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A Review of the Emergence of Modern Banking and Financing Structure in India

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***Abstract:** Banking of India is as old as ancient Vedic period. In l770, the English trading company founded the first modern bank in Calcutta, called as The Bank of Hindustan. Some exchange banks and Indian joint-stock banks were also established in the second half of the 19th century. Nine Indian joint banks, eight exchange banks, and three Presidency banks existed in 1900. The deposits in banks expanded from eighty two crores of rupees in 1910 to nine hundred fifty seven crores of rupees in 1948. During the previous five decades, many macroeconomic changes have occurred. The monetary and banking policies as well as the external environment have had varying effects on the development of Indian banking. To comprehend any economic aspect of the banking business in India, it is necessary to comprehend the industry's development.*

***Keywords:** Bank, India, Economic, Commercial, Government, Centralize, Private, Financing.*

I. CONTENT

Banking of India is as old as ancient Vedic period. In l770, the English trading company created the first modern bank in Calcutta, called as The Bank of Hindustan. After that Bengal Bank was set up in 1784 and around 1786 General Bank of India was established, however these banks could not deliver the services due to their own problems. The basis of banking system was formed during the early part of the nineteenth century with the establishment of three Presidency banks, namely the Bank of Bengal (1806), Bank of Bombay (1840), and the Bank of Madras (1846). Some exchange banks and Indian joint-stock banks were also established in the second half of the 19th century. Nine Indian joint banks, eight exchange banks, and three Presidency banks existed in 1900. The slow rate of growth of the banking business till the beginning of the present century was due to: (a) a high rate of failure banks, because most of them had been created in a speculative rush; (b) stagnant economic condition during the period; (c) declining prices; and (d) the passing of the Currency Act, 1861 which took away the power of banks to issue notes.

During the first fifty years of this century, the financial sector made tremendous progress. The amount of deposits in banks climbed from Rs. 82 crores in 1910 to Rs. 957 crores in 1948. Except for the Great Depression of the 1930s, the pace of economic development throughout this time was relatively fast. Three Presidency banks were merged in 1921 to become the Imperial Bank of India (IBI). The money market lacked a competent central bank until 1935, when the Reserve Bank of India (RBI) was created.

During the previous five decades, many macroeconomic changes have occurred. The monetary and banking policies as well as the external environment have already had varying effects on the development of Indian banking. In light of this, it would be interesting to analyse the development of Indian banking with reference to a certain period. The first phase covers the years 1948 to 1968 (the Pre-Nationalization Era), the second phase covers the years 1969 to 1990 (the Post-Nationalization

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Era), and the third phase started in 1991 (Globalization Era). The Indian banking business has developed in a distinct setting and even with specific goals. This historical context and purpose has a significant influence on the current management of the organization. To appreciate any economic aspect of the Indian banking business in appropriate perspective, it is necessary to comprehend the industry's development.

In the pre-nationalization era the nation inherited a banking system structured after the British prototype. There were several joint-stock corporations doing banking operations, and they were mostly concentrated in big cities. In those days, bank failures were prevalent due to the mushroom-like expansion of financial institutions. As many as 55 banks either liquidated or ceased operations in 1949. The Banking Regulation Act, enacted in 1948, established the legislative basis for the Reserve Bank of India to regulate the banking industry (RBI). The Act, which went into effect in March 1949, placed various regulations on joint-stock banks operating in India.

The banking system at the time of independence was deficient in many respects. The banks were largely urban-oriented and remained beyond the reach of the rural population. A large percentage of the rural peculation had to depend on the moneylenders as their main source of credit Banks' rural penetration was grossly inadequate, as agriculture was not considered as an economic proposition by banks in those days. Thus, the rural economy, in general, and the agricultural sector, in particular, which is the crucial segment of the Indian economy was not supported by banking system in any form.

In several ways, the financial system at the time of independence was weak. The banks were mostly urban-centric and out of reach for the rural populace. A significant portion of the rural populace had to rely on moneylenders as their primary source of credit. The rural penetration of banks was extremely insufficient, since agriculture was not seen as a viable economic venture in those days. Thus, the rural economy, in general, particularly the agricultural sector, which is the most important sector of the Indian economy, were not supported in any way by the banking system.

