Chapter - 3

Impact on Banking Performance After Nationalization
The nationalization of 14 major commercial banks was announced by the govt. of India through an ordinance by the president under Art. 123 of the constitution of India on July 19, 1969. The ordinance was replaced with the Banking Companies Act (Acquisition and transfer of undertakings) passed by the parliament on August 9, 1969.

Causes Behind Nationalization:

The first step in this direction was taken by the Government in 1955, when Imperial Bank of India converted into State Bank of India. This policy of the government was completely materialized when the fourteen (14) major commercial banks with a deposit of Rs. 50 crores or above were nationalized by the govt. of India under Banking Companies Act 1969. After nationalization the public sector of India now cover 84% of the banking business as against 27%.

If we study the total deposits of 14 nationalized banks (the commercial bank) in 1967 and bank credits they were
Rs. 2312 and Rs. 1583 crores respectively. In 1968 the position of deposits and bank advances in respect of the nationalized banks. We can observe that all the nationalized banks now cover 84% of the total deposits and 82.8% of the total bank credits of all banking business in India. These 14 nationalized banks alone cover 62.8% of the total deposits and 63.5% of the bank credits of the all nationalized banks including the State Bank and its subsidiaries. The estimated position of 14 Nationalized Banks, State Bank of India and subsidiaries in respect of the deposits during 1970 were as follows:

**Table - 1**

**Bank Deposit during 1970:**

<table>
<thead>
<tr>
<th></th>
<th>Rs. in Crores</th>
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<tbody>
<tr>
<td>14 Nationalized Banks</td>
<td>3,051</td>
</tr>
<tr>
<td>S.B.I.</td>
<td>1,177</td>
</tr>
<tr>
<td>Subsidiaries</td>
<td>322</td>
</tr>
<tr>
<td><strong>TOTAL</strong></td>
<td><strong>4,550</strong></td>
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*Source: Banking in India, Panandnikar.*

From the above figure it is clear that during 1969 (post nationalization) very few banking business was left to handle
by private sector. These banks were left open to run their business among small borrowers, small business and small industrialist. The exact figure of deposits of these banks was nearly Rs. 95 crores as in July 1969.

The main cause of nationalization of banks have been stated as to include the enlargement of resources for economic growth, the development of Agriculture and Industry in backward regions as well as making bank credit available to priority areas which had generally been neglected. To fulfill such objectives, the government felt that the lending policy should be governed by the government rather than by few monopolist shareholders who in the past divert bank resources to their self-desired channels ignoring the needs of the country’s economic planning. In this way the use of bank money for purposes of speculative activities and unproductive works shall be eliminated. The bank resources shall be utilized for encouraging new entrepreneurs. It is also proposed to secure professional standards in bank management and provide adequate training facilities for banking personnel by assuring reasonable terms of employment for the banking industry’s staff.
Economic Justification:

When we study pre-nationalization scenario we will find that the commercial banks were always favoured their lending for industry, trade and commerce in which their directions them self were interested, but they always deliberately neglected the requirement of the farmers artisans and small scale entrepreneurs because they were not interested to finance these community of the country due to the fact that they would not be benefited in person. The distribution of bank credit to these above sectors viz. farmers, artisans and small scale entrepreneurs, shows that only a negligible share of the total advances by the banks were made available to the said sector while the fact was that the govt. had always emphasized priority for them (farmers artisans and small scale entrepreneurs).

Further findings shows that the divergence of the commercial bank's credits for financing the farmers in the absence of adequate farm-finance from cooperatives was under the policy of the govt. to initiate for social control and effective measures to be adopted for Agricultural development though financing it by commercial cooperative
banks where as commercial banks complied with the formalities of reconstituting their boards in the desired manner, they reduced the size of the book-loan from 10.1% to 3.1% in 1968. They sanctioned additional credit limits to Agriculture and small scale industries and introduced new schemes to assist farmers. But these commercial banks explain their reasons to govt. that due to mass illiteracy of village peoples, unsuitable conditions, inadequate and practically nil transportation their staff are not willing to go to rural areas such social control could not compel these commercial banks to open their branches in such areas. In other condition there was around 2000-2300 crores Rs. was estimated to finance the agricultural needs and it was clear that even only 40% of farmers requirement can be fulfilled by these commercial banks and cooperative societies by March 1974.

