

Chapter 5

Instrument-wise Structure of Flow of Capital Funds

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INSTRUMENT-WISE STRUCTURE OF FLOW OF CAPITAL FUNDS

5.0 The structure of total Flows can be looked at from the angle of relative shares of various financial instruments that constitute it. The approach will bring out the changes, if any, in the relative importance of instruments in the Flows. This analysis can be undertaken at two levels - at the level of the Aggregate Economy and at the sectoral level.

5.1 At the sectoral level the instrument-wise composition can be analysed for the Sources and Uses separately.

5.2 In this chapter an analysis of the instrument-wise structure of Capital Flows is taken up for a period of twenty years from 1956-57 to 1975-76. No doubt, the data is available for this type of analysis from 1951-52 in the RBI Bulletins. But the data base for the earlier years is weak. As the compilation of data was started in 1955 and there were various problems of availability and deficiencies of data for the earlier years. For instance, for the years 1951-52 and 1952-53 both the Sources and Uses of Banking Sector are negative.* As the Sources and Uses of the Banking Sector are not negative for any other year, the analysis may get distorted if the earlier years are included. Hence, the study is confined to the period 1956-57 to 1975-76.

* See R B I Bulletin March 1967, page 313

5.3 Financial Instruments: Financial instruments are classified in RBI data for the Aggregate Economy as -

- (1) Currency and deposits
- (2) Investments
- (3) Loans and Advances
- (4) Small Savings
- (5) Life Fund
- (6) Provident Fund
- (7) Trade Debt/Credit

5.4 In currency and deposits, cash in hand, Demand deposits and Time deposits are included. Investments include Central and State Governments' Securities and Treasury Bills, other securities of the Government, Corporate securities which include Paid-up Capital and Debentures, Bank securities which include Paid-up Capital and Debentures, Other Financial Institutions Securities which include Bonds and Debentures, Foreign Securities and others.

5.5 To ascertain the changes in relative importance of the above mentioned instruments that constitute the Flow, yearly percentage share of each instrument is calculated for the twenty year period. As these percentage shares reveal no pattern due to fluctuations from year to year, the method of taking the average of 5 years is adopted. The instruments are ranked according to their 5-yearly percentage shares in the total Flows. (See Table 5.1).

Table 5.1: Instrument-wise Rank Chart

Period	Currency and Deposits	Invest- ments	Loans & Advances	Small Savings	Life Fund	Provi- dent Fund
I (1956-57 to 1960-61)	3 (21.8)	2 (27.9)	1 (31.5)	5 (6.2)	6 (3.0)	4 (8.8)
II (1961-62 to 1965-66)	2 (24.0)	3 (22.0)	1 (41.1)	5 (5.5)	6 (3.9)	4 (6.6)
III (1966-67 to 1970-71)	2 (22.0)	3 (18.2)	1 (40.1)	6 (3.3)	5 (4.3)	4 (7.3)
IV (1971-72 to 1975-76)	2 (27.3)	3 (21.1)	1 (28.1)	5 (3.7)	6 (3.6)	4 (7.3)

Note: Figures in brackets indicate percentage shares of each instrument in total Flows.

Source: Tables 5.1 to 5.13 are computed from the data on Flow of Funds in R B I Bulletins of March, 1967, July, 1969, August 1975 and March, 1980.

5.6 Loans and Advances: It can be seen that Loans and Advances retain the first rank for the entire period. Its share ranges from 28.1 to 41.1 per cent.

5.7 Currency & Deposits: The first instrument, namely Currency and Deposits has improved its rank from third in the first period to second for the rest of the period.

5.8 Investments: Investments' rank declines from second in the first period to third in subsequent periods.

5.9 Small Savings: The percentage share of Small savings declines over the twenty-year period.

5.10 Life Fund and Provident Fund: There has been hardly any change in the relative importance of these two instruments.

5.11 Thus, an inference can be drawn that there has been a shift in favour of Currency and Deposits in the Instrument-wise structure of Capital Flows in the Indian economy.

5.12 The composition of Instrument-wise Flow of the domestic sectors of the Indian economy is analysed both for the Sources and Uses.

