CHAPTER II
Banking is an instrument of making capital more productive to accelerate renewal of wealth. The focus of this chapter is primarily on the experience of commercial banks during the post-nationalisation period. A brief overall view of the significant changes in the organisational structure of banking is discussed. Further, the salient features of banking are studied to highlight modern view on the banking sector.

Definition

The word bank is derived from German word Back meaning a joint stock firm. This word was also derived as Banco. This Italian word banco means a bench where merchants huddled and conducted their business by bartering each other's need. The barter system gave away to money economy and money became the medium of exchange.

Modern Banking

Banking in India is of ancient origin. The modern banking took its birth seven decades ago. "Banking was known and practised in India at a time when the rest of the world had yet to evolve a medium of exchange in the form of money". The bankers first in the form of money lenders were followed by the indigenous bankers and, later commercial banks came into being which have been playing a decisive role in the economic life of India.

The three Presidency Banks namely the Bank of Bengal (1809), the Bank of Bombay (1840), and the Bank of Madras (1843), were amalgamated in 1921 and formed the Imperial Bank of India. The Banking Regulations Act 1949 came into force on March 16, 1949 to promote and develop banking industry on right and sound lines. The main motto of the Banking legislation is to promote and develop commercial banks. Nationalisation of the Imperial Bank as State Bank of India on July 1, 1955 by the SBI Act, 1955, conversion of the state-partnered commercial banks as subsidiaries of State Bank of India on September 10, 1959 by the SBI subsidiary Act, 1959 and nationalisation of fourteen commercial banks on July 19, 1969 as well as six more commercial banks on April 15, 1980 are some important steps taken in the post - RBI Act in Indian banking. The Reserve bank of India is an autonomous institution. It is the apex body. There is no exaggeration to say that the Reserve Bank is just a wing of the Union Finance Ministry. As the lender of last resort, the Reserve Bank has no choice but to foot the huge deficits that the central Government runs up every year.

The Indian scheduled commercial banks can be classified into: public sector commercial banks and private sector commercial banks. The former meets the prescribed national goals, and come into the direct purview of various credit control measures of the Reserve Bank of India. The latter differ from the organised joint-stock banks except lending loans, they do
under take banking services very little. Many important steps, have taken in Post - Reserve Bank of India Act in banking industry to make available banking services even to a common man.

OBJECTIVES OF BANK:

The main objective of a commercial bank is to promote the economic growth and development with equity. The specific objectives are being achieved through:

1. Means and mechanism for effective use of resources
2. Mobilising savings and deploying them in accordance with the national priorities
3. To associate with the adoption of technology and national programmes ensuring higher production and thereby strengthening the national economy. In other words, to improve the economic life of the people
4. Engulfing credit gap
5. Associating in national programmes for higher production
6. To subserve the social goals of planning

FUNCTIONS OF BANK:

The organisational set up of any institution depends upon the functions that it undertakes to perform. The history of banking discloses that it was essentially trade-oriented. The commercial bank has slowly expanded and, diversified its functions embracing the aspects of economic activity. Basically
bank undertakes two activities namely (i) receiving deposits and repaying on demand or at a stipulated time in future (ii), deploying funds for the promotion of the economy.

Deposits provide a major cushion to the banking industry. About 80 per cent of investible funds come from deposits. But, to meet the ever-increasing demand for financing and expanding credit economy, a high degree of concentration is to be placed on deposit mobilisation. Banks should promote the saving habit among the people and collect their savings which are small, idle and scattered, otherwise the banks could not augment the resources needs for the development of economy. They have to expand, their branches in the rural areas to increase the production of rural sectors, so also to increase deposits.

The basic cause that hinder the phenomena of economic development is inadequate resources and lack of effective use of available resources. Deployment of funds effectively in the different sectors of economy is the major function of the commercial banks. The repetitive and continuous effective lending lead to the function of "multiple credit creation". Besides these two functions, the commercial banks perform agent functions 2 as well as utility functions 3 to render services to their clientele.

