

EVOLUTION OF BANKS IN INDIA

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ABSTRACT:

The core of industry, trade, and commerce is banking and finance. As things stand, the banking industry is essential to a nation's ability to develop. Lending loans, taking deposits, and other associated services are all provided by banks. Lending money to those in need and depositing money from those with more to save are two different things. In the realm of human existence, banking is among the most vital and significant aspects. When it comes to facilitating quicker access to banking services, online banking systems are among the best tools available to banks, clients, and financial organizations.

Every day, banks have a lot of user-related tasks that require a large infrastructure, a larger workforce, and more labour for banking operations. The development of computers and networks led to the simplification of banking operations through the use of online, mobile, and ATM banking. There are advantages and disadvantages to every system, and the network banking system is no exception.

Some of the disadvantages include hacking and illegal access. Because a customer's account is linked to their money, the banking system must perform a number of important tasks in the authentication and validation of customer accounts. This study aims to outline the development of India's banking sector as well as the benefits of the new framework.

These days, banking permeates every facet of our daily lives—at home, at school, at work, on travel, and everywhere else we handle financial matters. The importance of banking in our daily lives is becoming more and more apparent. What are the institutions that are so necessary in today's world?

Very few people, aside from the very wealthy, purchase their homes with only cash. For most of us to make such a big purchase, we need credit in the form of loans. In actuality, a lot of people seek financial assistance from banks in order to meet their needs. The current state of the world wouldn't function properly without banks to grant credit. We will examine the origins of this burgeoning sector in this piece.

Key words: currency, money, nationalization, liberalization, and commercial banking

INTRODUCTON

One of the most important ideas for both practical applications and competitive examinations is the history of banking in India. Moreover, the nation's economic progress is based on the history of banking in India. Significant modifications to the banking system an administration have occurred over time, coupled with innovations that have taken into account the requirements of the public in terms of banking. An essential notion for banking awareness themes in bank exams is the history of banking in India.

The foreign banking system began to deteriorate in the 17th century when the British arrived. In 1770, Mayer's Alexander and Company established the Bank of Hindustan, the first bank in Europe.

A nation's ability to develop is dependent on its contemporary banking system. A developed economy is characterized by a banking system that is well-established, organized, and effective. A well-designed banking system increases economic efficiency by directing savings toward investments with better rates of return. An economy's resilience is contingent upon the effectiveness of its financial system, which is reliant on the nation's banking infrastructure.

The word "bank" comes from the old Italian word "banca" or the French word "banque," both of which refer to a bench or table used for exchanging money. In the past, European moneylenders and money changers would place large amounts of coins from various nations on tables or benches in order to lend or exchange. The origins of contemporary banking can be found in Florence during the Middle Ages, specifically in 1397. A wealthy family of merchants known as the Medici built a network of stores where customers could deposit money and take it out in a different city where a Medici agent was present.

The Church and a number of wealthy families stored their funds in Medici banks. This made it possible for wealthy people to travel without having to worry about robbery risks or carrying huge quantities of cash. By 1700, banking was becoming more and more common throughout Europe. In Europe, established banks existed in almost all of the nations.

The British founded the "Bank of Hindustan" in 1770, marking the beginning of banking operations in India. There, as autonomous entities, the "General Bank of India," "Bank of Bengal," "Bank of Bombay," and "Bank of Madras" were founded in 1786, 1809, 1840, and 1843, respectively; the last three were dubbed Presidency Banks. Following their 1920 merger, these banks became Imperial Bank of India, which subsequently changed its name to State Bank of India.

Evolution Banking System¹

The history of banking is fascinating and shows how trade and commerce have changed over time. Additionally, it sheds information on the political, cultural, and way of life of civilized humankind. Religion and faith in God have historically been the strongest human faiths. The place of worship and the seat of religion were seen as secure locations for cash and valuables. Due to the lack of steel safes in ancient residences, the majority of rich individuals kept accounts at their temples. The temples were constantly occupied by a large number of pious and trustworthy individuals, such as priests and temple employees, who added a feeling of safety. Records from antiquity, including Greece, Rome, Egypt, and Ancient Babylon, imply that temples not only stored wealth but also lent it out. The primary cause of temple looting during wartime is the fact that the majority of them served as the financial hubs of their communities.