5.13 Household Sector (Sources): The instruments through which the Household Sector acquires liabilities are classified in RBI data as Borrowing and Trade Debt. As there are only two instruments which constitute the Sources of the Household Sector out of which the share of the second is low and Borrowing is regarded as an instrument, in a very broad sense in the flow of funds analysis, instrument-wise structure of Sources of the Household Sector is not worth undertaking.

5.14 Household Sector (Uses): The Household Sector's financial assets are held in the following financial instruments:

1. Currency
2. Bank Deposits

3. Loans and Advances
4. Insurance
5. Provident Fund
6. Investments

Table 5.2 gives percentage shares of instruments in Total Flows and the ranks associated with them.

5.15 Currency: The share of currency in the Uses of the Household Sector declines over the period of the study from 20.5 per cent to 13.1 per cent.

5.16 Bank Deposits: Bank Deposits increase from 20.9 per cent in the first period to 45.2 per cent in the fourth period, its rank also improved from third in the first period to first for the rest of the periods of analysis.

5.17 Loans and Advances: This instrument's share is insignificant in the Uses of the Household Sector. It is lowest throughout (6th rank).

5.18 Insurance: The importance of Insurance increases marginally over the period and its rank improves from fifth to fourth.

5.19 Provident Fund: This instrument is important in the Uses of the Household Sector; its share ranges from 18 per cent to 23 per cent. Its rank is second, except in Period-II.

5.20 Investments: Investments rank first in the first period with 23 per cent share in the total Uses of the Household Sector. Its share declines to 3.8 per cent in the fourth period, and its rank also declines from the first to fifth. It can be seen from Table 5.2 that the preference of the Household Sector has shifted in favour of Bank Deposits as against Investments and to some extent Currency.

Table 5.2: Rank Chart - Household Sector (Uses)

Year	Currency	Bank Deposits	Loans & Advances	Insurance	Provident Fund	Investments
I (1956-57 to 1960-61)	4 (20.5)	3 (20.9)	6 (3.8)	5 (7.6)	2 (22.9)	1 (23.0)
II (1961-62 to 1965-66)	2 (20.7)	1 (30.4)	6 (5.4)	5 (10.1)	3 (18.0)	4 (14.7)
III (1966-67 to 1970-71)	3 (17.1)	1 (35.5)	6 (5.2)	4 (12.5)	2 (21.0)	5 (7.8)
IV (1971-72 to 1975-76)	3 (13.1)	1 (45.2)	6 (3.3)	4 (11.7)	2 (19.9)	5 (3.8)

5.21 Banking Sector (Sources): The instruments through which this Sector acquires liabilities are:

- (1) Currency and Deposits
- (2) Investments
- (3) Loans and Advances
- (4) Foreign claims (not elsewhere classified)
- (5) Other items (not elsewhere classified)

Of these Sources, the last three items have negligible share in total Sources, and only the first two instruments are significant in the Sources of this sector. It may be noted that the last item is not an instrument but an accounting device. Percentage shares of instruments in the total Sources of the Banking Sector are given in Table 5.3.

5.22 Currency & Deposits: Currency and Deposits rank first in all four periods. Its share, 92.4 per cent in the first period declines to 84.7 per cent in the last period. Thus, its share in total Sources of the sector is predominant.

5.23 Investments: Investments rank second in the first three periods, though its rank declines to third in the last period. Its share ranges from 5.3 per cent to 9.6 per cent.

5.24 The instrument-wise structure of the Sources of the Banking Sector has remained unchanged in the 20-year period under study.

Table 5.3: Rank Chart - Banking Sector (Sources)

Period	Currency & Deposits	Investments	Loans & Advances	Foreign Claims not elsewhere classified	Other items not elsewhere classified.
I (1956-57 to 1960-61)	1 (92.4)	2 (7.7)	3 (1.4)	4 (- 0.7)	5 (- 1.1)
II (1961-62 to 1965-66)	1 (88.9)	2 (6.5)	3 (2.8)	5 (0.1)	4 (1.6)
III (1966-67 to 1970-71)	1 (87.6)	2 (9.6)	4 (0.5)	5 (0.4)	3 (1.9)
IV (1971-72 to 1975-76)	1 (84.7)	3 (5.3)	5 (0.6)	4 (0.8)	2 (8.5)

5.25 Banking Sector (Uses): The instruments in which the Banking Sector holds its assets are classified in RBI data as -

- (1) Currency and Deposits
- (2) Investments
- (3) Loans and Advances
- (4) Foreign Claims (not elsewhere classified)
- (5) Other items (not elsewhere classified)

Amongst these, the important instruments are Investments, Loans and Advances. The other instruments' percentage share in the Uses of the sector is not significant. Percentage shares of instruments in the total Uses of the Banking Sector are given in Table 5.4.

