Reserve	Net Foreign Assets	Net Claims on Govt.	Non-Bank Financial Institutions	Claims on Banks	Net Other Liabilities	NFA	NCG	CFI	CB	Currency	Reserve	
1	2	3	4	5	6	7	8	9	10	11	12	13	14	15	
1957	79.0	67.7	11.3	51.4	14.5	-	-	-13.1	65.1	18.4	-	-	85.7	14.3	
1965	319.0	296.2	22.8	431.3	-55.1	1.4	3.0	61.6	135.2	-17.3	0.4	0.9	92.9	7.2	
1970	617.7	531.4	86.3	924.4	-182.6	11.8	21.0	156.9	149.7	-29.6	1.9	3.4	86.0	14.0	
1971	649.6	576.1	73.5	985.0	-148.3	18.9	10.8	216.8	151.6	-22.8	2.9	1.7	88.7	11.3	
1972	673.0	601.2	71.8	1082.3	-141.4	34.4	1.3	303.6	160.8	-21.0	5.1	0.2	89.3	10.7	
1973	797.5	694.7	92.8	1233.8	-58.7	53.8	7.3	438.7	154.7	-7.4	6.7	0.9	87.1	11.6	
1974	1005.0	878.6	126.4	1265.2	41.6	43.7	151.0	496.5	125.9	4.1	4.4	15.0	87.4	12.6	
1975	1098.1	916.5	181.6	897.9	185.2	134.7	368.9	488.6	81.8	16.9	12.3	33.6	83.5	16.5	
1976	1177.1	963.6	213.5	1345.6	360.2	113.1	24.1	665.9	114.3	30.6	9.6	2.1	81.9	18.1	
1977	1454.9	1193.2	261.7	1698.3	259.9	175.2	55.4	743.9	116.7	18.6	12.0	3.8	82.0	18.0	
1978	1718.2	1351.9	368.3	1565.1	614.0	254.4	174.1	889.4	91.1	35.7	14.8	10.1	78.7	21.3	
1979	1953.3	1615.2	338.1	1793.8	757.5	349.1	168.9	1116.0	91.8	38.8	17.9	8.7	82.7	17.3	
1980	2215.3	1799.3	416.0	1746.7	887.1	367.1	264.4	1050.0	78.9	40.0	16.6	11.9	81.2	18.8	
1981	2495.4	2065.7	429.7	1736.1	937.9	393.7	468.1	1040.4	69.6	37.6	15.8	18.8	82.8	17.2	
1982	3150.6	2436.7	713.9	2390.9	1419.7	444.8	137.8	1242.6	75.9	45.1	14.1	4.4	77.3	22.7	
1983	3668.8	2752.0	916.8	1901.4	2928.6	484.1	74.0	1719.3	51.8	79.8	13.2	2.0	75.0	25.0	
1984	4299.0	3273.4	1025.6	1542.7	3545.8	571.4	152.1	1513.0	35.9	82.5	13.5	3.5	76.1	23.9	

MONEY MULTIPLIER

<u>Mid-July</u>	<u>Money Supply (Rs. Million)</u>	<u>Monetary Base (Rs. Million)</u>	<u>Money Multiplier</u>	<u>Broad Money (Rs. Million)</u>	<u>Multiplier for Broad Money</u>
1966	521.5	362.5	1.439	570.7	1.574
1970	763.3	617.7	1.236	959.5	1.553
1975	1337.7	1098.1	1.218	2026.9	1.846
1980	2830.4	2215.3	1.278	5195.2	2.345
1983	4348.9	3668.8	1.185	8801.5	2.399
1984	4931.5	4299.0	1.147	10141.5	2.359
<u>5-Year Average</u>					
1966-70			1.348		1.569
1971-75			1.252		1.805
1976-80			1.253		2.197
1981-84 (4 years)			1.191		2.379

Appendix Table 7

MONETARY SURVEY
(Million N. Rupees)

Years Mid-July	Foreign Assets Net	Domestic Credit	Claims on Govt. Net	Claims on		Time Deposits	Margin Deposits	Capital & Other Items, Net	Money Supply
				Financial Institutions	Private Sector				
1960	171.9	28.4	-3.9	-	32.3	26.5	-	-0.3	174.1
1965	449.5	73.1	-51.7	1.4	123.4	43.4	-	32.9	446.3
1966	367.4	169.3	-24.2	4.5	189.0	49.2	-	-34.0	521.5
1967	408.5	180.0	5.8	3.8	170.4	73.1	9.4	-52.9	568.3
1968	660.6	140.3	-88.9	9.8	219.4	108.3	8.8	73.8	618.8
1969	894.3	32.2	-201.6	13.7	220.1	156.8	10.0	69.3	700.4
1970	1007.2	96.8	-201.2	18.6	279.4	212.0	15.8	128.7	763.3
1971	1047.6	212.8	-145.3	20.8	337.3	278.7	17.2	188.3	793.4
1972	1179.1	361.8	-80.3	41.0	401.1	404.1	21.4	279.1	857.7
1973	1383.0	597.3	42.2	63.1	492.0	513.4	36.1	451.1	1015.8
1974	1451.5	970.2	139.9	48.7	781.6	629.9	61.0	510.7	1281.1
1975	1029.1	1637.8	285.7	137.1	1215.0	726.7	37.5	602.5	1337.7
1976	1575.0	1763.3	479.8	115.0	1168.5	1071.5	70.1	814.3	1452.5
1977	1875.2	2125.0	749.8	177.5	1197.7	1370.1	77.8	777.2	1852.9
1978	1783.3	2905.3	965.5	292.4	1647.4	1711.5	112.0	916.5	2060.6
1979	2286.0	3540.8	1129.3	401.9	2009.6	2006.5	90.0	1317.4	2504.9
1980	2231.9	4305.8	1258.3	429.4	2618.1	2454.9	90.1	1252.4	2830.4
1981	2414.5	5161.4	1262.7	454.2	3444.5	3099.9	178.6	1268.2	3207.8
1982	3097.4	6043.1	2061.5	503.6	3478.0	3846.5	206.1	1682.5	3611.5
1983	2611.4	8490.9	4089.6	565.3	3836.0	4873.5	420.9	1879.9	4348.9
1984	2539.8	9824.5	5028.7	668.4	4127.4	5523.7	313.7	1909.1	4931.5

THE FINANCIAL STRUCTURE AND ITS IMPLICATIONS FOR MONETARY POLICY IN THE PHILIPPINES

by

Anita E. Sison

I. INTRODUCTION

The financial system is increasingly viewed in line with the country's development goals. One particular aspect of the system which is being emphasised is its function of financial intermediation. It is generally recognised that a relationship exists between the level of income of a country, on the one hand, and the level of development and differentiation of its financial system, on the other. To what extent the financial system grows as the economy develops depends partly on how far it is relied upon in mobilising financial resources for the economy. It seems that the simultaneous growth of the financial system together with the development of the economy is almost inevitable. This is due to the increasing monetisation of the economy, a growing differentiation between savers and investors, the varying demands of the savers requiring more diversified asset portfolios and the greater tendency towards functional specialisation among financial institutions themselves to enjoy the benefits of economies of scale.

One of the usual indicators of the development of the financial structure relative to the economy is the uptrend of the ratio of total assets of the financial institutions to Gross Domestic Product (GDP). For the Philippines, there has been a historical increase in the percentage of total assets of the organised financial sector to GDP: from 37 per cent in 1950, 74 per cent in 1970, 144 per cent in 1980 and 245 per cent in June 1984.

The role of the financial system in the Philippines is very important when viewed within the framework of the general objectives of the country's development plan, namely, a maximum growth rate possible, consistent with satisfactory price level changes, balance of payments objective, equitable income distribution and a decrease in the rate of unemployment and underemployment. The system is expected to attract savings more efficiently, to help improve the allocation of resources and to effect payments among various economic agents with minimum friction. Given these demands, a satisfactory government policy framework is deemed a necessary ingredient to enable the financial system to function effectively and thus contribute to economic welfare.

Purpose and Scope of the Study

This study aims to analyse the financial structure of the Philippines and its implications on the formulation and implementation of monetary policy from 1950 to 1984.

The financial system in the Philippines can be broadly divided into the organised and the unorganised sectors. The organised sector can further be sub-divided into the banking and non-banking institutions. The banking institutions are the Central Bank, commercial banks, savings and mortgage banks, rural banks, development banks, stock savings and loan associations and specialised government banks. Non-bank financial institutions include investment houses, investment companies, finance companies, fund managers, lending investors, securities dealers/brokers, insurance companies, pawnshops, non-stock savings and loan associations, mutual building and loan associations, venture capital corporations and cooperatives/credit unions. Little is known about the unorganised sector. Because of the lack of information on the unorganised sector, this study on the Philippine financial system will be limited to the operations and activities of the organised sector.

The method adopted in the study is analytical description of quantitative data. The overall balance sheet of the financial system was examined, not only at some points in time but over a period of time, as it contains important macro-economic variables. Considerable emphasis is laid on the component units or individual balance sheet statements of different types of financial institutions. Pitted with one another and with other variables, they can provide a meaningful framework or starting point in analysing the development of the financial system and in suggesting certain lines of policy action.

The difficulty encountered in the collection of data, particularly on financial operations of non-banking institutions prior to 1973, deserves mention. The paucity of information on the volume of equity securities and credit granted and outstanding of all types of non-bank financial institutions, classified by purpose, has rendered the consolidation of data on total credit of the financial system difficult.

Likewise, due to the dearth of accurate information on the stock of financial instruments, the empirical analysis on the nature and role of these variables are circumscribed within the various deficiencies of the data itself.

The study is divided into four sections. The first section consists of the introductory portion which contains the overview, the objective of the study, scope and methodology of research. A brief historical sketch of the Philippine financial system is also incorporated, together with the discussion of the growth and development of the existing financial system in terms of assets and number of financial institutions, and the major developments which affected the character of the financial structure.

An analysis of the country's financial structure is presented in Section II. The section starts with a descriptive analysis of each financial institution together with a discussion of

the degree of concentration among financial institutions and the competitiveness of each type of financial institution. Also in Section II, an attempt to evaluate the degree of development of the country's financial structure is made. This evaluation is done with the aid of some ratios/indicators of financial deepening like the marginal rate of financialisation of national wealth, the overall financial intermediation ratio and financial intermediation to the government sector. Attention is also focussed on the various types of instruments used from time to time, including the classification of financial instruments according to type of issue, as to marketability and currency denomination. Analysis of trends in the shares of each type of financial instrument to total instruments outstanding and other indicators is also included to give readers an understanding of the structure of financial instruments.

Section III is concerned with major Central Bank policies which contributed to the growth of the financial system. Specifically, the effectiveness of these policies in increasing financial intermediation, among others, is discussed. Section IV contains the summary and conclusion.

Nonetheless, this study is not complete. Future studies could include a survey of the stock and new issues of financial instruments by type of financial institutions many years back, a study of the country's capital market development, and more in-depth analysis on the effectiveness of monetary policy via the construction of empirical models examining the impact of monetary policy on intermediation and output growth and economic development.

Historical Perspective of the Financial System

The Philippine financial system has evolved gradually over a span of more than four centuries, starting with the establishment of the first organised credit institution, the "Obras Pias", to a

multifaceted system which supplies funds to almost every sector of the economy.

Organised during the Spanish Colonial era in 1554, the Obras Pias was a religious foundation whose resources were channelled into trade financing which in those days meant financing the country's galleon trade with Acapulco, Mexico. With the termination of this trade in 1620, the death of the Obras Pias soon followed.

Formal banking system was established in 1851 with the opening of the first commercial bank, the Banco Espanol Filipino de Isabel II, now the Bank of the Philippine Islands. The country's first savings bank started operations in 1882. Further, the expansion of the Filipino-European trade attracted two foreign banks to put up branches in the country. These were the Chartered Bank of India, Australia and China (now the Chartered Bank) and The Hongkong and Shanghai Banking Corporation. ^{1/} Thus, at the end of the Spanish era in 1898, four banks with resources of about P40 million were operating in the country.

The American and Commonwealth periods saw the opening of more banks. Said periods also ushered in increased government participation in the development of banking. This participation partly took the form of establishment of various types of financial institutions: the Philippine Postal Savings Bank in 1906; the Agricultural Bank in 1908; the Philippine National Bank in 1916 and the Agricultural and Industrial Bank in 1939. Government participation also took the form of greater supervision and regulation of banking institutions. In 1929, Act No. 52 which provided for the regular examination and inspection of banks was passed by the first Philippine

^{1/} Bankers Association of the Philippines. Banking in the Philippines, 1957. Part of the materials in the following paragraphs is based on this monograph.

Commission. In the same year, the Bureau of Banking was created and in it was transferred the power of supervision which was formerly vested in the Insular Treasury.

Meanwhile, other important segments of the financial system were established: the first stock exchange, the Manila Stock Exchange, in August 2, 1927 and the Manila Clearing House in 1930.

Thus, just before World War II, there were 17 banks in operation, 22 provincial branches, 54 provincial agencies and 1,000 sub-agencies. Of the 17, two were government-owned, seven were domestic banks and trust companies, two were savings and mortgage banks and six were branches of foreign banks. This growth in the units of banking institutions can be paralleled by the increase in their assets. For instance, the total assets of the commercial banks amounted to P0.06 billion in 1913, P0.26 billion in 1929 and P0.39 billion in 1939.

The financial system grew into a sizable sector after the Second World War. In 1946, the Rehabilitation Finance Corporation (RFC) was organised to provide financial aid in rehabilitating the country and to help in broadening and diversifying the Philippine's economic structure. This institution later evolved into a much larger and expanded development banking institution, the Development Bank of the Philippines (DBP).

In 1948, the General Banking Act was passed which contained the first major rules and regulations governing banks' operations, particularly those affecting commercial and savings banks. Moreover, the establishment of the Central Bank in 1949 defined the framework for monetary policy formulation and the role of the financial system in the economic system as a whole.

Expansion of the Existing Financial System

Following the opening of the Central Bank and the establishment of a new monetary system, structural changes occurred in the financial system, notably the growth of non-bank financial institutions, the rise of special credit institutions, the development of the money market and the opening of three more stock exchanges (Makati Stock Exchange, Metropolitan Stock Exchange and Cebu Stock Exchange), the licensing of foreign banks to operate in the offshore banking system in 1970, the granting of authority to domestic banks to accept foreign currency deposit and the establishment of the Philippine Deposit Insurance Corporation.

The growth and development of the organised financial sector is shown in Tables 1 and 2. There are two discernible trends from the tables, namely: increases in both the types of financial institutions and in the number of branches for most of these institutions. Despite the growth in other types of financial institutions like the non-bank financial intermediaries, the banking sector, particularly commercial banks, predominated. The number of head offices of commercial banks rose from 12 in 1950 to 22 in 1960, 40 in 1970 and 34 as of June 1984. Likewise, the branches and agencies grew from 95 units in 1950 to 137, 603 and 1,849 for the corresponding years. Commercial banks' resources comprised more than 40 per cent of the financial system's assets throughout the period.

Rural banks started with 18 in 1953; the units rose rapidly to 160 in 1960, 820 in 1967 and 1,158 as of June 1984. Rural banks, by virtue of the amended Republic Act (R.A.) 720, were established to provide financing for rural industries, farmers and merchants. From 1960 to 1984, their aggregate resources has grown by almost P9 billion.

Development banks have registered a more modest growth performance as compared with rural banks. The Development Bank of the

Philippines (DBP) increased its branches from three in 1950 to 26 in 1970 and 66 in 1984. In addition to the government-owned DBP, whose resources comprised about one-tenth of the system's assets in 1984, the Private Development Act of 1957 authorised the establishment of a system of private development banks to promote agriculture and industry and at the same time, place within easy reach of the people medium and long-term credit facilities at reasonable cost. Although the number of private development banks have grown steadily, their total assets comprised only 1.2 per cent of the system's resources in 1984.

Savings and mortgage banks were organised primarily to accumulate the small savings of depositors, investing them, together with their capital, in bonds or in loans secured by bonds, real estate mortgages and other forms of security. As of 1984, there were 210 savings and mortgage banks units with aggregate resources of P7.7 billion.

Savings and loans associations were placed under Central Bank supervision in 1963 to promote their development as home financing institutions. There were 74 non-stock and 267 stock savings and loan associations as of June 1984 as against 65 and 28, respectively, in 1970.

Non-bank financial institutions have likewise grown. In terms of assets, insurance companies including two government-owned companies, were the dominant non-bank institutions although the number of insurance companies have not substantially increased over the years.

The most dynamic non-bank financial institutions, however, are the investment institutions, particularly investment houses and investment companies, which not only assisted in the promotion and financing of new ventures but also had a hand in the development of the capital market and the money market in the early 1960s.

Finance companies which were established in the country in the mid-1950s also proliferated. As of June 1984, there were 541 finance companies with total assets amounting to P10.5 billion, as against only 164 companies and P3.5 billion resources in 1975.

The growth for some non-bank financial institutions has, however, been uneven. Mutual buildings and loan associations, which are private, mutually owned stock companies that specialise in extending ten-year mortgage loans to their members, started in 1904. However, their number did not expand beyond seven and their resources have declined steadily during the period.

Pawnbrokers whose business is to grant loans to the general public on pledge of personal properties, numbered 370 in 1973 and 908 in 1984 and their total assets aggregated P89.6 million in 1975 and P18.6 million in 1984.

Other types of non-bank institutions like the security dealers/brokers and fund managers were established and contributed to increased financial intermediation in the country.

The Money Market

The money market in the country can be regarded to have been born only in the 1960s. The interbank call market started in 1961, the inter-company sub-market in 1965, and the Treasury bills sub-market in 1966. Commercial paper appeared in 1967 and deposit substitutes, in 1969. Of late, the money market is still fragmented but greater integration among the sub-markets has been achieved.

The interbank call sub-market consists of tradings of overnight call funds among commercial banks for the purpose of adjusting their reserve positions with the Central Bank. In general, the volume of interbank trading among commercial banks appears to be a direct function of the monetary policy of the Central Bank, decreasing

or increasing with monetary tightness or ease. The volume of call loans in 1984 totalled P506 billion compared to only P134 million in 1963.

The Bancom Development Corporation, an investment house, organised the first intercompany market in 1965 when it introduced its own promissory notes (Bancom bills) of borrowing and lending. Commercial paper, on the other hand, was first introduced in 1967 when the acceptance and unsecured promissory notes of two oil companies, respectively, were traded in the market.

In 1969, banks began to offer trust certificates, bills of exchange, certificates of assignments, bankers acceptances, repurchase agreements and bank promissory notes (all included under the concept of deposit substitutes) at interest rates higher than the deposit rates. Commercial banks have played an important role in deposit substitutes operations as shown by the increase of their share to total liabilities, from 54 per cent in 1973 to 69 per cent in 1984.

The money market became a large source of funds for commercial banks in the years 1974-1975 when deposit substitutes increased to the equivalent of about 80 per cent of total savings and time deposits. This was before the imposition of policy measures whose objectives were to reduce and stabilise volatile fluctuations in money market rates. Monetary policies which allowed higher interest rates on deposits, imposed interest rate ceilings on deposit substitutes, increased reserve requirements for deposit substitutes and placed minimum lot requirements for money market operations, together with fiscal imposition of a transaction tax of 35 per cent on money market operations, were quite effective in arresting higher growth rates of deposit substitutes, and moderating fluctuations in the money market rates in the late 1970s.

Government securities sub-market. In 1966, an important segment of the money market came into being and this is the government securities sub-market. The government has pursued the development of this sub-market so that it can tap less inflationary sources in financing its expenditures and also to increase the effectiveness of open market operations as a tool for monetary stability in the economy.

The National Government has issued several types of government securities ranging from short-term Treasury bills and Treasury notes to long-term bonds as early as 1949. However, there was not much success achieved in the attempt to develop an active government securities market due to the relatively low interest rates of these bonds (ranging from four per cent and below) compared with other financial instruments. For a long time, participation in this sub-market (except for Treasury bills and the Central Bank Certificates of Indebtedness) was confined to commercial banks which purchased them on account of their eligibility to serve as legal reserves. Today, with the introduction of securities bearing more competitive yields and a wider choice of maturities, there is an expanding network of investors in government securities.

Treasury bills. The Treasury bills are considered the most actively traded money market instruments in the country today. They are direct and short-term obligations of the National Government. Initially sold on an auctioned basis, trading is currently conducted on a negotiated basis. The major holders of these bills are commercial banks, investment houses, insurance companies and corporate investors.

Although the Treasury bill had its first appearance as early as 1949, its character has been much altered in the sense that the volume, rates, and market interplay were given much emphasis after 1966 when a redesigned Treasury bill programme was launched.

To provide an active secondary market for these bills and to realign the Treasury bill programme to the forces of a free market mechanism, the National Association of Government Securities Dealers (NAGSD) was formed in 1967. The Central Bank gave tremendous support to the market through its repurchase agreements with the NAGSD members and Treasury bill dealers to provide their financing needs. This explained the widespread demand for Treasury bills as instruments of liquidity.

Central Bank Certificates of Indebtedness (CBCIs). In 1970, the Central Bank issued its own certificate of indebtedness (CBCI) as a supplement to the available range of government securities. Originally, the CBCIs were issued to mop up the then excess liquidity in the urban centres for reallocation to the rural sectors. The basic features of the CBCIs originally included: maturity of three years, interest rates of 9 per cent payable semi-annually, and added "sweeteners" such as the tax prepaid feature, the reserve-eligible feature, and its use as an alternative investment outlet by banking institutions in fulfillment of the requirement to set aside at least 25 per cent of their loanable funds for agricultural loans.

The redesigned issues of CBCIs sans "sweeteners" but more market-oriented as to interest rate and maturity period, have continued to be attractive and competitive against other government securities. Since its introduction in 1970, the CBCI has grown in stature as an actively traded security and has been used by the Bank as a "fine tuner" in highly volatile market conditions.

The Capital Market

The origin of the capital market can be traced to the establishment of the Manila Stock Exchange in 1927. After more than three decades, three more exchanges were opened, two in the Metro Manila area and one in Cebu province.

Over the years, volume of transactions in the three active stock exchanges in Metro Manila have expanded significantly. However, the concentration of trading volume was on the side of speculative stocks, particularly oil and minerals, which prejudices market growth of the industrial sector.

Prior to the Seventies, debt management in the Philippines and some monetary policies did not encourage the development of the stock and bond market. In the first place, government debt management was not conducive to the expansion of the securities market since long-term government securities were mostly of the non-competitive or non-marketable type. At the same time, the low loan rates obtained from banks made loan financing more attractive than equity financing.

Efforts to assist in the development of the capital market were undertaken by the government in the '70s, with the introduction of such debt instruments like Treasury bills and CBCIs whose maturities could be lengthened to form the base of the capital market. Of late, these instruments are the only government securities which are actively traded in the capital market. On the other hand, the supply of private sector corporate securities is minimal, most of which is privately placed.

Offshore Banking Units and Foreign Currency Deposit Units

In 1970, local commercial banks were authorised to accept foreign currency deposits with the purpose of developing offshore banking activities in the country. Six years later, licenses were also granted to foreign banks to operate offshore banking units (OBUs) and to conduct banking activities in foreign currencies. This was in pursuance to Presidential Decree No. 1034 dated September 1976, whose basic objectives are to facilitate the flow of desired investments in the Philippines, create employment opportunities and expertise in international finance and contribute to the national development

effort, and to develop another financial centre in Asia. A significant incentive to encourage foreign banks to set up OBUs is their exemption from all forms of local licenses, fees, dues or other taxes. The FCDU banks were also granted the same tax privileges starting 1976.

The existence of OBUs and FCDUs not only gave the financial system a vital link to the international financial market but also made available major foreign currencies needed for external transactions. As of June 1984, there were 28 OBUs with total resources amounting \$4.2 billion. The FCDUs have expanded rapidly also, with total resources growing from \$1,209 million in 1977 to \$6.8 billion in June 1984.

Major Developments Affecting the Nature and Character of the Existing Financial System

With almost all financial institutions already organised in the 1960s, the next two decades served as the period for reforms in the internal structure of financial institutions. Further, with the economic system becoming more complex and the population growing at a fast rate, the system underwent major transformation in its foundation and organisational orientation in order to effectively meet the challenges of the coming years.

Banking reforms of 1972. The first of these major changes came about in 1972. In the said year, the General Banking Act of 1949 was amended almost entirely, including the redefinition of basic banking terms, reclassification of financial intermediaries into banks and non-banks and their expanded functions as well as guidelines on their operations. The policy of establishing few but big banks was also put into effect through the capitalisation build-up requirement

for all banks. This capitalisation build-up programme also allowed the equity participation of foreign entities in domestic banks up to the extent of 30-40 per cent.

Likewise, rules and regulations as well as guidelines on branch banking were strictly enforced. The policy of encouraging the establishment of banks' branches in underbanked and rural areas was aimed at diffusing banking and financial services over a wide range to facilitate and speed up the transmission of monetary policy as well as to broaden the scope of the organised financial sector.

The most significant measure undertaken at this time was the amendment of the Central Bank Charter in order to expand the scope of central bank regulatory and supervisory authority to cover not only banks but non-banks as well. This was basically aimed at enhancing the effectiveness of monetary policy. In line with this purpose, the main objective of central banking was redefined and limited to maintaining monetary stability, while the responsibility of promoting economic growth and development, which used to be another central bank objective, was transferred to a national planning body created for this purpose.

Financial reforms of the 1980s. Further implementation of monetary and financial reforms was undertaken in the early 1980s. Foremost among these reforms was the orientation of the Philippine financial system towards the universal banking concept. Under the Philippine concept, the pure form of universal banking was not adopted; instead, the major categories of financial institutions were maintained. As long as the prescribed requirements (such as higher minimum paid-up capital of P500 million, among others) were met, existing banks and non-banks may emerge or graduate into higher category institutions including those providing varied and allied services, that is, authorised to engage in "expanded commercial banking". The latter phrase is the preferred term for modified universal banking in the Philippines.

To date, the Central Bank of the Philippines has authorised the operation of nine universal banks. A number of consolidation and mergers among banks and non-banks took place after April 1980 and the resulting institutions may also be expected to join the number of universal banks in the future.

II. ANALYSIS OF THE PHILIPPINE FINANCIAL STRUCTURE

Financial institutions and instruments are the main variables in analysing the financial structure of a country. The economic significance of the financial structure in the Philippines can not be assessed without exploring the important features of its financial institutions and instruments.

FINANCIAL INSTITUTIONS

The Philippine financial system can be divided into two: the monetary and non-monetary as shown in Chart 1.

The monetary system consists of money generating institutions, the monetary authorities and the deposit money banks. The monetary authorities are the Central Bank plus special funds or institutions which exercise specialised central bank functions such as the Stabilisation Fund, Foreign Exchange Funds, or specialised foreign exchange banks.

On the other hand, deposit money banks are composed of commercial banks and rural banks accepting demand deposits. The acceptance of demand deposits by rural banks, except those already having these accounts, was for sometime disallowed as a result of the 1972 amendment to the General Banking Act. However, a recent amendment has superseded this, and has allowed rural banks and banks

other than commercial banks, to accept demand deposits, subject to rules that may be prescribed by the Monetary Board.

The non-monetary financial system is classified into bank and non-bank institutions. The banking institutions consist of thrift banks, rural banks and specialised banks. In turn, thrift banks are composed of savings and mortgage banks, private development banks and stock savings and loan associations. The specialised banks include the Development Bank of the Philippines (DBP), the Land Bank (LB) and the Philippine Amanah Bank (PAB).

The non-bank financial institutions are composed of investment houses, finance companies, investment companies which may be open-ended or close-ended, securities dealers, securities brokers, pawnshops, fund managers which may be employee welfare funds or pension funds or trust funds, lending investors, non-stock savings and loan associations, mutual building and loan associations, private insurance companies and specialised government non-bank institutions like the Government Service Insurance System (GSIS), the Social Security System (SSS).

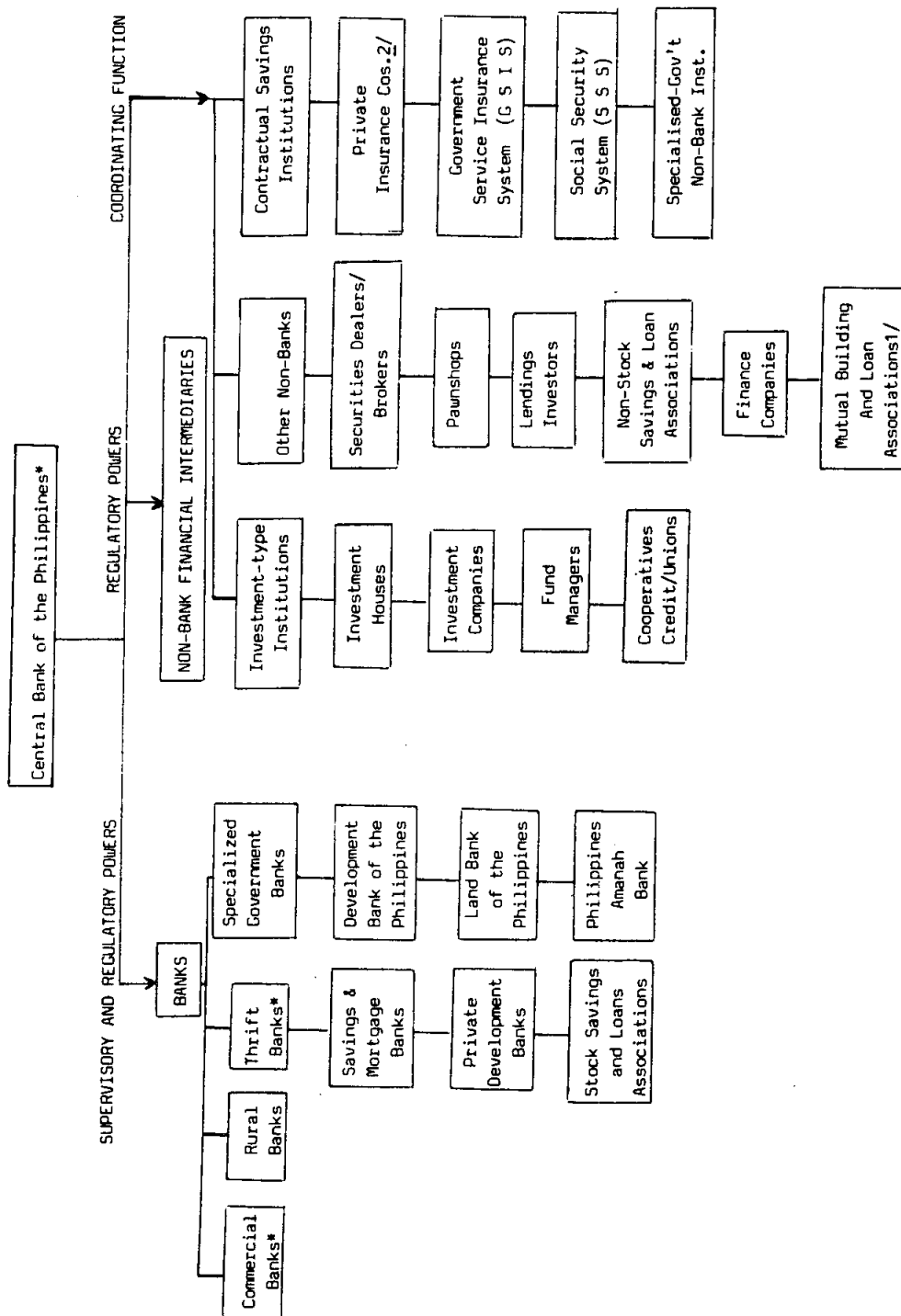
The Central Bank of the Philippines

The Central Bank of the Philippines was established as early as June 15, 1948 by virtue of Republic Act No. 265 known as the Central Bank Act. Its operations, however, started only on January 3, 1949.

Under its original Charter, the general objectives of the Central Bank consisted of: maintenance of monetary stability; preservation of the international value and convertibility of the peso into other freely convertible currencies; and promotion of a rising level of production, employment and real income. To amplify these objectives, Presidential Decree No. 72 amended the Central Bank Charter with more clearly-defined goals: (a) to maintain internal and

Chart 1

STRUCTURE OF THE PHILIPPINE FINANCIAL SYSTEM



* Monetary System composed of money-generating banks namely the CB, KBs, RBs, TBs Accepting Demand Deposits.

- 1/ Supervised and regulated by the Central Bank.
- 2/ Under the Office of Insurance Commission.

external monetary stability in the Philippines, and to preserve the international value of the peso and the convertibility of the peso into freely convertible currencies; and, (b) to foster monetary, credit and exchange conditions conducive to a balanced and sustainable growth of the country.

The primary function of the Central Bank of the Philippines is to manage the country's currency system. Its other functions include controlling the economy's supply of money and credit, managing the country's international reserves, acting as the country's sole bank of issue and as the depository and fiscal agent of the Philippine Government and its instrumentalities. The Philippine central bank also has lending functions which include the extension of rediscounts, discounts, loans and advances to banking institutions to regulate the volume, cost, availability and character of bank credit and to provide the banking system, when needed, with liquid funds. The Central Bank may also make direct provisional advances to the Government and its instrumentalities in financing their expenditures not to exceed twenty per cent (20%) of the average annual income of the borrower for the last three preceding fiscal years.

From its establishment in 1949 to 1984, the total assets and liabilities of the Central Bank expanded substantially, both approximating over P160 billion. These values comprised over 40 per cent of the total assets/liabilities of the entire financial system in 1950 (Table 2). In time, however, their respective shares to total decreased while those of other financial institutions expanded. Of great significance was the sharp decline in the ratio of currency issue to total liabilities and the increased share of other liabilities to total liabilities during the period. In 1949, currency issue comprised 81 per cent of total Central Bank liabilities. Its share to total liabilities dropped to 62 per cent in 1970 and to only 13 per cent by June 1984. On the other hand, the share of Central Bank demand deposit liabilities to its total liabilities increased from 15 per cent in 1949 to 23 per cent in 1970 and to 30 per cent in

June 1984 due to the rise in the deposit balances of the National Government and of financial institutions (Table 3).

THE BANKING SECTOR

Commercial Banks

Commercial banks play a dominant role in the financial sector, comprising about 40 per cent of the total resources of the financial sector and 74 per cent of that of the banking system in June 1984. They are the main mobilisers of funds but the allocation of these funds is geared mostly towards the short-term.

At the end of June 1984, there were 34 commercial banks, broken down into 28 private domestic commercial banks, two government or semi-government banks and four branches of foreign banks. Total bank assets have grown by P266 billion from 1950 to June 1984, and this was equal to 105 per cent of GNP in 1984. The government-owned Philippine National Bank (PNB), by far the largest bank with 203 branches and agencies, held more than one-fourth of all commercial banks' assets in 1984.

A review of significant developments in the operation of commercial banks shows the following:

1. Commercial banks' total liabilities as of end-June 1984 amounted to P244 billion or 47.3 per cent of total financial liabilities (see Table 4). The main component of commercial banks' liabilities was deposits which expanded continuously during the 1950-1984 period. The generally higher growth rate of savings and time deposits as compared with demand deposits has resulted in a structural change in the composition of deposits. In 1950, demand deposits comprised 66 per cent of total deposits while savings and time deposits constituted 34 per cent. In 1970, the proportionate shares

of demand deposits and savings and time deposits were 31 per cent and 69 per cent, respectively. These proportions have changed in 1984 in favour of savings and time deposits, at 86 per cent, while demand deposits accounted for 14 per cent. This development has been traced to the positive effect of the upward revisions in savings and time deposit rates during the period 1970 to 1984.

2. Commercial banks' deposit substitutes expanded by averages of 5 per cent and 10 per cent during 1975-1980 and 1981-1984, respectively.

3. With the increase in deposits, deposit substitutes and other sources of loanable funds, gross credits also grew from P627 million in 1950 to P181.1 billion in June 1984.

4. The capital reserves also rose, particularly in the 1970s, in response to the increased capitalisation programme of the government.

5. Information on credit allocation by industry of commercial banks showed a declining share of agricultural sector credit to total credit extended despite the law requiring banks to set aside 25 per cent of their loanable funds for agriculture (see Table 6). Total trade credit was also on the downtrend. The decline in the volume of trade credit could be partly explained by alternative direct sources of trade financing among the non-financial business organisations, including suppliers' credit. On the other hand, there was a significant growth of credit to financial institutions; its share to total credits rising from 7 per cent in 1970 to 12 per cent in March 1984, a development which implied increased financial layering and strong interconnection between financial intermediaries. The substantial growth in credit to financial institutions took place in the mid '70s when money market activities were booming. On credit extended classified by maturity, data on Table 7 shows that the bulk of commercial bank credit is of short-term nature. However, starting

in 1975, statistics on credit extended, by interest rate, show an increasing amount of lending at over 14 per cent, which presumably imply lending for more than two years' maturity (see Table 8).

Rural Banks

On June 6, 1952, the Rural Banks Act (R.A. 720) was legislated to broaden the monetised sector and to mobilise funds for rural investment and development.

Since 1953, rural banks have grown in number from 18 to more than 1,158 in June 1984, with wide geographical dispersion. Despite their number, total assets and aggregate liabilities comprised less than 2 per cent of the financial system's aggregate values. The bulk of rural banks' liabilities was in deposits, a large component of which was savings and time deposits, and the other, bills payable. However, in time, the percentage share of rural banks' deposits declined from 60.2 per cent of the system's total liabilities to only 45 per cent while other bills payable and other liabilities rose from 38 per cent to 55 per cent.

Thrift Banks

Private development banks. In terms of total assets, the largest of the three categories of thrift banks in 1984 were the private development banks, followed by savings banks and stock savings and loan associations (see Table 2). Private development banks (PDBs) provide medium and long-term credit mostly to the small and medium-scale industrial/agricultural sectors. They obtain financial assistance from DBP and also collect savings and time deposits which grew from P71 million or 72 per cent of total PDB liabilities in 1970 to P2.4 billion or 59 per cent in 1984 (see Table 13).

By virtue of the authority given to thrift banks by the Central Bank to accept demand deposits in August 1978, the volume of PDBs' demand deposits grew from P2 billion in 1980 to P112 billion in 1984 or 2.3 per cent of PDBs' total liabilities. Similarly, bills payable (including deposit substitutes liabilities) increased from P24.6 million in 1970 to P1,266.8 million in 1984. Despite these developments, the share of PDB liabilities to total liabilities of the financial system changed very little, from 0.4 per cent in 1970 to 0.7 per cent in 1984 (Table 4).

Savings banks collect savings from the community, particularly the small savers, and use the funds for lending to business and individuals and for investing in government securities.

Stock savings and loan associations accumulate the savings of its members or stockholders which in turn are lent to households for their personal finance and long-term financing for house building and development, and/or for investment in the securities of productive enterprises or the government.

Both the savings banks and stock savings and loan associations lend predominantly for real estate purposes and have higher shares of medium and long-term credit than commercial banks. Their total savings and time deposits comprised more than 80 per cent of their total liabilities. Of the two, savings banks were by far the larger in assets/liabilities size. The percentage share of aggregate liabilities of both types of banks to total liabilities of the financial sector, however, did not improve much, from less than 3 per cent of total liabilities throughout the period.

Specialised government banks. The fourth component of the banking sector is the specialised government banks which were set up for specific purposes. They consist of the Development Bank of the Philippines (DBP), the Land Bank and the Philippine Amanah Bank. Total assets of these banks accounted for more than 10 per cent of the

total assets of the financial system in 1984. Their sources of funds are deposits, capital accounts and borrowings. The DBP provides medium and long-term funds for industrial, agricultural and community development. Moreover, the DBP assists private development banks and rural banks through equity investments, rediscounting facilities, technical assistance and training programmes. The Land Bank was set up mainly to finance the acquisition of landed estates by the Government as part of its land reform programme. The third specialised government bank, the Philippine Amanah Bank, was established to accept deposits and to provide credit to the Muslim communities in Mindanao. The Land Bank and the Amanah Bank both function as commercial banks.

As a whole, specialised government banks' liabilities comprised less than 20 per cent of the financial system's total liabilities in 1984. Of the three banks, the DBP is the more dominant institution in terms of resources and liabilities. The biggest liability component of specialised government banks is the bills payable/deposit substitutes account which comprised 60 per cent of their liabilities. Deposit liabilities - demand, savings and time deposits - consisted of only 20 per cent of the total.

THE NON-BANK SECTOR

The non-bank sector has a wide variety of institutions. However, the sector comprised only one-fifth of the financial system's aggregate assets and aggregate liabilities.

Contractual Savings Institutions

Of the non-bank financial intermediaries, the most important in terms of assets and/or liabilities are those engaged in the provision of social security. These are the Government Service

Insurance System (GSIS), the Social Security System (SSS), both of which are government-owned, and the private insurance companies whose combined assets expanded by more than P40 billion during 1970-1984, but whose share to total resources declined from 18 per cent to 8 per cent during the period.

The share of their liabilities to total also decreased from 5 per cent to 2 per cent. The GSIS, SSS and private insurance companies are sources of long-term finance in the economy - in the form of loans, bond purchases and equity participation. Of the three institutions, the biggest in terms of assets in 1984 was the Social Security System (SSS) whose share to total financial assets comprised 3 per cent. The SSS is primarily an insurance company, membership of which is compulsory as provided for by law for all employers of private firms and their employees.

The SSS uses the major portion or more than 70 per cent of its funds for lending (such as salary loans, housing loans and other viable business projects) and the rest, investments in government and other securities. The bulk of its liabilities are in accounts payable, reserves for insurance premiums, losses, claims and other liabilities.

The operations of the Government Service Insurance System (GSIS) are very similar to the SSS, the only difference being that the former covers private companies and their employees while the GSIS covers all government employees. The primary objective of the GSIS is to provide insurance (retirement, pension and life) protection to its members who represent a specific sector of the population, the government employees. The premiums paid by the employers and employees are fixed by law and the amounts received by the GSIS from contributions of its members represent compulsory savings.

Its sources of funds are premiums received from life insurance, retirement insurance, mortgage redemption insurance and

salary loan insurance (which amounted to more than P900 million in June 1984) as well as income from investments, service income, commission and reinsurance, miscellaneous income and borrowings. Notes payable and claims payable comprised the major portion of its liabilities which expanded substantially during 1970-1984, but whose percentage share to total liabilities of the financial system remained at less than 2 per cent all throughout the period.

Loans and investments are not restricted to servicing the needs of its members whose loans are presently in the policy and salary loan categories. The larger part of these assets is in the form of industrial and real estate loans and stocks and bonds and other investments.

Private insurance companies numbering 136 in June 1984 recorded aggregate assets of P13.7 billion in June 1984 or 2 per cent of total resources of the financial system as compared to P1.7 billion in 1970. Their loan and investment operations stood at P4.8 billion in 1984, the latter comprising 46 per cent and the former, 54 per cent. The main sources of funds of private insurance companies are the premiums received from private individuals and corporations which during the 1975-1984 period expanded from 13 per cent to 20 per cent of gross private savings.

With a substantial amount of premiums periodically received (see Tables 9), total liabilities (composed largely of reserves for unearned premiums, claims payable due to reinsurer and accounts payable) of private insurance companies increased by more than P9 billion during 1970-1984 to P10.4 billion or 2 per cent of the financial system's liabilities in 1984 (see Table 4).

Investment-type Intermediaries

There are several kinds of investment institutions: the investment houses, investment companies, fund managers, lending

investors, venture capital corporations and cooperatives/credit unions (data on the last type of financial intermediaries is not available).

Investment houses in the Philippines perform the functions of investment banks or merchant banks. As of June 1984, there are 49 investment houses with total assets amounting to P7.5 billion or 56 per cent more than in 1975.

Twenty three investment houses in the Philippines are actively engaged in quasi-banking activities, that is, they accept deposit substitutes (promissory notes, repurchase agreements, certificates of participation and certificates of assignments) and other forms of money market instruments which provided the bulk of their income in money market booms. In recent years, investment houses have started to perform a wider variety of financial services which ranged from portfolio management to issuing and investing in bonds and securities and advancing loans receivables, underwriting of new issues of capital, term loans to industries and loan syndications.

In 1973, deposit substitutes issued by investment houses with quasi-banking functions comprised nearly 40 per cent of total deposit substitutes issued by the financial system. This percentage share of total issues gradually declined to less than 20 per cent in June 1984 as investment houses' underwritings and other activities expanded. Table 10 shows the volume of underwritings handled by investment houses. During the period, total underwriting volume has increased particularly in debt securities. However, the major portion of debt securities underwritten was privately placed and not listed on the exchanges.

In the 1970-1984 period, total liabilities of investment houses as a percentage of total liabilities of the financial sector declined from 4 per cent to 1 per cent.

Investment companies are primarily engaged in investing, reinvesting or trading in securities and are of two types, open-ended and close-ended. The former have no fixed amount of paid-in capital, and sell their shares on a day-to-day basis. Moreover, their shares are redeemable on demand. The close-ended company cannot redeem shares on a day-to-day basis, and has a relatively fixed amount of capital outstanding. Aggregate resources of investment companies during the 1973-1984 period expanded significantly from P2,226.3 million in 1973 to P4,603.1 million in 1984. Their liabilities also rose from P245.3 million to P2,452.6 million although the share to total financial liabilities dropped from 1.1 per cent to 0.4 per cent.

Venture capital corporations (VCC) established in 1981 refer to any entity organised jointly by private banks, the National Development Company, and the Technological Resource Center, the purpose of which is to develop, 'promote and assist, through debt, equity financing or any other means, any small and medium scale industry enterprise in the country. The number of VCC in operation grew from one in 1981 to 15 as of the end of 1984. As of June 1984, their assets amounted to P112 million or an increase of 133 per cent from the first date of their operation in 1981.

Fund managers administer funds on behalf of others. The funds consist mostly of pension or trust funds and employees' welfare funds. Over the years, the number of fund managers declined from 161 in 1963 to only 12 as of June 1984. Despite this development, total assets rose from P1,951.5 million in 1974 to P2,873.2 million in 1984. However, their total liabilities declined from P49.8 million in 1974 to P33.4 million in 1984. Fund managers did not incur substantial amounts of borrowings in the said periods and the bulk of their liabilities was in other liabilities' account.

Other Financial Institutions

Finance companies are stock corporations which extend credit

to both enterprises and consumers usually by discounting or factoring commercial papers or accounts receivables by buying and selling contracts, leases, chattel mortgages or other evidences of indebtedness, or by leasing industrial machinery, heavy equipment and motor vehicles. In June 1984, there were 344 finance companies with assets and liabilities aggregating P10.5 billion and P8.4 billion, respectively. Loans and investments of finance companies have expanded from P1.4 billion in 1973 to P7.8 billion in 1984. Finance companies borrow funds by issuing promissory notes and bonds and borrowing from other financial institutions.

Lending investors defined in the Philippines' Internal Revenue Code as persons who make a practice of lending money for themselves or others, number to 96 in June 1984, raise their own capital for the purpose of extending all types of loans, generally short-term, often times without collateral. The combined resources of lending investors amounted to P24.9 million in 1974 and P52.6 million in 1984.

Securities dealers and brokers numbered 126 in June 1984 and are engaged in transactions in securities on behalf of others, which earn them commission. They do not, however, act as a principal. For the years in review, total assets of securities dealers/brokers rose from P882.1 million in 1974 to P1,035.5 million in 1980, then declined to P836.7 million in 1984. Their liabilities, mostly in the form of borrowing, also dropped from P583.4 million or 0.8 per cent of total financial liabilities to P531.6 million or 0.1 per cent.

Pawnshops or business establishments which are engaged in lending money on personal property declared as security or pledge had total assets of P100.8 million in 1974 which rose to P518.6 million in 1984. Their aggregate liabilities also expanded from P19.9 million to P162.6 million.

The non-stock savings and loan associations whose operations and membership are confined to a well-defined group of persons and not to the general public, accept deposits from and grant loans to its member-depositors only. The system's aggregate resources amounted to P682.9 million in 1984 while its total liabilities reached P128.4 million.

The mutual building and loan associations whose purpose is to accumulate the savings of its stockholders to encourage industry, frugality and home building among its stockholders and to lend its funds to stockholders on the security of unencumbered real estate, had aggregate assets of P17.6 million and total liabilities amounting to P5.5 million in 1984.

There is a dearth of information on cooperatives and credit unions.

Degree of Institutional Concentration

Commercial banks constituted 43.3 per cent of the total assets of the financial system at the end of June 1984; Central Bank, 26.1 per cent; thrift banks, 2.5 per cent, specialised banks, 11.4 per cent; rural banks, 1.4 per cent; and non-bank financial institutions, 15.3 per cent. The predominant role of the commercial banks contrasted with the minor role of the thrift banks and rural banks.

The percentage share of commercial banks' assets to the system's total dropped from 53.4 per cent in 1950 to 45.4 per cent in 1970, thereafter maintaining an average share of about 44 per cent. This deceleration is also observed for Central Bank assets during the 1950s to the 1970s which contrasted with the rise in asset shares of other types, particularly non-bank financial intermediaries which gradually became an important segment in the financial sector. The expansion of the assets of specialised government banks is also significant especially in terms of their role in long-term finance.

INSTRUMENTS IN THE FINANCIAL STRUCTURE

It is recognised that the preponderance of various types of financial institutions alone cannot achieve maximum efficiency in the allocation of resources without the introduction and use of financial instruments. Aside from the allocative effect, the existence of financial claims enriches the array of assets available to asset holders, thus increasing the attractiveness of savings and facilitating transfer of investment to others.

Table 11 provides a broad indication of the types of financial instruments in the Philippines and their values during the 1950-1984 period. Financial institutions issued approximately 38 per cent of the total financial instruments outstanding in 1984. The types and values of financial instrument in earlier years, 1950-1960, were relatively small compared with the greater variety and larger values during the latter period. This was brought about by the emergence of other types of financial instruments like deposit substitutes, NOW accounts and foreign currency deposit accounts which were introduced to gather more funds.

The growth of deposit substitutes has been substantial. Introduced by commercial banks in the late Sixties as their own instruments to compete for funds in the then emerging money market, deposit substitutes have grown substantially from P3 billion in 1973 to P25 billion in June 1984 and have become an important source of loanable funds for banks and non-bank financial intermediaries.

As to Type of Issue

Available data during the 1950-1984 period indicated that the bulk of financial instruments was in the form of claims, while a minimal portion was in equity issues (see Table 11.1). The

insignificant share of equity issues to claims even declined from 7 per cent in 1970 to only 2 per cent in 1984 - an indication that, over time, the country's capital market has not developed significantly. More than one-half or 62 per cent of all financial claims in 1984 and 70 per cent in 1970 were claims of financial institutions against non-financial units (Table 11.2). Claims of non-financial units against financial institutions, on the other hand, comprised 38 per cent of all claims in 1984, against their share of 30 per cent in 1970 (Table 11.3). The rise in per capita income had contributed to the increase in the claims of non-financial units against banks/non-banks.

All financial instruments in June 1984 constituted approximately 281 per cent of the national wealth if claims against financial institutions are included, and a value of approximately 175 per cent if such claims are excluded. Comparing the 1984 value and the array of financial instruments with that of 1970 indicates various changes. For instance, the value of all the financial instruments to national wealth has increased substantially from 116 per cent to 281 per cent.

The share of financial institutions in total financial instruments has decreased from 27 per cent in 1970 to 38 per cent in 1984.

The share of currency in all financial instruments has declined, from 15.3 per cent in 1950 to 2.6 per cent in 1984. On the other hand, a substantial increase has occurred in the share of savings deposits and insurance premiums in all financial assets. The growth of savings deposits has been traced to the increase in deposit rates in the 1970-1984 period. Likewise, the growth of deposit substitutes has been substantial.

Of the claims against the non-financial sector, loans and government securities have increased considerably.

In summary, bank deposits have increased continuously. The higher growth rates of time and savings deposits over demand deposits induced a structural change in deposits. In 1960, total demand deposits constituted 43 per cent of total deposits and savings and time deposits, 57 per cent. This changed to a proportionate share of 28:72 per cent in 1970 and finally to 11 per cent (demand) and 89 per cent (savings and time) in June 1984.

Furthermore, there is a noticeable growth of longer-term deposits of over 2 years maturity as shown by the rise in the ratio of these deposits: total time deposits from 24 per cent in 1975 to 70 per cent in 1980 and 64 per cent in June 1984.

Banks' deposit substitutes similarly expanded during 1975 to 1984 although its share to total banks' liabilities declined.

Relative Importance of the Financial Structure

Financial interrelations ratio (FIR). One common measure of the importance of the financial structure is to relate it with the national wealth. This can be gauged through the financial interrelations ratio, that is, the total value of financial instruments outstanding divided by the Gross Domestic Product. In the Philippines, the FIRs obtained for selected years showed a growing financial sector. As shown in Table 14, the FIRs obtained in 1950 and 1960 meant that the total value of financial instruments was about half of the national wealth. By 1970, the value of financial instruments exceeded that of GDP, or an FIR of 1.14. By June 1984, the ratio more than doubled and reached a level of 2.81.

Financial intermediation ratio. Similarly, the relative importance of the country's financial sector can be measured by the financial intermediation ratio. This ratio indicates the extent of financing extended by the financial institutions to the non-financial

units and is obtained by dividing the total funds provided by financial institutions to non-financial units to the total funds raised by the latter. In 1980, the ratio was at .69, that is, financial institutions provided about 70 per cent of the financing needs of the non-financial sectors (see Table 15). This went down to that the financial institutions supplied three-fourths of the borrowings of the non-financial sectors.

Degree of monetisation of the economy. Various measures of financial deepening indicate that the degree of monetisation in the economy has been significant over the 1950-1984 period. For instance, the increasing use of broad money is evident in the consistent rise in the M2/GDP and M2/M1 ratio except in 1975 as shown in Table 15. The growth of near-money reflects not just rising monetisation but increasing sophistication in financial intermediation. The use of narrow money (M1) has declined with the increasing use of quasi-money. The monetisation process is also evident in the growth of real per capita deposits with reflected increases from P4 in 1950 to P240 in 1970, to P1,871 in 1980 and P2,548 in 1984.

III. IMPLICATIONS FOR MONETARY POLICY

The primary objectives of monetary policy in the Philippines are to have monetary stability without undue inflationary pressures and balance of payments disequilibrium, and to accelerate economic growth. The past decades or so saw policy measures being carried out and financial reforms and innovations introduced to make the financial system more responsive to changing development needs and contribute to the attainment of monetary and economic goals.

Changes in reserve requirements, open market operations and rediscount policy were the major monetary measures used by the Central

Bank to influence domestic credit and liquidity. Other instruments of monetary control employed were: selective credit control such as credit priorities, allocation and eligibility rules, variation of the marginal deposit requirement for opening import letters of credit, minimum capital requirements and minimum risk asset/capital ratio, interest rate policy with respect to the maximum deposit and lending rates, supervision and directives from the Central Bank and foreign exchange rate policies. Last but not least were policies adopted to promote and encourage the establishment of financial institutions and markets.

Monetary and Financial Policies and Measures

1949-1960. Reserve requirements, the discount window and open market operations were used sparingly during the period 1949-1960 as the thrust of policy was towards foreign exchange controls to solve the problem of high imports, dwindling foreign exchange reserves and prices. 2/ A detailed set of import and foreign exchange controls was instituted at the beginning of the decade to achieve this end. Foreign control instruments were also used to enhance the government's industrialisation policy which was mainly import substitution.

Moreover, policies towards the development of financial institutions were introduced. These policies included the grant of incentives including capital assistance to banks, particularly to rural banks (to bring banking facilities to the rural/agricultural sector and to neutralise the operations of the unorganised financial sector) and private development banks (to meet the medium and long-term requirements of industry). Direct government participation in financial institutions was also adopted to expand financial services to priority sectors and to attain national goals.

2/ DER-D Staff Paper on "Review of Monetary and Banking Policy", 1981. Subsequent sections were also taken from said review.

On the whole, exchange controls provided the momentum of economic growth as can be seen in the rising level of income. Conservative monetary policy also resulted in moderate growth in money supply which averaged 2 per cent from 1949 to 1955 and from 2 to 13 per cent between 1955-1960.

1960-1970. The Central Bank turned more frequently to the traditional tools of monetary policy following the lifting of exchange controls in 1962. Regulations that either raised the reserve requirements or the rediscount rates were imposed almost every year except in 1966. However, the orientation of monetary policy was towards promoting economic development in line with the objective -"to promote a rising level of production, employment and real income". To achieve this objective, selective credit measures were extensively used. With deliberate, selective credit policy, chosen sectors of the economy were expanded and developed.

The rediscount window began to be used as one of the major instruments for selective credit control. Preferential or concessional rates were given to preferred activities like rice and corn and other production activities, exports and small medium scale industries. Changes in the rediscount rate were made as a means of aligning them to changes in nominal rates of deposits and loans instead of as a means of controlling borrowings of commercial banks. Since a fairly wide margin was allowed between the discount rate and the loan rate (a margin which remained fairly constant over the years), banks were quite passive with regard to changes in discount rates. The margin of profit allowed tended to make the demand for funds from the Central Bank infinitely elastic. In this case, the level borrowed was determined mainly by what the Central Bank decided to lend to the banking system.

However, the importance to the banking sector of the discount window was not so much the margin between the loan and the rediscount rates, but more significance was having the Central Bank as

the major source of loanable funds. Indeed the Central Bank was not simply a bank of last resort, but might even be considered the bank of "first resort", resulting in a chronic condition of dependence and at the same time putting squarely on the Central Bank's lap the responsibility of keeping the banking system liquid and solvent.

Another selective instrument commonly used in the '60s was the use of differential interest rates on loans on priority activities. In general, loans for these activities were granted by government and government-supported financial institutions. The rates of interest on these loans were usually lower than on loans granted by private banks. Private banks were also encouraged to grant loans to these activities at lower rates by allowing them a more lenient discount privilege and portfolio ceilings on these loans.

In the '60s, the establishment of regional offices of the Central Bank in the provinces was also pursued to promote economic activities and growth in these areas.

The expansionary programme adopted to spur economic development resulted in more pronounced monetary growth during the 1961-1970 period. Growth in money stock ranged from 4 to 17 per cent. It was also during this time when significant increases in consumer prices were felt. Annual increases in consumer price index ranged from 1.3 to 14 per cent.

1970-1980. The next decade was characterised as a period of reforms in the financial system, influenced by the declaration of martial law which put forth drastic changes not only in the political set-up but in the socio-economic system as well.

Amendment of the Central Bank Act

One important development that affected the financial system was the amendment of the Central Bank Act in 1972, which among

others, extended the authority of the Central Bank over the entire credit system. Furthermore, the revised act stressed as the primary objective of the Central Bank the maintenance of internal and external stability instead of the task of economic development earlier assigned to it.

The General Banking Act of 1949 was also revised, almost entirely, including the redefinition of basic banking terms, the reclassification of financial intermediaries into banks and non-banks as well as guidelines on their operations. The capitalisation requirement was also increased and this allowed equity participation of foreign entities in domestic banks up to the extent of 30-40 per cent to diffuse ownership particularly in family-owned banks.

Interest Rate Revisions

Interest rate reforms were also enacted. The amendment to the Anti-Usury Law of 1906 in January 1973 authorised the Monetary Board to prescribe the maximum rate of interest as warranted by prevailing socio-economic conditions. However, the amendment authorised the Monetary Board to change the interest rate only once a year.

Other interest rate revisions effected towards the latter half of the '70s brought about upward changes in interest rate ceilings on savings and time deposits, deposit substitutes, loans and purchase of receivables and other obligations. On the whole, these interest rate changes were aimed at increasing deposits in banks, particularly long-term deposits, and at regulating the cost of borrowing.

The upward changes made on savings and time deposit rates had a positive impact on the volume of these deposits. Growth in savings deposits accelerated immediately after the revisions and more significant increases were registered in long-term time deposits which

were given higher interest rate differentials compared to savings deposits. On the other hand, deposit substitutes which recorded accelerated growth rates before the imposition of a ceiling on their yields experienced decelerated growth rates. This started in 1976 and they recorded their lowest growth in 1978.

The rise in the volume of deposits however could not be solely attributed wholly to the increase in interest rates, particularly periods of high prices which characterised the latter half of the '70s. Therefore, it may be said that the objective of giving a real positive reward on regular savers under a regime of administered interest rates has not been possibly attained. 3/

In the money market, the imposition of administered ceilings on money market rates eliminated what used to be a good indicator of the demand and supply situation in the funds market. It is believed that the ceilings on money market rates were directed only to the symptoms and not to the cause of the volatility and level of these rates. Often times, the volatility of money market rates was traced to the rapid changes in the banking system's reserves and the high penalties on bank reserve deficiencies.

Lending Rate Policy

The ceiling placed on lending rates meant a regime of cheap credit policy in the '70s. Large borrowers who could otherwise avail

3/ Ibid.

The penalty rate of 36 per cent imposed by the Central Bank on banks' reserve deficiencies accentuated this volatility. To meet their reserve deficiencies, banks resorted to the money market, and thus developed the interbank call loan market.

themselves of the securities or equities market turned to the loans market or to banks which offered relatively lower rates on long-term loans.

Credit Policy

Credit policy of the Central Bank in the '70s continued to be selective, encouraging exports, small-scale and agricultural activities which at times had an expansionary bias. Rediscount ceilings of banks were extended to allow them to accommodate further the credit needs of these sectors. Loan values were likewise revised upward. Some indications of the positive effect of this sustained credit support maybe gleaned from the boost in grain production and the growth in non-traditional exports. A further development in credit policy was the drawing up of an annual financial programme starting in 1976 which adhered to specific domestic credit and liquidity levels to support a targetted GNP growth rate consistent with a desired balance of payments account and inflation rate. Performance criteria set annually were observed with some revisions in the process to attune them with unexpected developments in the economic system. The observance of this financial programme allowed for the coordination of various instruments employed by the monetary authorities such as those relating to open market operations, rediscounts, repurchase and swap transactions. The greater significance of the programme was in the close coordination that has been achieved among the major policy-making bodies of the government like the Ministries of the Budget and Finance, the Central Bank and the National Economic and Development Authority, to attain the programme's objectives.

1980-Present. It has been said that the source of policy is dictated, not just by programme objectives but by critical events that have occurred. Perhaps, no other events as significant as the oil price hikes, world recession and restrictive trade practices have

influenced the direction of monetary policy in the late '70s up to the present.

The initial impact of the second oil hike in 1979-80 turned out to be longer and more serious than earlier expected. This was reflected in the rise in inflation rate from 7.8 per cent in 1978 to 17.6 per cent in 1980 and the slow down in the growth of real GNP from 5.8 per cent to 4.7 per cent.

The adverse effects of prolonged recession, moreover, continued to pose difficulties for the export sector. Total exports grew very much less, at the yearly average of 9.2 per cent between 1978-83 as compared to 23.8 per cent in 1973-78.

In its attempt to moderate the impact of these destabilising developments, the government adopted an adjustment programme and countercyclical fiscal policy which required substantial resources. The programme had for its main components the development of domestic energy sources, encouragement of non-traditional exports and market diversification, tariff reform, import liberalisation and rationalisation. All of these were geared towards improved productivity and efficiency of Philippine industries to enhance their international competitiveness and eventually achieve a better external payments position.

The financial system has also been strengthened through monetary and financial reforms specifically designed to lend support to affected industries, to moderate the impact of the worsening terms of trade and to minimise inflationary pressures. The most important monetary and financial policy measures have been: (1) the financial reforms and the adoption of a universal banking system; (2) the rationalisation of the rediscount window; (3) the deregulation of interest rates; (4) strengthening the money market; (5) developing the government securities market; (6) external account management, and, (7) flexible exchange rate policy.