The individual involved in this "lending" operation was referred to as the "Banker" due to the standard bench he established. It is also noted that as the furious depositors damaged the banker's bench and table, the term "bankrupt" changed. coins were certificates of value stamped by an authority, generally the king, on metal, mainly gold, silver, and bronze, but they might be any other metal. Paper was discovered to be an alternative to metal as a result of growing confidence in this authority's ability to value goods and services and the need for more trade. the instability of monarchical governance resulted in the banks gaining control over currency since they were able to maintain trust, manage credit, and engage in trading. Every type of money represented a unit of worth and guaranteed to reimburse the bearer of given value. A stable financial system emerged as a result of the inability to govern and organize due to foolish loans. Sweden's Stockholm's Banco introduced the world's first banknotes in July 1661.

India's Banking History²

In addition to being incredibly extensive and intriguing in and of itself, the history of Indian coinage sheds a great deal of insight on the diverse facets of life in various eras. The Rig Veda Only gold, silver, copper, and bronze are mentioned, and tin, lead, iron, and silver are also mentioned in later Vedic books. Iron coins have recently been discovered at extremely early stages in Pandu Rajar Dhibi (Bengal) and Attranji Kheri (U.P.).

In India, there has been a monetary economy since the time of the Buddha. trade in the modern sense. These instruments were used extensively during the Buddhist era. Large town merchants extended letters of credit to one another.

Trade guilds played the role of bankers, taking deposits and making loans. Larger temples functioned as bankers, while southern village communities provided loans to peasants in a profitable manner. Numerous bankers with expertise were present, and

¹ <https://citeseerx.ist.psu.edu/document?repid=rep1&type=pdf&doi=b61b7844652aabb2aa6eaa66afd08b3b6457f76c>

² <https://citeseerx.ist.psu.edu/document?repid=rep1&type=pdf&doi=b61b7844652aabb2aa6eaa66afd08b3b6457f76c>

The word "chief" actually refers to moneylenders such as the Sethi. It has endured in northern India as of late. Cowry shells, or varataka, were frequently used by the impoverished in several regions of India to pay for small goods.

Indigenous banking began as rural money lending, with some people utilizing their own personal savings for this kind of financing. The main bankers identified in the scriptures were the Vaishyas. The first type of Indian Bill of Exchange that existed was referred to as "Hundi". The barter system was used to govern imports and exports.

The Artha sastra of Kautilya speaks of a money called panas, and even court fines were paid with panas. Havell, E. B. in his work: According to India's History of Aryas Rule, Muhammad Tughlaq produced copper coins as counterweights and by an they were forced to pass by imperial decree at the price of silver and gold. Instead of using gold to pay their tribute, the people used copper to pay for all the necessities and extravagances they could afford.

Due to their lack of knowledge of the local language and the inexperience of the native individuals involved in the European trade, English traders who arrived in India in the 17th century were unable to take advantage of the local bankers. Consequently, the English In addition to their commercial operations, agency houses in Bombay and Calcutta started to engage in unlimited liability banking. These agency houses were set up by Europeans with aptitude for business who left the civil and military forces.

Between 1834 and 1847, a kind of corporate structure known as a managing agency emerged. These agency houses' main focus was trade, but they also ventured into banking as a side business to support the operations of their primary venture. With no capital of their own, the English agency houses that started acting as bankers to the East India Company relied on deposits to keep their money. They created joint stock banks, printed paper money, and funded the transportation of crops. The first of these was Hindustan Bank, which was founded in 1770 by one of the Calcutta agency firms.

