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THE COMMERCIAL BANKS AS AGENTS FOR DEVELOPMENT

by Frank M. Tamagna

In every country, irrespective of its stage of economic development and financial organization, commercial banks have a key role to play. As the intermediaries between the central bank and the market, they are the holders of financial liquidity, which they redistribute to the various sectors of the economy, in currency or demand deposits in accordance with the needs and preference of their customers. They are the largest depositories of national savings, which they attract though their many offices and the wide variety of services they offer. They are the links between their domestic and the world economies, and the channels through which foreign trade and investments flow. In developing countries they are all the more important, not only as savings and financing institutions, but also as the promoters of change, adapting in a continuing way their instruments of savings and credit to new needs and combining their own lending with investments by others for the growth of the economy.

In most of the developing countries, commercial banking was introduced at an early stage, by leading banks from Europe, the United States and Japan that established branches in the coastal trading outposts of Latin America, Asia and Africa. What brought them there was a demand for financial services related to the trade and shipping of their own nationals and the handling of exports of basic commodities and imports of manufactured goods. It was inevitable that these banks would soon shift to the financing of local production and processing of commodities, and hence of local manufacturing in those parts of the world in which they had set up their branches. This integrating process of foreign banks in the local economies was speeded up by the achievement of independence and the pressure exerted by political forces toward economic development. In many countries these branches of foreign banks were transformed in separate affiliates, with varying degrees of local participation and autonomy from the parent banks abroad, while in others these overseas banks were transformed into national institutions. In both cases, they contributed with the rise of domestic banks to the formation of national banking systems.

Most developing countries are now at a stage, in which agriculture is still predominant, manufacturing is at its beginnings promoted by public and private initiative, and large scale infrastructural projects are being undertaken by their governments with know-how and capital from foreign and international institutions. The needs for capital are great, and commercial banks lead in the mobilization of financial resources. They are of particular importance to private business initiative, which still holds to a closely controlled pattern and in many instances, while eager to expand, is seeking sources of financing that would not interfere with ownership and management. As the principal institutions attending to the finance needs of modern business, banks are accordingly shifting their operations from the non-traditional "commercial banking" to a "multi-function finance" pattern. From their origins and experience, they have acquired wide contacts with business and a knowledge of the structure and conditions of the market, that no other institution could easily duplicate; moreover, no other institution could build up a comparable volume of business, in which risks in new ventures could be adequately diversified. Consequently, advantages of time, skill and size give commercial banks a leading role as the formative institutions of modern financial systems.

Moving in this direction, commercial banks in many countries have adopted a "departmental" or "grouping" type of organization, equipped to handle savings and fixed deposits alongside with demand and checking accounts, to extend their financing operations from short term or revolving credits to term loans and equipment finance, to enter into real estate mortgages, and to branch out into investment management and other financial services. This functional expansion of banking is generally accompanied by a regional expansion, induced by the desire of the banks to acquire additional resources and the policies of the authorities to bring banks outside of cities and open their credit windows to new borrowers.

The banking expansion does much to spread the habits of deposits and savings in rural areas and among lower groups of the population, and also to accustom unexposed groups, like small business and farmers, to standards, procedures and conditions of borrowing. In short, commercial banks help introducing to modern financial practices those countries and areas, whose monetary and business sectors have not as yet reached a level, in number volume and diversity of transactions, that would justify and support separate and specialized institutions. This banking expansion -- both functional and regional -- has also the effect of spreading the use of available financial resources and making interest rates more uniform, with differentials based more on the relative credit risks and less on local savings formation.

By the time commercial banks have reached this more advanced stage of development and adapted their ordinary credits to local usages and needs, they find themselves financing the various sectors (commerce, industry, agriculture and services, public or private), and the various categories of borrowers (individuals, firms and companies, private or public institutions), for any purposes (finance, production or consumption) that the economy needs for its continuing and sustained development. As the "department stores" of modern finance, they are paving the way in turn to the formation of specialized institutions: as their activities grow along with the economy, so grow the need and the basis for separate institutions specializing in savings, investment and insurance, better able to cope with the larger and longer term requirements of corporate financing and the handling of securities. In many countries in Latin America and Asia, the commercial banks have initiated and participated in the establishment of finance companies and mutual funds -- thus providing a sound foundation for the development of capital markets.

The influence that commercial banks play in all countries is not confined to their day-to-day lending, and is only in part related to the operations they conduct through the use of their resources. Commercial banks in developing countries have gone a long way from the warehouses their predecessors had established as part of their India and China trade; nowadays the leading banks of Latin America and Asia are the promoters and participants in multiple concerns, handling in sophisticated ways commercial and industrial, mortgage and securities financing. They continue to be the essential links in the chain of trade and investments, that join the developing with the industrial countries of the world. What is more or less appropriate for commercial banks to do varies from country to country, but everywhere they are the key institutions of their own markets and the channels through which domestic savings and foreign funds merge for economic development.

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