Shift Towards the Universal Banking System

The modification of the Philippine financial system toward the universal banking concept at the start of the '80s was one of the more significant reforms implemented to adapt its basic structure to both domestic and foreign developments.

The Philippine financial system up to the '70s was made up of particular types of banks - one dealing exclusively with short-term financing and foreign trade, another with real estate and other medium and long-term loans, one bank type with agricultural credit, while other non-bank financial institutions were specifically confined to consumer financing or securities dealership.

The need to do away with a highly specialised type of financial system became apparent with the growing financial requirements of the country, particularly with the implementation of the new industrialisation scheme. In the past, the long-term funds requirement for investment and capital formation had not been adequately provided for, as indicated by the uneven growth and decline in recent years of real gross domestic investment.

The universal banking concept was adopted in modified form mainly to achieve two objectives: first, to attain greater efficiency in the financial system through increased competition and economies of scale and, second, to increase availability of and access to long-term funds.

To be able to attain the first objective, the limitation on the scope of activities of banks and quasi-banks was eliminated as much as possible. Under the Philippine concept, the pure form of universal banking was not adopted; instead the major categories of financial institutions were maintained with the possibility of graduation to higher category institutions, provided that the prescribed requirements were met. Thus, existing banks and non-banks

may merge to form expanded commercial banks which could provide varied and allied services. By broadening the range of services which financial institutions may offer, economies of scale could follow.

The shift in the orientation of the Philippine financial system toward universal banking required financial institutions to increase their capitalisation. This requirement was designed not only to meet the expanded needs of the economy but also to allow them to reap the benefits of economies of scale and participate more actively in international financial transactions. The universal banking regulations provided for a minimum capital of P500 million for banks with expanded commercial banking authority, P300 million for commercial banks and P20 million for investment houses. Thrift and rural banks were also required to have higher capitalisation bases, specifically those authorised to accept or create demand deposits. Moreover, to effect a more dispersed form of ownership, another prerequisite was for banks to undertake public offering of new shares of stocks to the extent of 10 per cent of the required minimum capital and for these to be listed on the stock exchange. As of June 1984, six commercial banks with expanded banking powers have been listed on the local stock exchanges.

An encouraging step in support of the government's move to encourage chain and/or branch-banking among rural banks, especially in areas inadequately served by them, took place in 1981 with the first consolidation of 14 rural banks in the province of Bohol.

The second major objective of the expanded commercial banking system is to increase the availability of and access to longer-term funds. It has been observed that the economic development of the country could have proceeded at a faster pace had it not been for the relative scarcity of longer-term funds. Commercial banks which accounted for about two-thirds of total resources of the financial system had their operations largely directed to short-term

lending. ^{4/} On the other hand, investment houses which had been established to develop the long-term funds market moved into the more lucrative short-term market and were dealing largely in money market transactions. In the main, the flow of funds into short-term investments was not in line with the growing long-term investment requirements of the country.

Although there existed a large and continuing permanent core of short-term deposits that could be lent to long-term credit, the flow of long-term funds was impeded by the rigidities imposed by legal regulations. The universal banking regulations of Batas Pambansa Blg. 61-67 of 1980 therefore included a number of legal and institutional amendments. One of these amendments is the power given to the Monetary Board to authorise a bank to maintain a lower net worth to risk asset ratio from the minimum 10 per cent to 8 per cent or 6 per cent under special cases. These lower ratios would afford banks and non-banks greater loan expansion capacity that could be directed to medium and long-term lending. To make the networth to risk asset ratio more realistic and meaningful, the list of non-risk assets was also expanded.

More importantly, the amendments introduced in the individual charters of Philippine financial institutions removed the functional distinction among these institutions to enhance their capability in mobilising longer-term funds.

Deregulation of Interest Rates

The freeing of interest rate ceilings initiated in 1981 and completed by January 1983 further complemented the move toward modified universal banking. In July 1981, interest rate ceilings on

^{4/} DER-D Staff Paper, "A Survey of the Philippines Financial System", 1983.

savings and time deposits and loans of over two-year maturities were lifted. Moreover, the revised definition of short-term maturity from two years to one year in October 1981 freed the ceilings on loan transactions with maturities of over one year. In January 1983, the lifting of the remaining interest rate ceiling on short-term loans (or those with maturities of 365 days or less) completed the last phase in the gradual deregulation of interest rates which started with the amendment of the Anti-Usury Law of 1906 in 1973. With the lifting of the last interest rate ceiling, a prime rate monitoring system was introduced and the Manila Reference Rate was improved, to provide up-to-date information on the lending rates charged by banks. These moves were expected to enhance competition among banks which may eventually lead to lower interest rates.

There are multiple goals behind the reforms in interest rates. The primary purpose is to encourage savings, particularly long-term placements needed in economic development programmes; and secondarily, to give a fair return to savers especially in periods of rising prices.

Strengthening the Money Market

The money market is a vital component of the Philippine financial system where banks, non-bank institutions, government and private entities as well as the general public, actively participate. Its notable growth in the late Sixties and early Seventies made short-term funds readily available so that even weak and non-prime borrowers gained access to this market. This led to the financial crisis in the early part of 1981 and led to the collapse of a number of financial as well as industrial entities which depended heavily on the money market for funds.

To ensure that no similar crisis would recur in the future, the Central Bank and the Securities and Exchange Commission formulated

measures to strengthen the money market. In 1982, supplementary money market rules and regulations have been issued which, among others, allowed only prime borrowers to avail themselves of funds in this market. The restriction of access to the money market to prime issuers and prime paper only was also expected to generate a greater volume of regular lending operations for banks. Other borrowers would have to deal with banks for their regular credit needs where proper evaluation procedures could be observed.

Developing the Government Securities Market

Part of the overall programme of broadening the country's financial system to enable it to become an effective agent of monetary policy is the development of the government securities market. An important component of this programme is to increase the issues of Treasury securities not only for the purpose of raising funds for the government but also to serve as a tool of monetary policy.

A new network of accredited dealers in government securities was set up to serve as the main outlet in distributing and promoting these securities in the open market. Moreover, a programme to develop a secondary market for government securities has been adopted as part of the on-going rationalisation of government securities.

Rationalising the Rediscount Window

In the '80s, the rediscount system continued to meet the needs of priority industries but efforts were taken to make the rates more market-oriented. This is in line with the prevalent view that subsidised rates make credit artificially cheap, not to mention its uneconomic and inefficient use. Subsidised credit, for instance, is said to favor capital intensive industries rather than labor intensive

ones which would have been a much better choice in the country like the Philippines. 5/

In addition to its allocative function, the rediscount window has gradually been used as an instrument to control bank borrowings. In 1980, a "lender-of-last resort" facility was established which reinforced its stabilisation role. This facility sought to encourage banks and non-banks with quasi-banking functions to tap other sources of funds before turning to the Central Bank. Hence, the cost of borrowings in this facility was set at a penalty rate to discourage over-dependence on the Central Bank.

External Account Management

The careful management of the country's external borrowings continued in the '80s in line with the heightened capital requirements during the period, paying particular attention to lengthening of maturity periods and lowering interest charges on negotiated loans.

To enhance greater competition among producers and minimise the impact of higher import cost on consumers, the liberalisation of a number of previously banned import items was undertaken by the government in the latter part of the '70s. The Central Bank, for its part, pursued policies which provide incentives to foreign exchange-earning activities.

Foreign Exchange Management

A flexible exchange rate policy has been maintained since 1970. This was pursued in a manner which allowed only small but frequent exchange rate changes as an alternative to irregular, large

5/ P.F. Neri. "Current Policy Consideration on Credit Allocation". CB Review, Vol. 37 No. 3, March 1985.

and abrupt adjustments. In more recent years, the peso has been floating with relatively greater flexibility.

Other Monetary Measures

Since 1980, the Central Bank has utilised changes in reserve requirements and open market operation for monetary control, especially in the control of domestic liquidity and influencing bank credit portfolios. In the 1980-1984 period, reserve requirements were raised three times, from 18 per cent in 1982 to 23 per cent in 1983 and finally to 24 per cent in 1984.

Open market operations became more active with the introduction of high-yielding Central Bank bills and Treasury bills. This policy instrument is most useful in its ability to influence levels of reserve money which directly affects the availability of credit.

EFFECTIVENESS OF MONETARY POLICY

The foregoing discussion of the country's financial and monetary development during the last 34 years shows the significant changes in the country's financial structure. The notable expansion in the financial development of the country was largely due to the support and influence of the Central Bank. While a central bank's basic area of concern is the management of liquidity and credit to achieve price, output, and balance of payments objectives, in the Philippines the Central Bank has assumed the broader and more difficult responsibility of promoting development objectives. In the last 34 years, the Central Bank has laid down the creation of a relevant financial institutional framework - financial institutions, financial instruments and financial markets, and had in many ways shouldered the task of development finance by providing funds directly or indirectly through financial institutions.

The establishment of financial institutions and their expansion, particularly in the countryside, has contributed in increasing the monetisation of the economy and the effectiveness of monetary policy. Various measures of financial deepening indicate that the degree of monetisation has been significant over the 1950-1984 period. For instance, the increasing use of broad money is evident and is indicated by the consistent rise in the M2/GNP and M2/M1 ratios (Table 16). The growth of near-money reflects not just growing monetisation, especially in the rural areas, but also growing sophistication in financial intermediation. The monetisation process is also evident in the growth of real per capital deposits which expanded from P4 in 1950 to P2,548 in 1984. The increase in the financial intermediation ratio from .11 to .17 per cent during 1970-1983 has been noted. Perhaps, the increase in ratios and their magnitudes would have been larger if the country's capital market is well-developed.

The effectiveness of monetary policy in recent years was assessed in terms of the achievement of monetary targets, including those for liquidity and credit, and economic objectives. The evaluation was carried out within the framework of the annual financial programme of the country.

The track record of the country's financial programming exercise, which has been in effect since 1976, has been generally satisfactory, performance showing close attainment of targets. The actual changes in domestic liquidity were in the direction called for. Comparison of the same set of growth rates reveals, however, that generally, monetary policy has been slightly more expansionary than was necessary. In six out of nine years, actual growth in domestic liquidity exceeded the target rate, from two to six percentage points.

In most instances, growth in internally generated money added to the expansion in liquidity. Increased government spending in most of these years for infrastructure projects as well as

expansionary fiscal policies designed to counteract prevailing recessionary trends exerted positive effects on the country's domestic liquidity level. Net credit to the public sector, however, remained below programme limit. Further, increases in domestic credit of the monetary system during the recessionary period of 1980-1983, intended to spur production activities in the agricultural and export sectors, resulted in expansion in domestic liquidity. Also, in most instances the component of domestic liquidity which recorded notable increases was savings and time deposits which in the main reflected the favourable reaction of savers to the uptrend in deposit rates after interest rate ceilings were deregulated.

On the other hand, the restrictive monetary and fiscal policies adopted in 1984 caused a much larger contraction in liquidity than was targetted. The control of domestic liquidity was aimed at reducing the inflationary pressures which reflected the spill-out effects of the upward adjustments in exchange rate on fuel, power rates, transportation fares, wages and speculative activities.

Assessed in terms of output growth, developments during the 1976-1984 period show that real growth rate of GNP fell short of targets during some of these years, to a large extent brought about by recessionary conditions abroad and domestic financial difficulties in the recent years. It is said that the tight monetary and fiscal policies and foreign exchange shortages in 1984 strained the finances of marginal and less efficient firms resulting in shutdowns and reduced operations. In turn, these contributed to significant decline in real growth of GNP and the rise in unemployment rate. The concern for accelerating output growth coupled with notable improvements in key areas of the economy resulted in the relaxation of monetary policy in the following year.

IV. SUMMARY AND CONCLUSIONS

The preceding sections have described the structure and functioning of the Philippine financial sector as it has developed in the last three and a half decades. The system was by no means static; it has changed substantially during the preceding decades and there is no reason to believe that the process of change is at end.

The evolution and development of the various components of the financial structure is seen as a consequence of the workings of a complex of interacting forces, some operating through the market and some through the initiative of the government. The government has affected the financial structure most directly through its regulatory policies and the whole gamut of financial policy -- monetary, fiscal and debt management aspects. The regulatory policies were of several types: chartering and branching policies that relate to the types of institutions allowed to operate and on the limitation on the number of physical facilities that an institution may operate; limitations on the range of services that each type may supply; and policies that relate to the type and mix of assets and liabilities of an institution. On the other hand, the monetary policy instruments frequently used were: (1) the quantitative instruments that control the volume of money and credit like reserve requirements, rediscount rate and open market operations; and, (2) the qualitative instruments like the selective allocation of credit, cash margin requirements for import letters of credit, interest rate regulations, minimum capital ratios, moral suasion, and foreign exchange regulations and controls. Fiscal policies including debt management strategy of the government have similarly influenced the growth and operations of the financial system.

The growth of financial institutions has been significant. From a relatively simple banking sector composed of the Central Bank, commercial and savings banks at the start of the 50s, the number of financial units rose to 5,955 consisting of expanded commercial banks,

rural banks, development banks, savings and loan associations, investment houses, finance companies and the like.

Total resources of the financial system have expanded as institutions involved in financial intermediation have evolved. The emergence of new non-bank financial intermediaries together with a marked growth in the capitalisation of commercial banks contributed to a more rapid rate of growth of the financial system after the 1970s. The growth of the non-banking sector was particularly significant, and was aided by the expansion of money market activities and the wide variety of new services offered by the non-bank financial intermediaries.

Accounting for almost half of the total resources of the financial system, commercial banks play a dominant role in the financial sector. They are the principal mobiliser of funds although their allocation of these resources is geared mostly to short-term credit for trade, financial services and industry. The government has considerable influence over the financial system through its ownership of the largest commercial bank and the largest development and two social security institutions.

Prior to the adoption of a modified type of universal banking system in 1980, financial institutions operated within the specific roles assigned to each type of institution. The narrowly focused specialisation of financial institutions is believed to have inhibited the economic development of the country in the long run.^{6/}

In the past three and a half decades, a sophisticated money market developed and a basis was laid for linkages with the international banking system with the establishment of the offshore banking system and foreign currency deposit system.

^{6/} A Joint World Bank/IMF Study on "The Philippines: Aspects of the Financial Sector", March 1979.

On the other hand, the capital market in the Philippines has not been a significant source of medium and long-term finance. In the bond market, public sector securities, principally Treasury bills and CBCIs predominated while the supply of private sector corporate securities was basically thin. The shares market was also small with equity ownership generally biased to speculative oil and mining shares.

The volume and array of financial instruments exchanged in the country's financial markets reflected to a great extent the state of these markets. Available data show the preponderance of non-marketable claims over marketable ones, the latter consisting mainly of those commonly traded in the money market like promissory notes, certificates of participation and assignment and government securities.

The slow growth in the country's financial markets has been ascribed to government debt management strategy in the earlier periods which was not conducive to securities market development. The direct controls imposed in said periods like the ceilings placed on interest rates, exchange controls, the regime of cheap credit policies designed to channel credit to some priority sectors and other forms of financial repressions also hindered the growth and smooth functioning of financial markets.

Nonetheless, financial intermediation grew. The financial intermediation ratio had an uptrend in the 1970-1983. Likewise, developments during the period show some evidence of increased monetisation and financial deepening.

The development of financial institutions and their related services is closely related to economic growth. However, the financial intermediation process has not been optimised as shown by the low values and minimal growth rates of the financial intermediation ratio. The observation is that the imposition of credit and financial policies, labelled by some writers as "financial

repressions", has inhibited the attainment of maximum efficiency in the allocation of resources for investment. Legal ceilings on interest rates which prevailed for more than two decades discouraged savings and the effective mobilisation of savings for investment purposes. Ceilings placed on interest rates have deprived the monetary authorities with a good indicator of the scarcity of financial resources. The allocative element of the rediscount window carried with it an expansionary bias. Aside from artificially cheapening credit for favoured economic activities, banks have become heavily dependent on Central Bank financing. It has also been argued that the cheap credit policy has distorted the choice and pattern of investment in favour of capital-intensive industries, although labor-intensive industries would have been a better alternative.

The move towards financial liberalisation and efforts to strengthen the financial system in the 1980s to promote efficiency, competitiveness and flexibility to meet domestic and international challenges are seen to be in the right direction. However, there should be more fiscal effort and incentives to accelerate the growth of the country's capital market for more effective financial intermediation.

Table 1
NUMBER OF FINANCIAL INSTITUTIONS, 1950-1984

	1950	1960	1970	1971	1972	1973	1974	1975	1976	1977	1978	1979	1980	1981	1982	1983	June 1984
Total ^{1/}	112	488	1542	1668	1778	2784	2850	3550	3942	4067	4364	4745	5057	5421	5569	5810	5955
1. Commercial Banks	107	159	643	691	742	825	896	996	1109	1208	1287	1405	1503	1732	1842	1905	1913
2. Thrift Banks	2	10	138	157	158	180	211	247	391	447	509	589	673	637	676	708	699
a. Savings Banks	2	4	56	59	54	63	76	92	161	184	207	236	268	187	193	209	210
b. PDBS	-	6	54	63	66	72	79	86	98	109	117	130	154	182	203	218	222
c. SLAs	-	-	28	35	38	45	56	69	132	154	185	223	251	268	280	281	267
3. Specialized Gov't Banks	-	1	28	28	31	57	63	67	73	81	84	89	92	116	119	97	98
a. DBP	3	1	27	27	30	56	56	57	57	58	60	65	65	67	67	67	67
b. LBP	-	-	1	1	1	1	2	4	9	14	15	18	18	42	43	21	22
c. PAB	-	-	-	-	-	-	5	6	7	9	9	9	9	9	9	9	9
4. Rural Banks	-	160	507	566	621	660	748	820	887	932	1024	1085	1096	1167	1112	1151	1158
5. Non-Bank Fin. Inst. ^{2/}	-	158	226	226	226	1062	932	1420	1482	1399	1460	1576	1693	1769	1820	1949	2087
a. Investment houses	-	-	N.A.	N.A.	N.A.	9	13	40	43	56	56	57	62	48	52	51	49
b. Finance companies	-	-	N.A.	N.A.	N.A.	164	133	319	348	388	424	478	531	559	537	532	541
c. Investment companies	-	-	N.A.	N.A.	N.A.	17	13	23	59	59	58	63	62	63	66	65	65
d. Securities dealers/brokers	-	-	N.A.	N.A.	N.A.	92	100	117	126	128	130	137	141	142	123	124	126
e. Pawnshops	-	-	N.A.	N.A.	N.A.	370	301	462	472	492	510	544	598	634	693	797	908
f. Fund Managers	-	-	N.A.	N.A.	N.A.	161	133	194	178	9	9	9	12	9	10	12	12
g. Lending Investors	-	-	N.A.	N.A.	N.A.	25	18	38	31	34	40	53	61	78	96	124	140
h. Non-stock savings & loan association	-	-	65	65	65	63	62	67	68	74	75	77	71	74	74	74	74
i. MBLA	-	7	7	7	7	7	7	7	7	7	7	7	7	7	7	7	7
j. Priv. insurance companies	-	147	150	150	150	150	148	149	146	145	143	141	137	136	136	136	136
k. Gov't non-banks	-	4	4	4	4	4	4	4	4	4	4	5	6	6	5	6	6
l. Venture capital corp.	-	-	-	-	-	-	-	-	-	-	-	-	-	8	15	15	17
Money brokers	-	-	-	-	-	-	-	-	-	3	4	5	5	5	6	6	6

^{1/} Consisting of head offices, branches, agencies and extension offices.

^{2/} Data for non-banks from 1973-1974 consist of head offices only.

Table 2

TOTAL ASSETS OF THE PHILIPPINE FINANCIAL SYSTEM

(Million Pesos)

	<u>1950</u>	<u>1960</u>	<u>1970</u>	<u>1975</u>	<u>1980</u>	<u>June 1984</u>
A. Banking Institutions	1,124.0	2,413.1	18,781.2	69,864.3	88,823.0	363,234.0
1. Commercial Banks	1,124.0	2,336.8	14,066.2	53,172.8	138,416.3	267,755.5
2. Thrift Banks	N.A.	18.3	944.5	2,126.5	10,557.6	15,322.3
POBs		0.4	161.0	381.9	1,620.6	4,734.8
Savings & Mortgage Banks	N.A.	12.9	724.4	1,421.9	7,352.4	7,686.9
Stock SLAs	-	-	59.1	322.7	1,584.6	2,900.6
3. Rural Banks	-	4.4	663.7	2,773.3	5,642.2	9,445.1
4. Specialised Banks	N.A.	53.6	3,106.8	11,791.7	34,206.9	70,711.1
DBP	N.A.	53.6	3,106.8	9,644.2	27,979.5	61,659.4
Land Bank	-	-	-	2,095.5	6,071.9	8,786.0
Phil. Amanah Bank	-	-	-	52.0	155.5	265.7
B. Non-Bank Financial Institutions	N.A.	N.A.	6,049.6	26,809.9	58,945.7	94,583.7
5. Investment Houses			4,774.0	4,774.0	8,607.3	7,468.1
6. Finance Companies			3,467.3	3,467.3	11,902.6	10,549.1
7. Investment Companies			1,092.3	1,092.3	4,979.1	4,603.1
8. Security Dealers/Brokers			1,067.3	1,067.3	1,035.5	836.7
9. Pawnshops			89.6	89.6	290.5	518.6
10. Fund Managers			2,609.8	2,609.8	1,658.1	2,873.2
11. Lending Investors			60.9	60.9	50.2	52.6
12. Non-stock SLAs			45.7	86.2	302.2	682.9
13. Mutual Bldg. & Loan Asso.			24.8	25.9	18.7	17.6
14. Private Insurance Cos.			1,669.5	4,224.3	9,997.4	13,715.7
15. Specialised Non-Bank Gov't			4,309.6	9,312.3	20,104.0	55,266.1
GSIS			2,851.9	4,720.7	8,077.1	15,490.6
SSS			1,128.2	2,997.4	9,260.3	17,759.3
ACA			86.1	698.0	496.8	-
Others			243.4	896.6	2,296.8	19,904.2
16. Venture Capital Corp.			-	-	-	112.0
C. Central Bank	969.5	1,948.3	6,003.2	25,974.2	65,447.3	161,662.5
D. Total	2,093.5	4,361.4	30,834.0	122,848.4	313,216.0	619,480.2

Table 3

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ASSETS AND LIABILITIES OF THE CENTRAL BANK

(Million pesos)

	<u>1949</u>	<u>1950</u>	<u>1960</u>	<u>1970</u>	<u>1980</u>	<u>1984(June)</u>
Total Assets	<u>793.6</u>	<u>969.5</u>	<u>1,648.3</u>	<u>6,003.2</u>	<u>65,447.3</u>	<u>162,764.0</u>
International Reserve	460.7	590.8	322.0	1,180.9	23,609.5	11,404.0
Contrib.-IMF	30.0	30.0	30.0	-	-	-
Domestic Securities	92.2	157.6	898.1	2,266.9	4,691.5	9,429.0
Loans & Advances	77.0	48.5	384.5	2,038.7	25,576.8	65,616.0
Account to Secure Coinage	113.3	113.3	98.4	34.5	-	-
Other Assets	20.4	29.3	215.3	482.2	11,569.5	76,315.0
Total Liab. & Networth	<u>793.6</u>	<u>969.5</u>	<u>1,948.3</u>	<u>6,003.2</u>	<u>65,447.3</u>	<u>162,764.0</u>
Total Liabilities	<u>777.1</u>	<u>949.6</u>	<u>1,636.2</u>	<u>5,731.5</u>	<u>64,943.4</u>	<u>162,399.0</u>
Currency Issue	629.9	726.2	1,012.6	2,720.8	12,283.6	21,263.0
Demand Deposits	117.7	208.0	375.3	787.5	21,190.0	48,726.0
International Financial Org.	24.9	2.9	90.0	447.4	7,478.1	64,041.0
Other Liabilities	4.6	12.5	158.3	1,775.8	23,991.7	28,369.0
Total Networth	<u>16.5</u>	<u>19.9</u>	<u>312.1</u>	<u>271.7</u>	<u>503.9</u>	<u>365.0</u>

Table 4

TOTAL LIABILITIES OF THE PHILIPPINE FINANCIAL SYSTEM

(Million Pesos)

	1950	1960	1970	1975	1980	June 1984
A. Banking Institutions						
1. Commercial Banks	1,034.5	2,473.2	16,250.9	63,947.3	169,263.4	336,143.9
2. Thrift Banks	1,034.5	2,052.9	12,593.4	47,997.5	127,709.8	243,964.6
PDBs	8.3	61.6	784.8	1,834.5	9,340.5	13,499.4
Savings & Mortgage Banks	-	-	98.6	294.5	1,309.1	4,040.6
Stock SLAs	8.3	61.6	648.6	1,274.7	6,730.8	7,083.3
Rural Banks	-	-	37.6	265.3	1,300.6	2,375.5
3. Specialised Banks	-	39.6	428.7	2,323.3	4,769.5	7,968.8
DBP	N.A.	319.1	2,442.0	11,792.2	27,443.6	70,711.1
Land Bank	N.A.	319.1	2,442.0	9,044.7	23,032.9	61,659.4
Philippine Amanah Bank	-	-	-	2,095.5	4,308.8	8,786.0
	-	-	-	52.0	101.9	265.7
B. Non-Bank Financial Institutions						
5. Investment Houses	N.A.	N.A.	5,935.5	13,123.8	28,924.5	29,546.7
6. Finance Companies			2,226.3	4,280.0	7,516.6	6,226.3
7. Investment Companies			1,320.2	2,875.4	10,238.3	8,406.5
8. Security Dealers/Brokers			245.3	1,071.1	2,406.8	2,452.6
9. Pawnshops			583.4	846.7	760.9	531.6
10. Fund Managers			19.9	24.1	88.2	162.5
11. Lending Investors			49.8	203.1	156.2	33.4
12. Non-Stock SLAs			6.2	20.3	23.0	20.1
13. Mutual Bldg. & Loan Association			11.8	17.2	71.3	218.4
14. Private Insurance Companies			4.8	5.7	4.8	5.5
15. Specialised Non-Bank Gov't			1,262.7	3,246.4	7,362.5	10,449.8
GSIS	-	N.A.	205.1	533.8	295.9	1,040.0
SSS	-	N.A.	178.9	256.7	242.5	945.9
ACA	-	N.A.	12.0	36.6	53.4	94.1
Others	-	N.A.	14.2	240.5	166.4	-
16. Venture Capital Corp.	-	-	-	-	-	-
C. Central Bank	946.6	1,637.2	5,731.5	5,644.6	64,943.4	161,073.8
D. Total	1,989.4	4,110.4	27,917.9	82,715.7	263,131.3	526,764.4

Table 5

ASSETS AND LIABILITIES OF COMMERCIAL BANKS, 1950-1984

(Million Pesos)

	<u>1950</u>	<u>1960</u>	<u>1965</u>	<u>1970</u>	<u>1975</u>	<u>1980</u>	<u>1981</u>	<u>1982</u>	<u>1983</u>	<u>June 1984</u>
Assets										
Cash & Other Cash Items	52.0	72.8	206.6	645.4	2,044.9	3,261.5	3,209.6	3,052.7	3,884.3	2,928.6
Due from CB & Other Banks	390.6	310.4	500.5	1,349.9	7,239.3	18,416.5	21,253.1	24,930.1	27,656.8	40,203.1
Loans & Discounts	549.4	1,717.9	4,932.6	9,205.7	32,608.8	88,611.2	103,581.3	116,635.5	149,866.5	155,554.4
Investments	77.5	131.9	615.1	1,762.3	6,810.0	13,453.1	15,840.2	20,225.4	21,696.0	25,529.5
Other Assets*	54.5	103.8	476.2	1,102.8	5,099.8	14,674.5	20,999.2	26,373.3	40,055.5	43,539.9
Total	1,124.0	2,336.8	6,731.0	14,066.1	53,172.8	138,416.8	164,883.6	191,225.0	243,150.4	267,755.5
Liabilities										
Demand Deposits	566.9	774.9	1,545.7	2,458.9	6,664.8	13,504.1	14,311.7	11,939.4	19,139.5	16,865.1
Savings Deposits	248.6	714.7	1,402.5	3,757.2	8,951.2	23,011.3	27,016.7	33,444.7	40,939.7	43,913.4
Time Deposits	39.5	242.4	1,053.9	1,469.6	5,130.7	36,114.8	37,933.3	47,846.3	56,147.8	58,014.4
Bills Payable**	10.0	81.2	814.1	1,948.7	18,209.5	32,832.8	44,788.3	47,752.5	61,139.8	67,489.7
Other Liabilities***	169.4	239.5	1,086.5	2,961.0	9,041.1	22,246.8	26,537.2	33,265.8	45,564.1	57,682.0
Capital & Reserves	89.6	284.1	828.3	1,470.7	5,175.5	10,707.0	14,296.4	16,976.3	20,219.5	23,790.9
Total	1,124.0	2,336.8	6,731.0	14,066.1	53,172.8	138,416.8	164,883.6	191,225.0	243,150.4	267,755.5

* Includes premises, furniture, equipment & other real property.

** Includes deposit substitutes.

*** Includes due to banks and officer's and managers checks.

Table 6

TOTAL LOANS OUTSTANDING OF COMMERCIAL BANKS
CLASSIFIED BY INDUSTRY, 1970-MARCH 1984

(Million Pesos)

End of Period	Total	Agriculture Fishery & Forestry	Mining & Quarrying	Manufac- turing	Electricity Gas & Water	Cons- truction	Wholesale & Retail Trade	Transport Storage & Communi- cation	Financing Insurance & Business Services	Real Estate	Community, Social & Personal Services
	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)	(11)
Mar. '84	109,062.6	13,260.5	13,906.8	34,784.3	677.5	6,019.9	13,100.4	4,218.8	13,050.9	4,304.6	5,738.9
Dec. '83	111,387.7	14,790.1	13,145.3	35,409.9	518.5	5,818.1	14,572.9	3,886.0	12,885.9	4,144.5	6,216.5
Sept. '83	108,643.0	12,969.9	10,814.5	36,148.8	771.0	5,518.1	18,439.4	3,412.3	13,908.6	4,198.4	2,462.0
Dec. '82	98,239.6	12,690.9	9,744.5	29,958.3	1,077.2	5,076.0	16,586.6	3,408.1	10,588.5	4,149.6	4,948.9
Dec. '81	86,505.2	11,120.1	7,068.3	26,347.5	975.8	4,049.5	15,560.5	2,786.1	10,620.4	3,808.3	4,168.7
Dec. '80	77,198.1	12,009.7	7,334.3	27,053.3	644.7	2,722.7	11,210.7	1,965.9	7,914.0	2,297.9	4,044.9
Dec. '79	68,264.2	8,120.2	5,507.8	22,104.6	763.6	2,043.6	14,045.6	1,746.4	6,140.5	2,620.4	5,171.5
Dec. '78	54,077.9	5,770.3	3,610.1	17,490.4	314.7	1,556.1	14,155.9	1,084.1	3,299.8	2,041.5	4,755.0
Dec. '77	40,172.9	5,447.6	1,577.5	13,126.4	114.8	386.8	11,830.5	797.8	2,575.7	1,810.5	2,005.3
Dec. '76	N.A.										
Dec. '75	N.A.										
June '74	21,107.3	2,706.2	460.4	9,092.4	142.6	606.7	4,906.8	236.1	938.4	269.8	1,747.9
Dec. '73	17,798.4	2,244.1	235.5	7,074.6	100.6	599.9	4,561.2	245.7	818.3	302.3	1,616.2
Dec. '72	12,427.3	1,774.3	194.5	4,180.2	86.2	473.7	2,719.5	257.6	736.8	272.2	1,732.3
Dec. '71	10,078.4	1,778.9	92.7	3,328.0	39.5	135.5	2,238.1	170.7	573.7	230.7	1,490.6
Dec. '70	8,433.8	1,714.6	45.7	2,776.3	31.9	148.4	1,764.1	140.3	622.8	170.8	1,018.7

Table 7

STRUCTURE OF COMMERCIAL BANKS' CREDIT BY MATURITY

1969-1984

(Per cent Distribution)

<u>Period</u>	<u>Total</u>	<u>Demand</u>	<u>Short-Term</u>	<u>Medium-Term</u>	<u>Long-Term</u>
Credit Granted					
1969	100.0	21.3	77.7	0.7	0.3
1970	100.0	21.4	77.1	1.2	0.3
1971	100.0	19.7	80.0	1.8	0.5
1972	100.0	21.0	75.6	2.3	1.1
1973	100.0	19.5	75.9	1.8	2.8
1974	100.0	26.8	66.7	2.9	3.6
1975	100.0	35.9	62.6	0.9	0.6
1976	100.0	29.6	68.6	0.7	1.1
Credit Outstanding					
1977	100.0	12.6	66.6	10.5	4.3
1978	100.0	16.9	65.1	10.3	7.7
1979	100.0	15.6	55.1	13.8	15.5
1980	100.0	13.5	64.6	10.0	11.9
1981	100.0	12.3	61.1	17.3	9.3
1982	100.0	9.5	59.5	18.1	12.9
1983	100.0	9.5	60.0	15.0	15.5
1984	100.0	7.2	53.5	24.4	14.9

Table 8

STRUCTURE OF INTEREST RATES OF CREDIT EXTENDED BY COMMERCIAL BANKS

1969-1984

	Total	Interest Rate					
		<u>0-4-1/2</u>	<u>5-7</u>	<u>8-10</u>	<u>11-12</u>	<u>13-14</u>	<u>Over</u>
1969	100.0	0.4	9.1	40.8	42.7	6.8	0.2
1970	100.0	0.4	0.5	25.0	60.1	14.0	-
1971	100.0	0.3	0.9	14.3	59.9	24.6	-
1972	100.0	1.0	2.0	13.0	54.3	29.7	-
1973	100.0	7.2	4.4	10.0	53.2	25.2	-
1974	100.0	4.8	1.8	5.6	50.5	37.3	-
1975	100.0	9.9	6.2	9.1	25.8	43.8	5.2
1976	100.0	10.8	3.9	7.0	22.8	48.2	7.3
Credit Outstanding							
1977	100.0	4.1	1.5	7.8	43.2	36.0	7.4
1978	100.0	4.3	0.7	7.8	41.4	39.9	5.9
1979	100.0	4.5	2.5	11.6	35.0	26.9	19.5
1980	100.0	4.9	5.1	12.8	17.8	19.5	39.9
1981	100.0	4.2	2.9	5.2	11.3	20.4	56.0
1982	100.0	3.4	5.2	6.3	10.5	20.5	54.1
1983	100.0	3.0	4.3	4.1	10.6	17.2	60.8
1984 (June)	100.0	2.3	2.2	1.9	10.3	18.8	64.5

Table 9

INSURANCE PREMIUMS OF PRIVATE INSURANCE COMPANIES
(Million Pesos)

<u>Year</u>	<u>(Non-Life)</u>	<u>(Life)</u>	<u>Total</u>
1983	P 3,053.9	P 1,951.9	P 5,005.8
1982	2,798.6	1,995.4	4,794.0
1981	2,713.2	1,710.7	4,423.9
1980	2,550.6	1,489.9	4,040.5
1979	2,264.0	1,315.8	3,579.8
1978	1,922.9	1,093.0	3,015.9
1977	1,700.2	795.3	2,495.5
1976	1,504.1	670.6	2,174.7
1975	1,192.3	609.2	1,801.5
1974	961.1	496.3	1,457.4
1973	699.5	436.2	1,135.7
1972	622.3	364.6	986.9
1971	573.9	313.8	887.7
1970	469.4	273.9	743.3
1965	194.8	410.7	335.5
1960	96.1	85.0	181.1
1955	76.6	46.4	123.0
1950	51.0	31.4	82.4

Source of Basic Data: Office of Insurance Commission.

Table 10

VOLUME OF SECURITIES UNDERWRITTEN
(In Million Pesos)

<u>Year</u>	<u>Debt</u>	<u>Equity</u>	<u>Total</u>
1976	P 577.0	P 230.0	P 807.0
1977	1,897.0	188.3	2,085.3
1978	2,857.7	275.6	3,133.3
1979	1,810.9	154.6	1,965.5
1980	1,298.7	451.1	1,749.8
1981	2,883.8	358.6	3,242.4
1982	4,072.2	348.0	4,420.2
1983	2,647.7	64.6	2,712.3
1984	1,788.4	12.8	1,801.2

Source of Basic Data: Department of Financial Intermediaries

Table 11

FINANCIAL INSTRUMENTS OUTSTANDING IN THE PHILIPPINES

(Million Pesos)

	<u>June 1980</u>	<u>1970</u>	<u>1960</u>	<u>1950</u>
Total	<u>718,400.1</u>	<u>48,586.2</u>	<u>8,168.2</u>	<u>4,400.7</u>
1. Currency in Circulation	18,815.3	2,410.0	952.9	675.0
2. Now Accounts	1.7	-	-	-
3. Deposit Substitutes	25,274.3	-	-	-
4. Foreign Currency Deposits	35,398.3	-	-	-
5. Foreign Securities	343.5	160.6	19.1	N.A.
6. Demand Deposits	58,559.2	3,252.1	1,151.1	793.3
7. Savings Deposits	53,457.3	4,594.1	796.9	255.4
8. Time Deposits	70,920.2	1,808.3	244.9	40.1
9. Insurance Premiums	5,005.8	743.3	181.1	82.4
10. Pension Fund	2,657.5	N.A.	N.A.	N.A.
11. Government Securities	54,943.0	5,233.0	1,484.0	1,065.0 ^{a/}
12. Corporation Bonds	3,886.3	92.7	2.2	N.A.
13. Bank Loans	317,442.4	26,520.7	3,336.0	1,489.5
14. Mortgages	55,695.8	N.A.	N.A.	N.A.
15. Equity Sec./Corp.Stocks	15,999.5	3,414.4	N.A.	N.A.

^{a/} As of 1953

Table 11.1

CLASSIFICATION OF FINANCIAL INSTRUMENTS OUTSTANDING

(Million Pesos)

I. <u>As to Type</u>	June 1984	1970	1960	1950
	<u>718,400.1</u>	<u>48,586.2</u>	<u>8,168.2</u>	<u>4,400.7</u>
Claims	702,400.6	45,171.8	8,168.2	4,400.7
Equity	15,999.5	3,414.4	N.A.	N.A.
II. <u>As to Marketability</u>				
Marketable	<u>144,661.9</u>	<u>11,667.7</u>	<u>972.0</u>	<u>675.0</u>
Claims - FI	79,833.1	2,927.6	972.0	675.0
Claims - NF	58,829.3	5,325.7		N.A.
Equity Securities/Corp.Stock	15,999.5	3,414.4	N.A.	N.A.
Non-Marketable	<u>563,738.2</u>	<u>36,918.5</u>	<u>7,196.2</u>	<u>3,725.7</u>
Fin. Inst.	190,600.0	10,397.8	2,374.0	1,171.2
Non-Fin. Inst.	373.138.2	26,520.7	4,822.2	2,554.5
III. <u>As to Currency Denomination</u>				
Domestic Currency	682,658.3	48,068.6	8,149.1	4,400.7
Foreign Currency	35,741.8	517.6	19.1	-
Total	<u>718,400.1</u>	<u>48,586.2</u>	<u>8,168.2</u>	<u>4,400.7</u>
IV. <u>Money (M1)</u>	<u>31,500.4</u>	<u>4,696.6</u>	<u>1,867.2</u>	<u>1,225.1</u>
Currency	18,815.3	2,410.0	952.9	675.0
D/Ds	12,685.1	2,286.6	914.3	550.1
V. <u>Total Securities (o/s)</u>	<u>59,172.8</u>	<u>5,486.3</u>	<u>1,505.3</u>	<u>1,065.0</u>
Government securities	54,943.0	5,233.0	1,484.0	1,065.0
Corp. bonds	3,886.3	92.7	2.2	N.A.
Foreign securities	343.5	160.6	19.1	N.A.

Table 11.2
CLAIMS AGAINST NON-FINANCIAL UNITS
(Million Pesos)

	<u>June 1984</u>	<u>1970</u>	<u>1960</u>	<u>1950</u>
A. Marketable Instruments	<u>58,829.3</u>	<u>5,325.7</u>	N.A.	N.A.
1. Gov't Securities o/s	<u>54,943.0^{a/}</u>	<u>5,233.0^{a/}</u>	N.A.	N.A.
2. Corp. Bonds	<u>3,886.3</u>	<u>92.7</u>		
B. Non-Marketable Instruments	<u>373,138.2</u>	<u>26,520.7</u>	<u>4,822.2</u>	<u>2,554.5</u>
1. Banks Loans ^{1/}	317,442.4	26,520.7	3,336.0	1,489.5
2. Consumer Credits	N.A.	N.A.	N.A.	N.A.
3. Trade Credits	N.A.	N.A.	N.A.	N.A.
4. Mortgages	55,695.8	N.A.	N.A.	N.A.
5. Government Securities	N.A.	N.A.	1,486.2	1,065.0
C. Total (A plus B)	<u>431,967.5</u>	<u>31,846.4</u>	<u>4,822.2</u>	<u>2,554.5</u>

^{a/} Includes a small holdings of non-marketable securities which is difficult to segregate.

^{1/} Includes consumer credits, trade credits and mortgages.

Table 11.3
CLAIMS AGAINST FINANCIAL INSTITUTIONS
(Million Pesos)

	<u>June 1984</u>	<u>1970</u>	<u>1960</u>	<u>1950</u>
A. Marketable Instruments	<u>79,833.1</u>	<u>2,927.6</u>	<u>972.0</u>	<u>675.0</u>
1. Local Currency	44,091.3	2,410.0	952.9	675.0
Currency in Circulation	18,815.3	2,410.0	952.9	675.0
NOW Accounts	1.7	-	-	-
Deposit Substitutes	25,274.3	-	-	-
2. Foreign Currency	35,741.8	517.6	19.1	-
Deposits	35,398.3	357.0	-	-
Securities	343.5	160.6	19.1	N.A.
B. Non-Marketable Instruments	<u>190,600.0</u>	<u>10,397.8</u>	<u>2,374.0</u>	<u>1,171.2</u>
Demand Deposits	58,559.2	3,252.1	1,151.1	793.3
Savings Deposits	53,457.3	4,594.1	796.9	255.4
Time Deposits	70,920.2	1,808.3	244.9	40.1
Insurance Premiums	5,005.8 ^{a/}	743.3	181.1	82.4
Finance Company Debentures	N.A.	N.A.	N.A.	N.A.
Pension Funds Contributions	2,657.5	N.A.	N.A.	N.A.
C. Total Claims (A plus B)	<u>270,433.1</u>	<u>13,325.4</u>	<u>3,346.0</u>	<u>1,846.2</u>

a/ 1983

Table 12

PERCENTAGE DISTRIBUTION OF LOANS GRANTED BY THE BANKING SYSTEM
CLASSIFIED BY ECONOMIC ACTIVITY

(As of Dates Indicated)

	<u>1960</u>	<u>1965</u>	<u>1973</u>	<u>1981</u>	<u>1982</u>	<u>1983</u>	<u>1984</u> (Jan-Mar)
1. Trade	37.6	38.0	48.5	22.5	20.6	18.5	16.5
2. Services	1.4	1.1	1.3	2.7	3.7	3.1	4.1
3. Banks and Other Financial Institutions	2.5	8.2	12.5	21.9	25.0	26.9	27.1
4. Real Estate	1.5	1.8	2.1	2.1	2.2	2.8	2.6
5. Manufacturing	30.9	29.3	22.5	32.1	28.7	31.1	29.1
6. Mining and Quarrying	1.3	0.7	1.8	4.7	5.2	4.4	5.6
7. Construction	1.6	1.7	0.8	2.6	2.6	2.1	2.2
8. Public Utility	2.3	2.0	1.9	2.2	2.4	2.2	3.5
9. Agriculture, Fishery and Forestry	17.5	15.3	6.5	8.9	9.1	8.0	8.9
10. Consumption	3.4	1.9	2.0	0.3	0.5	0.9	0.4

Table 13

BREAKDOWN OF LIABILITIES OF THE BANKING SYSTEM, 1970, 1980 & 1984
(In Million Pesos)

	Commercial Banks	Rural Banks	Savings Banks	Private Development Banks	Stock Savings and Loan Asso.	Specialized Government Banking	Total Banking System Liabilities
1970							
Total Liabilities	12,595.4	428.7	648.6	98.6	37.6	2,442.0	16,250.9
Deposits	7,685.7	260.4	557.8	70.8	34.2	253.8	8,862.7
Demand	2,458.9	7.7	-	-	-	-	2,466.6
Savings	3,757.2	214.8	502.7	60.9	26.4	25.9	4,587.9
Time	1,469.6	37.9	55.1	9.9	7.8	277.9	1,808.1
Bills Payable	1,948.7	143.2	57.8	24.6	-	1,803.7	3,978.0
Other Liabilities	2,961.0	25.1	33.0	3.2	3.4	384.5	3,410.2
1980							
Total Liabilities	127,709.8	4,769.5	6,730.8	1,309.1	1,300.6	27,443.6	169,263.4
Deposits	72,630.2	2,050.5	5,985.5	779.4	1,097.4	7,821.4	90,364.4
Demand	12,792.0	13.9	162.3	1.9	-	129.1	13,099.2
Savings	23,047.1	1,265.6	3,738.3	429.9	698.0	5,287.3	34,466.2
Time	36,791.1	771.0	2,084.9	347.6	399.4	2,405.0	42,799.0
Deposit Substitutes	12,371.4	-	-	-	-	-	12,371.4
Bills Payable	20,461.4	2,513.1	93.2a/	469.8a/	103.6	16,384.6	40,020.7
Other Liabilities	22,246.8	205.9	652.1	64.9	99.6	3,237.6	26,506.9
1984-June							
Total Liabilities	243,964.6	7,519.0	7,083.3	4,040.6	2,375.5	60,309.1	325,292.1
Deposits	118,792.9	3,360.4	5,903.8	2,379.3	1,866.7	9,370.9	141,674.0
Demand	16,865.1	22.6	94.4	111.6	28.3	174.5	17,296.5
Savings	43,913.4	1,960.4	2,988.9	1,035.8	975.3	2,573.5	53,457.3
Time	58,014.4	1,377.4	2,810.5	1,231.9	863.1	6,622.9	70,920.2
Deposit Substitutes	15,031.4	-	-	-	-	-	15,031.4
Bills Payable	52,458.3	3,740.8	632.3	1,266.8	153.3	38,726.5	96,978.0
Other Liabilities	57,682.0	417.8	547.2a/	394.5a/	355.5	12,211.7	71,608.7

a/ Includes deposit substitutes.

Table 13.1

BREAKDOWN OF LIABILITIES OF NON-BANKS: 1970, 1980 & 1984

(In Million Pesos)

	Securities														Grand Total
	Private Insurance		Investment Houses	Investment Companies	Fund Managers	Finance Cos.	Dealers Brokers	Lending Investors	Pawnshops	Non-Stock SLAs	MBLAs				
	GSIS	SSS													
1970															
Total Liabilities	178.9	12.0	1,262.7	2,226.3	245.3	49.8	1,320.2	583.4	6.2	19.9	11.8	4.8	5,921.3		
Borrowings	-	-	-	2,165.2	169.4	2.4	1,017.8	416.0	5.8	17.3	7.1	1.3	3,802.2		
Short-term	-	-	-	1,689.2	131.8	2.4	929.1	396.0	4.5	17.3	7.1	1.3	3,179.5		
Medium & Long-term	-	-	-	476.0	37.6	-	88.1	20.0	0.8	-	-	0.1	622.7		
Other Liabilities	178.9	12.0	1,262.7	61.1	75.9	47.4	302.4	167.4	0.9	2.6	4.7	3.5	2,119.1		
1980															
Total Liabilities	242.5	53.4	7,362.5	7,576.6	2,406.8	156.2	10,238.3	760.0	23.0	88.2	71.3	4.8	28,983.4		
Borrowings	10.9	0.4	-	6,897.0	1,418.1	145.8	7,694.2	507.0	15.3	71.7	40.9	2.1	16,792.4		
Short-term	-	-	-	5,619.7	835.7	145.6	6,561.2	488.0	10.9	71.7	40.9	2.0	13,776.3		
Medium & Long-term	-	-	-	1,277.3	582.4	0.2	1,133.0	19.0	4.4	-	-	0.1	3,016.1		
Other Liabilities	231.6	53.0	7,362.5	678.6	988.7	10.4	2,544.1	253.0	7.7	16.5	30.4	2.7	12,181.0		
1984															
Total Liabilities	945.9	94.1	10,449.8	6,226.3	2,452.6	33.4	8,406.5	295.0	20.1	162.5	218.4	5.5	29,567.0		
Borrowings	189.6	0.6	-	5,725.8	1,500.7		5,724.0	283.0	15.6	134.4	125.5	1.4	13,724.9		
Short-term	-	-	-	3,666.7	1,230.6		4,695.2	11.0	15.0	134.4	-	1.4	-		
Medium & Long-term	-	-	-	2,059.1	270.1		1,028.8	272.0	0.6	-	92.9	-	-		
Other Liabilities	756.3	93.5	10,449.8	500.5	951.9	33.4	2,682.5		4.5	28.1	-	4.1	15,842.1		

Table 14
FINANCIAL INTERRELATIONS RATIO (FIR)

<u>Year</u>	Total Financial Instruments <u>(million pesos)</u>	Gross Domestic Product <u>(million pesos)</u>	<u>FIR</u>
	(1)	(2)	(1/2)
1950	4,400.7	6,990	.63
1960	8,168.2	14,030	.58
1970	48,586.2	42,450	1.14
1984 June	718,400.1	255,746	2.81

Table 15
FINANCIAL INTERMEDIATION RATIO

	1	2	1/2
	Funds Raised by Non-financial Units Thru Financial Institutions* <u>(million pesos)</u>	Total Funds Raised by Non-Financial Units** <u>(million pesos)</u>	Financial Intermediation <u>Ratio</u>
1980	53,190	78,085	.69
1982	51,335	86,674	.59
1983	95,749	126,001	.76

* Estimated from balance sheets of financial institutions
** Taken from Flow of Funds Accounts

Table 16

INDICATORS OF MONETISATION AND FINANCIAL DEEPENING IN THE PHILIPPINES
1950-1984

<u>Year</u>	<u>M1/GDP</u>	<u>M2/GDP</u>	Currency Issue/ <u>M1</u>	<u>M2/M1</u>	Per Capita <u>Deposits(P)</u>	<u>Banking Density(000)</u>
1950	.17	.21	.55	1.22	4	186
1960	.13	.20	.51	1.51	66	78
1970	.11	.23	.58	2.00	240	24
1975	.09	.17	.54	1.87	650	12
1980	.09	.21	.54	2.46	1,871	9
1981	.08	.22	.58	2.79	2,008	9
1982	.07	.23	.64	3.35	2,064	9
1983	.09	.25	.69	2.95	2,711	9
1984 (June)	.12	.38	.67	3.07	2,548	9

THE FINANCIAL STRUCTURE AND ITS IMPLICATIONS FOR MONETARY POLICY IN SINGAPORE

I. INTRODUCTION

The growth of Singapore's financial structure has largely taken place over the last 15-20 years although its history can be traced to the establishment of the first commercial bank, the Union Bank of Calcutta, in 1840. The early financial system established in the 1850s was rudimentary, comprising a handful of banks which sprang up to meet the needs of the trading port. With the shortage of silver dollar coins, these early banks began the issue of bank notes in 1850, a role which they fulfilled until the establishment of the Currency Board in 1897. The Post Office Savings Bank (POSB) was started in 1877 but did not make much headway in collecting deposits until its revitalisation in 1967. Insurance business dated back to the beginning of Singapore's history, but in those early days it was conducted by business houses. Stockbroking became a significant activity with the rubber boom around the turn of the century. Finance companies sprouted in the 1950s and underwent a consolidation period in the late 1960s. In 1955, the Central Provident Fund (CPF) was established to provide for retirement benefits of workers but the rate of contribution to the Fund accelerated only in the late '70s.

The development of Singapore as a financial centre has an even more recent history dating back to 1968 when the Bank of America established the first Asian Currency Unit. Merchant banks and money broking firms appeared in the 1970s.

The objectives of this study are to assess the development of the financial structure in Singapore and to analyse the implications of the institutional framework on the effectiveness of monetary policy. In view of the foregoing, this study will be based on data from 1970 to 1984. The year 1970 is also a convenient

starting point since it marked the commencement of operations of the Monetary Authority of Singapore.

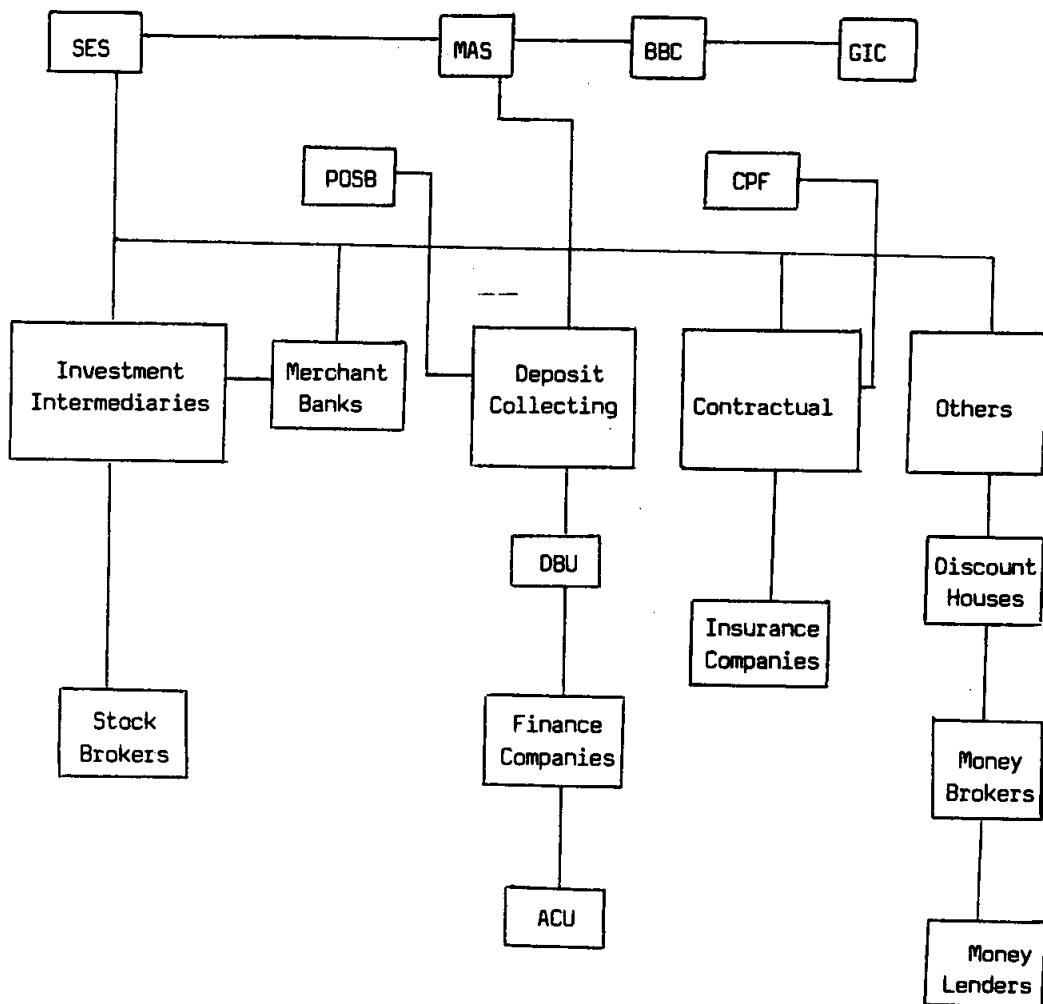
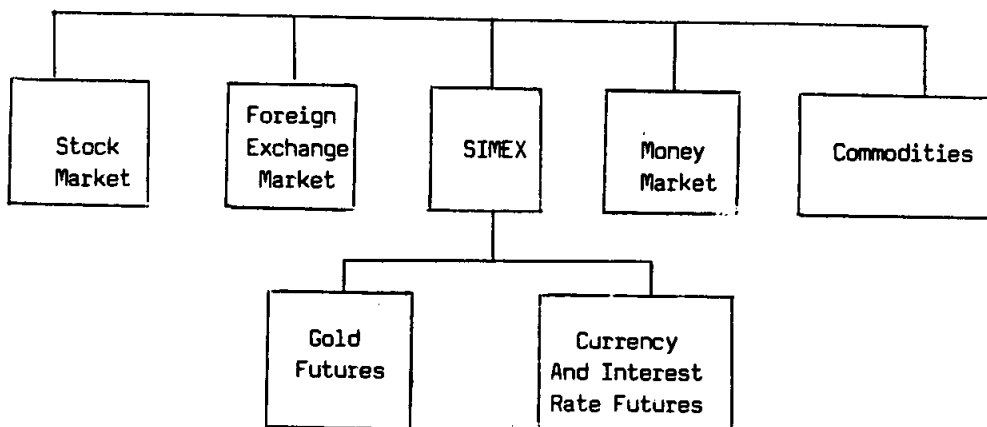
Section II provides a survey of the financial institutions in Singapore and their evolution through time. Section III analyses the financial institutions and instruments quantitatively in various ways. Section IV provides an analysis of monetary and exchange rate policies in Singapore within the general context of Singapore's economy and the particular framework of its financial system.

II. INSTITUTIONS IN THE FINANCIAL STRUCTURE

The structure of the present financial system of Singapore is shown in Chart 1. The Monetary Authority of Singapore (MAS) is the regulatory body of most of the major financial institutions except the Central Provident Fund (CPF) and the Post Office Savings Bank (POSB). The latter two institutions are statutory boards operating within well-delimited areas. The Stock Exchange of Singapore or SES functions as a self-regulatory body of the stockbrokers and works in close cooperation with the MAS and the Securities Industry Council (SIC). ^{1/} The Board of Commissioners of Currency or BCCS performs the currency-issuing function of a central bank. The Government of Singapore Investment Corporation (GIC) performs foreign investment functions for the government.

^{1/} This is an advisory and consultative body, comprising representatives from MAS business which advises the Ministry of Finance and government on matters relating to the securities industry.

THE FINANCIAL SYSTEM OF SINGAPORE

FINANCIAL STRUCTUREMARKETS

The various institutions in the private financial system are classified into the following standard categories:

- 1) deposit-collecting institutions,
- 2) contractual institutions,
- 3) investment intermediaries, and
- 4) others.

At the bottom of the chart are the financial and commodity markets, the latest being the SIMEX- the Singapore International Monetary Exchange which deals in financial futures.

In this study, eleven financial institutions or groups of financial institutions will be dealt with in detail: BCCS, MAS, commercial banks, finance companies, POSB, merchant banks, discount houses, life and general insurance companies, CPF, and Asian Currency Units (ACUs).

The Currency Board

Singapore has always had a Currency Board. So the history of the evolution of the Currency Board is largely co-terminus with the history of the development of the financial system in Singapore. A review of the development of the Currency Board is therefore a good, natural starting point for a survey of the evolution of money, banking and other financial institutions in the country.

Singapore may be said to be on the silver standard prior to the issuance of Currency Board notes in 1899. Silver coins of many varieties, consisting mainly of the Mexican dollar, British trade dollar, Hong Kong dollar, American trade dollar, Peruvian dollar, Spanish dollar and Japanese yen were in wide circulation. They were brought in through trade with Britain, China, India, the Dutch East Indies and Spanish America. As part of the Straits Settlements, Singapore was under the jurisdiction of the East India Company and

then Indian Office until 1867 when it became a British Crown Colony. During the period 1835-67, the Indian silver rupee and subsidiary coins were enforced to be the only legal tender. The rupee did not gain popular acceptance and was used chiefly by the keepers of government accounts. Precious metals were scarce then, and the shortage of silver coins led to the emergence of bank notes from about 1850. Such bank notes were issued by the first banks established in the country, namely, the Asiatic Banking Corporation, Oriental Banking Corporation, Merchantile Bank, Chartered Bank and the Hongkong and Shanghai Banking Corporation. Their notes were backed by bullion and silver dollars.

In 1899, the first official notes were issued by the Board of Commissioners of Currency for the Straits Settlements established under Ordinance VIII of 1897. These Currency Board notes were 100 per cent - 105 per cent backed by foreign exchange reserves, at least two-thirds of which was to be in silver coins and the balance to be invested in approved government securities. Private bank notes were then gradually phased out.

During 1903-06, a currency reform based on the Barbour Plan was instituted. As from February 26, 1906, the parity of 2s 4d to one Malayan dollar had been maintained. The parity was adjusted for the first time in November 1967 to 2s 8.67d to one Singapore/Malaysian dollar following the devaluation of the pound sterling. Thus, Singapore had been on a sterling exchange standard since 1906 until June 25, 1972, when it switched over to the use of the US dollar as its intervention currency and maintained a basic parity rate of US\$1=S\$2.81955.

The success of the Currency Board for the Straits Settlements eventually led to the passing of a Currency Ordinance in 1938, under which the Board was reconstituted to extend its area of operation to the Federated and Unfederated Malay States, including Brunei. After World War II, a Malaya-British Borneo Currency

Agreement was signed in 1950, under which a joint Currency Board was set up for the Federation of Malaya, Singapore, Sarawak, Brunei and North Borneo. The Currency Agreement was revised in 1960, after the achievement of independence for Malaysia (1957) and self-government for Singapore (1959), to make provisions for some amount of judiciary issue, some non-sterling reserves and the withdrawal of individual governments from the Board. Although Bank Negara Malaysia was established in 1959 under the Central Bank Ordinance of 1958, the function of currency issue had remained with the joint Currency Board until 1967.

On June 12, 1967, the joint Currency Board was dissolved, Bank Negara took over the currency issuing function for Malaysia and the Board of Commissioners of Currency in Singapore came into operation in Singapore. However, a currency interchangeability agreement existed under which the Malaysian and Singapore currencies were permitted to circulate freely in both countries. The interchangeability agreement was finally terminated in mid-1973. The BCCS functions in essentially the same way as the old joint Currency Board. The issue of Singapore currency is fully backed by external assets. The BCCS moved off the sterling exchange standard in 1972 when the Singapore dollar was unhinged from the pound sterling and the US dollar was used as the intervention currency. During the transition period ending June 1973, the value of the Singapore dollar was also defined in terms of a gold parity of 0.290299 grammes of fine gold.

The Singapore dollar was floated on June 21, 1973, in the wake of a series of international monetary crises, which caused a continual influx of speculative capital and built up pressure on the Singapore dollar. Full convertibility of the Singapore dollar has been maintained since its floating. The BCCS undertakes to convert Singapore currency into foreign currencies and vice versa, using current market exchange rates.

The assets of BCCS consist of gold, foreign exchange, Treasury bills and securities of foreign governments and international financial institutions. As Table 1 shows, the assets of BCCS have grown steadily over time, and always exceed total currency issued in value. For a small country with meagre natural resources, the Currency Board system has worked to inspire confidence in its currency, and contributed significantly to the maintenance of a stable financial environment required for sustained economic growth.

