An Historical Analysis of Nationalization of Commercial Bank and Its Role in Financial Inclusion

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Abstract— A bank refers to a financial institution which receives funds from the public and gives loans and advances to those who need them. The Indian Banking Regulation Act of 1949 – Section 5 (1) defines bank as "Accepting of deposit of money from the public, for the purpose of lending or investment, repayable on demand or otherwise and withdrawable by cheque draft, order or otherwise". Section 6 of the same act states that, a bank apart from above foresaid functions provides various subsidiary services to customers such as collection of cheques, drafts and bills, remittance of fund, acceptance and safe custody deposits etc., But the above definition was not comprehensive, as it didn't include all branches of activities that a bank performs. Therefore definition of Sir John Paget is considered to be the comprehensive one, which quotes "No person or body corporate or otherwise can be a banker, who doesn't take deposit account, take current a/c, issue and pay cheques and collect cheques, crossed and uncrossed, for his customer and one claiming to be a banker must profess himself to be one, the public must accept him as such and finally banking should be his main business". There are many types of banks, like industrial banks, agricultural banks, exchange banks, commercial banks, etc. The ones we generally refer to are commercial banks. They perform all forms of banking businesses and deal in financial trade and commerce. The First Commercial Bank, "Bank of Hindoostan" was established in India in the year 1770. But it was maintained and managed by Britishers. The first Indian commercial bank was "The Oudh Commercial Bank" and was established in 1881. During this time, the Britishers, for the convenience of administration had divided India into three Provinces. They are Province of Bombay, Culcutta and Madras. In each these province, they had established a Presidency Bank. Later, these three presidency banks were merged into one and named as "The Imperial Bank of India' on 27th Jan 1921. Later on this Imperial Bank of India was nationalised and renamed as 'The State Bank of India' on 1st July 1955. This was the first commercial bank, nationalized in our country. Nationalisation is a process of taking over the control and ownership from private to government. The process of nationalization was inevitable, because, these private commercial banks were flooded with numerous drawbacks. Therefore, this paper makes an attempt to highlight, the intention and objectives of nationalization, which primarily aimed at financial inclusion, bringing and offering banking services to the masses.

Index Terms- Banking sector, Customer, Accessibility of services, Nationalisation, Ownership.

I. INTRODUCTION

The Indian banking system, at the time of its attaining independence, had a well developed mechanism. It had 645 banks with more than 4,800 branch offices. However, the role of these banks did not extend to meet the societies' social needs. While these banks could cater to the requirements of the big industries, the desirable sectors like agriculture and small scale industries were often neglected. Therefore, nationalization was observed to be only panacea for achieving national equality. Some of the prominent reasons, which led to nationalization of Indian banking sector were:

Removal of private ownership of commercial banks and concentration of economic power: Prior to nationalisation, banks were controlled by business houses which used the savings of the public for their own personal benefits by financing selected projects that would benefit them. This resulted in concentration of wealth in the hands of a few. The small units and other priority sectors were deprived of funds. Thus, it was important to nationalise banks in the interest of the country.

To reach out to non urban areas: Prior to nationalisation, branches were opened in cities, thus neglecting the semi urban and rural areas. This not only led to concentration of banking facilities in urban areas, but also in depriving these facilities to a major chunk of our population. Out of about 5.6 lakh villages in India, only 5,000 were served by commercial banks. Ahmadabad, Mumbai, Kolkata, Delhi and Chennai

had about 1/7th share in the number of branch offices and 50% share of bank deposits and bank credit. This led to the slow growth of the rural areas.

Low advances to agricultural sector: The banks advanced finances to commerce and industry, increasing their share in the scheduled bank's advances from 70% in 1951 to 87% in 1968. Agriculture accounted for only 2.2% of the total advances.

Violation of norms: Commercial banks often granted loans to those industries which did not appear in the priority list. This was against the norm and priorities laid down in the plans.

Speculative activities: Commercial banks encouraged socially undesirable activities like hoarding, black marketing, etc. against high rates of interest.

Ignoring the priority sectors: Apart from neglecting the agricultural sector, the needs of other sectors such as export, small-scale industries etc. were unmet.

Objectives of Nationalisation

The objectives of nationalisation were as follows:

- Removal of control by a few
- Provision of adequate credit for agriculture, small scale industries and export sector
- Encouraging a new class of entrepreneurs
- Giving a professional touch to management
- Provision of banking services in backward areas by opening new branches
- Enforcing discipline in the commercial banks and complying with national priorities

Therefore, when Indira Gandhi was the Prime Minister of the country, her government took one daring decision of nationalizing 14 commercial banks, who had a total deposits and reserves of 50 crores of more than that. (1) Central Bank of India (2) Bank of India (3) Indian Bank (4) Union bank of India (5) United Commercial Bank (6) United Bank of India (7) Dena Bank (8) Syndicate bank (9) Punjab National Bank (10) Allahabad Bank (11) Bank of Baroda (12) Canara Bank (13) Bank of Maharashtra (14) Indian Overseas Bank – these 14 commercial banks were nationalised on 19th July 1969.