2. Such as payment and receipt of subscription Premia, rent purchase and sale of shares, stock, debentures, bonds and act as a trustee, an attorney etc.

3. Such as safe - vault, credit instrument, referee, etc.
ORGANISATION:

A banking company has no physical existence of its own, so, it cannot act by itself. Human agency is needed to pool together various means to achieve an end. The term organisation means the process of arranging, allocating and bringing the relationship among money, men, material and machine. A sound organisation will solve every business problem; a poor organisation could run a good problem, and a good organisation with a poor product could run a good market. Vasant Desai stated: "A well developed banking structure is an essential prerequisite, and the options of such structure had often impeded the growth of economy".4

SOCIAL CONTROL:

The Indian economy primarily rests on the rural economy. Banking was largely reflected in the development of the privileged class people neglecting the masses. Rural borrowers become a prey in the hands of money lenders, they can never get rid of the debt set up by the so called money lenders. This had become a chronic ailment and consumed the main tissues of the national economy. Therefore, the commercial banks involvement in the national programmes is to be in consonance with the welfare of the people. Then the Government of India fathomed the development pattern of the States, regions, sectors and people.

Such pattern led to the widening of the imbalances and to the aggravations of the unemployment problem. So the policy of social control over the commercial banks was introduced on December 14, 1967 with two objectives (1) wide spread of bank credit 2) engulfing the regional and sectoral imbalances.

The National Credit Council was set up by the Government of India on December, 22, 1967 to serve the socio-economic objectives of development. The National Credit Council started functioning on February 2, 1968. But the credit allocation to the potential sectors was not achieved to the expected level. So, there is a need to control the ownership of the big commercial banks. As a result, fourteen commercial banks, each with deposits of more than Rs. 50 crores, were nationalised on July 19, 1969. Again six more commercial banks, whose deposits amounted to more than Rs. 200 crores, were also nationalised on April 15, 1980. The main objectives of bank nationalisation have been removal of control by a few, provision of adequate credit for agriculture, small scale industries and exports, encouragement of new classes of enterpreneurs and giving a professional bent to the bank management. The nationalisation of commercial banks, thus, was a "revolution in the Indian banking sphere."}


Mrs. Indira Gandhi’s statement at the congress working committee meeting in Bangalore is worth mentioning: "Nationalisation was a significant step in the process of public control over the financial institutions which are the most important levers that any society has at command". The preamble to the Ordinance stated that nationalisation was necessary in order to serve better the needs of development of economy in conformity with national priority and objectives. Nationalisation was a major instrument of policy to direct credit to specific areas; improving the rate of deposits by increasing the savings potential; extending the volume and scope of credit disbursement; implementation of specific anti-poverty programmes like the Integrated Rural Development Programme (IRDP) and so on. Of all these, the main two issues are.

1. Profitability and balance sheet parameters.
2. Customer service and expectations.

PROFITABILITY AND BALANCE SHEET PARAMETERS:

Profitability considerations have never been paramount in the first twenty odd years of nationalised banking. So much so adequate in attention has been paid to the pricing of the services. The other side to the neglect of profitability has been fostering of a belief among the customers that a bank’s costing of any service has lead to the belief that the bank’s services need not be priced any higher.

Customer Service and expectations:

There are very few absolute standards relating to customer service. The notice board announcements in most branches of the nationalised banks indicating a specific time frame for each of the major activities are pathetic attempts by well meaning but innocuous bank administrators to maintain a semblance of management: their regular breach causes consternation to no one except to some customers. In defence of the Public Sector Banks as a whole it must be said that since more than nine out of ten branches belong to one of them there is a real problem of over exposure leading simultaneously to higher expectations and lower standards of service.

After nationalisation the credit policy of the bank has undergone a major change. Nationalisation of banks has placed thousands of crores of rupees at the disposal of the Government as additional resources. Many banks have created export cells, small scale industry advisory panels and opportunities have been offered to unemployed technical graduates to get self employed by giving not only to financial but also technical aid. After nationalisation, the lead bank system done wonderful service to the agriculture, small industries and other priority sectors.  