The Monetary Authority of Singapore (MAS)

The Monetary Authority of Singapore Act was passed in Parliament in November 1970, and the Authority started functioning in January 1971. The principal objects of MAS are:

- (a) to act as banker to, and financial agent of, the government;
- (b) to promote, within the context of the general economic policy of the government, monetary stability and credit and exchange conditions conducive to the growth of the economy;
- (c) to administer the Banking Act 1970, Finance Companies Act 1967, Exchange Control Ordinance 1953, the Insurance Act 1970, Local Treasury Bills Act, Development Loans Act and Money-changing and Remittance Business Act; and
- (d) to provide lender-of-last-resort facilities.

Prior to the establishment of MAS, its powers were exercised and its duties and functions were performed by the Minister of Finance, Accountant-General, Commissioner of Banking, Commissioner for Finance Companies, Controller of Foreign Exchange and Insurance Commissioner within the Ministry of Finance. MAS' powers and functions have evolved and broadened over time. For example, the MAS Act was amended in 1972 to enable the Authority to provide lender-of-

last-resort facilities. The amendment was passed in Parliament just before the establishment of discount houses. The office of the Insurance Commissioner had stayed with the Ministry of Finance until 1977 when it was transferred to MAS. The Money-changing and Remittance Business Act did not come into being until 1979.

As banker to and financial agent of the government, MAS provides current account and deposit facilities to the government. It undertakes to issue, manage and redeem public debt. It acts as manager of government's external loans. It also acts as investment manager of official foreign reserves and foreign assets of some statutory boards. However, as from May 1981, substantial portions of the official foreign reserves have been transferred to and placed under the management of a specialised agent, the Government of Singapore Investment Corporation. Finally, MAS represents the Singapore Government in the International Monetary Fund, and acts as correspondent to other international financial institutions like IBRD and ADB.

As banker to and supervisor of financial institutions such as commercial banks and finance companies, MAS carries out regular inspections of these financial institutions with a view to ensuring capital adequacy and solvency, quality of management and asset structure, and compliance with the Acts and guidelines. It provides banking facilities to commercial banks, finance companies and discount houses. These three groups of institutions keep an account with MAS for the purposes of maintaining statutory cash reserves (minimum cash balances), of inter-bank clearing of cheques, and of recording and clearing of transactions with the Authority and the government.

Finally, MAS plays a critical role in the money market. When the interbank market is tight, discount houses finding themselves in a short position will rediscount their Treasury bills or commercial bills with MAS and/or seek lender-of-last-resort assistance from MAS. The Authority also engages in swap operations to regulate the

liquidity of banks. Another form of MAS' money market operations is the rediscounting of export bills, which has been introduced primarily for the purpose of providing concessionary financing for exports and pre-exports. MAS may influence interest rates in the money market and eventually banks' lending and deposit rates by adjusting its rediscount rate and by varying the Treasury bills issued at its weekly tender.

No less important, perhaps more important, is the role of MAS in promoting the development of Singapore as a financial centre. Promotional efforts consist mainly of creating and regulating new financial institutions, markets and instruments. The streaming of banks into full banks, restricted banks and offshore banks was an innovative move. The creation of the Asian dollar market, licensing and regulation of the Asian Currency Units (ACUs), encouragement of the issue of Asian dollar bonds and floating-rate notes, and the authorisation of the issue of Asian dollar and Singapore dollar negotiable certificates of deposit: all these were part and parcel of the Authority's promotional efforts. MAS was also instrumental in attracting reputable international money brokers to Singapore and in setting up the market for gold futures.

Commercial Banks

The first commercial bank in Singapore was established in 1840, and it was an Indian bank by the name of the Union Bank of Calcutta. The second bank was a British bank by the name of the Oriental Bank, established in 1846. Following in their wake were Mercantile Bank (1856), Chartered Bank (1859), Hongkong and Shanghai Bank (1877), and Nederlandsche Handel-Maatschppij N.V. 'l (1883, now renamed as Algemene Bank Nederland N.V.). In 1902, the First National City Bank of New York (now known as Citibank N.A.) set up office in Singapore. In 1903 the first local bank, the Kwong Yik Bank, was established. The commercial bank is thus the oldest

financial institution in the country. Commercial banks have sprung up since early days to meet the needs of trade, commerce and industry.

As Table 2 shows, there are now a total of 129 banks, which fall into three categories: full banks, restricted banks and offshore banks. The number of full banks is 37 with 250 branch offices. Of the 37 full banks, only 13 are locally incorporated. The remaining 24 are foreign banks. Full banks provide the whole range of banking services such as accepting chequing accounts, savings and fixed-period deposits, extending credit to households and business, opening letters of credit, purchasing or discounting commercial and trade bills, and conducting transactions in foreign exchange.

Restricted banks may conduct the whole range of banking businesses. However, their operations are subject to three restrictions. First, they may not accept time deposits below S\$250,000 per deposit. Second, they may not accept savings deposits. Third, they are not allowed to open branches. The concept of the restricted bank was borne out of the desire to admit more foreign banks of good international repute without creating excessive competition in the domestic banking system. The first restricted bank was granted a licence to operate in Singapore in 1971. There are now a total of 14 restricted banks.

Offshore banks specialise in providing wholesale banking services to non-residents. Prior to the complete liberalisation of exchange control, offshore banks were permitted to carry out domestic banking operations subject to several restrictions: they could accept time deposits of a minimum size of S\$250,000 per deposit, they could not operate savings accounts, and they could grant loans to residents of a minimum size of S\$1 million and of maturity of two or more years and the total credit ceiling was S\$15 million per bank.

After the complete liberalisation of exchange controls in July 1978, offshore banks have been permitted to provide all credit

facilities. However, they are not permitted to accept savings, fixed-period and other interest-bearing deposits. The ceiling on total credit facilities extended by each offshore bank to residents has been raised to S\$30 million. The first offshore bank was admitted in 1973. There are now a total of 78 offshore banks.

All banks have to observe a statutory reserve ratio and hence, maintain cash balances with MAS. While the Banking Act prescribes a legal maximum of 30 per cent, the ratio in force since mid-1975 has been 6 per cent. The banks, too, have to observe a statutory liquidity ratio which has been set at 20 per cent. Under this liquid asset requirement, the first 10 per cent of a bank's total liabilities base must consist of primary liquid assets, which include balances with MAS in excess of the minimum cash balance, notes and coins which are legal tender in Singapore, money at call with discount houses, Treasury bills and other government securities with less than 12 months to maturity. The second 10 per cent must consist of secondary liquid assets which include bills of exchange and government securities of over 12 months to maturity.

Prior to July 1975, the Association of Banks in Singapore, in consultation with MAS, set the common lending and deposit rates for all banks to observe. Since July 1975 when MAS implemented a policy of free and open competition, interest rate determination has been decartelised. Individual banks now quote lending and deposit rates according to their own specific market conditions.

Tables 3 and 3.1 present data which bring out the main characteristics of commercial banks in quantitative terms. Total loans and securities formed an increasing proportion of banks' total assets during 1975-84. The decline experienced in 1981 was the result of world recessionary conditions. While loans and advances increased relatively, portfolios of securities and equities suffered a relative decline during the period. Total deposits, including S\$NCDs issued, constituted the most important source of liabilities. But their share

in banks' total liabilities declined during the period, a reflection of increased dependence on inter-bank funds, and, to a lesser extent, on banks' greater capitalisation. Table 3.1 reveals the increasing share of term loans and the declining shares of the other three forms of financing, namely bills, overdrafts, and trust receipts. Such changes in the loan structure reflected the tendency of banks to provide longer-term financing for industries and property development.

Finance Companies

Finance companies came into existence in the 1950s to meet the demand for small loans, particularly the demand for consumer credit, which grew after several years of post-war peaceful life. They operated under the Companies Act and, unlike banks, were not subject to specific regulations with respect to asset structure, cash management and investment policy. Some finance companies, in pursuit of quick turnovers and high profits, ventured into speculative and risky activities, including those on the stock exchange and property market. Public concern eventually led to the passage of the Finance Companies Act in 1967, the implementation of which in the following year eliminated many which failed to satisfy the stringent requirements of the Act. Out of about 80 finance companies, only 36 passed the test and survived. Over the period 1970-84, finance companies went through a period of adjustment and consolidation, and the process of mergers and closures plus one new entry had brought the total number of finance companies to 34 and the total number of their branch offices to 99 at the end of 1984 (see Table 2).

On the liabilities side, finance companies accept savings and fixed-period deposits from the public. They may not operate chequing accounts. On the assets side, they specialise in the provision of consumer credit: housing loans and hire-purchase finance for motor vehicles and other consumer durables. They are not permitted to engage in speculative investment and to deal in foreign exchange and gold. During the 1970s, competition from banks, POSB and

CPF both in attracting deposits and in the provision of housing loans, the imposition of higher import duties on cars, the raising of maximum interest rates chargeable under the Hire Purchase Regulations, and the effects and aftermath of world recession (1973-75), all worked against the traditional business of finance companies. With the permission of MAS and under its encouragement, finance companies broadened their scope of activities, and branched into lease financing, trade financing (opening letters of credit), bills and account-receivables discounting, and inventory financing. The growth of "other loans and advances," as shown in Table 4, bore evidence of the diversification of financial companies into the provision of these various types of business financing.

Out of the present 34 finance companies, 16 are affiliated with banks. Finance companies compete with banks for deposits by offering high interest rates. In the early 1960s, when all banks had to observe common interest rates, some banks set up their own finance companies to bid for the public's funds. These affiliates of banks have remained although since mid-1975, all banks have been allowed to quote competitive rates.

Under the Finance Companies Act 1967, all finance companies, like all banks, have to observe a statutory reserve ratio and a statutory liquidity ratio. Thus far, they have been required to maintain the same minimum cash balances as banks, viz., 6 per cent of their liabilities base as from mid-1975. However, unlike banks, they have to observe only a one-tier liquid asset ratio, which is 10 per cent.

The Post Office Savings Bank (POSB)

The POSB was established as far back as 1877 under the Postmaster General. Over time, although the number of deposits had increased, total net deposits had stagnated or even declined. In 1967, it was re-vitalised through a campaign to encourage savings,

especially among school-children. In 1972, it was reconstituted and became a statutory board under the Post Office Savings Bank Act 1971. The principal objects of POSB, as spelt out by the Act, are: (a) to provide means for the deposit of savings and to encourage thrift; and (b) to mobilise domestic savings for the purpose of public development.

Apart from the advantage that interest income from POSB deposits is tax-exempt, the POSB has introduced a number of innovations to compete for deposits. It computerised its accounting system and installed on-line banking terminals at all of its many branches. It provides group savings scheme, save-as-you-earn scheme, Giro payment services and safe deposit boxes, etc. In 1974, it started a housing loans scheme through a subsidiary, Credit POSB, for its depositors. During the period 1974-78, it offered a higher interest rate than banks on savings deposits, and succeeded in collecting more deposits than all finance companies as a group in 1977. From a small lethargic thrift institution, the POSB has now grown into a giant in the financial scene. As at the end of 1984, it had nearly 2.7 million savings accounts and it was the depository of more than \$7 billion from the public.

As from 1978, the POSB has adopted a two-tier interest rate system: a higher rate being offered on deposits of \$100,000 or less, and a lower rate on deposits exceeding \$100,000. In compliance with statutory requirements, POSB invests more than 50 per cent of its assets in government securities and loans to statutory boards and government enterprises such as DBS and SIA. It participates in the money market by providing overnight funds to banks and discount houses. With foreign and local partners, it has also set up several joint ventures including a discount house and a merchant bank.

The POSB (Amendment) Act 1984 authorises the POSB to operate chequing accounts, and buy, sell, discount and rediscount bills of exchange, promissory notes and Treasury bills. However, it is not

allowed to grant loans to the private sector. It will, however continue to extend credit to the government, statutory bodies and government enterprises in fulfilment of its objective of mobilising domestic savings for the purpose of public development.

Discount Houses

In 1972, three discount houses were established under the British model. The discount houses are the links between MAS and the financial institutions, mainly the commercial banks. They accept short-term funds from the banks, and, to a much lesser extent, other financial institutions. These funds are the surplus funds which banks place with discount houses on an overnight basis or on call to earn interest. On their part, the discount houses invest these funds in Treasury bills, S\$NCDs, commercial and trade bills, and short-term government securities.

The functions of the discount houses are such that they take an active part in MAS' weekly tenders of Treasury bills. As a matter of principle, they underwrite every issue of Treasury bills. They trade actively in the secondary market for government securities and S\$NCDs, and have become the most active participants in the market. They provide funds to banks by discounting their Treasury bills and trade bills. In discounting trade bills, they finance related business activities indirectly. Such bills constitute about a quarter of discount houses' assets. When the banking system is in a tight liquidity situation, funds may be recalled from the discount houses. The latter may then have to rediscount Treasury bills and trade bills with MAS, or seek lender-of-last-resort assistance from MAS.

There is no formal legislation to govern the behaviour of discount houses. Instead, they operate under the guidelines of MAS. Two important ratios are prescribed in the guideline: the gearing ratio and the asset ratio. The former sets the upper limit on the ratio of discount houses' borrowings to their paid-up capital, which

now stands at 30. The latter sets the lower limit on discount houses' portfolios of government securities as a proportion of their total assets, which now stands at 70 per cent.

The discount houses work closely with MAS in order to maintain maximum confidence in the banking system and to provide maximum flexibility and efficiency in the deployment of funds for banks and other financial institutions.

Merchant Banks

Merchant banks are new entrants in the financial scene in Singapore. The first merchant bank was established in 1970. Many merchant banks operate an Asian Currency Unit, which tends to absorb the bulk of their resources. All merchant banks are registered under the Companies Act. There is no legislation to govern their conduct of business, but approval from MAS is necessary before they become approved merchant banks and hence qualified to apply for an ACU licence. They operate under the guidelines of MAS, which stipulate that a merchant bank may not accept deposits from the public, or issue any promissory notes. However, they may borrow from financial institutions. They may also participate in the interbank market.

Their domestic operations (ACU activities excluded) are such that about a third of their liabilities is borrowings from banks, another one-third borrowings from other financial institutions, mainly finance companies; on the other hand, about a third of their assets is lendings to banks, and about two-thirds is loans and advances to non-bank customers.

The functions of merchant banks are variegated. They arrange or supply loans for business or industry, underwrite or float stocks and bond issues, provide investment and financial advisory services, and deal in gold and foreign exchange. In the area of business credit, the primary function of merchant banks is to arrange

finance, say, in the form of a syndicated loan, rather than supply the loan itself. Thus, the value of the total assets or liabilities of merchant banks tends to be an inadequate indicator of the scope and significance of their activities.

All the merchant banks in Singapore are multinationals. Many of them are joint ventures between financial institutions of different nationalities, and a handful are joint ventures between foreign and Singapore partners.

Insurance Companies

As at the end of 1984, there were 82 insurers in Singapore, with six specialising in life insurance and 69 conducting general insurance business only. The remaining seven insurers undertook both types of business. The relatively large number of insurers has much to do with the history of the development of insurance business in Singapore, which may be said to date as far back as the founding of the port. Since the beginning of Singapore's history, British trading houses had acted as agents for insurance companies in UK to provide cover for marine hazards. Until the Insurance Act of 1966 came into effect, any unincorporated company established in the UK before 1862 which had been carrying on insurance business may do so. In fact, any company registered under the Companies Act and any co-operative society registered under the Co-operative Societies Act in Singapore may carry on insurance business. Since the Insurance Act was enforced in 1967, only those insurers registered under the Act may continue in the business. Since 1970, a process of consolidation has set in, phasing out many small and inefficient companies. At the same time, efforts have been stepped up to attract reputable international insurers who can contribute to the development of the industry, particularly those in the field of specialised risks and offshore business. Tax concessions are offered for offshore reinsurance business.

The two most important provisions of the Insurance Act of 1966, as modified by two orders of 1967, are (a) the establishment of the Singapore life insurance fund and general insurance fund, into which all receipts, including investment income, arising from policies in Singapore must be paid, and out of which only expenses attributable to the operation of these policies may be met; and (b) the prescription of asset ratios which require that at least 75 per cent of the life insurance fund must be held in authorised assets with at least 20 per cent in government securities, and that at least 55 per cent of the general insurance fund must be held in authorised assets with a minimum of 15 per cent in government securities.

Over the past one and a half decades, the rapid growth of POSB and CPF savings has tended to blunt the incentives to the public to purchase life insurance covers, especially endowment policies.

The Central Provident Fund (CPF)

The Central Provident Fund (CPF) was established in 1955 with a view to providing retirement benefits to employees at the age of 55. Since 1968, the CPF has undergone many significant changes to become a major financial institution. Significant changes have taken place with respect to both the sources and the uses of funds.

As regard the sources of funds, the past one and a half decades have witnessed increased contributions to the CPF. The scheme is funded by employees and employers, equally for most of the years. The combined monthly contribution started off at a modest 10 per cent of the employee's wage or salary. In 1968, the rate of contribution was raised by 3 percentage points to enable CPF members to accumulate sufficient balances for the purchase of Housing and Development Board (HDB) flats. It was further raised many times in subsequent years. As from mid-1984, the combined contribution rate of the employer and employee has been raised to a high level of 50 per cent of the employee's pay. Another cause of the growth of the CPF balances was

the expansion in employment resulting from rapid economic growth. The number of CPF members was 180,000 in 1955. It rose to a million in 1974, and stood at 1.9 million in 1984 - a ten-fold increase in 28 years. A third cause of the growth of CPF balances was the sustained wage and salary increments under the National Wages Council's guidelines implemented since 1972.

With respect to the uses of funds, many liberalisation measures have been adopted since 1968. The first use of CPF balances permitted before a member's retirement is the purchase of HDB flats. Over time, the provision has been extended to include the purchase of all other public-sector flats, i.e., those built by the Jurong Town Corporation, Housing and Urban Development Corporation and Ministry of Defence, and, finally, to include private residential property as well. The second use of CPF balances is the purchase of Singapore Bus Service shares, up to a maximum of \$5,000 per member. The third use is the payment of premiums for a mortgage reducing insurance policy with respect to public sector flats. The fourth use is the payment of premiums for a CPF life insurance policy. Finally, 6 per cent of a member's balances has been set aside as a Medisave account, out of which hospital bills and other medical expenses may be met.

With these liberalised uses of CPF balances notwithstanding, the total annual withdrawals from the Fund for all reasons, including retirement and purchase of flats, forms only about one-third of the total annual gross contributions. The balance of two-thirds remains with CPF as an important part of domestic savings. Net CPF balances were \$9 million in 1955. They shot up to nearly \$5 billion in 1977, and then to about \$23 billion at the end of 1984. In compliance with statutory requirements, more than 90 per cent of the net CPF balances is invested in government securities, almost exclusively in those with maturity of 10 to 15 years. On the average, CPF absorbs about 90 per cent of the net annual issue of government domestic debt.

ACUs and ADM

The Asian Dollar Market (ADM) based in Singapore is essentially an international money and capital market, where foreign currency funds are transacted. The Asian dollars transacted in the market are United States dollars and currencies other than the Singapore dollar. The main feature of the market is the predominance of interbank activity. Transactions with non-bank customers are also largely of a short-term nature while dealings in longer term bonds although increasing, are negligible when compared to the overall size of the market. Credit extension in the form of loans syndication has, however, been growing in importance.

While several financial centres in Europe participate in the Euro-currency market, London is regarded as the main centre and is more widely identified with the market. Similarly in Asia, although Asian dollar-type transactions are also undertaken by operators in other centres including Tokyo and Hong Kong, the Asian Dollar Market is more closely associated with Singapore. The development of the Asian Dollar Market in Singapore has been fostered by the authorities through conscious policy efforts to create an environment conducive to its growth.

An ACU is a book-keeping unit within a bank or merchant bank which has been granted approval by MAS to operate in the ADM: to accept deposits and make loans in US dollars and other foreign currencies. Prior to the complete liberalisation of exchange control in June 1978, ACUs' transactions with Singapore residents were subject to various exchange control restrictions. But after June 1978, ACUs may freely accept time and call deposits from and lend to residents as they do to non-residents, provided these transactions are in currencies other than the Singapore dollar. ACUs are governed by the Banking Act and regulated by the guidelines of MAS. However, they are exempted from having to maintain minimum cash balances and statutory liquid assets. To pave the way for the establishment of the ADM, the

withholding tax on interest paid to non-residents on their foreign-currency deposits with banks was abolished in August 1968. In November the same year, the first approval was given to a foreign bank to operate an ACU. As at the end of 1984, nine local banks, six foreign full banks, all the 14 restricted banks, all the 78 offshore banks, and 53 merchant banks were licensed to operate an ACU.

Table 5 presents statistical data on the ADM. The size of the market increased at a fast pace, from less than US\$ 400 million in 1970 to US\$128 billion in 1984. While interbank funds form the bulk of ACUs' assets and liabilities, loans to non-bank customers increased from some 4 per cent in 1970 to 26 per cent in 1984. On the other hand, deposits of non-bank customers constituted about 15 per cent to 18 per cent of the sources of funds, except for an initial year like 1970. Asian dollar loans, viewed as an asset or liability of an ACU, are mostly short to medium term, with 70 per cent to 80 per cent being of less than one-year maturity. ACUs perform a limited degree of positive maturity transformation, borrowing short and lending long, and thereby creating new liquidity.

An important instrument in the ADM is the Asian dollar bond. An Asian dollar bond is a bond managed by an Asian institution and listed on the Stock Exchange of Singapore. It is an instrument whereby borrowers may raise medium-and long-term funds in the ADM. The first Asian dollar bonds, valued at US\$10 million, were issued in 1971. Up till the end of 1984, the number of such bond issues totalled 132 and the total cumulative value of these bonds was US\$6,497 million (see Table 5.1).

ACUs may issue fixed-rate or floating rate US dollar negotiable certificates of deposits (US\$NCDs) after consultation with MAS.

Money Brokers

International money brokers are an integral part of Singapore's financial system as it becomes internationalised to serve the needs of the region and the world. The first of such brokers was admitted in 1971. As at the end of 1984, there were a total of eight international money brokers. With their global contacts and communication system, they put Singapore in touch with all financial centres in the world. Their presence upgrades the quality and efficiency of foreign-exchange operations in the country. MAS supervises international money brokers by way of guidelines. Present guidelines require that the brokers (a) should not deal on their own account, (b) should deal only with banks and not with non-bank customers, and (c) should be adequately staffed with people of high professional standards and provide local employees with proper training.

Stock Exchange of Singapore (SES)

The Stock Exchange of Singapore was formed in June 1973. Its predecessor was the joint Stock Exchange of Singapore and Malaysia. Transactions in shares of joint-stock companies have had a long history and took place even before the turn of the 20th century. But sharebroking did not become an activity of significance until the rubber boom in 1910. After the Wall Street crash in 1929, brokers found it necessary to come together to formulate rules and regulations to govern their conduct of business. Thus, in June 1930, the Singapore Stockbrokers Association was formed with 15 founder members.

As at the end of 1984, there were 25 member companies and 108 stockbroking members of the Exchange, and the total number of listed companies amounted to 308 with a paid-up capital of \$207 billion and a market capitalisation of \$262.1 billion. Government securities and Asian dollar bonds are listed on the SES. With the relaxation of exchange control regulations in June 1973, non-residents

can buy or sell securities listed on SES without having to seek prior approval. There is also no restriction on the remittance of money out of Singapore on the sale of securities.

OVERALL VIEW

This part will now—put the pieces together to form a coherent whole. Only those pieces which are important to subsequent analysis are put together in Tables 1, 1.1, 1.2 and 2. Out of a complex of many institutions and dimensions, common denominators are required to build up an overall picture. The common denominators chosen here are firstly, numbers — numbers of members within a group, say, of banks or finance companies, and secondly, assets — dollar values of the total assets of various groups of financial institutions. An analysis of particular types of financial assets is held over for the next section. In the meanwhile, numbers and assets will be used to obtain an indication of the relative importance of 11 groups of financial institutions and of their changes over time.

Table 2 shows the number of full banks, restricted banks, offshore banks, finance companies, merchant banks, ACUs and other financial institutions. It also shows the number of branches of full banks, finance companies and POSB. It is the considered view of MAS that there are sufficient financial institutions in existence catering to the domestic needs. Hence, it has in effect declared a moratorium on the licensing of full banks and finance companies. However, the number of branches of banks and finance companies increased at a controlled pace. On the other hand, the number of offshore banks and ACUs, which operate mainly in offshore markets, rose rapidly. The POSB, functioning independently under its own Act, enjoyed a four-fold increase in the number of branches. The total number of financial institutions, excluding branches but including CPF, BCCS and MAS, was 441 at the end of 1984.

Table 1 presents values of assets of the 11 groups of financial institutions. The grand total of all assets rose by a factor of 45 during 1970-84. While banks' assets increased eleven-fold, ACUs' assets jumped by a factor of 200. Thus the growth of ACUs in terms of assets had dwarfed the growth of all other institutions except merchant banks. The percentage distribution of financial institutions by assets and its changes over the period are given in Table 1.1. The dominance of ACUs is an unmistakable indication of the increased openness of Singapore's financial system and of Singapore's success as a financial centre for the region and the international community.

For purposes of an analysis of the financial system vis-a-vis the domestic economy, and of an analysis of domestic monetary policy, it may be desirable to exclude ACUs. Thus, excluding ACUs from Table 1, the percentage distribution of assets is obtained as in Table 1.2. It is seen here that banks had retained their dominant position although their relative importance was declining. Finance companies suffered a relative decline. The POSB was on the ascent and had caught up with finance companies as a group. Merchant banks rose fast to take second place in the hierarchy. The CPF rose steadily to occupy third place. Both life and general insurance companies experienced a relative decline in terms of assets.

Table 1.2 may still be misleading for purposes of analysing monetary or financial policy in relation to the domestic economy. For example, CPF lends exclusively to the government and the impact of its credit policy differs from that of banks. Merchant banks (excluding their ACUs) lean rather heavily on borrowings from and placements with banks, and the size of their total assets may not provide a good gauge of the impact of their activities on domestic credit and liquidity conditions. Therefore, even if one abstracts from structural changes in the use of funds, the size of assets of a given institution relative to that of the others may be inadequate for analysis. In the

next section, discussion shall move into many more dimensions of the financial structure of Singapore.

III. FINANCIAL STRUCTURE, FINANCIALISATION AND FINANCIAL INTERMEDIATION

In this section, the financial structure of Singapore is analysed in greater detail from a quantitative angle. The relative importance of the financial structure, the degree of financialisation and financial intermediation in the economy is evaluated using two main measures: the marginal rate of financialisation (MRF) and the financial intermediation ratio (FIR).

The MRF is defined as the ratio of the annual change in financial assets to the Gross Domestic Product (GDP). ^{2/} This ratio provides an indication of the degree of financialisation of the economy. The greater the ratio, the greater the extent to which economic agents turn to the market, with all its range of financial institutions and financial instruments, to place their surplus funds or to obtain their needed financial resources. A high MRF sustained over time necessarily implies the growth of the financial sector relative to the real sector.

The financial intermediation ratio (FIR) as introduced by Goldsmith is "the extent to which the issues of domestic non-financial and of foreign issues are absorbed or held by domestic financial institutions rather than by domestic non-financial sectors or by foreigners, particularly by domestic households. It is this

^{2/} This ratio is comparable to Goldsmith's financial interrelations ratio which is obtained by dividing the total stock value of all financial assets by the total value of tangible assets plus net foreign balance, i.e., the national wealth.

relation which reflects the degree of institutionalisation in the country's financial structure Statistically, the financial intermediation is determined in the flow dimension as the ratio of the net acquisition during a given period by domestic financial institutions of instruments issued by domestic non-financial sectors and by the rest of the world to total issues of such instruments." 3/ In this study, given the lack of data on net total primary issues, a proxy has to be used. The proxy is the sum of gross domestic capital formation and the annual change in consumer credit provided by financial institutions.

The significance of the FIRs lies in the important role played by financial intermediaries in a modern monetary economy. Economic agents in such an economy may be classified into deficit and surplus units according to whether their total expenditures exceed or fall short of their current incomes. Deficit units have to finance their excess expenditures externally by new security issues, which are referred to as primary securities by Gurley and Shaw. 4/

The term primary securities is thus defined very broadly to embrace not only securities in the standard usage such as bonds and equities, but also mortgages, business loans and consumer credit of various sorts. Primary securities may be sold either to the surplus units directly, or to financial institutions. In the former case, funds flow from the ultimate lenders to the ultimate borrowers, and no financial intermediation has taken place. This is a case of financialisation without financial intermediation. In the latter

3/ Raymond Goldsmith, Financial Structure and Development, p. 317.

4/ John G. Gurley and Edward S. Shaw, Money in a Theory of Finance (Washington, D.C.: The Brookings Institution, 1960), especially Chapter VI.

case, financial institutions purchase primary securities (make a loan). They do so with funds obtained by the issue of indirect securities - currency, demand deposits, savings deposits, fixed-period deposits and various forms of deposit-equivalents. The holders of such deposits are the ultimate lenders from whom funds flow to the ultimate borrowers through the intermediation of financial institutions.

Thus, the principal function of financial intermediaries is to purchase primary securities from the ultimate borrowers on the one hand, and to issue indirect securities to the ultimate lenders, on the other. Benefits of financial intermediation arise from specialisation and exploitation of economies of scale, which make for a reduction in unit costs of portfolio management, and a reduction in risks through the diversification of portfolios. These benefits are eventually passed on to the borrowers in the form of favourable interest payments. In the absence of markets for external finance, every economic agent would maintain a balanced budget, and the surplus units may invest only in tangible assets. Under such an arrangement, the opportunities and incentives to save and invest would be extremely limited. When direct external financing is made possible, surplus units respond to opportunities and incentives and save more. With the introduction of financial intermediaries, a wide variety of markets and instruments come into being which encourage savings and raise the savings rate; and, similarly, a wide array of markets and instruments are also developed to meet the requirements of deficit units and to distribute funds among competing investment opportunities. The distinct advantage of financial intermediation is the efficiency with which savings are mobilised and funds are allocated among alternative uses. Efficiency offered by financial intermediation tends to raise both savings and investment rates and expedites the process of economic growth.

In what follows, the percentage distributions, MRFs and FIRs for a range of financial assets will be analysed across eleven types

of financial institutions and four non-financial sectors. The range of financial assets include currencies, deposits and deposit-equivalents, housing loans, hire-purchase finance, business loans and advances, shares and bonds, government securities, foreign securities and equities. The four non-financial sectors are: household, business, government and the rest of the world (ROW). For present purposes, the government sector excludes statutory boards and quasi-government bodies, which are treated as part of the business sector.

Total Financial Assets

Table 6 sets out the financial assets for the period 1970-1984. The left-hand panel of the table presents all forms of credit provided by all financial institutions to the four non-financial sectors: household, business, government and rest of world. Credit is defined to include loans and advances, bills purchased or discounted, hire purchase, and holdings of securities and equities. The right-hand panel consists of three entries:

- i) Total claims of the non-financial sectors on financial institutions, which are deposits and deposit-equivalents placed with all financial institutions. The two deposit-equivalents are net CPF balances due to members and the Singapore life insurance fund;
- ii) The amount of government securities held by the non-financial sectors; and
- iii) Amount of shares, bonds, debentures and loan stocks held by the non-financial sectors.

Tables 6.2 and 6.3 show that the MRF and FIR for all financial assets have generally been on a rising trend between the mid-'70s to 1982. The estimated value of the MRF increased from 54 per cent in 1975 to 73 per cent in 1982 whilst the estimated FIR rose

from 136 per cent to 153 per cent over the same period. The increase in the two ratios is not as dramatic as would have been expected from the proliferation of financial institutions and growth of the financial structure detailed in Section II. However, growth of the financial system since the 1970s has been, to a large extent, in offshore ACU operations. Further, given the dominance of foreign multinationals in Singapore's industries, their business operations are partly financed from abroad, for example through intercompany accounts.

Over this period, the MRF and FIR in respect of financial assets of both the financial sector and non-financial sector grew. Thus, each sector roughly maintained their share in total financial assets (Table 6.1).

The FIR for the total primary securities held by the financial institutions, especially in respect to claims against business, showed a general uptrend from the mid-'70s indicating a deepening of the financial intermediation process in Singapore.

The non-financial sector's MRFs with respect to total deposits and holdings of shares and bonds also went up. But their MRFs with respect to government securities fell, reflecting the declining attractiveness of government securities with their low yields relative to those of other financial assets. Government securities are held mainly by financial institutions to meet statutory requirements. The share of government securities in total financial assets held by financial institutions increased from 10 per cent in 1974 to 14 per cent in the early 1980s but their share in the non-financial sector's claims declined to less than 1 per cent (Table 6.1).

Over 1983-84, both the MRF and FIR for all financial assets slipped. This can be partly explained by the accelerated drawdown of deposits with the CPF for purchase of houses. This acquisition of

real assets by the household sector was not only reflected in the drop in the MRF and FIR with respect to their deposits with the CPF. Financial institutions also substantially increased housing loans as supplementary financing to households, as reflected in the increase in MRF and FIR for their claims against households during those two years. Besides this factor, there was also a substantial inflow of foreign capital funds through the non-monetary sector during those two years, leading to the drop in MRF and FIR with respect to financial institutions' claims to business, after substantial increases in the immediate preceding years.

Claims of Non-financial Sector: Indirect Securities

Table 7 shows the deposits and deposit-equivalents placed by the non-financial sectors with all the financial institutions. These financial assets are referred to as indirect securities by Gurley and Shaw.

There has been a gradual increase in foreign currency deposits over the years but S\$ deposits still account for the bulk of indirect securities. There was a relative fall in currency and bank deposits. Deposits with POSB and net CPF balances however increased relatively as well as absolutely. These trends reflect the rapid growth of POSB after its reconstitution in 1972 and of the CPF since 1968.

Within bank deposits, there has been, in recent years, a shift away from non-interest earning deposits on current accounts to interest bearing deposits especially savings deposits. Financial innovations like autosave accounts, ATMs, credit cards, daily interest rate accrual have facilitated and encouraged the use of saving accounts with banks, finance companies and the POSB, for transaction as well as for precautionary and income maximising purposes. This trend is likely to continue with the shift to a cashless society and

the introduction of EFTPOS (electronic funds transfer at point-of-sale).

The MRFs and FIRs in Tables 7.2 and 7.3 confirmed this pattern of growth in indirect securities.

Claims of Financial Institutions or Primary Securities

Table 8 shows the outstanding claims of the various types of financial institutions on the four non-financial sectors. As shown, total credit to households (consumer credit) formed the smallest fraction of the grand total in each year. Total credit to the business sector took up the largest fraction of the grand total followed by the government sector and the foreign sector (ROW).

Whilst credit from banks and POSB to the household sector, consisting entirely of housing loans, increased as a proportion during the period, such loans by finance companies, the most important suppliers of consumer credit, did not increase. This trend is confirmed by the MRFs and FIRs. The observed increase in the MRF and FIR with respect to total consumer credit was due mainly to the increase in housing loans extended by banks and POSB. Commercial banks used to show an aversion to consumer credit and housing loans were negligible in their asset portfolios. However, when the POSB introduced a housing loan scheme and set up Credit POSB to handle it, commercial banks, under the pressure of competition began to take a more favourable approach towards housing loans. The sluggish growth in the demand for business loans during 1974-78 may well have been yet another important cause of bankers' changed attitude towards consumer credit. Finance companies used to specialise in supplying consumer credit and provided the bulk of loans to the household sector in two main forms: housing loans and hire purchase finance for motor vehicles and other consumer durables. With the pressure of competition from POSB and the banks and faced with a shrinking market

in hire-purchase finance for motor cars, they diversified into other activities.

Finance companies' share of total claims of the financial sector on the business sector has doubled to 4 per cent between 1970 and 1980, as they widened their scope of operations into term loans, leasing, account receivables financing and inventory financing. As a result, their MRF and FIR with respect to business credit rose. Merchant banks, as new arrivals on the scene, made their presence felt through an aggressive business-loans policy. Their MRF and FIR displayed an uptrend over time and are an underestimation of their intermediation role as these ratios do not include off-balance sheet activities of merchant banks like providing guarantees, fund management, arranging loan syndication, etc. However, the bulk of business loans still came from the commercial banks and their MRFs and FIRs in respect of business loans, picked up after 1978.

The MRFs and FIRs with respect to government securities showed no significant trend across all financial institutions except the CPF. The uptrend for CPF holdings reflected the expansion in employment, wage increases and upward revisions of CPF contribution rates.

Claims on the foreign sector by financial institutions showed a slowdown in relative terms over the period.

Financial Sector's Claims: Loans, Bills and Securities

Table 9 divides the primary securities into the three major types of instruments: loans and advances, bills and securities. Tables 9.1, 9.2 and 9.3 set out the percentage distribution, MRFs and FIRs for these three instruments classified by type of financial institutions, respectively.

It is seen that total loans and advances increased as a proportion of the grand total whilst bill financing and securities have fallen in relative terms. The share of loans in total credit granted by the financial sector grew from 31 per cent in 1970 to 43 per cent in 1984. Except for insurance companies, all the three ratios in respect of loans and advances showed an uptrend for all the financial institutions.

In terms of securities and equities, the three ratios of all the financial institutions except the CPF, did not register any distinct uptrend.

Total Primary Securities by Financial Institution

Table 10 shows the total portfolio of primary securities held by the major financial institutions. As shown in Table 10.1, the relative share of banks in total primary securities has dropped slightly from 45 per cent in 1970 to 41 per cent in 1984. This occurred as a result of the more rapid expansion of newer institutions like the merchant banks, discount houses, finance companies besides the POSB and the CPF.

However, the MRF and FIR ratios for banks in Tables 10.2 and 10.3 in respect of their total primary securities had actually increased over the same period. Whilst the MRF and FIR for CPF were on the increase, that for the POSB did not exhibit any consistent trend because of the slowdown in its growth since 1979.

Marketable and Non-marketable Instruments

Finally, this section concludes with an analysis of total financial assets in terms of marketable versus non-marketable instruments. This can be analysed in terms of claims of the non-financial sector against financial institutions and claims of the community against the non-financial sectors.

Claims against financial sector. Non-financial sectors' claims against financial institutions may be classified into marketable and non-marketable instruments. The former comprises currency and S\$NCDs. The latter consists of deposits and deposit equivalents including the Singapore life insurance fund and net CPF balances (Tables 11 and 11.1). It is seen from Table 11.1 that the share of total marketable instruments has been halved since 1970, and that of non-marketable instruments has risen to account for 93 per cent of total claims against financial institutions. At the level of individual instruments, currency, bank deposits and deposits with life insurance fund have suffered a relative decline. Bank deposits however still accounted for the biggest single share of 38 per cent of total claims. Deposits with the CPF have risen to account for 1/3 of total non-financial sector's claims against the financial sector by end-1984. Deposits with the POSB have also risen in relative terms whilst finance companies have more or less maintained their share. The MRFs and FIRs in Tables 11.2 and 11.3 confirmed the above trends.

Claims against non-financial sector. As laid out in Table 12, marketable claims against the non-financial sector consists of government securities, shares bonds, debentures and loan stocks, commercial and trade bills and foreign securities. Non-marketable instruments held by financial institutions are loans and advances (excluding bills) extended directly to the household, business and foreign sectors. Table 12.1 reveals a relative fall in total marketable instruments, particularly government securities and bills. On the other hand, the shares of total non-marketable instruments, viz., loans and advances increased.

IV. EFFECTIVENESS OF MONETARY AND EXCHANGE RATE POLICIES

The foregoing sections have shown that, apart from the rapid internationalisation of the financial system over the last one and a

half decades, there has been increased financialisation and deepening financial intermediation in Singapore.

Increased financialisation means the channelling of financial resources through formal organised markets and institutions whose activities may be more rapidly monitored, supervised and regulated. Monetary policy may vary or re-direct the flow of these financial resources by changing the rules of the markets or institutions, by re-shaping this conduct or by introducing changes to the cost and returns on their operations.

Increased financial intermediation coupled with a fractional reserve regime implies a magnification of the impact of monetary policy. A credit multiplier greater than unity transmits and amplifies an expansionary or contractionary policy by a multiple factor in the desired direction. In the ultimate analysis, the effectiveness of the given policy depends on what the market participants perceive to be their appropriate portfolio balances in relation to the changed cost and yield conditions which are partly induced by policy.

Difficulties would arise if some of the financial intermediaries were not under the control of the same central monetary authority. For them, the response of the non-controlled institutions and markets may be such as to vitiate the intended effects of a given policy. In Singapore, all major financial institutions with obvious exceptions, function under laws administered by or guidelines issued by MAS. Policies impinging on these institutions can therefore be harmonised. The obvious exceptions referred to above are the CPF and POSB which operate fairly independently of MAS in well-delimited areas and are unlikely to fall foul of the pursuit of any given monetary policy.

In fact, the CPF, and the large proportion of savings that it harnesses, serves to give the MAS greater control over liquidity in the financial system. Contributions to the CPF, at a gross rate of 50 per cent of income, exert a persistent contractionary impact on liquidity. The bulk of CPF savings is placed with MAS as advance deposits and is used for subscription to government securities. The MAS, as banker to both the CPF and the Government, thus has control over money market liquidity through this pool of CPF funds which is generally recycled into the system.

Difficulties would also arise if there were impediments to the effective workings of competitive market forces. For example, in the US, where ceilings on banks' deposit rates were imposed under Regulation Q, deposit rates, disintermediation occurred in boom times. With the decartelisation of interest rate determination since mid-'75, the financial system in Singapore has moved towards one of free and open competition.

However, two major structural factors inhibit the use of traditional monetary policy measures in Singapore:

- i) the openness of the economy and financial system; and
- ii) the relatively underdeveloped capital market.

As mentioned earlier, although financial intermediation has increased over the years, Singapore's economy is an open one, dominated by foreign multinational companies with recourse to foreign financing. Thus during the inflationary period of early 1973, traditional monetary measures designed to stem the inflow of 'hot money' attracted by exchange and capital gains were largely not successful, until the S\$ was floated.

A second problem concerns the insulation of the domestic economy from the offshore activities of financial institutions operating in Singapore. Since 1978, there has been no exchange control barrier between residents and the offshore market. In the context of free capital mobility, the trend in domestic interest rate is largely determined by external interest rates. Too low a domestic rate relative to external rates could encourage outflow of deposits, depending on exchange rate expectations. In view of Singapore's openness and the potential disrupting influence of capital flows, the MAS has taken steps to limit the internationalisation of the Singapore dollar, so as to maintain control over domestic liquidity.

The presence of the ACUs whose deposits are not subject to liquidity requirement, also enable banks to circumvent the statutory requirements on these domestic liabilities through 'round-tripping' operations. In the simplest form, this involves booking a resident's deposit with the DBU, as a deposit with the bank's ACU and making a corresponding accounting entry to show a net interbank borrowing by the DBU from the ACU, which is not subject to reserve requirement. This practice, discovered and stamped out in recent years, poses a potential problem to the effectiveness of adjusting reserve requirements.

Further, open market operations are hampered by the relatively undeveloped capital market in government securities. As noted in Section III, the market for government securities is mainly a captive market with the CPF and financial institutions holding the government securities to meet statutory requirements and generally keeping them till maturity. Because of this and their low yield relative to other assets, secondary trading in them is thin although growing in recent years.

V. CONCLUSION

Summing up, it can be seen that the centrepiece of demand management in Singapore rests on the fiscal and financial policy of the government, institutionalised essentially in the CPF. Monetary policy in the broad sense, plays a complementary, usually, accommodating role and operates mainly through the exchange rate.

The policy emphasis on the exchange rate stems from the consideration of Singapore's openness and other structural factors described in the previous section which hampers the use of money or interest rate targetting. Given the contractionary effect of CPF contributions as well as the budgetary surpluses of the government,

foreign exchange interventions by MAS have generally tended to moderate the appreciation of the Singapore dollar and inject liquidity into the banking system, thereby increasing the money supply to meet the needs of the economy. The money supply is therefore a result of the exchange rate policy.

Further, the exchange rate is being managed more as an instrument to cushion the economy against imported inflation. Due to the high import content of Singapore's exports and other elements of final demand, import prices are a major determinant of the costs of production and costs of living. A strong Singapore dollar keeps down domestic prices of imports and lowers the cost of production and cost of living. Other things being equal, a low cost of living anchors money wages without undermining real wage levels. Low money wages in turn, contribute to the stability of the domestic component of costs of production and help maintain the competitive edge of exports.

However, the use of the exchange rate policy does not totally obliterate the role of monetary policy. Money market assistance, in the form of overnight loans and export bill rediscounting, is still provided. Swap arrangements are used to help

banks tide over short run liquidity difficulties and at times, to soften or reinforce the intended effects of exchange rate policy. The rediscount rate can also be used to impact on interbank overnight rates and subsequently on other market rates. However, the rediscount window is relatively small. MAS can also use its lender-of-last-resort facility to regulate liquidity. Credit control and selective credit guidelines were also used once during the inflationary period in 1973 and early 1974, before the onset of recession made the controls redundant. Finally, the MAS has also had recourse to using moral suasion.

Table 1
ASSETS OF FINANCIAL INSTITUTIONS

Year	All											\$ Million
	Institutions	Banks*	Finance Companies	POSB	Discount Houses	Merchant Banks*	Life Insurers	General Insurers	CPF	ACUs	BCCS	
1970	8,952.2	5,041.6	521.1	72.3	0.0	0.0	164.5	90.0	833.8	1,193.3	774.2	261.4
1971	12,932.9	6,062.9	705.7	91.8	0.0	0.0	185.9	107.4	1,081.0	2,996.7	905.6	795.9
1972	22,052.9	8,182.7	867.7	127.1	126.6	0.0	221.1	137.0	1,401.9	8,391.4	1,105.2	1,492.2
1973	33,478.1	10,648.9	1,155.6	173.9	370.3	0.0	251.8	172.7	1,859.6	15,605.7	1,228.3	2,011.3
1974	47,064.9	12,282.9	1,392.4	275.5	436.0	1,422.3	284.1	212.4	2,509.5	23,946.1	1,509.3	2,794.4
1975	60,030.2	14,416.6	1,430.4	568.2	493.7	1,839.7	337.1	250.1	3,346.3	31,361.2	1,874.1	4,112.8
1976	78,153.7	16,526.8	1,607.3	1,027.2	552.7	2,656.7	387.4	299.8	4,208.6	42,613.0	2,231.0	6,043.2
1977	90,154.8	18,238.0	1,761.2	1,642.5	618.5	2,463.9	445.4	325.1	5,096.7	49,151.3	2,527.7	7,884.5
1978	107,495.0	21,218.3	2,017.3	2,114.3	684.7	3,746.7	505.0	392.1	6,127.5	58,501.3	2,933.8	9,254.0
1979	146,185.1	26,747.8	2,472.8	2,664.8	763.6	8,378.4	585.1	437.3	7,652.1	82,393.3	3,244.3	10,845.1
1980	193,753.6	33,316.1	3,075.1	2,951.6	949.5	13,299.6	705.1	527.8	9,694.0	113,870.9	3,583.1	11,780.8
1981	274,875.3	44,630.7	4,275.4	3,502.2	1,603.8	19,279.6	834.7	684.4	12,310.6	175,650.5	3,722.1	8,381.3
1982	339,275.0	48,537.2	5,357.4	5,326.9	2,050.5	22,020.4	998.8	797.7	15,865.8	217,799.0	4,776.9	15,744.4
1983	374,095.3	56,537.8	6,523.8	6,597.9	2,248.0	23,625.0	1,196.5	873.3	19,763.8	237,928.2	4,968.5	13,832.5
1984	433,334.0	65,707.2	7,239.6	7,759.4	2,563.0	25,844.9	1,384.2	899.4	23,025.2	278,903.1	5,381.5	14,626.5

* Excluding their ACUs.

Source: MAS

Table 1.1

ASSETS OF FINANCIAL INSTITUTIONS: PERCENTAGE DISTRIBUTION

Year	All Institutions \$m	Finance			Discount		Merchant		Life		General		CPF	ACUs	BCCS	MAS
		Banks*	Companies	POSB	Houses	Banks	Insurers	General	Insurers	General	Insurers					
1970	8,952.2	56.3	5.8	0.8	0.0	0.0	1.8	1.0	9.3	13.3	8.6	2.9				
1971	12,932.9	46.9	5.5	0.7	0.0	0.0	1.4	0.8	8.4	23.2	7.0	6.2				
1972	22,052.9	37.1	3.9	0.6	0.6	0.0	1.0	0.6	6.4	38.1	5.0	6.8				
1973	33,478.1	31.8	3.5	0.5	1.1	0.0	0.8	0.5	5.6	46.6	3.7	6.0				
1974	47,064.9	26.1	3.0	0.6	0.9	3.0	0.6	0.5	5.3	50.9	3.2	5.9				
1975	60,030.2	24.0	2.4	0.9	0.8	3.1	0.6	0.4	5.6	52.2	3.1	6.9				
1976	78,153.7	21.1	2.1	1.3	0.7	3.4	0.5	0.4	5.4	54.5	2.9	7.7				
1977	90,154.8	20.2	2.0	1.8	0.7	2.7	0.5	0.4	5.7	54.5	2.8	8.7				
1978	107,495.0	19.7	1.9	2.0	0.6	3.5	0.5	0.4	5.7	54.4	2.7	8.6				
1979	146,185.1	18.3	1.7	1.8	0.5	5.7	0.4	0.3	5.2	56.4	2.2	7.4				
1980	193,753.6	17.2	1.6	1.5	0.5	6.9	0.4	0.3	5.0	58.8	1.8	6.1				
1981	274,875.3	16.2	1.6	1.3	0.6	7.0	0.3	0.2	4.5	63.9	1.4	3.0				
1982	339,275.0	14.3	1.6	1.6	0.6	6.5	0.3	0.2	4.7	64.2	1.4	4.6				
1983	374,095.3	15.1	1.7	1.8	0.6	6.3	0.3	0.2	5.3	63.6	1.3	3.7				
1984	433,374.0	15.2	1.7	1.8	0.6	6.0	0.3	0.2	5.3	64.4	1.2	3.4				

Table 1.2

ASSETS OF FINANCIAL INSTITUTIONS: PERCENTAGE DISTRIBUTION*

Year	All Institutions \$m	Finance		Discount		Merchant		Life		General		CPF	BCCS	MAS
		Banks	Companies	POSB	Houses	Banks	Insurers	Insurers	General	Insurers	General			
1970	7,758.9	65.0	6.7	0.9	0.0	0.0	2.1	1.2	1.2	10.7	10.0	3.4		
1971	9,936.2	61.0	7.1	0.9	0.0	0.0	1.9	1.1	1.1	10.9	9.1	8.0		
1972	13,661.5	59.9	6.4	0.9	0.9	0.0	1.6	1.0	1.0	10.3	8.1	10.9		
1973	17,872.4	59.6	6.5	1.0	2.1	0.0	1.4	1.0	1.0	10.4	6.9	11.3		
1974	23,118.8	53.1	6.0	1.2	1.9	6.2	1.2	0.9	0.9	10.9	6.5	12.1		
1975	28,669.0	50.3	5.0	2.0	1.7	6.4	1.2	0.9	0.9	11.7	6.5	14.3		
1976	35,540.7	46.5	4.5	2.9	1.6	7.5	1.1	0.3	0.3	11.8	6.3	17.0		
1977	41,003.5	44.5	4.3	4.0	1.5	6.0	1.1	0.8	0.8	12.4	6.2	19.2		
1978	48,993.7	43.3	4.1	4.3	1.4	7.6	1.0	0.8	0.8	12.5	6.0	18.9		
1979	63,791.8	41.9	3.9	4.2	1.2	13.1	0.9	0.7	0.7	12.0	5.1	17.0		
1980	79,882.7	41.7	3.8	3.7	1.2	16.6	0.9	0.7	0.7	12.1	4.5	14.7		
1981	99,224.8	45.0	4.3	3.5	1.6	19.4	0.8	0.7	0.7	12.4	3.8	8.4		
1982	121,476.0	40.0	4.4	4.4	1.7	18.1	0.8	0.7	0.7	13.1	3.9	13.0		
1983	136,167.1	41.5	4.8	4.8	1.7	17.4	0.9	0.6	0.6	14.5	3.6	10.2		
1984	154,430.9	42.5	4.7	5.0	1.7	16.7	0.9	0.6	0.6	14.9	3.5	9.5		

* Excluding ACUs.

Table 2

NUMBER OF FINANCIAL INSTITUTIONS AND BRANCH OFFICES^{1/}

Year	Banks				Finance Companies				POSB				Life General		ACUs Stock		Money Brokers		All Institutions ^{3/}
	Full Banks		Restrict- ed Banks	Off- shore Banks	No. HQs		No. Bran.	Discount Houses	Merchant Banks	Insurance ^{2/}	Insurance ^{2/}	Brokers	Brokers	Brokers	Brokers	Brokers			
	No. HQs	No. Bran			No. HQs	No. Bran.													
1970	37	139	0	0	37	35	34	42	0	2	15	72	16					181	
1971	36	150	6	0	42	36	39	44	0	2	15	71	21	n.a.				191	
1972	36	153	8	0	44	36	43	47	3	8	15	72	24				2	208	
1973	35	158	12	7	54	36	46	51	3	17	15	73	46	19			4	264	
1974	36	169	12	14	62	36	51	56	4	20	16	66	56	19			4	273	
1975	37	173	12	21	70	36	55	62	4	21	16	62	66	19			5	282	
1976	37	178	12	23	72	34	58	65	4	22	17	61	69	19			5	284	
1977	37	184	13	27	77	34	60	75	4	23	17	61	78	19			5	295	
1978	37	190	13	31	81	34	59	84	4	27	16	64	85	19			6	309	
1979	37	199	13	39	89	34	62	98	4	33	16	64	101	20			7	333	
1980	37	212	13	47	97	34	66	105	4	37	15	65	115	21			7	352	
1981	37	219	13	58	108	35	83	107	4	41	16	69	131	24			7	381	
1982	37	239	13	68	118	35	97	109	4	47	16	74	150	25			9	414	
1983	37	244	14	71	122	34	98	122	4	51	13	75	159	25			8	424	
1984	37	250	14	78	129	34	99	131	4	54	13	76	172	25			8	441	

Notes: 1/ CPF, BCCS and MAS not listed.

2/ An insurance company which carries on both types of business counts as one life insurer and one general insurer.

3/ Defined by functions and include CPF, BCCS and MAS.

Source: MAS

Table 3
COMMERCIAL BANKS: KEY RATIOS^{1/}

	Loans and Securities			Total Deposits ^{2/}
	Total	Securities & Equities	Loans & Advances	
1975	64.3	10.0	54.3	56.5
1977	66.3	10.5	55.8	51.1
1979	67.5	7.7	59.8	47.4
1981	62.6	6.1	56.5	45.7
1983	68.0	7.8	60.2	47.3
1984	62.8	6.7	56.1	43.1

Notes: ^{1/} All ratios are percentages of total assets/liabilities.
^{2/} Including total S\$NCDs issues.

Source: MAS, Quarterly Bulletin and Monthly Statistical Bulletin.

Table 3.1

COMMERCIAL BANKS: LOAN STRUCTURE

	Total Loans & Advances	Bills Financing	Overdrafts	Trust Receipts	Term Loans
1975	100.0	16.9	48.0	11.5	23.5
1977	100.0	23.1	39.9	10.9	26.1
1979	100.0	24.6	39.0	11.0	25.4
1981	100.0	15.8	41.0	10.6	32.7
1983	100.0	11.5	45.4	9.0	34.2
1984	100.0	11.2	43.8	8.7	36.3

Source: MAS, Quarterly Bulletin and Monthly Statistical Bulletin.

Table 4

FINANCE COMPANIES: KEY RATIOS*

	Loans and Advances				Securities and Equities	Total Deposits
	Total	Housing Loans	Hire- Purchase Finance	Others		
1975	62.7	24.8	13.4	24.5	2.7	73.3
1977	66.8	24.5	14.7	27.6	4.0	74.1
1979	73.9	22.3	21.5	30.1	4.5	73.3
1981	74.6	17.9	20.9	35.8	2.7	68.8
1983	80.9	17.9	13.9	49.1	2.1	70.0
1984	79.1	18.6	11.5	49.0	2.3	72.9

* All ratios are percentages of total assets/liabilities.

Sources: MAS, Quarterly Bulletin and Monthly Statistical Bulletin.

Table 5

ASSETS AND LIABILITIES OF ACUS

	US\$m			
	1970	1978	1983	1984
Total Assets	389.8	27,040.1	111,860.9	128,054.7
Loans to non-bank customers	13.9	6,376.8	30,384.6	33,766.1
Interbank funds	370.2	19,829.7	74,446.8	85,329.0
in Singapore	13.1	866.6	2,791.4	3,832.1
inter-ACUs	) 357.1	3,718.9	19,690.0	21,862.5
outside Singapore	) —	15,244.2	51,965.4	59,634.4
Other assets	5.7	833.6	7,029.5	8,959.6
Total Liabilities	389.8	27,040.1	111,860.9	128,054.7
Deposits of non-bank	243.7	3,600.0	20,619.9	21,523.6
Interbank funds	141.0	21,987.2	84,743.4	100,186.5
in Singapore	5.7	1,442.5	1,787.7	2,943.2
inter-ACUs	) 135.3	3,719.1	19,697.9	21,866.5
outside Singapore	)	16,825.6	63,257.8	75,376.8
Other Liabilities	5.1	1,452.9	6,497.8	6,344.6

Sources: MAS, Quarterly Bulletin and Monthly Statistical Bulletin.

Table 5.1

ASIAN DOLLAR BOND ISSUES, 1971-1983

Year	Number of issues	Value of issues	Maturity of issues (US\$m)	
			Up to 7 years	Over 7 years
1971	1	10	-	10
1972	2	51	-	51
1973	3	70	-	70
1974	-	-	-	-
1975	3	47	32	15
1976	9	266	206	60
1977	14	368	293	75
1978	12	403	294	109
1979	8	358	200	158
1980	18	659	444	215
1981	12	1,238	535	703
1982	16	1,018	421	597
1983	16	1,145	596	549
1984	8	864	275	589*

Source: MAS

* Includes issue of \$150m 7 & 15 years bonds.

