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Nationalization of Banks

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SUMMARY

50 years ago, the Indian financial sector underwent a tectonic shift, when Indira Gandhi government nationalized the 14 biggest commercial banks in 1969. According to many economists nationalization of banks was the single-most-important economic policy decision taken by any government after 1947. The impact of this decision is considered by some to be, even more than the economic reforms of 1991. During that time many Asian countries were switching to more market-oriented policies, India on the other hand, supported the socialist policies. However, with the looming banking crisis in current times, debates have emerged about the privatisation of banks. This raises the question of whether nationalisation of the bank in the first place was the right move or not. The nationalized commercial banks were at that time controlling 91% of total deposits and total credit. Nationalization of commercial banks in India is looked as a significant effort of the Government of India to strengthen the economy.

INTRODUCTION

After independence the government of India (GOI) adopted planned economy development for the country (India.). Accordingly, five year plans came into existence since 1951. This economic planning basically aimed at social ownership of the means of production. However, commercial banks were in the private sector those days. In 1950-51 there were 430 commercial banks. The Government of India had some social objectives of planning. These commercial banks failed helping the government in attaining these objectives. Thus, the government decided to nationalize 14 major commercial banks on 19th July, 1969. All commercial banks with a deposit base over Rs. 50 crores were nationalized. It was considered that banks were controlled by business houses and thus failed in catering to the credit needs of poor sections such as cottage industries, village industries, farmers, craft man etc. The second dose of nationalisation came in April 1980 were 6 banks nationalized with a deposit base over Rs. 200 crores.

A Brief History of Nationalization

In 1955, India nationalized Imperial Bank of India with extensive banking facilities on a large scale, especially in rural and semi-urban areas. It formed State Bank of India to act as the principal agent of RBI and to handle banking transactions of the Union and State governments all over the country. On 19th July 1969, a major process of nationalization was carried out and 14 major commercial banks in India were nationalized.

List of banks nationalized on 19th July 1969.

- Allahabad Bank (now Indian Bank)
- Bank of Baroda
- Bank of India
- Bank of Maharashtra
- Central Bank of India
- Canara Bank
- Dena Bank (now Bank of Baroda)
- Indian Bank
- Indian Overseas Bank
- Punjab National Bank
- Syndicate Bank (now Canara Bank)
- UCO Bank
- Union Bank of India
- United Bank of India (now Punjab National Bank)

The second phase of nationalization Indian Banking Sector Reform was carried out in 1980 with six more banks.

- Punjab and Sind Bank

- Vijaya Bank (now Bank of Baroda)
- Oriental Bank of India (now Punjab National Bank)
- Corporation Bank (now Union Bank of India)
- Andhra Bank (now Union Bank of India)
- New Bank of India (now Punjab National Bank)

This step brought 80% of the banking segment in India under Government ownership.

Benefits of Nationalization of Banks

- Prevention of Monopoly : Before the government nationalised banks, corporate families controlled banking systems in India. It effectively ensured a monopoly over capital. Bank nationalisation helped make the economy more equitable and opened bank credit to even people without connections.
- Reducing Regional Imbalance : Bank nationalisation helped in more equitable regional growth since banking system was concentrated in urban centres and that too largely in the West and the North.
- Improvement in working conditions: As per RBI records, there were 1833 banks in rural areas in the country in 1969, which increased to 33,004 by 1995 and continued to grow over the next decade. Government banking improved working conditions of the employees also in the banking sector. The state ensured higher wages, security of services and other fringe benefits.
- Protection of Public Interest : Unhealthy competition among industrialists injured the interest of the public which was measured and mitigated by state ownership.
- Centralised Management: Centralised management made possible due to coordination in nationalised banks helped provide uniform services throughout the country. It thus enabled the state to solve the problems of organisation, capital, labour operation and marketing.
- Use of Surplus Profit: Under state ownership the profit earned by banking enterprises could be utilised for greater public good and help in supporting the Government's economic policies.
- Uniformity and Stability in Services: Nationalisation ensured uniform banking services and reached banking services to different corners of the country. Banking services were placed within reach of people in rural areas and reduced their dependence on moneylenders.
- Core Sector Lending: Private Banks were averse to lend to Agriculturists and to the core sector of steel and coal, which required huge investment. Nationalisation made funds available to these sectors.
- **Increase in Standard of Living:** It enabled rapid increase in the number of banking offices in rural and semi-urban areas and helped considerably in deposit mobilisation with the added benefit of the expansion of personal loans giving a fillip to consumption.
- Developing banking habits: RBI records show that per capita deposits increased from Rs. 88 in 1969 to Rs. 4242 by 1995 and have further increased with time.

Criticism on Nationalisation of Banks

- Nationalisation of banks was criticized as an instrument to use the financial resources of the economy to serve the political purpose rather than the productive purpose.
- Nationalisation of banks has been criticized for vesting enormous powers in the hands of RBI for controlling banks resources. It has been criticized as the beginning of state capitalism by replacing corporate capitalism.
- Nationalisation of banks has been criticized for increased inefficiency and corruption in the banking sector. The increase in non-performing assets in the public sector banks is an example.
- Public sector banks have been criticized for providing less attractive customer services and increasing red tapism.
- The argument of branch expansion in rural areas has been criticized as branch expansion is possible only if it is economically viable. This can be achieved even by the private banks.
- The government had to pay heavy compensation to the shareholders of these banks during nationalisation. Also, it was argued that this would not bring much profits to the government.

CONCLUSION

From the above discussion we can say that the nationalization of banks helped expansion of branches in small town and village area. It was necessary for the time being to nationalization of banks which were performed in effectively. It had achieved many objectives such as credit expansion, priority sector lending, which were beneficial for agriculture, small scale industries but due to global requirements of economic conditions which eventually led the government to adopt the policy of LPG model of economy, nationalization had to be eased privatization of banks was demand of the situation. Since then private sector banks have dominated the banking sector.

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