India first established banking in the latter half of the eighteenth century. The General Bank of India, established in 1786, and the Bank of Hindustan, established in 1790, were the earliest banks; both are now closed. The bank that has been around the longest the State Bank of India is located in India. It was first established in June 1806 as the Bank of Calcutta, which quickly changed its name to the Bank of Bengal. The Bank of Bombay and the Bank of Madras were the other two presidency banks, all of which were founded under charters from the British East India Company.

What is Bank?³

A bank is a financial entity that provides its clients with banking services and other financial operations, according to the Banking Companies Act of 1949. Generally speaking, a bank is an organization that offers basic financial services including loan provision and deposit acceptance.

³ <https://testbook.com/banking-awareness/history-of-banking-in-india>

Evolution of bank ⁴

India's banking industry has seen significant change. Banks have been around for a very long time; in fact, they existed even before the nation gained its freedom. An overview of the development of banking is provided below:

India's banking history can be roughly categorized into the following phases: prior to Independence (1947 or before) phase Following Independence: (Between 1947 until 1991) liberalization (1991–Present)

Phase 1: The Pre-Independence Phase⁵

Almost 600 banks operated in India prior to its independence. The Bank of Hindustan was the first bank to be established, having been established in Calcutta in 1770. The bank dissolved in 1832. In the history of Indian banking, the Oudh Commercial Bank was the country's first commercial bank. Some 19th-century banks have withstood the test of time and are still in operation today, like Allahabad Bank (founded in 1865) and Punjab National Bank (founded in 1894). Established in the early to mid-1800s, the Bank of Bengal, the Bank of Madras, and the Bank of Bombay were among the other institutions that were merged into one to form the Imperial Bank, which subsequently evolved into the State Bank of India.

Phase 2: The Post-Independence Phase⁶

- Following its independence, India's financial system continued to develop essentially in the same way. In accordance with the 1949 Banking Regulation Act, the Indian government chose to nationalize the banks in 1969. The Reserve Bank of India was one of the fourteen banks that were nationalized (RBI). The Indian government acknowledged that several communities were being financially excluded in 1975. It established banking organizations with specialized roles between 1982 and 1990 to keep up with the development of financial services in India.

- NABARD (1982) – to support agricultural activities
- EXIM (1982) – to promote export and import
- National Housing Board – to finance housing projects
- SIDBI – to fund small-scale industries

⁴ <https://testbook.com/banking-awareness/history-of-banking-in-india>

⁵ <https://byjus.com/bank-exam/history-banking-india/>

⁶ <https://www.idfcfirstbank.com/finfirst-blogs/finance/the-evolution-of-banking-in-india>

Phase 3: The LPG Era (1991 Till Date)⁷

There was a radical shift in the Indian economy starting in 1991. India opened its doors to private investment by the government. The RBI approved ten private banks. Among the well-known brands that have survived this liberalization are IndusInd Bank, ICICI, HDFC, Axis Bank, and DCB. two further banks were granted licenses in the early to mid-2000s: Kotak Mahindra Bank (2001) and Yes Bank (2004).

Other notable changes and developments during this era were:

International banks that have branches in India include Bank of America, HSBC, and Citi bank. the process of nationalizing banks came to a complete halt.

- Payments banks were established.
- It was approved for small financing banks to open branches across India.
- Digitalization of transactions and other associated banking processes started to happen in banks.

Reasons India Nationalized Its Banks:

Let us examine the rationale behind the government's decision to nationalize banks to gain a better understanding of the effects of nationalization on the banking sector and the broader public:

- To Energize Priority Sectors: Between 1947 and 1955, 361 banks failed, or around 40 banks annually, indicating that the bank collapse was occurring quickly! Clients lost their deposits

And had no way to get back.

- **A Neglected Agricultural Sector:** Banks gave preference to big companies and industries while ignoring the rural area. With nationalization came a promise to uphold the agriculture industry.
- **Branch Expansion:** Nationalization made it easier for new branches to open, ensuring that banks were as widely represented as possible across the nation.
- **Mobilization of Savings:** By giving individuals greater access to banks and encouraging them to save, nationalizing the banks would help a cash-strapped economy by bringing in more money.