5.26 Investments: This instrument ranks second throughout the period but its share increases from 22.4 per cent in the first period to 47.4 per cent in the last period.

5.27. Loans and Advances: Loans and Advances rank first in all the four periods, though its share declines from 71.4 per cent in the first period to 48.6 per cent in the fourth period.

5.28 The relative importance of Investments in the Uses of the Banking Sector has increased significantly. Table 5.4 reveals a clear shift in favour of Investments as an instrument against the instrument, Loans and Advances.

Table 5.4: Rank Chart - Banking Sector (Uses)

Period	Currency & Deposits	Investments	Loans & Advances	Foreign Claims not elsewhere classified	Other items not elsewhere classified
I (1956-57 to 1960-61)	3 (0.8)	2 (22.4)	1 (71.4)	4 (- 0.4)	--
II (1961-62 to 1965-66)	5 (-0.7)	2 (45.0)	1 (54.7)	3 (0.8)	4 (0.2)
III (1966-67 to 1970-71)	5 (- 0.6)	2 (38.3)	1 (61.4)	4 (0.7)	3 (1.6)
IV (1971-72 to 1975-76)	5 (- 0.2)	2 (47.4)	1 (48.6)	4 (0.02)	3 (4.1)

5.29 The Other Financial Institutions Sector (Sources):

The instruments through which the sector mobilises its Sources are -

- (1) Paid-up Capital
- (2) Bonds and Debentures
- (3) Borrowing
- (4) Life Fund
- (5) Other Insurance Fund
- (6) Provident Fund
- (7) Trade Debt/Other Liabilities
- (8) Unit Capital

5.30 Provident Fund: For this sector, Provident Fund is the most important constituent of its Sources. Its rank remains first in all the four periods. It accounts for 58.8 per cent in the first period and 40.3 per cent in the last period. See Table 5.5 which gives the relative shares of instruments in total Sources of the Sector.

5.31 Life Fund: This instrument is second in importance in the Sources of the Other Financial Institutions Sector. Its share ranges from 29.8 per cent to 36.8 per cent. Table 5.6 brings out an interesting feature in the Sources of this sector, that borrowing as an instrument, no doubt, retains its third rank for the entire period, in percentage terms it gains substantially from 4.8 per cent to 13.2 per cent.

5.32 The share of other instruments, by and large, is insignificant in the Sources of this Sector.

5.33 The analysis of the composition of instruments in the Sources of the Other Financial Institutions Sector, shows a marginal change; borrowing as an instrument has gained some importance.

Table 5.5 : Rank Chart - Other Financial Institutions Sector (Sources)

Period	Paid-up Capital	Bonds and Deben- tures	Borrow- ing	Life Fund	Other Insu- rance Fund	Provi- dent Fund	Total Debt/ Other Liabi- lities	Unit Capi- tal
I (1956-57 to 1960-61)	6 (1.9)	4 (2.4)	3 (4.8)	2 (29.8)	5 (2.1)	1 (58.8)	7 (0.2)	-
II (1961-62 to 1965-66)	6 (1.7)	5 (1.8)	3 (17.1)	2 (36.7)	4 (3.0)	1 (38.3)	8 (0.2)	7 (2.9)
III (1966-67 to 1970-71)	7 (1.3)	6 (1.8)	3 (14.4)	2 (36.8)	4 (3.9)	1 (38.2)	8 (0.4)	5 (3.1)
IV (1971-72 to 1975-76)	6 (1.6)	4 (6.9)	3 (13.2)	2 (30.4)	5 (4.9)	1 (40.3)	8 (1.2)	7 (1.5)

5.34 Other Financial Institutions Sector (Uses): The sector holds its assets in the following instruments:

1. Currency and Deposits
2. Loans and Advances
3. Investments
4. Miscellaneous

5.35 Investments: Investments is the most important constituent of the Financial Flow (Uses) of the Sector. Its average share in the first period is 88.3 per cent which declines to 59.7 per cent in the last period. Although it maintains its relative importance with a first rank throughout, its share declines over the period of study (Table 5.6).