Performance Appraisal:

(a) Banking in India after nationalization:

The history of the banking system in India has been changed by the nationalization of 14 commercial banks in 1969. It added a new chapter of progress and development
in banking system. At this juncture the banks were required to transform themselves into an instrument for social development and well being. These objectives were achieved only by expansion of their branches and penetration of the rural and semi-urban areas, explicit recognition of banks as an agency for mobilization of savings and development of the money-market, promotion of the banking habits and exploration of new avenues for credit deployment, especially for the benefit of the weak and under-privileged sections of the community.

It was observed that there was a remarkable change in banking both geographically and functionally. A largely implemented branch expansion programme with a major concentration to villages and remote areas surrounded by millions of small borrowers, attempts at decentralization of power and delegation of authority, introduction of special credit schemes to meet the credit needs of majority engaged in small but gainful business, and shift in emphasis from security-oriented lending to production-based lending are all indicators of revolution in banking system.
The major achievements of the banking industry in the first decade (1970-80) can be explained as follows:

(i) Tremendous improvement in branch expansion. It was 8262 in 1969 and raise to 30,303 in June 1979.

(ii) There was 65000 population per branch in June 1969. It decline to 18000 per branch in June 1979.

(iii) The inter-state disparity in the availability of bank offices declined from the highest of 4,97000 and the lowest of 7000 persons per bank office in June 1969 to the highest of 35000 and lowest of 3000 per bank office in June 1979.

(iv) Level of deposit mobilization of Nationalized Banks rise 488 percent till 1979.

(v) Public sector bank advances to priority sectors increased from Rs.441 crores covering 2.6 lakhs accounts in June 1969 to Rs. 4791 crores covering 89.1 lakh accounts in December 1978.

(vi) Public sector bank's advances under the differential rate of interest scheme, increased from Rs. 87.7 lakhs
covering 26,202 borrower, accounts in December 1972 to Rs. 103.17 crores, covering 17.57 lakhs borrower accounts at the end of March 1979.

The major achievement of banking sector after nationalization was fast growing branch network throughout the country. The main thrust of banking administration has been towards making credit available to those sectors of society which have all along been neglected by the security-oriented banking system which used to operate mainly from metropolitan and urban centres. The hitherto neglected sectors have now been given priority and government has deliberately adopted the policy that bank credited should be available to small scale agriculture so long dependent on village money lenders. Similarly, priorities have been specifically allocated to artisans and small scale industrialists, operators of transport services and those who are self employed. By and large, bank advances to these sectors, which stood at about 15% of their total advances in 1969, had exceeded 26% of total advances by June 1975.

After nationalization various policy initiative have followed, lead bank scheme was the first measure which
implemented. In this schemes specific commercial bank allotted the responsibility of a specific district where they have to provide all the banking facilities and initiative for process of other developmental activities of the same district. All of the 338 rural districts in India have been allotted to specific lead banks. So far survey reports have been received with regards to 330 districts.

Since nationalization the branch expansion was given highest priority, on an average about 1800 branches have been open annually. It is fact that the principal hindrance of Indian economy is that it is not monetised and it can only be fulfilled by providing adequate banking services. The total absence of banks in vast tracts of the country inhabited the development of modern financial discipline. Therefore it is very important to make a drive to take banks to unbanked or under banked areas. There is a need to bring banking not only door to door but also invite public for taking maximum participation in fund mobilization. After nationalization all these hindrances were near about removed further. After nationalization there was introduction of several schemes for fulfilling the needs
of backward and weaker section of the society. Under such schemes loans were given to the backwards at differential rates of interest. On March 20, 1972, it was announced that a specified weaker sections of the society would get loans at 4%. The scheme has since been extended to all districts where the agriculture ministry offers special assistance because of backwardness so that practically 265 out of 338 districts of India covered by the scheme. There was provision of maximum limit of working capital provided under such scheme. The maximum amount was Rs.1500 for working capital and for loan the amount has been fixed at Rs. 5000 .Persons engaging paid labor on a whole time basis are ineligible under this scheme. The progress under the scheme upto the end of June 1975 was that an amount of Rs. 148 million had been loaned approximately to 347,152 persons.