⁷ <https://jupiter.money/blog/evolution-of-banking-in-india/>

• **Political and Economic Factors:** The economy was severely impacted by the two conflicts in 1962 and 1965. Increased deposits from the nationalisation of Indian banks would be the advantage to Nationalization. One of the most important developments in the history of Indian banks was the nationalisation of those institutions. India now has nineteen nationalized banks.

Here are a few ways that nationalisation benefited the economy:

1. **1. Higher Savings:** The creation of new branches resulted in a notable rise in savings. Gross domestic savings nearly doubled in the 1970s as the country's income increased.
 2. **2. Enhanced Efficiency:** With more responsibility, banks' efficiency increased. Additionally, it raised public trust.
 3. **3. Empowering SSIs:** The economy improved proportionately as a result of the support given to small-scale enterprises (SSIs).
 4. **4. Financial Inclusion:** The Indian economy and banking industry's overall statistics demonstrated a noticeable improvement. It was reflected in metrics such as the gross investment rate from 1969 to 1991, the gross savings rate, the share of advances to DGP, and the GDP share of bank deposits.
2. **2. Expanded Reach:** Financial institutions were no longer confined to large cities. In the most isolated regions of the nation, branches were opened.
 3. **3. An Increase in Public Deposits:** The expansion of banks' operations aided in the growth of exports, small businesses, and agriculture. Public deposits also increased proportionately to this rise.
 4. **4. Strengthening the Green Revolution:** One of the top priorities on the government's agenda, the Green Revolution benefited from the assistance that the recently nationalized banks gave to the farming industry.

Nationalization & Its Impacts⁸

The process of transferring assets from the public sector to the federal or state governments for management or ownership is known as nationalization. Through the process of nationalization, banks in India that had previously operated under the private sector were moved to the public sector. Consequently, the nationalized banks were established. The banking sector and the nation's economic expansion benefited from the nationalization of banks in the following ways: Higher levels of efficiency in the banking sector raised public trust in the banks Small-scale industry growth resulting in a rise in funding and economic expansion increased bank presence, particularly in rural regions, with a shift in focus from profit to service Cost stabilization as the supply of necessities rose reduction of competition and improvement of the banks' operational effectiveness and performance.

The Negative Aspects of Nationalization⁹

To offer an objective perspective on the matter, the following are some drawbacks of nationalization:

1. **Socio-economic Challenges:** The banks were unable to help the grassroots levels of society sufficiently to end poverty or to give them with necessary funding. This was especially clear in India's rural areas.
2. **Competition from Private Banks:** Public sector banks were never able to outperform private banks in terms of performance, even with government support and additional push from a growth in deposits.
3. **Inability to Achieve Financial Inclusion:** Despite being the main goal of nationalizing banks, financial inclusion was not sufficiently supported. It was only partially realized until the introduction of the Jan Dhan Yojana savings account program.

⁸ <https://testbook.com/banking-awareness/history-of-banking-in-india>

⁹ <https://testbook.com/banking-awareness/history-of-banking-in-india>

List of Banks in India Before Independence¹⁰

Here is a list of banks before Independence. The small, brief list bears testimony of how few banks existed during that era:

Bank	Year Established
Allahabad Bank	1865
Punjab National Bank	1894
Bank of India	1906
Central Bank of India	1911
Canara Bank	1906
Bank of Baroda	1908

Types of Banks in India

We should talk about the different kinds of banks that are currently operating in India as we wrap off our exploration of the development of the country's banking sector. The following are the main types of banks that you are probably going to encounter:

1. Public Sector Banks

In a public sector bank, the majority of the shares are owned by the government. The State Bank of India is a good example, since the Indian government owns 58.6% of its shares. Another option is Punjab National Bank, in which the government has a 58.87% share. State banks, their affiliated organizations, and nationalized banks make up the two further categories

of public sector banks. In nationalized banks, the government controls every aspect of the bank and maintains total authority over it. However, selling shares of these banks is another option available to the government. The government's interests are diminished when this takes place.

