



REVIEW OF RESEARCH



BANKING SECTOR IN INDIA: POST LIBERALISATION ERA

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ABSTRACT

It is well appreciated that the gains in the real sector of an economy are spurred and sustained by the strength of the financial sector which is at its back. Within the financial sector, it is the strength and structure of the banking sector and how its strengths and weaknesses make or break an economy has been very amply demonstrated by the recent experiences in the South East Asian crisis. It is now widely recognized that in South east Asian economies, one of the important reasons of the crisis was the weak structure of the banking system and its resultant inability to cope up with the changes that were taking place in the real sector. India economy has largely remained protected against the crises and has shown considerable resilience purely on account of strong fundamentals.



KEYWORDS : *banking sector , strong fundamentals.*

INTRODUCTION

The present banking system in India was evolved basically to meet the financial needs of trade and industry. The banking sector in India comprises the public sector commercial banks, private sector banks, co-operative banks and regional rural banks. The minimum capital requirement for setting up banks in the private sector was prescribed at Rs. 100 crores. Upon review of the position of the capital funds of old private sector banks in 1998-99 it was indicated that old private sector banks having net worth of less than Rs.50 crores were to attain the level of Rs. 50 crores by March end, 2001. Subsequently, the RBI directed that capital requirement of old private sector banks should be on par with that of new private sector banks at Rs. 200 crores with commitment to increase it to Rs. 300 crores within three years. It also directed that all banks would have a net worth of at least Rs. 300 crores. At present it has been enhanced to Rs. 500 crores². Technology has played and is playing a critical and arguably the most important role in redefining the financial business.

Deregulation in the financial sector has brought about new opportunities which have also added to the risk profile of banks.

CHANGING PROFILE OF INDIAN BANKING

As a rule, banking systems are adapted to the structure and needs of the particular economy they exist in. Indian economic policy has been founded on the philosophy of economic growth with social justice. It is against this background that we have to assess the steps taken by the Indian banking system during the

recent past which marks a significant departure from the beaten track of traditional banking. As a matter of fact, the concept on banking has undergone a dynamic change in keeping with the need to achieve rapid socio-economic progress although the achievements have not been without cost and shortcomings.

The most striking feature is its reach. Banks are no longer confined to metropolitan cities and large towns. The branch network is extensive and these branches are now spread out into the remote corners of our country. In terms of the number of branches, Indian banking system is one of the largest, if not the largest, in the world today. An equally important achievement is the close association of our banks with the country's developmental efforts. The diversification and development of our economy, and the acceleration of the growth process, are in no small measure as a result of the critical role which our banks have played in financing economic activities in various sectors.

FROM SECURITY ORIENTATION TO PURPOSE ORIENTATION

According to traditional banking theory, the creditworthiness of a person is based on the basis of the tangible assets owned by him. The result is that people who have money can get more money from the banks. This concept does not fit in the social concept which enjoins that it is not enough that only people of means are given bank finance. What is more important is that bank finance should go to make people creditworthy, through productive efforts on their part, and to turn them into people of means. Basic to this new concept of banking, a shift in the approach to lending from security orientation to purpose orientation is necessary. In fact, technical competence of the borrower, operational flexibility and economic viability of the project rather than the security which the borrower can offer are gradually becoming popular among the banking community in evaluating a loan proposal.

The identification of the priority sectors for the purpose of financing by banks has given a new orientation to the Indian banking system. The measures taken by the banks in this regard, which are primarily aimed at furthering the welfare of the common man, have already been highlighted at an earlier point. It may briefly be mentioned here that the change in the pattern of banks' business has taken the form of a much-enlarged quantum of credit to the hitherto neglected, or more positively, the new priority sector. From a mere Rs. 307 crores which represented about an eighth of the total bank credit in December 1966 and Rs. 504 crores which represented 15 percent of the total bank credit in June 1969, the share of public sector banks in the priority sector was Rs. 1,46,546 crores as at the end of March 2001. As a share of net bank credit, this constituted 43 percent. Agricultural credit had risen from under Rs. 200 crores in June 1969 to Rs. 53,685 crores in March 2001 with its share at 15 percent. An important point worth noting here is that this large increase has been reasonably well distributed as is evident from the fact that the total number of borrowed accounts from the banking system which stood at 1.64 lakh in June 1969 increased manifold in the case of agricultural borrowers alone. The overall picture of the priority sectors is still more impressive. On the side of bank credit, there were barely 4 lakh accounts in the priority sectors in June 1969. By 2002, the number of such accounts had risen to nearly 40 million. The importance of the priority sectors in our economy can be gauged from their contribution to the national income generation, the creation of employment opportunities and the diffusion of economic power. Prior to social control and nationalization, the banking system was negligent in its attitude to these sectors. It was social control and the guidelines of the erstwhile National Credit Council which brought the first stirrings towards a major meaningful sectoral deployment of credit in favour of these areas of activity and, as was only to be expected, banks operated in the margin in the sense that the incremental ratio of the new credit to these sectors went up sharply. Also, the internationalization of the new philosophy was quickly reflected in the new orientation given to policies and programmes of the various banks and innovations introduced by them in their schemes.