5.36 Loans and Advances: This instrument ranks second throughout the period, in the Uses of the Other Financial Institutions Sector. However, its share records an increase from 10.2 per cent in the first period to 31.4 per cent in the last period.

5.37 Currency and Deposits: Asset creation through this instrument is insignificant for the first two periods. In the third period its share increases to 8.9 per cent which declines marginally to 8.3 per cent in the last period. However, this instrument ranks third in relative importance throughout. It can be observed from Table 5.6 that as an instrument, the relative importance of Loans and Advances has increased, while that of Investments has declined in the composition of instruments in the Uses of Other Financial Institutions Sector.

Table 5.6: Rank Chart - Other Financial Institutions (Uses)

Period	Currency & Deposits	Loans and Advances	Invest- ments	Miscella- neous
I (1956-57 to 1960-61)	3 (2.8)	2 (10.2)	1 (88.3)	4 (- 1.6)
II (1961-62 to 1965-66)	3 (1.9)	2 (29.4)	1 (70.5)	4 (- 0.1)
III (1966-67 to 1970-71)	3 (8.9)	2 (32.4)	1 (59.2)	4 (- 0.7)
IV (1971-72 to 1975-76)	3 (8.3)	2 (31.4)	1 (59.7)	4 (0.5)

5.38 Corporate Sector (Sources): The instruments through which the Corporate Sector acquires capital funds are :

1. Paid-up Capital
2. Debentures
3. Deposits (Household)
4. Borrowing
5. Trade Debt
6. Miscellaneous

5.39 Borrowing: Borrowing is the most important source of funds for this Sector. It accounts for 65.7 per cent in the first period, which increases to 80.4 per cent in the third period and it shows a decline in the last period (53.3 per cent).

5.40 Paid-up Capital: Paid-up Capital shows a declining trend from 28.7 per cent in the first period to 9.9 per cent in the fourth period. It should be noted that the decline in the borrowing is accounted for by an increase in trade debt from 3.9 per cent to 18.4 per cent and in Miscellaneous category from 2.8 per cent to 19.1 per cent. Deposits (Household) gains importance only in the fourth period (See Table 5.7). One may conclude that the reliance of the Corporate Sector on sources other than paid-up capital, mostly borrowing has increased, resulting in change in the relative importance of instruments in the Sources of Corporate Sector.

Table 5.7: Instrument-wise Rank Chart - Corporate Sector
(Sources)

Period	Paid-up Capital	Deben- tures	Deposits (Households)	Borrow- ing	Trade Debt	Miscel- laneous
I (1956-57 to 1960-61)	2 (28.7)	5 (2.2)	3 (4.5)	1 (65.7)	6 (0.1)	4 (3.6)
II (1961-62 to 1965-66)	2 (22.4)	3 (3.2)	4 (2.0)	1 (77.9)	6 (-28.7)	5 (0.2)
III (1966-67 to 1970-71)	2 (12.8)	3 (4.9)	5 (2.6)	1 (80.4)	6 (3.9)	4 (2.8)
IV (1971-72 to 1975-76)	4 (9.9)	6 (1.3)	5 (8.3)	1 (53.3)	3 (18.4)	2 (19.0)

5.41 Corporate Sector (Uses): Financial asset creation of the Corporate Sector will be negligible for obvious reasons. The Table 5.8 below shows that the structure of instruments through which the sector acquires financial assets fluctuates markedly from period to period.