Before 1969 (Pre-nationalization era) it was observed that the concentration of business was restricted to only metropolitan and urban areas, where large amount of bank credit and top management of major banks being held by leading business tycoons in the country. At that time loans
were sanctioned only on the basis of credit worthiness of the borrowers and viability of the schemes were ignored. The performance of a bank was judged by the amount of profit it made and the dividend it declared. Under such condition it is clear that, it was very difficult for entrepreneur or a small farmer to procure credit even if he had a viable schemes. It was surprisingly to know that the agriculture, which employed about 70% of the labor forces and contribution of about 50% of the national income got only 2% of total bank credit. There was a thinking among commercial banks that they were not to serve the interest of farmers, small business and rural artisans. After considering all such problem govt. plan to do the nationalization of some of the major commercial banks.

By the end of June 1969, the commercial banking sector consisted of 72 scheduled commercial and 16 non-scheduled banks out of the 72 banks, 8 banks - State Bank of India with its 7 subsidiaries, were in the public sector and there were 49 Pvt. Sector banks, 15 foreign and 16 non-scheduled banks. Fourteen banks (Commercial) with deposit of Rs. 50 crores and above were nationalized in June 1969.
In further development on nationalization on April 15, 1980 the govt. of India nationalized six more commercial banks having more than Rs. 200 crores of total deposits, and now 91% of total deposits came under the nationalized banking sector of the country only about 4.5% banking now remain in the private sector.

At the time of first nationalization, the total deposits of all commercial banks stood at Rs. 5000 crores and about 31000 crores Rs. at the end of 1978. In case of schedule commercial banks the deposit is around 27250 crores. The 14 nationalised bank and SBI and its subsidiaries alone share of Rs. 24,262 crores. Now the total balance of about 2988 crores Rs. in which the six neatly nationalised banks holding was Rs. 1,903 crores which is about 63.6% of the non-nationalised and non-public sector of the banking industry. The credit facility provided by the six newly nationalised banks at Rs. 81,174 crores at the end of 1978 formed 6.4% of the total credit of Rs. 18,350 crores of all commercial banks and 48.7% of the total credit of Rs. 2,412 crores of all the non-nationalised non-public banks.
The performance record after nationalization was not satisfactory during seventies. It has created a serious credibility gap with respect of public ownership and control by govt. Indian economy faces severe setback during this period. The rate of inflation was too high drought and acute poverty problem was high in the country, and the first phase of nationalization doesn’t prove much effective. It was only a walk of power struggle and the radicals led by Mrs. Gandhi who swore by socialism and Gharibi hatao andolan. People were having faith in public philosophy that the assumption of comminuting heights by the public sector was synonymous with advancement towards social justice. This philosophy now turned out to be hollow. Under such circumstances the nationalization of six more banks on April 15, 1980, draw very poor response from economist even the then FICCI President comments on the second phase of nationalization that, this decision is not only bad as well as sad, because, when many urgent problems are crying out for solution of which improvement in the services of nationalised banks is one, the govt. should not waste their energies in this type of exercise and bad because at this juncture it will disturb the investment climates.
After the nationalization of six more banks, it can't be ignored that the additional sum of Rs. 945 crores more will now be available for credit allocation to agriculture and other priority sectors. When we study the following figure we can see that these six banks contribute about 30.9%. Whereas previously nationalised, 14 banks contribute 30.4% to the priority sector till December 1978.

**Branch Expansion After Nationalization:**

The branch expansion programme was one of the major agenda of nationalization. The Prime Minister Mrs. Indira Gandhi clearly indicated in her speech on July 19, 1969, that bank can be a source of financial facilities to the self-employed persons, farmer and other small and neglected areas of the society. Therefore, it was clearly indicated that the branch expansion programme must be of paramount importance in whole agenda. Therefore, the most obvious achievement since nationalization of banks, has been the spread of banking branch network throughout the country. Therefore, the total number of branches of commercial banks has increased from 8262 in June, 1969 to 30,303 in June 1979. As a result of their rapid expansion, the average
population served by each branch has came down from 65,000 in June 1969 to 18,000 in June 1979 of this public sector bank alone 79% of the total banking facility provided by the commercial bank till 1979. This shows that branch expansion programme gained real pace after the nationalization.