Correction of Regional Imbalances: Developments in the Field of Branch Banking

The increasing realization on the banking system to fall in line with the social-economic objectives necessitated the expansion of the network of branches to the underbanked areas of the country. In December 1966, there were little under 6,600 branches and by June 1969, this figure reached to about

8,260. Between June 1969 and end-April 1976, the number of all commercial banks in the country increased by 12,555, bringing down the average population served per bank office from 65,000. By June 2002, there were 66,186 branches of commercial banks. The average population per bank office had come down to 15,000 at the end of June 2002. Such a pace of expansion has few, if any, parallels in the history of banking development anywhere in the world. Most of the branch expansion has occurred in the rural and semi-urban areas, reflecting the concern to achieve a more balanced spatial distribution of credit, and today there is a bank office in almost all the 5,000 odd development blocks in the country. As at the end of June 2002, rural branches accounted for 49.1 percent of all the branches. Thus, the branch expansion of banks has been aimed at correcting the regional imbalances in banking development. Branches of a bank are a means, an essential means, to the end we are seeking, namely, a greater involvement of banks with decentralised activity. The new branches in the rural areas are expected to increase the flow of credit to rural occupations in general and agriculture in particular, and to mobilize the savings generated in the rural sector.

The 'area approach' is another method adopted by the banking system to correct the regional imbalance in development. The 'Lead Bank Scheme' is the main instrument of this aspect of banking policy. The Lead Banks are engaged in preparing credit plans based on bankable schemes which are expected to assist in the economic development of the rural areas of the country and to bring about a more systematic involvement of banks in grassroot level development.

Development of Banking Habit

As a natural corollary to the development in the field of branch banking, development of banking habits in India during the last few decades has been at an unparalleled pace. Obviously, the banking system in the country has made a significant contribution to ensure such progress. Sustained efforts have been made by banks to induce people to keep a part of their savings as bank deposits, and to expand and diversify their lending portfolio to cover a considerably large number of borrowers than ever before. A good measure to the development of banking habit is provided by the growth in the volume of banking transactions in relation to gross domestic product. In 1969, deposits amounted to 13 percent of GDP and advances 10 percent. By 2002, deposits as proportion of GDP had risen to around 50 percent and advances to well above 25 percent, indicating the extent to which the banking system has been instrumental in spreading the banking habits in the country. An idea of the extent to which the banking system has been able to spread banking habits in the rural areas is indicated by the fact that the growth of deposits of rural branches has been much faster than that of total deposits. The rapid development of banking habits is also evidenced by the considerable increase in the use of cheques in recent years. Another important parameter which is a symbolic indicator of the growing banking habits is the growth in bank credit.

Attitudinal change on the Part of Bankers

A welcome change in the philosophy and techniques, particularly in the field of bank lending, is taking place. This relates to the attitudes on the part of banks. As observed by the former governor of the Reserve Bank of India:

'Commensurate with the growth of branch banking in the rural areas and the larger involvement of banks with agricultural and small industrial clients, we have had an attitudinal change on the part of bankers, a change symbolized by banking going retail instead of its erstwhile wholesale character and the system itself shedding its elitist image to become more retail banking orientation.

From Moneylending to Development Banking

As an extension to the above, it may be noted that from being dispensers of short-term credit, banks are now actually helping industrial development of the country by providing access to capital market and long-term savings of the economy. The transformation of banks from being moneylenders to development bankers is a recent phenomenon in the Indian banking system.

Establishment of Specialized Branches

Another recent trend visible in the banking system, especially with the onset of liberalized branch licensing policy of the Reserve Bank, has been the establishment of specialized branches to cater to the needs of specific segments of the clientele. The following are the main types of such specialised branches:

NRI Branches	-	to cater to the needs of NRI clientele.
Industrial Finance Branch clients exclusively	-	to cater to the needs of industrial clients exclusively
Overseas Branches	-	to specifically concentrate on export-import business
Small-scale Industries Branches	-	to deal with small-scale industries exclusively.
Professional Branches	-	to cater to the needs of professionals such as Engineers, Doctors, Chartered Accountants, lawyers, contractors, etc.
Agricultural Finance Branches	-	to cater to the needs of high-tech agriculture, agro exports and corporate clients dealing with agri-business.
Recovery Branches	-	to exclusively concentrate on recovery on non-performing assets.

CUSTOMER FOCUS

Growing expectations of the bank customers is a marked feature of the current banking environment. Forces of competition and growth of technology are mainly responsible for this change. At the same time, however hard a bank may try to meet customer expectations, there will be occasions for customer complaints. Hence, the Banking Ombudsman Scheme instituted by the Reserve Bank, discussed in detail elsewhere, is a welcome step in the right direction. It may briefly be pointed out here that the main objective of the scheme is to create a forum for the speedy redressal of customers' grievances and also to receive unresolved complaints about the provision of banking services, as well as to facilitate the settlement or withdrawal of such grievances.

CONCLUSION:

Liberalisation of economy paved the ways for opening up of the Indian banking system resulting from which a number of foreign banks have evinced interests in the international banking business. The decade 1990s witnessed a number of developments in the banking industry. The globalisation made ways for liberalisation of regulatory provisions and new generation of private and foreign banks started gaining popularity.

The process of technological sophistication gained a rapid momentum and the customers started envying the world class banking services. The electronic banking channel virtually redefined the concept of banking services and general masses started thinking in favour of shifting to them but only rich and middle classes could enjoy the techno-driven services offered by private and foreign banks. The public sector commercial banks realised that delaying the infusion of technology would be suicidal for them and therefore policy decision makes opened doors for promoting technology. Thus, the process of technological sophistication started gaining momentum since the beginning of 21st century and now we find a good number of public sector banks offering techno-driven services.

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