Table 5.8: Instrument-wise Rank Chart Corporate Sector (Uses)

Period	Cash in hand	Bank balance	Fixed Deposits	Loans & Advances	Invest- ments	Miscel- laneous
I (1956-57 to 1960-61)	6 (- 2.0)	2 (18.0)	1 (107.9)	3 (10.2)	4 (5.5)	5 (- 0.5)
II (1961-62 to 1965-66)	4 (7.1)	1 (29.5)	2 (20.6)	1 (29.5)	3 (7.7)	5 (2.9)
III (1966-67 to 1970-71)	3 (37.1)	5 (8.8)	2 (48.9)	1 (81.1)	4 (23.9)	.6 (0.4)
IV (1971-72 to 1975-76)	5 (3.7)	3 (13.2)	2 (16.5)	1 (45.6)	6 (3.5)	4 (8.8)

5.42 Government Sector (Sources): The analysis of the structural composition of Instruments in the Sources of the Government Sector presents some problems, as some of the instruments are replaced by others in the RBI presentation of data during the period of study. For instance, Investment of US Government counterpart funds appear from the year 1960-61 and end in 1965-66. The item "Sterling Pension annuities" end

in 1958-59. Hence, the methodology adopted is to select the instruments that are common for the entire period, for analysis. The instruments selected for the analysis represent 58.2 per cent to 112.8 per cent of total Sources of the Government Sector. This is due to the fact that all instruments through which the borrowing of the Government Sector has been undertaken could not be included as these instruments do not figure in all the years. If in a particular year in which an instrument which has a negative entry is not taken up for analysis, the percentage in Sources of Instruments analysed exceeds 100 per cent. (See Table 5.9)

Table 5.9: Government Sector (Sources): Percentage Share of Sources Analysed of Total Sources of the Sector

Year		Percentage of Sources analysed
1956-57	..	112.8
1957-58	..	101.0
1958-59	..	97.8
1959-60	..	93.2
1960-61	..	58.0
1961-62	..	91.0
1962-63	..	85.5
1963-64	..	87.3
1964-65	..	93.1
1965-66	..	88.3
1966-67	..	90.5
1967-68	..	72.1
1968-69	..	93.1
1969-70	..	58.2
1970-71	..	78.3
1971-72	..	78.0
1972-73	..	73.6
1973-74	..	81.5
1974-75	..	71.5
1975-76	..	82.1

5.43 In the years 1960-61 and 1969-70 the instruments considered cover about 58 per cent of the total Sources of the Sector. In 1960-61 'Investment of U.S. Government counterpart Funds', which is not included for analysis as it does not figure throughout the period, accounts for 34 per cent of the Sources of the Government Sector. In 1969-70 items like Provident Fund and Insurance and Security Deposits of Electricity Boards figure in the data which are not taken up. Thus, the items that are analysed are common for the entire period and they add up to a large percentage of Sources of Government Sector. (See Table 5.10).

5.44 Government Securities other than Treasury Bills: This instrument ranks first with 38.8 per cent as its share, in the first period. From the second period onwards, it ranks second and its percentage share has registered a fall over the period of the analysis.

5.45 Borrowing: This instrument ranks second in order of importance, for the first period (21.1 per cent). Its relative importance increases from the second period (1st rank, 42.4 per cent) though its rank remains first in the last period, its Share declines to 23.3 per cent.

5.46 Treasury Bills: Treasury Bills rank third throughout, except in the second period when its rank declines to fourth.

5.47 The structure of instruments in the Sources of the Government Sector has changed over the 20-year period under

study, though not significantly (see Table 5.10). Borrowing has gained at the expense of Government Securities, ~~have gained~~ while Treasury Bills and Small Savings' share is more or less constant.

Table 5.10: Instrument-wise Rank Chart -Govt.Sector (Sources)

Period	Govt. Securi- ties other than Treasury Bills	Trea- sury Bills	Borrow- ing	Small Savings	One Rupee Notes and Coins	Paid-up Capital
I (1956-57 to 1960-61)	1 (38.8)	3 (19.1)	2 (21.1)	4 (12.1)	5 (1.3)	--
II (1961-62 to 1965-66)	2 (21.4)	4 (11.7)	1 (42.4)	3 (12.4)	5 (1.1)	--
III (1966-67 to 1970-71)	2 (17.7)	3 (11.1)	1 (41.2)	4 (7.8)	5 (0.6)	--
IV (1971-72 to 1975-76)	2 (21.4)	3 (20.3)	1 (23.3)	4 (11.7)	5 (0.8)	6 (0.1)

5.48 Government Sector (Uses): The Uses of the Government Sector also pose certain problems, for, the composition of the Uses of Government Sector is not uniform, as certain instruments are absent in some years and data on others is not available for all the years. To overcome this problem, only the main instruments of asset creation of the Government Sector for which the data is available for the entire period of study

is taken up for analysis. Generally, the percentage share of Sources covered by the instruments taken up for analysis is more than 75 per cent. Therefore, the analysis can reveal changes in the structure of instruments' composition in the Uses of the Government Sector.