With the introduction of economic planning in 1951, it became necessary to connect the country's monetary and banking activities with the planning needs. The first move was made to include commercial banks into rural bank loans, which was formerly reserved for cooperative credit organisations fighting moneylenders. As part of the geographical development of banking facilities to suit the credit demands of cooperatives, many banking organisations that had previously functioned as princely states were transformed into subsidiaries of State Bank of India (SBI), which were subsequently renamed Associate Banks of SBI. The technique of financing shifted from security-based to capacity-to-produce-and-sell standards. An examination of the ownership of bank deposits during this time period showed the connection between business houses and financial institutions, revealing the nature of business houses' power over banks.

Although the Indian banking industry achieved significant functional and geographical advancements during this time, there were still many rural and semi-urban regions that were not covered by banks. In addition, the majority of credit facilities tended to be used by large enterprises and well-established corporations. Agriculture, small-scale enterprises, and exports did not get the attention they merited as vital and important sectors. By amending financial rules, the government established in 1968 social control on banks. The purpose was to ensure an effective allocation of banking resources in accordance with the demands of the economy and the priority sectors. This resulted in RBI acquiring expanded authority over the selection of bank presidents, directors on bank boards, and auditors.

Intriguing is the effect of implementing societal control over banks. One is that credit planning became an integral component of credit policy design. The second objective of the Lead Bank Scheme was to transform the banking sector into a tool for development. Under social control, the financial sector, especially smaller banks, began to acquire strength, as indicated by the lack of voluntary or mandated mergers. Consequently, social control was a landmark in the development of banking system policy. In 1969, the Banking Commission was appointed to recommend improvements to the Indian banking system's structure, operations, and policies. This period started slowly. However, the Commission did not have much time to fulfil its job

due to rapid political and economic events that resulted in the nationalisation, on July 19, 1969, of the 14 largest Indian scheduled commercial banks in the private sector. Six more private sector banks were nationalised on April 15, 1980, therefore expanding state control over the Indian banking system. Nationalization was seen as a significant measure for ensuring enough credit flow into actual productive regions in accordance with plan goals.

In the post-nationalization era the primary objectives of nationalisation were growth; reduction in regional imbalances of economic activities; making the banking system accessible to the common man in rural and semi-urban areas; and extending banking facilities to areas not previously served by banks so that they not only absorbed potential savings but also filled credit gaps in agriculture, small-scale industries, and other neglected sectors of the economy. The objective was to include a substantial portion of economic activity into the structured banking system.

Therefore, the two key features of nationalisation were fast branch development and priority-based credit management. In the aftermath of nationalisation, the Indian banking sector saw tremendous growth and expansion. At the conclusion of the second decade of nationalisation, the Indian banking system was rather sophisticated, with a vast branch network, enormous deposit resources, and substantial credit operations. This time saw an upsurge of financial activity that may be defined as a banking explosion. In terms of the RBI's branch licencing policy, the focus was placed on the creation of branches in rural and semi-urban areas, backward regions, and under-banked states in order to decrease regional inequities.

India's banking system has evolved into a social banking system since nationalisation, and even before that. Banking has been used as a tool to promote socioeconomic goals; for instance, in the early 1970s, banking policy was expanded to ensure a decrease in income inequality. The "Priority Sector Lending Scheme" was succeeded in 1971 by the "Credit Guarantee Corporation." This corporation provides assurances against the risk of loan default for a broad range of small borrowers. Later, a number of advances were developed in the area of social banking, and substantial amounts of credit were extended via programmes such as the "2-Point Economic Programme", the Integrated Rural Development Programme (IRDP), and the "Programmes for Self-Employment of Educated Unemployed Youth" (SEEUY). The banking system of finance embraced a number of poverty-alleviation programmes in the form of mass-lending schemes.

Although rural regions were accessed by banks, the quantity of credit offered to the weakest segments of society remained insufficient. The Narasimham Committee investigated these issues in 1974 and suggested the formation of Regional Rural Banks (RRB) under the Regional Rural Banks Act of 1975. Regional Rural Banks were established in some locations where the co-operative system was weak and commercial banks were not particularly active, in partnership with the federal and state governments.

