HISTORICAL PERSPECTIVES OF BANKING IN INDIA

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INTRODUCTION

Banking and financial services along with the manufacturing sector roled out higher salary hikes compared with other sectors in 2011, according to compensation trend study from DELOITTE. (Economic times, 4, 3-9-2011). Hiring and compensation experts say that, barring the first quarter of 2010-11, the subsequent three quarters were positive in hiring sentiment. The continuous demand for talent, salary increments remained healthy and similar to those incremental levels of 2009-10.

India's growth fundamentals like significant savings, investment and consumption rates, labour force growth ensures and more or less steady economic performance in growth rates in year to year. As a result, the overall average annual increment across sectors has been 12.9% for 2010-11. The banking sector occupies a dominant and vibrant role in future. The entry of new banks will explore and change the Indian financial system dramatically and radically. The increase in competition among banks definitely will show impact on customer's satisfaction. The Reserve bank of India has taken the next step towards delivering on the assurance contained in its January 2001 guidelines that, it would consider licensing more banks, three years later, after a review of the working of a private sector. The new draft guidelines reveals that the banks licensed under the 1993 and 2001 guidelines and the feed back to its august 2010 discussion paper and are a vast improvement over the earlier guidelines. Thus the minimum capital requirement has been raised to Rs. 500 crores (as against Rs. 200 crores earlier) and the capital adequacy ratio increased to 12% (9% for existing banks). The new banks will have to ensure that 25% of their branches are located in rural areas. Foreign share holding has been capped at 49% for the first five years, as against 74% at present. While the entry of corporate has not been banned, per se, a number of safeguards have been incorporated.

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The banks occupied an important role in the economy. The development of economy depends upon the services provided by banking system. The peace of the economy depends upon the velocity of the money. The velocity of money will be monitored through banks by the government. The government will make policies and reforms in order to achieve its goal. The policies are enzymes and reforms are antibiotics. The central bank is agent of union government. The government will make all policies to the welfare of society. The policies will be implemented by the government through its different organs. In this juncture, the commercial banks are service providers to the nation. They are not financing the public. The public money will be utilized for public purpose. The financial resources will be coordinated by banks, through deposits and lending system. They mobilize deposits from rich community and divert the resources to the needy sectors of the society. The banks are just like a traffic island in a busy junction. It coordinates in all directions and monitors the traffic movement. The central bank occupies the place of closed circuit television of the traffic junction. It monitors, regulates, coordinates and controlled banking system in the country. The banks are poor man's nest of his hard earned money. However, the banking system in India should be functioned as a service provider rather than a fund based agency. In India, there is a huge potential for small savings sector. The commercial banks should also enter into chit fiancé sector. The chits are poor man's paradise. The public of India is based on private chits to fulfill their long term desires and dreams. In this modern world, desires and dreams are the biggest business opportunities to the right business man. There are crores of people in private chits, but there is no guarantee for their dreams. Hence the commercial banks should enter into this lucrative sector, where confidence is the biggest opportunity for the banking system in India. The creation of competition between foreign banks and India banks are very quite good idea. But all good ideas may not generate rewards. The competition is best weapon for healthy growth of any sector in the economy. A high competition between players in the market will definitely be useful to the ultimate consumers. A lot of research has to be done in this area of Indian banking versus foreign banking.

HISTORY OF BANKING IN INDIA:

Without a sound and effective banking system in India it cannot have a healthy economy. The banking system of India should not only be hassle free but it should be able to meet new challenges posed by the technology and any other external and internal factors. For the past three decades India's banking system has several outstanding achievements to its credit. The most striking is its extensive reach. It is no longer confined to only metropolitans or cosmopolitans in India. In fact, Indian banking system has reached even to the remote corners of the country. This is one of the main reasons of India's growth process.

The government's regular policy for Indian bank since 1969 has paid rich dividends with the nationalization of 14 major private banks of India.