TABLE 6

FINANCIAL ASSETS

(S\$M)

	CLAIMS OF FINANCIAL INSTITUTIONS				CLAIMS OF NON-FINANCIAL SECTOR				
	C R E D I T		T O		REST OF WORLD	TOTAL	DEPOSITS	GOVT SECURITIES	SHARES & BONDS
	TOTAL	HOUSEHOLD	BUSINESS	GOVT					
1970	N.A.	8090.8	166.5	2895.3	1634.5	N.A.	5110.9	382.1	N.A.
1971	N.A.	10295.3	212.9	3456.6	2215.9	N.A.	6138.8	518.1	N.A.
1972	N.A.	12974.2	298.2	4581.8	2753.3	N.A.	7803.4	729.9	N.A.
1973	N.A.	16507.2	447.9	6820.5	2924.1	N.A.	9674.7	833.5	N.A.
1974	35474.3	18996.6	524.7	7827.1	3597.7	16477.7	11534.6	924.7	4018.4
1975	42642.0	22188.0	563.9	8937.5	4618.9	20454.0	13945.7	1079.2	5429.1
1976	49845.2	26013.6	672.7	10219.9	6039.1	23831.6	16654.2	1276.0	5901.4
1977	60836.9	29796.7	742.4	11331.3	7532.9	31040.2	18994.3	1597.3	10448.6
1978	67069.5	36399.4	852.0	13888.5	8680.0	30670.1	22240.2	2012.6	6417.3
1979	80222.1	43863.3	1151.9	17694.8	10303.0	36358.8	27157.9	2093.5	7107.4
1980	97578.3	53132.6	1508.7	23009.0	12667.7	44445.7	33771.3	2001.8	8672.6
1981	121191.1	64737.9	1862.2	30322.3	15477.9	56453.2	41604.5	1660.3	13188.4
1982	146324.6	77553.3	2064.7	36625.2	19214.9	68771.3	51714.8	1515.5	15541.0
1983	172225.1	91281.1	2837.6	43511.2	23654.2	80944.0	61039.0	1377.3	18527.7
1984	193012.1	101391.8	3566.0	46753.2	26834.9	91620.3	68013.0	1242.4	22364.9

TABLE 6.1

FINANCIAL ASSETS : PERCENTAGE DISTRIBUTION

	CLAIMS OF FINANCIAL INSTITUTIONS					CLAIMS OF NON-FINANCIAL SECTOR				
	C R E D I T					T O				
	GRAND TOTAL	TOTAL	HOUSEHOLD	BUSINESS	GOVT	REST OF WORLD	TOTAL	DEPOSITS	GOVT SECURITIES	SHARES & BONDS
1974	100.1	53.6	1.5	22.1	10.1	19.9	46.4	32.5	2.6	11.3
1975	100.0	52.0	1.3	21.0	10.8	18.9	48.0	32.7	2.5	12.7
1976	100.0	52.2	1.3	20.5	12.1	18.2	47.8	33.4	2.6	11.8
1977	100.0	49.0	1.2	18.6	12.4	16.7	51.0	31.2	2.6	17.2
1978	100.0	54.3	1.3	20.7	12.9	19.4	45.7	33.2	3.0	9.6
1979	100.0	54.7	1.4	22.1	12.8	18.3	45.3	33.9	2.6	8.9
1980	100.0	54.5	1.5	23.6	13.0	16.3	45.5	34.6	2.1	8.9
1981	100.0	53.4	1.5	25.0	12.8	14.1	46.6	34.3	1.4	10.9
1982	100.0	53.0	1.4	25.0	13.1	13.4	47.0	35.3	1.0	10.6
1983	100.0	53.0	1.6	25.3	13.7	12.4	47.0	35.4	0.8	10.8
1984	100.0	52.5	1.8	24.2	13.9	12.6	47.5	35.2	0.6	11.6

TABLE 6.2

FINANCIAL ASSETS : MRFS

CLAIMS OF FINANCIAL INSTITUTIONS										CLAIMS OF NON-FINANCIAL SECTOR			
GRAND TOTAL	C R E D I T T O					REST OF WORLD	TOTAL	DEPOSITS	GOVT SECURITIES	SHARES & BONDS			
	TOTAL	HOUSEHOLD	BUSINESS	GOVT									
1971	N.A.	32.3	0.7	8.2	8.5	14.9	N.A.	15.1	2.0	N.A.			
1972	N.A.	32.8	1.0	13.8	6.6	11.4	N.A.	20.4	2.6	N.A.			
1973	N.A.	34.6	1.5	21.9	1.7	9.5	N.A.	18.3	1.0	N.A.			
1974	N.A.	19.8	0.6	8.0	5.4	5.8	N.A.	14.8	0.7	N.A.			
1975	53.6	23.9	0.3	8.3	7.6	7.6	29.7	18.0	1.2	10.5			
1976	49.4	26.2	0.7	8.8	9.7	7.0	23.2	18.6	1.4	3.2			
1977	68.8	23.7	0.4	7.0	9.4	6.9	45.1	14.7	2.0	28.5			
1978	35.1	37.2	0.6	14.4	6.5	15.7	-2.1	18.3	2.3	-22.7			
1979	64.3	36.5	1.5	18.6	7.9	8.5	27.8	24.0	0.4	3.4			
1980	71.5	38.2	1.5	21.9	9.7	5.1	33.3	27.2	-0.4	6.4			
1981	82.4	40.5	1.2	25.5	9.8	3.9	41.9	27.3	-1.2	15.8			
1982	79.1	40.3	0.6	19.8	11.8	8.1	38.8	31.8	-0.5	7.4			
1983	73.2	38.8	2.2	19.5	12.6	4.6	34.4	26.4	-0.4	8.4			
1984	53.5	26.0	1.9	8.3	8.2	7.6	27.5	17.9	-0.3	9.9			

TABLE 6.3

FINANCIAL ASSETS : FIRS

	CLAIMS OF FINANCIAL INSTITUTIONS				CLAIMS OF NON-FINANCIAL SECTOR			
	C R E D I T		T O		TOTAL	DEPOSITS	GOVT SECURITIES	SHARES & BONDS
	TOTAL	HOUSEHOLD	BUSINESS	GOVT				
GRAND TOTAL				REST OF WORLD				
1971	N.A.	1.7	20.1	20.8	36.4	N.A.	36.8	N.A.
1972	N.A.	2.5	32.7	15.6	27.1	N.A.	48.4	N.A.
1973	N.A.	3.6	53.9	4.1	23.5	N.A.	45.1	N.A.
1974	N.A.	1.4	17.8	11.9	12.9	N.A.	32.8	N.A.
1975	135.9	0.7	21.0	19.4	19.3	75.4	45.7	26.7
1976	121.0	1.8	21.5	23.9	17.0	56.7	45.5	7.9
1977	193.0	1.2	19.5	26.2	19.5	126.6	41.1	79.9
1978	91.8	1.6	37.7	16.9	41.1	-5.5	47.8	-59.4
1979	148.7	3.4	43.0	18.3	19.6	64.3	55.6	7.8
1980	152.9	3.1	46.8	20.8	10.9	71.3	58.3	13.8
1981	179.2	2.7	55.5	21.3	8.6	91.1	59.4	34.3
1982	173.4	1.4	43.5	25.8	17.8	85.0	69.8	16.2
1983	153.4	4.6	40.8	26.3	9.7	72.1	55.2	17.7
1984	110.0	3.9	17.2	16.8	15.7	56.5	36.9	20.3

Table 7

INDIRECT SECURITIES

SINGAPORE-DOLLAR CURRENCY AND DEPOSITS														S\$m
GRAND TOTAL	SUB- TOTAL	DEPOSITS WITH BANKS OF WHICH				DEPOSITS WITH FINANCE COMPANIES OF WHICH				LIFE INSURANCE FUND	CPF	FOREIGN CURRENCY DEPOSITS WITH BANKS		
		TOTAL	CURRENCY	DEMAND	FIXED	SAVINGS	TOTAL	FIXED	SAVINGS					POS8
1970	5110.9	5110.9	681.9	3014.3	947.7	1818.3	412.9	400.0	1818.3	412.9	72.7	777.5	0.0	
1971	6138.8	6138.8	806.0	3514.7	1082.9	2167.8	480.4	553.1	504.3	16.1	91.2	987.9	0.0	
1972	7803.4	7745.5	1004.8	4395.2	1557.4	2550.2	602.8	683.2	621.1	19.7	125.2	1316.0	57.9	
1973	9674.7	9581.5	1114.4	5419.4	1786.2	3264.8	708.5	853.8	779.0	25.7	170.9	1770.7	93.2	
1974	11534.6	11403.9	1306.4	6100.2	1806.5	4000.3	738.5	1031.1	966.3	26.0	268.5	2413.7	130.7	
1975	13945.7	13752.0	1637.7	6945.5	2111.1	4565.9	890.6	1048.4	965.2	36.1	548.4	3234.9	193.7	
1976	16654.2	16365.8	1946.8	7778.3	2378.2	5062.4	999.2	1191.2	1115.1	43.9	996.0	4066.1	288.4	
1977	18994.3	18722.3	2242.6	8185.9	2513.9	5328.3	1069.5	1305.4	1221.5	50.6	1589.0	4954.0	272.0	
1978	22240.2	22027.6	2582.8	9419.4	2732.1	6045.3	1211.2	1510.0	1419.2	55.5	2029.0	5981.4	212.6	
1979	27157.9	26799.2	2941.2	11419.9	3244.3	7473.0	1394.8	1812.3	1691.2	62.8	2525.2	7515.5	358.7	
1980	33771.3	33301.1	3137.0	15029.9	3484.0	10788.4	1692.5	2121.2	1961.7	65.1	2756.7	9551.2	470.2	
1981	41604.5	40979.7	3381.8	18405.3	4441.0	13315.4	2168.1	2942.2	2728.4	75.9	3265.9	12149.8	624.8	
1982	51714.8	50943.5	3996.0	21523.3	4781.4	15619.7	2917.4	3711.5	3304.7	112.3	5058.4	15655.5	771.3	
1983	61039	60106.1	4335.3	24264.6	4982.7	17099.6	4079.9	4564.1	3979.7	171.8	6240.9	19504.7	932.9	
1984	68013.0	66991.5	4619.2	25752.1	4856.7	18191.5	4870.1	5278.3	4655.4	209.2	7287.3	22670.4	1021.5	

Table 7.1

INDIRECT SECURITIES : PERCENTAGE DISTRIBUTION

SINGAPORE-DOLLAR CURRENCY AND DEPOSITS

GRAND TOTAL	SUB- TOTAL	CURRENCY	DEPOSITS WITH BANKS OF WHICH			DEPOSITS WITH FINANCE COMPANIES OF WHICH				LIFE INSURANCE		FOREIGN CURRENCY DEPOSITS WITH BANKS	
			TOTAL	DEMAND	FIXED	SAVINGS	TOTAL	FIXED	SAVINGS	POSB	FUND	CPF	
1970	100.0	7.9	34.8	10.9	21.0	4.8	4.6	4.2	0.1	0.8	1.9	9.0	0.0
1971	100.0	7.8	33.8	10.4	20.9	4.6	5.3	4.9	0.2	0.9	1.8	9.5	0.0
1972	100.0	7.6	33.4	11.8	19.4	4.6	5.2	4.7	0.1	1.0	1.7	10.0	0.7
1973	100.0	6.9	33.4	11.0	20.1	4.4	5.3	4.8	0.2	1.1	1.6	10.9	0.1
1974	100.0	6.8	32.0	9.5	21.0	3.9	5.4	5.1	0.1	1.4	1.5	12.7	1.4
1975	100.0	7.3	30.8	9.4	20.3	4.0	4.7	4.3	0.2	2.4	1.5	14.4	1.7
1976	100.0	7.4	29.6	9.1	19.3	3.8	4.5	4.2	0.2	3.8	1.5	15.5	1.4
1977	100.0	7.7	28.1	8.6	18.3	3.7	4.5	4.2	0.2	5.4	1.5	17.7	1.0
1978	100.0	7.7	27.9	8.1	17.9	3.6	4.5	4.2	0.2	6.0	1.5	17.7	1.3
1979	100.0	7.2	27.8	7.9	18.2	3.4	4.4	4.1	0.2	6.2	1.4	18.3	1.4
1980	100.0	6.1	29.0	6.7	20.8	3.3	4.1	3.8	0.1	5.3	1.4	18.5	1.5
1981	100.0	5.3	28.6	6.9	20.7	3.4	4.6	4.2	0.1	5.1	1.3	18.9	1.5
1982	100.0	5.1	27.4	6.1	19.9	3.7	4.7	4.2	0.1	6.4	1.3	20.0	1.5
1983	100.0	4.7	26.6	5.5	18.7	4.5	5.0	4.4	0.2	6.8	1.3	21.4	1.5
1984	100.0	4.6	25.5	4.8	18.0	4.8	5.2	4.6	0.2	7.2	1.4	22.5	1.5

Table 7.3

INDIRECT SECURITIES : FIRS

SINGAPORE-DOLLAR CURRENCY AND DEPOSITS

	DEPOSITS WITH BANKS OF WHICH			DEPOSITS WITH FINANCE COMPANIES OF WHICH				LIFE INSURANCE			FOREIGN CURRENCY DEPOSITS WITH BANKS			
	GRAND TOTAL	SUB- TOTAL	CURRENCY	TOTAL	DEMAND	SAVINGS		TOTAL	FIXED	SAVINGS		POSB	FUND	CPF
						FIXED	SAVINGS							
1971	36.8	36.8	4.4	17.9	4.8	12.5	2.4	5.5	5.0	0.2	0.7	0.8	7.5	0.0
1972	48.4	46.7	5.8	25.6	13.8	11.1	3.6	3.8	3.4	0.1	1.0	1.0	9.5	1.7
1973	45.1	44.2	2.6	24.7	5.5	17.2	2.5	4.1	3.8	0.1	1.1	0.8	11.0	0.9
1974	32.8	32.1	3.4	12.0	0.4	13.0	0.5	3.1	3.3	.0	1.7	0.6	11.3	0.7
1975	45.7	44.5	6.3	6.0	5.8	10.7	2.9	0.3	.0	0.2	5.3	1.0	15.6	1.2
1976	45.5	43.9	5.2	14.0	4.5	8.3	1.8	2.4	2.5	0.1	7.5	0.8	14.0	1.6
1977	41.1	41.4	5.2	7.2	2.4	4.7	1.2	2.0	1.9	0.1	10.4	1.0	15.6	-0.3
1978	47.8	48.7	5.0	18.2	3.2	10.6	2.1	3.0	2.9	0.1	6.5	0.9	15.1	-0.9
1979	55.6	53.9	4.1	22.6	5.8	16.1	2.1	3.4	3.1	0.1	5.6	0.9	17.3	1.7
1980	58.3	57.3	1.7	31.8	2.1	29.2	2.6	2.7	2.4	.0	2.0	1.1	17.9	1.0
1981	59.4	58.3	1.9	25.6	7.3	19.2	3.6	6.2	5.8	0.1	3.9	1.0	19.7	1.2
1982	69.8	68.8	4.2	21.5	2.3	15.9	5.2	6.3	4.0	0.3	12.4	1.1	24.2	1.0
1983	55.2	54.3	2.0	16.2	1.2	8.8	6.9	5.0	4.0	0.4	7.0	1.2	22.8	1.0
1984	63.9	36.9	1.5	7.9	-0.7	5.8	4.2	3.8	3.6	0.2	5.5	1.0	16.8	0.5

TABLE 8
CLAIMS OF FINANCIAL INSTITUTIONS AGAINST NON-FINANCIAL SECTOR (CONT'D)

	G O V E R N M E N T										R E S T O F W O R L D					(S\$m)
	F I N A N C E					I N S U R A N C E					D I S C O U N T					
	TOTAL	BANKS	COMPANIES	POSB	CPF	MERCHANT BANKS	HOUSES	TOTAL	BANKS	COMPANIES	FINANCE	MERCHANT BANKS	MONETARY AUTHORITIES			
1970	1634.5	691.2	4.6	61.6	58.6	818.5	0.0	3394.5	292.8	3.8	0.0	0.0	3097.9			
1971	2215.9	975.8	26.0	86.7	65.5	1061.9	0.0	4409.9	311.4	3.7	0.0	0.0	4094.8			
1972	12974.2	298.2	0.0	298.2	0.0	4581.8	210.8	1.9	124.8	0.0	14.2					
1973	16507.2	447.9	0.0	447.9	0.0	6820.5	292.9	32.6	175.0	0.0	73.7					
1974	18996.6	524.7	44.0	479.8	0.9	7827.1	374.8	98.2	181.5	178.9	101.7					
1975	22188.0	563.9	61.7	478.6	23.6	8937.5	439.2	209.7	214.5	191.3	80.2					
1976	26013.6	672.7	78.8	554.0	39.9	10219.9	489.5	420.9	248.1	264.8	92.5					
1977	29796.7	742.4	87.4	604.1	50.9	11331.3	590.7	427.5	266.1	282.4	117.7					
1978	36399.4	852.0	107.3	687.6	57.1	13888.5	742.5	977.4	305.1	356.3	147.3					
1979	43863.3	1151.9	139.3	925.1	87.5	17694.8	954.5	1255.3	359.8	453.5	158.5					
1980	53132.6	1508.7	188.3	1187.5	132.9	23009.0	1243.8	1502.1	430.0	690.0	230.0					
1981	64737.9	1862.2	273.7	1406.7	181.8	30322.3	1859.0	1577.3	541.7	1313.1	375.0					
1982	77553.3	2064.7	331.6	1475.3	257.8	36625.2	2747.7	1752.3	620.8	1513.9	493.9					
1983	92128.1	2837.6	562.6	1781.4	493.6	43511.2	3603.2	2169.5	723.7	2116.6	540.4					
1984	101391.8	3566.0	916.1	1920.4	729.5	46753.2	3913.7	2133.5	756.6	2440.3	594.0					

TABLE 8.1
CLAIMS OF FINANCIAL INSTITUTIONS: PERCENTAGE DISTRIBUTION

	H O U S E H O L D					B U S I N E S S					(\$m)				
	GRAND TOTAL	FINANCE		TOTAL	BANKS	FINANCE COMPANIES	POSB	TOTAL	BANKS	FINANCE COMPANIES		POSB	INSURANCE COMPANIES	MERCHANT BANKS	DISCOUNT HOUSES
		TOTAL	BANKS												
1970	100.0	2.1	0.0	2.1	0.0	35.8	32.9	1.7	0.0	1.2	0.0	0.0	0.0	0.0	
1971	100.0	2.1	0.0	2.1	0.0	33.6	30.7	1.8	0.0	1.2	0.0	0.0	0.0	0.0	
1972	100.0	2.3	0.0	2.3	0.0	35.3	32.6	1.6	0.0	1.0	0.0	0.0	0.1	0.1	
1973	100.0	2.7	0.0	2.7	0.0	41.3	37.8	1.8	0.2	1.1	0.0	0.0	0.4	0.4	
1974	100.0	2.8	0.2	2.5	0.0	41.2	36.3	2.0	0.5	1.0	0.9	0.9	0.5	0.5	
1975	100.0	2.5	0.3	2.2	0.1	40.3	35.3	2.0	0.9	1.0	0.9	1.0	0.4	0.4	
1976	100.0	2.6	0.3	2.1	0.2	39.3	33.5	1.9	1.6	1.0	1.0	1.0	0.4	0.4	
1977	100.0	2.5	0.3	2.0	0.2	38.0	32.4	2.0	1.4	0.9	0.9	0.9	0.4	0.4	
1978	100.0	2.3	0.3	1.9	0.2	38.2	31.2	2.0	2.7	0.8	1.0	1.0	0.4	0.4	
1979	100.0	2.6	0.3	2.1	0.2	40.3	33.1	2.2	2.9	0.8	1.0	1.0	0.4	0.4	
1980	100.0	2.8	0.4	2.2	0.3	43.3	35.6	2.3	2.8	0.8	1.3	1.3	0.4	0.4	
1981	100.0	2.9	0.4	2.2	0.3	46.8	38.1	2.9	2.4	0.8	2.0	2.0	0.6	0.6	
1982	100.0	2.7	0.4	1.9	0.3	47.2	38.0	3.5	2.3	0.8	2.0	2.0	0.6	0.6	
1983	100.0	3.1	0.6	2.0	0.5	47.7	37.6	3.9	2.4	0.8	2.3	2.3	0.6	0.6	
1984	100.0	3.5	0.9	1.9	0.5	46.1	36.4	3.9	2.1	0.7	2.4	2.4	0.6	0.6	

TABLE 8.1
CLAIMS OF FINANCIAL INSTITUTIONS: PERCENTAGE DISTRIBUTION (CONT'D)

(S\$m)

	G O V E R N M E N T					R E S T O F W O R L D								
	TOTAL	BANKS	FINANCE		INSURANCE	CPF	MERCHANT BANKS	DISCOUNT HOUSES	TOTAL	BANKS	COMPANIES	FINANCE BANKS	MERCHANT BANKS	MONETARY AUTHORITIES
			COMPANIES	POSB										
1970	20.2	8.5	0.1	0.8	0.7	10.1	0.0	0.0	42.0	3.6	0.0	0.0	0.0	38.3
1971	21.5	9.5	0.3	0.8	0.6	10.3	0.0	0.0	42.8	3.0	0.0	0.0	0.0	39.8
1972	21.2	8.4	0.1	0.7	0.6	10.5	0.0	0.9	41.2	3.1	0.0	0.0	0.0	38.0
1973	17.7	4.1	0.1	0.3	0.5	11.0	0.0	1.8	38.3	3.1	0.0	0.0	0.0	35.1
1974	18.9	3.7	0.0	0.2	0.5	12.7	0.0	1.7	37.1	2.8	0.0	0.0	0.0	34.2
1975	20.8	3.8	0.1	0.3	0.5	14.6	0.0	1.5	36.4	2.5	0.0	0.0	0.1	33.7
1976	25.3	4.2	0.1	1.2	0.6	15.7	0.0	1.5	34.9	3.1	0.0	0.0	0.0	31.8
1977	25.3	4.0	0.1	2.3	0.6	16.6	0.0	1.5	34.2	3.9	0.0	0.0	0.0	30.3
1978	23.8	3.5	0.2	1.9	0.6	16.3	0.0	1.3	35.7	4.1	0.0	0.0	0.0	31.5
1979	23.5	2.9	0.1	1.6	0.6	17.1	0.0	1.2	33.5	4.9	0.0	0.0	0.0	28.6
1980	23.8	2.9	0.1	1.4	0.5	17.8	0.0	1.2	30.0	4.1	0.0	0.0	0.0	25.9
1981	23.9	2.3	0.0	1.1	0.5	18.3	0.0	1.7	26.4	2.4	0.0	0.0	0.0	23.9
1982	24.9	2.0	0.0	0.8	0.5	19.6	0.0	1.8	25.3	2.2	0.0	0.0	0.0	23.1
1983	25.9	2.2	0.0	0.7	0.5	20.9	0.0	1.6	23.3	1.6	0.0	0.0	0.0	21.6
1984	26.5	1.9	0.1	0.6	0.5	21.5	0.0	1.8	23.9	1.4	0.0	0.0	0.0	22.4

TABLE 8.2

CLAIMS OF FINANCIAL INSTITUTIONS: MRFs

	GRAND TOTAL	HOUSEHOLD				BUSINESS						
		TOTAL	BANKS	FINANCE COMPANIES	POSB	TOTAL	BANKS	FINANCE COMPANIES	POSB	INSURANCE COMPANIES	MERCHANT BANKS	DISCOUNT HOUSES
1971	32.3	0.7	0.0	0.7	0.0	8.2	7.3	0.7	0.0	0.2	0.0	0.0
1972	32.8	1.0	0.0	1.0	0.0	13.8	13.1	0.3	0.0	0.2	0.0	0.2
1973	34.6	1.5	0.0	1.5	0.0	21.9	19.8	0.8	0.3	0.5	0.0	0.6
1974	23.9	0.6	0.4	0.3	0.0	8.0	5.1	0.7	0.5	0.1	1.4	0.2
1975	23.9	0.3	0.1	0.0	0.2	8.3	6.8	0.5	0.8	0.2	0.1	-0.2
1976	26.2	0.7	0.1	0.5	0.1	8.8	6.2	0.3	1.4	0.2	0.5	0.1
1977	23.7	0.4	0.1	0.3	0.1	7.0	5.9	0.6	0.0	0.1	0.1	0.2
1978	37.2	0.6	0.1	0.5	0.0	14.4	9.7	0.9	3.1	0.2	0.4	0.2
1979	36.5	1.5	0.2	1.2	0.1	18.6	15.4	1.0	1.4	0.3	0.5	0.1
1980	38.2	1.5	0.2	1.1	0.2	21.9	18.1	1.2	1.0	0.3	1.0	0.3
1981	40.5	1.2	0.3	0.8	0.2	25.5	20.0	2.1	0.3	0.4	2.2	0.5
1982	40.3	0.6	0.2	0.2	0.2	19.8	15.2	2.8	0.6	0.2	0.6	0.4
1983	38.8	2.2	0.7	0.9	0.7	19.5	13.7	2.4	1.2	0.3	1.7	0.1
1984	26.0	1.9	0.9	0.4	0.6	8.3	6.6	0.8	-0.1	0.1	0.8	0.1

TABLE 8.2
CLAIMS OF FINANCIAL INSTITUTIONS: MIFS (CONT'D)

	G O V E R N M E N T						R E S T O F W O R L D						
	TOTAL	FINANCE			INSURANCE		MERCHANT BANKS	DISCOUNT HOUSES	TOTAL	BANKS	FINANCE COMPANIES	MERCHANT BANKS	MONETARY AUTHORITIES
		BANKS	COMPANIES	POSB	COMPANIES	CPF							
1971	8.5	4.2	0.3	0.4	0.1	3.6	0.0	0.0	14.9	0.3	0.0	0.0	14.6
1972	6.6	1.4	-0.2	0.0	0.2	3.7	0.0	1.4	11.4	1.2	0.0	0.0	10.2
1973	1.7	-4.1	0.0	-0.4	0.1	4.3	0.0	1.8	9.5	1.0	0.0	0.0	8.5
1974	5.4	0.2	0.0	0.0	0.1	4.9	0.0	0.2	5.8	0.2	0.0	0.0	5.6
1975	7.6	1.0	0.0	0.2	0.1	6.1	0.0	0.2	7.6	0.2	0.0	0.1	7.4
1976	9.7	1.7	0.1	1.6	0.2	5.7	0.0	0.3	7.0	1.6	0.0	0.0	5.3
1977	9.4	0.7	0.1	2.4	0.3	5.5	0.0	0.3	6.9	2.2	0.0	-0.1	4.8
1978	6.5	0.4	0.1	0.0	0.2	5.6	0.0	0.3	15.7	1.9	0.0	0.0	13.8
1979	7.9	0.0	0.0	0.1	0.1	7.5	0.0	0.2	8.5	3.2	0.0	0.0	5.3
1980	9.7	1.1	-0.1	0.1	0.1	8.0	0.0	0.6	5.1	0.1	0.0	0.1	4.9
1981	9.8	-0.3	0.0	-0.2	0.1	8.5	0.0	1.6	3.9	-2.1	0.0	0.0	6.0
1982	11.8	0.4	0.0	-0.1	0.2	10.6	0.0	0.8	8.1	0.5	0.0	0.0	7.6
1983	12.6	1.3	0.0	0.0	0.2	10.8	0.0	0.3	4.6	-0.7	0.0	0.1	5.2
1984	8.2	-0.2	0.1	0.0	0.2	7.2	0.0	0.8	7.6	-0.1	0.0	0.0	7.7

TABLE 8.3

CLAIMS OF FINANCIAL INSTITUTIONS: FIRS

	H O U S E H O L D						B U S I N E S S					
	GRAND TOTAL	FINANCE			POSB	TOTAL	BANKS	FINANCE COMPANIES	POSB	INSURANCE COMPANIES	MERCHANT BANKS	DISCOUNT HOUSES
		TOTAL	BANKS	COMPANIES								
1971	79.0	1.7	0.00	1.66	0.00	20.1	17.9	1.7	0.0	0.5	0.00	0.00
1972	77.9	2.5	0.00	2.48	0.00	32.7	31.1	0.7	0.1	0.4	0.00	0.41
1973	85.1	3.6	0.00	3.61	0.00	53.9	48.6	2.0	0.7	1.2	0.00	1.43
1974	43.9	1.4	0.78	0.56	0.02	17.8	11.4	1.4	1.2	0.1	3.16	0.49
1975	60.5	0.7	0.34	-0.02	0.43	21.0	17.3	1.2	2.1	0.6	0.24	-0.41
1976	64.3	1.8	0.29	1.27	0.27	21.5	15.1	0.8	3.5	0.6	1.23	0.21
1977	66.4	1.2	0.15	0.88	0.19	19.5	16.6	1.8	0.1	0.3	0.31	0.44
1978	97.3	1.6	0.29	1.23	0.09	37.7	25.2	2.2	8.1	0.6	1.09	0.44
1979	84.4	3.4	0.36	2.68	0.34	43.0	35.6	2.4	3.1	0.6	1.10	0.13
1980	81.7	3.1	0.43	2.31	0.40	46.8	38.8	2.5	2.2	0.6	2.08	0.63
1981	88.1	2.7	0.65	1.66	0.37	55.5	43.6	4.7	0.6	0.8	4.73	1.10
1982	88.4	1.4	0.40	0.47	0.52	43.5	33.4	6.1	1.2	0.5	1.39	0.82
1983	81.3	4.6	1.37	1.81	1.40	40.8	28.8	5.1	2.5	0.6	3.57	0.28
1984	53.5	3.9	1.87	0.74	1.25	17.2	13.5	1.6	-0.2	0.2	1.71	0.28

TABLE 8.3
CLAIMS OF FINANCIAL INSTITUTIONS: FIRS (CONT'D)

	G O V E R N M E N T						R E S T O F W O R L D					
	TOTAL	FINANCE		INSURANCE	CPF	MERCHANT	DISCOUNT	FINANCE		MERCHANT	MONETARY	
		BANKS	COMPANIES					POSB	COMPANIES			BANKS
1971	20.8	10.2	0.8	0.9	0.2	8.7	0.0	0.0	36.4	0.7	0.00	35.7
1972	15.6	3.4	-0.4	0.1	0.4	8.8	0.0	3.3	27.1	2.8	0.00	24.3
1973	4.1	-10.1	-0.1	-1.0	0.2	10.7	0.0	4.4	23.5	2.4	0.00	21.0
1974	11.9	0.5	0.0	0.0	0.2	10.8	0.0	0.4	12.9	0.5	0.07	12.4
1975	19.4	2.6	0.1	0.4	0.3	15.5	0.0	0.4	19.3	0.9	0.17	18.6
1976	23.9	4.2	0.3	4.0	0.5	14.1	0.1	0.8	17.0	3.9	-0.01	13.0
1977	26.4	2.0	0.3	6.8	0.8	15.5	-0.1	0.9	19.5	6.3	-0.17	13.4
1978	16.9	1.1	0.2	-0.1	0.4	14.6	0.1	0.7	41.1	4.9	0.07	36.1
1979	18.3	0.0	0.0	0.2	0.3	17.4	-0.1	0.5	19.6	7.3	0.00	12.3
1980	20.8	2.4	-0.2	0.2	0.1	17.1	0.0	1.2	10.9	0.2	0.11	10.5
1981	21.3	-0.6	0.0	-0.4	0.3	18.6	0.0	3.4	8.6	-4.5	-0.09	13.2
1982	25.8	0.8	-0.1	-0.2	0.4	23.1	0.0	1.7	17.8	1.0	-0.02	16.7
1983	26.3	2.7	0.0	0.0	0.4	22.5	0.0	0.7	9.7	-1.4	0.17	10.9
1984	16.8	-0.4	0.1	0.0	0.5	14.9	0.0	1.7	15.7	-0.1	-0.05	15.8

TABLE 9
PRIMARY SECURITIES OF FINANCIAL INSTITUTIONS, BY TYPE

	GRAND TOTAL	L O A N S			A N D		A D V A N C E S			B I L L S			(S\$m)
		TOTAL	BANKS	FINANCE COMPANIES	POS	MERCHANT BANKS	INSURANCE COMPANIES	TOTAL	LOCAL	FOREIGN			
1970	8090.8	2494.7	2167.7	294.7	0.0	0.0	32.3	554.4	354.7	199.7			
1971	10295.3	3037.3	2615.0	389.4	0.0	0.0	32.9	554.7	343.6	211.1			
1972	12974.2	4099.7	3565.2	498.9	0.0	0.0	35.6	741.8	448.4	293.4			
1973	16507.2	5947.4	5146.5	724.9	30.0	0.0	46.0	1198.4	780.2	418.2			
1974	18996.6	6857.3	5697.0	840.3	95.5	161.5	63.0	1335.1	891.5	443.6			
1975	22188.0	7837.2	6503.1	897.0	195.3	175.1	66.7	1406.3	991.5	484.8			
1976	26013.6	8882.6	7271.7	1026.4	268.8	249.5	66.2	1715.0	1000.9	714.1			
1977	29796.7	9659.8	7830.8	1176.9	321.6	267.3	63.2	2469.9	1379.6	1090.3			
1978	36399.4	12045.0	9398.9	1397.1	839.9	336.2	72.9	2974.8	1550.7	1424.1			
1979	43863.3	15581.9	12058.7	1827.9	1154.7	430.0	110.6	4106.8	2021.8	2085.0			
1980	53132.6	20767.2	16157.5	2367.1	1468.7	644.2	129.7	4279.3	2189.5	2089.8			
1981	64737.9	27473.7	21249.7	3187.6	1586.0	1258.2	192.2	4354.5	2861.3	1493.2			
1982	77553.3	32946.5	25335.6	4129.8	1806.2	1463.4	213.5	4601.2	3008.3	1592.9			
1983	91281.1	49236.2	30145.3	5277.3	2498.7	2071.2	243.7	4440.9	3099.7	1341.2			
1984	101391.8	43836.9	32742.7	5727.3	2719.9	2366.2	280.8	4718.8	3403.2	1315.6			

TABLE 9
PRIMARY SECURITIES OF FINANCIAL INSTITUTIONS, BY TYPE (CONT'D)
(S\$m)

	SECURITIES AND EQUITIES							
	TOTAL	BANKS	FINANCE COMPANIES	POSB	MERCHANT BANKS	DISCOUNT HOUSES	INSURANCE COMPANIES	CPF
1970	5041.7	920.7	18.1	61.6	0.0	0.0	124.9	818.5
1971	6703.3	1276.5	38.5	86.7	0.0	0.0	144.9	1061.9
1972	8132.7	1438.1	27.0	90.8	0.0	112.0	169.4	1365.5
1973	9361.4	1156.6	33.1	48.5	0.0	294.8	219.4	1808.9
1974	10804.2	1240.9	28.0	48.0	21.7	320.1	220.8	2421.8
1975	12944.5	1437.7	38.3	104.1	29.6	341.1	268.2	3239.5
1976	15416.0	1775.3	56.9	496.2	33.0	386.1	329.9	4077.1
1977	17667.0	1911.4	71.4	851.0	18.9	436.2	395.6	4959.6
1978	21379.6	2010.1	95.1	882.8	34.0	481.5	454.0	5948.3
1979	24174.6	2060.5	111.3	896.3	33.3	523.9	498.8	7488.1
1980	28086.1	2603.8	100.5	893.8	68.0	663.8	566.8	9431.7
1981	32909.7	2739.6	114.6	854.4	64.8	1113.8	653.6	11877.8
1982	40003.6	3686.3	120.5	860.2	56.1	1360.9	769.5	15232.2
1983	46604.0	4390.3	139.8	820.7	80.3	1470.9	910.7	19036.0
1984	52836.1	4379.0	165.2	799.4	99.9	1795.3	1001.5	21847.8
								22748.0

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TABLE 9.1
PRIMARY SECURITIES OF FINANCIAL INSTITUTIONS, BY TYPE: PERCENTAGE DISTRIBUTION

	L O A N S			A D V A N C E S			B I L L S			
	GRAND TOTAL	TOTAL	BANKS	FINANCE COMPANIES	POSB	MERCHANT BANKS	INSURANCE COMPANIES	TOTAL	LOCAL	FOREIGN
1970	100.0	30.8	26.8	3.6	0.0	0.0	0.4	6.9	4.4	2.5
1971	100.0	29.5	25.4	3.8	0.0	0.0	0.3	5.4	3.3	2.1
1972	100.0	31.6	27.5	3.8	0.0	0.0	0.3	5.7	3.5	2.3
1973	100.0	36.0	31.2	4.4	0.2	0.0	0.3	7.3	4.7	2.5
1974	100.0	36.1	30.0	4.4	0.5	0.9	0.3	7.0	4.7	2.3
1975	100.0	35.3	29.3	4.0	0.9	0.8	0.3	6.3	4.2	2.2
1976	100.0	34.1	28.0	3.9	1.0	1.0	0.3	6.6	3.8	2.7
1977	100.0	32.4	26.3	3.9	1.1	0.9	0.2	8.3	4.6	3.7
1978	100.0	33.1	25.8	3.8	2.3	0.9	0.2	8.2	4.3	3.9
1979	100.0	35.5	27.5	4.2	2.6	1.0	0.3	9.4	4.6	4.8
1980	100.0	39.1	30.4	4.5	2.8	1.2	0.2	8.1	4.1	3.9
1981	100.0	42.4	32.8	4.9	2.4	1.9	0.3	6.7	4.4	2.3
1982	100.0	42.5	32.7	5.3	2.3	1.9	0.3	5.9	3.9	2.1
1983	100.0	44.1	33.0	5.8	2.7	2.3	0.3	4.9	3.4	1.5
1984	100.0	43.2	32.3	5.6	2.7	2.3	0.3	4.7	3.4	1.3

TABLE 9.1
PRIMARY SECURITIES OF FINANCIAL INSTITUTIONS, BY TYPE: PERCENTAGE DISTRIBUTION (CONT'D)

	TOTAL	SECURITIES AND EQUITIES							
		BANKS	FINANCE COMPANIES	POSB	MERCHANT BANKS	DISCOUNT HOUSES	INSURANCE COMPANIES	CPF	MONETARY AUTHORITIES
1970	62.3	11.4	0.2	0.8	0.0	0.0	1.5	10.1	38.3
1971	65.1	12.4	0.4	0.8	0.0	0.0	1.4	10.3	39.8
1972	62.7	11.1	0.2	0.7	0.0	0.9	1.3	10.5	38.0
1973	56.7	7.0	0.2	0.3	0.0	1.8	1.3	11.0	35.1
1974	58.3	6.5	0.1	0.3	0.1	1.7	1.2	12.7	34.2
1975	58.3	6.5	0.2	0.5	0.1	1.5	1.2	14.6	33.7
1976	59.3	6.8	0.2	1.9	0.1	1.5	1.3	15.7	31.8
1977	59.3	6.4	0.2	2.9	0.1	1.5	1.3	16.6	30.3
1978	58.7	5.5	0.3	2.4	0.1	1.3	1.2	16.3	31.5
1979	55.1	4.7	0.3	2.0	0.1	1.2	1.1	17.1	28.6
1980	52.9	4.9	0.2	1.7	0.1	1.2	1.1	17.8	25.9
1981	50.8	4.2	0.1	1.3	0.1	1.7	1.0	18.3	23.9
1982	51.6	4.8	0.2	1.1	0.1	1.8	1.0	19.6	23.1
1983	51.1	4.8	0.2	0.9	0.1	1.6	1.0	20.9	21.6
1984	52.1	4.3	0.2	0.8	0.1	1.8	1.0	21.5	22.4

TABLE 9.2

PRIMARY SECURITIES OF FINANCIAL INSTITUTIONS, BY TYPE: MRFs

	GRAND TOTAL	L O A N S			A N D			A D V A N C E S			B I L L S		
		TOTAL	BANKS	FINANCE COMPANIES	POS	MERCHANT BANKS	INSURANCE COMPANIES	TOTAL	LOCAL	FOREIGN			
1971	32.3	8.0	6.6	1.4	0.0	0.0	0.0	0.0	-0.2	0.2			
1972	32.8	13.0	11.7	1.3	0.0	0.0	0.0	2.3	1.3	1.0			
1973	34.6	18.1	15.5	2.2	0.3	0.0	0.1	4.5	3.3	1.2			
1974	19.8	7.3	4.4	0.9	0.5	1.3	0.1	1.1	0.9	0.2			
1975	23.9	7.3	6.0	0.4	0.7	0.1	0.0	0.5	0.2	0.3			
1976	26.2	7.2	5.3	0.9	0.5	0.5	0.0	2.1	0.5	1.6			
1977	23.7	4.9	3.5	0.9	0.3	0.1	0.0	4.7	2.4	2.4			
1978	37.2	13.4	8.8	1.2	2.9	0.4	0.1	2.8	1.0	1.9			
1979	36.5	17.3	13.0	2.1	1.5	0.5	0.2	5.5	2.3	3.2			
1980	38.2	21.4	16.9	2.2	1.3	0.9	0.1	0.7	0.7	0.0			
1981	40.5	23.4	17.8	2.9	0.4	2.1	0.2	0.3	2.3	-2.1			
1982	40.3	17.2	1.97	3.0	0.7	0.6	0.1	0.8	0.5	0.3			
1983	38.8	20.6	13.6	3.2	2.0	1.7	0.1	-0.5	0.3	-0.7			
1984	26.0	9.3	6.7	1.2	0.6	0.8	0.1	0.7	0.8	-0.1			

TABLE 9.2

PRIMARY SECURITIES OF FINANCIAL INSTITUTIONS, BY TYPE: MRFS (CONT'D)

	TOTAL	SECURITIES					AND EQUITIES			
		BANKS	FINANCE COMPANIES	POSB	MERCHANT BANKS	DISCOUNT HOUSES	INSURANCE COMPANIES	CPF	MONETARY AUTHORITIES	
1971	24.4	5.2	0.3	0.4	0.0	0.0	0.3	3.6	14.6	
1972	17.5	2.0	-0.1	0.1	0.0	1.4	0.3	3.7	10.2	
1973	12.0	-2.8	0.1	-0.4	0.0	1.8	0.5	4.3	8.5	
1974	11.5	0.7	0.0	0.4	0.1	0.2	0.4	6.1	7.4	
1975	16.0	1.5	0.1	0.4	0.1	0.2	0.4	5.7	5.3	
1976	17.0	2.3	0.1	2.7	0.0	0.3	0.4	5.7	5.3	
1977	14.1	0.9	0.1	2.2	-0.1	0.3	0.4	5.5	4.8	
1978	20.9	0.6	0.1	0.2	0.1	0.3	0.3	5.6	13.8	
1979	13.7	0.2	0.1	0.1	0.0	0.2	0.2	7.5	5.3	
1980	16.1	2.2	0.0	0.0	0.1	0.6	0.3	8.0	4.9	
1981	16.8	0.5	0.0	-0.1	0.0	1.6	0.3	8.5	6.0	
1982	22.3	3.0	0.0	0.0	0.0	0.8	0.4	10.6	7.6	
1983	18.7	2.0	0.1	-0.1	0.1	0.3	0.4	10.8	5.2	
1984	16.0	0.0	0.1	-0.1	0.1	0.8	0.2	7.2	7.7	

TABLE 9.3
PRIMARY SECURITIES OF FINANCIAL INSTITUTIONS, BY TYPE: FIRS

	L O A N S			A N D			A D V A N C E S			B I L L S		
	GRAND TOTAL	TOTAL	BANKS	FINANCE COMPANIES	POSB	MERCHANT BANKS	INSURANCE COMPANIES	TOTAL	LOCAL	FOREIGN		
1971	79.0	19.4	16.0	3.4	0.0	0.0	0.0	0.0	-0.4	0.4		
1972	77.9	30.9	27.6	3.2	0.0	0.0	0.1	5.4	3.0	2.4		
1973	85.1	44.5	38.1	5.4	0.7	0.0	0.3	11.0	8.0	3.0		
1974	43.9	16.1	9.7	2.0	1.2	2.8	0.3	2.4	2.0	0.4		
1975	60.5	18.6	15.3	1.1	1.9	0.3	0.1	1.3	0.6	0.8		
1976	64.3	17.6	12.9	2.2	1.2	1.3	0.0	5.2	1.3	3.9		
1977	66.4	13.6	9.8	2.6	0.9	0.3	-0.1	13.3	6.7	6.6		
1978	97.3	35.1	23.1	3.2	7.6	1.0	0.1	7.4	2.5	4.9		
1979	84.4	40.0	30.1	4.9	3.6	1.1	0.4	12.8	5.3	7.5		
1980	81.7	45.7	36.1	4.8	2.8	1.9	0.2	1.5	1.5	0.0		
1981	88.1	50.9	38.6	6.2	0.9	4.7	0.5	0.6	5.1	-4.5		
1982	88.4	37.8	28.2	6.5	1.5	1.4	0.1	1.7	1.0	0.7		
1983	81.3	43.2	28.5	6.8	4.1	3.6	0.2	-0.9	0.5	-1.5		
1984	53.5	19.1	13.8	2.4	1.2	1.6	0.2	1.5	1.6	-0.1		

TABLE 9.3
PRIMARY SECURITIES OF FINANCIAL INSTITUTIONS, BY TYPE: FIRS (CONT'D)

	TOTAL	SECURITIES AND EQUITIES					CPF	MONETARY AUTHORITIES
		BANKS	FINANCE COMPANIES	POSB	MERCHANT BANKS	DISCOUNT HOUSES	INSURANCE COMPANIES	
1971	59.5	12.8	0.7	0.9	0.0	0.0	0.7	8.7
1972	41.6	4.7	-0.3	0.1	0.0	3.3	0.7	8.8
1973	29.6	-6.8	0.1	-1.0	0.0	4.4	1.2	10.7
1974	25.5	1.5	-0.1	0.0	0.4	0.4	0.0	10.8
1975	40.5	3.7	0.2	1.1	0.1	0.4	0.9	15.5
1976	41.5	5.7	0.3	6.6	0.1	0.8	1.0	14.1
1977	39.5	2.4	0.3	6.2	-0.2	0.9	1.2	15.5
1978	54.7	1.5	0.3	0.5	0.2	0.7	0.9	14.6
1979	31.6	0.6	0.1	0.2	0.0	0.5	0.5	17.4
1980	34.5	4.8	-0.1	0.0	0.3	1.2	0.6	17.1
1981	36.6	1.0	0.1	-0.3	0.0	3.4	0.7	18.6
1982	48.9	6.5	0.0	0.0	-0.1	1.7	0.8	23.1
1983	39.1	4.2	0.1	-0.2	0.1	0.7	0.8	22.5
1984	33.0	-0.1	0.1	-0.1	0.1	0.7	0.5	14.9

TABLE 10
PRIMARY SECURITIES, BY FINANCIAL INSTITUTIONS

	(S\$m)								
	GRAND TOTAL	BANKS	FINANCE COMPANIES	POSB	INSURANCE COMPANIES	CPF	MERCHANT BANKS	DISCOUNT HOUSES	MONETARY AUTHORITIES
1970	8090.8	3642.8	312.8	61.6	157.2	818.5	0.0	0	3097.9
1971	10295.3	4446.2	427.9	86.7	177.8	1061.9	0.0	0	4094.8
1972	12974.2	5730.9	525.9	90.8	205.0	1365.5	0.0	126.2	4929.9
1973	16507.2	7427.8	758.0	78.5	265.4	1808.9	0.3	368.5	5800.1
1974	18996.6	8171.3	868.3	143.5	283.8	2421.8	183.2	421.8	6502.9
1975	22188.0	9266.9	935.3	299.4	334.9	3239.5	204.7	421.3	7486.0
1976	26013.6	10669.5	1083.3	765.0	396.1	4077.1	282.5	478.6	8261.5
1977	29796.7	12094.4	1248.3	1172.6	458.8	4959.6	286.2	553.9	9022.9
1978	36399.4	14236.5	1492.2	1722.7	526.9	5948.3	370.2	628.8	11473.8
1979	43863.3	18067.5	1939.2	2051.0	609.4	7488.1	463.3	682.4	12562.4
1980	53132.6	22810.6	2467.6	2362.5	696.5	9431.7	712.2	893.8	13757.7
1981	64737.9	27968.8	3302.2	2440.4	845.8	11877.8	1323.0	1488.8	15491.1
1982	77553.3	33129.2	4250.3	2666.4	983.0	15232.2	1519.5	1854.8	17917.9
1983	91281.1	38436.0	5417.1	3319.4	1154.4	19036.0	2151.5	2011.4	19755.3
1984	101391.8	41246.5	5892.5	3519.3	1282.3	21847.8	2466.1	2389.3	22748.0

TABLE 10.1
PRIMARY SECURITIES, BY FINANCIAL INSTITUTIONS: PERCENTAGE DISTRIBUTION

	GRAND TOTAL	BANKS	FINANCE COMPANIES	POSB	INSURANCE COMPANIES	CPF	MERCHANT BANKS	DISCOUNT HOUSES	MONETARY AUTHORITIES
1970	100.0	45.0	3.9	0.8	1.9	10.1	0.0	0.0	38.3
1971	100.0	43.2	4.2	0.8	1.7	10.3	0.0	0.0	39.8
1972	100.0	44.2	4.1	0.7	1.6	10.5	0.0	1.0	38.0
1973	100.0	45.0	4.6	0.5	1.6	11.0	0.0	2.2	35.1
1974	100.0	43.0	4.6	0.8	1.5	12.7	1.0	2.2	34.2
1975	100.0	41.8	4.2	1.3	1.5	14.6	0.9	1.9	33.7
1976	100.0	41.0	4.2	2.9	1.5	15.7	1.1	1.8	31.8
1977	100.0	40.6	4.2	3.9	1.5	16.6	1.0	1.9	30.3
1978	100.0	39.1	4.1	4.7	1.4	16.3	1.0	1.7	31.5
1979	100.0	41.2	4.4	4.7	1.4	17.1	1.1	1.6	28.6
1980	100.0	42.9	4.6	4.4	1.3	17.8	1.3	1.7	25.9
1981	100.0	43.2	5.1	3.8	1.3	18.3	2.0	2.3	23.9
1982	100.0	42.7	5.5	3.4	1.3	19.6	2.0	2.4	23.1
1983	100.0	42.1	5.9	3.6	1.3	20.9	2.4	2.2	21.6
1984	100.0	40.7	5.8	3.5	1.3	21.5	2.4	2.4	22.4

TABLE 10.2

PRIMARY SECURITIES, BY FINANCIAL INSTITUTIONS: MRFS

	GRAND TOTAL	BANKS	FINANCE COMPANIES	POSB	INSURANCE COMPANIES	CPF	MERCHANT BANKS	DISCOUNT HOUSES	MONETARY AUTHORITIES
1971	32.3	11.8	1.7	0.4	0.3	3.6	0.0	0.0	14.6
1972	32.8	15.8	1.2	0.1	0.3	3.7	0.0	1.5	10.2
1973	34.6	16.6	2.3	-0.1	0.6	4.3	0.0	2.4	8.5
1974	19.8	5.9	0.9	0.5	0.1	4.9	1.5	0.4	5.6
1975	23.9	8.2	0.5	1.2	0.4	6.1	0.2	.0	7.4
1976	26.2	9.6	1.0	3.2	0.4	5.7	0.5	0.4	5.3
1977	23.7	8.9	1.0	2.6	0.4	5.5	.0	0.5	4.8
1978	37.2	12.1	1.4	3.1	0.4	5.5	0.5	0.4	13.8
1979	36.5	18.7	2.2	1.6	0.4	7.5	0.5	0.3	3.3
1980	38.2	19.5	2.6	1.3	0.4	8.0	1.0	0.9	4.9
1981	40.5	18.0	2.9	0.3	0.5	8.5	2.1	2.1	6.0
1982	40.3	16.7	3.0	0.7	0.4	10.6	0.6	1.2	7.6
1983	38.8	15.0	3.3	1.8	0.5	10.8	1.8	0.4	5.2
1984	26.0	7.2	1.2	0.5	0.3	7.2	0.8	1.0	7.7

TABLE 10.3
PRIMARY SECURITIES, BY FINANCIAL INSTITUTIONS: FIRS

	GRAND TOTAL	BANKS	FINANCE COMPANIES	POSB	INSURANCE COMPANIES	CPF	MERCHANT BANKS	DISCOUNT HOUSES	MONETARY AUTHORITIES
1971	79.0	28.8	4.1	0.9	0.7	8.7	0.0	0.0	35.7
1972	77.9	37.4	2.8	0.1	0.8	8.8	0.0	3.7	24.3
1973	85.1	40.9	5.6	-0.3	1.5	10.7	0.0	5.8	21.0
1974	43.9	13.1	1.9	1.1	0.3	10.8	3.2	0.9	12.4
1975	60.5	20.8	1.3	3.0	1.0	15.5	0.4	.0	18.6
1976	64.3	23.6	2.5	7.8	1.0	14.1	1.3	1.0	13.0
1977	66.4	25.0	2.9	7.2	1.1	15.5	0.1	1.3	13.4
1978	97.3	31.6	3.6	8.1	1.0	14.6	1.2	1.1	36.1
1979	84.4	43.3	5.1	3.7	0.9	17.4	1.1	0.6	12.3
1980	81.7	41.8	4.7	2.7	0.8	17.1	2.2	1.9	10.5
1981	88.1	39.1	6.3	0.6	1.1	18.6	4.6	4.5	13.2
1982	88.4	35.6	6.5	1.6	0.9	23.1	1.4	2.5	16.7
1983	81.3	31.4	6.9	3.9	1.0	22.5	3.7	0.9	10.9
1984	53.5	14.9	2.5	1.1	0.7	14.9	1.7	2.0	15.8

TABLE 11

CLAIMS AGAINST FINANCIAL SECTOR, CLASSIFIED BY MARKETABILITY

(\$m)

MARKETABLE INSTRUMENTS					NON-MARKETABLE INSTRUMENTS					FOREIGN CURRENCY DEPOSITS WITH BANKS
GRAND TOTAL	TOTAL	CURRENCY	S\$NCDS	TOTAL	S			LIFE INSUR- ANCE FUND	CPF	
					BANKS	\$ FINANCE COMPANY	POSB			
1970	5110.9	681.9	0.0	4429.0	3014.3	400.0	72.7	164.5	777.5	0.0
1971	6138.8	806.0	0.0	5332.8	3514.7	553.1	91.2	185.9	987.9	0.0
1972	7803.4	1004.8	0.0	6798.6	4395.2	683.2	125.2	221.1	1316.0	57.9
1973	9674.7	1114.4	0.0	8560.3	5419.4	853.8	170.9	252.3	1770.7	93.2
1974	11534.6	1306.4	0.0	10228.2	6100.2	1031.1	268.5	284.0	2413.7	130.7
1975	13945.7	1718.7	81.0	12227.0	6864.5	1048.4	548.4	337.1	3234.9	193.7
1976	16654.2	2115.7	168.9	14538.5	7609.4	1191.2	996.0	387.4	4066.1	288.4
1977	18994.3	2401.4	158.8	16592.9	8027.1	1305.4	1589.0	445.4	4954.0	272.0
1978	22240.2	2786.1	203.3	19454.1	9216.1	1510.0	2029.0	505.0	5981.4	212.6
1979	27157.9	3220.7	279.5	23937.2	11140.4	1812.3	2525.2	585.1	7515.5	358.7
1980	33771.3	3287.5	150.5	30483.8	14879.4	2121.2	2756.7	705.1	9551.2	470.2
1981	41604.5	3598.1	216.3	38006.4	18189.0	2942.2	3265.9	834.7	12149.8	624.8
1982	51714.7	4227.7	231.7	47487.0	21291.5	3711.5	5058.4	998.8	15655.5	771.3
1983	61039.0	4542.4	207.1	56496.6	24057.5	4564.1	6240.9	1196.5	19504.7	932.9
1984	68013.0	4654.9	35.7	63358.1	25716.4	5278.3	7287.3	1384.2	22670.4	1021.5

TABLE 11.1

CLAIMS AGAINST FINANCIAL SECTOR, CLASSIFIED BY MARKETABILITY: PERCENTAGE DISTRIBUTION

	MARKETABLE INSTRUMENTS				NON-MARKETABLE INSTRUMENTS					FOREIGN CURRENCY DEPOSITS WITH BANKS
	GRAND TOTAL	TOTAL	CURRENCY	\$NCDs	TOTAL	BANKS	\$ FINANCE COMPANY	POS LIFE INSUR- ANCE FUND	CPF	
1970	100.0	13.3	13.3	0.0	86.7	59.0	7.8	1.4	15.2	0.0
1971	100.0	13.1	13.1	0.0	86.9	57.3	9.0	1.5	16.1	0.0
1972	100.0	12.9	12.9	0.0	87.1	56.3	8.8	1.6	16.9	0.7
1973	100.0	11.5	11.5	0.0	88.5	56.0	8.8	1.8	18.3	1.0
1974	100.0	11.3	11.3	0.0	88.7	52.9	8.9	2.3	20.9	1.1
1975	100.0	12.3	11.7	0.6	87.7	49.2	7.5	3.9	23.2	1.4
1976	100.0	12.7	11.7	1.0	87.3	45.7	7.2	6.0	24.4	1.7
1977	100.0	12.6	11.8	0.8	87.4	42.3	6.9	8.4	26.1	1.4
1978	100.0	12.5	11.6	0.9	87.5	41.4	6.8	9.1	26.9	1.0
1979	100.0	11.9	10.6	1.0	88.1	41.0	6.7	9.3	27.7	1.3
1980	100.0	9.7	9.3	0.4	90.3	44.1	6.3	8.2	28.3	1.4
1981	100.0	8.6	8.1	0.5	91.4	43.7	7.1	7.8	29.2	1.5
1982	100.0	8.2	7.7	0.4	91.8	41.2	7.2	9.8	30.3	1.5
1983	100.0	7.4	7.1	0.3	92.6	39.4	7.5	10.2	32.0	1.5
1984	100.0	6.8	6.8	0.1	93.2	37.8	7.8	10.7	33.3	1.5

TABLE 11.2

CLAIMS AGAINST FINANCIAL SECTOR, BY MARKETABILITY: MRFS

	MARKETABLE INSTRUMENTS				NON-MARKETABLE INSTRUMENTS						
	GRAND TOTAL	TOTAL	CURRENCY	\$NCDS	TOTAL	S BANKS	\$ FINANCE COMPANY	DEP POS	INSUR- ANCE FUND	CPF	FOREIGN CURRENCY DEPOSITS WITH BANKS
1971	15.1	1.8	1.8	0.0	13.2	7.3	2.2	0.3	0.3	3.1	0.0
1972	20.4	2.4	2.4	0.0	18.0	10.8	1.6	0.4	0.4	4.0	0.7
1973	18.3	1.1	1.1	0.0	17.0	10.0	1.7	0.4	0.3	4.5	0.3
1974	14.8	1.5	1.5	0.0	13.3	5.4	1.4	0.8	0.3	5.1	0.3
1975	18.0	3.1	2.5	0.6	14.9	5.7	0.1	2.1	0.4	6.1	0.5
1976	18.6	2.7	2.1	0.6	15.9	5.1	1.0	3.1	0.3	5.7	0.6
1977	14.7	1.8	1.9	-0.1	12.9	2.6	0.7	3.7	0.4	5.6	-0.1
1978	18.3	2.2	1.9	0.3	16.1	6.7	1.2	2.5	0.3	5.8	-0.3
1979	24.0	2.1	1.8	0.4	21.9	9.4	1.5	2.4	0.4	7.5	0.7
1980	27.2	0.3	0.8	-0.5	27.0	15.4	1.3	1.0	0.5	8.4	0.5
1981	27.3	1.1	0.9	0.2	26.3	11.6	2.9	1.8	0.5	9.1	0.5
1982	31.8	2.0	1.9	0.0	29.8	9.8	2.4	5.6	0.5	11.0	0.5
1983	26.4	0.9	1.0	-0.1	25.5	7.8	2.4	5.3	0.6	11.9	0.5
1984	17.9	0.3	0.7	-0.4	17.7	4.3	2.7	0.5	0.5	8.1	0.2

TABLE 11.3
CLAIMS AGAINST FINANCIAL SECTOR, BY MARKETABILITY: FIRS

	MARKETABLE INSTRUMENTS				NON-MARKETABLE INSTRUMENTS						
	GRAND TOTAL	TOTAL	CURRENCY	S\$NCDS	TOTAL	S			LIFE INSUR- ANCE FUND	CPF	FOREIGN CURRENCY DEPOSITS WITH BANKS
						BANKS	\$ FINANCE COMPANY	DEPOSITS POSB			
1971	36.8	4.4	4.4	0.0	32.4	17.9	5.5	0.7	0.8	7.5	0.0
1972	48.4	5.8	5.8	0.0	42.6	25.6	3.8	1.0	1.0	9.5	1.7
1973	45.1	2.6	2.6	0.0	42.5	24.7	4.1	1.1	0.8	11.0	0.9
1974	32.8	3.4	3.4	0.0	29.4	12.0	3.1	1.7	0.6	11.3	0.7
1975	45.7	7.8	6.3	1.5	37.9	14.5	0.3	5.3	1.0	15.6	1.2
1976	45.5	6.7	5.2	1.5	38.8	12.5	2.4	7.5	0.8	14.0	1.6
1977	41.1	5.0	5.2	-0.2	36.1	7.3	2.0	10.4	1.0	15.6	-0.3
1978	47.8	5.7	5.0	0.7	42.2	17.5	3.0	6.5	0.9	15.1	-0.9
1979	55.6	4.9	4.1	0.9	50.7	21.8	3.4	5.6	0.9	17.3	1.7
1980	58.3	0.6	1.7	-1.1	57.7	32.9	2.7	2.0	1.1	17.9	1.0
1981	59.4	2.4	1.9	1.9	57.1	25.1	6.2	3.9	1.0	19.7	1.2
1982	69.8	4.3	4.2	0.1	65.4	21.4	5.3	12.4	1.1	24.2	1.0
1983	55.2	1.9	2.0	-0.1	53.4	16.4	5.0	7.0	1.2	22.8	1.0
1984	36.9	0.6	1.5	-0.9	36.3	8.8	3.8	5.5	1.0	16.8	0.5

TABLE 12

CLAIMS AGAINST NON-FINANCIAL SECTOR, CLASSIFIED BY MARKETABILITY
(S\$m)

	MARKETABLE INSTRUMENTS				NON-MARKETABLE INSTRUMENTS				
	GRAND TOTAL	TOTAL	GOVERNMENT SECURITIES	SHARES & BONDS	FOREIGN SECURITIES	BILLS	TOTAL	HOUSEHOLD	BUSINESS
1970	N.A.	N.A.	2016.6	N.A.	3194.8	554.4	2494.7	166.5	2328.2
1971	N.A.	N.A.	2734.0	N.A.	4198.8	554.7	3037.3	212.9	2824.4
1972	N.A.	N.A.	3483.2	N.A.	5047.5	741.8	4099.7	298.2	3801.5
1973	N.A.	N.A.	3757.6	N.A.	5896.5	1198.4	5947.4	447.9	5499.5
1974	23939.7	17082.4	4522.4	4621.4	6693.5	1335.1	6857.3	524.7	6332.6
1975	28696.3	20859.1	5698.1	6171.8	7582.9	1406.3	7837.2	563.9	7273.3
1976	33191.0	24308.4	7315.1	6910.5	8367.8	1715.0	8882.6	672.7	8209.9
1977	41842.6	32182.8	9130.2	11482.9	9099.8	2469.9	9659.8	742.4	8917.4
1978	44829.3	32784.3	10692.6	7562.1	11554.8	2974.8	12045.0	852.0	11193.0
1979	53064.2	37482.3	12396.5	8350.4	12628.6	4106.8	15581.9	1151.9	14430.0
1980	63807.0	43039.8	14669.5	10233.6	13857.4	4279.3	20767.2	1508.7	19258.5
1981	80586.6	53112.9	17138.2	15037.9	15582.3	5354.5	27473.7	1862.2	25611.5
1982	94609.8	61661.3	20730.4	18274.1	18055.6	4601.2	32948.5	2064.7	30883.8
1983	111186.1	70949.9	25031.5	21540.6	19936.9	4440.9	40236.2	2836.7	37398.6
1984	124999.1	81162.2	28077.3	25444.0	22922.1	4718.8	43836.9	3566.0	40270.9

TABLE 12.
CLAIMS AGAINST NON-FINANCIAL SECTOR, CLASSIFIED BY MARKETABILITY: PERCENTAGE DISTRIBUTION

	MARKETABLE INSTRUMENTS				NON-MARKETABLE INSTRUMENTS			
	GRAND TOTAL	TOTAL	GOVERNMENT SECURITIES	SHARES & BONDS	FOREIGN SECURITIES	BILLS	TOTAL	HOUSEHOLD BUSINESS
1974	100.0	71.4	18.9	19.3	27.6	5.6	28.6	2.2 26.5
1975	100.0	72.7	19.9	21.5	26.4	4.9	27.3	2.0 25.3
1976	100.0	73.2	22.0	20.8	25.2	5.2	26.8	2.0 24.7
1977	100.0	76.9	21.8	27.4	21.7	5.9	23.1	1.8 21.3
1978	100.0	73.1	23.9	16.9	25.8	6.6	26.9	1.9 25.0
1979	100.0	70.6	23.4	15.7	23.8	7.7	29.4	2.2 27.2
1980	100.0	67.5	23.0	16.0	21.7	6.7	32.5	2.4 30.2
1981	100.0	65.9	21.3	18.7	19.3	6.6	34.1	2.3 31.8
1982	100.0	65.2	21.9	19.3	19.1	4.9	34.8	2.2 32.6
1983	100.0	63.8	22.5	19.4	17.9	4.0	36.2	2.6 33.6
1984	100.0	64.9	22.5	20.4	18.3	3.8	35.1	2.9 32.2

TABLE 12.2

CLAIMS AGAINST NON-FINANCIAL SECTOR, CLASSIFIED BY MARKETABILITY: MRFS

	GRAND TOTAL	MARKETABLE INSTRUMENTS			NON-MARKETABLE INSTRUMENTS			
		TOTAL	GOVERNMENT SECURITIES	SHARES & BONDS	FOREIGN SECURITIES	BILLS	TOTAL	HOUSEHOLD BUSINESS
1971	N.A.	N.A.	10.5	N.A.	14.7	0.0	8.0	0.7 7.3
1972	N.A.	N.A.	9.2	N.A.	10.4	2.3	13.0	1.0 12.0
1973	N.A.	N.A.	2.7	N.A.	8.3	4.5	18.1	1.5 16.6
1974	N.A.	N.A.	6.1	N.A.	5.6	1.1	7.3	0.6 6.6
1975	35.6	28.2	8.8	11.6	7.3	0.5	7.3	0.3 7.0
1976	30.8	23.7	11.1	5.1	5.4	2.1	7.2	0.7 6.4
1977	54.2	49.3	11.4	28.6	4.6	4.7	4.9	0.4 4.4
1978	16.8	3.4	8.8	-22.1	13.8	2.8	13.4	0.6 12.8
1979	40.3	23.0	8.3	3.9	5.3	5.5	17.3	1.5 15.8
1980	44.2	22.9	9.4	7.8	5.1	0.7	21.4	1.5 19.9
1981	58.6	35.2	8.6	16.8	6.0	3.8	23.4	1.2 22.2
1982	44.1	26.9	11.3	10.2	7.8	-2.4	17.2	0.6 16.6
1983	46.9	26.3	12.2	9.2	5.3	-0.5	20.6	2.2 18.4
1984	35.5	26.3	7.8	10.0	7.7	0.7	9.3	1.9 7.4

TABLE 12.3
CLAIMS AGAINST NON-FINANCIAL SECTOR, CLASSIFIED BY MARKETABILITY: FIRS

	GRAND TOTAL	MARKETABLE INSTRUMENTS				NON-MARKETABLE INSTRUMENTS			
		TOTAL	GOVERNMENT SECURITIES	SHARES & BONDS	FOREIGN SECURITIES	BILLS	TOTAL	HOUSEHOLD	BUSINESS
1971	N.A.	N.A.	25.7	N.A.	36.0	0.0	19.4	1.7	17.8
1972	N.A.	N.A.	21.8	N.A.	24.7	5.4	30.9	2.5	28.4
1973	N.A.	N.A.	6.6	N.A.	20.5	11.0	44.5	3.6	40.9
1974	N.A.	N.A.	13.5	N.A.	12.5	2.4	16.1	1.4	14.7
1975	90.2	71.6	22.3	29.4	18.6	1.3	18.6	0.7	17.8
1976	75.5	58.0	27.2	12.4	13.2	5.2	17.6	1.8	15.7
1977	151.9	138.3	31.9	80.3	12.9	13.6	13.6	1.2	12.4
1978	44.0	8.9	23.0	-57.8	36.2	7.4	35.1	1.6	33.5
1979	93.1	53.1	19.3	8.9	12.1	12.8	40.0	3.4	36.6
1980	94.7	49.0	20.0	16.6	10.8	1.5	45.7	3.1	42.5
1981	127.3	76.4	18.7	36.5	13.1	8.2	50.9	2.7	48.2
1982	96.8	59.0	24.8	22.3	17.1	-5.2	37.8	1.4	36.4
1983	98.2	55.0	25.5	19.3	11.1	-0.9	43.2	4.6	38.6
1984	73.1	54.1	16.1	20.7	15.8	1.5	19.1	3.9	15.2

THE FINANCIAL STRUCTURE AND ITS IMPLICATIONS FOR MONETARY POLICY IN SRI LANKA

by
A.G. Karunāsena

I. INTRODUCTION

The financial sector, as some of the other sectors of the Sri Lankan economy, has experienced continuous improvements, expansion and structural changes during the period which followed after the political independence of the country in 1948. With these developments, the financial system increased its services not only to improve the smooth functioning of the economic activities of the country but also its assistance towards achieving a high level of economic development.

