PUBLIC SECTOR BANKS IN INDIA
- AN OVERVIEW
CHAPTER II

PUBLIC SECTOR BANKS IN INDIA - AN OVERVIEW

Banking in India on western lines started from the beginning of the 19th century. The first Joint Stock Bank was established at Calcutta by the name of Bank of Hindoostan. At that time, Bank of Bengal (1806), Bank of Bombay (1840) and Bank of Madras (1843) were started with the financial participation of the Government. These banks were called the Presidency Banks and were given the right of note issue in their respective regions.

The first purely Indian Joint Stock Bank was the Oadh Commercial Bank which came into existence in 1889; it was followed by the Punjab National Bank in 1894 and the People’s Bank in 1901. The Swadeshi Movement of 1905 gave great stimulus to the starting of Indian banks. The Indian banking system had gone through a series of crises and consequent bank failures its growth was quite slow during the first half of this century.

But after independence, the Indian banking system recorded rapid progress. This was due to planned economic growth, increase in money supply, growth of banking habit, control and guidance by the Reserve Bank of India and the nationalisation of banks etc.

Indian banking development since independence is a saga of successful orientation of commercial banks evolved on the British pattern to the growing needs and complexities of development. The Indian banking system has been undergoing structural and ideological changes, particularly after nationalisation. The global banking environment is also undergoing a transformation in recent years. The Indian banking system has to adjust and assimilate itself in the coming years not only to the internal environment but also to the ever changing international banking scenario.
2.01. PRE NATIONALISATION ERA

In the pre nationalisation period, the Indian banking system had gone through a series of crises and bank failures and its growth was quite slow during this period. The commercial banks were owned and controlled by a very small number of shareholders who happened to be big industrial magnets who used the funds of the banks to build up their huge industrial empires, which had become virtual monopolies. This had led to the concentration of wealth and economic powers in the hands of few persons.

Small industrial and business units were continuously and consistently ignored. Agricultural credit was never seriously considered. Banks had also failed to open branches in semiurban and rural areas. As a result, savings of the rural community remain untapped. Besides they had drained off the savings of some states and had diverted them to others, thus resulting in lop sided regional development. It was for the above mentioned reasons the Government of India resorted to nationalisation of commercial banks.

The organised banking in regulated form started in 1921 when the Imperial Bank of India was constituted under a Special Act. In 1955, the Imperial Bank of India was converted into State Bank of India. It will be regarded as a red letter day in the annals of Indian banking. With the establishment of the State Bank of India, a new chapter of state ownership opened in the history of commercial banking.

The Government associated banks were made subsidiaries of the State Bank of India. At the time of take over subsidiaries were eight. Since the amalgamation of State Bank of Jaipur and State Bank of Bikaner in 1963, the number goes down to seven. Following are the subsidiaries of State Bank of India.
During the period July 1955 to July 1969, State Bank of India made considerable progress in the areas of branch expansion, deposit mobilisation and purveying credit. However, in branch expansion, the performance was skewed in that preference was given to urban and metropolitan areas. Similarly small scale industries, agriculture and allied activities were kept outside the purview of bank credit facilities.

The role of other commercial banks was worse than this. Advances to wholesale trade still predominated and the needs of the retail trade were not met adequately. Modern technology being divisible, finance which acts as a catalytic agent had to be provided in rather large measure. Thus the role of commercial banks need to be revamped.

It was only as a consequence of this great realisation that the ordinance of nationalisation of 14 major commercial banks in India was promulgated on 19th July, 1969. The basic objective of this step was to accelerate development and thus make a significant impact on the problems of poverty and unemployment and to bring about progressive reduction of disparities between the rich and poor sections of our people and between the relatively advanced and backward areas of our country.

1 Gadgil Study Group of the Committee to review arrangements for Institutional Credit for Agriculture and Rural Development, RBI, Bombay (1981), P. 84.

2 Text of the Statement made by the Prime Minister in Parliament, The Banker, July 1969, P. 366, also Government of India, Nationalisation of Banks, a symposium.
The main objectives of nationalisation of commercial banks are summed up in the preamble to the Banking Companies (Acquisition and Transfer of Undertaking) Act, 1970 are as follows:

'To control the commending heights of the economy and to meet progressively and serve better the needs of development of the economy in conformity with national policy and objective and for the matters connected herewith or incidental thereto'.

The nationalisation of 14 major commercial banks constitute a landmark in the banking history of the country. Following were the banks nationalised in 1969.

1. The Central Bank of India Ltd.,
2. The Bank of India Ltd.,
3. The Punjab National Bank Ltd.,
4. The Bank of Baroda Ltd.,
5. The United Commercial Bank Ltd.,
6. The Canara Bank Ltd.,
7. The United Bank of India Ltd.,
8. The Dena Bank Ltd.,
9. The Syndicate Bank Ltd.,
10. The Union Bank of India Ltd.,
11. The Allahabad Bank Ltd.,
12. The Indian Bank Ltd.,
13. The Bank of Maharastra Ltd., and
14. The Indian Overseas Bank Ltd.

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On 15th April 1980, six more banks were nationalised. They are:

1. The Andhra Bank Ltd.,
2. Corporation Bank Ltd.,
3. The New Bank of India Ltd.,
4. The Oriental Bank of Commerce Ltd.,
5. The Punjab and Sind Bank Ltd., and
6. Vijaya Bank Ltd.