The average population served per bank office at the time of nationalization was 65000 approximately and it comes down to 17000, December 1979. There was clear improvement in some bank shared states, like Assam, Bihar, J&K, U.P. as compare to 1969, the population per bank office in Assam has come down from 1.98 lakhs to 33000 has come down from 1.98 lakhs to 35000 in June 1979 in Bihar from 207 lakhs to 35000 in Orissa from 2.17 lakhs to 31000, in Jammu & Kashmir from 1.14 lakhs to 12000 and in Uttar Pradesh from 1.19 lakhs to 26000.

It was observed that in the year 1978-79 commercial bank open 2,191 offices. They have prefer Assam, Bihar, M.P., Orissa, U.P. and W.B. Thus we can say that the growth of branches was very rapid after nationalization.
It became quite clear that the nationalization of 14 banks in 1969, laid great emphasis on the coverage of unbanked centers by banks as compared to the pre-nationalization period. This is clear from the data available that commercial banks in India open around 22,090 branches in between the year 1969-79 and out of this, 11,373 offices were opened in unbanked centres which comprise more than 50% of the total bank offices, during this period. Nationalized banks alone have opened 9,379 branches in unbanked centres which is 82.5% of the total branches opened in unbanked centres. While 54.2% were situated in unbanked centres as against 57.5% in case of commercial bank since July 1969.

As per the Government decision that there must be at least one office in unbanked area, latest by June 30, 1979, the commercial banks had opened offices in 619 blocks out of 697 unbanked community development blocks in the country, till June 1978.

Under the branch expansion programme of commercial bank since nationalization, there is a distinct shift in favour of areas designated as rural population up to 10,000.
Therefore such rural branches increased from 22.4% in June 1969 to 44.1% in June 1979. There was around 13,333 rural branches till June 1979. As per government decision that, there should be one branch per 10,000 population in rural areas, there must be around 32000 additional offices are needed for, then rural population of around 450 million. It was also witnessed that, when the share of rural branches increased from 22.4% to 26% during 1969-79. If we take “rural” and “semiurban” areas together the increase in their share to total bank branches appears very ineffective it increase from 62.4% in June 1969 to only 70.1% in June 1979. thus we can say that the increase in rural branches since nationalization has taken place at the cost of semi urban centres, whose share of branches come down from 40% in June 1969 to 26% in June 1979.

If we make an analysis of new rural branches in total new branches opened after nationalization, we find that it has declined from 66% in 1969-70 to 35% in 1976. The percentage share of new rural offices in total new branches has declined rapidly after 1970-71 to 1975-76 During the
same period, the share of new rural branches in total bank offices has increased from 35.4% to 51.5% in 1976-77, which is partly because of the establishment of Regional Rural Banks in October 1975 and imposition of internal emergency in June 1975.

After the implementation of new branch licensing policy, formulated by R.B.I. in September 1978, about 45000 new offices were opened up within 1978-81. The formula for branch licencing in force since Jan. 1, 1977 stipulates that a bank will have to open 4 offices in the embarked rural areas to get an entitlement to open one office in a metropolitan and one office in a baked centre. This is known as 4:1:1 formula.

The needs of the rural sector including small scale and cottage industries would be adequately taken care of by the spread of bank branches.

Impact on Priority Sector After Nationalization:

Beside branch expansion and availability of banking services to remote area, priority sector was also one of the major target of nationalization of Banks in India. Because
priority sector was the most neglected area in pre-nationalization area. The credit facilities were available to only those who are directly related to the banks and very low risk area because of high risk and non-availability of participation in key position of banks these areas were neglected by the security oriented banking system which used to operate mainly from metropolitan and urban centres. Therefore, the neglected sectors like artisans, small scale industrialists, operators of transport services and farmers were provided highest priority, for credit distribution.

As we know that the different sectors of the economy like Agriculture industry, trade, transport-services, education etc. are inter-related to each other and simultaneous development of all these sectors are guarantee of rapid economy development in country in long-run. However at any time a particular sector or one or two of these sector is may be more important than the others either as the leading sectors in realising certain immediate and short run objectives or as the limiting sectors which obstruct the realisation of such objectives like increasing production,
containing inflationary pressures of generating employment opportunities such sectors are then designated as the priority sectors of the economy, though at some other point of time some other sectors may assume a strategic role and may come to be called the priority sectors. The role of agriculture, cottage and small scale industry, retail traders, small businessman, water transport undertakings, education and self employment, are considered to be the priority sectors because they play major role in accelerating the rapid and long-term development of the Indian economy, these sectors are designated as the priority sectors of the economy. For the growth of priority sector it is important to make available the sufficient credit at low rates of interest. The nationalization of banks in particular proved very helpful and since 1969 all the nationalized banks and other commercial banks in general are asked to mobilise funds at large to meet the credit needs of these sectors and from help to the growth of Indian economy.