The financial structure of a country is closely related to its economic structure because financial institutions have the important role of providing financial intermediation for economic activities by mobilising savings from surplus units and lending these funds to deficit units. Furthermore, an efficient financial system serves as a financial vehicle to achieve rapid economic growth rates. Also, due to the inter-relationship of the financial and the economic structures their impact on either is interdependent.

Sri Lanka, with a population of about 16 million in 1984, is mainly an agricultural and a trade dependent small economy. Its per capita income is about US\$335 (Rs.8,643) in 1984. The country experienced a marginal economic growth during the post-independent period while the population grew at a high rate, around 2 per cent annual rate, though it decelerated in the last few years. Despite the massive investments of the Government in development programmes and various production incentives offered by several institutions, the economy faces a number of problems even today, such as unemployment,

inflation, balance of payment problems and slow growth rate in aggregate production. However, the newly-independent government introduced a number of welfare schemes to subsidise basic needs such as food, health and education. The country's economic structure was basically an export oriented agricultural economy under the colonial system and experienced gradual changes after the political independence in 1948.

Thus, the economy has undergone several structural changes during the last three and a half decades. It is not necessary to emphasise the fact that the present structural characteristics of the economy are results of historical developments and policies implemented by governments from time to time and helped the system to evolve to its present position. Similarly, the present structure of the financial system in Sri Lanka and its changes during the last three and a half decades are also results of historical developments and government policies implemented during the period under study.

Hence, the purpose of this study is to analyse the changes in the financial structure and their implications for monetary policy in Sri Lanka during the period 1950 to 1984.

This study covers the entire financial system of the country. However, some activities of some financial institutions are not analysed deeply compared with others due to lack of data. The selected time period for the data analysed is from 1950 to 1984, except in some cases where data is not available for the 1950s and the 1960s. However, more analytical emphasis is given for the more recent period. Also, the study covers all the financial institutions and instruments for which information is available. The only section in the system not analysed in detail is the unorganised financial sector due to lack of required information. Hence the coverage of the study is wide. The evaluation of the effectiveness of monetary policy in this study is based on the financial structure and its changes through time.

The study is divided into four main sections, namely, an overview of the financial system, an analysis of the financial structure, the implications for monetary policy and summary and conclusion of the study.

Section II provides an overview of the financial structure in Sri Lanka, discussing the historical perspective and the major activities of the financial institutions and their legal frameworks as well as the financial instruments. In sum, Section II serves as the introductory part of the study.

In Section III, an attempt is made to evaluate the financial structure of the country. The evaluation is done in the form of an analysis of the importance of the entire financial system and the aggregate value of financial instruments in relation to the size of the economy. Also, attention is focussed on changes in the relative size of each type of institutions and type of instruments used from time to time.

Section IV is devoted to a discussion of policies on the financial structure and their implications on the transmission process and effectiveness of monetary policy.

Finally, a summary and conclusion of the study are given in Section V.

II. INSTITUTIONS AND INSTRUMENTS IN THE FINANCIAL STRUCTURE

In this section, an overview of the financial structure in Sri Lanka is presented by discussing the historical perspective and providing a general description of financial institutions and instruments in the country.

The financial institutions in Sri Lanka were in the very early state of development prior to the establishment of the Central Bank in 1950. The commercial banks mainly financed import and export trade, in keeping with the limited needs of the economy which was largely dependent on the plantation sector. Consequently, banking activities were confined to Colombo and a few provincial capitals. Meanwhile, the activities of other financial institutions were also not significant during this period. The situation was further worsened due to the absence of an authority with powers to administer, regulate and promote the financial system in the country. With this background, the Central Bank of Ceylon which was established in 1950 was entrusted with the task of developing and controlling the financial institutions thereby creating a conducive environment for the economic progress of the country. The decades that followed the establishment of the Central Bank witnessed a rapid development in the financial system. Some of the institutions which entered the financial scenario since 1950 were established/promoted by the Central Bank while some were necessitated by developments that took place in the economy. Responding to these changes, the money and capital markets also indicated significant development in the recent years.

The number of financial institutions in Sri Lanka increased from 15 in 1950 to 17 in 1960 and further to 18 and 104 in 1970 and 1984, respectively. Similarly, the number of branches of financial institutions increased from 31 in 1950 to 49 in 1960 and further to 259 and 1,725 in 1970 and 1984, respectively. The total nominal value of financial instruments increased from Rs.1,894 million in 1950 to Rs.146,835 million in 1984 while its real value rose from Rs.1,957 million to Rs.28,357 million during the same period. Furthermore, the real per capita financial instruments increased from Rs.255 in 1950 to Rs.1,818 in 1984. All of these indicators show that the financial structure in Sri Lanka has expanded and improved significantly during the period of 1950 to 1984 (see Table 1).

INSTITUTIONS IN THE FINANCIAL STRUCTURE

The financial institutions existing in the country can be broadly categorised as the Monetary Authority, i.e., the Central Bank, commercial banks, savings institutions, rural banks, development banks, finance companies and other specialised financial institutions such as merchant banks and leasing companies. The savings institutions include the National Savings Bank (NSB) and the four major contractual savings institutions, namely, the Sri Lanka Insurance Corporation, the National Insurance Corporation, the Employees' Provident Fund and the Employees' Trust Fund. The development banks that are in operation are the National Development Bank, the State Mortgage and Investment Bank and the Development Finance Corporation of Ceylon. Finance companies which are engaged in deposit mobilisation, lending and hire purchase business, transact mainly at the short and medium ends of the market. The composition of the financial system in Sri Lanka is given in Chart 1.

The money market comprises four major sub-markets, namely, the inter-bank call money market, limited off-shore market, international foreign exchange market and the Treasury bill markets (primary and secondary). The capital market transactions are mainly confined to share transactions and hence, consist of primary and secondary share markets.

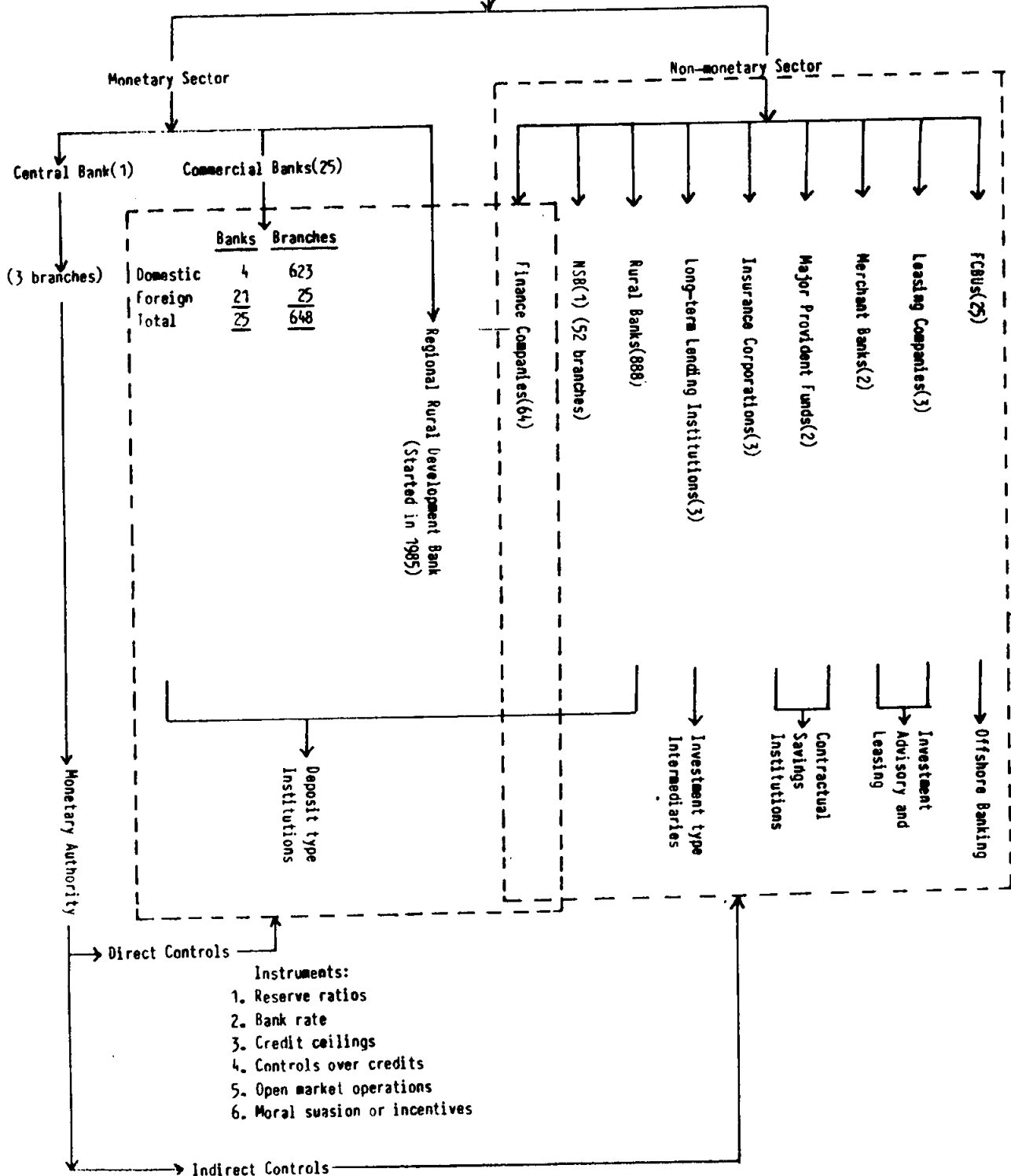
The Monetary Authority

The monetary system that prevailed in Sri Lanka prior to 1950 was the Currency Board System. This system had been functioning in the country since the enactment of the Paper Currency Ordinance of 1884. The Currency Board was not given any powers to influence the money supply. The Board was expected to increase or reduce the currency issue along with the increases or reductions in the external reserves. Thus, the currency issue was directly linked to the external trade. The other component in the money supply, i.e., bank

Chart 1

FINANCIAL SYSTEM OF SRI LANKA (As at end of 1984)

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Note: Number of institutions are given in brackets.

- (1) After 1979 the Central Bank introduced some direct controls (liquidity ratio, restriction on credits for imports etc.) over finance companies.

deposits, was also directly responsive to balance of payments position. During this period, bank deposits emanated almost entirely from the plantation sector. Thus, the Currency Board performed a purely passive role as far as the money supply is concerned. Furthermore, the Currency Board did not have the power to fix or maintain the external value of the Sri Lanka rupee which was linked to the Sterling Pound via the Indian rupee.

In view of the inherent weaknesses of the Currency Board System, a need for the establishment of an independent monetary authority was greatly felt, particularly after Sri Lanka gained independence. As a result, the Central Bank of Ceylon was established in 1950, with an initial capital of Rs.15 million, in terms of the Monetary Law Act (MLA). As indicated in the MLA, the Central Bank was established as the authority responsible for the administration and regulation of the monetary and banking system in Sri Lanka. The Monetary Law Act empowers the Central Bank to regulate the supply, availability, cost and international exchange of money with a view mainly to stabilising the domestic and international value of the Sri Lanka rupee and promoting/maintaining a high level of production, employment and real income. The Bank is also entrusted with the task of developing productive resources of Sri Lanka.

To achieve these broad objectives, the Central Bank was given wide powers for the purpose of achieving stability. The Bank influences aggregate demand through quantitative credit controls, while selective credit controls are employed to reduce or stimulate demand in selected areas. The Bank places emphasis on supply promotion policies to achieve growth on the one hand and long-term stability on the other. The supply promotion measures include the refinance scheme operated by the Central Bank, which makes available adequate low cost funds to priority areas such as agriculture, exports and industry. Medium and long term funds are channelled to productive sectors through refinance facilities provided under the Medium and Long-term Credit Fund established in 1964. In addition, short-term

refinance facilities, too, are made available to agricultural and export sectors under various refinance schemes.

As mentioned above, the Central Bank contributed significantly towards developing the financial system. The Bank took steps to create a state sector in the banking industry. The two state banks, i.e., the Bank of Ceylon and the People's Bank have become the two largest banks in the island. The Central Bank further participated in promoting the establishment of the other two domestic banks, namely, the Hatton National Bank and the Commercial Bank of Ceylon. The Central Bank also performed an important role by making recommendations for and assisting the establishment of a number of financial institutions such as the Development Finance Corporation of Ceylon, National Savings Bank, National Development Bank and the State Mortgage and Investment Bank. As the authority responsible for the administration and regulation of the banking system, the Central Bank is required to inspect, supervise and regulate the operations of the banking system. The Bank Supervision Department, the establishment of which is a statutory requirement in terms of the MLA, is responsible for the continuous supervision and periodical examination of banking institutions. In recent years, the Central Bank widened its supervisory role by starting to supervise the finance companies too.

The Central Bank continued to perform an important role with respect to the development of the banking system. In terms of the MLA, the written approval of the Central Bank is required to establish a bank and no commercial bank shall open any branch, agency or office thereof in any part of Sri Lanka except with the prior approval of the Minister of Finance and Planning. An application seeking approval to open a bank will have to be made initially to the Central Bank. After examining the application carefully, the Central Bank makes recommendations and the Minister of Finance and Planning would make the final decision.

Deviating from the hitherto followed practice of confining the Central Bank activities to Colombo, the Central Bank started to decentralise some of its operations in 1981. In 1981, the Bank opened its first regional branch in Matara, in the Southern Province. In 1982, the Bank opened its second regional branch in Anuradhapura in the North-Central Province. The Bank is expected to open more branches in other regions in the years to come. The objective of establishing regional offices is to promote economic activities in these areas. Moreover, it contributes towards improving the financial system.

The growth in total assets/liabilities of the Central Bank during the last three decades has been very impressive. The total assets/liabilities which stood at Rs.587 million as at end of 1950 rose to Rs.3,333 million by end 1970. These assets/liabilities further rose to Rs.22,832 million and Rs.33,272 million by end of 1980 and 1984, respectively.

Commercial Banks

In Sri Lanka, there is no separate law governing the establishment of commercial banks. The relevant regulations are found in laws such as the Monetary Law Act and amendments thereto, Companies Ordinance, Bills of Exchange Ordinance, Bank of Ceylon Ordinance and People's Bank Act.

There is evidence to show that the first commercial bank in Sri Lanka was established in 1828. But the first commercial bank and many banks which were established subsequently were short-lived. Prior to 1950, the banking activities in the country were not very impressive. Until 1939, the banking industry was in the hands of foreign banks whose activities were dominated by exchange business, in keeping with the needs of the plantations sector. Although attempts were made to form indigenous banks, until 1939 in which year the Bank of Ceylon was established, the country was deprived of a local bank to

cater to the needs of indigenous business community. Many of the foreign banks established in this period, too, were short-lived. The banking activities were centred in Colombo, while only a few branches were established in provincial capitals. The banking services were supplemented by chettians to a large extent, by providing credit to local entrepreneurs. However, banking activities were not satisfactory and this led to the appointment of a banking commission in 1934, to enquire and report upon the existing conditions of banking and credit in Sri Lanka and to consider the steps, if any, that were feasible and desirable in respect of the provision of banking and credit facilities for agriculture, industry and trade and also to make recommendations regarding the desirability of establishing a state-aided bank and a sound local bank.

In view of the shortcomings in the banking and credit structure, the establishment of a state-aided indigenous bank was recommended by the Banking Commission in 1934. Accordingly, the Bank of Ceylon was established in 1939 in terms of the Bank of Ceylon Ordinance 53 of 1938. The Bank of Ceylon (BC) competed successfully with the existing banks. By 1953, BC had established 10 branches outside Colombo.

The establishment of the Central Bank led to significant changes in the banking system. Thus, the year 1950 marked the beginning of a new era in the banking history in Sri Lanka. The Central Bank took steps to introduce a state sector into the banking system. The Bank of Ceylon was nationalised in terms of the Finance Act No. 65 of 1961, while the People's Bank was established under the People's Bank Act No. 29 of 1961. These two banks significantly contributed towards expanding banking activities to areas which had been neglected by the foreign banks. The two banks also engaged in an aggressive branch expansion programme thereby making available banking facilities to a large portion of the population in this country.

The Central Bank further participated in banking development by promoting the formation of banking companies. The Commercial Bank of Ceylon was established in 1969 with participants in its share capital from government corporations, the Eastern Bank and the public. In 1970, the Hatton National Bank was formed as a banking company with its share capital subscribed by a local company, the National Grindlays Bank and the public. These two banks were also permitted to open branches outside Colombo. However, the seven foreign banks which were in operation in the 1970s were not allowed to establish branches in outstations. Also, no new foreign banks were permitted to open branches in the country during this period.

The year 1977 marked a new era for the banking industry in Sri Lanka. The open economic policies introduced in Sri Lanka encouraged foreign banks of international repute to open branches in the country. Accordingly, three foreign banks opened branches in Colombo in 1979. Subsequently, 11 banks established branches in the country. Thus, the total number of banks operating in the country amounted to 25 by end-1984. The total number of bank branches in the country was 648 at end-1984.

Since 1977, the banking industry has undergone rapid changes. The banks expanded their activities catering to the changing needs of the economy. They actively participated in financing import and export trade which expanded since 1977. The competition among banks led to a general improvement in banking services. More complex and sophisticated services were made available to customers. The commercial banks, under the guidance of the Central Bank, established Foreign Currency Banking Units which are engaged in the provision of offshore banking services to non-residents and approved residents. The banks in competition with each other provided numerous incentives to savers thereby attracting more deposits. Novel instruments such as certificates of deposits were introduced.

The total assets/liabilities of commercial banks which stood at Rs.1,197 million as at end of 1960 rose to Rs.3,122 million by end 1970. These assets/liabilities further rose to Rs.26,601 million and Rs.50,382 million by end of 1980 and 1983, respectively. By end 1984, total assets/liabilities of the commercial banks stood at Rs.56,553 million.

Savings Institutions

The National Savings Bank. In view of the need to promote savings, the Central Bank took steps to create an efficient institutional framework for mobilising savings of the public. Accordingly, the National Savings Bank (NSB) was established in 1972 under the National Savings Bank Act No. 31 of 1971 by amalgamating the Post Office Savings Bank, the Ceylon Savings Bank and the National Savings Movement. Today, the National Savings Bank has been effectively engaged in mobilising domestic savings and channelling such savings towards economic development. The Bank provides incentives such as tax exemptions and higher interest rates to savers, thereby competing with the other deposit mobilising institutions. The Bank's savings schemes include savings accounts, fixed deposit schemes, savings certificates, gift tokens and special long-term savings schemes. The total amount of savings mobilised by the NSB amounted to Rs.11,611 million as at end of 1984. In addition to the provision of funds to the Government for development activities, the Bank is directly engaged in lending activities particularly housing loans to account holders. The total number of branches of the NSB stood at 52 by end 1984.

The insurance corporations. The Insurance Corporation of Sri Lanka that was established under the Insurance Corporation Act No. 2 of 1961 commenced business in 1962 as the sole institution transacting life insurance in the country. The Finance Act No. 11 of 1963 also vested in the Corporation the sole right of transacting general insurance as from January 1964. In 1984, the Corporation

issued 32,032 new life policies valued at Rs.1,041 million. The total number of life policies as at end of 1984 was 284,773 while the amount insured was Rs.3,397 million. The savings mobilised by the Corporation are invested in government securities, fixed deposits in commercial banks and in ordinary shares of private companies. In addition, the Corporation is engaged in the provision of housing loans to its policy holders and its employees.

The other contractual savings institutions in the country, the National Insurance Corporation, was established in terms of the National Insurance Corporation Act No. 22 of 1979. The Corporation commenced operations in 1980 as an insurer transacting life assurance and general insurance in the country. The Corporation has not engaged in any lending operations so far.

The Employees Provident Fund. The Employees' Provident Fund (EPF) was established in terms of the provisions of the Employees' Provident Fund Act No. 15 of 1958. Every employee, other than those excluded from the operation of this Act, is presently liable to contribute every month 8 per cent of his earnings to the Fund. The contribution of the employer is fixed at 12 per cent. The investment and management of the Fund is entrusted with the Monetary Board of the Central Bank. The savings mobilised by the EPF are invested mainly in government securities. Members' balance as at 31 December, 1984 before allocation of interest for the year stood at Rs.10,393 million as against Rs.2,051 million recorded for 1983.

The Employees' Trust Fund. The Employees' Trust Fund (ETF) was created by Act of Parliament No. 46 of 1980. The specific objectives of the ETF which became operational in March 1981 are to promote economic democracy in Sri Lanka and to provide meaningful retirement benefits to employees in public corporations and the private sector. The rate of contribution is 3 per cent of the monthly earnings of every employee and is paid by the employer. The ETF is empowered to invest or buy shares in enterprises, to establish and

operate commercial or industrial undertakings and to develop immovable property. The total assets/liabilities of the ETF amounted to Rs.1,014 million by end-1984.

The Development Banks

The Development Finance Corporation of Ceylon. The Development Finance Corporation of Ceylon (DFCC) was established in 1956 to provide long-term investment capital to the private sector. The DFCC was expected to cater to the need for long-term capital which was not sufficiently provided by the commercial banks. The objectives of the DFCC are as follows:

- (a) To assist in the promotion, establishment, expansion and modernisation of private industrial, agricultural and commercial enterprises in Sri Lanka; and
- (b) To encourage and promote the participation of private capital, both internal and external, in such enterprises.

The DFCC assists the private sector by providing long-term capital at subsidised rates of interest, participating in equity in private sector investments, providing certain merchant banking facilities, guaranteeing of loans and participating in consortium lending.

During 1984, the DFCC approved loans amounting to Rs.318 million while loans granted in 1984 amounted to Rs.220 million.

The State Mortgage and Investment Bank. The State Mortgage and Investment Bank (SMIB) was established in 1979, amalgamating the Agricultural and Industrial Credit Corporation and the State Mortgage Bank which were established in 1943 and 1931, respectively. According to the State Mortgage and Investment Bank Law No. 13 of 1975, the

objective of the Bank is to provide, inter alia, loan facilities for the agriculture, industry, fishing and housing purposes. The Bank's outstanding loans granted at end 1984 stood at Rs.494 million.

The National Development Bank. The National Development Bank of Sri Lanka (NDB) established under the National Development Bank of Sri Lanka Act No. 2 of 1979 commenced business in 1979. The main function of the Bank is to promote the industrial, agricultural and commercial development of the economy having regard to the development of the rural sector. The Bank is expected to grant term financing and other assistance to appropriate enterprises to stimulate the investment, share and security markets of Sri Lanka. The Bank is also expected to mobilise internal and external capital for investment in industrial, commercial, agricultural and other enterprises, thereby contributing towards the economic development of the country.

At present, the Bank is mainly engaged in refinancing and direct lending activities. The Small and Medium Industrial Project, under which refinancing facilities are granted to lending institutions, is financed by two lines of credit made available to the Government by the International Development Association. The first loan of US\$12 million was fully committed by the end of 1981 and the second loan of US\$28 million was negotiated in August 1981.

At-end 1981, its total loans outstanding was Rs.935 million while equity investments in development projects amounted to Rs.58 million. The total refinance credit outstanding amounted to Rs.103 million at the same date.

Finance companies

The finance companies (FCs) are generally engaged in the business of accepting term deposits and provision of hire purchase finance. At present, the finance companies are governed by the Finance Companies Act No. 27 of 1979. The necessity for

controlling/regulating the FCs arose due to several reasons such as their considerable impact on the monetary and banking system, and the need to ensure liquidity and solvency of these companies to protect the interest of depositors.

The FCs are compelled to compete with the commercial banks and other savings institutions in mobilising deposits. Therefore, they usually offer higher rates of interest which in turn raise their lending rates.

In 1984, 50 FCs furnished information on their assets and liabilities on a regular basis. Total deposits of these FCs rose from Rs.1,404 million to Rs.2,453 million during 1984. Meanwhile, amounts outstanding under hire purchase business rose from Rs.1,010 million to Rs.1731 million during the year.

Rural Banks

The scheme of rural banks (RBs) was inaugurated in 1964 by the People's Bank as the major avenue for mobilising rural savings and channelling credit to the rural sector. In a strict sense, RBs are not commercial banks because they do not accept demand deposits and their activities are limited. However, during the past two decades, the RBs grew in number providing basic banking services to a large portion of the rural population. At end-1984, the total number of RBs stood at 888 while their total assets/liabilities amounted to Rs.905 million at the same date.

Other Specialised Financial Institutions

The Sri Lanka Export Credit Insurance Corporation. The Sri Lanka Export Credit Insurance Corporation (SLECIC) was established by Act 15 of 1978 and commenced operations in 1979. The Corporation was created in view of the need to promote exports under the new economic

policies introduced in 1977. The major objectives of the Corporation are:

- (a) To issue insurance policies to exporters of goods and services against non-receipt or delayed receipt of payments resulting from commercial and non-commercial risks;
- (b) To issue guarantee to banks and other financial institutions to facilitate the granting of pre-shipment and post-shipment finances;
- (c) To issue guarantees to persons or institutions abroad in connection with goods exported by any person or institution from Sri Lanka or for the due performance of any services to be rendered to such persons or institutions, within or outside Sri Lanka;
- (d) To help exporters to diversify and expand exports, find new markets and sell their goods abroad on competitive terms of payments; and
- (e) To discharge such other functions as the SLECIC may consider as necessary for the achievement of any of its objectives.

The SLECIC, with the idea of promoting, and diversifying the country's export trade, introduced two schemes in 1979. These were the Credit Guarantee Scheme and the Export Payment Insurance Scheme. Under the Guarantee Scheme, the pre-shipment, post-shipment and export performance guarantees issued and in force at end-1984 were Rs.888 million, Rs.94 million and Rs.96 million, respectively.

Merchant banks. The establishment of merchant banks was necessitated by the development that took place in the economy since

1977. To cater to the growing demand for more specialised financial services, the Bank of Ceylon established a separate division in 1981 to deal exclusively with merchant banking and consultancy services. In 1982, this division was replaced by the Merchant Bank of Sri Lanka Limited, a subsidiary of the Bank of Ceylon. In 1983, the People's Bank also established a merchant bank, namely, the People's Merchant Bank, in collaboration with the Guinness Mahon & Co. Ltd. of London. Services provided by these merchant banks include consultancy and advisory services, equipment leasing, discounting of trade bills, and brokering.

Leasing companies. Three leasing companies, namely Mercantile Lloyds Leasing Company, Lanka Orient Leasing Company and Maharajah Leasing Company were established in Sri Lanka in recent years. Leasing is a new concept in the context of Sri Lanka. These three leasing companies are still in the infant stage with respect to their activities.

The Money Market

By definition, the money market consists of sub-markets operating at the short end of the market transacting in financial assets whose maturity periods are less than one year. The inter-bank call money market, the primary and secondary Treasury bill markets, the internal foreign exchange market and the limited off-shore market are the major sub-markets in the money market of Sri Lanka. Money broking firms operate in all these sub-markets. At present, seven money broking firms are in operation.

Inter-bank call money market. In Sri Lanka, the inter-bank call money market transactions are normally dominated by commercial banks. The National Savings Bank (NSB) and the National Development Bank (NDB) occasionally participate in this market. During the last few years, activities of this market increased significantly following the commencement of operations by branches of foreign banks.

Commercial banks deal directly or through money brokers in this market, depending on their liquidity position. Usually, monetary policy measures effected by the Central Bank, the amount of liquidity available to the banking system, the demand for credit and in some cases, institutional forces exert direct impact and change the interest rates and overall transactions in this market. The foreign banks, whose deposit base is narrower when compared with those of the indigenous banks, often resort to short-term funds in the call market.

Primary Treasury bill market. The Central Bank has been the major buyer in the primary Treasury bill market as the participation of commercial banks and the non-bank public in this market has been marginal.

Secondary Treasury bill market. The introduction of a secondary Treasury bill market (STB) by the Central Bank in April 1981 was a significant move towards the development of a sub-market on Treasury bills. The movement of funds to and from this market has been corollary to the transactions in the inter-bank call money market. At the beginning, interest rates on secondary Treasury bills followed the call money rates. However, since 1982 the Central Bank intervened in fixing the secondary bill market rates in view of the excess liquidity situation experienced by most commercial banks.

Internal foreign exchange market. Effective November 1977, Sri Lanka departed from the practice of adopting a multiple exchange rate system through the unification of the exchange rate. Since then, the Sri Lanka rupee was allowed to float in the exchange market vis-a-vis the other foreign currencies. The objective of this reform was to create a more market-oriented exchange rate for Sri Lanka, thereby allowing the smooth functioning of the open economic policies pursued by the Government.

With the introduction of the unified exchange rate, the value of the Sri Lanka rupee was determined at daily meetings held by the Central Bank and commercial banks. The indicative rate given by the Central Bank, the fixing of the rate at daily meetings and the continuous intervention of the Central Bank ensured a greater degree of stability in the market. Commercial banks were allowed to square their foreign exchange position among themselves or with the Central Bank. The Central Bank also determined the maximum buying and selling rates of foreign exchange on telegraphic transfers to be applied by the banks for their customers. In November 1982, the Central Bank discontinued fixing the exchange rate at daily meetings and the Central Bank's foreign exchange transactions with commercial banks were limited to purchases and sales of spot dollars (U.S.) and forward purchases of dollars up to six months. Under this practice, the Central Bank announced the official buying and selling rates on telegraphic transfers to banks. Consequently, commercial banks are now allowed to determine their own buying and selling rates for various foreign currency instruments such as bills, drafts and travellers' cheques.

In January 1983, the Sri Lanka Forex Club was established with the objective of fostering personal contacts between foreign exchange and money market dealers in Sri Lanka and abroad with a view to promoting friendship and mutual trust. It was also expected to improve techniques of foreign exchange dealings. The establishment of the Forex Club could be considered as an important step in the development of Sri Lanka's financial market on more sophisticated lines.

Limited offshore market. Foreign Currency Banking Units (FCBUs) were introduced with a view to developing offshore banking activities in Sri Lanka and to cater to borrowing requirements of the entrepreneurs in the Free Trade Zone (FTZ) which was created in 1979. The number of the FCBUs established with commercial banks totalled 25 at the end of 1984. The major part of the operations of these units

include financing projects in the FTZ, Euro-currency lending to approved residents and participating in Euro-currency loan syndicates.

The total assets and liabilities of FCBUs increased from US\$366 million (Rs.7,516 million) at end-December 1981 to US\$756 million (Rs.19,870 million) at end-December 1984.

The Capital Market

While the money market deals at the short end of the financial market, the capital market by nature deals at the long end. However, there is a fair degree of overlapping between the two markets and hence, one market cannot be clearly separated from the other.

The origin of the capital market in Sri Lanka can be traced back to the early 19th century when the needs of the export-oriented plantation economy were met to a limited extent by the issue of shares and debentures of companies formed in Sri Lanka and the United Kingdom. In 1894, the Share Brokers Association was set up to meet the growing long-term financial requirements of the tea and rubber plantations. In 1904, the Colombo Brokers' Association took over the control of the Colombo share market. The rules and regulations governing the share business were first enforced in 1910 and the requirements for quotations and dealings of rupee company shares were introduced in 1955. During the colonial era, the Colombo share market even dealt with securities of companies quoted in foreign financial markets. Although share transactions were largely confined to foreign citizens and a few urban locals, the share market was fairly active. With the introduction of exchange control regulations in 1953, these activities gradually diminished. Meanwhile, from 1960 onwards, a rapid development was experienced in the field of commercial lending. However, it was biased more towards short-term financing of trade. The provision of long term credit accounted for only a minimal share of total advances and came under the Medium and Long-term Refinance Scheme of the Central Bank.

With the re-awakening of the economy through the adoption of liberalised economic policies, the private sector began to play an important role in the economic resurgence. A number of public companies were established, increasing the supply of shares in the capital market. Consequently, the limitations and distortions which hindered the development and efficient working of the capital market were brought to the notice of the Government and action was initiated with a view to revitalising the activities of this market. The establishment of an effective capital market was among the major objectives of financial development in Sri Lanka.

The capital market in Sri Lanka constitutes two sub-markets, namely, the primary market relating to the supply of initial finance for a new company or the Government, and the secondary market providing facilities for trading in existing securities of the Government or companies. At present, these twin facilities in the capital market are covered by the Colombo share market, commercial banks and other financial institutions.

INSTRUMENTS IN THE FINANCIAL STRUCTURE

Financial instruments in Sri Lanka can be classified into two broad categories, namely, claims and equity securities. Subsequently, financial claims can be divided into claims of non-financial units against financial institutions and claims of financial institutions against non-financial units.

Currency, certificates of deposits and the Central Bank securities are marketable claims of non-financial units against financial institutions while demand deposits, interest-bearing deposits, insurance premium and contributions to pension and provident funds are their non-marketable instruments. Government securities, Treasury bills, corporate bonds and export bills are major items among claims of financial institutions against non-financial institutions.

The category of equity securities can be further divided into marketable issues and non-marketable issues. However, a comparable and complete data is not available for the category of equity issues in Sri Lanka for the period under review. Nevertheless, the share of this category is very small compared with claims based on available information.

The use of financial instruments increased and expanded during the last 34 years in Sri Lanka. Not only new financial instruments were introduced during the period but also the quality of instruments and their availability improved significantly. Commercial banks and other financial institutions offered new financial instruments mainly through their deposit mobilisation schemes. Also, the Central Bank improved the composition of the available set of notes and coins. The expansion and improvement of financial institutions increased the availability of financial instruments and their services to the public.

Currency was the major financial instrument in the marketable claims of non-financial institutions against financial institutions while the deposits in commercial banks, NSB and finance companies are the major non-marketable claims of non-financial units against the financial sector. As in many other developing countries, government securities and Treasury bills are the major marketable claims of financial institutions against non-financial institutions while bank loans are their non-marketable claims in Sri Lanka.

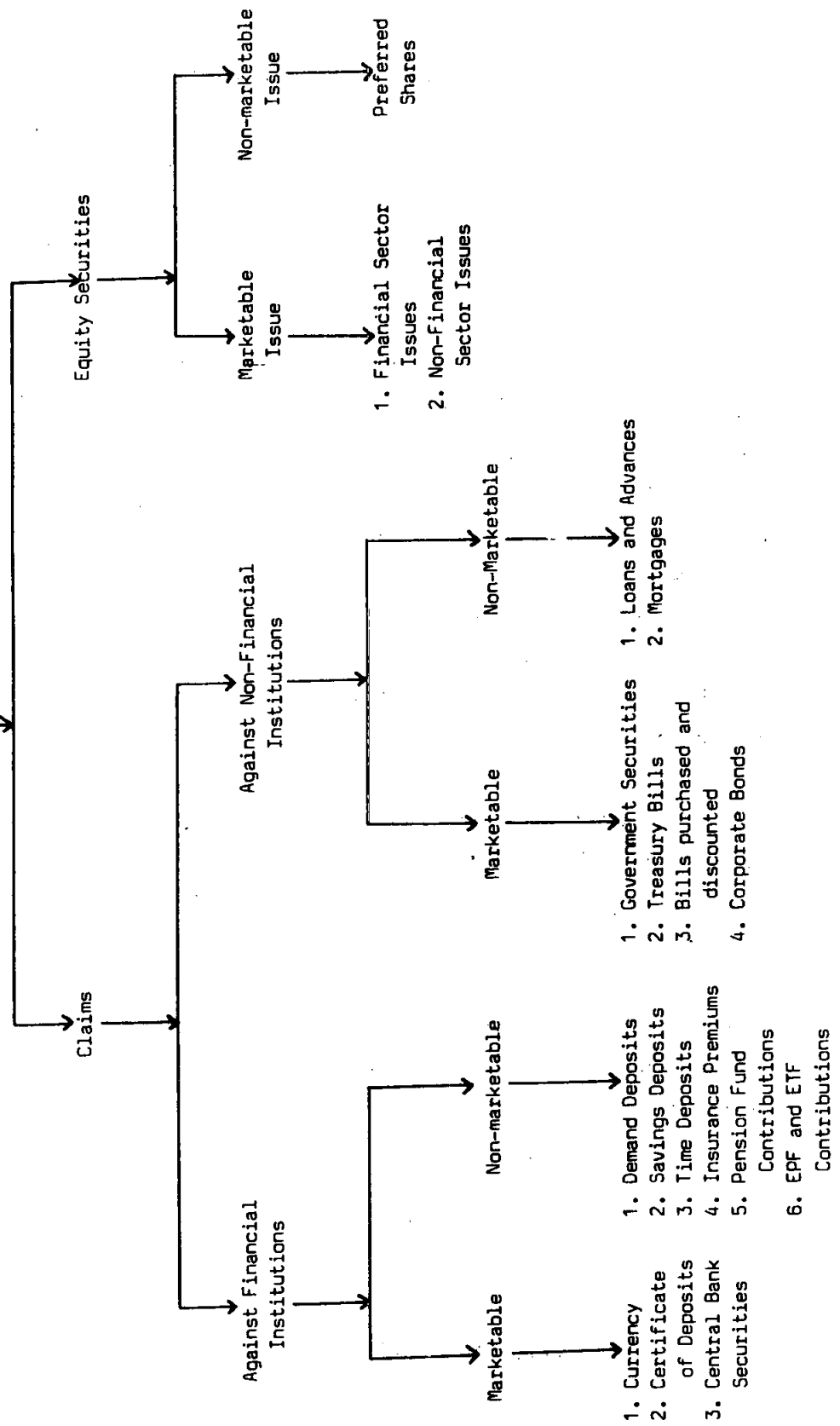
The composition of financial instruments in Sri Lanka is given in Chart 2.

III. ANALYSIS OF THE FINANCIAL STRUCTURE

An analysis of the country's financial structure is essential to perceive the workings of monetary instruments towards the

Chart 2

FINANCIAL INSTRUMENTS IN SRI LANKA
(As at end of 1984)



achievement of the main objectives of economic policies, i.e., the transmission mechanism and to evaluate the effectiveness of the monetary policy. Over the last three and a half decades, Sri Lanka's financial structure has experienced significant developments and changes. The continuous expansion of the financial system and the gradual extension of monetisation and subsequently the financial transformation of the economy tend to significantly influence savings-investment activity in the country. Hence, the objective of this section is to analyse the evolution of the financial structure of Sri Lanka based on currently available information. This will be done in the form of examining the composition of institutions, the importance of the entire financial system and aggregate financial instruments in relation to the economy. Also an attempt will be made to analyse changes in the relative magnitude of each type of financial institution and financial instrument during the period.

As in any other country, the financial structure of Sri Lanka consists of institutions in the monetary and non-monetary systems. The present monetary system of the country comprises the Central Bank and 25 commercial banks while the non-monetary system comprises savings institutions, rural banks, four long-term credit institutions sponsored by the government, 64 finance companies, two merchant banks, seven money brokers, three insurance corporations, three leasing companies, 25 FCBUs and two major employees' provident funds. Furthermore, there are a few money and capital market institutions operating in the country.

The distinction between the monetary system and the non-monetary system is made on the basis of the applicability of monetary controls and the effectiveness of such controls. The operations of the monetary system are directly affected by the changes in monetary policy while the operations of non-monetary system are not affected by these policy measures except indirectly. Also, the transactions in the non-monetary system are not counted as monetary transactions for purposes of monetary policy. Although the financial inter-connection

between these two sectors in the country has developed over the period, there does not seem to be a very strong link even at present. For instance, the dependence of the non-monetary system on the monetary system for financial resources is marginal except in few cases, especially to the Central Bank and commercial banks which supply funds to the long-term lending institutions. Similarly, the non-monetary institutions' investments in the monetary system are limited to their current savings and fixed accounts in commercial banks and limited participation in the call-money market.

A brief discussion of major institutions in the financial system will help to understand the relative position of the financial system in the economy, the general indicators of financial development and the structural changes in the financial sector.

Table 2 gives the number of institutions in the financial system with their branches. There are 104 institutions and 1,725 branches in the financial system in 1984. Among them, 26 institutions and 651 branches are under the monetary system while all others are under the non-monetary system. As in any other country, the deposit-type institutions (commercial banks, the NSB, and finance companies) dominate in the Sri Lanka financial system. Also, the NSB, the finance companies, the two provident funds and two insurance corporations accounted for a large share in the non-monetary sector. Merchant banks and leasing companies are still in the infant stage.

Other than these institutions,, there are some government institutions for the purpose of supplying financial facilities for housing construction.

As can be seen from Table 2, the financial structure has been modernised in recent years with the establishment of many sophisticated new financial institutions. However, the commercial banks still play a major role in the financial structure of Sri Lanka.

The Central Bank is at the apex of Sri Lanka's financial system. As any other central bank, it serves as the currency issuing authority, bank for commercial banks, supervisor and regulator of financial institutions, policy adviser to the Government and as an authority responsible for monetary policy of the country. Its income is derived mainly from investment in government papers and foreign securities and lending to commercial banks. Table 3 gives the major items in the assets and liabilities of the Central Bank. On the assets side, the relative share of foreign assets has declined while the domestic component increased its share during the period under study. Loans to the Government and investments on government securities are the major domestic assets of the Bank. Currency issue and commercial banks' deposits are the major liability items.

As in any other developing country, the financial structure of the country is dominated by the commercial banking system. The number of banks observed a negligible growth in the 1950s and 1960s but a high growth rate was noted after new economic policies were introduced in 1978. The number of commercial bank branches increased from 28 in 1950 to 45 and 165 in 1960 and 1975, respectively, and further to 680 in 1983. As a result of the amalgamation of some branches due to security reasons, the number of branches declined to 648 in 1984. Although Sri Lanka has a branch banking system, most of the foreign banks are confined to Colombo except for two branches of foreign banks which have one branch office each out of Colombo. The domestic banks, mainly the Bank of Ceylon and the People's Bank, owned more than 95 per cent of branches in 1984. Table 4 gives the assets and liabilities of the commercial banking sector. Their major asset items are loans and advances to the private sector and purchased and discounted trade bills while their major liabilities are deposits and borrowings from the money market. In 1984, loans and advances accounted for 64 per cent of total assets while deposits accounted for 69 per cent of liabilities. Traditionally, the business of foreign banks is concentrated in financing the requirements of export-import trade while the two state banks dominate in the financing of

requirements in the agricultural and industrial sectors. Also, both state banks assist in implementing government agricultural and industrial credit schemes.

Mobilisation of rural savings and supply of rural credit are the main functions of a rural bank. It also engages in pawn broking business. These banks are not required to maintain reserve requirements. However, they do maintain a close and continuous relationship with the People's Bank. Deposits of customers and borrowings from the People's Bank are the major sources of funds of these banks while advances and deposits in commercial banks are their major assets.

The National Savings Bank occupies a predominant place among savings institutions. It increased its branches from 20 in 1975 to 52 in 1984. It also operates through the network of post offices scattered throughout the country. In addition, the NSB operates mobile banking facilities. Table 5 gives the composition of assets and liabilities of the NSB. Private sector deposits accounted for 97 per cent of total liabilities in 1984 while investment in government papers contributed 89 per cent of total assets.

The three insurance corporations and the two employees' provident funds are the major contractual savings institutions. These institutions do not accept savings accounts. The members' contributions to the funds and returns on investments are the two sources of funds for EPF and ETF while refunds for members with interests are the major expenditures. The main difference between these two funds is that the employees and employers both contribute to the EPF while only employees contribute to the ETF. Furthermore, the EPF invests in government papers while the ETF invests mainly in private sector equities. Apart from these two funds, there are a large number of private provident and pension funds operating in the country. However, no reliable compiled data are available regarding them.

The state-owned two insurance corporations enjoy a monopoly position with respect to both life and general insurance business in Sri Lanka. Premium collections and income from investments less claims comprise the net financial resources of the corporations. Their funds are invested mainly in government securities.

The activities of the long-term lending institutions are limited to lendings for private sector investment projects in production sectors and for housing construction. Contributions from the Central Bank, domestic commercial banks and international financial organisations and income from issuing debentures are the sources of funds for them.

All active finance companies do not supply data regularly. Only 50 finance companies supplied comparable data before 1983 to the Central Bank while this number increased to 64 in 1984. The deposits collected from customers are the main source of funds of these companies and they compete with the NSB and commercial banks for interest bearing deposits. As a compensation for the high risk element contained in their deposits, finance companies offer high interest rates for depositors. Hire purchase business comprised the main lending activities of these companies as given in Table 6. Thus, deposits are the major liabilities of these companies while loans and hire purchase lendings, their major assets. Finance companies are no longer free from Central Bank regulation as was the case before 1979. Since December 1979, they are subjected to the statutory liquidity ratio as specified by the Central Bank.

The two merchant banks and three leasing companies started their business very recently. Hence, adequate information regarding them are not available yet. However, they help raise the level of sophistication in the financial system.

RELATIVE IMPORTANCE OF THE FINANCIAL STRUCTURE

The relative importance of the financial structure is evaluated on the basis of the importance of the entire financial system and the aggregate value of financial instruments in relation to the economy as well as the changes in the relative magnitude of each type of institution and instrument. A number of indicators are selected for this purpose, depending on the availability of data.

Relative Position of the Financial System to Total Employment and GDP

The relative position of the financial system in the composition of employment and Gross Domestic Product (GDP) is given in Table 7. The relative contribution of the financial system to total employment of the country increased from 0.5 per cent in 1963 to 0.7 per cent in 1973 and further to 1.1 per cent in 1981. Similarly, in the composition of GDP of Sri Lanka, the share of the financial sector increased from 0.9 per cent in 1953 to 1.3 per cent in 1973 and further to 2.9 per cent in 1984. Thus, the financial system's relative shares in both employment and GDP registered upward trends during the period under review.

Table 8 shows the share of total financial instruments or assets to national wealth, otherwise known as the financial interrelations ratio (FIR). This ratio is another indicator of the relative importance of the financial sector vis-a-vis the national economy. In Sri Lanka, the FIRs obtained from 1950 to 1984 revealed an increasing financialisation of the economy. The FIRs of a little more than .30 in the 1950s increased through the years, although not tracing a smooth trend, reaching as high as 1.14 in 1983.

Financial Intermediation Ratio

Another useful measure that can be used to evaluate the relative importance of the country's financial structure lies in the

degree of financial intermediation. When deficit economic units require additional funds through borrowings, they have to issue debt instruments, directly or indirectly to the surplus units. In this process, there is no financial intermediation involved if the deficit units issue their debt instruments directly to the surplus units. Thus, a financial intermediation takes place only when ultimate borrowers acquire surplus funds indirectly, that is, via financial institutions. In this process, financial institutions acquire surplus funds from non-financial economic units by issuing their claims against themselves through the issue of deposits and equities and subsequently lend this acquired funds to borrowers.

Hence, the financial intermediation ratio is defined in flow terms as the ratio of net acquisition during a given period by financial institutions of instruments issued by non-financial economic units to the total issues of such instruments. Because of the limitation in data availability proxies were used to derive the financial intermediation ratio for Sri Lanka. First, the difference of gross credit extended by all financial institutions to the private non-financial sector, the government and the external sector is summed up to derive the net acquisition or net purchase/sales balance by financial institutions. The major instruments that were considered in this analysis were equities and securities. Since data is not available on the flow of securities, it was defined as the sum of the first difference of credit extended by financial institutions for consumption purposes, and net fixed capital formation (gross fixed capital formation minus depreciation allowance) of the country. It can be argued that this proxy should be very close to primary securities issued by non-financial sector to finance their consumption and investment expenditures.^{1/}

^{1/} In the absence of a developed securities market, this may not be a good measure. The government securities market in Sri Lanka is a captive one and there is no developed secondary market for government securities.

The estimated value for this ratio increased from 46 per cent in 1950 to 64 per cent in 1970 and further to 87 per cent in 1984 as given in Table 9. The average value of this ratio was 51 per cent for the 1950s, 67 per cent for the 1960s, 76 per cent for the 1970s and 87 per cent for the first four years in the 1980s. Thus, the financial intermediation ratio registered an upward trend during the period under review. Apart from these impressive growth rates, the recent values of this ratio indicate a satisfactory level of financial intermediation.

Financial Intermediation to the Government Sector

Financial intermediation to the government sector is another useful indicator. This will not only help in evaluating financial intermediation in the government sector but also in getting an idea on the question of how the government competes with the private sector for funds and hence, the possibility for the effectiveness of open-market operations. The ratio of new government loans to the proxy representing the financial instruments issued by non-financial sector increased in the 1950s and in the 1960s and then decreased in the 1970s and the first half of the 1980s. The proportion of financial intermediation to the government sector comprises more than 40 per cent and it is considered too high in the light of limited availability of financial resources to the private sector. However, the contribution of commercial banks to government debt financing is very small. The contractual savings institutions and the NSB are the major financial lenders to the government in the last two decades.

Degree of Institutional Concentration

Table 10 gives the degree of institutional concentration according to relative shares of total assets of financial institutions in the country. In 1950, the banking sector accounted for 84 per cent of total financial system's assets and its share declined with some marginal fluctuations to 71 per cent in 1984. The relative values

varied between the range of 66-84 per cent during the period under study. Within the banking sector, commercial banks accounted for more than 50 per cent except in 1970 and 1975 when their share was almost equal to that of the Central Bank. During the last 34 years, the share of the Central Bank in total assets of the financial sector varied in the range of 27-37 per cent while the commercial bank share was in the range of 33-50 per cent.

The non-monetary sector's asset share in the financial system indicated an upward trend but with some marginal fluctuations. The sectoral share values varied between 16 and 34 per cent. Within the non-monetary sector, subsectoral shares are in the range of 8-6 per cent for the NSB, 0-1 per cent for rural banks, 1-3 per cent for finance companies, 1-2 per cent for long-term lending institutions, 1-7 per cent for insurance institutions and 6-15 per cent for provident funds.

Thus, it is clear that although the banking sector's relative share in the total assets of the financial system shows a downward trend, its sectoral value is still more than 70 per cent. Another important factor that can be observed from Table 10 is that the degree of sophistication of the banking sector increased, arising from the introduction of new types of financial institutions and instruments, though the total value of its assets grew at a marginal rate. The annual growth rate of assets of financial institutions in nominal terms was in the range of 4-31 per cent during the period while the respective growth rate for real financial assets was in the range of 3-20 per cent.

FINANCIAL INSTITUTIONS

In this section, financial institutions are classified according to the nature and characteristics of their liabilities as given in Table 11. Accordingly, five sub-categories are identified in

the financial system in Sri Lanka. The first category, the monetary authority, comprises the Central Bank of Ceylon and its major liabilities are currency and commercial banks' deposits. The second subcategory covers deposit-type institutions and more than 65 per cent of these institutions' liabilities are deposits. Institutions such as the two insurance corporations and provident funds are included in the third subcategory of contractual savings institutions and their major liability items are members' outstanding balances and contractual insurance values. Fourth, investment type intermediary subgroup covers medium and long term investment institutions and their major liabilities are borrowings and equities. Merchant banks, leasing companies and other financial institutions that are not included elsewhere comprise the fifth.

The first subcategory, the monetary authority, accounted for 27 per cent of total assets of the financial system in 1984 and this share was in the range of 30-37 per cent during the other selected year as given in Table 12. This sectoral share, therefore, shows a marginal downward trend with some fluctuations. The relative share of deposit-type institutions subcategory was in the range of 44-65 per cent in total assets. This subsectoral share value declined till 1970 and subsequently experienced an upward trend. The relative contributions of contractual savings institution to the total assets of the financial sector varied in the range of 7-22 per cent during the period of the study. This sectoral share shows an upward trend during the last four years though it experienced a declining trend before 1980. The relative asset share of investment-type intermediary subcategory was not more than 4 per cent and it was less than 2 per cent during the last two decades. Reliable information is not available for other types of financial institutional subcategory. However, the limited information available indicated that this subsector share in the total assets of the financial system was negligible even in 1984.

Financial Markets

As a result of the new economic policy to develop money and capital markets in Sri Lanka, there were a number of new developments in these markets during the last few years. After the introduction of money brokers' services in 1978, the activities of the money market increased substantially. The major submarkets operating in the Sri Lankan money market are the inter-bank call money market, primary and secondary Treasury bill markets, internal foreign exchange market and limited offshore banking market. The total outstanding value of lendings (or borrowings) in the call money market increased from Rs.2 million in 1950 to Rs.25 million in 1960 and further to Rs.3,394 million in 1984. Commercial banks trade directly or through money brokers in this market depending on the liquidity situation. The outstanding value of total offered primary Treasury bill market increased from Rs.79 million in 1950 to Rs.550 million in 1960 and further to Rs.14,860 million in 1984. The Central Bank was the major buyer in the primary Treasury bill market and participation of commercial banks has been negligible.

The secondary Treasury bill market introduced in 1981 by the Central Bank to improve a secondary market for government short-term debt papers improved during the last four years. The value of total sales/purchases varied according to the liquidity position of commercial banks. The total sales value increased from Rs.7,542 million in 1981 to Rs.39,587 million in 1984 indicating a 42 per cent annual growth rate. Activities in the internal foreign exchange market improved during the last four years continuously. Limited offshore banking activities conducted by Foreign Currency Banking Units reflected a significant progress during the last five years.

Major submarkets operating in the Sri Lankan capital market are the primary and the secondary share markets. The activities in the primary share market recorded a high growth rate in the 1980s. The number of share issues increased from 5 in 1980 to 37 in 1984

while the value of shares offered increased from Rs.14 million to Rs.1,004 million during the same period by observing 16 per cent annual growth rate. The value of total transactions in the secondary market increased from Rs.2 million in 1981 to Rs.24 million in 1984 reflecting a high growth rate. Selected values for primary and secondary share markets are given in Table 13.

Unorganised Financial Sector

Although continuous information is not available, the services of pawnshops, money lenders and kerb markets (especially in Colombo) cannot be ignored. The unorganised financial sector is still a major source of funds for short term purposes, especially consumption, cultural and social functions. However, loans obtained from the unorganised sector has shown a downward trend during the period under review. As shown by the Consumer Finance Survey (CFS) reports, the proportion of loans obtained by the household sector from the unorganised sector declined from 86 per cent in 1963 to 80 per cent in 1973 and further to 75 per cent in 1979 as given in Table 14. According to the latest available CFS report (for 1982), 62 per cent of total loans was obtained from the unorganised sector.

As shown in this section, the degree of concentration between commercial banks and savings institutions in the financial sector is high like in any other developing country and this concentration has shown only marginal changes over the last three and a half decades. However, new financial institutions were introduced and expanded into the economy during this period, thereby contributing to the sophistication of the financial system in Sri Lanka. Also, the short term and long term financial markets reflected higher growth rates during the last six years compared to the period before 1978.

Interrelation among Financial Institutions

Tables 15 and 16 give the interrelation among financial institutions in 1975. As these tables show, the concentration by institution is high and the inter-institutional dependency is very low. Most boxes in both tables giving assets and liabilities are empty which indicate limited inter-institutional transactions. This is partly due to the underdeveloped money and capital markets in Sri Lanka. However, developments in the financial markets, especially after 1978, has improved inter-institutional transactions.

FINANCIAL INSTRUMENTS

As seen in section II, the major financial instruments in Sri Lanka are currency, deposits in and advances from deposit-type institutions and government debt papers (securities and Treasury bills). The composition of financial instruments of the country for 1984 indicates 6 per cent for currency, 38 per cent for deposits in deposit type institutions, 20 per cent for advances from deposit-type institutions and 26 per cent for government debt papers. Thus, these four categories accounted for 90 per cent of total financial instruments of Sri Lanka in 1984.

For the relative importance of various financial claims, Table 17 gives a more detailed classification and their relative shares.

Total financial claims against financial institutions declined from 72 per cent in 1950 to 52 per cent in 1980 indicating a downward trend with some marginal fluctuations. This value declined from 72 per cent in 1950 to 46 per cent in 1975 but it increased to 52 per cent in 1984. On the other hand, claims against non-financial institutions increased from 28 per cent in 1950 to 54 per cent in 1975 and decreased to 48 per cent in 1984. In both these categories the

share of non-marketable instruments decreased over time. Thus, the total of marketable instruments in both these categories increased from 57 per cent in 1950 to 62 per cent in 1984.

The share of the domestic component in the total financial instruments was higher (96 per cent in 1984) than foreign-currency denominated instruments as given in Table 18.

The interesting structural change that took place in the composition of financial instruments was the upward trend observed in interest-bearing instruments while the share of non-interest bearing instruments declined continuously as given in Table 18. The relative share of interest-bearing instruments increased from 44 per cent in 1950 to 87 per cent in 1984 while the share of non-interest bearing instruments declined from 56 per cent to 13 per cent during the same period. Increased deposit rates and improved facilities relating to availability and transferability of interest-bearing assets were the major reasons for this shift from non-interest-bearing assets to interest-bearing assets.

Table 18 also gives the composition of financial instruments according to issuing institutions. In this, the share of the monetary authority has declined. The share of deposit-type institutions in total financial instruments decreased from 55 per cent in 1950 to 27 per cent in 1975 but rose to 38 per cent in 1984. The share of long-term investment-type institutions was low and it was in the range of 5-11 per cent during the period. The relative share of the government sector in total financial instruments increased from 23 per cent in 1950 to 46 per cent in 1975 and decreased thereafter to 26 per cent in 1984.

Tables 19 and 19.1 give details of the composition of claims against financial institutions while Table 20 gives the composition of claims against non-financial units. The interesting difference in these two groups is that the share of marketable instruments was

more than 61 per cent in claims against non-financial units while it was less than 27 per cent in claims against financial institutions.

The growth in foreign currency instruments was marginal and its high growth rate in the last few years indicated an increasing degree of openness of the country's financial sector.

Table 21 gives the composition of equity and securities. The non-financial sector's (including the government sector) share in the total equity and securities was over 96 per cent during the period. The share of financial sector issue of equity and securities was negligible and it was less than 2 per cent. However, data on outstanding private sector shares and equities were not readily available.

Table 22 gives total outstanding advances while Table 23 gives new loans granted by long-term lending institutions.

Table 24 gives commercial banks' advances according to maturity period. The relative share of medium and long term advances decreased while the share of short term lendings increased over the period thereby showing a high preference for short term lendings by commercial banks. This has been one of the major reasons for the establishment of long term lending institutions such as the DFCC, SMIB and NDB by the Government.

Purpose-wise classification of advances is available only for the commercial banking sector lendings. As given in Table 24.1 the sub-sector for commercial purposes accounted for over 42 per cent in total commercial banks' advances while agricultural and industrial sectors together accounted for less than 36 per cent. A desirable structural change in this composition of bank advances is that the advances for consumption decreased from 9 per cent in 1965 to 1 per cent in 1984 as a result of selective demand management policies of the monetary authority.

Table 25 gives the ownership distribution of public sector debt. The relative share of foreign debt decreased from 20 per cent in 1950 to 12 per cent in 1965 and rose sharply to 51 per cent in 1984. On the other hand, the share of domestic debt increased from 80 per cent in 1950 to 88 per cent in 1965 and subsequently decreased to 49 per cent in 1984. The Central Bank, the EPF, the NSB and the Insurance Corporation of Sri Lanka owned a large proportion of government domestic debt while the commercial bank holdings of the same decreased from 38 per cent in 1950 to 1 per cent in 1984 thereby limiting the conduct of open market operations by the monetary authority.

Table 26 gives the composition of foreign-currency denominated financial instruments in the country. The establishment of FCBUs increased transactions in foreign instruments in the country.

The composition of new advances is given in Table 27. The monetary sector accounted for more than 81 per cent of new loans during the period under study. However, the share of provident funds and the NSB in total new advances increased during the same period.

Advances and investments in financial assets by financial institutions are given in Table 28. In this connection, the relative share of advances increased over time while the share of investments declined. Commercial banks alone supplied more than 63 per cent of total advances while the whole banking sector including the NSB supplied more than 91 per cent of loans. The relative share of commercial banks in investments decreased considerably while the Central Bank, the NSB and the EPF increased their relative shares in total investments mainly through investments in government papers.

Table 29 gives the composition of outstanding deposits while Table 30 gives the deposits of the private sector with commercial banks. The commercial banking sector accounted for more than 50 per cent of total deposits while the contribution of finance companies

and insurance corporations are still negligible and recorded relative share values of less than 4 per cent. However, the relative shares of the NSB and the EPF in total deposits increased significantly during the study period. Composition of deposits with commercial banks shows that the private sector contributed more than 43 per cent of total deposits. The relative share of the plantation sector showed a downward trend with some fluctuations.

IV. IMPLICATIONS FOR MONETARY POLICY

Policies and Other Developments Affecting the Financial Structure

Developments, innovations and reforms in the financial sector shown in the previous sections were due to a number of reasons. Some of these changes have been due to policies introduced by the Government to induce changes in the financial system while others are due to requirements created by the changing environment. Most of these developments have been due to both reasons.

The financial system in Sri Lanka was in an under-developed state when the Central Bank of Ceylon was established in 1950. Financial institutions mainly rendered their services only for the sectors engaged in export crops and neglected a large proportion of the other activities of the economy. Thus, the dichotomy which existed in a colonial economy was seen in the Sri Lankan financial sector before the country's independence in 1948. Under this system, the export crops and the modern sectors received services of financial institutions in every stage of their business while the traditional sector was neglected their most crucial needs. Hence, one of the major policies of the newly independent government was to spread and improve financial services to the traditional sector.

Furthermore, one of the objectives of the Central Bank of Ceylon as a development-oriented monetary authority was to improve and

expand financial services in the economy. Hence, the Central Bank of Ceylon recommended and advised the government to introduce, reform, improve and expand the number of financial institutions and instruments. Some of them were the establishment of the People's Bank; a reform of the Bank of Ceylon; establishment of the NSB by amalgamating the Ceylon Savings Bank and the Post Office Savings Bank; establishment of NDB and DFCC; reform of SMIB; establishment of insurance corporations, merchant banks, leasing companies, rural banks, regional rural development banks, money brokers and share market participants; and permission to establish foreign bank branches and FCBUs.

To reduce the gap between modern and traditional economic sectors and to increase the growth of the industrial sector, the Government decided to give more incentives for traditional cultivators and new industrialists. These new developments demanded more and more financial services. Government programmes implemented for rural sector development demanded increasing services from financial institutions to those areas. Also, the policy makers needed to reduce the farmers' dependence on the unorganised sector for their financial requirements. The rapid branch expansion of commercial banks, expansion of deposit mobilisation by the NSB and the increase in the number of rural banks were results of these policies implemented by the Government.

The increased government participation in economic activities and policies directed to achieve high economic growth rate and improvements in the traditional agricultural sector resulted in more participation of the public sector in the financial system.

However, government policies towards the development of the financial structure expanded with new economic policies introduced after 1978. Under the new policies, the Government gave new incentives and allowed legal facilities to develop the financial system rather than directly participating in the financial markets.