The process of nationalization did not stop over here. Instead, the on a large scale, the second phase of nationalization started again on 14th March 1980, the Government has nationalised 6 more commercial banks. They are: - (1) Punjab and Sindh bank (2) Vijaya Bank (3) Andhra Bank (4) Corporation Bank (5) New Bank of India (6) Oriental Bank of Commerce. This time the criteria was, those banks, which had a total deposits and reserves of Rs. 200 crores or more than that. But later on New bank of India was merged with Punjab National Bank. Hence finally, the total number of nationalised commercial banks is 19.

Progress after Nationalisation

After nationalisation, the Indian economy has seen a growth in the branch network of commercial banks. These developments have been highlighted in the following points.

- *Expansion of Branches:* It was 8,262 in 1969. It has increased to 1,11,723 by the end of 2012. As a result, the average population served per bank office, which was around 55,000 in 1969 has come down to 12,000 in 2013, further to less than 10,000 in 2016. This increase shows a better reach of banking facilities to the general masses, which is the prime objective of financial inclusion.
- *Rural Branches:* Only 22% bank branches were located in rural areas in June 1969. It has increased to 38% in June 2015.
- *Deposit Mobilisation:* the aggregate deposits of commercial banks have increased from Rs. 4,665 crore in 1969 to around 93,27,300 crore in 2016. In terms of deposit mobilisation, Maharashtra state leads all other states with 22% of the total deposit mobilisation of the country. followed by Delhi, UP, WB, Karnataka, Andhra Pradesh, Tamil Nadu respectively.
- *Bank Lending:* It was 3,399 crore in June 1969 to more than 72,50,000 crore in 2015- 2016. Priority sector 15% has increased to 36% by March 2013.

These points indicates, positive growth and allowing the access of financial sector of our country to the general masses. This is a clear sign of 'financial inclusion'. Therefore, it is factually proved that, the process of nationalization laid the foundation stone for

financial inclusion in our country, around four decades ago itself.

- Shortcomings of commercial banking in India

Although commercial banks have come a long way after nationalisation of banks, they still suffer from the following shortcomings.

Insufficient growth: Though commercial banks have spread to every nook and corner of the country, their growth is still insufficient considering the huge population of India. Rural areas have just 38% of the bank branches where more than 70% population of the country resides.

Regional imbalances: States like Arunachal Pradesh, Jammu and Kashmir, Uttaranchal, Manipur and Tripura still have lesser number of banks on an average when compared to other states. Even in well banked states like Maharashtra, West Bengal and Tamil Nadu, if metropolitan cities are excluded, the population per bank office is larger than the average of these states.

Bad debts and over dues: Most of the commercial banks suffer from excessive over dues, bad and doubtful debts which have adversely affected the capacity of a bank to lend money. Bad and doubtful debts of commercial banks, called non-performing assets (NPA's) which were more than Rs. 50,000 crore in 1997-98 have increased to Rs. 70,000 crore in 2001-02. However, the gross NPAs have fallen due to strict credit norms followed by the banks. The gross advances also have fallen from 10.5% in 2001-02, 2.3% in 2010-11.

Deterioration of quality of service: With the passage of time, the quality of service rendered by commercial banks has deteriorated. This has affected their overall efficiency. Also the staffs are in disciplined and there is no proper system of accountability and control over the banks located in rural areas.

Falling profitability: Although the absolute profits have increased, their profitability ratio has fallen considerably. This is due to

- Lesser interest on Government borrowings from banks
- Subsidisation of credit to priority sector
- Rapid branch expansion
- Blocked funds in low-term, low-yielding securities resulting from directed credit programmes of banks
- Absence of competition
- Huge expenditure resulting from over staffing and mushrooming of non-viable branches

Lack of professionalism: Banks lack expertise in the areas of merchant banking and agricultural financing. There is a need of a professional approach in these areas.

CONCLUSION

The term 'financial inclusion' was explicitly used for the first time in the Annual Policy Statement for 2005-06. It observed that there were legitimate concerns in the banking practices that tended to exclude vast sections of population. To bring them under the banking services ambit, nationalized laid the foundation stone, as it paved the path and played key role in attracting the deposits and disbursing the loans to include vulnerable section in the financial services sector. The business correspondents have done their job as well by the way of linking the people to bank. Financial inclusion will strengthen financial deepening and provide resources to the banks to expand delivery of credit. The trend of increasing commercialization of agriculture and rural activities should generate greener pastures and banks should examine the benefits of increasing penetration therein.

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