The specific objectives of nationalisation of the commercial banks are:

1. To tap deposits on a massive scale.

2. To generate gainful employment on a much larger scale than before.

3. To deploy funds for productive ends of diverse types irrespective of the size and the socio status of the borrowers.

4. To encourage new entrepreneurs and contribute to the development of all backward areas.

5. To secure balanced development.

6. To act as catalyst in feasible development programmes in as many sectors of the economy as possible.

7. To ensure professionalisation of banks.

8. To achieve organisational and functional reorientation of the banking sector to accelerate faster growth.

9. To extend services to the general public.

Banking Policy:

A policy is a direction to achieve the objectives fostering economic growth and development. An organisation without definite policy is like a ship without rudder". A basic policy guides the executive management in its conduct. An

institution's competence and capacity are reflected in the policy. The Reserve Bank of India is policy making body and an organisation of higher control. Koontz and O'Donnel have described the policy as "a general statement or understanding which guides or channels the thinking in decision making of sub-ordinance". The executives should carry out the business in accordance with these policy guidelines. Balanced growth with rapid development is a salient feature of widening and deepening banking services. The objectives set the goal and the policy shows the way towards the goal. The policy should be (1) made in consonance with the objectives (2) feasible and possible, (3) with temporal dimensions, and (4) with stock environment dimensions.

"The aim of Policy should be to facilitate the beneficial use of credit and to restrain its potentially harmful effects". The policy guides thinking and actions in decision making. A lukewarm policy was adopted till 1956 and therefrom a liberal policy was adopted in branch expansion. In 1977 a new branch expansion policy came into existence with stipulation that a bank will have to open four branches in unbanked rural areas to


get permission to open one branch each in metropolitan and banked centres. This policy was to be known as 4:1:1.\textsuperscript{12} This policy was expected to snap the dictum flat: 'Real India lies in Rural India'. Nationalisation led the progressive credit policy which aimed at envisaging extension of banking services to priority and neglected sectors on preferential terms and conditions. The programmes are:

1. Rural development and anti-poverty programme.
2. Employment programme.
3. Industrial development programme.
4. Production programme.

RURAL ORIENTATION:

Economic development is a complex process which needs higher level of activity of all the interrelated sectors - Integrated Rural Development Programme (IRDP) giving keen participation to weaker sections. The commercial banks have to pool their resources and to cater to the needs of the society on social justice. The commercial banks would think of even organising adult education programme for the weaker sections. So financing of all rural or agricultural economic activities for rural economic development is the task presently laid on commercial banks.

PRODUCTION - ORIENTED:

Credit is not a subsidy or relief but is be repaid from the income earned by the assets created. To create credit absorption capacity in rural areas especially in backward areas where agriculture is generally the main economic activity, the interrelated bankable schemes for the rapid growth of the main sector of the economy have been prepared. The Reserve Bank of India enunciated and encouraged the adoption of production oriented philosophy in sanctioning loans by the commercial banks. This undermines the influence of the concept of security based credit; and many people particularly weaker sections being covered under it. Further, the schemes like dairy, poultry farming, sheep rearing etc., have been developed to augment the income of weaker sections.

CHANGE CONCEPT:

The banking sector today is entirely different from what it was two decades ago in quality, style and range of services offered by it. This revolutionary change and the dramatic transformation that have taken place in the portfolio of Indian banking since nationalisation 1969, speak highly of the banking system's dynamic response to the challenging tasks set before it. To meet the challenge (i.e. change) is a sign of good management. The challenge is to end exploitation of the poor by the rich, of the masses by the privileged classes, of the weak by the strong, of the villages by the town and of social justice by the
monopoly. Further, the economic development entirely hinges on rural development which is multi-dimensional activity requiring multi-pronged approach. Towards this end, the commercial banks have undertaken various programmes.