The objectives of these policy measures are the improvement of financial services through market competition, establishment and expansion of new institutions such as merchant banks, leasing companies, money brokers, money market and capital market institutions and develop the country's financial system as an international financial centre. These new policies resulted in a number of improvements and changes in the Sri Lankan financial system such as opening of branches by 11 foreign banks, seven money brokers commencing their money market operations, improvement in the share market operations, establishment of two merchant banks and three leasing companies and commencing of business activities of 25 FCBU units.

Monetary Policy: Instruments and Implementation

Before analysing the effect of the financial structure and its changes on monetary policy, a brief outline of policy instruments available to the Sri Lankan monetary authority and the prevailing monetary transmission process would be more appropriate.

Policy instruments available for the monetary authorities can be divided into two categories: (i) quantitative or volume-controlling instruments covering open market operations, variable reserve ratio and the Bank rate and (ii) qualitative or direction-controlling instruments covering ceiling for maturities, ceiling on credits, minimum ratios on the capital and surplus of commercial banks to their assets, marginal cash reserve requirements for letters of credit, control over interest rates, moral suasion and incentives for selected sectoral credits. The MLA has empowered the Central Bank with these instruments in pursuance of its objectives such as monetary and price stability, exchange rate stability and economic development.

The mechanism or the channels through which the effects of these instruments get translated into the real or economic sector are not readily identifiable. These processes of effectiveness can be

divided into two parts, the effects of monetary instruments on monetary targets (or intermediate targets) and subsequently, the effects of monetary targets on real/economic targets (or ultimate targets). The link between changes of monetary instruments and monetary targets is direct and clear. However, the link between the changes of monetary targets and economic targets is not only indirect but also very vague. The first part of the transmission process takes place in the money market while the second part of this process mostly takes place in the capital market. As in any other developing country, the capital market in Sri Lanka is an underdeveloped market. Hence, the second part of the transmission process of changes of monetary instruments into changes in economic activities is more indirect.

1950 to 1965. The Sri Lankan monetary authority has used the above mentioned instruments at different occasions depending on the economic situation. However, the implementation of monetary policy in Sri Lanka can be divided into three sub-periods. During the first period from 1950 to 1965, the Sri Lankan economy experienced a reasonably high degree of monetary stability except in few years such as the Korean boom years in 1951/52 and the 1954/55 tea boom years. Stable conditions in monetary aggregates, and hence the price level, did not create a necessity for anti-inflationary measures during this period. However, the monetary policy measures undertaken during the end of the 1950s and the early part of the 1960s were mainly aimed to face the deteriorating balance of payment situation resulting from unfavourable terms of trade of the country. Also, some policy measures were introduced to expand and increase financial resource availability for the underdeveloped sectors in the economy, especially to traditional and rural agricultural sectors.

1965 to 1977. In the second period covering 1965 to 1977, the money supply and the price levels experienced an increasing trend, requiring some demand management policy measures. Thus, monetary policy measures adopted during this period included quantitative

restrictions on bank credit except for priority sector advances, ceiling on bank credit to non-productive purposes such as consumption and speculative purposes and ceiling on overall bank credit. Meanwhile, some quantitative measures such as refinance facilities, marginal cash deposits against letter of credit for non-essential imports and moral suasion were used to divert more credit to priority sectors from non-essential sectors.

Post 1977. The period after 1977 was identified as the third period. During this period, all monetary aggregates indicated higher growth rates compared with the previous two periods. Hence, monetary policy measures have been directed more towards controlling inflation. However, the monetary authorities continued with some expansionary policy measures to improve the balance of payments. Also, special measures were taken to insulate priority sectors such as agriculture, industry, exports and tourism from adverse conditions. Some of these measures were refinance, credit guarantee and interest rebate schemes.

Monetary Policy: Transmission Mechanism

As seen in the previous sections, the commercial banking sector has dominated the financial sector of the country. Also, the Central Bank conducted regular control and supervision of the banking sector during the period under review. Furthermore, the Central Bank has increased and expanded its supervision on finance companies. The impact of monetary policy on commercial banking activities indirectly affect the NSB and finance companies since these institutions compete with commercial banks for deposits. For example, an increase in the Bank rate will not only reduce bank credit but also compels the banks to mobilise new deposits even at high interest rates. Subsequently, the NSB and finance companies have to increase their deposit rates to maintain their relative position in the domestic savings mobilisation. Similarly, if a credit ceiling is imposed resulting in a decrease in commercial bank lendings and hence increase in excess liquidity, the

banking sector has to reduce its deposit rates to minimise its cost of funds. Consequently, the NSB and finance companies have the opportunity to reduce their cost of funds by reducing deposit rates.

However, based on past experience, the lending rates of financial institutions have shown less flexibility to policy changes compared with deposit rates. Also the transmission mechanism between changes in the financial sector and the real sector is not highly developed due to the under-developed capital market. Therefore, the above analysis suggests two conclusions about monetary policy transmission mechanism in Sri Lanka. First, the transmission process from monetary policy instruments to monetary aggregates and hence to monetary targets is direct and felt within a fairly short period. This is not only due to the ability of monetary variables to adjust for changes but also due to the monetary authorities' influence on commercial banks and high competition among deposit mobilising institutions. Furthermore, most instruments used in Sri Lanka directly affect the monetary base and hence, their effects on monetary targets are quick. However, the transmission process from monetary aggregates to economic objectives, particularly to the real sector variables, is indirect and takes a longer time period. Weak relationship between monetary and real sectors is mainly attributable to the under-developed nature of the capital market. This situation and slow adjustment process of real variables result in sluggish adjustments in real economic variables for monetary policy changes.

A consideration of the relationship between monetary and fiscal policies including exchange rate policies is also useful. The monetary authority, the Central Bank of Ceylon, is the major economic adviser to the Government and the institution in charge of public debt. The Central Bank not only gives regular reports including annual reports, pre-budget reports and analysis of the economy to the Government but also gives special reports and precautionary advice on irregular movements of monetary and price variables. Also, the membership of the Secretary to the Minister of Finance and Planning in

the Monetary Board member, enhances the relationship between monetary and fiscal policies. Monetary policy is not only used as an alternative to fiscal policy in achieving economic objectives but also as a complementary measure to reduce some unfavourable effects of fiscal policy. For instance, some contractionary monetary policy measures were used to reduce the inflationary pressure that arose due to government expansionary fiscal policy. Thus, it seems in the case of Sri Lanka, monetary and fiscal policies are closely coordinated and monetary policy seems to be more influenced by fiscal policy rather than the other way round.

The Implications on Monetary Policy

In the light of the above discussion of the changes in the financial structure and existing monetary transmission process, it is now possible to consider the effects of these policies on the financial structure and their implications on the effectiveness of monetary policy.

The major problems encountered in the implementation of monetary policy in Sri Lanka, as in any other developing country, are the under developed financial system, particularly the money and/or capital markets, limited number of financial institutions and instruments, weak relationships among financial institutions and very limited relationship between the real and financial sectors. For a few instances, the under-developed capital market situation is a limitation to implement open-market operations; the weak relationship between the financial and real sectors not only reduces the effect of monetary policy but also reduces the speed of the transmission process; the poor inter-dependency relationship among financial institutions and the high concentration of financial activities in few institutions reduce the spread of monetary policy resulting to a less responsive real sector to such policy changes.

The evaluation of the financial structure and its implications on monetary policy suggests that the situation in Sri Lanka improved during the period under study. Although the problems mentioned above have not been resolved yet, their undesirable effects have been reduced continuously over time after the establishment of the Central Bank. Institutions and activities in the money market expanded and developed during the period under study. Also, new financial instruments were introduced into the financial system. Initial steps were already taken to develop the capital market of the country. At present, the secondary Treasury bill market and the Colombo share market are improving at moderate rates. Most importantly, the expansion of financial institutions and activities especially in rural (remote) areas increased the monetisation of the economy by expanding the coverage of the financial sector. Also, the relationship between fiscal policy and monetary policy improved during the period as a result of increasing regular contacts between ministries and the monetary authorities by improving their mutual understanding.

These improvements and expansion of the financial system in Sri Lanka increased the effectiveness of monetary policy and its speed of transmission. The improvement and sophistication of the financial structure of the country by adding more financial institutions and instruments resulting in noticeable structural changes, enhanced the impact of monetary policy. Particularly, these new institutions spread the effects of monetary policy over different areas in the economy.

In particular, the expansion of financial institutions over the country which cover various economic sectors not only increased the effectiveness of monetary policy but also made the whole country fall within the framework of monetary policy. For example, the traditional rural agricultural sector, and fisheries and small manufacturing sectors including handicraft, obtain services from the

financial system. These services are, in turn, subjected to the effects of monetary policy.

Both these expansion and improvements gave more opportunities to use new monetary policy instruments by expanding the policy makers' set of effective instruments. Also, these structural changes increased the speed of transmission of monetary policy.

As done in the previous sections, policies on the financial structure have an impact on monetary policies and these can be analysed and explained although it is not easy to quantify their effectiveness. However, some selected indicators of "financial deepening" can be considered as proxies to evaluate quantitatively the results of these policies in the financial structure of the country. Also, these indicators provide an idea about the possible strength of measures brought about by monetary policy.

Indicators of Financial Deepening

It is worthwhile to consider how the growth of financial institutions and markets described in the previous sections affected financial deepening in the country. A number of financial indicators (as used by McKinnon and Shaw) can be used to evaluate financial deepening of an economy depending on data availability. Table 31 gives some leading indicators to evaluate financial deepening in Sri Lanka.

Accumulation and diversification of financial assets. One widely accepted measure of financial deepening is the accumulation and diversification of financial assets over time, adjusted for population and price changes. Based on data available on financial assets in Sri Lanka, five monetary aggregates are used as proxies for financial assets/wealth to estimate per capita holdings of real financial assets. The Colombo Consumer Price Index is used to derive the real

values and the entire population is used to calculate the per capita values. All these five indicators show that financial deepening increased continuously in Sri Lanka during the period under review. However, the per capita real balance holding with respect to M1 dropped marginally in the last few years. This was due to shift of deposits from non-interest-bearing deposits to interest-bearing deposits due to high deposit rates. Also, all five indicators show a similar increasing growth pattern over time. The annual average growth rate of these indicators increased from the range of 3-5 per cent in the 1950s to 2-24 per cent in the 1960s and further to 9-80 per cent in the 1970s.

Financial institution density. Financial deepening can also be gauged by financial institution (or banking) density and the access of the people to these institutions. Both the absolute savings level and the marginal propensity to save are positively related with the existence of financial institutions and use of their services by the people. Also the intermediation of transactions is highly connected to the number of institutions and the access of the people to these institutions. Hence, two indicators, namely, financial institution density and relative share of account holders in adult population, are calculated. These two indicators show a continuous increase, confirming the growth of financial deepening over time.

Ratio of financial stocks to national income. Another important indicator of financial deepening is the ratio of financial stocks to national income. Five versions of monetary assets are used to calculate this ratio. These results are given in Table 32 and they all show that the financial deepening of the country increased over time with only some marginal fluctuations.

Share of financial sector to GDP/labour force. Finally, financial deepening may be captured by structural shifts in the economy in favour of the financial sector. The two indicators constructed for this purpose are the relative shares of the financial

sector in GDP and labour force. These two indicators have also increased over time.

Thus, all constructed financial deepening indicators have shown a positive growth trend. The annual growth rate of these indicators are in the range of 5-10 per cent. Apart from these impressive growth rates, some of the indicators are remarkable in terms of their absolute magnitudes.

At present, there are a number of policies aimed to develop and expand further financial institutions and instruments. They will improve the financial structure by increasing the effectiveness of monetary policy. One of them is a reduction of regulatory interference in financial institutions by the authorities while allowing more adjustments through market forces. Under this policy, the private sector is allowed to establish and expand financial institutions. The interest rates and exchange rate are allowed to be determined by market forces as and when considered appropriate. Also, the incentives and assistance introduced to improve the financial system are being continued by the Government. A special programme was introduced to increase banking assistance to rural production activities under the Regional Rural Development Bank Scheme.

Policy measures are implemented by the government to improve financial intermediation in new investments rather than self-financing. The Government has recognised the necessity of a developed capital market and has offered various tax incentives not only to those who invest in shares but also to companies whose shares are listed in the share market. Also, the Government supplies free information on share market activities to the public to improve their participation in this market. Likewise, policy measures are introduced to improve foreign collaboration in the development of the financial system of Sri Lanka. Under this scheme, foreign financial institutions are allowed to open their branches in Sri Lanka singly or in collaboration with domestic firms and the Government has allowed

domestic institutions to undertake foreign financial transactions and to obtain foreign technical assistance. Furthermore, the Government is moving more towards borrowing at market rates while reducing its dependence on captive sources such as the NSB and EPF. This will not only increase the availability of funds to the private sector, but will also improve the efficient allocation of financial resources.

Thus, the continuation of these policies on the financial structure and related activities would no doubt improve and expand the financial system in Sri Lanka by increasing the effectiveness of monetary policy and the speed of the monetary transmission process.

V. SUMMARY AND CONCLUSION

The financial structure of Sri Lanka has gradually expanded and improved during the last 34 years in terms of institutions, branches, activities, instruments and interdependency among institutions. Introduction of new financial institutions and innovations in financial instruments increased the sophistication of the financial structure of the country. Expansion of branches throughout the country increased the financial system's coverage of the economy. Special credit schemes and development projects implemented to develop the rural agricultural sector expanded banking activities to remote areas. Thus, it is clear that the structural changes in the financial sector of Sri Lanka during the period under review were results of Government policies, particularly the efforts initiated by the monetary authorities, and historical developments. These structural changes in the financial system, in turn, enhanced the effectiveness of monetary policy and increased the speed of the monetary transmission process.

However, the Sri Lanka financial system still has some major problems such as weak interdependence among institutions, high concentration on a few institutions and instruments, under-developed

capital market and a lack of sufficient long-term lending institutions, absence of secondary markets for marketable claims and hence, the weaker impact of monetary policy on the real sector. The banking system still plays the major role in the financial sector. The banking system has contributed much towards economic development and it has effectively collected savings from the community, even from the rural areas. However, there is much room for improvement with respect to diverting bank funds to the more productive areas, and to increase interdependency among financial institutions. Likewise, the money and capital markets need to be further strengthened so as to make them more effective channels of monetary policy in Sri Lanka.

Table 1

FINANCIAL INSTITUTIONS AND FINANCIAL INSTRUMENTS IN SRI LANKA: SELECTED DATA

	1950	1960	1970	1980	1984
1. Number of Financial Institutions	15	17	18	68	104
2. Number of Branches	31	49	259	1,365	1,725
3. Total Assets of Financial System					
) (i) Nominal - Rs.Mn.	1,725	2,936	9,152	62,226	125,569
) (ii) Real - Rs.Mn.	1,782	2,837	6,622	19,556	22,703
4. Value of Financial Instruments					
) (i) Nominal - Rs.Mn.	1,894	4,034	11,475	69,660	146,835
) (ii) Real - Rs.Mn.	1,957	3,898	8,303	21,892	26,548
5. Per-capita value of Financial Instruments					
) (i) Nominal - Rs.	247	408	917	4,727	9,413
) (ii) Real - Rs.	255	394	663	1,485	1,702

Note: Nominal values are deflated by CPI to derive real values.

Source: Central Bank of Ceylon.

Table 2

NUMBER OF FINANCIAL INSTITUTIONS - SRI LANKA

	Number of Institutions										Number of Branches									
	1950	55	60	65	70	75	80	83	84	1950	55	60	65	70	75	80	83	84		
MONEY SECTOR																				
1. Central Bank	1	1	1	1	1	1	1	1	1	1	1	1	1	1	1	1	1	3	3	
2. Commercial Banks	12	12	12	12	11	11	20	25	25	28	37	45	97	165	562	615	680	648		
NON-MONEY SECTOR																				
3. National Savings Bank	-	-	-	-	-	1	1	1	1	-	-	-	-	-	20	42	50	52		
4. Rural Banks	-	-	-	-	1	1	1	1	1	-	-	-	8	90	447	641	843	888		
5. Finance Companies	-	-	-	-	-	31	40	60	64	-	-	-	-	-	31	40	40	64		
6. Long-term Lending Institutions (Development Banks)	2	2	3	3	3	3	3	3	3	2	2	3	3	3	3	6	6	6		
7. Insurance Corporations	-	-	-	1	1	1	1	2	2	-	-	-	-	-	-	-	-	34		
8. Provident Funds (Major)	-	-	1	1	1	1	1	2	2	-	-	-	-	-	-	-	-	-		
9. FCBUs	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	18	24	25		
10. Merchant Banks	-	-	-	-	-	-	-	2	2	-	-	-	-	-	-	2	2	2		
11. Leasing Companies	-	-	-	-	-	-	-	3	3	-	-	-	-	-	-	-	3	3		

Source: Central Bank of Ceylon.

Table 3
COMPOSITION OF ASSETS AND LIABILITIES OF THE CENTRAL BANK OF CEYLON

	A s s e t s					L i a b i l i t i e s					Rs. Million
	1950	1960	1970	1980	1984	1950	1960	1970	1980	1984	
1. Cash and Balances abroad including Treasury Bills	280 (48)	90 (9)	91 (3)	3,937 (17)	9,843 (30)	1. Capital Account	25 (4)	71 (2)	80 (...)	84 (...)	
2. Foreign Government and Non-government Securities	285 (48)	100 (10)	103 (3)	467 (2)	2,716 (8)	2. Currency Issue	367 (62)	1,090 (33)	5,009 (22)	9,600 (29)	
3. Special Drawing Rights	-	-	-	-	5 (1)	3. Central Bank Securities	-	-	-	557 (2)	
A. Total Foreign Assets	565 (96)	190 (19)	194 (6)	4,404 (19)	12,564 (38)	4. Borrowings abroad	-	412 (12)	429 (2)	13 (...)	
<u>Loans and Advances</u>						<u>Deposits</u>					
4. Special loans to Government	14 (2)	191 (19)	93 (3)	-	-	5. Government Deposits	192 (33)	848 (25)	5,343 (23)	11,120 (33)	
5. Provisional loans to Government	-	-	243 (7)	1,628 (7)	4,043 (12)	6. Government Agencies and Institutions	13 (2)	78 (2)	1,346 (6)	1,344 (4)	
6. Others	-	21 (2)	149 (4)	1,124 (5)	2,312 (7)	7. Commercial Banks	...	9 (1)	13 (...)	84 (...)	
7. Government and Government Guaranteed Securities	5 (1)	569 (58)	1,883 (56)	9,338 (41)	11,206 (34)	8. International Organisations, Foreign Gov. and Banks	165 (28)	224 (16)	1,264 (10)	4,026 (12)	
8. Other Assets and Accounts	3 (1)	14 (1)	770 (23)	6,338 (28)	3,147 (9)	9. Others	01 (...)	10 (...)	346 (2)	590 (2)	
B. Total Domestic Assets	22 (4)	795 (81)	3,138 (94)	18,428 (81)	20,708 (62)	10. Other Liabilities	3 (1)	912 (27)	11,971 (52)	11,898 (36)	
Total Assets	587 (100)	985 (100)	3,332 (100)	22,832 (100)	33,272 (100)	Total Liabilities	587 (100)	3,332 (100)	22,832 (100)	33,272 (100)	

Note: Relative percentage values are in brackets.

Source: Central Bank of Ceylon.

COMPOSITION OF ASSETS AND LIABILITIES OF COMMERCIAL BANKS: SRI LANKA

(Rs. Million)

Assets	1950	1960	1970	1980	1984	Liabilities	1950	1960	1970	1980	1984
1. Cash in hand	36.0 (4)	39.3 (3)	145.7 (5)	824.4 (3)	1,034.5 (2)	1. Paid up capital, reserve funds and undistributed profits	15.3 (2)	32.7 (3)	129.6 (4)	1,272.3 (5)	2,931.5 (5)
2. Due from Central Bank	163.2 (19)	186.8 (11)	244.9 (7)	1,224.3 (5)	4,349.8 (8)	2. Demand deposits					
3. Due from Domestic Banks	2.6 (...)	7.7 (1)	34.9 (1)	468.8 (2)	845.9 (2)	2.1 Domestic	3.6 (...)	0.9 (...)	0.2 (...)	20 (...)	62.8 (...)
4. Cash items in process of collection	10.3 (1)	24.7 (2)	180.3 (6)	1,348.0 (5)	1,999.6 (4)	2.2 Foreign	10.7 (1)	5.1 (...)	1.9 (...)	40.8 (...)	86.4 (...)
5. Foreign currency on hand and due from banks abroad	180.4 (21)	56.3 (5)	44.1 (1)	845.1 (3)	3,172.5 (6)	2.3 Sri Lanka Government	34.4 (16)	71.5 (6)	200.7 (6)	1,411.2 (5)	2,011.6 (4)
6. Investments						2.4 Resident Constituents	572.1 (67)	595.6 (50)	1,005.3 (32)	5,138.5 (19)	8,001.6 (14)
6.1 Treasury Bills	54.4 (6)	47.9 (4)	281.4 (9)	7.9 (3)	1,469.6 (3)	2.5 Non-resident Constituents	13.2 (2)	11.8 (1)	17.3 (1)	95.5 (...)	176.9 (...)
6.2 Securities	216.5 (25)	287.5 (24)	356.8 (11)	557.2 (2)	1,270.9 (2)	3. Time and Savings Deposits					
7. Loans and Advances						3.1 Government of Sri Lanka	4.3 (1)	8.6 (1)	20.4 (1)	171.4 (1)	249.6 (...)
7.1 Local	0.2 (...)	2.4 (...)	-	0.6 (3)	0.2 (3)	3.2 Resident Constituents	67.5 (8)	357.0 (30)	1,111.5 (36)	10,376.4 (39)	26,368.5 (47)
7.2 Import	7.6 (1)	53.3 (5)	38.0 (1)	1,713.2 (6)	1,777.7 (3)	3.3 Non-resident Constituents	5.4 (1)	6.6 (1)	36.7 (1)	55.6 (...)	2,161.1 (4)
7.3 Export	44.9 (5.2)	55.4 (5)	106.5 (3)	1,501.9 (6)	2,033.0 (4)	4. Total Deposits					
7.4 Overdrafts	97.9 (11)	294.7 (25)	589.1 (19)	3,888.8 (15)	10,294.7 (18)	4.1 Demand	733.9 (86)	684.9 (57)	1,225.5 (39)	6,687.8 (25)	10,339.3 (18)
7.5 Loans	31.5 (4)	136.1 (12)	814.2 (26)	9,895.7 (37)	20,996.9 (37)	4.2 Time and Savings	77.1 (9)	372.2 (31)	1,168.6 (37)	10,603.5 (40)	28,779.2 (51)
7.6 Total	182.1 (21)	543.9 (46)	1,547.7 (50)	17,000.2 (64)	35,102.5 (62)	4.3 Total	811.1 (95)	1,057.1 (88)	2,394.0 (77)	17,291.3 (65)	39,118.5 (69)
8. Fixed and other Assets	13.0 (2)	52.3 (4)	300.8 (10)	3,963.0 (15)	6,555.6 (12)	5. Borrowings					
9. Total Assets or Liabilities	858.5	1,196.5	3,122.0	26,601.1	56,552.9	5.1 Inter Bank	2.0 (...)	25.4 (2)	213.9 (7)	1,719.1 (7)	3,393.5 (6)
						5.2 Other		2.0 (...)	-	-	-
						5.3 Foreign	7.7 (1)	5.9 (1)	3.6 (...)	280.3 (1)	716.9 (1)
						6. Other Liabilities	22.4 (3)	73.4 (6)	380.8 (12)	6,036.0 (23)	10,392.5 (18)
						Total	858.4	1,196.5	3,122.0	26,601.1	56,552.9

Note: Relative percentage values are in brackets.
Source: Central Bank of Ceylon.

Table 5

COMPOSITION OF ASSETS AND LIABILITIES OF
THE NATIONAL SAVINGS BANK (NSB) : SRI LANKA

(Rs. Million)

	1975	1980	1983
Assets			
1. Current Assets	83.3 (4)	365.0 (7)	974.2 (9)
1.1 Cash in hand and with Banks	14.0 (1)	39.6 (1)	70.4 (1)
1.2 Other Current Assets	69.3 (4)	325.4 (6)	903.8 (9)
2. Loans	41.8 (2)	100.0 (2)	147.6 (1)
3. Securities and Investments	1,730.1 (93)	4,848.0 (91)	9,256.5 (89)
3.1 Sri Lanka Government	1,730.0 (93)	4,847.0 (91)	9,199.6 (89)
3.2 Others	0.1 -	1.0 -	56.9 (1)
4. Fixed Assets	10.4 (1)	15.8 -	13.6 -
Total	1,865.7	5,328.5	10,391.9
Liabilities			
1. Current Liabilities	23.7 (1)	42.2 (1)	139.5 (1)
2. Deposits	1,804.1 (97)	5,202.7 (97)	10,088.0 (97)
2.1 Ordinary savings	N.A.	N.A.	2,887.1 (28)
2.2 Fixed Deposits	N.A.	N.A.	6,425.4 (62)
2.3 Others	N.A.	N.A.	775.5 (6)
3. Reserve	37.9 (2)	82.6 (2)	164.4 (2)
Total	1,865.7	5,328.5	10,391.9

Note: Relative percentage values are in brackets.

Source: Central Bank of Ceylon.

Table 6

FINANCE COMPANIES: SELECTED DATA: 1975-1984

(Rs. Million)

Year	No. of Companies Reported	Total Assets	Total Deposits	Hire Purchase	Loans Outstanding	Investment
1975	31	-	123.2	90.0	23.8	-
1980	40	635.6	410.6	311.2	73.2	-
1981	44	1,146.2	557.3	518.5	116.6	38.7
1982	50	1,612.0	1,024.0	893.4	284.2	106.6
1983	50	2,121.0	1,403.7	1,009.5	441.4	133.1
1984	50	3,553.5	2,452.5	1,731.1	639.1	224.9

Source: Central Bank of Ceylon.

Table 7
RELATIVE POSITION OF THE FINANCIAL SECTOR IN
TOTAL EMPLOYMENT AND GDP

(In Per Cent)

Year	In Total Employment ^{1/} %	In GDP ^{2/} %
1953	-	0.9
1963	0.5	1.0
1973	0.7	1.3
1981	1.1	2.2
1983	-	2.8
1984	-	2.9

^{1/} This is the percentage value of the ratio of employment in financing, insurance, real estate and trade services to the employment.

^{2/} This is the percentage value of the ratio of value added of banking, insurance and real estate sector to the total GDP at constant prices.

Source: Central Bank of Ceylon and Population Census Reports.

Table 8

FINANCIAL INTERRELATIONS RATIO (FIR)

<u>Year</u>	<u>Total Financial Instruments</u> <u>(Rs. Million)</u>	<u>GDP</u> <u>(Rs. Million)</u>	<u>FIR:1/2</u>
	(1)	(2)	
1950	1894	6136	.31
1955	2498	7635	.33
1960	4034	8529	.47
1965	7350	10139	.72
1970	11475	13187	.87
1975	20293	25691	.79
1980	69660	62246	1.12
1983	128136	111976	1.14
1984	146835	138173	1.06

Table 9

FINANCIAL INTERMEDIATION RATIO - SRI LANKA

(Rs. Million)

Year	NAFI	ESNF	Government New Borrowings	Financial Intermediation Ratio (Percentage values)		
				To the Economy	To the Government Sector	
				(2)/(3) %	(4)/(3) %	(4)/(2) %
(1)	(2)	(3)	(4)	(5)	(6)	(7)
1950	189	408	0	46	0	9
1955	348	635	80	55	13	23
1960	1,074	1,681	875	63	52	81
1965	1,780	2,508	1,572	71	63	88
1970	2,959	4,596	2,743	64	60	93
1975	5,834	6,595	3,451	88	52	59
1980	27,320	32,105	12,875	85	40	47
1983	48,935	56,049	24,083	87	43	49
1984	50,359	58,155	23,519	87	40	47

Note: NAFI = Net acquisition by financial institutions) = First difference of gross credit extended by all financial institutions to other sectors.

ESNF = Equities and primary securities issued by non-financial sector) = First difference of credit for consumption purposes and net capital formation of the country.

Source: Central Bank of Ceylon.

Table 10

TOTAL ASSETS OF THE FINANCIAL SYSTEM IN SRI LANKA

	1950	1955	1960	1965	1970	1975	1980	1983	1984
	(Rs. Million)								
1. Banking Sector	1,445 (84)	1,689 (82)	2,183 (74)	3,540 (66)	6,455 (71)	10,661 (67)	49,433 (79)	83,479 (75)	89,825 (72)
1.1 Central Bank	587 (34)	689 (33)	986 (34)	1,726 (32)	3,333 (36)	5,365 (34)	22,832 (37)	33,097 (30)	33,272 (27)
1.2 Commercial Banks	858 (50)	1,000 (49)	1,197 (40)	1,814 (34)	3,122 (35)	5,296 (33)	26,601 (43)	50,382 (45)	56,553 (45)
2. Other Institutions	280 (16)	382 (18)	753 (26)	1,842 (34)	2,697 (29)	5,211 (33)	12,793 (21)	27,659 (25)	35,744 (28)
2.1 National Savings Bank	249 (14)	324 (16)	451 (15)	556 (10)	781 (8)	1,866 (12)	5,329 (9)	10,392 (9)	11,508 (9)
2.2 Rural Banks	-	-	-	1 (..)	17 (..)	87 (0.5)	37 (..)	718 (1)	905 (1)
2.3 Finance Companies	-	-	-	-	134 (1)	203 (1)	636 (1)	2,121 (2)	3,554 (3)
2.4 Long-term Lending Institutions	31 (2)	58 (2)	103 (4)	113 (2)	156 (2)	178 (1)	523 (1)	1,591 (1.5)	2,155 (2)
2.5 Insurance Corporations and Companies	-	-	12 (1)	391 (7)	421 (5)	714 (4.5)	1,216 (2)	2,733 (2.5)	4,781 (4)
2.6 All Provident Funds	-	-	187 (6)	781 (15)	1,188 (13)	2,163 (14)	5,051 (8)	10,104 (9)	12,841 (10)
Total	1,725	2,071	2,936	5,382	9,152	15,872	62,226	111,138	125,569
Growth Rate - Annual	-	(4)	(8)	(17)	(14)	(15)	(58)	(26)	(13)
Geometric Growth Rate - Annual	-	(4)	(7)	(111)	(11)	(12)	(31)	(21)	(13)

Source: Central Bank of Ceylon

Note: Relative percentage values are in brackets.

Table 11
CLASSIFICATION OF THE FINANCIAL SYSTEM OF SRI LANKA,
BY LIABILITIES : 1984

1. Monetary Authority	Authority of the Monetary Sector	Currency	Central Bank of Ceylon
	Bank's Bank	Bank's Deposits (Reserves)	
	Banker for the Government		
	Policy Advise		
	Currency Authority		
2. Deposit Type Institutions	Deposit Mobilisation	Domestic and Foreign Deposits and Borrowings	Commercial Banks, National Savings Bank, Rural Banks, Finance Companies
	Supply of Advances		
	Investment in Equities and Securities		
3. Contractual Saving Institutions	Insurances - Provident Funds	Contracted Liabilities	Insurance Corporation, Employees' Provident Fund, Employees' Trust Fund
4. Investment Type Intermediaries	Medium and Long-Term Investment Facilities	Borrowings, Contributions, Debentures, Equities and Capital	Development Finance Corporation of Ceylon, State Mortgage & Investment Bank, National Development Bank
5. Other Type	Investment Advisory and Leasing Facilities	Capital, Equities, Debentures and Borrowings	Merchant Banks, Leasing Companies, Sri Lanka Export Credit Insurance Corporation

Table 12

DISTRIBUTION OF FINANCIAL ASSETS BY MAJOR FINANCIAL TYPE

(Percentage Values)

	1950	1955	1960	1965	1970	1975	1980	1983	1984
a) Monetary Authority (Currency)	34	33	34	32	36	34	37	30	27
b) Deposit-type institutions (domestic and foreign currency denominated deposits to be segregated)	64	65	55	44	44	47	53	57	58
c) Contractual savings intermediaries	-	-	7	22	18	18	10	11	14
d) Investment type intermediaries	2	2	4	2	2	1	1	2	2
e) Other types	-	-	-	-	-	-	-	-	-
Total	100	100	100	100	100	100	100	100	100

Source: Central Bank of Ceylon.

Table 13

PRIMARY AND SECONDARY SHARE MARKETS : SELECTED DATA

	1975	1980	1983	1984
<u>Primary Share Market</u>				
Number of Shares offered (in Million)	0.07	1.4	94.0	63.2
Value of Shares offered (in Rs. Million)	0.7	14.0	1004.0	632.5
Total Amount Subscribed or underwritten	0.7	14.0	721.0	7.8
<u>Secondary Share Market</u>				
Number of Transactions	-	-	1811.0	2776.0
Number of Shares Sold	-	-	1,374,903	3,131,033
Value (Rs. Million)	-	-	20.0	32.8

Source: Central Bank of Ceylon.

Table 14

BORROWINGS OF HOUSEHOLD SECTOR FROM NON-INSTITUTIONAL SECTOR : SRI LANKA

(Percentage Values)

Sectors	Total Proportion of Loans from Non-Institutional Sector				Proportion of Loans from Money Lenders Only			
	1963	1973	1978/79	1981/82	1963	1973	1978/79	1981/82
Urban	88	79	58	59	23	38	19	27
Rural	78	78	69	60	20	35	19	20
Estate	99	99	96	93	24	63	40	24
All Island	86	80	75	62	29	37	20	23

Source: Consumer Finance Survey Reports - Central Bank of Ceylon.

Table 15

FINANCIAL INSTITUTIONS' INTERRELATION : SRI LANKA

(Percentage Values, End of 1975)

Assets of :

	10	10	2	4	10	12	10	18	4	94	23
	(12)	(12)									
Monetary Authorities								18	4	94	23
Commercial Banks								34	81	6	4
Insurance Corporation of Sri Lanka								6	11		2
Finance Companies								2			-
Employee Provident Fund								21			-
Agricultural and Industrial Credit Corporation											
State Mortgage Bank											
Development Finance Corporation of Ceylon									3		
Savings Institutions								18			
Cooperative Banks											
Private Sector											
Government and Government Entities	51	8	84	71	100	100	95	98	100	100	70
Foreign Banks	5	8									
Foreign Entities (Government)	4										
Others	29	9	1	25			3				
Total	101	100	100	100	100	100	100	100	100	100	100

Source: Central Bank of Ceylon

Table 16

FINANCIAL INTERRELATION : SRI LANKA

(Percentage Values, End of 1979)

Liabilities of :										
Monetary Authorities	10									
Commercial Banks	12 (12)									
Insurance Corporation of Sri Lanka										
Finance Companies	(14)									
Employee Provident Fund										
Agricultural and Industrial Credit Corporation										
State Mortgage Bank										
Development Finance Corporation of Ceylon	25	6								
Savings Institutions										
Cooperative Banks										
Private Sector	59	1	3	33	-	1	1			
Government and Government Entities	18	3	5					12		
Foreign Banks	37	63								
Foreign Entities (Government)	100									
Others	73	24	3							

Source: Central Bank of Ceylon

Table 17

FINANCIAL CLAIMS : SRI LANKA

(Rs. Million)

	1950	1955	1960	1965	1970	1975	1980	1983	1984
A. Claims Against Financial Institutions	1,364 (72)	1,604 (64)	2,268 (56)	3,802 (52)	5,235 (46)	9,275 (46)	32,422 (47)	63,273 (49)	77,046 (52)
1. Marketable Instruments	331 (17)	406 (16)	623 (15)	992 (14)	999 (9)	1,676 (8)	4,499 (7)	11,079 (9)	13,893 (9)
2. Non-Marketable Instruments	1,033 (55)	1,198 (48)	1,645 (41)	2,810 (38)	4,236 (37)	7,599 (38)	27,923 (40)	52,194 (40)	63,153 (43)
B. Claims Against Non-Financial Units	530 (28)	894 (36)	1,766 (44)	3,548 (48)	6,240 (54)	11,018 (54)	37,238 (53)	64,863 (51)	69,789 (48)
1. Marketable Instruments	498 (26)	845 (34)	1,628 (40)	3,265 (44)	5,412 (47)	8,905 (44)	25,779 (37)	42,118 (33)	42,678 (29)
2. Non-marketable Instruments	32 (2)	49 (2)	138 (4)	283 (4)	828 (7)	2,113 (10)	10,894 (15)	20,650 (16)	25,085 (17)
3. FCBU Loans & Advances to approved Residents	-	-	-	-	-	-	565 (1)	2,095 (2)	2,026 (2)
Total (A) + (B)	1,894 (100)	2,498 (100)	4,034 (100)	7,350 (100)	11,475 (100)	20,293 (100)	69,660 (100)	128,136 (100)	146,835 (100)

Note: Relative percentage values are in brackets.

Source: Central Bank of Ceylon.

Table 18

CLASSIFICATION OF FINANCIAL INSTRUMENTS : SRI LANKA

	1950	1955	1960	1965	1970	1975	1980	1983	1984
	(Rs. Million)								
A. As to Currency Denomination									
1. In Domestic Currency	1,894 (100)	2,485 (99)	4,016 (99)	7,319 (99)	11,421 (99)	20,227 (100)	68,780 (99)	122,774 (96)	141,044 (96)
2. In Foreign Currency	-	13 (1)	18 (1)	31 (1)	54 (1)	66 (1)	880 (1)	5,362 (4)	5,791 (4)
B. As to Yield									
1. With Yield	829 (44)	1,360 (54)	2,744 (68)	5,503 (75)	9,305 (81)	16,801 (83)	58,788 (84)	111,866 (87)	127,931 (87)
2. Without Yield	1,065 (56)	1,138 (46)	1,290 (32)	1,847 (25)	2,170 (19)	3,492 (17)	10,872 (16)	16,270 (13)	18,804 (13)
C. By Financial Institution (Liabilities)									
1. Monetary Authority	331 (17)	393 (16)	605 (15)	966 (13)	945 (8)	1,610 (8)	4,184 (6)	7,202 (6)	9,121 (6)
2. Deposits Type Institutions	1,033 (55)	1,211 (48)	1,476 (37)	2,055 (28)	3,102 (27)	5,502 (27)	23,186 (33)	45,967 (36)	55,084 (38)
3. Contractual Savings Institutions	-	-	187 (5)	781 (11)	1,188 (10)	2,163 (11)	6,062 (7)	10,104 (8)	12,841 (9)
4. Investment Type Institutions	-	-	-	-	-	1	29	1,033 (1)	699
5. Government	445 (23)	753 (30)	1,520 (38)	3,079 (42)	5,266 (46)	8,305 (41)	22,534 (33)	37,397 (29)	38,168 (26)
6. Others	85 (5)	141 (6)	246 (5)	469 (6)	974 (9)	2,712 (13)	14,675 (21)	26,433 (20)	30,922 (21)
Total	1,894	2,486	4,034	7,350	11,475	20,293	69,660	128,136	146,835

Note: Relative percentage (share) values are in brackets.

Source: Central Bank of Ceylon.

Table 19

COMPOSITION OF CLAIMS AGAINST FINANCIAL INSTITUTIONS: SRI LANKA

Rs. Million

	1950	1955	1960	1965	1970	1975	1980	1983	1984
A. Marketable Instruments	331 (24)	406 (25)	623 (27)	992 (26)	999 (19)	1,676 (18)	4,499 (14)	11,079 (18)	13,893 (18)
1. Currency	331 (24)	393 (24)	605 (26)	908 (24)	945 (18)	1,610 (17)	4,184 (13)	7,202 (11)	8,564 (11)
1.1 Held by Government	6 (...)	9 (...)	10 (...)	7 (...)	10	...	4 (...)	2 (...)	3 (...)
1.2 Held by Public	325 (24)	384 (24)	595 (26)	901 (24)	935 (18)	1,610 (17)	4,180 (13)	7,200 (11)	8,561 (11)
2. Certificates of Deposits (CDs)	-	-	-	-	-	-	-	610 (1)	1,007 (1)
2.1 Commercial Banks	-	-	-	-	-	-	-	513 (1)	908 (1)
2.2 Finance Companies	-	-	-	-	-	-	-	97 (...)	99 (...)
3. Central Bank Securities	-	-	-	53 (1)	-	-	-	-	557 (1)
4. Deposits in Foreign Currency in Commercial Banks	-	13 (...)	18 (1)	31 (1)	54 (1)	66 (1)	151 (...)	1,942 (3)	2,338 (3)
5. Deposits in FCBU, by Resident Approved	-	-	-	-	-	-	164 (...)	1,325 (2)	1,427 (2)
B. Non-marketable Instruments	1,033 (76)	1,198 (75)	1,645 (73)	2,810 (74)	4,236 (81)	7,599 (82)	27,923 (86)	52,194 (82)	63,153 (82)
6. Commercial Bank Deposits in Domestic Currency	811 (60)	898 (56)	1,039 (46)	1,515 (40)	2,340 (45)	3,544 (38)	17,140 (53)	30,821 (49)	35,872 (47)
6.1 Demand Deposits	734 (54)	745 (46)	685 (30)	939 (25)	1,225 (23)	1,882 (20)	6,688 (21)	9,068 (14)	10,340 (13)
6.2 Interest Bearing Deposits	77 (6)	153 (10)	354 (16)	576 (15)	1,115 (21)	1,662 (18)	10,452 (32)	21,753 (34)	25,532 (33)
7. N.S.B. Deposits	222 (16)	300 (19)	419 (18)	514 (13)	708 (13)	1,769 (19)	4,953 (15)	9,472 (15)	11,582 (15)
8. Finance Companies Deposits	-	-	-	-	123	411 (1)	1,404 (1)	2,452 (2)	- (3)
9. Contribution to Insurance	-	-	-	-	-	-	367 (1)	393	406
10. Contribution to EPF and ETF	-	-	187 (9)	781 (21)	1,188 (23)	2,163 (23)	5,052 (16)	10,104 (16)	12,841 (17)
11. Total A + B	1,364	1,604	2,268	3,802	5,235	9,275	32,422	63,273	77,046

Note: Relative percentage values are in brackets.

Source: Central Bank of Ceylon

CLASSIFICATIONS OF CLAIMS AGAINST FINANCIAL INSTITUTIONS : SRI LANKA

(Percentage Values)

	1950	1955	1960	1965	1970	1975	1980	1983	1984
A. As to Currency Denomination									
1. Domestic	100	100	100	99	99	99	-	95	95
2. Foreign	-	-	-	1	1	1	-	5	5
B. As to Marketability									
3. Marketable	24	25	27	26	19	18	14	18	18
4. Non-marketable	76	75	73	74	81	82	86	82	82
C. As to Yield									
5. With Yield	46	54	70	75	77	80	79	86	87
6. Without Yield	54	46	30	25	23	20	21	14	13
D. Liabilities of :									
Central Bank	24	24	26	24	18	17	13	11	11
Commercial Banks	60	57	47	41	46	39	53	54	52
NSB	16	19	18	13	13	19	15	15	15
Finance Companies	-	-	-	-	-	1	1	2	3
Insurance	-	-	-	-	-	-	...	...	17
Provident Funds	-	-	9	21	23	23	16	16	17

Source: Central Bank of Ceylon.

Table 20

COMPOSITION OF CLAIMS AGAINST NON-FINANCIAL UNITS : SRI LANKA

(Rs. Million)

	1950	1955	1960	1965	1970	1975	1980	1983	1984
A. Marketable Instruments	498 (94)	845 (95)	1,628 (92)	3,265 (87)	5,412 (92)	8,905 (81)	25,779 (69)	42,118 (65)	42,678 (61)
1. Government Securities	366 (69)	693 (78)	970 (55)	1,779 (50)	3,316 (53)	5,955 (54)	12,734 (34)	19,997 (31)	23,308 (33)
2. Government Treasury Bills	79 (15)	60 (7)	550 (31)	1,300 (37)	1,950 (31)	2,350 (21)	9,800 (26)	17,400 (27)	14,860 (21)
3. DFCC Equity			1 (...)	1 (...)	1 (...)	1 (...)	11 (...)	5 (...)	9 (...)
4. NDB Equity							4 (...)	24 (...)	57 (...)
5. New Share Issues						1 (...)	14 (...)	1,004 (2)	633 (1)
6. Commercial bank bills purchased and discounted	53 (10)	92 (10)	107 (6)	185 (5)	145 (2)	599 (6)	3,216 (9)	3,688 (5)	3,811 (5)
6.1 Export Bills	48 (9)	69 (8)	51 (3)	47 (1)	107 (2)	317 (3)	1,502 (4)	2,099 (3)	2,033 (3)
6.2 Imports and other local bills	8 (1)	23 (2)	56 (3)	138 (4)	38 (-)	282 (3)	1,714 (5)	1,589 (2)	1,778 (2)
B. Non-Marketable Instruments	32 (6)	49 (5)	138 (8)	283 (8)	828 (13)	2,113 (19)	10,891 (29)	20,650 (32)	25,085 (36)
7. Commercial Bank Loans	32 (6)	49 (5)	138 (8)	282 (8)	814 (13)	1,874 (17)	9,896 (27)	17,956 (28)	20,997 (30)
8. Commercial Bank Investments					5 (-)	4 (...)	362 (1)	592 (1)	837 (1)
9. N.S.B. Loans to Private Sector						34 (...)	75 (...)	126 (...)	148 (...)
10. Rural Banks				1 (...)	9 (...)	87 (1)	177 (...)	392 (...)	508 (1)
11. Finance Companies Hire Purchases Loans and Investments						114 (1)	384 (1)	1,584 (2)	2,595 (4)
Total A + B	530 (100)	894 (100)	1,766 (100)	3,548 (100)	6,240 (100)	11,018 (100)	36,673 (98)	62,768 (97)	67,763 (97)
C. FCBU Loans and Advances to Approved Residents	-	-	-	-	-	-	565 (2)	2,095 (3)	2,026 (3)
Total A + B + C	530 (100)	894 (100)	1,766 (100)	3,548 (100)	6,240 (100)	11,018 (100)	37,238 (100)	64,863 (100)	69,789 (100)

Notes: Relative percentage values are in brackets.

Source: Central Bank of Ceylon.

Table 21

EQUITY AND SECURITIES: SRI LANKA

Rs. Million

	1950	1955	1960	1965	1970	1975	1980	1983	1984
1. Financial Sector	-	-	1	54 (2)	6 (..)	4 (..)	377 (2)	621 (2)	1,460 (3)
1.1 Central Bank Securities	-	-	-	53 (1)	-	-	-	-	557 (1)
1.2 DFCC and NSB Equities	-	-	1	1	1	-	15	29	66 (..)
1.3 Commercial Bank other Investments	-	-	-	-	5	4	362 (2)	592 (1)	837 (2)
2. New Share Issues	-	-	-	-	-	1	14 (..)	1,004 (2)	633 (1)
3. Non-Financial Sector Issues	445 (100)	753 (100)	1,520 (100)	3,079 (98)	5,666 (100)	8,304 (100)	22,520 (98)	36,313 (96)	40,075 (96)
3.1 Government	445 (100)	753 (100)	1,520 (100)	3,079 (98)	5,266 (100)	8,305 (100)	22,534 (98)	37,317 (98)	40,708 (96)
Treasury Bills	79 (18)	60 (8)	550 (36)	1,300 (41)	1,950 (37)	2,350 (28)	9,800 (43)	17,320 (45)	17,400 (41)
Securities	366 (82)	693 (92)	970 (64)	1,779 (57)	3,316 (63)	5,955 (72)	12,734 (55)	19,997 (53)	23,308 (55)
Total (1)+(2)+(3)	445	753	1,521	3,133	5,272	8,309	22,911	37,938	42,168

Note: Relative percentage values are in brackets.

Source: Central Bank of Ceylon

Table 22

TOTAL ADVANCES OUTSTANDING OF FINANCIAL INSTITUTIONS: SRI LANKA

	1960	1965	1970	1975	1979	1980	1983	1984
	Rs. Million							
1. Commercial Bank (Loans)								
(i) Total	560.9	762.9	1,544.1	3,512.9	11,914.4	17,136.2	31,418.2	34,918.6
(ii) Consumption & Housing Consumption only	35.1	64.7	99.1	306.2	776.6	1,123.1	2,470.3	3,000.0
(iii) Agriculture	10.4	34.7	203.0	494.5	1,763.5	2,270.5	3,418.5	3,385.6
(iv) Industry & Tourism	20.1	73.8	416.0	786.1	3,082.7	3,837.7	8,640.1	9,305.0
(v) Commercial	385.1	445.4	643.9	1,655.4	5,723.3	8,771.8	15,262.1	17,364.7
(vi) Financial	101.9	90.8	237.3	142.5	3229.5	447.3	711.1	787.6
(vii) Others	8.6	53.5	44.9	128.2	338.8	685.7	916.2	1,076.0
2. Finance Companies (Loans and hire purchase)			118.7	113.8	151.2	384.4	1,450.9	2,370.2
3. NSB (Total)				34.2	74.0	74.6	125.5	148.2
4. Development Banks								
(i) SMIB (Total)					112.8	126.6	290.9	509.4
(ii) DFCC (Total Loans)	17.8	28.3	70.9	83.0	254.3	323.5	618.3	779.3
(iii) NDB (Direct Loans)	-	-	-	-	-	72.5	682.1	934.7
5. Insurance (Total)					81.9	105.8	6.8	N.A.

Source: Central Bank of Ceylon

Table 23

NEW LOANS GRANTED BY LONG-TERM LENDING INSTITUTIONS : SRI LANKA

(Rs. Million)

Institution	1950	1955	1960	1965	1970	1975	1980	1983	1984
State Mortgage & Investment Bank	9	11	17	9	16	10	27	95	248
National Development Bank	-	-	-	-	-	-	72	288	600
Development Finance Corporation	-	-	5	5	24	17	84	107	213
National Savings Bank	-	-	-	3	5	9	15	31	36
Insurance Corporation	-	-	-	-	-	-	20	36	31
Housing Department	-	-	-	5	15	35	33	n.a.	193*
Total	9	11	22	22	60	71	251	557	1,321

* Housing Development Authority.

Source: Central Bank of Ceylon.

Table 24

COMMERCIAL BANK ADVANCES ACCORDING TO MATURITY : SRI LANKA

(Rs. Million)

	1960	1965	1970	1975	1980	1981	1982	1983	1984
Short-term (below 1 year)	235 (41.9)	287 (37.6)	910 (58.9)	2,620 (74.6)	12,030 (70.2)	14,469 (68.9)	17,401 (68.9)	22,306 (71.0)	25,223 (72.2)
Medium Term (1 to 5 years)	239 (42.7)	274 (35.8)	444 (28.7)	677 (19.3)	3,636 (21.2)	4,381 (20.9)	5,600 (22.1)	6,409 (20.4)	6,489 (18.6)
Long-Term (over 5 years)	86 (15.4)	202 (26.5)	191 (12.3)	216 (6.1)	1,470 (8.6)	2,148 (10.2)	2,264 (9.0)	2,703 (8.6)	3,207 (9.2)
Total	561 (100.0)	763 (100.0)	1,544 (100.0)	3,513 (100.0)	17,136 (100.0)	20,997 (100.0)	25,265 (100.0)	31,418 (100.0)	34,919 (100.0)

Note: Relative percentage values are in brackets.

Source: Central Bank of Ceylon.

Table 24.1

COMMERCIAL BANKS' ADVANCES BY PURPOSE : SRI LANKA

	1960	1965	1970	1975	1980	1981	1982	1983	1984
	(Rs. Million)								
Commercial	385 (68.7)	445 (58.4)	644 (41.7)	1,655 (47.1)	8,772 (51.2)	10,181 (48.5)	12,120 (48.0)	15,262 (48.6)	17,365 (49.7)
Financial	102 (18.1)	91 (11.9)	137 (8.9)	143 (4.1)	447 (2.6)	301 (1.4)	551 (2.2)	711 (2.3)	788 (2.3)
Agriculture	10 (1.9)	35 (4.5)	203 (13.1)	495 (14.1)	2,271 (13.2)	2,277 (13.2)	3,054 (12.1)	3,419 (10.9)	3,386 (9.7)
Industrial	20 (3.6)	74 (9.7)	416 (26.9)	786 (22.4)	3,838 (22.4)	4,624 (22.0)	6,171 (24.4)	8,033 (25.6)	8,605 (24.6)
Housing	-	-	-	140 (4.0)	769 (4.5)	1,181 (5.6)	1,539 (6.1)	1,982 (6.3)	2,519 (7.2)
Consumption	35 (6.3)	65 (8.5)	99 (6.4)	148 (4.2)	354 (2.1)	397 (1.9)	425 (1.7)	488 (1.5)	480 (1.4)
Others	9 (1.5)	54 (7.0)	45 (2.9)	146 (4.1)	686 (4.0)	1,536 (7.3)	1,405 (5.6)	1,522 (4.8)	1,776 (5.1)
Total	561 (100.0)	763 (100.0)	1,544 (100.0)	3,513 (100.0)	17,136 (100.0)	20,997 (100.0)	25,265 (100.0)	31,418 (100.0)	34,918 (100.0)

Note: Values in brackets are sectoral shares.
Source: Central Bank of Ceylon.

Table 25

OWNERSHIP OF PUBLIC DEBT: SRI LANKA

Rs Million										
	1950/51	1954/55	1959/60	1964/65	1969/70	1975	1980	1983	1984	
A. Domestic	514.6 (80.4)	889.3 (81.3)	1,936.7 (86.8)	3,695.5 (86.3)	6,294.8 (80.0)	10,859.4 (74.5)	29,378.8 (56.8)	52,354.6 (53.2)	52,237 (49.3)	
1.1 Central Bank	-	19.1 (1.7)	677.8 (30.4)	1,327.6 (31.7)	2,457.2 (31.2)	2,911.0 (20.0)	11,296.5 (21.8)	20,096.8 (20.4)	17,409 (16.4)	
1.2 Commercial Banks	245.1 (38.3)	292.4 (26.7)	302.5 (13.5)	446.7 (10.6)	386.5 (5.0)	350.3 (2.4)	522.3 (1.0)	1,069.3 (1.0)	949 (0.9)	
1.3 Cooperative Banks				7.0	7.0	6.2	9.3	5.7	-	
1.4 Savings Institutions	97.9 (15.3)	251.5 (23.0)	358.6 (16.0)	475.0 (11.3)	653.9 (8.3)	1,694.9 (11.6)	4,822.2 (9.3)	9,174.5 (9.3)	11,214 (10.6)	
Sub-total	343.0 (53.6)	563.0 (51.4)	1,338.9 (60.0)	2,256.3 (54.0)	3,504.6 (44.5)	4,962.4 (34.1)	16,650.3 (32.2)	30,346.3 (30.8)	29,572 (27.9)	
2. Insurance Funds	21.6 (3.3)	49.7 (4.5)	89.9 (4.0)	219.7 (5.2)	481.5 (6.1)	879.2 (6.0)	1,548.8 (3.0)	1,385.9 (1.4)	1,286 (1.2)	
3. Provident & Pension Funds	40.7 (6.3)	80.5 (7.3)	189.9 (8.5)	642.3 (15.3)	1,281.2 (16.3)	2,473.5 (17.0)	5,588.6 (10.8)	9,783.5 (10.0)	11,791 (11.1)	
4. Balance (A-1-2-3)	109.3 (16.1)	196.1 (18.0)	318.0 (14.2)	577.2 (13.8)	1,027.5 (13.0)	2,544.3 (17.5)	5,591.1 (10.8)	10,838.9 (11.0)	9,588 (9.1)	
B. Foreign	125.4 (19.6)	205.0 (18.7)	293.7 (13.1)	489.3 (11.7)	1,578.4 (20.0)	3,704.9 (25.4)	22,276.8 (43.1)	46,025.0 (46.8)	53,681 (50.7)	
Total	640.0	1,094.3	2,230.4	4,184.8	7,873.2	14,564.3	51,655.6	98,379.6	105,918	

Note: Percentage values are in brackets.

Source: Central Bank of Ceylon

Table 26

COMPOSITION OF FOREIGN CURRENCY FINANCIAL INSTRUMENTS: SRI LANKA
FOREIGN INSTRUMENTS

Year	Foreign Instruments						Rs Million
	Foreign Currency			SDR			
	Central Bank (Including Treasury Bills)	Commercial Banks	FCBUs Loans and Advances	FCBUs Other Assets	Export bills of Commercial banks	holdings of Foreign Securities of Central Bank	
1950	279.5	180.4	-	-	44.9	265.5	
1955	495.7	156.1	-	-	68.6	151.2	
1960	90.0	56.3	-	-	55.4	95.4	
1965	180.5	44.7	-	-	47.1	101.6	
1970	91.1	44.1	-	-	106.5	102.9	
1975	230.3	78.3	-	-	316.7	207.8	
1979	7,238.0	475.5	523.9	72.4	1,205.7	722.2	
1980	3,937.4	845.1	3,620.3	175.9	1,501.9	466.9	
1981	5,591.1	752.2	7,162.6	353.8	1,589.6	1,075.6	
1982	6,219.5	2,031.8	13,140.4	687.2	1,549.8	876.4	
1983	6,003.9	3,015.3	19,510.0	947.5	2,098.5	1,243.0	
1984	9,842.9	3,172.3	18,582.9	1,287.7	2,033.0	2,721.0	

Source: Central Bank of Ceylon.

Table 27

NEW LOANS AND ADVANCES: SRI LANKA										(Rs. Million)
	1950	1955	1960	1965	1970	1975	1980	1983	1984	
Central Bank to Gov't	-	18 (5)	760 (71)	1347 (76)	2219 (75)	2861 (49)	10965 (40)	19393 (40)	15249 (30)	
Commercial Banks	180 (95)	319 (92)	239 (22)	321 (18)	563 (19)	2377 (41)	14159 (52)	23553 (48)	25807 (51)	
Finance Company	-	-	-	-	-	24	73	273	919	
N.S.B.	-	-	-	-	-	252 (4)	918 (3)	2300 (5)	1031 (2)	
Development Bank	9 (5)	11 (3)	12 (1)	14 (1)	33 (1)	31 (1)	183 (1)	494 (1)	778 (2)	
E.P.F.	-	-	63 (6)	98 (5)	144 (5)	289 (5)	1022 (4)	2345 (5)	5625 (11)	
E.T.F.	-	-	-	-	-	-	-	577 (1)	950 (2)	
Total	189 (100)	348 (100)	1097 (100)	1780 (100)	2959 (100)	5834 (100)	27320 (100)	48935 (100)	50359 (100)	

Note: Relative percentage values are in brackets.

Source: Central Bank of Ceylon.

Table 28

ADVANCES AND INVESTMENTS IN FINANCIAL ASSETS BY FINANCIAL INSTITUTIONS: SRI LANKA

(Rs. Million)

	1950	1955	1960	1965	1970	1975	1980	1983	1984
A. Advances									
1. Central Bank to Gov't	14 (7)	-	112 (15)	238 (20)	337 (16)	589 (13)	1,628 (7)	2,795 (6)	4,044 (7)
2. Commercial Banks	183 (89)	324 (97)	544 (72)	850 (71)	1,548 (75)	3,533 (76)	17,000 (69)	31,415 (67)	33,102 (63)
3. N.S.B.	-	-	-	-	-	143 (3)	4,873 (20)	9,278 (20)	11,360 (21)
4. Rural Banks	-	-	-	1	9 (1)	87 (2)	177 (1)	392 (1)	508 (1)
5. S.M.I.B.	9	11	88	86	97	100	127	291	500
6. N.D.B.	(4)	(3)	(11)	(7)	(5)	(2)	...	(1)	(1)
7. D.F.C.C.	-	-	16	23	62	82	268	531	686
8. Finance Company (Loans & Hire Purchases)	-	-	-	-	-	114 (2)	384 (2)	1,451 (3)	2,370 (4)
Total	206	335	760	1,198	2,053	4,648	24,525	46,811	55,447
B. Investments									
1. Central Bank Treasury Bills and Securities	5 (2)	18 (5)	569 (52)	1,148 (49)	1,883 (47)	2,272 (41)	9,338 (58)	16,599 (57)	11,206 (41)
2. Commercial Banks (Securities & Investments)	271 (85)	284 (74)	335 (31)	455 (19)	638 (16)	376 (7)	565 (3)	1,193 (4)	2,741 (10)
3. N.S.B.	-	-	-	-	- (1)	34 (1)	75 (1)	126 (1)	148 (1)
4. D.F.C.C. Equity	-	-	3	5	9	12	55	87	93
5. N.D.B. Equity	-	-	-	-	-	-	...	...	...
6. Insurance	-	-	-	115 (5)	199 (5)	364 (6)	478 (3)	650 (2)	945 (3)
7. E.T.F.	-	-	-	-	-	-	-	577 (2)	950 (3)
8. E.P.F.	41 (13)	81 (21)	190 (17)	642 (27)	1,281 (32)	2,474 (45)	5,589 (35)	9,783 (34)	11,428 (42)
Total	317	383	1,097	2,365	4,010	5,532	16,104	29,039	27,569

Note: Relative percentage values are in brackets.

Source: Central Bank of Ceylon.

Table 29
VALUE OF TOTAL DEPOSITS OUTSTANDING : SRI LANKA

	(Rs. Million)								
	1950	1955	1960	1965	1970	1975	1980	1983	1984
1. Currency (held by public and government)	331 (24)	393 (25)	605 (27)	908 (24)	945 (18)	1,610 (18)	4,184 (13)	7,202 (12)	8,564 (11)
1.1 Held by Public	325 (24)	384 (24)	595 (26)	901 (24)	935 (18)	1,610 (18)	4,180 (13)	7,200 (12)	8,561 (11)
1.2 Held by Government	6 (1)	9 (1)	10	7	10	-	4	2	3
2. Deposits (Total)	1,033 (76)	1,211 (75)	1,476 (65)	2,060 (54)	3,119 (59)	5,453 (59)	23,390 (72)	45,263 (72)	54,463 (71)
2.1 Commercial banks (Total)	811 (59)	911 (57)	1,057 (47)	1,546 (41)	2,394 (46)	3,610 (39)	17,291 (53)	33,276 (53)	39,118 (51)
2.1.1 Demand Deposits	734 (54)	745 (46)	685 (30)	939 (25)	1,225 (23)	1,882 (20)	6,688 (20)	9,068 (14)	10,340 (14)
2.1.2 Other Deposits	77 (6)	166 (10)	372 (16)	607 (16)	1,169 (22)	1,728 (19)	10,603 (32)	24,208 (39)	28,778 (38)
2.2 NSB Deposits	222 (16.2)	300 (19)	419 (18)	514 (14)	708 (13)	1,769 (19)	4,953 (15)	9,472 (15)	11,582 (15)
2.3 Rural Banks	-	-	-	-	17	74 (1)	368 (1)	718 (1)	905 (1)
2.4 Finance Companies	-	-	-	-	-	-	411 (1)	1,404 (2)	2,452 (3)
2.5 Contribution to Insurance	-	-	-	-	-	-	367 (1)	393 (1)	406 (1)
(Value of CO's)	-	-	-	-	-	-	-	(610) (1)	(1,007) (1)
3. Total (1 + 2)	1,364 (100)	1,604 (100)	2,081 (92)	2,968 (78)	4,064 (77)	7,063 (77)	27,574 (85)	52,465 (84)	63,027 (82)
4. Central Bank Securities	-	-	-	53 (1)	-	-	-	-	557 (1)
5. E.P.F.	-	-	187 (08)	781 (21)	1,188 (23)	2,163 (23)	5,052 (15)	9,480 (15)	11,827 (16)
6. E.T.F.	-	-	-	-	-	-	-	624 (1)	1,014 (1)
Grand Total	1,364	1,604	2,268	3,802	5,252	9,226	32,626	62,569	76,425

Note: Relative percentage values are in brackets.
Source: Central Bank of Ceylon.