When we study the trends of scheduled commercial banks to advances to priority sectors from 1969 to 1978 we find that the share of priority sectors in the total credit
advanced by the scheduled commercial banks in the country has been steadily on the increase except for the two years 1976 and 1977 since 1969, from 14% at the end of June 1969 to 27.1% at the end of June 1973. The incremental ratio is still higher at 30.9% at the end of June 1978, showing thereby that 30.9% of the additional credit granted by the scheduled commercial banks in the country since 1969 has gone into the priority sector in the economy. At the end of June 1978 we see that the small scale industries get highest share around 78.9% of the total credit available to priority sector.

In March 1979, the govt. of India suggested to the banks that they have to direct their one third of the total credit to the priority sector. Such type of suggestion cause rapid development in priority sector and clearly visible in agriculture sector, which gives desired result in recent year.

**Impact of Nationalization on Banks Profit:**

By the analysis we find that during 1970-71 there was increase in profits and in 1972-73 the trend become dealing in the profitability of the operation of scheduled commercial banks in the country, as is indicated by the percentage ratio
of their aggregate profit to their aggregate credit. During 1974 and 1975, situation became better compared to 1973 and then deteriorating again in 1976-77. Reserve Bank of India mentioned this decline, because of the profitability of bank became slower in growth of earning as a result of a relatively lower bank credit expansion during the year in Nov. 1976, the increase in liquidity requirement of banks and imparting of a part of the incremental deposits from January 1977. It may be pointed out that in view of the need to mobilize a still larger share of their resources to the priority sectors of the economy and to the weaker sections of the society.

Financing of the priority sectors on an increasing scale required to meet the needs of rapid economic development, price stability and social justice criticism may raise if the nationalization proved at the cost of profitability and efficiency.

The diversion of larger bank credit into these sectors of the economy requires that the commercial banks should give up the traditional commercial loan, while deciding loan and should make the purpose of the loan, rather than the
formal security against it to be the deciding factor while assessing a loan application. The banks are prepared to sacrifice 'private profitability' in favour of the social importance and necessity of the project finance from the point of view of attaining the various socio-economic objective of the economic planning in the country. It may be pointed out that this total preoccupation in the past, of the Indian commercial banks with "profitability" that had been partly responsible for denying the priority sectors their genuine need for banking credit, since the financing of these sectors is subject to a higher degree of risk of default and lower profitability when compared with the financing of large scale industry and commerce, which are the traditional sector as commercial bank operations in India. After consideration of priority sector the definition of profitability of the banks reinterpreted in order to include in it the socio-economic importance of the purpose of the lone. There are lots of difficulties in financing the priority sectors. The major difficulty face by the banks in diverting larger bank loans to the priority sector involves round the need for theoretical and policy changes, but it is easy to change policy rather than conceptual belief like security and
profitability of banks. As we know that the traditional concepts are easy to implement rather than modern concept of fast growing economic and social concept. There are further lots of other difficulties arises after loan sanctioned. It is difficult task to supervise the agriculture loan, borrowed by the cultivation dispersed all over the village often at long distance from the lending bank office, and in their circumstances the user may be liable to put loans in unproductive uses, resulting in mounting debts apart from the waste of scarce resources from the social point of view. Therefore to overpower such circumstances banks are needed to have extra staff which ultimately cause extra overhead expenditure to the banks. Ultimately diversion of high amount towards priority sector will divert the banks attention from their traditional customers who are profitable and strength of the banks may cause heavy loss. All the points indicates that it is good to divert the attention towards priority sector but traditional sector should not be ignored because their strength know the banks. So banks should make their policy which is security friendly as well as profitable to the commercial banks. Such a participation will accelerate the commercialisation of Indian agriculture, a
trend that has recently set into the Indian agricultural system, so as to increase the marketable surplus of food grains in the country required to feed its non-agricultural population and possibly even for export. It will help in providing the banking habit among the rural peace and in mobilising rural savings for the purpose of capital formation and economic development and enable the Indian commercial banking system to fulfil its socio-economic obligations in the context of the rapid economic progress of the country.
References:


