BANKING IN INDIA

Historical Background : -

- Alexander & company established first bank on european system "Bank of Hindustan" in 1770 at Kolkata.
- After this, "General bank of India" came in existance in 1786 but both of these 2 banks proved unsuccessful.
- Three presidency bank were established in India which was based on private equity based on the "Act of 1830".

1st presidency bank — Established in 1806.
— Bank of Kolkata or Presidency bank of Kolkata.

2nd presidency bank — Established in 1840.
— Presidency bank of Bombay.

3rd presidency bank — Established in 1843.
— Presidency bank of Madras.

- British East India Company passed Join Company Act. 1860, Acc to it Now Bank could be established on the basis of Limited libility & this Act of British gov. is known as formtion of banking in Indian.
- In 1865, Allahabad Bank, it was the first bank with total Indian ownership.
- In 1881, Awadh commercial Bank, first bank to be established under Indian system & also first bank to be established on the concept of limited libility.
- In 1894, Punjab National Bank.
- In 1901, People's Bank.
- In 1906, Bank of India.
- In 1907, Indian Bank.
- In 1908, Bank of Baroda.
- In 1911, Central Bank of India.
- In 1921, Imperial Bank of India.
  By mearging 3 presidency Bank.

Reserve Bank of India (RBI)

- RBI was established under the recommendation of "Hiltton - Young committee."
- RBI was established under the Reserve Bank of Indian Act 1934 on 1st April 1935.
- It was nationalized on 1st Jan. 1949. RBI is the central bank of the coutnry.

Functions of RBI : -

1. It is the soul authority to issue currency in India. It issues two rupee notes & above while one rupee notes & subsidiary coines are issued by the ministery of finance but distributed by the RBI on behalf of the government.
   - ❑ It issues currency under minimum reserve system under which it keeps a minimum backing of 2100 crores out of which 115 crore worth of gold & 85 crores worth of foreign securities i.e. bounds of U.S. govt. and some other advanced countries of Europe.
   - ❑ Against this backing, RBI can issue unlimited amount of currency in the country it issues currencies acc to the projection of GDP.

More About RBI

- Head office of RBI is in Mumbai & other offices are in : -
  (i) Delhi
  (ii) Mumbai
  (iii) Chennai
  (iv) Kolkata
- It is also having its office in London.
- The governer of RBI is the head of RBI.
- SIR, OSBORN ADAM SMITH was the first governer of RBI.
- C.D. deshmukh was the first Indian governer of RBI.
- D. Subba Rao is the present governer of RBI.
- It consists total 20 members governer —1
  Deputy governer — 4
  Regional director — 4
  No. of person from finance ministery — 1
  No. of members or Economist (Nominated) — 1
- RBI consists the symbol of coconut tree & tiger.

2. RBI is government bank.
3. RBi is bankers bank.
4. RBI acts as an agent to the Indian govt. as a member to the IMF.
5. RBI acts as the central clearing house for inter bank transactions.

6. RBI is custodian of Indian's foreign exchange reserves.
7. RBI is the lender of the cast resort. In other words, when a banks fails to get funds from any other source it can always depend on the RBI.
8. RBI is the controller of credit given by bank to various sectors of the economy. It controls credit by adopting the following set of measures.
   (i) Quantitative measures.
   (ii) Qualitative measures are also called selective measures.

♦ Quantitative measures are measures armed at controlling & regulating the over all quantum/volume of credit (i.e.-Loans) given by commercial banks to various sectors of the economy.
  Quantitative measures are —
  1. Bank Rate (BR)
  2. Cash Reserve Ratio (CRR)
  3. Open market operations (OMO)
  4. Statutory Liquidity Ratio (SLR)
  5. Repo/Reverse Repo.

Bank Rate : Bank Rate is the rate of interest at which the RBI provides assistance to commercial banks. When this rate is raised it is called "Dear money policy". Generally this rate may be raised during a period of inflation may be lowered during a period of recession.

Cash Reserve Ratio : - It is that ratio of the total deposit of a bank which it has to necessarily keep with the central bank of a country at any given point of time the ratio generally may be raised at the time of inflation & lowered at the time of recession.

Statutotry Liquidity Ratio : SLR is that Ratio of the total deposits of a bank which it has to maintain & keep with itself in the form of liquid funds i.e. in the form of —
  (a) Cash in hand
  (b) Governments securities.

Open Market Operations (OMO) : OMO are operations conducted by the central bank of any country under which of may buy government securities from commercial bank or sell securities to commercial bank.

Repos — Repo means repurchase options exercised by the RBI since 1992 under which RBI buys govt. Securities from banks repos are essentially short term operations conducted to manage the supply & demand of liquidity. In a short period. Thus repo means injection of liquidity by the RBI.

Reverse Repo — Reserve repo-operation started by the RBI since 1946 implies that it is banks which lend to the RBI by buying govt. securities from the RBI for a short period with a promise to sell them back to the RBI on a specified date at a certain price.

Thus reverse repo imply absorption of liquidity under which banks give loans to RBI against govt. security for a a short period.

Qualitative measures are those aimed at controlling not only the quantum but also the purpose for which the loans are given by banks to various sectors of the economy e.g. wine making or wheat production.

♦ Qualitative measures are —
  1. Rationing of credit.
  2. Regulation of credit for consumption purpose.
  3. Variation of margin requirements.
  4. Moral control.
  5. Direct action.

Rationing of Credit — Under this method the RBI directs banks to give credit in accordance with the importance of various sectors in economy from time to time eg. It has directed banks that they must give 40% of their total credit at any given point of time to priority sector as identified by the RBI which consists of sectors like agriculture, small scale industries. Road & water transport, retail trade, low cost housing, poverty alleviation, employment generation etc.

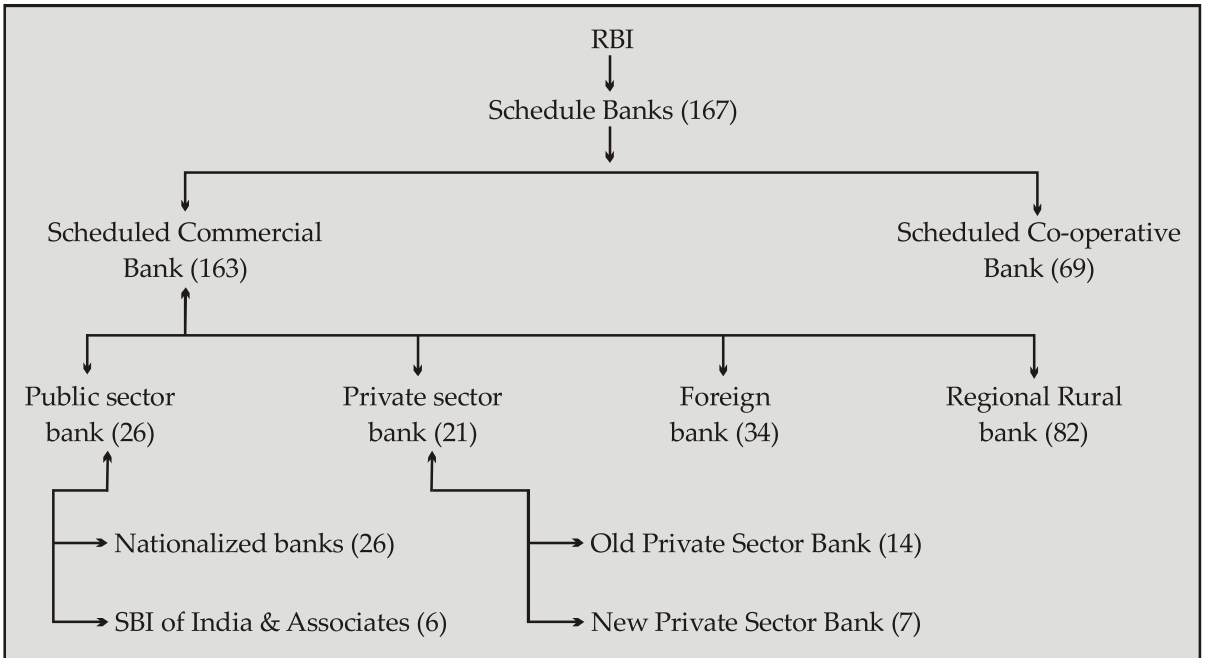
Regulation of credit for consumption purpose — RBI directs banks to restrict credit for purchase of consumer durable like TV, fridge etc. & instead give more credit for productive purpose.

Variation of margin requirements — The RBI directs bank from time to time to vary (raise or lower) margins on loans given by banks particulary for sensitive & essential commodities eg - when a person required to take loan for a car then bank will give 85% loan & ask 15% for paying on his own (down payment).

Moral control — When banks defy from the instruction & regulation of RBI, the RBI gives moral pressure or advice from time to time to restrain from doing it & when the banks do not obey, it allows the public to know about it.

Direct Action —
  (a) Charge penalty interest rate.
  (b) Stop lending.
  (c) Moratorium for few months.
  (d) Cancel the license of the bank.

Commercial banking in India —



Commercial Banking — Commercial banks are the institutions that ordinarily accept, deposits from the people & advances loans. Commercial banks also create credit. In India such banks alone are called commercial banks which have been established in accordance with the provisions of the banking regulation Act, 1949.

Scheduled Commercial Banks — Banks that we deal with on a day to day basis are called scheduled commercial banks. A scheduled commercial bank is a bank listed in the second schedule of the RBI act 1934 acc. to which such a bank must satisfy the following 2 conditions —

(i) Paid up capital of 5 lakhs & above.

(ii) Such a bank must function in the interest of the depositors.

- A scheduled commercial bank enjoys patronage refinancing of RBI while a non-scheduled bank does not.
- Present structure of schedule commercial banks in India can be classified into 3 types—

1. **Public sector banks —**There are 107 public sector banks. Out of these, 1 state bank + 5 subsidardy banks + 19 nationalised banks + 82 regional rural banks.
2. **Private sector banks —** There are 21 private sector banks. Out of which & are new + 14 are old private sector bank.
3. **Foreign banks —** There are 32 foreign banks operating in India.

State Bank of India (SBI) & ITS Associate Banks :

- On the recomendation of gorewala committee, imperial bank was nationalised to become SBI on July 1, 1995.
- Imperial bank of India was established in 1921 by mearging 3 presidency bank that is —

(i) Presidency bank of Kolkata.

(ii) Presidency bank of Bombay.

(iii) Presidency bank of Madras.

Management : -

- SBI is managed by a central board of directors. It can have maximum of 21 members.
- Head office of this bank is located in mumbai.

Associate banks of SBI —

- These associates banks were nationalized in 1959 however these banks refused their merger with SBI.
- The associate banks which are at present in no are —

(i) State bank of Patiala.

(ii) State bank of Hyderabad.

(iii) State bank of Travancore.

(iv) State bank of Bikaner & Jaipur.

(v) State bank of Mysore.

- At the time of nationalization they were 7 in numbers but ***state bank of sarashtra & state bank of Indore were merged in 2008 & 2009*** respectively.

Private Sector Banks - Private sector banks are those banks which are owned by the private sector.

Old private sector banks - At present there are 14 old private sector bank. The names are as follows.

1. City union bank Ltd.
2. Tamil Nadu mercantile bank Ltd.
3. SBI commercial & international bank Ltd.
4. The catholic syrian bank Ltd.
5. The dhana Lakshmi bank Ltd.
6. The federal bank Ltd.
7. The Jammu & Kashmir bank Ltd.
8. The Karnataka bank Ltd.
9. The Kasur vysya bank Ltd.
10. The Laksmi Vilas bank Ltd.
11. The Nainital Bank Ltd.
12. The Ratnakar Bank Ltd.
13. The South Indian Bank Ltd.
14. ING Vysya Bank Ltd.

New Private sector Banks - According to Narsimham Rao committee private sector banks should be allowed to be established in India.

- ♦ The minimum capital of new private sector banks should be Rs. 100 crore.
- ♦ The total no. of new private sector banks are 8.
  1. Axis Bank.
  2. ICICI Bank.
  3. Global trust Bank.
  4. Times Bank.
  5. Centurian Bank.
  6. Bank of Punjab.
  7. HDFC Bank.
  8. IDBI Bank.

Foreign Banks - Foreign bank is that bank whose head office is located in a foreign coutnry. It is regulated acc. to the rules of its own country.

- ♦ Minimum capital requirement for foreign bank should be us $ 25 million.
- ♦ Functions of foreign banks -
  1. Financing of export trade.
  2. Financing of import trade.
  3. Financing of internal trade.
  4. General banking functions.
- ♦ At present, there are 32 foreign banks with 31 branches.

Regional Rural Banks (RRB's)

- ♦ RRB's, the newest form of banks, have come into existence with the objective of developing rural & other productive activities of all kinds in rural areas.
- ♦ The emphasis is on providing such facilities to small & marginal formens, agriculture labourers, rural artisans & other small entrepreneurs in rural area.
- ♦ First RRB was established on 2nd Oct. 1975.

Development Banks

Industrial Development Bank of India (IDBI) —

- ♦ Established in 1964.
- ♦ Main functions - providing finance to large & medium scale industrial units.

Industrial finance co-operation of India (IFCI)

- ♦ Established in 1948.
- ♦ Main function -
  (a) Project finance.
  (b) Promotional services.

Industrial credit & investment co-operation of India limited (ICICI)

- ♦ Established in 1991.
- ♦ Main functions - Providing term loans in Indian & foreign currencies under writings of issues of shares & debentures.

Small Industries development bank of India (SIDBI) —

- ♦ Established in 1989.
- ♦ Main functions : providing assistance to small scale industries through state finance corporations, state industrial development corporations, commerical banks etc.

Expert - Import Bank of India (Exim. Bank)

- ♦ Established in 1982
- ♦ Main functions : co-ordinating the working of institutions engaged in financing export & import trade, financing export & imports.
- ♦ National housing bank (NHB) started operations in 1988.
- ♦ Main functions : development of housing finance in the country.

NABARD - (National Bank for Agriculture & Rural development) —

- ♦ Established in 1982.
- ♦ The paid - up capital of NABARD stood at Rs. 2000 crore as on 31 March 2010

Main function : To serve as an apex refinancing agency for institutions engaged in providing agricultural finance to develop credit delivery system to co-ordinate rural financing activities.

Various committees related to development in the field of banking -

1. **Narasimham - I** : The purpose of the narasimham - I committee was to study all aspects relating to the structure, organisation, function as & procedures of the financial system & to recommend improvements in their efficiency & productivity.

- The committee submit its report to the finance minister in 1991.

2. Narasimham - II -The narasimham - II committee was tasked with the progress review of the implementation of the banking reforms since, 1992 with the aim of further strenghtening the financial institutions of India.

- It focussed on issue like size of banks & capital adequacy ratio among other things.
- The committee submit its report of the committee on "Banking sector Reforms." to finance minister Yashwant Sinha in April 1998.

3. Damodaran committee -

4. Khandelwal committee report -

BASEL NORMS -

- Basel norms are set by banks of international settlement (BIS) in basel switzerland.
- 55 countries central bank are member of the BIS.

Basel I norms - Basel I prescribing for a set of minimal capital requirements for banks was introduced in 1988.

Basel - II norms - Basel II takes 3 pillar approach. These are -

1. Pillar I (minimum capital requirements)
2. Pillar II (Supervisory oversight)
3. Pillar III (Market discipline & disclosures)

- The RBI has adopted a gradual approach to implement the basel II norms.
- Foreign banks in Indian & Indian banks aperating abroad to meet basel II norms by march 31, 2008.
- Other scheduled commercial bank to meet basel II norms by march 31, 2009.
- RRB's & local area banks to meet the norms by march 31, 2010.

Basel - III norms - It will become operational from Jan 1, 2013 in phased manner.

Rules for basel III - RBI released its guideline on basel - III capital regulation on may 2, 2012.

Guidelines for basel III -

1. Indian bank have to maintain Teir-I capital or crore capital atleast 7% of their risk weighted assests or on going basis.
2. The total capital ratio including Tier- 1 & tier-II must be atleast 9%.
3. For tousle year ending march 31, 2013 bank will have to disclose capital ratio computed under existing guidelines.

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