

# Banking Industry: Nationalization and its impact on Public Sector Banks

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## Abstract: -

The economic prosperity of a country is greatly influenced by various sectors. Mainly, the Industrial Sector looks like the Growth Engine of the Economy. However, it is noted that, the Service Sector in India dominates all the other Sectors as it contributes as much as 58 % of the total GDP of India. Banking is the main Service Sector and life line for all the economic activities of every Sector. Indian Banking System has a long track record and Reserve Bank of India RBI is the apex of all the banks. Incidentally, Nationalisation of major Commercial Banks in India, which was a very turning point for the Banking Sector and the Economy as a whole has recently completed 50 years and much is being talked about the advantages and limitations of the same. This Research Paper is based on this situation to take a review of the impacts of Nationalization of Banks in India, In view of the present Lockdown situations, prevailing in India as well as worldwide, this research is based on the Secondary data only.

**Keywords:** - Nationalization, Basel Committee, Nirsimha Committee, NPA, Private Banks, RRB (Regional Rural Bank)

**Research Methodology:** -This research is carried on the basis of Secondary Data. The details of tables have been taken mainly from the website

## Introduction:-

Nationalization refers to an act of taking public control of an industry or properties. In the case of banks, this means that banks which were formerly in the private sector have been moved by an act of nationalization to the public sector. Privatization is the opposite of nationalization. The Indian banking system is currently split into commercial banks, cooperative banks, regional banks and so on. There are two kinds of banks in commercial banks: public sector banks, and banks in the private sector. The nationalization of banks is the biggest occurrence in the history of Indian banks. This made India the path to becoming the world's leading economies. The banking sector in India can be divided into three phases. Before 1947-1969, the pre-Independence stage was the second phase from 1969 to 1991 and the third phase from 1991 and beyond. A analysis of all three phases is taken into account in this research paper.

In the first phase, the banking system in India was getting established. Thus, it began with the foundation of the Bank of Hindustan in 1770. It operated till 1832. These were other banks like: Allahabad bank, Bank of India, Punjab National Bank, etc. Thus, the main event during this time was the evolution of banking as well as merger of the Presidency banks like: **Madras Presidency Bank, Bombay Presidency Bank and the Bengal Presidency Bank** were merged to form the **Imperial Bank of India**. Later on, it was named as the **State Bank of India**. The second phase is broadly known as the phase of nationalization of banks in India. The third phase was marked by the all-round development of banking system in India. This was due to the economic liberalization policies adopted by the Government. Many large and private banks came into the picture during this time and the entire banking scenario has changed.

### **Nationalization of Banks: A historical thread:**

The first bank in India to be nationalized was the **Reserve Bank of India** itself, which happened in January 1949. Further, the State Bank of India was established in 1955 with 8 Subsidiary banks to add to it in 1959. Later on, 14 other banks were nationalized in July 1969 such as, Bank of India, PNB, Bank of Maharashtra, Bank of Baroda and many others were the part of this nationalization process.

**The First Phase:** On 19th July 1969 14 main commercial banks got nationalized. This is was the major economic as well as political decision taken by the then Prime Minister Smt. Indira Gandhi. Thus, in India public sector banking started taking shape and a yeoman's role in the banking sector of India. Earlier to nationalization, the private banks were controlled by rich business houses. They used to exploit the poor public on the counts of deposits from them as well as extending loan facilities to them. After nationalization, all the banking system was overhauled, changed substantially and standardized. Both Deposit mobilization and loaning started on sound banking principles directed by the Government through RBI's controls. Branch Expansion was deliberately undertaken by all the nationalized banks. People started getting loans for small businesses, agriculture, housing loan, vehicle loan, travel and education loans too. This was the first time when the farmers got the loan from nationalized banks instead of the Savkars. The Savkari's at village was the same in the urban areas like big businessman's private banks which got cut down due to nationalization.

**The Second Phase:** Again in 1980, in view of rapid economic expansion with Government Objectives, another 6 major commercial banks were nationalized. The nationalized banks started branch expansion in rural areas. So their network was substantially increased. Total deposits of the nationalized banks increased by 92%.

While the second phase of nationalization saw 6 other commercial banks that were nationalized in 1980. These included Vijaya Bank, Andhara Bank, Corporation Bank, and others. The need for second phase of nationalization of banks arose due to many reasons. These banks were catering to the needs of big business houses and large industries. The moneylenders used to exploit the poor masses in India. Therefore, the expansion of banking network to reach to many such sectors was taken into consideration during the second phase of nationalization of banks. The **Regional Rural Banks (RRBs)** were formed. The objective was to serve large masses of the unserved rural population. Further, the specific requirements of sectors like foreign trade, housing, and agriculture were also to be met. This was taken up by establishing NABARD, NHB, SIDBI, and EXIM.

**The Third Phase:** Further, in 1991, Indian Economy got a very big blow of Economic Crisis. The Reserve of Foreign Exchange of the Economy reached to the bottom most level, sufficient hardly for the next fortnight. There was no other way but to accept strict economic disciplines, there was no other way, but to adopt ways of borrowings from the World Bank / IMF. In 1991 India got conditional loan on the

basis of 47 tones gold from the International Monetary Fund (IMF). This further led to the various economic norms; The World itself was undergoing a different Change all over. A new World Economic Order demanded for coming close called Globalization. Indian Economy also adapted the new Economic pattern called LPG which means adopting the Golden Terms: **Liberalization, Globalization and Privatization**. A natural outfall of this was the adaptation of economic policies in other field like Banking and Insurance. A lot of Private Sector Banks were permitted by the GOI like: HDFC Bank, ICICI Bank, IDBI Bank, etc.