The phenomenon expansion of the Indian banking sector in the two decades before reforms gave birth to a number of issues that became increasingly apparent in the mid-1980s. Internal and external restrictions made the banking system unmanageable as a result of the banking sector's fast and large expansion. These included poor operating efficiency, an insufficient capital base, a large proportion of nonperforming assets, low profitability, an unhealthy balance sheet, and bad customer service. During this time period, the financial system's viability has come into doubt.

Prior to the changes, from 1985 to 1991, the financial sector had a consolidation phase. This consolidation required activity on several fronts. Individual banks resorted to Enterprise Resource Planning (ERP) systems for action plans pertaining to organisational structure, housekeeping, training, customer service, credit management, loan recovery, productivity, and profitability. According to the recommendations of the Rangrajan Committee on computerization in banks, banks have been instructed to implement information technology in their operations. Even while the banking system has achieved enormous progress in terms of geographical and functional coverage, resource mobilisation, and credit deployment, this is still an inexplicable trait of a suppressed financial system.

During liberalization era, as a consequence of the adoption of financial reforms, particularly banking reforms, the third phase of the regime of reforms started with a major shift away from regulated banking towards market-oriented banking. At the macro level, the reforms attempt to remove the external limitations of the banking sector as a whole and create an environment conducive to liberalisation. At the micro-level, the changes are focused on helping the banking system to overcome internal limits on the function of banking organisation. The Committee on Financial Reforms (Narasimham Committee), which made recommendations in November 1991, provided the foundation for banking reforms. These recommendations are a landmark in the evolution of banking policy in the country, as they transformed the Indian banking system into a more market-oriented system.

The government created a second high-level "Committee on Banking Sector Reforms" under the chairmanship of M. Narasimham to examine the execution of the first round of reforms. In its April 1998 report, the Committee provided extensive suggestions encompassing a variety of institutional, supervisory, and legislative dimensions of banking policy. The Committee issued recommendations regarding: capital adequacy; asset quality, non-performing assets; directed credit; prudential norms; disclosure requirements; asset liability management; earnings and profitability; systems and methods in banks; restructuring, including mergers and amalgamations; the reduction of government and RBI shareholding in public sector banks to 33 percent; the formulation of effective regulatory norms; and the review of banking sector liabilities. These suggestions are being implemented in stages. As a follow-up to Narasimham Committee's (1998) reference to weak banks in the context of bank restructuring, the Verma Committee was constituted in 1999 with the particular mission of identifying weak public sector banks, assessing their difficulties, and recommending restructuring methods. The Committee's proposals were agreed in general.

The Indian banking system comprises the central bank, commercial banks, development banks, specialised banks, and foreign banks. (a) The country's central bank is known as the Reserve Bank of India (RBI). R.B.I., the top monetary and financial authority in the country, is responsible for regulating the nation's banking sector. b) Commercial banks are the publicly traded corporations that deal in money and credit. These banks mobilise deposits and make them accessible to big and small industrial and commercial enterprises, primarily for their working capital needs. (c) Most cooperative banks based on the unit banking concept are located in rural regions, but a few operate in metropolitan areas. The majority of agricultural state funding are channelled via state cooperative banks and central cooperative banks. d) Numerous apex banks operate in specific fields. Among them are NABARD, IDBI, the EXIM bank, and the National Housing Bank. IDBI, ICICI, and IFCI are the three most prominent term lending institutions. The Reserve Bank of India Act of 1934 designated banks as scheduled banks.

Scheduled banks were included in the second schedule of the RBI Act of 1934. These are the banks having a paid-up capital and reserves of at least 5 lakhs rupees and which meet the RBI's regulations for this purpose. Scheduled banks include all commercial banks, both domestic and international, regional rural banks, and cooperative banks. In contrast, non-scheduled banks are those not listed in the second schedule of the RBI Act of 1934. There are currently relatively few unscheduled banks in India. Hence the banking take its modern format during and after the British period. After independence an evolution is been seen in banking and financing sector of India.

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