Table 30

OWNERSHIP OF DEPOSITS OF THE PRIVATE SECTOR WITH COMMERCIAL BANKS: SRI LANKA

	1960	1965	1970	1975	1980	1981	1982	1983	1984
1. Financial Institutions	105 (11.4)	122 (9.3)	208 (10.0)	200 (6.8)	1,116 (7.8)	1,330 (7.2)	1,712 (7.3)	1,666 (6.0)	1,576 (4.8)
2. Plantation	183 (19.8)	113 (8.6)	99 (4.8)	96 (3.2)	329 (2.3)	279 (1.5)	504 (2.2)	1,040 (3.7)	1,978 (6.1)
3. Trading	86 (9.3)	216 (16.5)	286 (13.7)	336 (11.4)	1,438 (10.1)	1,588 (8.5)	1,502 (6.4)	2,145 (7.7)	2,032 (6.2)
4. Manufacturing Establishments	-	-	141 (6.8)	295 (10.0)	966 (6.8)	1,144 (6.1)	1,101 (4.7)	1,792 (6.4)	1,373 (4.2)
5. Other Business	91 (9.8)	153 (11.7)	166 (8.0)	327 (11.1)	2,551 (17.8)	3,801 (20.3)	5,102 (21.9)	3,747 (13.4)	4,661 (14.2)
6. Non-Business Institutions	38 (4.1)	76 (5.8)	122 (5.8)	137 (4.6)	1,265 (8.9)	1,161 (6.2)	1,728 (7.5)	2,501 (9.0)	3,005 (9.2)
7. Local Authorities	23 (2.5)	43 (3.2)	29 (1.4)	62 (2.1)	163 (1.1)	120 (0.6)	102 (0.4)	179 (0.6)	1,121 (3.4)
8. Individuals	399 (43.1)	590 (44.9)	1,032 (49.5)	1,490 (50.6)	6,463 (45.2)	9,286 (49.6)	11,576 (49.6)	14,859 (53.2)	16,983 (51.9)
9. Total	925 (100.0)	1,314 (100.0)	2,083 (100.0)	2,942 (100.0)	14,292 (100.0)	18,710 (100.0)	23,328 (100.0)	27,928 (100.0)	32,730 (100.0)

Note: Relative percentage values are in brackets.

Source: Central Bank of Ceylon.

Table 31

INDICATORS OF FINANCIAL DEEPENING: SRI LANKA

Indicators	1950	1955	1960	1965	1970	1975	1980	1983	1984
(1) Per Capita Real Balance of M1 (adjusted for CPI) Rs	122.5	122.4	118.0	139.9	113.7	115.4	201.0	201.7	191.5
(2) Per Capita Real Balance of M2 (adjusted for CPI) Rs	132.3	139.7	153.5	186.1	180.0	177.7	423.5	509.6	509.8
(3) Per Capita Real Balance of M3 (adjusted for CPI) Rs	162.2	173.8	194.5	228.0	221.0	243.9	529.1	639.2	643.3
(4) Per Capita Real Balance of M4 (adjusted for CPI) Rs	162.2	173.8	194.5	228.0	222.0	246.6	536.9	649.0	653.8
(5) Per Capita Real Balance of Monetary Assets (adjusted for CPI) Rs	232.0	236.2	286.6	438.7	529.1	592.6	1333.9	1511.7	1443.6
(6) Relative Share of Financial Sector in GDP (at current prices) %	-	-	1	1	1	1	3	2	2
(7) Banking Density: Number of Banks per* 10,000 Adult Population**	0.061	0.071	0.076	0.161	0.300	1.271	1.468	1.701	1.697
	0.061	0.071	0.076	0.148	0.220	0.694	0.695	0.735	0.692
(8) Relative Share of Account-holders in Adult Population %	-	-	-	-	8	16	34	53	55

* Only commercial bank branches.

** Commercial bank branches, rural banks and the branches of the NSB.

Source: Central Bank of Ceylon

Table 32

MONETARY AGGREGATES AND THEIR RELATIVE SHARE IN GDP : SRI LANKA

(Rs Million)

Year	GDP	M1	M2	M3	M4	TFA	As a Percentage of GDP				
							M1	M2	M3	M4	TFA
1950	6136	911	984	1206	-	1725	15	16	20	-	28
1955	7635	1073	1225	1524	-	2071	14	16	20	-	27
1960	8529	1209	1573	1992	-	2936	14	18	23	-	34
1965	10139	1716	2283	2797	-	5381	17	23	28	-	53
1970	13187	1967	3115	3823	3840	9152	15	24	29	29	69
1975	25691	3088	4757	6527	6601	15859	12	18	25	26	62
1980	62246	9428	24813	25181	25181	62557	15	32	40	40	100
1983	111976	14748	37257	46729	47447	110514	13	33	42	42	99
1984	138173	16522	43923	55506	56411	124555	12	32	40	41	90

Note: M1 = Demand Deposit + Currency

M2 = M1 + Time and Savings Deposits in Commercial Banks

M3 = M2 + Deposits in the NSB + Rural Banks

M4 = M3 + Deposits in Finance Companies

TFA = Total Financial Assets as defined in Table 11.

Source : Central Bank of Ceylon.

THE FINANCIAL STRUCTURE AND ITS IMPLICATIONS FOR MONETARY POLICY IN THAILAND

by

Nongnart Sondysuvan

I. INTRODUCTION

Overview of the Financial Sector

The financial sector, as one of the most modern and advance sectors in the Thai economy, has undergone various stages of evolution in the past few decades. The dawn of Thailand's modern banking era was in the Sixties when the foundation for a sound banking system was laid through the legislation of the 1962 Commercial Banking Act. Since the inception of this Act, commercial banks have grown phenomenally. However, during the initial period of banking growth, competition was rather limited. In the eyes of the monetary authorities at the time, this was not conceived of as being irrational. Their prime objective then was to achieve monetary stability supported by a sound financial system. Growth came about as a result of this stability and was a testimonial to the success of monetary policies during that era.

Evidences from the mid-Seventies point towards commercial banks' increasing involvement with the nation's priority development sector. For the first time in 1975, all commercial banks in Thailand were requested by the Central Bank to extend at least 5 per cent of their total credits outstanding of the preceding year to the agricultural sector. The branching policy that also emerged during this period further articulated commercial banks' role in the rural areas. When the required credit allocation measure was made applicable to outlying branches, the branch banking system was reactivated and transformed from a group of passive deposit centres

into a relatively more dynamic catalyst in the development of the rural economy.

The banking system's contribution to public finance also went through many aspects of regulations such as the requirement to hold government bonds for branch opening at 16 per cent of total deposits, the inclusion of government bonds in reserve requirements and the creation of the repurchase market in 1979.

Guided credit allocation resulted in banks' declining profitability. This pressure was more acutely felt than rising competition, thus urging commercial banks to become more cost-effective and to seek out new channels to shore up their profits. Entry into the overseas market was made by setting up branches, representative offices, agencies or subsidiaries. This external market has gradually turned into a significant source of earnings for some of Thailand's larger banks. Computerisation schemes have been ambitiously introduced into the banking sector. Professional staff began to take over more responsible positions while the structure of shareholding slowly transformed towards a more publicly-based ownership. But all these appear to have proceeded somewhat unevenly. The transition into more professional banking could be sustained by only a selected number of banks, leaving the others to struggle along and even to be surpassed in terms of assets size by some finance companies.

The emergence of finance companies in the late Sixties conveniently filled the gap of the lack of competition in the financial system. They were initially allowed to operate loosely with neither specific license nor supervision. Eventually, they were legalised as financial institutions with the aim of providing investment banking services. The experience with finance companies, however, turned out to be a glaring example of the possible incongruity between rapid growth and financial soundness.

The performance of finance companies has not fulfilled the early hopes that inspired the liberal regulations to which they were subjected prior to 1979. Flexible interest rates have brought in substantial funds, at times more than what the finance companies could handle. However, these funds were mostly short-term, preventing these companies from going into the longer end of the market, particularly project financing. The stock market boom helped to absorb these funds but nearly sank the system of finance companies with its downfall. Lacking a strong foundation and a clearcut legal framework, the system could not reap any benefits from its previous rapid growth. Moreover, the large number of finance companies has become a perennial problem, causing incessant supervisory difficulties.

With the temporary trough in the system of finance companies, the traditional shortage of term finance in the Thai economy has become more apparent and crucial. Development finance institutions are, as a rule, timid in their operations, constrained partly by a rigid legal structure and partly by unprofessional management. The Bank for Agriculture and Agricultural Cooperatives (BAAC) has made admirable efforts to break out of its strait-jacket operations but is still burdened with large amounts of rescheduled loans with low interest rates. The Industrial Finance Corporation of Thailand (IFCT), on the other hand, can boast of a sounder but a limited loan portfolio. The IFCT has yet to solve its chronic problem of being awash with foreign funds but short of the local currency needed by the clients. The Government Housing Bank has been more or less sidelined due to the shortcomings of its management and liquidity shortage. This typical source of long-term finance is saddled with an additional burden of having to refinance its long-term commitments with short-run credit carrying high and rising interest costs. 1/

1/ Supachai Panitchpakdi, Financial Development in Thailand and Other Developing Countries, Marketing Media: 1985, Bangkok, Thailand.

Compared with the financial sector of other developing countries, Thailand's financial institutions have not fully matured, although already fairly advance in some segments. The Government has tried to put great efforts on the financial system to meet the targets of the national plans, particularly in the areas of improved economic efficiency and resource mobilisation and a better macroeconomic resource balance.

This overview of the financial sector is intended to provide a better understanding of the main focus of this study, that is, the development of the financial structure of Thailand and the policies made upon it so as to make such structure a more effective mechanism in the transmission of monetary policy. A brief historical perspective of the Thai economy and some macroeconomic policies adopted are also discussed in the first part of this study. The second part deals with a more in-depth treatment of the financial institutions while the third part touches on the financial instruments. The evolution of the financial structure of Thailand is traced in the fourth part through the use of some statistical measures of financial development. The instruments of monetary control are described in part five and their effectiveness were related to the financial structure of Thailand. The last part provides some conclusions based on the study's findings.

Historical Perspective of the Thai Economy 2/

A distinguishing feature of the Thai economy has been the tenacity with which, even in the most unfavourable internal and external conditions, a cautious and conservative monetary policy has been pursued with the aim of preserving the international value of the baht. The objective of political independence and a strong national

2/ IBRD, Thailand: Perspectives for Financial Reform, Washington, D.C., 1983.

currency thus combined historically to encourage an aversion to borrowing and a fondness for piling up foreign reserves. Except for a period during the 1930s and 1940s when economic policy was designed along statist and protectionist lines, Thailand was able to pursue an open economy and a market-oriented development strategy from the mid-20th century until the 1970s. The adverse financial and other consequences of the interventionist interregnum of the 1930s led to a broad liberalisation policy in the mid-1950s, including a reform of the foreign exchange and interest rates, a phasing down of import controls and a return to macroeconomic policy environment of reduced public sector involvement in the economy with a renewed emphasis on broad monetary and fiscal discipline.

The years following the liberalisation of 1955-58 until the early 1970s were a period of rapid, sustained and remarkably even economic development in Thailand. GDP grew at an average of 7 to 8 per cent per year while per capita GNP growth averaged 4 to 5 per cent. Real growth in agriculture of nearly 5 per cent was a major contributory factor to these developments as well as to the sustained growth in exports. An increase in investment share to GDP from about 20 per cent to 27 per cent contributed to rapid industrial growth. Investment was largely financed by domestic savings, keeping the foreign debt service ratio quite low.

Since the mid-1970s, Thailand's development problems have been compounded by deteriorating terms of trade and other adverse external factors, including oil price increases, and an increase in inflation and slow growth in developed countries. A relatively high rate of overall growth was maintained but this was accompanied by a shift in economic policy towards rising protectionism and government intervention in the financial system; large fiscal and external deficits; rapid growth of domestic money creation; a decline in the foreign exchange position; and growing dependence in foreign borrowing.

In the latter part of the 1970s, the Government recognised that these trends could not be sustained and policy adjustments were undertaken at a gradually accelerated pace. They included sharp increases in prices of most petroleum products and electricity; measures to increase government revenue; amendments to the usury laws which permitted an increase in interest rate ceilings; and the introduction of regulations to increase financial stability and exercise more monetary restraint.

In the second half of 1980, the Government began to give serious attention to developing a longer-term comprehensive programme in restructuring the economy, and initiated a number of important economic decisions. In late 1980, price controls were lifted on 29 of 36 goods; the Government started on a reform of tariff structure, reducing import duties on 10 categories of electrical goods between 10-60 per cent, and retail prices of sugar, which had fallen out of line with international prices, causing domestic shortage, were increased by 60 per cent. In a number of successive steps, electricity and petroleum prices were increased further, and by mid-1981 they were nearly two-and-a-half times as high as at the start of 1979. During the first half of 1981, charges for other public services (water, transport and communications) were increased substantially. During this period, the Government also introduced various fiscal measures designed to contain the central government deficit.

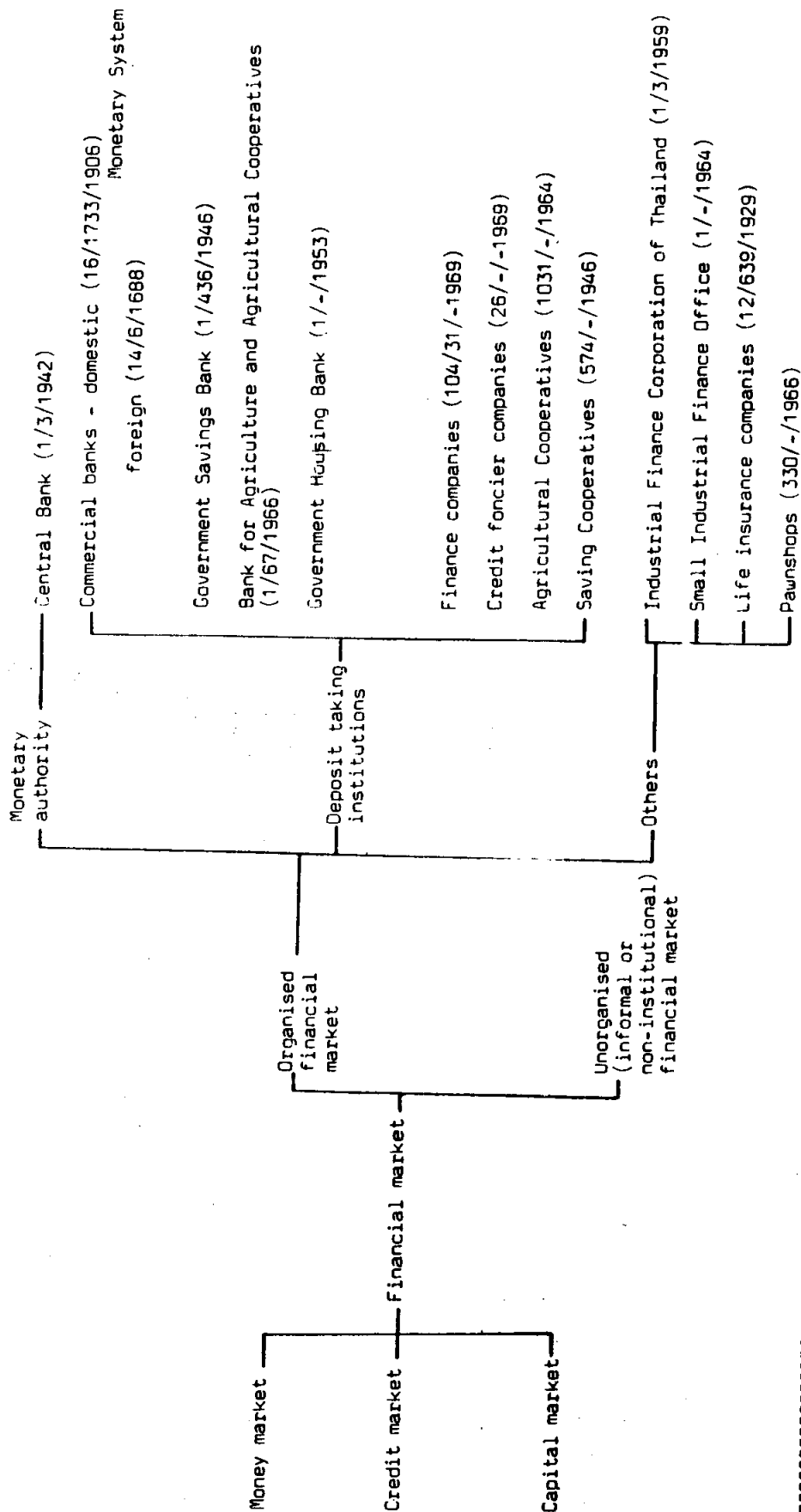
For the remainder of the 1980s, most of the positive factors which contributed to Thailand's rapid socio-economic development over the past quarter-century will continue to do so. These factors include a relatively equitable land distribution, responsiveness of farmers to economic incentives and to appropriate opportunities in technological innovation, provision of infrastructure by the Government and the dynamism of the private sector in both industry and agriculture. The Fifth Five-Year Plan covering the period 1981-86, sets out as its major objectives the recovery of

internal and external financial stability, greater economic efficiency, improvement in the quality of life, particularly of the rural population and national security. These objectives are to be achieved by a reduction in lower priority public expenditures, further reform of public sector pricing and structural adjustments designed to increase the efficiency of market forces and improved competitiveness in world trade. These structural adjustments will be supported by improved fiscal, monetary and balance of payments management; reduced protectionism and the reform of the industrial incentive system; and the reduction of government interference in the market. Interest rate policy is to be the main stimulus to private savings and financial intermediation.

II. INSTITUTIONS IN THE FINANCIAL STRUCTURE

Thailand has a substantial number of financial institutions, the majority of which are privately-owned (see Chart 1). Some, including the Bank of Thailand, belong to the Government. Commercial banks are by far the most important among the different types of financial institutions and form the largest group in terms of total assets, total savings mobilised, and total credit extended. Forming the second largest group are the finance companies. Other groups of financial institutions are the life insurance companies, agricultural cooperatives, savings cooperatives, pawnshops, and credit foncier companies. All of these financial institutions have been operating in Thailand for quite some time except in the case of credit foncier companies which came into existence at about the same time as finance companies. In addition to the financial intermediaries already mentioned, there are a number of specialised financial institutions whose functions are indicated by their names. These are: the Government Savings Bank, the Bank for Agriculture and Agricultural Cooperatives, the Industrial Finance Corporation of Thailand, the Government Housing Bank, and the Small Industries Finance Office. The

Chart 1
THE FINANCIAL SYSTEM IN THAILAND
(As at the end of 1984)



N.B. Figures in parentheses are numbers of institutions, branches and year of the beginning of operation respectively.

salient features of the financial system are enumerated in Tables 1 and 1.1.

The Thai financial system also consists of a substantial unorganised (or non-institutionalised) sector. This refers to all the financial transactions which do not go through organised or legally registered financial institutions. Such transactions include lendings by private money-lenders, operation of the so-called "pia-huay" (or "rotating credit societies"), operation of private credit cooperatives and borrowing and lending among individuals.

The Bank of Thailand

The role of the central bank in Thailand is performed by the Bank of Thailand. The Bank was established in 1942 by the Bank of Thailand Act, B.E. 2485 (1942), with the purpose of assuming central banking functions. The Bank, with the status of a government enterprise, took over the net assets of the Thai National Banking Bureau which was set up in 1939 as the forerunner of a proper central bank. The management of the Bank is vested in the Court of Directors presently composed of 11 members, with the Governor as ex-officio Chairman and the Deputy Governor as ex-officio Deputy Chairman. The Governor and the Deputy Governor are appointed by the Crown on the advice of the Cabinet and the other members of the Court and by the Cabinet on the advice of the Minister of Finance respectively.

The Bank of Thailand has three branches in the provinces: Southern Region Branch at Hat Yai, Northeastern Region Branch at Khon Kaen and Northern Region Branch at Lampang. These branches were set up to provide central banking services to the different regions of the country.

The Bank's main functions, powers and responsibilities are broadly similar to those of central banks in other countries. The Bank is to act: (1) as the note-issuing authority; (2) as banker to

the Government and other banks; and (3) as fiscal agent of the Government in its dealings with international monetary organisations. The Bank is also authorised by the Ministry of Finance to manage public debt, to administer exchange control and to supervise commercial banks, finance companies, securities companies, and credit foncier companies. It carries out its policy functions by the use of the powers conferred on it and through consultation with members of the banking system.

As banker to the Government, the Bank of Thailand holds the main accounts of the Government and those of Government enterprises. Under the Bank of Thailand Act, B.E. 2485 (1942), the Bank may make short-term loans without security to the Government up to 25 per cent of the Government's annual ordinary expenditure. The Government borrows through the sale of Treasury bills and government bonds which may be denominated either in baht or in foreign currencies. Apart from financing part of the Government's budget deficits, the Bank also has the major responsibility of advising the Government on the formulation of monetary policy and its implementation.

The Bank's statutory powers include, in particular, a requirement that all commercial banks are to maintain legal reserves with the Bank of Thailand. The Commercial Banking Act of 1962 and 1979 (revised) also set the ranges within which the Bank may vary statutory reserves of commercial banks and the form in which they may be held. The current ratio is 7 per cent, not more than 5.0 per cent of total deposit may be maintained in the form of cash in hand and unobligated Thai government securities. The Bank may prescribe various other rates and ratios in regulating commercial banks' operations, e.g., the ratio of capital funds to risk assets, maximum deposit rates, maximum loan rates and discount rates.

The Bank is lender of last resort to commercial banks. There are two channels of lending. The Bank makes discretionary loans to commercial banks against government and government-guaranteed

bonds. This is intended as the lender of last resort to commercial banks and the interest rate charged varies from time to time. Lending is also effected through the rediscount window where credit is available for approved promissory notes at a relatively low rate of interest. This function is mainly designed for promotional purpose, and the papers eligible for rediscounting are limited to export bills, agricultural and certain industrial bills. Nonetheless, the rediscount window is also used for special purposes as deemed necessary from time to time.

The Bank is constantly endeavouring to implement new methods and procedures which would make the financial system work more efficiently. A repurchase market for government bonds was established on April 9, 1979 whereby the Bank of Thailand buys and sells government bonds with an agreement to repurchase or resell. This market enables commercial banks to invest their surplus funds on a short-term basis while those which are temporarily short of funds will be able to adjust their positions easily and expeditiously. This is another window for lending to the commercial banks and finance companies through bond repurchasing agreement.

Commercial Banks 3/

Commercial banking has a long history in Thailand. Its success has been a natural outgrowth of its role as the custodian of the means of payment, but this has also been nurtured by protective, solvency-oriented government regulations.

Commercial banking began in Thailand in 1888 with the opening of a Bangkok office of the Hong Kong and Shanghai Bank. The first Thai bank, Siam Commercial Bank, was set up under Royal patronage in 1906, but Thai banks did not play a major role compared

3/ Ibid.

to foreign banks. During the pre-World War II period, for instance, twelve banks had already existed in the Kingdom, only 5 of which were owned by Thais. As a result, commercial banks' major activity was to facilitate foreign trade, especially with Western Europe. Foreign banks, moreover, could offer cheaper trade financing services in and out of the Kingdom because of the advantage of worldwide network of branches and correspondents. Even the Thai banks still concentrated on foreign trade and their operations did not have much effect on other activities such as those of the farmers. This is because most Thai banks were started and managed mainly by merchants whose knowledge of what the banks could do outside the trade sector was indeed very limited.

After the liberalisation reform of 1955-58, foreign banks have been severely restricted. Thai banks opened new branches at an average of 33 each year over the period 1955-69, and by 1967, each of the 71 provinces in Thailand was served by at least one branch of the commercial banking system. Credit extension has become broadly diversified into areas besides the financing of foreign trade, which at end-1984 represented less than one quarter of total bank credit. Up to this period, commercial banks in Thailand remained the most broadly diversified financial institutions, although they are restricted by regulation from engaging in securities business, life insurance, issuance of promissory notes and other activities.

Thai banks experienced a remarkable record of growth in the years following the financial and exchange reforms of 1955-1958. The low inflation and high real deposit rates and level of public confidence that resulted from those reforms enabled commercial banks to generate rapid rates of deposit growth, and hence lending capacity, throughout the 1960s. The liberal financial sector policies of the government prior to the mid-1970s meant that banks were subject to moderate reserve requirements of only 7 per cent, of which 50 per cent could be held in the form of interest-bearing government securities. Banks were also free of mandatory credit allocation requirements which

would have reduced bank profitability and the inducement to increase their equity base to accommodate increased demand for credit.

Nonetheless, the 1950s was a period of trial and error for many Thai banks. Many of them were, in fact, on the verge of insolvency at various times, but the Government intervened on every occasion to restore their solvency, and this, no doubt, provided a strong initial impetus to the growth and credibility of domestic banks. There have been no bank runs in Thailand since 1950, but this early postwar experience in bank regulation created a strong and lasting policy orientation towards protection of bank solvency and stability, a preferred policy over greater competition and access. No new domestic banks have been formed in more than 15 years, as already noted, and there was no detailed structure of regulations providing for orderly and objective conditions of entry, exit, and ownership transfer in the financial system.

As at end-1984, there were 16 Thai banks with a total of 1,749 branches including 22 branches overseas, compared with 20 branches of 14 foreign banks in the country. Thai banks now overwhelmingly dominate the commercial banking business, accounting for 98 per cent of total deposits, 93 per cent of total advances and 94 per cent of total assets of all commercial banks. Despite the spectacular growth of existing Thai banks, entry of new banks has been limited. The latest domestic bank to be incorporated was the Asia Trust Bank, which started operations in 1965. The Krung Thai Bank was established a year later by the merger of two ailing Government-owned banks, the Bank of Agriculture and Provincial Bank. Subsequent to the licensing of the Asia Trust Bank in 1965, no new domestic banks have been granted licenses.

Finance and Securities Companies (FSCs) 4/

Thailand's finance and securities companies constitute an important part of the financial sector. As an indication of size, FSCs' assets of B 118.1 billion as at year-end 1984 was 18.5 per cent of total commercial bank assets. The top five of the 104 Thai finance companies with combined total assets of about B 33.1 billion, or 28 per cent of total finance company assets, are comparable in size to Thailand's small and medium size banks. Most FSCs, however, are very small, with average assets of about US\$ 20 million, without including the top five.

FSCs proliferated in the late 1960s and early 1970s in response to overregulation on commercial banks' activities, prescribed interest rate ceilings, entry, required asset holdings, minimum capital, and the like. Thus, finance companies thrived for a time in a much less restrictive regulatory and legal environment. Many of the early FSCs, established between 1969 and 1975, were set up by domestic and foreign banks. After the FSCs were formally brought under the regulation and supervision of the Bank of Thailand in 1972, the authorities, frustrated by the dilemma between allowing entry of new banks and concern with the long-standing issue of bank solvency, encouraged the growth of FSCs in the hope that they would indirectly bring increased competitive pressure on commercial banks and would mobilise longer-term funds through a less restrictive control of their interest rates. At the same time, as discussed below, finance companies were themselves restricted in a variety of ways after 1972, and many became too heavily involved in the Securities Exchange of Thailand (SET). During the collapse of the stock market in 1979, one prominent finance company went bankrupt, signalling an incipient erosion of public confidence. The authorities intervened on behalf of several other FSCs to protect them from overt bankruptcy or liquidation.

4/ Ibid.

Even before the collapse of the SET in 1979 and the weakening of finance company sector, from which in fact it has not yet recovered, it could not be said that the early expectations of the authorities were realised. While the number of domestic banks has remained fixed at 16 since 1965, FSCs proliferated almost unrestricted until the end of 1977. By 1984, the average size of a commercial bank was thirty times that of an average FSC, but the six largest finance companies are large enough to be among the top thirty financial institutions in Thailand. Yet these characteristics of the sector obscure the fact that the majority of the medium and larger size FSCs are partly or wholly owned by either domestic or foreign commercial banks or jointly. Assets of FSCs with no ties to commercial banks constitute only 25 to 30 per cent of total FSC assets and their average size, as measured by total assets as of end-1984, is below US\$20 million, compared to US\$400 million for an average medium-size commercial bank.

What in fact emerged was a relationship between banks and finance companies that was partially competitive and partially complementary. By and large, the banks, as lenders to FSCs, were able to channel resources into activities either disallowed by regulations or considered inappropriate for banks on the one hand to mobilise resources indirectly through financial instruments (e.g., promissory notes) that were not subject to interest ceilings on the other. Also, promissory notes offered banks an attractive means of holding excess cash, given their high liquidity and rate of return above the cost of deposits.

FSCs thus could not and did not offer much effective competition to existing commercial banks, except in terms of providing opportunities for an enlarged presence of foreign banks in Thailand. On balance, it appears that FSCs in practice have increased the effective relative market shares of the larger commercial banks, by indirectly enabling the latter to undertake a number of activities which had previously been off-limits to them, including the issue of

large denominated promissory notes and commercial paper at unregulated interest rates (until 1980), discounting of post-dated checks, consumer and housing finance, and securities brokerage and underwriting.

FSCs have developed rapidly in the last ten years. They accounted for 70 per cent of the credit to businesses and households supplied by the nonbank financial institutions. Assets of finance companies rose from only \$2.4 billions Baht in 1971 to P105.4 billion baht at the end of 1983. However, in October 1983, a finance company and two of its affiliates were dissolved and it became known that several other companies were facing serious liquidity shortages. As a result, deposits of finance companies declined steadily. The authorities have taken several measures to shore up the financial position and to improve the management of the FSCs. Immediately after the onset of the crisis, the authorities sponsored a "liquidity support fund" financed by commercial banks. The weakest finance companies were put under government control and a few lost their licenses. The authorities announced a scheme by which the Government would take up equity interest in finance companies and credit foncier companies, in exchange for management support. The scheme attracted a large number of finance companies and resulted in a substantial improvement in their public image. The Government also amended the Act regulating FSCs in December 1983, in order to pave the way for a more orderly development of the FSCs. The amendments gave the authorities more power to prescribe preventive measures, to examine and supervise companies and to prosecute violators with criminal offenses. After the amendment, the Bank of Thailand tightened the qualifications of independent auditors, eliminating small firms and establishing higher standards. It also issued regulations on the following points: (1) the qualifications of management of the FSCs, including educational level and minimum financial experience; (2) lending to affiliates; (3) public disclosure requirement regarding the true identity of shareholders, management, and auditors; (4) clear definitions of bad and doubtful assets.

Life Insurance Companies

According to historical records, life insurance business has existed in Thailand since the latter part of the 1870s. However, its operations were carried out rather scarcely, with scant public awareness and even fewer in the case of policy holders. One of the several assumptions explaining such situation was that Thai households at that time were possibly economically sound and stable. This, coupled with a poor understanding of life insurance philosophy amongst the public, resulted in operational stoppage of the so-called business by the end of the then ruling monarch's period. It was not until the reign of King Rama VII (1926-1943), when its essentiality to national economic development was recognised, that the life insurance business resumed and revived its operations. By that time, the authorities found it necessary to bring insurance business under control so that it might not have negative impact on public safety and welfare. This led to the passage of the Act for the Control of Commercial Undertakings Affecting Public Safety and Welfare, B.E. 2471 (1928), which banned the undertaking of insurance business and related activities unless the related regulations are strictly followed. Consequently, the life insurance business has since then been subject to licensing. Subsequently on July 31, 1929, the criteria and procedures for insurance business were first issued, accompanied by the establishment of the "Insurance Division" under the jurisdiction of the Permanent Secretary Office of the then Ministry of Commerce and Communications which is entrusted with registering and supervising insurance companies.

At the initial phase, all the five registered insurance companies operating during the years 1930-1938 were foreign companies. It was not until 1942 that two life insurance companies owned by Thai citizens had come into existence, viz., the Thai Insurance Company and the Thai Sreshthakich Insurance Company.

At present, the network of life insurance companies has broadened as reflected in the increasing number of branches opened in provincial areas all over the country. The number of branches increased rapidly from 195 in 1974 to 639 in 1984, representing a triple increase in the course of ten years. A notable growth was observed for the years 1979 and 1980, when the branches grew to a total of 124 and 66, in that order. In view of such rapid growth, the Ministry of Commerce, on April 9, 1981, issued a ministerial notification prescribing criteria governing the opening of insurance company branches in addition to the former notification issued in 1968 where only qualifications and authority of branch managers were specified. According to the new announcement, more details concerning branch authority, establishment and operations as well as its five-year working plan are required in order to standardise newly-opened branches and control their number at a reasonable level. As a result, only five new branches were opened in 1981. However, the number significantly increased to 123 in the year 1984.

All life insurance companies operate under the Life Insurance Act, B.E. 2510 (1957) and fall under the regulation and supervision of the Ministry of Commerce. Among other things, the Act requires each life insurance company to make a security deposit of B 2 million and to maintain a minimum capital of B 5 million. The Act also empowers the Ministry of Commerce, among others, to specify the various forms in which life insurance companies can invest their funds, to require life insurance companies to deposit a portion of their insurance reserves with the official insurance registrar, and to approve the rate of insurance premium to be set by life insurance companies.

Cooperatives

Agricultural Cooperatives. The cooperative movement in Thailand began in 1916. The number of cooperatives has increased substantially over the years and at the end of December 1984, there

were altogether 2,251 cooperatives. These are classified into six categories, but the most important are the "agricultural cooperatives" and the "savings cooperatives".

The agricultural cooperatives are the largest in number and are spread throughout the country. At the end of December 1984, there were altogether 1,031 agricultural cooperatives. These have been organised by farmers for the purpose of making mutual efforts connected with farming activities as well as making credit available to members. Their principal sources of funds are borrowings (mainly from the Bank for Agriculture and Agricultural Cooperatives) and capital accounts (members' subscriptions to capital plus retained earnings). Deposits have been negligible. Agricultural cooperatives lend directly to their members.

All cooperatives operate under the Cooperative Act, B.E. 2511 (1968). Two departments in the Ministry of Agriculture and Agricultural Cooperatives (the Department of Cooperatives Promotion and the Department of Cooperative Auditing) are empowered to regulate cooperatives and are in charge of their organisation, registration, liquidation, supervision, and audit.

Savings Cooperatives. Savings cooperatives, or registered credit unions, are formed mainly on an occupational basis. The major ones have been organised by school teachers, university employees, provincial policy units, employees of public entities and government departments. A great majority of the savings cooperatives are organised by teachers, and most of the members of all the savings cooperatives are salary earners.

The main source of loanable funds for the savings cooperatives has been their paid-up share capital from members. Each member is required to pay a minimum monthly subscription which is obtained through a payroll-withholding system. Other sources of funds

are reserves and deposits, but these have been relatively insignificant; borrowings and other liabilities have been negligible.

Savings cooperatives utilise most of their funds as loans to members. These loans can be for a variety of purposes including meeting current needs as well as unforeseen expenditures, financing the purchase of consumer durables, home repairs or improvements, etc. Some cooperatives also provide long-term credit for the purchase of user or for financing secondary occupational activities.

The law governing the establishment and operations of savings cooperatives is the same as that for agricultural and other cooperatives, i.e., the Cooperative Act, B.E. 2511 (1968), and the regulatory agencies are—as is the case for all cooperatives—the Department of Cooperatives Promotion and the Department of Cooperative Auditing in the Ministry of Agriculture and Cooperatives.

Pawnshops

Pawnshops lend money against a variety of articles, the most common being jewelry, wrist watches, sewing machines, electrical appliances, and household wares. They may be incorporated or unincorporated. Pawnshops generally operate as small units, with up to ten persons carrying out the operations, and they have no branches. There are presently 3 types of pawnshops: those operated by private businessmen (or "private pawnshops" which may be in the form of companies, partnerships, or one-man business), those operated by the Department of Public Welfare (or "government pawnshops"), and those run by municipalities (or "municipal pawnshops").

Private pawnshops rely mainly on their own resources for loanable funds, but there may also be occasional borrowings from banks and individuals. Municipal pawnshops and government pawnshops obtain initial capital from the municipalities and government budget, respectively, and may also borrow from a variety of sources.

Most loans extended by pawnshops are for the financing of consumption expenditures. Government and municipal pawnshops tend to lend for immediate consumption needs while private pawnshops provide both consumption and small business loans. Most borrowers have relatively low income, and most loans are in relatively small amounts.

All pawnshops operate under the Pawnshop Act, B.E. 2505 (1962), with the Ministry of Interior as the regulatory agency. Registration with the Police Department is required for all pawnshops in the Bangkok metropolis; those in the provinces must register with their respective provincial authorities.

Credit Foncier Companies

Credit foncier companies finance the purchase of immovable property through any of the following methods: (1) loans secured by immovable property, and (2) buying immovable property with the seller's right of redemption. Credit foncier companies are presently allowed to mobilise medium term funds (not less than three years) from the public at a minimum amount of 1,000 baht per account.

Under the Finance, Securities and Credit Foncier Business Act B.E. 2522, credit foncier companies must be authorised by the Bank of Thailand which also issues rules and regulations governing their operations and carries out the supervision and examination functions. By the end of December 1984, 26 credit foncier companies have been authorised.

The Government Savings Bank

The history of the Government Savings Bank (GSB) dates back to 1913 when King Rama VI set up the Savings Office attached to the Royal Treasury. In 1929, the Savings Office was transferred to the Post and Telegraph Department and remained there until 1947 when all its assets and liabilities were transferred to the newly created

Government Savings Bank. The creation of the GSB was effected through an Act of Parliament - the Government Savings Act, B.E. 2489 (1946). The Bank operates as a non-profit organisation under the control and guarantee of the Government but with an autonomous management appointed by the Minister of Finance.

In addition to performing the function of a typical savings institution, the GSB has a Banking Department which carries out normal banking operations including the acceptance of demand (checking) and time deposits, making loans to enterprises and individuals, and selling domestic traveller's cheques. The GSB also undertakes a small life insurance business.

In spite of its various activities, the GSB's role is basically one of mobilising small savings. It has an extensive network of branches throughout the country and also operates a number of mobile units on land as well as along waterways. Savings mobilised by the GSB are mainly in the form of savings and fixed deposits as well as through the sale of premium savings certificates (with a lottery feature). The students (including schoolchildren) are the biggest group of savers, followed by farmers, small traders, government officials, and labourers.

The bulk of the GSB's funds is invested in government securities. This is a matter of policy in compliance with the guideline set by the Ministry of Finance. The GSB has not been encouraged to make loans to the private sector although a certain amount of credit has been granted to enterprises and individuals. A very small amount of housing loans has also been extended.

The Bank for Agriculture and Agricultural Cooperatives

As the name implies, the Bank for Agriculture and Agricultural Cooperatives (BAAC) has the objective of providing credit to farmers and cooperatives. It was set up by the Bank for

Agriculture and Agricultural Cooperatives Act, B.E. 2509 (1966), taking over the assets and liabilities of the Bank for Cooperatives which had been in existence since 1947. Presently, the Ministry of Finance owns about 99 per cent of the BAAC's shares; the remaining shares belong to agricultural cooperatives, farmer groups and individuals. The BAAC has a network of branches throughout the country. Each branch has several field offices.

Nearly half of the BAAC's sources of funds comes from commercial banks. Other sources are capital and reserves (11 per cent), deposits (19 per cent) and loans from the Bank of Thailand (13 per cent).

The BAAC grants credit to farmers either directly or, indirectly, through agricultural cooperatives and farmer groups. Most loans are short and medium term, but a limited amount of long term loans (over 3 years) has also been extended.

The Industrial Finance Corporation of Thailand

The Industrial Finance Corporation of Thailand (IFCT) was set up by the Industrial Finance Corporation of Thailand Act, B.E. 2502 (1959) to supersede the Industrial Bank of Thailand which had been operating since 1952. The IFCT assumed some of the assets of its predecessor in the form of an interest-free 50 year-loan from the Government. Although set up by a special legislation, the IFCT is owned entirely by private interests, principally Thai commercial banks. The Government (through the Minister of Finance), however, has the right to appoint somebody to sit on its Board of Directors as long as the IFCT is accommodated with government loans or government guarantee for its borrowings.

The IFCT functions along the lines of a private development bank or a development finance company. It specialises in financing fixed assets through the extension of medium and long term loans to

industry. It also participates in its customers' equity but up to now this facet of the IFCT's operations has been very limited. Its surplus funds are usually kept as call loans to commercial banks. Moreover, the IFCT issues guarantees to commercial bank on behalf of its customers in order to issue letters of credit since it has no foreign exchange license. In 1972, the Industrial Finance Corporation of Thailand Act was revised so as to enable the IFCT to carry out operations related to the development of the capital market in Thailand.

The IFCT's principal sources of funds at present are long term borrowings (mainly from the Asian Development Bank, long-term credit from the Bank of Thailand, the Thai Government, and the Kreditanstalt fur Wiederaufbau, the International Bank for Reconstruction and Development, Syndicated Yen Loan, Syndicated Singapore Loan, Commonwealth Development Corporation and Japan EXIM Bank) and its own capital and reserves. All foreign borrowings are guaranteed by the Government. From 1971 onwards, rediscount facilities with respect to industrial undertakings have also been made available by the Bank of Thailand to the IFCT.

The Government Housing Bank

The Government Housing Bank (GHB) was established in 1953 under the Government Housing Bank Act, B.E. 2496 (1953). It is completely owned by the Government and is under the supervision and control of the Ministry of Finance. The basic function of the GHB is to help individuals of moderate incomes to obtain houses of their own through its financing facilities. Its principal sources of funds at present are deposits, bond issues and long-term foreign borrowings.

The Small Industries Finance Office (SIFO)

SIFO is not a juristic entity but an office in the Department of Industrial Promotion of the Ministry of Industry. The

principal objective of SIFO is to provide financial and technical assistance to small industrial enterprises including cottage and handicraft industries. It does not grant loans directly but through joint operations with the Krung Thai Bank (a government-owned commercial bank) which also provides matching amount to SIFO's account, presently at the ratio of 3 to 1, for the purpose of lending to small industries. Approval of loan applications is made by SIFO while the Bank undertakes the actual lending operations and also assumes all the credit risks.

The Money Market

Treasury bills are normally purchased by commercial banks and a few other financial institutions. Commercial banks' holdings of such bills vary according to their liquidity position. Purchases of government bonds by commercial banks are substantial because the bonds may be used as part of legal reserve requirement against deposits, and also as pledge against borrowings from the Bank of Thailand. The secondary markets for these two types of government securities are very limited. Buyers usually hold them until their maturities.

Short-dated local bills are not prevalent in Thailand. Instead, post-dated cheques are used and these may be discounted with banks or finance companies. The cheques are never rediscounted. Discount rates on such cheques are usually fairly high, presently at about 18-21 per cent or more.

The call loan market is well developed and instruments issued are normally unsecured. The usual participants are Thai banks as lenders and foreign bank branches and finance companies as borrowers.

The government bond repurchase market, established on April 9, 1979, is part of the Money Market Development Project initiated by the Bank of Thailand. This market will help increase the liquidity

of government bonds held by commercial banks, the GSB, the BAAC, the GHB and finance companies as well as pave the way for the effective implementation of short-term interest rate policy and open market operations.

The Capital Market

An unofficial stock exchange, the Bangkok Stock Exchange, has been in existence since 1962 but it has been rather inactive. In May 1974, a law (the Securities Exchange of Thailand Act) was promulgated to establish a new stock exchange and to place it under the general supervision of the Ministry of Finance and the Bank of Thailand. This law also requires the Bangkok Stock Exchange to cease operations as a stock exchange within nine months. In addition, another legislation is pending which will give certain inducements for the public to hold shares which are listed on the stock exchange and for companies to become "public", i.e., listed on the stock exchange.

In 1972, the Government through Announcement No. 58 of the National Executive Council, required all securities companies to obtain authorisation from the Ministry of Finance through the Bank of Thailand. By the end of December 1984, 92 securities companies had been authorised. Of these companies, 77 also operate as finance companies (authorised to carry on the financing business) and 15 are securities companies only).

III. INSTRUMENTS IN THE FINANCIAL STRUCTURE

Financial instruments in Thailand can be classified into two broad categories, namely claims and equity securities. Total claims have increased from 1967 to reach a level of Baht 730 billion in 1980 and constituted more than 97 per cent of total financial instruments (see Table 2). On the other hand, equity issues amounted to Baht 19.8 billion in 1980, an almost ten-fold increase from its level of Baht 2

billion in 1967. However, as a percentage of total financial instruments, equity issues only accounted 2.6 per cent, a slight improvement over the 2.1 per cent registered in 1967.

All claims against financial institutions have exhibited substantial expansion, namely, currency, deposits and deposit equivalent and life insurance reserves. Likewise, claims of financial institutions against the non-financial sector also showed tremendous acceleration as reflected in short/long term loans and mortgages. Hire purchase debts, on the other hand, only increased marginally from 1967 to 1980 due mainly to the policy of the authorities to discourage such activities of the finance companies.

When viewed on the changes in the share of each type of claims to total claims during the period 1967- 1980, the following percentage shares were obtained. The share of deposits and deposits equivalent has declined from 54 per cent in 1967 to 38 per cent in 1980 while mortgages went down to 1.3 per cent from 2.6 per cent. Such observed declines were compensated for by the increase in the percentage shares of currency, from 2 per cent to 6.1 per cent; short and long term loans, from 18.3 per cent to 28.6 per cent; and commercial bills, from 0.4 per cent to 7.7 per cent.

Claims of non-financial units against financial institutions included currency, with an average share 7-8 per cent while deposits (demand + savings and time) had the largest percentage share at 70-80 per cent as shown in Table 3. Claims of financial units against non-financial units included government securities, at an average share of 20-30 per cent in comparison with the 40-50 per cent share of short and long term loans extended to private sector as shown in Table 4. In the case of equity issues, corporate equities issued by financial institutions shared an average rate of 10-20 per cent of the total equities issued in the economy. Divestiture requirements imposed on financial institutions by the three major legislative reforms of 1979

appeared initially to be a promising method of broadening bank ownership and limiting interlocking group interest.

Of these financial instruments, government bonds and corporated securities are marketable. Transactions in the Securities Exchange of Thailand (SET) as shown in Table 5 showed that since 1977 (2 years after the SET was established), corporated securities comprised the major proportion at nearly 100 per cent. Only the first issue market is fairly well developed for government securities as they are sold mainly to captive buyers, i.e., commercial banks, finance companies, insurance companies and the Bank of Thailand as lender of last resort.

IV. INDICATORS OF FINANCIAL DEVELOPMENT

Financial Interrelations Ratio

One of the most basic techniques of analysing the development of the financial structure of a country is to use the financial interrelations ratio (FIR) which is defined as the ratio of total value of the financial assets in the economy to the Gross Domestic Product (GDP). In the case of Thailand, data derived from the national flow of funds accounts indicated that the ratio of total financial instruments to GDP increased from .89 in 1967, when the first Five-Year National Economic and Social Development Plan started to 1.10 in 1980 (see Table 2). The rise in the ratio during the period was due mainly to the greater demand for financial assets by the private and public sectors generated from the process of economic development as targeted in each Five-Year National Economic Plan. A sluggish trend occurred shortly in some years due to external and internal factors such as the adjustment process in domestic production, on account of the slowdown in world demand (1975-1976), tight liquidity in the economy due to sharp increase in interest rates abroad and negative rates of return in the economy in 1981 and the

restrictive monetary policy adopted in 1984 to dampen the pressure on the external position.

Financial Intermediation Ratio

Indirect funds, that is, funds raised by non-financial sectors through the financial sector accounted for about 30-60 per cent of total funds raised by the non-financial sectors during the period 1967 to 1984 (see Table 6). These shares are in effect, the financial intermediation ratios for Thailand. As the table shows, the ratios fluctuated every year and reached an average of .38 in the 1980s. The ratio of indirect funds raised through the financial sector to GDP rose from 6 per cent in 1967 to a peak of 21.6 per cent in 1983 (see Table 6). This reflects the efficiency of financial intermediation which could transform the process of internal finance (self-financing and taxation) into the process of external finance with the debt-asset system as the principal technique for mobilising savings.

The monetary authorities have also went very far in making financial instruments available in all parts of the country by permitting commercial banks and other nonbank financial institutions to open branches in remote areas to bridge the gap between the organised and unorganised money markets. The success of mobilisation of domestic savings is due mainly to the traditional stability and the unconventional courage to adjust the interest structure. This blend of courage with conservatism in running present-day monetary policy is becoming a necessity as financial uncertainties, particularly in the overseas markets, are multiplying. There is also a prevalent atmosphere of consistency, lucidity, cooperation and non-intervention which provides a fertile ground for long lasting stability of the financial sector. The much-needed stability cultivates a sense of unshaken confidence of the public in Thailand's financial system.

Financial Intermediation to the Government Sector

Financial intermediation provided to the Government sector which is mostly in the form of Government securities (bonds and Treasury bills) has increased over the years from a share of 12.2 per cent of the total funds raised via the financial sector in 1967 to 25.6 per cent in 1980 as the absolute values in Table 4 show. Of the total increase each year, the commercial banking system's contribution to public finance went through many aspects of regulations such as the requirement to hold government bonds for branch opening at 16 per cent of total deposits, the inclusion of government bonds in the composition of the required reserves and the start of operation of the repurchase market in 1979.

Degree of Concentration of Financial Institutions

In mobilising savings. The data in Tables 7, 7.1 and 7.2 show quite clearly the dominance of commercial banks in the mobilisation of private savings vis-a-vis other financial institutions. Throughout the period 1969-1984, the percentage share of outstanding savings of the private sector at commercial banks never fell below 70 per cent, the rate obtained in 1979 when there was an increase in private savings mobilised by the GSB and went as high as 75.6 per cent at the end of 1984.

The case of finance companies is a notable one. In a period of 15 years since their emergence in 1969, their share to outstanding savings grew from 0.4 per cent of total at the end of that year to 9.2 per cent at the end of 1984. Up to 1977, those rankings were still behind that of the Government Savings Bank which came second to the commercial banks. However, the year 1978 saw, for the first time, the emergence of finance companies as the second largest financial intermediaries. Both the Government Savings Bank and life insurance companies have, over the years, had their shares reduced, as have also savings cooperatives and agricultural cooperatives. The share of

household savings held at the Bank for Agriculture and Agricultural Cooperatives was still very small, the share during 1969-1984 has been on the average rate of 0.5 per cent.

Financial institutions which register the highest growth rates of outstanding household savings are the finance companies with rates as high as 42.2 per cent in 1977 and 59.2 per cent in 1978. However, at the end of 1979, the rate dropped to 3.1 per cent due mainly to the failure of one of the large finance companies. The growth rate rose again at 27.3 per cent in 1980 and move up to 32.5 per cent in 1981. However, the rate dropped sharply to -10.2 per cent due mainly to the failure of three and five finance companies in 1983 and 1984, respectively.

The household savings growth rate in commercial banks has been quite steady, averaging 23.1 per cent for the period 1971-1978. However in 1979, the rate dropped to 11.2 per cent. After the upward adjustment of interest rates on all types of deposits since January 1980, the growth rate at the end of 1980 rose to 27.4 per cent per annum.

Also fairly steady, though at a level lower than in the case of commercial banks, is the growth rates for life insurance companies. Life insurance companies experienced setbacks in 1964 and 1968. From 1969 onwards, life insurance companies grew at a rate of 22 per cent.

The Government Savings Bank has been moderately successful in mobilising savings from the general public. The growth rates for the GSB have been relatively high except for the years 1969-1971 and 1974 - 1976 when some declines were noted. In 1972 and 1977, the GSB revised upward interest rate on its deposits so as to make them comparable to those offered by commercial banks. As a result, household savings held by the GSB grew spectacularly, reaching 21.5 per cent in 1972 and 26.2 per cent in 1973.

In providing credit. From the data in Tables 8 and 8.1, it is quite clear that commercial banks are way ahead as the most important source of institutional credit, providing between a low of 68.3 per cent and a high of 80.9 per cent of total credit extended by all financial institutions between 1971 and 1984. It is interesting to note, however, that the share of credit provided by commercial banks fell every year from 84.8 per cent at the end of 1969 to 68.3 per cent at the end of 1978. This fall coincided with the steep rise in the share of credit extended by finance companies which come second as the principal source of institutional credit. Finance companies' share rose every year from only 1.7 per cent at the end of 1969 to 20.7 per cent at the end of 1978. In 1979, its share dropped to 17.3 per cent as a result of the failure of some finance companies as noted earlier, but it went up to 17.7 per cent and 18.4 per cent in 1981 and 1982, respectively. In 1984, its share went down to 14.9 per cent due to the failure of some finance companies. None of the other financial institutions appear really significant as far as the magnitudes of their lendings are concerned, with the exception, of the Bank for Agriculture and Agricultural Cooperatives whose share has been fairly steady, averaging 3.7 per cent for the period 1969-1984.

With respect to growth rates in outstanding credit, the fastest growth rates were from finance companies, registering 99.6 per cent in 1970, rising to the highest rate of 171.7 per cent in 1972, and then coming down slightly but at still very high rates of 63.3 per cent and 61.1 per cent in 1973 and 1974, respectively. After 1975, growth rates have slowed down substantially to a low rate of 23.1 per cent in 1976, and after a negative rate of 1.2 per cent in 1979, the rate picked up to 15.6 per cent in 1980 in line with the rise in savings in finance companies.

Financial institutions with steady and fairly high credit growth rates are commercial banks, life insurance companies, agricultural cooperatives and saving cooperatives. The Government Savings Bank has not been encouraged to make loans to the private

sector and has put most of its funds in government securities. Hence, the GSB has actually reduced its loan portfolio in most of the years between 1964 and 1973. However, since the change in the Banks' administration in 1975, the amount of loans outstanding has somewhat improved. In 1979, the rate of increase was registered at 73.4 per cent. In 1980, the rate of growth turned to negative 1.7 per cent as a result of its sizeable investments in government securities and the use of some of its funds for the rice price support scheme.

The Government Housing Bank is another institution with declining amounts of outstanding loans in some of the years, especially in 1973 when part of its assets was transferred to the National Housing Authority. Nevertheless, there has been a revival in the activities of this agency since 1975 when its loans grew by 58.4 per cent, 82.7 per cent and 65.8 per cent in 1978, 1979 and 1980, respectively.

The Bank of Agriculture and Agricultural Cooperatives' outstanding credit experienced negative growth rates in 1964 through 1966, the period in which it was still the Bank of Cooperatives. (The BAAC was created in 1966 to take over the functions and assets of the Bank for Cooperatives). From 1967 onwards, however, its growth rates were quite high and 1983 saw an increase of approximately 8.7 per cent.

Growth rates for the Industrial Finance Corporation of Thailand were not very steady but were nevertheless quite high also, except for a negative growth rate in 1977.

As to the Small Industries Finance Office, credit extended was very small to begin with, and although in the beginning (1965-1969) very high growth rates were registered, from 1970 to 1977 its credit became almost stagnant. In 1979, a growth rate of 0.7 per cent was observed, and turned to negative rates of 27.9 per cent, 24.7 per cent, 21.7 per cent and 7.3 per cent in 1981, 1982, 1983 and 1984,

respectively. This was caused by the fact that SIFC was awaiting the adjustment of its lending rate from the present 9.5 per cent per annum so as to reduce the interest differential vis-a-vis other financial institutions which had already been adjusted upwards. Certain steps have to be taken before the adjustment could be affected, that is, negotiations with the major contributor, Krung Thai Bank, which charges interest on loans to small industries at 9.5 per cent per annum while SIFO receives 4 per cent per annum on the money deposited at the Krung Thai Bank. (At present, out of the total B 202 million of credit lines to small industries, the Krung Thai Bank provides B 151.5 million and SIFO deposits B 50.5 million or a ratio of three to one). This matter is to be submitted to the cabinet for approval prior to implementation.

Degree of Openness of the Financial Sector

With regard to the degree of openness of the financial sector, data in Table 4 shows that gross foreign funds had an average proportional share of 20-30 per cent of total funds raised by non-financial sectors. Debt in private corporate sector plays a dominant role in mobilising funds from abroad with an average share of 80-85 per cent of total foreign funds during the period prior the year 1975. This has dropped to an average rate of 50-60 per cent since 1976 when government and state enterprise sectors began to rely more on foreign sources. Private borrowings are mostly in short and long-term loan while portfolio investment is minimal.

V. IMPLICATIONS FOR MONETARY POLICY

Instruments of Monetary Policy

The Bank of Thailand as the monetary authority has the responsibility of maintaining the activities of the monetary sector in conformity with the desirable economic objectives of the country. The

power to carry out this task lies with its ability to control the behaviour of commercial banks in general and their lending activities in particular. Three types of control instruments possessed by the Bank of Thailand may be distinguished. Firstly, the Bank of Thailand may exercise the control instruments derived from statutory or administrative enactment as defined in the Bank of Thailand Act (1942) and the Commercial Banking Act (1962 and revised in 1979). The powers that fall in this class are the power to:

- (a) vary the legal cash reserve requirement in relation to the volume of deposits or the volume of borrowings;
- (b) vary the ratio of risk assets to capital;
- (c) prescribe the ratios of specified assets to capital;
- (d) set maximum interest rates on loans and various types of deposits;
- (e) regulate the proportion of loans to one borrower; and
- (f) examine the accounts of commercial banks.

Apart from the powers conferred by the Bank of Thailand Act and Commercial Banking Act, the Bank of Thailand is also empowered to control finance companies under National Executive Council Decree No. 58, 1972, Ministry of Finance Notifications 1972 and 1978, replaced by the Finance, Securities and Credit Foncier Companies Act 1979 and 1983 (Emergency Decree). The instruments specified in the new Act include:

- (a) liquidity ratio, which, at present, is set at 7 per cent for borrowings from both individuals and juristic persons;

- (b) capital to risk assets ratio which is fixed at not less than 6 per cent;
- (c) minimum registered capital which is fixed at 60 million baht;
- (d) minimum amount for promissory note which is stipulated at 10,000 baht for Bangkok and 5,000 baht for non-Bangkok regions;
- (e) maximum amount of loans to any one person which is stipulated to be 30 per cent of capital funds, as from May 1, 1983;
- (f) examination of finance company accounts;
- (g) terms and conditions of hire purchase finance;
- (h) maximum amount of loan for specific purpose which is set at 5 per cent growth rate in the case of hire purchase financing;
- (i) selective credit control;
- (j) maximum interest rate on loans; and
- (k) maximum interest rate on promissory notes.

Details of monetary control by the Bank of Thailand on commercial banks and finance companies as well as details of other instruments exercised by the Ministry of Finance, the Ministry of Commerce, the Ministry of Agriculture and Agricultural Cooperatives, the Ministry of Industry, and the Ministry of Interior are presented in Table 9.

Policies on the Financial Structure and their Implications on the
on the Effectiveness of Monetary Policy

Thailand's record of financial deepening and sophistication over the past quarter century is among the more impressive in the developing world. However, the 1970s brought the country to a period of difficult adjustments to external instability. The Government sought to offset the effect of worldwide recession and inflation through expansionist macropolicy and more active intervention in the economy. Since the mid-1970s, financial sector policy in Thailand has tended to increasingly regulate the flow of financial resources, and this has had adverse effects on the strength of a number of important financial institutions. Continued Government intervention in the allocation and pricing of financial resources would weaken the financial system, increase its dependence on scarce Government resources, and discourage savings mobilisation.

After some apparent early success, the economy began to show in the late 1970s evidence of macroeconomic imbalances and a financial sector under stress. Thus, Thailand entered the 1980s facing a broad restructuring and reassessment of its economic policies in general, and of the role of the Government in the financial system, in particular. The Government has taken a number of steps to bring domestic, financial, monetary and fiscal policies into better balance than what was seen in the 1970s. Moreover, the Fifth Five-Year Plan contains a number of proposals for restructuring policy incentives as well as the financial system. The success of these efforts will be important in helping to ensure that the financial system will have the ability to make resources available at the sectoral level to finance the targets of the Plan.

The discussion on monetary policies and measures in this section will be divided into two major areas which are closely related

to the main strategies to maintain economic stability in Thailand: (1) interest rate policy and mobilisation of domestic savings and (2) flexible adjustments in monetary policy in response to changes in the world economy.

1) Interest rate policy and its effectiveness in mobilising domestic savings. Although the statutory powers of the Bank of Thailand and the Ministry of Finance have been used to determine maximum rates on deposit, adjustments in these rates prior to 1978 (starting year of taxation on interest from deposits) had been infrequent and of a very small magnitude. The major change in policy on interest rates on deposits (and also on lending by financial institutions) took place at the end of 1979, when the Civil and Commercial Code Section 654, which set a ceiling on interest rates on lending at 15 per cent per annum, was amended. This usuary law, which had been in existence for 51 years, in effect had limited the monetary authority's ability to make upward adjustment of the ceiling on deposit rates. The amendment empowered the Ministry of Finance and the Bank of Thailand to set ceilings on loan and deposit rates in line with economic conditions. As a result, the ceiling on the deposit rate was revised twice during 1980-1981, resulting in a total increase of 4 percentage points compared with the rate prevailing at the end of 1979. This measure, coupled with the deceleration in rates of price increases which began at the end of 1981, made net return on deposits at financial institution become much higher than the inflation rate, thus producing a major incentive for people to save. Time and savings deposits of the banking sector rose up markedly from 16.1 per cent in 1979 to 25.1 per cent in 1984. This consequently improved the savings-investment balance, from a net surplus of 1.2 per cent for the period 1975 to 1979 to a surplus of 4.1 per cent of GDP from 1980 to 1984.

2) Flexible adjustments in monetary policy in response to to changes in the world economy. 5/ Under the circumstance that the volatile world economic performance inevitably affects the Thai economy as has occurred since the mid-1970s, it is necessary for Thailand to maintain flexibility in the management of its major economic policies and keep abreast with changing world conditions, in order to mitigate the destabilising effects on the economy both in the short and long runs. Monetary policy responses to external disturbances are discussed as follows:

1. The first oil crisis which was associated with the commodity boom of 1973-74 resulted in high growth of both import values and export values. Substantial surpluses in net receipt on services and transfers as well as in the balance of payments were also recorded in this period.

1.1 High export growth stimulated related activities and demand for bank credit especially in the second half of 1973. To contain commercial banks' borrowing from the Bank of Thailand, the Bank rate was increased by 2 percentage points in August and commercial banks were also asked to restrain and to specify purposes for borrowing from the Bank. Nonetheless, private credit expanded at a record rate of 43.0 per cent and domestic credit increased by 28.2 per cent. The year 1973 thus saw both an increase in net foreign assets and acceleration in domestic credit expansion.

1.2 Additional restrictive monetary measures were implemented in the first half of 1974 when demand for commercial bank credit of the private sector remained strong. The measures comprised

5/ Department of Economic Research, Bank of Thailand, Answers to the SEACEN Questionnaire for Research Project on Monetary Responses to Exogenous Shocks, Bangkok, 1985.

a further increase in the Bank rate to 11 per cent, an increase in ceiling rates on commercial bank deposits of all maturities and on commercial bank loans by 1 percentage point, and an increase in required reserve of commercial banks from 7 per cent of total deposits to 8 per cent.

In mid-1974, the tight liquidity position of commercial banks prompted the Bank to relax monetary policy stance by reducing required reserve to 7 per cent in early September. Private credit thus continued to grow at a high rate of 34.0 per cent. Meanwhile, credit to the government declined by 13.2 per cent due to a record government cash surplus. Therefore, the growth of domestic credit slowed down markedly whereas net foreign assets rose further.