5.49 The important instruments through which the Government Sector creates financial assets are (1) Loans and Advances, (2) Investments, (3) Deposits with Banking Sector. Items like Cash Balance and Net purchase of Domestic Gold form a very small percentage of total Uses of the Government Sector and, therefore, are not considered.

5.50 Loans and Advances: The share of Loans and Advances is relatively high throughout, in the total Uses, but its share declines from 70.8 per cent in the first period to 48 per cent in the last period.

5.51 Investments: This instrument retains its second rank throughout except in the first period when subscriptions to international organisations secures, the second rank.

5.52 Deposits with Banking Sector: This instrument's share declines over the 5-yearly periods. Its percentage share ranges from 15.7 to 3.4.

5.53 Thus, from the analysis of the Uses of the Government Sector it may be concluded that there is marginal change in

the instrument-wise structure of its financial asset creating activity. However, though the instrument Loans and Advances retains its first rank, its percentage share declines significantly.

Table 5.11: Government Sector (Uses). Percentage Share of Uses Analysed of Total Uses of the Sector

<u>Year</u>	<u>Percentage of Uses</u>
1956-57	75.7
1957-58	81.7
1958-59	69.3
1959-60	94.5
1960-61	90.7
1961-62	175.9
1962-63	101.0
1963-64	74.5
1964-65	85.2
1965-66	87.2
1966-67	83.2
1967-68	94.3
1968-69	93.5
1969-70	61.4
1970-71	103.2
1971-72	67.2
1972-73	54.0
1973-74	63.2
1974-75	62.9
1975-76	97.0

Table 5.12: Instrument-wise Rank Chart -Govt.Sector (Uses)

Period	Cash Balance	Deposits with Banking Sector	Loans & Advances	Invest- ments	Subscrip- tions to Internat- ional organisa- tions	Net Purchase of Domes- tic Gold and Silver
I (1956-57 to 1960-61)	6 (1.24)	3 (15.7)	1 (70.8)	4 (11.8)	2* (20.5)	5* (3.1)
II (1961-62 to 1965-66)	5 (1.7)	3 (7.2)	1 (72.4)	2 (13.1)	4 (6.3)	6 (2.0)
III (1966-67 to 1970-71)	5 (1.2)	4 (4.9)	1 (56.9)	2 (18.0)	3 (6.9)	6 (0.5)
IV (1971-72 to 1975-76)	5 (2.2)	4 (3.4)	1 (48.0)	2 (11.0)	3 (4.1)	6 (0.2)

* 3 year averages have been calculated as data is available only for three years.

5.54 R.W.Goldsmith has made a significant contribution by using different ratios to measure and analyse the financial structure and its interrelations with the real variables, e.g., Financial Inter-relations Ratio (FIR), Finance Ratio (FR) and New Issue Ratio (NIR). As we are primarily concerned with the structure of Capital Flows in the economy, the Intermediation Ratio (IR) which is a ratio of Secondary to Primary Issues has been worked out for a period of twenty years for the Indian Economy. As the ratio fluctuates from year to year, five year

** R.W.Goldsmith: Financial Structure and Development, (Yale University Press, 1969), pp.49 to 108.

averages have been worked out, from 1956-57 to 1975-76. See Table 5.13. This ratio reflects the development of Financial Institutions which is mirrored in the changes in the level of Financial Intermediation in the economy. The Intermediation Ratio is 55 per cent in the first period, declines to 48 per cent in the second period and shows an increase in the next two 5-year periods.

Table 5.13: Average Intermediation Ratio

Period	Intermediation Ratio (%)
I (1956-57 to 1960-61)	55
II (1961-62 to 1965-66)	48
III (1966-67 to 1970-71)	56
IV (1971-72 to 1975-76)	78

5.55 Thus, the structure of Capital Flows has changed as the share of Secondary Issues, has increased in relation to Primary Issues. It is evident from this that the level of Financial Intermediation has increased in the Indian economy over the period of study.