### **Need to review the impact:**

On 19<sup>th</sup> July 2019 the first decision of nationalization of commercial banks has completed 50 years. In the history of Indian banking sector, the decision of Nationalization of series of banks is very important. Because of nationalization the banking sector has brought out the positive changes in the economy at various stages in these 50 years. Nationalization of banks also helped the general public to know the banking and adopt good banking habits. But what is the overall assessment of the banking sector after 50 years? A sea change is experienced by the banking sector after nationalization, LPG and the reorganizing of the World itself. The world of banking, particularly the nationalized banks have been experiencing a lot of total change in the reverence directions.

### **Comparison of Times:**

The Nationalization of Banks and then after for span of 50 long years can be analyzed on the following points of comparison:

### **Following were the reasons for nationalization of banks:-**

1. For the Social welfare of people
2. To control the private monopoly
3. Extension of Banking in Rural Areas
4. To reduce regional imbalances to prevent urban and rural classification
5. To give loans to priority sectors
6. To increase the mobility of savings

### **Impacts of Nationalization of banks:**

The performance of the banking system in India has increased because of the nationalisation of banks. This also boosted the confidence of the public about the overall banks system. The sectors that were lagging behind like Housing, small-scale industries and MSMEs along with agriculture got a boost. This led to an increase in funds and thus increases in the economic growth of India. Following are the important events during the span of last 50 years after nationalization of banks:

- 14 major Commercial banks were nationalized.
- Lead Bank Scheme was introduced.
- Credit Guarantee Corporation was established to cater the Priority Sector Lendings.
- Regional Rural Banks (RRB) were started in the light of the 20 Point Program of the Government.
- Six other major Commercial banks were nationalized in 1980

- Two more specialized banks – NABARD and EXIM bank were established.
- National Clearing Centre(NCC) was formed for MICR Cheques' clearing function.
- RBI took more active role as the Banker of Banks in India.

### **Important Contributions of the Narsimham Committee :**

Narsimhan Committee is yet another mile stone in the history of banking in India during last 50 years. The Narsimham Committees went into a detailed investigation into the causes of nationalized bank problems and identified the following problems & practice, as reasonable causes eating into the productive efficiency and profitability of the Indian Commercial Banks.

- 1) Directed Investment Programme
- 2) Directed Credit Programme
- 3) Interest Rate Structure
- 4) Subsidized Credit
- 5) Political and administrative Interference
- 6) Increasing Expenditure
- 7) Profitability of Indian Banks
- 8) Weakening of Banking Concept
- 9) Priority Sector Lending
- 10) Other Problems

### **Review of Narsimham Committee:-**

- Review the relative role of the different types of financial institutions in the financial system & to make recommendations for their balanced growth.
- Review the existing legislative framework to suggest amendment for implementing 'the recommendation that may require legislative changes '.
- Review the existing supervisory arrangements relating to various entities in financial sector.
- The determination of interest rate should be on ground of market forces. 5. It further suggested minimizing the slabs of interest.

### **Recommendations of Narsimham Committee Report (I) 1991**

#### **1) Reduction in the SLR & CRR:-• Reduction in SLR:-**

- Interest Rate Structure
- Capital Adequacy Norms
- Income Recognition & Asset Classification
- Structure of Banking System
- Management of non-performing asset
- Removal of Dual Control
- Banking Autonomy

#### **Recommendations of Narsimham Committee Report (II) 1998:-**

A second banking sector reforms committee was set up under the chairmanship of Shri. M. Narhimham on 10 th Dec. 1997, to review the progress in the banking sector reforms & make suitable recommendations.

The Recommendations of this Committee

Directed Credit

Bank Ownership

Review of Banking Laws

Investment

Asset Quality

Income Recognition

### **Recent trends about nationalized banks:**

The banking Sector in general and the nationalized banks in India, in particular have been experiencing a lot of changes in the last two decades. They are summarized as follows:

- Rising figures of NPA accounts
- Bulk defaulters running out , even from the nation
- Rising pressure of technology driven banking
- Compelling necessity of mergers of nationalized banks
- Urgency of take overs of other commercial banks by nationalized banks to retain public confidence on the overall banking system.
- Rising trends of Cyber Crimes on Banks.

The above mentioned points are just a trailer and indicator of the present day scene of the banking sector in India in general and about the nationalized banks in particular. A detailed study of the present status and the steps for smooth and reliable banking calls attention of the researchers.

### **Epilogue:-**

Indian Economy shows a majority share of the Services Sector contributing in the GDP of the nation. Banking Sector is one of the prime movers of the Economy. In fact, all the other economic functioning of the nation largely depends upon the efficient and reliable banking system. Nationalization of commercial banks in India has completed 50 years recently. The process of nationalization has resulted into many economic benefits for the nation and the nationalized banks have made yeoman's contribution in the last 50 years. However, the recent trends in banking and in the economy in general show that, it is high time to reconsider the nationalization policy. A lot of changes are expected in the Banking Sector of India in the next decade.

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