2. Depressed commodity prices in 1981-84 and world recession necessitated the implementation of a number of adjustment policies. For one thing, export-led growth could no longer be expected as in the 1960s and the 1970s. Meanwhile, domestic demand could not be allowed to expand excessively if economic stability is to be maintained. Policies of adjustment in this period comprised successive devaluations (twice in 1981 and again in 1984), adjustments of interest rate ceilings (1981, 1983 and 1984), the imposition of credit ceiling in 1984, the control on the opening of letters of credit for imports in 1983-84, and cautious monetary and fiscal policy stance.

The objectives of some of these measures were not only for curtailing domestic demand but also for allowing the Thai financial system to adjust more flexibly against volatile foreign interest rates and exchange rates. Adjustments of interest rate ceilings were the continuation of the move towards flexible interest rate regime which started in 1980.

3. The baht remained pegged to the US dollar after the Smithsonian Agreement in 1971 until 1978. Exchange rate policy had

not played an active role in the country's economic management in spite of the fact that exchange rates of major currencies fluctuated widely in some years. Upward adjustment of the baht vis-a-vis the US dollar by 4 per cent was made once in July 1973. Gradual moves toward a flexible regime were made in 1978 when the baht was unpegged from the US dollar and aligned with a basket of currencies in March to ensure greater flexibility of the baht value. However, the value of the baht against the US dollar remained practically unchanged.

In November, the Exchange Equalisation Fund brought into effect the system of daily fixing of exchange rate of the baht vis-a-vis the U.S. unit and six other currencies to reflect market supply and demand more closely. Nonetheless, the baht was allowed to move within a narrow band of 20.2 - 20.98 per US dollar in November 1978 to June 1981, while the trade-weighted index of the real exchange rate of the baht was in the range of 81.377 - 102.396 (1973=100). In 1981, huge trade deficit brought the baht under heavy speculative pressure. The baht was therefore devalued twice and the system of daily fixing was abolished in July. When the value of the US dollar shot up in recent years the baht which was pegged to the U.S. unit came under pressure again. Devaluation of the baht against the U.S. unit by another 14.8 per cent was made in November 1984 when a flexible system of aligning the baht with a basket of currencies was also reintroduced. Subsequently, wider fluctuations of the unit against the US dollar have been allowed as the latter has become very volatile.

4. The first and second oil crises entailed unprecedented import and export price hikes and hence, the country's inflation rates were in double digits in 1973-74 and 1979-81. A number of policy measures were adopted to alleviate the effects of imported inflation.

4.1 In the high inflation period of 1973-74, a number of fiscal measures were endorsed. Firstly, excise tax on petroleum and

petroleum products as well as business tax and import duties on raw materials and essential finished products were reduced. Secondly, Government financial operations also helped dampen upward pressure on prices from the demand side. On the one hand, Government capital expenditures declined by delaying the implementation of a number of projects as the Government's capital expenditures appropriated at the beginning of the fiscal year had not amply allowed for the shoot-up in prices. On the other hand, Government revenues rose sharply, due to high inflation. Government cash position thus improved markedly in 1973 and recorded a surplus in 1974, despite a significant pay rise for Government employees. As a result, net claims of the monetary sector on the Government grew by only 9.5 per cent in 1973, compared with 37.4 per cent in 1972, and then dropped by 13.2 per cent in 1974.

4.2 The second oil shock which started in 1979 brought another upsurge in the country's domestic price level and was also accompanied by volatility in foreign interest rates and exchange rates. Apart from encountering these economic problems, the country was also faced with a number of difficulties in its financial system. These were the collapse of one large finance company which triggered off a confidence crisis, a slump in the Securities Exchange of Thailand, as well as tight money situation. The fight against inflation in this period was therefore more difficult than during the first oil shock. Monetary measures implemented were successive upward adjustments in the ceilings on both deposit and loan rates of financial institutions to allow financial institutions to adjust more flexibly against volatile foreign interest rates. Thus, although the authorities had to give financial assistance to the securities business and inject money to alleviate the tight money situation arising from massive capital outflows, domestic demand, and especially private investment, was significantly dampened by higher interest rates.

VI. CONCLUSION

The study has already led to a better understanding of the relationship between the development of the financial structure in Thailand and the effectiveness of monetary policy. The general rise in the financial interrelations ratio through time since 1967 indicates greater demand for financial assets of private and public sectors generated from the process of economic development as targetted in each five-year plan. Indirect funds raised through the financial sector in proportion to GDP increased satisfactorily during the same period and reflected the efficiency of financial intermediation which could transform the process of internal financing (self-financing and taxation) into the process of external financing with the debt-asset system as the principal technique for mobilising savings.

The monetary authorities have also done considerable efforts in making financial instruments available in all parts of the country by permitting commercial banks and other non-bank financial institutions to open branches in remote areas. This was also intended to bridge the gap between the organised and unorganised money markets. The success in mobilising savings is due mainly to the traditional stability of the economy and the unconventional courage of the Bank of Thailand to adjust the interest rate structure. This blend of courage with conservatism in running present-day monetary policy is becoming a necessity as financial uncertainties, particularly in the overseas markets, are multiplying.

The analysis of Thailand's monetary experience provides several lessons with regard to formulation and implementation of monetary policy. 6/

1. Monetary policy needs to be formulated and implemented in a flexible manner to allow for changing circumstances which includes changing economic environment, both external and internal. These factors could alter the balance among key economic variables which have been targetted for earlier, and also include important structural changes that could change the basic relationship among key monetary variables which have been used in formulation of the policy.

2. Effectiveness of monetary policy, particularly in a developing countries setting, depends on several factors. Among the important factors are the nature of financial system and functioning of financial mechanism, the availability of instruments for monetary control and the ability to minimise the impact of external monetary shocks.

3. Monetary policy must be conducted within the framework of overall macroeconomic policy. Monetary measures need to be supplemented by other adjustment policies in a coordinated and sustained manner, particularly when the authorities are dealing with complicated economic problems which involve significant trade-offs among basic economic objectives.

6/ Chaiyawat Wibulsawasdi, Formulation and Implication of Monetary Policy: A Study of Thailand's Monetary Experience during 1983-1984. Paper prepared for the SEANZA Central Banking Course, Kathmandu, Nepal, 1984.

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Table 1
SALIENT FEATURES OF FINANCIAL INSTITUTIONS IN THAILAND AS AT THE END OF 1984 1/

Institutions	Operations began	No.	Branches	Deposits Equivalent	Borrowing	Households Savings Mobilised	Capital Account	Credit extended	(Millions of Baht)	
									Investment	Total assets
1. Commercial banks	1,888	30	1,739	500,893.5	73,084.0	399,055.8	36,291.0	474,993.2	86,465.5	639,359.8
2. Finance companies	(1,969)	104	29	74,404.5	25,475.9	48,551.9	9,028.6	95,029.6	8,729.4	118,148.9
3. Life insurance companies	1,929	12	639	(13,553.7)	(50.0)	(13,553.7)	(520.0)	(6,256.4)	(4,767.0)	(15,250.6)
4. Agricultural cooperatives	1,916	1,031	-	(308.2)	(4,512.7)	(2,428.2)	(2,246.0)	(5,136.3)	(111.4)	(7,235.4)
5. Savings cooperatives	1,946	574	-	(1,213.6)	(454.9)	(10,055.2)	(10,978.7)	(10,978.7)	(4.5)	(12,136.2)
6. Pawnshops	1,866	330	-	-	(2,454.3)	-	(1,493.8)	(3,506.5)	-	(4,070.2)
7. Credit foncier companies	(1,969)	26	-	2,319.3	986.8	1,322.5	767.9	2,962.5	178.7	4,352.4
8. Government Savings Bank	1,946	1	435 3/	47,083.9	-	45,856.6	2,866.8	1,228.2	46,573.1	54,159.1
9. BAAC	1,966	1	67	13,900.1	7,691.3	1,984.4 2/	2,743.8	19,608.5	250.0	25,203.6
10. Industrial Finance Corp. of Thailand	1,959	1	3	-	7,730.3	-	1,781.5	6,094.8	242.2	11,103.2
11. Government Housing Bank	1,953	1	-	5,481.5	5,432.4	5,178.1	1,719.8	10,084.5	0.1	12,912.9
12. Small Industrial Finance Office 2/	1,964	1	-	-	-	-	55.9	40.7	-	55.9
Total		2,112	2,912	659,158.3	127,882.6	527,986.4	69,897.1	635,923.7	147,321.9	903,988.2

1/ Figures in parentheses are estimated

2/ At September 1983

3/ Including 7 amphur (district) agencies.

Table 1.1

FINANCIAL INSTITUTIONS IN THAILAND: CLASSIFIED BY ACTIVITIES AND ASSETS

Institution	Establishment	Activity	Assets (Billion Baht)		Growth Rate of Total Assets (%)		
			Amount (1984)	Share (%)	1971- 1975	1976- 1980	1981- 1984
1. Commercial Banks (CB)	Foreign Bank established in 1988 Thai Bank established in 1906	1. Mobilize funds by taking deposits from the public 2. Lending in the forms of loan, overdraft and bills discounting 3. Investing in securities	639.4	71.3	19.3	16.5	15.9
2. Finance Companies (FC)	Finance companies have been operation since 1953 but full-fledged finance companies began operations in 1969	1. Issuing promissory notes 2. Purchasing promissory notes 3. Investing in securities	118.1	13.2	57.2	18.5	11.3
3. Government Saving Bank (GSB)	1946	1. Mobilize funds by taking deposits from the public 2. Investing in government securities 3. Lending to public	54.2	6.1	13.0	12.4	14.8
4. Bank for Agricul- ture and Agricul- tural Cooperatives (BAAC)	1966	1. Taking deposits from the public 2. Lending to farmer and agricultural cooperatives	25.2	2.8	26.4	18.3	6.8
5. Government Housing Bank (GHB)	1953	1. Mobilize funds by taking deposits from the public 2. Lending to public for housing purpose	12.9	1.4	144.6	38.8	2.4

Table 1.1 (cont'd)

Institution	Establishment	Activity	Assets (Billion Baht)		Growth Rate of Total Assets (%)			
			Amount (1984)	Share (%)	1971- 1975	1976- 1980	1981- 1984	
6. Credit Foncier Companies (CF)	1958	1. Mobilize medium term funds (not less than 3 years) from public by issuing promissory notes at minimum amount of 1,000 Baht per note	4.4	0.5	17.3	24.1	-4.0	
		2. Lending for housing purpose						
7. Industrial Finance Corporation of Thailand (IFCI)	Established in 1959 to supersede the Industrial Bank of Thailand which had been in operation since 1952	1. Borrowing long term funds from both domestic and foreign source	11.1	1.2	20.5	15.8	19.0	
		2. Extending medium and long term credit to industry						
8. Agricultural Cooperatives (ACCOOP)	1916	1. Main sources of funds are borrowing from BAAC and member's subscriptions to capital account	6.8	0.8	29.6	10.9	0.0	
		2. Lending directly to their members						
9. Saving Cooperatives (SCOOP)	1946	1. Main sources of funds are paid-up share capital and members' savings	5.7	0.6	15.1	20.7 (1981)	29.2	
		2. Lending short term and long term to members						
10. Life insurance companies (IC)	1928	1. Selling life insurance policy	15.3	1.7	14.8	19.4	17.2	
		2. Lending and investing in securities						

Table 1.1(Cont'd)

Institution	Establishment	Activity	Assets (Billion Baht)		Growth Rate of Total Assets (%)			
			Amount (1984)	Share (%)	1971- 1975	1975- 1980	1981- 1984	1984
11. Pawnshop	1866	1. Main source of funds are their own savings and borrowing from financial institutions 2. Lending money against a variety of articles, jewelry, gold, machines, electrical appliances etc.	4.1	0.4	17.3	13.7	3.5	
12. Small Industrial Finance Office (SIFO)	1964	1. Receiving funds appropriated from government budget and then deposit it with Krung Thai Bank. When provide funds to small scale industries, Krung Thai Bank provide matching amounts to SIFO's account at the ratio of 3 to 1	0.06	0.0	1.1	0.04	0.02	
13. Securities Exchange of Thailand	Unofficial stock exchange, Bangkok Stock Exchange had been operated since 1962. In 1974 Bangkok stock exchange was replaced by Securities Exchange of Thailand which has been set by special Act	Working as the capital market						

Table 2

FINANCIAL INSTRUMENTS IN THAILAND
(In Million Baht)

	<u>Outstanding Amount</u>		<u>Percentage Distribution</u>	
	<u>1967</u>	<u>1980</u>	<u>1967</u>	<u>1980</u>
I. Claims	<u>93,994.6</u>	<u>730,124.7</u>	<u>97.9</u>	<u>97.4</u>
A. Claims against financial institutions	<u>54,055.9</u>	<u>339,657.8</u>	<u>56.3</u>	<u>45.3</u>
1. Currency	9,823.9	45,681.6	10.2	6.1
2. Demand deposits	5,882.4	21,358.7	6.1	2.8
3. Other deposits and deposit equivalents *	38,049.6	266,853.4	39.6	35.6
4. Life insurance reserves	300.0	5,764.1	0.3	0.8
B. Claims against non- financial sectors	<u>39,938.7</u>	<u>390,466.9</u>	<u>41.6</u>	<u>52.1</u>
1. Commercial bills	364.7	58,103.5	0.4	7.7
2. Short & long term loans	17,532.1	214,222.3	18.3	28.6
3. Mortgages	2,437.3	9,586.8	2.5	1.3
4. Hire purchase debts	3,871.3	3,877.5	4.0	0.5
5. Government securities	15,733.3	104,676.8	16.4	14.0
II. Equity	<u>2,058.4</u>	<u>19,840.0</u>	<u>2.1</u>	<u>2.6</u>
Total	<u>96,053.0</u>	<u>749,964.7</u>	<u>100.0</u>	<u>100.0</u>
	=====	=====	=====	=====
Ratio of Total to GDP	.89	1.10		

* Includes promissory notes payable of finance companies

Table 3
SOURCES OF FUNDS OF FINANCIAL SECTORS (CONSOLIDATED)

Line	1967	1968	1969	1970	1971	1972	1973	1974	1975	1976	1977	1978	1979	1980
1	Total Source of Funds (Excluded Share Capital)													
2	5,342.5	4,515.7	7,145.5	6,214.7	7,262.0	16,615.1	23,584.2	23,927.5	15,715.1	29,522.6	48,183.5	66,674.5	47,677.6	63,986.8
3	4,095.3	4,662.3	4,369.3	5,324.3	8,102.7	13,490.1	17,019.3	17,989.9	15,814.5	24,607.5	36,928.5	36,928.5	34,496.3	68,340.4
4	3,643.2	4,435.5	3,908.8	4,810.2	7,104.0	12,059.1	15,085.5	16,234.2	15,748.1	21,615.3	28,144.2	38,347.8	29,406.3	61,233.8
5	396.1	721.9	281.6	836.1	954.3	2,187.1	3,160.2	1,434.6	1,516.3	3,381.5	2,240.3	3,999.0	3,194.3	3,194.3
6	2,670.4	3,183.1	3,110.0	3,541.9	5,396.8	9,225.5	9,592.4	13,059.2	12,906.5	16,948.8	21,262.4	18,658.6	18,872.8	40,859.8
7	6.0	- 7.7	9.1	23.7	- 17.7	- 30.9	144.0	- 1.9	- 95.0	- 36.7	1,574.1	1,231.0	92.2	724.1
8	- 0.3	- 0.3	- 0.2	- 0.3	- 0.3	- 9.8	- 112.4	1.3	4.9	15.9	70.9	133.6	57.9	1,486.6
9	-	-	10.2	-	-	-	- 178.3	203.7	85.2	- 409.4	532.5	10,311.7	147.1	5,048.5
10	517.0	528.3	405.8	408.8	770.9	686.2	2,123.0	1,537.3	1,329.0	1,715.9	2,364.2	3,956.2	2,888.0	9,917.7
11	452.1	226.8	460.4	514.1	998.7	1,431.0	1,933.8	1,755.7	66.4	2,992.2	8,784.3	5,503.5	5,090.0	7,106.6
12	482.8	230.0	463.7	498.8	869.3	1,154.7	1,769.6	1,529.9	351.7	2,242.0	6,467.3	4,167.0	3,946.7	4,373.5
13	- 26.2	- 6.6	- 0.6	- 30.5	7.8	146.6	-	- 3.4	- 0.5	-	3,006.2	2,547.9	1,441.4	275.8
14	-	-	-	-	-	-	-	-	-	-	-	-	- 759.8	368.1
15	-	-	-	-	-	-	-	-	-	-	-	-	-	-
16	- 4.5	- 3.4	- 2.7	45.8	121.6	129.7	169.3	185.4	- 257.8	275.2	- 811.79	- 619.6	- 659.8	1,151.0
17	349.3	- 1,041.3	1,582.6	- 663.6	- 1,363.2	2,072.0	1,999.9	3,280.4	- 2,802.9	56.0	244.7	1,512.1	1,586.8	2,736.3
18	60.7	315.3	205.6	170.7	191.7	- 93.6	232.6	336.7	390.8	- 254.0	- 675.4	1,166.6	- 585.8	663.1
19	296.7	- 1,340.7	1,386.2	- 780.8	- 1,561.9	2,241.2	1,661.5	2,569.0	- 3,264.9	161.5	789.4	172.1	2,258.8	2,041.5
20	-	-	-	-	-	-	-	- 0.3	10.6	6.6	80.5	4.5	10.2	- 1.5
21	- 13.1	- 15.9	- 9.2	- 8.9	- 6.0	- 6.6	104.6	286.2	- 33.5	63.0	13.7	214.2	- 143.3	37.1
22	5.0	-	-	- 34.6	23.0	- 69.0	1.2	88.2	94.1	58.9	56.5	- 45.3	46.9	- 3.9
23	24.7	17.1	34.1	96.2	226.0	173.3	195.2	218.9	410.6	293.3	507.6	162.4	- 274.3	- 131.9
24	4.9	1.5	-	0.9	- 6.2	- 0.6	- 0.2	0.6	-	4.8	- 4.0	1.6	4.8	- 8.4
25	19.8	15.6	34.1	95.3	232.2	173.9	195.4	218.3	410.6	288.5	611.6	160.8	- 279.1	- 123.5
26	-	-	-	-	-	-	-	-	-	-	-	-	-	-
27	439.6	366.0	437.5	448.7	- 173.7	122.2	569.6	381.9	103.0	891.9	2,118.6	3,127.4	393.3	1,023.7
28	- 14.5	5.8	37.8	- 2.1	12.8	- 13.7	- 4.6	19.8	63.2	- 47.5	47.5	60.7	63.3	- 34.6
29	454.2	380.3	399.7	450.8	- 186.5	135.9	574.2	362.1	39.7	938.9	2,071.1	3,066.7	402.8	1,061.3
30	- 0.1	- 0.1	-	-	-	-	-	-	0.1	-	-	-	- 72.8	- 3.0
31	433.6	491.6	722.1	999.1	460.2	757.5	3,800.2	2,056.4	2,189.9	3,673.9	8,284.1	18,021.3	11,475.5	- 7,981.7
32	366.6	462.9	603.1	941.0	263.2	417.2	3,673.0	1,668.0	1,808.0	1,724.0	7,368.0	12,818.4	6,606.6	- 8,977.9
33	67.0	28.7	119.0	58.1	197.0	340.3	125.1	388.2	372.0	1,941.2	910.9	5,192.1	4,868.9	996.2
34	-	-	-	-	-	-	2.1	- 0.8	9.9	8.7	5.2	10.8	-	-
35	327.5	335.4	114.6	506.6	645.4	330.3	683.4	1,092.2	886.2	632.8	2,254.3	2,922.3	3,486.6	2,920.3
36	168.8	180.9	62.0	265.7	260.6	279.6	675.1	1,068.4	862.1	806.9	1,969.6	2,798.1	3,413.8	1,400.1
37	0.4	0.4	-	-	1.7	-	8.3	1.8	4.1	4.9	- 15.3	4.2	2.4	2.8
38	158.7	154.1	52.6	240.9	383.1	50.7	-	22.0	30.0	21.0	300.0	120.0	70.4	1,523.0
Line 1 + 35	5,670.0	4,851.1	7,260.1	6,721.3	7,907.4	16,945.1	24,267.6	25,019.7	16,611.3	30,155.4	50,437.8	69,596.8	51,164.2	66,907.1

FUNDS RAISED BY NON-FINANCIAL SECTOR THROUGH FINANCIAL INSTITUTIONS

(Millions of Baht)

Line	1967	1968	1969	1970	1971	1972	1973	1974	1975	1976	1977	1978	1979	1980	1981E	1982E	1983E	1984E
1 Total Funds Raised (Excluded Share Capital)	6,466.5	5,761.3	8,173.0	7,855.2	8,847.3	18,427.1	25,665.6	28,271.2	18,732.5	32,701.6	43,417.5	73,299.6	57,242.2	66,281.8	90,161.4	106,982.2	198,804.2	139,008.2
2 Private Sector	3,612.0	3,649.2	4,263.5	5,691.3	3,805.1	5,063.8	16,782.1	19,620.1	18,076.4	17,476.0	37,980.8	56,667.7	43,793.4	41,016.3	78,756.5	61,992.7	145,134.6	105,665.7
3 Household	1,192.5	1,441.1	1,868.2	1,147.0	2,056.0	2,125.4	2,881.8	4,330.2	8,601.9	8,053.8	25,119.1	20,414.9	16,127.6	17,270.4	37,938.1	28,999.1	73,450.6	51,464.5
4 - Currency	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
6 - Short-term loans	665.8	1,066.4	1,502.1	970.9	1,617.8	1,567.3	2,775.0	3,138.6	7,028.7	4,335.5	10,366.8	12,139.3	10,845.9	2,042.0	5,383.3	7,428.5	14,483.6	8,198.3
7 - Long-term loans	211.0	361.3	383.2	255.2	231.2	312.2	292.7	612.8	1,381.6	1,864.1	11,760.1	4,432.1	561.2	6,888.3	8,319.6	7,085.5	13,534.1	16,120.5
8 - Commercial bills	-	-	-	-	-	-	-	-	-	-	-3.4	775.8	40.7	529.3	2,322.4	1,195.2	4,099.9	2,062.0
9 - Mortgages	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
10 - Others	315.7	13.4	-16.1	-79.1	207.0	245.9	653.3	550.5	-8.6	1,381.3	1,795.6	1,726.3	2,434.8	5,872.3	20,987.7	12,949.1	41,369.0	25,016.2
11 Business	2,419.5	2,208.1	2,394.3	4,544.3	1,749.1	2,938.4	12,900.3	15,289.9	9,474.5	9,422.2	12,861.7	36,252.8	27,685.8	23,745.9	40,818.4	32,993.6	71,684.0	54,221.2
13 - Short-term loans	1,313.7	1,186.8	1,740.7	2,929.3	465.0	607.5	5,704.5	8,527.2	4,270.1	4,985.3	5,253.4	21,289.4	13,680.9	12,175.6	15,270.3	19,215.3	19,215.3	30,680.9
14 - Long-term loans	75.2	27.4	141.3	100.2	100.2	146.3	344.2	424.7	387.1	2,629.4	6,057.9	2,713.5	5,490.7	6,410.9	2,584.3	4,000.6	7,600.9	7,600.9
15 - Commercial bills	991.1	902.2	467.0	1,390.4	1,057.5	2,086.8	6,733.9	5,534.3	3,746.3	3,407.6	6,115.9	7,621.3	8,672.9	4,859.8	14,791.5	8,505.8	28,412.1	19,038.9
16 - Others	39.5	91.7	45.3	124.4	126.4	97.8	404.4	884.2	1,033.4	642.2	-1,137.0	1,284.2	2,618.5	1,219.8	4,345.7	2,688.7	8,590.4	5,194.7
17 Central Government	926.5	1,509.4	4,347.7	3,938.3	4,937.9	9,396.8	4,565.2	-1,311.1	2,103.0	10,342.2	10,439.2	12,839.9	11,717.4	23,618.2	10,031.7	35,600.7	30,128.2	22,969.5
18 - Currency	-2.4	0.3	1.1	-0.6	0.6	-0.3	2.9	2.3	2.2	-4.8	0.6	-2.3	3.5	1.1	n.a.	n.a.	n.a.	n.a.
19 - Deposit	97.0	11.2	30.6	117.0	81.7	444.0	133.0	145.2	450.6	918.6	-1.2	1,066.2	-88.0	8,904.2	-4,475.7	10,567.9	-76.2	-2,640.2
20 - Public authorities securities	787.9	1,548.6	4,328.3	3,752.1	4,921.4	8,897.0	4,477.6	-1,365.1	1,709.7	9,393.8	10,332.0	11,974.8	11,099.1	16,782.0	14,357.8	25,068.3	30,526.9	25,378.7
21 - Short-term loans	21.6	-25.2	12.1	-9.5	14.5	3.2	28.6	-45.7	22.6	89.3	140.8	-217.2	135.5	23.7	149.4	-156.9	-116.0	139.6
22 - Long-term loans	2.0	-0.8	1.7	40.3	-55.4	-15.7	-77.3	56.8	13.6	3.3	-5.1	-2.1	422.3	1.1	n.a.	n.a.	n.a.	n.a.
- Commercial bills	-	-	-	-	-	-	-	-	-	-	29.9	-25.4	33.8	-74.2	78.7	170.0	-51.3	184.3
- Others	20.4	-24.7	-26.1	39.0	-24.9	68.6	0.4	-84.6	-95.7	-58.5	-57.8	45.9	11.2	-21.7	-78.5	-48.6	-155.2	-93.9
23 Local Government	-8.2	-	-8.8	4.6	18.2	0.1	-1.1	15.0	-14.4	-6.9	7.1	27.0	-32.3	0.6	61.5	-5.9	118.3	125.4
24 - Public authorities services	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
25 - Short-term loans	8.2	-	-8.8	4.6	18.2	0.1	-1.1	15.0	-14.4	-5.9	7.1	27.0	-32.3	0.6	61.5	-5.9	118.3	125.4
26 - Long-term loans	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
27 - Others	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
28 Public Enterprise	156.7	-43.2	19.4	-24.7	101.0	-100.3	241.2	160.8	164.7	1,803.8	939.2	787.0	788.1	5,585.0	14,863.2	8,258.7	24,680.5	21,454.9
29 - Public authorities securities	83.8	42.0	16.8	-16.0	-16.0	6.4	208.4	149.2	172.0	984.0	-34.4	-246.0	-15.4	-140.8	n.a.	n.a.	n.a.	n.a.
30 - Short-term loans	72.9	-85.2	2.6	-8.7	117.0	-106.7	-24.3	68.3	-10.4	691.7	750.3	1,261.0	783.9	1,805.6	801.4	-441.5	-3,136.2	4,646.0
31 - Long-term loans	-	-	-	-	-	-	57.0	-57.0	3.0	127.9	212.1	-18.1	29.5	-42.4	n.a.	n.a.	n.a.	n.a.
32 - Others	-	-	-	-	-	-	0.1	0.3	0.1	0.2	11.2	-209.9	-9.9	3,944.6	14,061.8	8,700.2	27,796.7	16,808.9
33 Rest of the World	1,779.5	645.9	-448.8	-1,754.3	-14.9	4,066.7	4,078.2	9,788.4	-1,597.2	3,085.5	51.2	2,978.0	975.6	-3,918.3	-13,551.5	1,136.2	-1,237.0	-11,227.3
34 - International reserve position	1,773.9	646.6	-445.2	-1,743.5	-15.4	4,066.8	4,077.0	9,780.5	-1,600.9	3,093.2	49.4	2,985.5	979.2	-3,922.0	-13,551.5	1,136.2	-1,237.4	-11,227.3
35 - Foreign debts and claims	5.6	-0.7	-3.6	-10.8	0.5	-0.1	1.3	6.1	3.4	-7.7	1.8	-7.5	-3.6	3.7	n.a.	n.a.	n.a.	n.a.
36 - Others	-	-	-	-	-	-	-0.1	-0.2	0.3	-	-	-	-	-	-	-	-	-
37 Share Capital	-1.0	-	0.7	3.5	6.0	422.3	19.8	31.5	115.5	21.5	136.3	886.3	261.7	-621.8	661.8	1,631.7	2,321.1	1,909.1
38 - Business	-1.0	-	0.7	3.5	6.0	422.3	19.8	31.5	115.5	21.5	136.3	886.3	261.7	-621.8	661.8	1,631.7	2,321.1	1,909.1
Line 1 + 37	6,465.5	5,751.3	8,173.7	7,855.2	8,847.3	18,427.1	25,665.6	28,271.2	18,732.5	32,701.6	43,417.5	73,299.6	57,242.2	66,281.8	90,161.4	106,982.2	198,804.2	139,008.2

Table 4.1
TOTAL FUNDS RAISED BY NON-FINANCIAL SECTOR

Line	1967	1968	1969	1970	1971	1972	1973	1974	1975	1976	1977	1978	1979	1980
(Millions of Baht)														
1 Total Funds Raised (Excluded Share Capital)	14,336.1	15,901.4	20,285.7	19,619.5	22,766.7	33,292.8	45,742.8	53,390.0	45,016.4	59,435.2	81,051.4	122,732.4	123,114.3	176,045.8
2 Private Sector	7,212.8	8,561.8	9,542.0	11,007.5	10,267.2	13,287.7	23,998.8	34,637.0	31,657.0	29,202.0	52,717.5	72,742.6	69,206.3	92,722.2
3 Household	957.2	1,117.3	1,617.5	795.8	1,881.4	2,254.0	4,340.9	5,001.2	9,107.1	8,320.2	25,047.2	21,155.0	21,870.7	18,001.2
4 Short-term loans	665.8	1,066.4	1,502.1	970.9	1,617.8	1,567.3	2,775.0	3,138.6	7,028.7	4,335.5	10,366.8	12,139.3	10,845.9	1,945.5
5 Long-term loans	211.0	361.3	383.2	312.2	292.7	312.2	292.7	612.8	1,381.6	1,864.3	11,760.1	4,432.1	561.2	6,888.3
6 Mortgages	9.3	34.7	27.3	-5.8	-18.7	-50.7	115.8	40.3	222.2	278.7	1,000.0	1,321.2	2,245.0	1,938.5
7 Others	71.1	-345.1	-285.1	-424.5	51.1	425.2	1,151.9	1,209.6	465.1	1,630.7	1,733.5	3,946.1	8,001.9	7,228.9
8 Business	5,255.6	7,544.5	8,024.5	10,211.7	8,385.8	11,033.7	19,657.9	29,635.8	22,549.7	20,882.7	27,670.3	50,877.6	47,535.6	74,721.0
9 Short-term loans	1,313.7	1,186.8	1,740.7	2,929.3	465.0	607.5	5,704.5	8,527.2	4,270.1	4,985.3	5,253.4	21,289.4	13,680.9	12,156.1
10 Long-term loans	75.2	27.4	141.3	100.2	146.3	146.3	57.5	344.2	424.7	367.1	2,629.4	6,057.9	2,713.5	5,490.7
11 Commercial bills	991.1	902.2	467.0	1,390.4	1,057.5	2,086.8	6,733.9	5,534.3	3,746.3	3,407.6	6,115.9	7,621.3	9,196.5	4,468.9
12 Foreign debts & claims	3,516.7	4,936.0	5,415.8	5,503.8	6,118.4	7,834.2	5,887.7	12,319.9	12,309.1	10,205.4	14,336.7	13,063.1	23,049.0	48,054.8
13 Other	358.9	492.1	259.7	288.0	644.7	358.9	1,264.3	2,910.2	1,799.7	1,897.3	-665.1	2,845.9	-1,103.8	4,550.5
14 Central Government Sector	2,734.1	2,614.8	5,900.3	5,629.2	6,891.0	9,821.7	8,091.9	-898.8	3,474.0	12,923.1	13,057.7	17,814.9	20,458.1	32,979.3
15 Securities	803.8	1,718.2	4,405.4	3,834.9	4,921.0	9,152.6	4,709.6	-1,461.5	2,612.8	9,862.9	10,794.8	12,422.7	11,581.1	19,214.7
16 Foreign debts & claims	564.2	781.5	797.9	481.6	389.4	345.7	711.2	339.0	210.8	643.0	1,441.7	4,364.0	10,391.6	7,563.5
17 Other	1,566.1	115.1	697.0	1,312.7	1,580.6	323.4	2,671.1	223.7	650.4	2,417.2	851.2	1,028.2	-1,514.6	7,201.1
18 Local Government Sector	67.9	53.5	77.3	116.7	160.3	47.9	135.1	222.5	189.2	348.1	220.2	-289.4	2.3	255.0
19 Other	67.9	53.5	77.3	116.7	160.3	47.9	135.1	222.5	189.2	348.1	220.2	-289.4	2.3	255.0
20 State Enterprises Sector	555.0	946.3	1,344.8	445.9	1,612.1	1,403.8	3,108.0	4,924.8	4,902.3	7,280.0	8,300.9	12,800.1	17,240.2	25,473.1
21 Short-term loans	72.9	-85.2	2.6	-8.7	117.0	-106.7	-18.5	65.7	-13.0	691.8	750.4	1,261.1	901.0	1,751.0
22 Long-term loans	136.2	83.8	166.2	463.9	557.4	394.4	649.8	-11.0	323.9	127.9	212.1	6.9	65.1	51.9
23 Foreign debts & claims	290.7	369.9	554.6	632.7	500.8	856.9	997.1	1,573.8	2,452.4	4,136.7	5,018.3	7,660.7	13,862.5	19,543.8
24 Other	55.2	577.8	621.4	-642.0	436.9	259.2	1,479.6	3,296.3	2,139.0	2,323.6	2,320.1	3,871.4	2,391.6	4,126.4
25 Rest of the World Sector	3,766.3	3,625.0	3,321.3	2,420.2	3,836.1	8,731.5	10,409.0	14,504.5	4,793.9	9,681.1	6,689.1	19,664.2	16,207.4	24,616.2
26 Foreign debts & claims	2,086.7	2,713.0	3,632.0	4,131.2	4,110.9	4,322.9	5,871.8	4,824.5	5,843.9	6,467.1	6,513.1	16,479.3	15,228.2	28,536.2
27 International reserve position	1,679.6	912.0	-310.7	-1,111.0	-274.8	4,408.6	4,537.2	9,680.0	-1,050.0	3,214.0	176.0	3,184.9	979.2	-3,922.0
28 Share Capital	3,217.5	2,563.8	3,763.6	4,507.2	3,180.0	5,426.4	9,736.0	8,761.7	3,487.5	4,460.4	5,837.9	12,988.0	17,153.7	9,986.9
29 Private sector	2,337.2	1,905.1	3,004.5	3,503.9	2,923.1	4,953.0	6,274.6	8,203.3	2,349.7	3,529.9	4,613.3	9,292.7	13,641.6	5,999.5
30 Central Government														
31 Local Government														
32 State Enterprises	880.3	658.8	759.1	1,003.3	256.9	473.4	1,461.4	556.4	1,137.8	930.5	1,224.5	3,695.3	3,512.1	3,987.4
33 Rest of the World														
34 Total Funds Raised & Share Capital	17,553.6	18,485.3	24,049.3	24,126.7	25,946.7	36,719.0	55,478.8	62,151.7	48,503.9	63,895.6	86,853.3	135,720.4	140,268.0	186,032.7

Table 5
TRANSACTIONS IN THE STOCK EXCHANGE OF THAILAND
(Millions of Baht)

Year	Total	Government securities	Corporated Securities
1975	1,522.9	963.4	559.5
1976	3,204.8	1,651.7	1,553.1
1977	26,591.3	310.2	26,281.1
1978	57,272.4	206.6	57,065.8
1979	22,533.1	82.6	22,450.5
1980	6,559.1	10.0	6,549.1
1981	2,897.7	376.5	2,521.2
1982	5,965.5	87.7	5,877.8
1983	9,323.9	203.4	9,120.5
1984	10,870.6	275.4	10,595.2
1985 (Mar.)	4,575.3	104.8	4,470.5

Table 6

FINANCIAL INTERMEDIATION RATIO IN THAILAND

<u>Funds Raised by non-Financial Units*</u>				
<u>Year</u>	<u>Total</u>	<u>From Financial Institutions (Indirect Funds)</u>	<u>Financial Intermediation Ratio</u>	<u>Indirect Funds/ GDP</u>
	(1)	(2)	(2)/(1)	%
1967	17,554	6,466	.37	6.0
1968	18,465	5,751	.31	5.0
1969	24,049	8,174	.34	6.4
1970	24,127	7,856	.33	5.8
1971	25,947	8,853	.34	6.1
1972	38,719	19,849	.51	11.4
1973	55,479	25,685	.46	11.9
1974	62,152	28,303	.46	10.4
1975	48,504	18,848	.39	6.3
1976	63,896	38,723	.61	9.7
1977	86,853	49,554	.57	12.6
1978	135,720	74,186	.55	15.8
1979	140,268	57,504	.41	10.3
1980	186,032	65,660	.35	9.6

* In million bahts

Table 7

HOUSEHOLD SAVINGS AT FINANCIAL INSTITUTIONS: OUTSTANDING AMOUNTS^{1/}

(Millions of Baht)

Institutions	Definition of Savings	1971	1972	1973	1974	1975	1976	1977	1978	1979	1980	1981	1982	1983	1984
1. Commercial banks	Deposits	26,680.4	34,631.1	42,304.7	54,092.5	65,910.2	80,826.3	99,559.0	115,528.2	128,519.8	163,751.1	198,298.4	253,339.4	328,773.0	399,055.8
2. Finance companies	Promissory note etc.	679.4	1,853.9	3,177.0	6,275.0	7,306.5	9,865.4	14,030.9	22,332.0	23,031.9	29,309.0	38,024.8	49,814.2	54,050.7	48,551.9
3. Life insurance Co.	Life insurance reserve	991.2	1,119.7	1,365.3	1,301.8	1,896.4	2,347.1	2,847.1	3,506.7	4,282.4	5,403.9	6,924.8	8,793.3	11,109.1	13,553.7
4. Agricultural cooperatives	Deposits & capital funds	387.9	343.5	453.0	614.7	742.2	934.7	1,027.8	1,263.3	1,447.8	1,637.0	1,835.4	2,128.2	(2,228.2)	(2,428.2)
5. Savings	Deposits &	386.4	808.6	960.9	1,144.6	1,360.6	1,408.6	1,728.1	2,136.3	2,829.9	3,696.5	4,714.9	6,042.0	7,794.8	(10,055.2)
6. Pawnshops		-	-	-	-	-	-	-	-	-	-	-	-	-	-
7. Credit	Note payable	n.a.	n.a.	288.0	524.0	504.0	468.2	557.4	1,014.1	1,348.3	1,981.6	2,808.0	2,026.0	1,973.4*	1,322.5*
3. Government Savings Banks	Deposits savings Certificates etc.	6,181.2	7,507.1	9,472.2	10,504.8	10,834.9	12,943.5	15,543.1	16,986.7	20,830.6	24,132.4	26,833.2	31,854.0	39,040.0	45,866.6
9. BAAC	Deposits	143.6	196.6	274.3	381.7	571.4	586.2	606.9	812.9	1,105.1	1,271.3	1,262.4	1,543.5	1,797.32/	1,984.42/
10. Industrial Finance Corp. of Thailand		-	-	-	-	-	-	-	-	-	-	-	-	-	-
11. Government Housing Bank	Deposits	-	-	88.8	132.4	180.7	381.5	449.7	554.3	735.9	1,558.3	1,555.2	1,834.8	1,725.1	5,178.1
12. Small Industrial Finance Office 2/		-	-	-	-	-	-	-	-	-	-	-	-	-	-
Total		35,750.1	46,260.5	58,384.7	75,271.5	89,295.7	109,657.1	136,380.0	164,174.5	184,140.7	232,750.0	283,057.1	357,175.4	448,491.6	527,988.4

1/ See footnote under Table also

2/ As at the end of September

* 1983 No. of Companies 30 Companies

* 1984 " " 26

Table 7.1

HOUSEHOLD SAVINGS AT FINANCIAL INSTITUTIONS IN THAILAND
(As percentage share of total)

Institutions	Definition of Savings	1971	1972	1973	1974	1975	1976	1977	1978	1979	1980	1981	1982	1983	1984
1. Commercial banks	Deposits	74.63% (21.63%)	74.86% (29.80%)	72.48% (22.16%)	71.86% (27.86%)	73.81% (21.85%)	73.71% (22.63%)	73.00% (23.18%)	70.37% (16.04%)	69.79% (11.25%)	70.36% (27.42%)	70.05% (21.09%)	70.93% (27.76%)	73.31% (29.78%)	75.58% (21.38%)
2. Finance companies	Promissory note, etc.	1.90% (156.67%)	3.58% (143.44%)	5.44% (92.09%)	8.34% (97.51%)	8.18% (16.44%)	9.00% (35.03%)	10.29% (42.22%)	13.60% (59.16%)	12.51% (3.13%)	12.59% (27.25%)	13.72% (32.47%)	13.95% (28.31%)	12.05% (8.50%)	9.19% (-10.17%)
3. Life insurance co.	Life Insurance reserve	2.77% (13.19%)	2.42% (12.96%)	2.34% (21.93%)	2.13% (17.32%)	2.12% (18.39%)	2.14% (23.80%)	2.09% (21.27%)	2.14% (23.17%)	2.32% (22.13%)	2.32% (26.19%)	2.45% (28.14%)	2.46% (26.98%)	2.48% (26.34%)	2.57% (22.01%)
4. Agricultural cooperatives	Deposits & capital funds	1.09% (21.14%)	0.74% (-11.45%)	0.78% (31.88%)	0.82% (35.70%)	0.83% (20.74%)	0.76% (11.46%)	0.75% (23.13%)	0.77% (22.91%)	0.79% (14.60%)	0.70% (13.13%)	0.65% (12.06%)	0.59% (15.95%)	0.50% (4.70%)	0.46% (8.98%)
5. Savings cooperatives	Deposits & capital funds	1.92% (18.06%)	1.75% (17.80%)	1.65% (18.84%)	1.52% (19.12%)	1.53% (18.67%)	1.28% (3.53%)	1.27% (22.68%)	1.34% (27.09%)	1.54% (28.85%)	1.59% (30.62%)	1.67% (27.55%)	1.69% (28.15%)	1.74% (29.01%)	1.90% (29.00%)
6. Pawnshops		-	-	-	-	-	-	-	-	-	-	-	-	-	-
7. Credit for- ier companies	Note payable	-	-	0.49% (81.94%)	0.70% (-3.82%)	0.57% (-7.10%)	0.43% (27.60%)	0.44% (27.60%)	0.62% (69.75%)	0.73% (32.96%)	0.85% (46.97%)	0.99% (41.70%)	0.57% (-27.85%)	0.44% (-2.60%)	0.25% (-32.98%)
8. Government Savings	Deposits, savings certi- ficate etc.	17.29% (9.27%)	16.23% (21.45%)	16.22% (26.18%)	13.95% (10.90%)	12.14% (3.14%)	11.81% (11.51%)	11.30% (20.04%)	10.33% (9.16%)	11.32% (22.83%)	10.37% (15.80%)	9.48% (11.19%)	8.92% (18.71%)	8.70% (22.56%)	8.69% (17.46%)
9. BAAC	Deposits	0.40% (36.69%)	0.42% (36.91%)	0.47% (39.78%)	0.51% (39.90%)	0.64% (49.70%)	0.54% (4.34%)	0.44% (1.79%)	0.49% (33.94%)	0.60% (35.95%)	0.55% (15.04%)	0.44% (-0.70%)	0.43% (22.27%)	0.40% (16.44%)	0.38% (10.41%)
10. Industrial Finance Corp. of Thailand		-	-	-	-	-	-	-	-	-	-	-	-	-	-
11. Government Housing Bank	Deposits	-	-	0.15% (49.10%)	0.17% (21.37%)	0.18% (127.19%)	0.33% (24.40%)	0.33% (24.40%)	0.34% (23.26%)	0.40% (32.76%)	0.67% (111.46%)	0.55% (-0.07%)	0.46% (5.12%)	0.36% (5.52%)	0.98% (200.16%)
12. Small Indus- trial Finance Office		-	-	-	-	-	-	-	-	-	-	-	-	-	-
Total		100.00	100.00	100.00	100.00	100.00	100.00	100.00	100.00	100.00	100.00	100.00	100.00	100.00	100.00

Note: Figures in parentheses are annual growth rates.

Table 7.2

FINANCIAL INSTITUTIONS IN THAILAND: SHARE IN SAVINGS MOBILISATION AND LENDING

Institutions	No. of Firms	No. of Branches (1984)	Savings Mobilisation			Lending		Other Services
			Share	Average Size (Thousand of Baht)	Instruments	Share	Average Size	
1. Commercial Bank	14 foreign banks and 16 Thai banks	1,739	75.6	24.0	deposits	74.7	-	1. Foreign exchange 2. Guarantee 3. Selling and purchasing government securities
2. Finance Companies	104	31	9.2	652.5	Promissory notes	14.9	-	1. Securities business dealer, broker, underwriter, investment consultant 2. Hire purchasing
3. Government Saving Bank	1	436	8.7	-	Deposits	0.2	-	-
4. Bank for Agriculture and Agricultural Cooperative	1	67	0.4	-	Deposits	3.1	-	-
5. Government Housing Bank	1	-	1.0	-	Deposits	1.6	-	-
6. Credit Foncier Companies	26	-	0.2	644.2	Promissory Notes	0.5	-	-
7. Industrial Finance Corporation of Thailand	1	3	-	-	Bond and debenture	1.0	-	1. Investing in equities 2. Guarantee
8. Agricultural Cooperative	1,031	-	0.4	-	Deposits and subscriptions to capital accounts	0.8	-	-

Table 7.2 (cont'd)

FINANCIAL INSTITUTIONS IN THAILAND: SHARE IN SAVINGS MOBILISATION AND LENDING

Institutions	No. of Firms	No. of Branches (1984)	Savings Mobilisation		Lending		Other Services
			Share	Average Size (Thousand of Baht)	Instruments	Share	
9. Savings Cooperatives	574	-	1.9	-	Deposits and subscriptions to capital accounts	1.7	-
10. Life insurance	12	639	2.6	-	Insurance policy	1.0	-
11. Paumshop	330	-	-	-	-	0.5	-
12. Small Industrial Finance Office	1	-	-	-	-	0.01	-
Total	2,112	2,915	-	-	-	100.0	-

Table 8

CREDIT EXTENDED BY FINANCIAL INSTITUTIONS : OUTSTANDING AMOUNTS

(In Million Baht)

Institution	1971	1972	1973	1974	1975	1976	1977	1978	1979	1980	1981	1982	1983	1984
Commercial Banks	31,564.3	35,652.6	51,184.2	57,678.5	81,302.3	95,145.4	121,768.7	158,600.0	195,072.4	218,931.2	254,449.6	299,760.1	401,648.2	474,993.2
Finance Companies	2,266.9	6,153.9	10,055.7	16,199.1	20,493.7	25,227.1	33,652.7	49,127.9	47,570.2	54,977.6	55,389.6	79,515.0	90,711.1	95,029.6
Life Insurance Companies	513.6	575.9	597.5	815.6	933.1	1,183.0	1,323.0	1,445.6	2,062.4	2,697.9	3,261.9	4,062.9	(5,080.6)	6,258.4
Agricultural Cooperatives	912.2	731.5	957.1	1,234.1	1,899.6	2,276.5	2,913.5	3,522.4	3,639.2	3,877.0	4,169.7	4,536.3	(4,836.3)	(5,136.3)
Saving Cooperatives	625.1	735.0	887.6	1,107.1	1,327.3	1,623.1	1,955.6	2,489.8	3,165.1	4,038.5	5,196.7	(6,678.7)	8,615.5	(10,978.7)
Postshop	577.5	629.0	758.9	1,147.2	1,222.9	1,324.1	1,431.6	1,758.9	2,436.6	2,798.0	3,138.0	(3,162.5)	(3,283.0)	(3,508.5)
Credit Foncier Companies	114.6	90.0	334.4	559.5	634.8	603.1	919.0	1,359.0	1,370.0	2,419.2	2,931.2	(3,535.4)	3,630.0	(2,962.5)
Government Savings Bank	400.8	373.4	323.5	323.9	329.1	458.5	666.8	657.7	1,140.7	1,121.8	2,094.2	(2,049.9)	3,285.0	1,228.2
SAC	1,439.5	1,736.9	1,952.1	2,650.7	4,714.8	6,778.4	8,521.8	9,703.3	10,943.5	12,464.4	14,142.0	15,741.4	17,117.9	19,608.3
Industrial Finance Corp.														
of Thailand	484.0	585.4	601.1	912.8	1,333.1	1,663.2	1,648.0	1,903.8	2,480.6	3,339.6	4,300.9	4,700.5	4,919.5	6,094.8
Government Housing Bank 1/	149.4	124.9	32.6	83.6	311.1	890.3	1,679.9	2,669.3	4,300.1	8,122.9	9,410.9	9,469.9	9,285.7	10,084.5
Small Industrial Finance 2/														
Office	75.3	75.5	76.0	56.6	76.1	65.3	111.5	127.7	128.6	103.4	74.6	56.2	44.0	40.8
Total	39,003.1	47,468.9	57,770.6	92,781.7	114,577.9	137,238.0	176,590.1	232,345.4	275,586.4	314,361.4	369,659.3	433,265.8	552,466.8	635,923.8

1/ During 1969 - 1973 the outstanding amounts are as at the end of September

2/ During 1969 - 1975 the outstanding amounts are as at the end of September

Table 8.1

CREDIT EXTENDED BY FINANCIAL INSTITUTIONS IN THAILAND
(As Percentage Share of Total)

Institutions	1971	1972	1973	1974	1975	1976	1977	1978	1979	1980	1981	1982	1983	1984
1. Commercial banks	80.93% (12.57%)	75.11% (12.95%)	75.52% (43.56%)	72.94% (32.22%)	70.96% (20.13%)	69.33% (17.03%)	68.96% (27.98%)	68.26% (30.25%)	70.78% (23.00%)	69.53% (12.23%)	69.02% (16.22%)	69.19% (17.81%)	72.70% (33.99%)	74.69% (18.26%)
2. Finance companies	5.81% (143.78%)	12.97% (171.69%)	14.84% (63.27%)	17.46% (61.05%)	17.89% (26.51%)	18.38% (23.10%)	19.06% (33.40%)	20.72% (43.01%)	17.26% (-1.16%)	17.46% (15.57%)	17.74% (18.94%)	18.35% (21.60%)	16.43% (14.08%)	14.94% (4.76%)
3. Life insurance companies	1.32% (11.87%)	1.21% (12.13%)	1.03% (21.11%)	0.88% (16.93%)	0.81% (14.41%)	0.85% (24.64%)	0.75% (13.76%)	0.62% (9.27%)	0.75% (42.67%)	0.86% (30.81%)	0.91% (24.62%)	0.94% (20.85%)	0.92% (25.29%)	0.98% (22.94%)
4. Agricultural cooperatives	2.08% (24.32%)	1.54% (-9.93%)	1.28% (18.54%)	1.33% (42.32%)	1.66% (53.93%)	1.66% (38.20%)	1.65% (41.75%)	1.52% (29.82%)	1.40% (14.81%)	1.23% (0.98%)	1.13% (7.55%)	1.05% (8.79%)	0.88% (6.61%)	0.81% (6.29%)
5. Savings cooperatives	1.60% (17.39%)	1.55% (17.58%)	1.31% (20.76%)	1.19% (24.73%)	1.16% (19.89%)	1.18% (22.28%)	1.11% (20.48%)	1.06% (26.59%)	1.15% (34.42%)	1.28% (27.59%)	1.41% (28.68%)	1.54% (28.52%)	1.56% (29.00%)	1.73% (27.43%)
6. Pawnshops	1.48% (7.46%)	1.33% (8.92%)	1.12% (20.63%)	1.24% (51.19%)	1.07% (6.60%)	0.96% (8.28%)	0.81% (8.12%)	0.76% (22.86%)	0.88% (38.53%)	0.89% (14.83%)	0.85% (12.15%)	0.73% (0.76%)	0.59% (3.81%)	0.55% (6.87%)
7. Credit financier companies	0.30% (-21.46%)	0.19% (-21.46%)	0.49% (271.55%)	0.60% (67.31%)	0.55% (13.46%)	0.45% (3.75%)	0.52% (37.72%)	0.56% (49.83%)	0.68% (37.53%)	0.77% (29.37%)	0.79% (21.16%)	0.82% (20.61%)	0.66% (2.68%)	0.47% (-18.39%)
8. Government Savings Bank	1.03% (-4.41%)	0.78% (-6.84%)	0.48% (-13.36%)	0.35% (1.05%)	0.29% (0.67%)	0.33% (39.32%)	0.38% (45.43%)	0.28% (-1.36%)	0.41% (73.44%)	0.36% (-1.66%)	0.57% (86.68%)	0.47% (-2.12%)	0.59% (40.25%)	0.19% (-62.61%)
9. BRAC	3.69% (19.09%)	3.66% (20.85%)	2.88% (12.40%)	2.86% (35.79%)	4.11% (77.87%)	4.94% (43.77%)	4.83% (25.62%)	4.18% (13.86%)	3.97% (12.76%)	3.96% (13.90%)	3.84% (13.46%)	3.63% (11.31%)	3.10% (8.74%)	3.08% (14.55%)
10. Industrial Finance Corp. of Thailand	1.19% (24.97%)	1.24% (26.16%)	0.89% (2.68%)	0.99% (51.85%)	1.16% (46.04%)	1.21% (24.76%)	0.93% (-1.03%)	0.82% (15.66%)	0.89% (29.25%)	1.05% (34.50%)	1.17% (29.95%)	1.08% (9.29%)	0.89% (4.66%)	0.96% (23.89%)
11. Government Housing Bank	0.38% (-11.07%)	0.26% (-16.40%)	0.05% (-73.90%)	0.09% (156.44%)	0.27% (272.13%)	0.65% (187.46%)	0.95% (89.34%)	1.15% (58.43%)	1.78% (82.66%)	2.58% (65.77%)	2.55% (15.86%)	2.19% (0.63%)	1.68% (1.95%)	1.59% (8.60%)
12. Small Industrial Finance Office	0.19% (3.72%)	0.16% (0.27%)	0.11% (0.66%)	0.07% (-12.37%)	0.07% (14.26%)	0.06% (17.08%)	0.06% (25.14%)	0.05% (14.53%)	0.05% (0.70%)	0.03% (19.60%)	0.02% (-27.85%)	0.01% (-24.66%)	0.01% (-21.71%)	0.01% (-7.27%)
Total	100.00	100.00	100.00	100.00	100.00	100.00	100.00	100.00	100.00	100.00	100.00	100.00	100.00	100.00

Notes: Figures in parentheses are annual growth rates.

Table 9

INSTRUMENTS OF MONETARY CONTROL

Institution	Government Authorities	Statutory Power Conferred by	Monetary Instruments (as at December 1984)
Commercial banks	Bank of Thailand Ministry of Finance	1) Commercial Banking Act 1962 and 1979 (revised) 2) Bank of Thailand Act 3) Currency Act	1) Cash reserves ratio = 7% of total deposits of which:- - balance at BOT: not less than 2% - cash in hand: not exceed 2.5% - government securities 2.5% 2) Capital to Risk assets ratio = 8.0% 3) Capital to the aggregate sum of its avail to bills, issuing of L/C and etc. = not less than 20% 4) Proportion of any one borrower: not avail to bills, accepting bills, issuing of L/C and etc. to any one person = not more than 50% of capital fund 5) Proportion of loans to any one borrower: not more than 25% of capital funds 6) Specified assets to capital ratio = not being exercised

Table 9 (cont'd)

INSTRUMENTS OF MONETARY CONTROL

Institution	Government Authorities	Statutory Power Conferred by	Monetary Instruments (as at December 1984)
			7) Maximum interest rates on deposits and loans
			Demand deposits -
			Savings deposits %
			Time deposits
			Less than 3 months
			3 months - less than
			2 years - 13%
			2 years and over - 14%
			Foreign currency deposits - floating rates
			Loans 19%
			8) Examination of Commercial bank accounts
			9) Selective Credit Control
			10) Exchange rate
			11) Rediscounting facilities
			12) Conditions for bank branching
			13) Moral suasion

Table 9 (cont'd)

INSTRUMENTS OF MONETARY CONTROL

Institution	Government Authorities	Statutory Power Conferred by	Monetary Instruments (as at December 1984)
Finance companies	Bank of Thailand and Ministry of Finance	1) National Execu- tive Council Decree (No.58) 2) The Finance Securities and and Credit Foncier Business	1) Liquidity ratio = 7% of total borrowings, of which:- - Balance at BOT: not less than 0.5% - Unobligated government securities: not less than 5.5% - Deposit at & call loan to domestic banks: not more than 1.0% 2) Risk assets to capital ratio Capital ----- not less than 6% Risk assets 3) Ratio of Capital to the aggregate sum of its avail to bills and accepts bills: not less than 25% 4) Minimum registered capital which has been fully paid up = 60 million baht 5) Minimum amount for P/N Bangkok 10,000 baht Other Provinces 5,000 baht 6) Maximum amount of loans to any one person = no more than 30% of capital funds as from May 1, 1983

Table 9 (cont'd)

INSTRUMENTS OF MONETARY CONTROL

Institution	Government Authorities	Statutory Power Conferred by	Monetary Instruments (as at December 1984)
			7) Examination of finance company accounts
			8) Terms and conditions of car hire-purchase finance - minimum amount for down- payments = 30% of a car's prices - maximum period for term- payment = 42 months
			9) Maximum amount of loans for specific purpose - no more than 5% of capital funds for car hire-purchase
			10) Selective credit control
			11) Maximum interest rates on loan: not exceed 21% p.a. as from March 5, 1984 Maximum service charge = not being exercised
			12) Maximum interest rate on P/11 = not exceed 16% p.a.
			13) Moral suasion

Table 9 (cont'd)

INSTRUMENTS OF MONETARY CONTROL

Institution	Government Authorities	Statutory Power Conferred by	Monetary Instruments (as at December 1984)
Government Savings Bank	Ministry of Finance	Government Savings Bank Act 1946	1) Maximum interest rate on loans: not exceed 19% p.a. 2) Interest rates on deposits Demand deposit 9% Time deposits 6 months 11% 12 months - 2 years 12.5% 2 years and over 13.5% Savings bonds 4%, 6%
	Ministry of Finance and of Thailand	Informal Consultation on budget formulation	3) Deficits financed by the Government savings Bank
Bank for Agriculture and Agricultural Cooperatives. (BAAC)	Ministry of Finance	Bank for Agriculture and Agricultural Cooperatives Act 1966	1) Interest rates on deposits:- Demand deposit 9% Time deposits 3 deposits 11% 6 months 12% 1 year 12.5% 2 year and over 13.5% 2) Maximum interest rates on loan: not exceed 19% p.a.
	Bank of Thailand BAAC Commercial Banks	Informal consultations and co-operations between the three agencies	3) Channelling credits to agricultural sector through the BAAC

Table 9 (cont'd)

INSTRUMENTS OF MONETARY CONTROL

Institution	Government Authorities	Statutory Power Conferred by	Monetary Instruments (as at December 1984)
Life insurance companies	Ministry of Commerce	Life Insurance —	1) Minimum capital = 5 million baht 2) Liquid asset requirements for security purpose = 2 million baht 3) Conditions for branching 4) Policy Reserves deductible from premiums paid (25% of reserves deposited with the Registrar) 5) Stipulated channels of investment - Government bonds - Bonds guaranteed by the Ministry of Finance Max. 25% 6) Premium rates
Credit Fonciers	Bank of Thailand	1) National Execu- tive Council- Decree (No.58) 2) The Finance Securities and Credit Fonciers Business Act, 1979 amended by Emergency Decree, 1983	1) Minimum registered capital which has been fully paid up 30 million baht. 2) Minimum period of P/N = 3 years. 3) Maximum interest rate on P/N 16% p.a. 4) Maximum amount of loans to any one person = no more than 50% of capital funds

Table 9 (cont'd)

INSTRUMENTS OF MONETARY CONTROL

Institution	Government Authorities	Statutory Power Conferred by	Monetary Instruments (as at December 1984)
			5) Minimum amount of P/N = 1,000 baht 6) Liquidity ratio = not less than 5% of total borrowings of which:- - Balance at BOT; not less than 0.5% - Unobligated government securities: not less than 3.5% - Deposits at & call loans to domestic banks: not exceed 1.0% 7) Capital to risk assets ratio: Capital ----- = not less than 6% Risk assets 8) Maximum interest rate on loans = not exceed 21% p.a. 9) Maximum loans by pledging its own P/N = not more than 90% of their face values 10) Maximum unsecured call-loans to any commercial bank, GHB, FC and CF = not more than 20% of capital fund but total amount not exceed 100%

Table 9 (cont'd)

INSTRUMENTS OF MONETARY CONTROL

Institution	Government Authorities	Statutory Power Conferred by	Monetary Instruments (as at December 1984)
Government Housing Bank	Ministry of Finance	Government Hous- sing Bank Act*1953	1) Interest rates on deposits - same as commercial banks
		Revolutionary Party Decree No. 317, 1972	2) Maximum interest rates on loan: not exceed 19% p.a.
		Royal Decree Defining the Scopes and Opera- tions of the Government Housing Bank 1975	
	Bank of Thailand Government Commercial Banks National Housing Authority	Consultations and Cooperations	3) Channelling funds to housing sector
Private Pawn- shops	Police Depart- ment Ministry	Pawnshop Act 1962	1) Interest rates on loan Principal Interest rates ----- (Baht) (% per month) 1- 2,000 2.00 2,001 - 10,000 1.25 2) Account examination
Government- Pawnshops	Public Welfare Department Ministry of Interior	Pawnshop Act 1962	1) Interest rates on loan Principal Interest rates ----- (Baht) (% per month) 1 - 500 1.25 over 500 but less than 2,000 1.50 2,000 - 10,000 1.25 - 2.00 (2,000 2.00) (over 2,000 1.25) 2) Account examination

Table 9 (cont'd)

INSTRUMENTS OF MONETARY CONTROL

Institution	Government Authorities	Statutory Power Conferred by	Monetary Instruments (as at December 1984)
Municipal Pawnshops	Municipalities	Pawnshop Act 1962	1) Interest rates on loan: same as Government Pawnshops 2) Account examination
Industrial Finance Corporation of Thailand	Ministry of Finance	Industrial Finance Corporation of Thailand Act 1959	1) Maximum interest rate on loan: = not exceed 19% p.a. 2) Channelling funds to industrial sector esp. long-term capital (consultations & cooperations between Ministry of Finance, BOT, commercial banks & IFCT)
Agricultural and Savings Cooperatives	Ministry of Agriculture and Agricultural Cooperatives	Cooperatives Act 1968	1) Interest rate on deposits. Saving Deposits 8.5% - 10% Time Deposits 3 months 8.5% - 10% 6 months 8.5% - 11% 12 months-2 years 13.0%-13.5% 2) Interest rate on loans 12%-15% Channelling funds to the agricultural sector. (consultations & cooperations between Ministry of Agriculture and Agricultural Cooperatives, BOT, BAAC & Commercial banks)
Small Industry Finance Office	Ministry of Finance of Ministry of Industry	-	Channelling funds to small industrial establishments by using 1) budget appropriations 2) advances from Krung Thai Bank