Occasionally, the government acquires a minority stake in these institutions, following which the bank is listed on the Indian stock exchange.

2. Private Sector Banks

¹⁰ <https://testbook.com/banking-awareness/history-of-banking-in-india>

Banks in the private sector are owned by private companies. They gained notoriety in the 1990s. Owing to their superior service, private banks pose a serious threat to public sector banks.

3. Small Finance Banks in India

Basic banking services including deposits, loans, and bank transfers are offered by a few specialty banks in India. These are small finance banks that serve segments of the economy such as small industries, marginal farmers, and other unorganized sector segments that are not served by traditional banks. Ujjivan Financial Services Pvt Ltd in Bangalore and Equites Holdings Pvt Ltd in Chennai are two examples of these banks.

4. Payment Banks in India

The RBI developed a brand-new model known as payment banks. These banks are not permitted to offer credit cards or loans, but they are able to take restricted deposits. In addition to offering savings and current accounts, they also have the ability to issue debit or ATM cards. Bharti Airtel established Airtel Payments Bank, an illustration of a payment bank in India. Because these banks provide online payment options such as mobile payment apps, they also play a significant role in the development of e-banking in India.

The Indian Banking System Drives the Economy

Indian banks have changed the grim financial scene in the nation throughout time in order to support its expanding economy. Without a question, the Indian banking sector is the backbone of the nation's economy even now. The 2016 demonetization of currency notes serves as a perfect illustration. Current banknotes were destroyed almost instantly, causing turmoil throughout the country. Banks enabled citizens to exchange their obsolete banknotes across the nation, which aided in the economy's recovery from the shock. The Indian banking sector is constantly changing, and with it, so is its capacity to offer solid assistance to a country that is

constantly in need of financial advancement.

Liberalization of Banking in India's Past and Current Situation

India's banking industry can be broadly classified into organized and unorganized sectors. The RBI, commercial banks, cooperative banks, and specialist financial organizations like as ICICI, IFC, and others make up the organized sector. The sector that is not subject to government or RBI regulation is known as the unorganized sector. These organizations are very susceptible to instability and deception. In the part below, let's take a closer look at the Indian banking industry's organizational structure:

Banks on Schedule

The banks included in the second schedule of the RBI Act of 1934 are referred to as scheduled banks. To qualify as a scheduled bank, it needs to meet the following requirements:

The total amount of paid capital and monies received must not be less than INR 5 lakhs. The bank's actions shouldn't be harmful or negatively impact the interests of its clients.

Scheduled commercial banks come in four varieties:

banks in the public sector

banks in the private sector

overseas banks

local banks in rural areas

CONCLUSION

India's banking industry is currently fairly developed in terms of supply, scale, and product offerings. Partnerships should strike the correct balance between obligation and value by having the proper combination of long-term assets and chance cash flow, especially in a non-industrialized country like India where framework projects are common. Furthermore, a strong domestic capital market is essential for the financial industry to raise capital, fund growth, and maintain an appropriate capital sufficiency ratio to manage risk. Furthermore, bank investments are increasing. The banking industry is facing a number of challenges as a result of the money market's ongoing downturn, according to the researcher's analysis of the industry. The financial sector in India has now actually advanced in terms of item contributions, supply, and extension. Their entry into the nation of India continues to cause problems for the private sector and foreign banks. To calculate the optimal debt-to-equity ratio, firms in emerging countries like India need to have the right mix of risk capital and long-term resources. A strong domestic capital market is also essential for the financial industry to raise money, promote growth, and maintain an appropriate capital sufficiency ratio to manage risk. Additionally, bank interests are shifting vertically. After studying the banking sector, the researcher found that more issues are facing the sector as a result of the money market's continuous decrease.

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