The nationalisation of the commercial banks was a “revolution” in the Indian Banking System. This “revolution” did not merely signify a change in the ownership of these banks, but it was the beginning of a co-ordinated endeavour to use an important part of the financial mechanism for the country’s economic development. There is a thinking to gradually withdraw the budgetary and federal support that public sector banks have been provided so far and put them on par with any other market participant as far as regulation, competition and adhering to the prudential guidelines are concerned. These developments would bring about tremendous changes in the functioning of public sector banks.

2.02. POST NATIONALISATION ERA

Banking development in India is a notable example of the successful orientation of commercial banks evolved on the western pattern to the growing needs and complexities of development. Since the nationalisation of major commercial banks in the country, Indian banking has undergone a metamorphosis in the very concept, precept and outlook. Explosive growth coupled with functional diversification in consonance with the national objectives and priorities has been the hallmark of this phenomenal transformation. These developments are best depicted by telling some statistics.
Between June 1969 and March 1992 the total number of commercial bank offices rose from 8,262 to 45,964. The average population served by bank offices has declined from 65,000 to 12,000.

Aggregate deposits showed a spectacular increase from Rs.5,258 crores in June 1969 to Rs.2,64,920 crores by the end of March 1992.

Total bank credit recorded a jump from Rs.3,732 crores to Rs.1,59,051 crores during the period June 1969 to March 1992. The total number of borrowal accounts under the priority sector has increased from 2.6 lakhs in June 1969 to 349.2 lakhs in June 1991.

Profits of the banks has increased from Rs.11.10 crores in June 1969 to Rs.1,200 crores in March 1992.

After nationalisation public sector banks were directed to make special efforts to augment their lending to neglected sectors. Population coverage of banks has dramatically improved in states like Assam, Megalaya, Nagaland, Bihar, Orissa, Uttar Pradesh, Madhya Pradesh and Jammu and Kashmir which in the past were very poorly served by the banking system.

It may thus be seen that banking is no longer confined to a narrow segment of the population. It has acquired a broad base and has emerged as an instrument of economic development. Social banking was given due attention and every commercial bank was directed to set aside 40% of its net bank credit to the priority sector. Thus Indian Banking System in post nationalisation period was governed by mass banking and purpose oriented banking.
2.03. PRESENT SCENARIO

Sweeping reforms were brought about in several important areas pertaining to functioning of banks, like capital adequacy, income recognition, provisioning, investment foreign exchange management, accounting practices and procedures etc. Though the ramifications of these guidelines would be felt by all the banks irrespective of their ownership or origin, their intensity would be steep in the case of public sector banks.

The recent developments relating to public sector banks is discussed though it is outside the scope of the present study.

Nationalisation of commercial banks is also not free from its drawbacks. Profitability of commercial banks were strained due to increased societal marketing obligations. Recovery had become the recurring problems for the banks, which resulted in mounting overdues. In order to remedy the above defects and to make the Indian banks globally competitive the Government of India set up a high level committee with Mr. M. Narasimham, a former Governor of Reserve Bank of India as a Chairman to examine all aspects relating to the structure, organisation, functions and procedures of financial system. The committee submitted its report in 1991. The Government of India and Reserve Bank of India accepted and implemented some of the recommendations to revamp the banking sector. The recommendations were implemented in tune with the liberalisation measures introduced in other sectors of the economy and this period 1990's marks the globalisation period of the banking industry.

The following are some of the major reform measures implemented in the Indian Financial Sector.
1. SLR has been slashed down to 31.75% from 38.50%
2. The branch licensing policy has been abolished considering the heavy losses suffered by banks by opening branches in unviable areas.
3. Interest rates have been deregulated.
4. Prudential norms have been introduced to make the banks globally competitive.
5. Private sector banks are allowed to enter into the field in order to infuse an element of healthy competition in the banking industry.
6. The supervisory system of Reserve Bank of India is being strengthened with the establishment of new board for financial supervision within the Reserve Bank of India under the exclusive charge of a Deputy Governor.
7. Joint Publicity Committee has been abolished in order to make the public sector banks more competitive in terms of promotional strategies.

On account of the introduction of the above mentioned measures, competition has been intensified in financial sector due to the encouragement given to private sector banking, introduction of liberalised terms and conditions which facilitates easy accessibility to the capital market by the corporate sector, mushroom growth of mutual funds etc. Thus a bank faces tough competition in mobilisation of deposits from various avenues viz., non-banking finance companies, corporate sector, mutual funds, post offices etc., apart from the unorganised sector.
Similar is the case in advances too with deregulation of interest rates and more flow of foreign investments into the country. Banks are much interested in choosing credit-worthy corporate borrowers. But the corporate sector is much interested in tapping the funds directly from public instead of approaching the banks.

As interest rates were deregulated and though initially there was a scramble for reduction, rates have been stabilised. With the entry of more number of players into the market, there has been an explosion of career opportunities in the banking industry. This has resulted in exodus of personnel from the public sector banks and to arrest this trend, a level playing field has been provided to public sector banks and now they are allowed to fix their own pay structure. Autonomy is expected to be given to public sector banks in the areas of recruitment also in the days to come.