Not long ago, an account holder had to wait for hours at the bank counters for getting a draft or for withdrawing his own money. Today, he has a choice. Gone are days when the most efficient bank transferred money from one branch to other in two days. Now it is simple as instant messaging or dials a pizza. Money has become the order of the day.

The first bank in India, though conservative, was established in 1786. From 1786 till today, the journey of Indian Banking System can be segregated into three distinct phases. They are as mentioned below:

- Early phase from 1786 to 1969 of Indian Banks
- Nationalization of Indian Banks and up to 1991 prior to Indian banking sector Reforms.
- New phase of Indian Banking System with the advent of Indian Financial & Banking Sector Reforms after 1991.

Commercial banks have been categorized into various categories of the banking system. They are classified into different ways. One classification of banks is presented below:

a. Branch banking
b. Unit banking

Another classification of banks is:

a. Group banking
b. Chain banking

They are also classified on the basis of merits:

a. Deposits banks
b. Investment banks/mixed banks

a. BRANCH BANKING:

Branch banking means a number of branch offices scattered throughout the country to look after the banking business. It refers to that banking system which assumes each bank as a single entity having one board of directors and one group of shareholders in the hole of the branches. In some situations, the branches may extend beyond the territories of the country and may spread over different countries. The policies and instrumental are used to implement the instructions. The branches undertake the business and perform the functions. In this banking system a single bank is able to transact the banking business in a broader way. At present the branch banking has become very popular. USA and European nations have developed branch banking system. In India it has also become very popular. All of the major commercial banks have opened their branches in rural and remote areas. The branch banking system has the following advantages:

1. They are involved in extensive coverage of business
2. They are doing the business more efficiently without risk.
3. They do the business in large scale.
4. Rationalization and scientific management is possible.
5. Investments can be made in diversified areas.
6. The personal bias and favouritism is avoided in this system.
7. The diversification of investment reduced the risk.
8. Non-performing assets may be reduced substantially.
9. The economies and operations are available in this system
10. The financial stringencies are possible with system

DISADVANTAGES:

The branch banking system suffers from the certain disadvantages which are presented below:

1. The systems ignore the needs of people.
2. The head office sometimes unable to understand the local.
3. The regional disparities will be increased
4. Partially will be shown while granting the loans
5. The small customers may be ignored.
6. There is no proper control on branches.

7. Head office is holding all the powers.
8. The red -tapism and delay of decisions.
9. It leads to concentration of economic power in few.
10. Speculative activities may develop and favouritism may be exercised.

b. Unit banking:

Unit banking refers that business operations are carried out through a single office and at one place. The units are working within a limited area. The banking business is not carried on through the wide network of branches. Unit banking was very popular in USA. Branch banking operates through only one office. Unit banks are separate entities and have their own capital board of directors and shareholders. The area of the operation is very small. The unit banks understand the needs of the local people. These banks give first priority to the local funds are used for local developments and the funds are not transferable to any other areas. The unit banks know the pulse of the local customers and know better to cater the needs of the local business community. The local industries agriculture gets the opportunities for their development. Individual entrepreneurs are given personal attachment by the unit banks. The unit banks are very small, do not exist any problem relating to the management and control of the business. In unit banking there is no chance for frauds and irregularities. Unit banking also suffers for limited resources. The unit banking cannot expand their business. The banks are unable to earn maximum profits because of the scarcity of resources. The unit banks are liable to work in a limited area. The possibilities of survival are least. The cyclical fluctuations of business may severely hit the business. The economies of large scale are not available in this system. Unit banks are unable to achieve balanced growth. The unit banking system neglects the backward people where the financial assistance is much required to develop the nation. These banks suffers from the local influence to patronage the unworthy of the credit are granted. They suffer from numerical disadvantages.

a. Group banking:

Another classification of banking system the commercial banks may be known as group banking. The group banking has some special distinctive features. These banks are the direct outcome of the effects of the unit banking. In this system two more banks are brought directly or indirectly under the control of holding company. The holding company will coordinate all the things of the affairs. Group banks are very common in the USA. The group banking system has been emerged with the combination of the advantages of branch banking and unit banking. Each member bank maintains its identity and functions economically without losing the confidence of people. Each banks its own board of directors and officers. The member bank can enjoy the experience and technical expertise of the holding company. The business can be expanded and profitability can be increased. The holding company provides the advertisement, support and standardizes the accounting pattern. The member bank can avail of the services of the holding company. The member banks will get instructions from the holding company to carry the business very smoothly and effectively. Therefore, there are some intricacies in the group banking system. The grouping bank system operates as the principles of centralization. Every decision will be taken by the holding company and there may not be any freedom to member bank. The member bank is only an instrumental to implement the policies of holding company. The holding control does not impact as the functioning of the member bank. In the group banking these will be possibilities of manipulation and speculation are higher. The failure of the member bank will adversely affect on other banks.

b. Chain banking:

The chain banks were emerged in America and were very popular up to 1920. In this banking system the individual banks are incorporated and brought under common control. There is no existence of holding company. Some persons are directories of two or more banking companies. The ownership is common in India. The managing agents were playing an important role and these were utilized by the resources chain members. The chain banking system enjoys the advantages on par with the group banking. It also suffers from the problems as in the case of group banking.

c. Deposits banking:

Other classifications of commercial banks are two kinds. They are categorized on the basis of deposits and investment. They are presented below:

a. Deposit banking
b. Investment banking
c. Mixed banking

Deposits banking are the type of banking where the deposits are mobilized from the public. These banks are known as deposits banks. The deposits banks sanctioned the loans for short-term loans. These loans are sanctioned to meet the needs of working capital of the industry. These banks have grown up in England. These banks cannot freeze their funds in long-term investments. They were sanctioning the loans for only short-term basis. They were not granted the loans for long-term for only short-term basis. They were not granted the loans for long-term capital investments. These banks were to provide working capital for currents and seasonal requirements.

The deposit banks are acting as trustees of the depositors. The depositors are the main customers of the banks. The business of the bank depends upon the credibility. The depositor's hard earned money should be preserved. The depositors may demand their money at any time. Therefore, the bank should maintain the liquidity position. Therefore, these banks are invested towards short-term finance to the corporate sector. These banks are providing finance to the industrial sector and too small or medium type industries.

Investment banking is mainly interested for providing long-term finance to the corporate sector. The investment banks are also known as "industrial banks". These banks are advancing loans on long-term finance to the industries. The investment banks are very popular in Germany. These banks were established to promote industrial development. These banks did not accept the deposits initially. But later on, they mobilized the resources from the public. Several banks were formed as consortium or syndicate. They took the responsibility of financing to industrial units. These banks enjoyed the mutual cooperation of the industries. The promotion of new industries and development of established industries were developed by the mutual assistance of the banks and other related industries. The banks were expertise in the mobilization of resources and sanctioning loans to the industries.

MIXED BANKING:

The mixed banking involves in mobilization of deposits and grant term loans to the corporate sector. It developed in UK after the First World War. Industrialization, competition, mass production encouraged the mixed banking system. They functioned as investments banking. In India the mixed banking system was emerged on the recommendations of central banking enquiry committee (1931). The shroff committee also recommended indirect participation of banks in industrial finance. The demand of industrial financing through commercial banks had been increasing tremendously. The IDBI was established in 1964. It took initiatives to finance the industries. The RBI also encourages the commercial banks for increasing the term lending. The term lending was very popular in USA and is taking important position in India. There are several industrial financial institutions which have been established to look after the welfare of industrial sector. These institutions were established by the parliament by making an act. They are IFCI, ICICI, IDBI, IRCI, etc. the term lending finance has extended from industries to agriculture after nationalization of banks in 1969. The commercial banks in India are turning to mixed banking.

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